

NEW SHERIFF IN TOWN: BIDEN TO FOCUS ON REVERSING TRUMP POLICIES

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With Democrats now controlling the White House and both chambers of Congress, President Biden could be poised to implement an agenda that may affect millions of taxpayers.

During his presidential campaign, President Joe Biden, in an effort to raise revenue by nearly \$3.5 trillion over the course of the next 10 years, laid out his plan to raise taxes on corporations, estates and high-income households, as well as reverse key parts of the Tax Cuts and Jobs Act (TCJA). At the same time, he repeatedly assured voters that individuals earning less than \$400,000 would not see an increase in their tax bills. While sweeping changes to the tax code may take time, with the Democrats

now controlling the White House and both chambers of Congress, President Biden could be poised to implement an agenda that may affect millions of taxpayers.

Although Biden has already set forth numerous tax proposals, at the time of this writing he has not released detailed tax policy on many of his changes. The following is a summary of the current law, as well as Biden's core proposals:

ORDINARY INCOME TAXES

Current law: Following the TCJA, seven tax brackets apply for individuals ranging from 10 percent to 37 percent, with the top rate for ordinary income in 2021 beginning at \$523,600 for single taxpayers and \$628,300 for joint filers.

Proposal: Biden has proposed raising the top income tax rate from 37 percent to 39.6 percent.

CAPITAL GAINS AND DIVIDENDS

Current law: The maximum federal income tax rate on net long-term capital gains and qualified dividends recognized by individual taxpayers is 23.8 percent (20 percent plus an additional 3.8-percent net investment income tax (NIIT) for certain high-income households).

Proposal: Under the Biden plan, taxpayers earning more than \$1 million would face higher taxes on the sale of capital assets. The top tax rate for long-term capital gains and qualified dividends would increase from 20 percent to 39.6 percent. Therefore, with the additional 3.8-percent NIIT, the maximum effective rate on net long-term gains would be 43.4 percent.

ITEMIZED DEDUCTIONS

Current law: The TCJA prohibits taxpayers from claiming a deduction for state and local taxes in excess of \$10,000. In addition, the TCJA eliminated the Pease limitation which reduced a taxpayer's total itemized deduction by 3 percent for each dollar of income that exceeds \$400,000. Finally, the TCJA eliminated the cap on a taxpayer's itemized deduction.

Proposal: Biden has indicated that he would cap the tax benefit of itemized deductions at 28 percent for those taxpayers earning more than \$400,000. Biden's proposal would also reinstate the Pease limitation for taxpayers who earn more than \$400,000 and eliminate the \$10,000 cap for state and local taxes.

SOCIAL SECURITY TAXES

Current law: Taxpayers are required to pay a 12.4-percent Social Security tax on the first \$142,800 of 2021 wages or net self-employment income. While employers and employees split the tax, self-employed individuals must pay the entire tax on their own (however, self-employed taxpayers may deduct one-half of the tax on their individual tax return).

Proposal: Biden has proposed to restart the 12.4-percent Social Security tax on wages and net self-employment income on earnings in excess of \$400,000. Therefore, Biden's approach would create a "donut hole" where income in excess of \$137,700, but below \$400,000, would not be subject to the tax. Over the years, the donut hole would gradually close as the lower threshold creeps closer to the upper threshold due to inflation.

ESTATE TAX

Current law: The current lifetime federal estate and gift tax exemption is \$11.7 million per person and \$23.4 million for couples. An individual's estate in excess of the exemption is taxed at a rate of 40 percent. Any taxable gift made during an individual's lifetime (prior to death) simply reduces the amount of his/her exemption. However, it is important to note that the individual exemption is scheduled to sunset to a reduced amount of \$5 million at the end of 2025 (indexed for inflation). In addition, the federal income tax basis of an inherited asset is stepped up to fair market value as of the decedent's date of death. Therefore, if an heir sells an inherited asset, the heir will owe capital gains tax only on the post-death appreciation.

Proposal: Biden has indicated that he would decouple the estate and gift tax regime. His plan would reduce the amount that an individual can transfer tax-free at death from \$11.7 million to \$3.5 million and limit the amount of aggregate tax-free lifetime gifting available to an individual at \$1 million. In addition, Biden's plan would increase the estate tax rate to from 40 percent to 45 percent. Finally, Biden would eliminate the basis step-up for inherited assets. As a result, any inherited asset would be taxed based upon the decedent's basis, which means more taxes on wealth would be passed on to heirs.

CORPORATE TAX

Current law: The TCJA reduced the corporate tax rate from 35 percent to a flat 21 percent.

Proposal: The corporate tax rate would increase from 21 percent to 28 percent. Additionally, Biden would implement a new minimum tax on corporations with at least \$100 million in annual book income. Such corporations would pay the greater of their federal income tax bill or 15 percent of reported book income.

QUALIFIED BUSINESS INCOME (QBI)

Current law: A taxpayer may generally deduct 20 percent of the domestic QBI earned from a partnership, S corporation or sole proprietorship.

Proposal: The QBI deduction would be phased out for taxpayers with taxable income in excess of \$400,000.

REAL ESTATE

Current law: Taxes on the gains of certain real property may be deferred if the property is exchanged for like-kind property in a valid §1031 exchange.

Proposal: The Biden tax plan would 1) eliminate §1031 like-kind exchanges which permit deferral of capital gains taxes on swaps of appreciated real property, 2) eliminate the \$25,000 exemption from the passive loss rules for rental real estate losses incurred by middle-income individuals and 3) eliminate rules that permit faster depreciation for certain real property.

TAX CREDITS

Biden has indicated a willingness to offer a number of new and/or expanded tax credits for low- and middle-income taxpayers, including the following:

- ✓ Expansion of the child and dependent care credit to \$4,000 for one qualifying child or \$8,000 for two or more qualifying children. The credit would be fully refundable but would begin to phase out once gross income exceeds \$125,000 and be completely phased out once income exceeds \$400,000.
- ✓ Expansion of the child tax credit to a maximum of \$3,000 per child for children ages 6 to 17, plus a \$600 bonus for children under six. The entire credit would be fully refundable.
- ✓ Expansion of the earned income tax credit from approximately \$530 to \$1,500 for taxpayers without children. Biden has also proposed to increase the income limit to \$21,000 and eliminate the age cap for older workers.
- ✓ A new \$5,000 credit for "informal caregivers" of aging family members.
- ✓ A new refundable credit of up to \$15,000 for first-time homebuyers. The credit could be collected when a home is purchased rather than requiring taxpayers to wait until they file their tax returns.
- ✓ A new refundable tax credit for low-income renters. The credit would be intended to hold rent and utility

payments to a maximum amount of 30 percent of monthly income.

With the federal budget deficit now over \$3.3 trillion (and growing) and the need for additional stimulus spending due to the COVID-19 pandemic, new tax laws could initially face an uphill battle, regardless of Democratic control of Congress. Nevertheless, if Biden's proposals are implemented, low- and middle-class wage earners stand to benefit, while affluent taxpayers, business owners and large corporations will likely pay substantially more. ■■■

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