JSF FINANCIAL

IS TAX REFORM COMING—AGAIN?

A Forward Look at Potential Tax Policy Changes

INTRODUCTION

With record-breaking stimulus injected into the economy both this year and last, alongside the stated priorities of the Biden Administration, it's likely we'll be seeing some changes to tax policy sometime this term. A number of provisions in the 2017 tax reform are set to expire in 2025 as it is, setting the stage for further negotiation in Congress.

What's in store? At this writing, President Biden is unveiling his first formally proposed change to the tax code with the American Jobs Plan, a sweeping $2.25 trillion infrastructure proposal. The plan includes a proposed increase in the corporate tax rate (to 28%) and a 21% minimum tax on global corporate earnings.[1] Beyond this initial proposal, we can piece together several of the White House's core positions and start thinking through what the White House's tax policies might look like both in this negotiation and going forward.

In this short paper, we'll cover some of the big items that we're paying close attention to and walk you through the legislative process involved in these kinds of changes. Of course, with the pandemic front and center, it's not likely that we'll see a lot of movement in this area until later this year or even a couple of years out.

However, it's our view that it's always better to at least think through what might be coming down the line, so that we have time and flexibility to start setting appropriate strategies.

As such, this paper focuses on the broad proposals and positions made by the Biden White House—these go beyond the scope of the recently announced American Jobs Act to include other policies that may enter the current infrastructure plan negotiation or future legislative activities.

As always, please reach out with any questions or concerns you may have, and please remember to reach out to your tax advisor for advice on any specific tax planning strategies. While new policies can affect all of us in some way, the specific implications for you and your family might be unique. That's why it is such a high priority for us to plan ahead with you individually.

Thank you, as always, for your support and trust in our firm.

Jeff Fishman

Tax Policy Planning

President Biden's tax policy statements have largely proposed higher tax rates on high-income individuals and corporations, plus the elimination of a number of incentives and deductions that currently benefit those groups.[2]

Based on various non-partisan estimates, the types of changes President Biden has broadly discussed could generate somewhere between $2.4 trillion to about $3.3 trillion between 2021 and 2030 (if they were to be implemented immediately). He has called for deploying this tax revenue towards tax-relief for lower earners, infrastructure and healthcare spending, sustainable energy investment, and U.S. manufacturing.

"A critical priority for us is to be prudent and cautious, and to help make sure our clients aren't caught off guard."

– Jeff Fishman, founder

In this note we'll focus primarily on the proposals that could impact the majority of our clients; this, of course, isn't pertinent to each individual.

We also have to caution that it's very important to remember that, so far, we have only the announcement of a single legislative proposal and, of course, campaign documents and other public statements. By their very nature, these are largely pretty general.

Policy Proposals for Individuals

President Biden has proposed higher taxes on individuals with income over $400,000 (it has not been clarified if this is a joint filer or single filer threshold). His proposals have included the following adjustments to current tax rates for individuals:

Top Income Tax Rate	A restoration of the top income tax rate to 39.6% (it is already scheduled to revert back to this rate in 2025)
Long Term Capital Gains	The taxation of long-term capital gains and certain dividends at ordinary income tax rates for those with incomes over $1 million
Estate Taxes	He has indicated his support for returning the estate tax exemption to 2009 levels (to $3.5 million per person and a top rate of 45%). The current exclusion, which was $11.58 million per taxpayer in 2020, is set to expire in 2025 and revert back to approximately $5 million per taxpayer
Social Security	Additional payroll taxes on those earning over $400,000 to shore up Medicare and Social security (this would create a "donut hole" on those above the current inflation-adjusted threshold but below $400,000, as those earners are not currently subject to the payroll tax)

Aside from general tax planning around these issues, it may be important to revisit the various strategies that can be used to protect family assets across generations. This is obviously a complex issue and one which we believe should be addressed early and often. After all, estate taxes in particular have varied wildly over the years, and it's important to be prepared for any unfavorable shifts.

Estate planning is obviously a complex issue, and one which we believe should be addressed early and often. With the potential for changes to the estate tax exemption, there is no reason to wait to consider strategies that could shield family assets across generations.

State and Local Tax Deduction (SALT)

After the 2017 tax reform, there is a $10,000 cap on federal deductions for state and local taxes. Democratic leaders in Congress have repeatedly called for the repeal of this cap, which had a significant impact on residents of relatively higher-tax blue states. As such, it's reasonable to look towards the possibility that the rules may change with Democratic control of the White House and Congress.

"We've advised waiting on property tax payments for some situations given the potential for significant legislative change, including the potential restoration of the SALT deduction. However, it's critical that we monitor the situation and plan for both possibilities, rather than assuming one thing or another."

– Jeff Fishman, founder

However, the full restoration of the SALT deduction is far from a given. With the uneven economic impact of the pandemic and a stated focus on inequality by both the Biden administration and Congressional Democrats, it might not be such an easy sell. After all, about 52% of the benefit from re-implementing the SALT deduction would flow to households with over $1 million per year in income.

As such, it's possible that Democrats will seek a middle road; for example, by partially restoring the cap or by offering it to households under a certain income level or, AMT exposure could once again diminish the value of the deduction. Should any of these versions go through, it appears likely to be done through budget reconciliation (more on that below).

In other words, while a restoration of the SALT deduction is a real possibility, we're not prepared call it a foregone conclusion, especially considering the other high-priority policy proposals under discussion.

Corporate Policy Measures

While we won't cover them in detail here, President Biden has also called for changes to the corporate tax code. The Tax Cuts and Jobs Act reduced the corporate tax rate to 21% from the previous 35%, and Biden has proposed the increase of that rate back up to 28%. This could have a ripple effect on other key tax formulas that are connected to the corporate income tax rate, such as global intangible low-taxed income and foreign-derived intangible income. It could also have an impact on the pass-through income deduction and estate taxes for some filers.

For both our corporate clients and families, we believe that effective tax planning starts early, which is why we prioritize ongoing coordination with your tax advisors and accountants. That way, we can navigate policy changes and map out your tax strategies in the most prudent way.

The Thin Democratic Majority

While much focus has gone into the Biden proposals, it's critical to remember that tax policy actually originates and is passed in Congress. This adds a few potential twists and turns to the process.

A few issues to keep in mind on that front.

First, Democrats are not necessarily unified behind Biden's point of view and holding all 50 Democratic senators together may not be an easy feat. There are a variety of preferences about appropriate tax policy changes within the party, as well as competing priorities. This means a degree of compromise and debate will likely be baked into the process.

From there, with the absolute slimmest possible majority in the Senate, Democrats will need to rely either on a procedural loophole (the "budget reconciliation") or a bi-partisan, filibuster-proof majority to pass legislation. The latter would require further negotiation and coordination between parties.

Of course, there is also the possibility of regulatory actions in support of Biden policies. Federal agencies are not permitted to change legislation, but they do have latitude in the way that laws are interpreted and enforced. We believe it will be critical to keep an eye on any activities in this area that may impact our clients.

Conclusions

There are, clearly, a number of potential changes on the horizon. For now, we'll be watching as the proposed American Jobs Act makes its way through Congress, with the expectation that we'll see a degree of opposition and negotiation around any specific tax changes.

Again, when it comes to these other tax policy measures, we're not planning to take a passive point of view: wherever possible, feasible, and prudent, we value the ability to plan for contingencies within the guidance we offer to our clients. Please also remember to consult your tax advisor about any specific strategies or plans that could apply to your personal situation.

What is budget reconciliation?[3]

Like the budget, a reconciliation bill requires a simple majority to pass the Senate. In other words, a reconciliation bill cannot be filibustered, though there are limits to what can be included.

How does it work?

Essentially, the annual budget sets out totals for spending, revenue, debt, and surplus or deficit, and it can also include budget reconciliation instructions. Those instructions tell the relevant committees to provide recommendations on what can be changed in an existing law to achieve the specified objectives. Those changes can come from any program directed by that committee.

How often is it used?

Since 1980, Congress has sent 25 reconciliation measures to the White House; of those, 21 were passed. Recently, Republicans used reconciliation in 2017 in support of tax cuts. This was the reason many of the tax cuts enacted in 2017 were set to sunset in 2025, as legislation under budget reconciliation that increases the deficit can't go beyond the specified budget window.

As always, we look forward to continuing this conversation with you personally, where we can discuss how current and potential tax policies might impact you and your family.

SOURCES

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1. https://www.bloomberg.com/news/articles/2021-03-31/biden-kicks-off-next-big-push-with-2-25-trillion-economy-plan?sref=c4RUGNV1

2. Unless otherwise noted, tax policy information from: https://www2.deloitte.com/us/en/pages/tax/articles/biden-tax-policy-impact.html

3. Source: https://budget.house.gov/publications/fact-sheet/budget-reconciliation-basics and https://www.forbes.com/sites/alisongriffin/2021/01/14/what-is-budget-reconciliation-anyway/?sh=3748930ca590