

APEG Alert – June 2021

A Comprehensive Look at Potential Tax Law Changes

On May 28, 2021, President Biden released his Fiscal Year 2022 Budget Proposalsⁱ, and the Treasury issued its General Explanations of the Administration's Revenue Proposals (i.e., "Green Book"), which explores in more detail the Administration's revenue proposalsⁱⁱ. The Green Book generally contains a "wish list" of tax proposals to support the President's Budget.ⁱⁱⁱ

In this APEG Alert, we will highlight the key proposed tax changes found in the Green Book and discuss the other Individual Tax Proposals that are "out there" (House and Senate Bills, etc.). Finally, we will summarize the changes that have been proposed as they relate to the various types of Federal Taxes. At this point, there is no way to determine which, if any, of these proposals will make it into law. However, at least some of these proposals could likely be enacted before the end of this year. Any, or a combination of, these proposals could significantly impact tax planning as we know it.

Key 2022 Green Book Proposals^{iv}

<u>Proposal</u>	<u>Details</u>	<u>Proposed Effective Date</u>
Increase the top marginal income tax rate to 39.6% for high-income earners	<ul style="list-style-type: none"> For 2022, taxable income over \$509,300 for married filing jointly & \$452,700 for single taxpayers. Indexed for inflation after 2022. 	Effective for tax years beginning after December 31, 2021
Tax capital income for high-income earners at ordinary tax rates	<ul style="list-style-type: none"> Long-term capital gains and qualified dividends of taxpayers with an adjusted gross income of more than \$1 million (\$500,000 for married filing separately) would be taxed at ordinary income tax rates. Net Investment Income Tax (NIIT) of 3.8% also applies. Indexed for inflation after 2022. 	Effective for gains recognized after date of announcement (interpreted to be April 28, 2021 – i.e., date American Families Plan was introduced)

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<p>Treat transfers of appreciated property by gift or on death as realization events</p>	<ul style="list-style-type: none"> • Donor or deceased owner of the appreciated asset would realize capital gain at the time of gift/death. • Amount of gain realized would be the excess of the asset's fair market value on the date of the gift/death over the donor/decedent's basis in the asset. • \$1 million per person exclusion (indexed for inflation after 2022). Amount would be portable to surviving spouse. • Transfers to US spouse or charity would not be recognized; however, the surviving spouse would receive a carryover basis in transferred assets. • Transfer to a Revocable Trust would not be recognized. • Exclusion for household furnishings & personal effects (not collectibles). • Exclusion of \$250,000 per person of gain from sale of any residence (not only principal residence). • Gain would be taxable income to the decedent on the Federal gift or estate tax return or on a separate capital gains return. The use of capital losses and carry-forwards would be similar to the current rules for individual taxpayers. • Appears that transfers of partial interests would be valued at proportional share of FMV of entire property (i.e., no discounts). 	<p>Effective for gains on property transferred by gift and on property owned at death by decedents dying, after December 31, 2021</p>
<p>Recognize gain on unrealized appreciation for assets held in a trust, partnership, or other non-corporate entity every 90 years</p>	<ul style="list-style-type: none"> • Tax gain on property that has not been the subject of a recognition event within the prior 90 years. • Effective for certain property owned by trusts, partnerships, and other non-corporate entities on January 1, 2022, with testing period to begin on January 1, 1940. 	<p>The first possible recognition event for any taxpayer under this provision would be December 31, 2030</p>
<p>Repeal deferral of gain from like-kind exchanges on real estate</p>	<ul style="list-style-type: none"> • Allows deferral of gain up to \$500,000 per year for each taxpayer (\$1 million for married individuals filing jointly) for like-kind exchanges of real property. • Gains in excess of \$500,000 (\$1 million married filing jointly) during a taxable year would be recognized in the year the taxpayer transfers the real property subject to the exchange. 	<p>Applies to exchanges completed in taxable years beginning after December 31, 2021</p>
<p>Apply 3.8% Medicare Tax to all income & earnings over \$400,000</p>	<ul style="list-style-type: none"> • Ensures that all trade or business income of taxpayers with income over \$400,000 is subject to the 3.8% Medicare tax. 	<p>Taxable years beginning after December 31, 2021</p>

Other Tax Proposals^v

- President Biden's "American Families Plan"– Green Book proposals listed above clarify and provide greater details about the revenue provisions of the American Families Plan. April 28, 2021.
- Sensible Taxation and Equity Promotion ("STEP") Act – Senate Statement & Discussion Draft introduced by Senator Chris Van Hollen (D – MD). March 29, 2021.
- House Bill 2286 - (House version of STEP Act) To amend the Internal Revenue Code of 1986 to treat property transferred by gift or at death as sold for fair market value.... (introduced by Representative Bill Pascrell (D - NJ). March 29, 2021.
- For the 99.5% Act – Senate Bill introduced by Senator Bernie Sanders (D – NH). March 25, 2021.
- The Ultra-Millionaire Tax Act - Senate Bill introduced by Senator Elizabeth Warren (D – MA). March 1, 2021.
- Other – Campaign Proposals, etc.

Federal Taxes That Might Be Impacted

<u>Tax Impacted</u>	<u>Various Proposals</u>	<u>Proposed Effective Date</u>
Individual Income Tax	<p>Increase top marginal tax rate for taxpayers with taxable income over \$509,300 for married filing jointly & \$452,700 for single taxpayers.</p> <ul style="list-style-type: none"> • Biden Campaign Proposal • American Families Plan / Green Book 	January 1, 2022
Capital Gains Tax	<p>Increase capital gains rate to 39.6% for people making over \$1million. Tax unrealized gains over \$1million at death (eliminate "step-up"). Mark-to-Market gain recognition on Trust Assets (21 or 30 years). Treat transfers by gift or death as realization events & recognize gain / loss. Recognize gain on unrealized appreciation for assets held in a trust, partnership, or other non-corporate entity every 90 years. Repeal deferral of Capital Gain on like-kind exchanges on real estate.</p> <ul style="list-style-type: none"> • STEP Act • American Families Plan / Green Book 	January 1, 2021 or April 28, 2021
Gift Tax	<p>Lower Exemption from \$11.7M per person to \$1M per person Change current \$15,000 per donee per year annual exclusion to \$10,000 per donee with a \$30,000 <u>per donor</u> per year limit for gifts to certain Trusts & flow-through entities.</p> <ul style="list-style-type: none"> • For the 99.5% Act 	January 1, 2022

Estate Tax	<p>Lower Exemption from \$11.7M per person to \$3.5M per person Increase Tax rates from current 40% top rate to 45% on estates from \$3.5M – \$10M, 50% between \$10M and \$50M, 55% between \$50M and \$1B and 65% on estates over \$1B.</p> <ul style="list-style-type: none"> For the 99.5% Act 	January 1, 2022
Generation Skipping Transfer Tax (GSTT)	<p>Lower Exemption from \$11.7M per person to \$3.5M per person. Long-term or "dynasty" trusts will be limited to a 50-year term.</p> <ul style="list-style-type: none"> For the 99.5% Act 	Date Signed into Law
Social Security / FICA Taxes	<p>Social Security taxes would continue to be imposed on wages up to \$137,700 (adjusted) AND imposed on wages over \$400,000. Rate would remain at 12.4%, split evenly between employer and employee.</p> <ul style="list-style-type: none"> Biden Campaign Proposal 	TBD
3.8% Net Investment Income Tax	<p>Trade or business income of taxpayers with income over \$400,000 would be subject to the additional 3.8% Medicare tax.</p>	January 1, 2022
NEW – Wealth Tax	<p>Would implement a 2% annual Wealth Tax on Americans with at least \$50 million in wealth and a 3% tax on those with at least \$1 billion in wealth.</p> <ul style="list-style-type: none"> Ultra-Millionaire Tax Act 	TBD
Other changes that could impact Income/ Estate Planning	<p><u>For the 99.5% Act:</u> Trusts treated as Grantor Trusts for income tax purposes will be includable in Grantor's estate at death. <i>Will impact existing Irrevocable Life Insurance Trusts (ILITS).</i> Use of Grantor Retained Annuity Trusts (GRATS) will be limited. Limitations on the use of Valuation Discounts.</p> <p><u>Biden Campaign Proposals:</u> Eliminate the deferral of Capital Gains from like-kind exchanges (ex: 1031 exchanges) for taxpayers with income over \$400,000. Re-instate "Pease Limitation" and Cap the Value of Itemized Deductions to 28% of the value of the deduction for Households making more than \$400,000.</p> <p><u>American Families Plan:</u> \$80 Billion to IRS over next ten years to increase enforcement of tax laws.</p>	TBD

Please note that, as with any proposals, it is impossible to predict what, if any, changes will be enacted into law. APEG will continue to monitor these proposals and other potential tax legislation as it evolves and keep you up to date. Stay tuned for future Publications of our 2021 Tax Legislation Series of Alerts.

We hope this helps you to increase your knowledge to better serve your clients. Regards, *Jeff & Ruth*

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ⁱ Full text of the Budget Proposals can be found at <https://www.whitehouse.gov/omb/budget/>.

ⁱⁱ Full text of the Treasury explanations is at <https://home.treasury.gov/system/files/131/General-Explanations-FY2022.pdf> (see pages 59-101 for tax proposals that will impact Individuals).

ⁱⁱⁱ For a discussion of how the Federal Budget process works see <https://www.taxpolicycenter.org/briefing-book/how-does-federal-budget-process-work>.

^{iv} Note that this Alert discusses only those proposals related to individual income taxes that have the broadest application for the clients of APEG Members. Please see the full text of the Treasury explanations in footnote ii for full details. Also note that none of the Green Book proposals discuss changes to Federal Estate, Gift or Generation-Skipping Transfer Taxes.

^v Note that there are also two Republican proposals “out there” that are unlikely to gain any traction during the current administration but for the sake of completeness, we’d like to mention them here:

- **Estate Tax Reduction Act** – Bill to reduce the estate tax to 20% (half of the current top rate of 40%). Introduced by Senator Joni Ernst (R-Iowa), along with Senators Tom Cotton (R-Arkansas) and John Boozman (R-Arkansas). May 13, 2021.
- **Death Tax Repeal Act of 2021** (S. 116) – Bill to repeal Federal estate and generation-skipping transfer taxes. Introduced by Senator Kevin Cramer (R-North Dakota) & Senator John Thune (R-South Dakota). March 9, 2021.