Biden's 'American Families Plan' proposes significant tax hikes for upper-income individuals but leaves out key details

President Biden this week called for increasing the top individual income tax rate and the capital gains tax rate, taxing carried interests as ordinary income, eliminating stepped-up basis for certain inherited assets, and other tax hikes focused on upper-income taxpayers to help offset the cost of his proposed $1.8 trillion initiative known as the "American Families Plan."

The president formally rolled out his proposal during an address to a joint session of Congress on April 28. But the White House thus far has not provided key details on how his revenue-increase proposals would operate, and early indications suggest the administration is likely to encounter resistance from Republicans and could even face challenges in holding together the tight Democratic majorities in the House and Senate as it attempts to move the proposal through Congress.

Revenue-raising provisions

At a high level, the American Families Plan proposes new spending on what the administration has called "human infrastructure" priorities such as paid family and medical leave, universal child care, access to pre-kindergarten education and free community college, and nutrition assistance programs, along with tax relief targeted primarily at lower- and middle-income taxpayers.

According to a fact sheet that the White House released ahead of the president's speech, these provisions would be paid for through revenue offsets drawn largely from proposals that then-candidate Biden put forward during the 2020 presidential campaign. (For an overview of tax proposals in Biden's campaign platform, see *A change in course: Tax policy implications of a Joe Biden presidency* from Deloitte Tax LLP.)
URL: https://www.whitehouse.gov/briefing-room/statements-releases/2021/04/28/fact-sheet-the-american-families-plan/
URL: https://www2.deloitte.com/us/en/pages/tax/articles/biden-tax-policy-impact.html

Ordinary income tax rates: Following through on his campaign pledge to ensure that wealthy individuals pay "their fair share" in taxes, the president has proposed to increase the top individual income tax rate to 39.6 percent (from 37 percent under current law) for taxpayers "within the top one percent."

The White House fact sheet does not cite specific income thresholds that would apply for individual filers and married taxpayers filing jointly; however, *Axios*, citing comments by an unnamed White House official, reported on April 29 that the 39.6 percent rate would begin at $452,700 for individuals and $509,300 for joint filers, the thresholds that would have been in effect prior to the enactment of the Tax Cuts and Jobs Act (TCJA, P.L. 115-97).

Capital gains and dividends, net investment income tax: Under the president's plan, income from long-term capital gains and certain dividends would be taxed at ordinary rates for "households making over $1 million," although the White House does not specify how the threshold would be calculated for taxpayers with a mix of both ordinary and capital income.

Presumably, taxpayers in this income bracket would see their capital gain and dividend income taxed at the president's proposed top rate of 39.6 percent. That rate, combined with the 3.8 percent Medicare tax on net investment income that was enacted 2010 as part of the Patient Protection and Affordable Care Act, would bring the maximum tax rate on capital gain and dividend income to 43.4 percent.

The White House fact sheet also states – without additional explanation – that the president's plan would ensure that the net investment income tax will be applied "consistently to those making over $400,000."

Carried interest income: The plan would "permanently eliminate the carried interest loophole." Although the administration has not provided additional detail, this presumably means that carried interest income would be taxed at ordinary rates.

Estate tax: The president proposes to repeal the step-up in basis of inherited assets at death for gains greater than $1 million (which could be as much as $2.5 million per couple when combined with current-law tax exemptions for certain proceeds from the sale of a primary residence). Special rules – which the administration has not described – would apply to protect family-owned businesses and farms that are passed on to "heirs who continue to run the business."

Notably, the plan does not appear to include a campaign proposal to return the estate tax to the parameters in effect for 2009 (that is, a top rate of 45 percent and an exemption of $3.5 million per taxpayer).

Like-kind exchanges: The White House fact sheet states that the president's plan would "end the special real estate tax break that allows real estate investors to defer taxation when they exchange property" – presumably a reference to the like-kind exchange rules – for gains on real property greater than $500,000.

Excess business losses: The president proposes to permanently extend the excess business loss rule, which generally limits certain losses attributable to trades or businesses for noncorporate taxpayers to $250,000 ($500,000 in the case of joint filers), indexed for inflation.

The limitation was originally put in place through 2025 in the TCJA, but was suspended for taxable years beginning in 2018, 2019, and 2020 in last year's Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136). It was extended through 2026 in the recently enacted American Rescue Plan Act of 2021 (P.L. 117-2).

Some campaign proposals left out: The plan does not appear to include other notable revenue-raising proposals from Biden's presidential campaign, such as capping the value of itemized deductions for upper-income taxpayers, reinstating the so-called "PEP" and "Pease" limitations on itemized deductions, or eliminating the 20 percent deduction for certain passthrough business income under section 199A.

Stricter reporting and enforcement requirements

Just how much revenue the president's tax-increase proposals might raise is impossible to determine until Congress drafts actual legislative language that fills in the critical missing details. The administration does suggest, however, that its proposals for stricter enforcement of existing tax laws, additional funding for the Internal Revenue Service, and more stringent information reporting requirements will narrow the "tax gap" – the difference between the amount of tax owed to the government and the amount paid – and net an additional $700 billion for the fisc over 10 years.

The IRS's most recent published estimate, which covers the years 2011-2013, puts the gross annual tax gap at $441 billion. But IRS Commissioner Charles Rettig recently told the Senate Finance Committee that the tax gap actually could equal or even exceed $1 trillion a year due in part to the growth of cryptocurrency transactions and other sophisticated financial transactions and tax-avoidance strategies in the marketplace. (For prior coverage, see *Tax News & Views*, Vol. 22, No. 20, Apr. 16, 2021.)
URL: https://www.irs.gov/newsroom/the-tax-gap
URL: https://dhub.blob.core.windows.net/dhub/Newsletters/Tax/2021/TNV/210416_3.html

Enforcement: To address the tax gap, the president proposes to boost the IRS's enforcement budget to expand its audits of high-income individual taxpayers and corporations. The exact amount of the proposed budget bump is not specified on the administration's fact sheet, but the Treasury Department confirmed in an April 28 news release that it would be "roughly $80 billion" over 10 years. According to Treasury, the additional funds would be allocated to "overhauling technology to improve enforcement efforts" as well as "hiring and training auditors to focus on complex investigations of large corporations, partnerships, and global high-wealth individuals."
URL: https://home.treasury.gov/news/press-releases/jy0150

Information reporting: In addition, the administration's fact sheet says the plan would require financial institutions to "report information on account flows so that earnings from investment and business activity are subject to reporting more like wages already are." The Treasury Department explained in its news release that this proposal "leverages the information that financial institutions already know about account holders, simply requiring that they add to their regular, annual reports information about aggregate account outflows and inflows." The enhanced reporting requirements would "help [the IRS] improve audit selection so it can better target its enforcement activity on the most suspect evaders, avoiding unnecessary (and costly) audits of ordinary taxpayers," Treasury said.

Paid preparer regulation: To reduce fraud and improper payments under various tax credit programs such as the child tax credit and earned income tax credit – something the administration says is attributable largely to unscrupulous practitioners – the plan also proposes to give authority to the IRS to regulate paid tax return preparers.

No mention of effective dates

One key detail missing from the descriptions of all of the president's proposed revenue raisers is when they would take effect. We likely will learn more in the coming weeks when the president releases his budget blueprint for fiscal year 2022, which is expected to be accompanied by a Treasury "Green Book" that typically contains more detailed descriptions of an administration's revenue proposals.

Enhanced family tax credits

On the incentive side, the American Families Plan calls for extending certain enhancements to several family-focused tax relief provisions that the president proposed on the campaign trail and were put in place for just one year under the American Rescue Plan Act.

Child tax credit: The president's plan would make the child tax credit fully refundable on a permanent basis. (The American Rescue Plan allows full refundability of the credit for 2021 only.)

The administration also would extend through 2025 the increased the credit amount ($3,000 per child or $3,600 for a child under age 6, subject to a phase-out), the increased age limit for a qualifying child (to 17), and a provision making the credit available in advance in equal installments on a "periodic" basis. As enacted in the American Rescue Plan, all of these provisions are scheduled to expire at the end of this year.

Child and dependent care tax credit: The president's plan would permanently extend the American Rescue Plan's temporary enhancements to the child and dependent care tax credit, including:

- Full refundability;
- The increased maximum credit rate (50 percent);
- The higher income threshold for phasing out the credit ($125,000 of adjusted gross income instead of $15,000); and
- The increased amount of child and dependent care expenses that are eligible for the credit ($8,000 for one qualifying individual and $16,000 for two or more qualifying individuals).

Without congressional action, these provisions also will expire at the end of 2021.

Earned income tax credit: The president's proposal would permanently extend a provision in the American Rescue Plan Act that expanded eligibility for and the amount of the earned income tax credit for taxpayers with no qualifying children (the "childless EITC") for 2021 only.

Specific enhancements that would be made permanent include the reduction in the minimum age to claim the childless EITC from 25 to 19 (except for full-time students) and elimination of the upper age limit, an increase in the childless EITC credit percentage and phase-out percentage from 7.65 to 15.3 percent, an increase in the earned income limit for the maximum credit amount to $9,820, and an increase in the income threshold at which the credit begins to phase out to $11,610 for non-joint filers.

Health insurance premium assistance credit: The White House proposal would permanently extend American Rescue Plan Act provisions that made the premium assistance credit under the Patient Protection and Affordable Care Act more generous and expanded the income thresholds used in determining eligibility for the credit. As enacted in the American Rescue Plan Act, these provisions are effective only for 2021 and 2022.

SALT-free: The president's plan as released does *not* include a proposal to repeal or relax the $10,000 cap on the deduction for state and local taxes (SALT), which was enacted in 2017 as part of the TCJA. Biden took no position on the deduction cap during the campaign, but a number of congressional Democrats – and some Republicans – have urged the administration to address the cap in any significant tax proposals he sends to Congress. (More on that below.)

Next steps

With the release of the American Families Plan, the president and administration officials now begin the task of selling the tax-and-spending package to the public and to members of Congress.

As he has done with his American Jobs Plan, the president maintains that he would like to move this portion of his economic agenda with bipartisan support.

"I wanted to lay out, before the Congress, my plan before we got into the deep discussions," Biden said during his address to Congress. "I'd like to meet with those who have ideas that are different – they think are better. I welcome those ideas."

Resistance from Republicans

Based on initial reactions from some top Senate Republicans, however, the administration would have to make some significant changes for the president's proposal to win over any members of the GOP.

In a statement released April 28, House Ways and Means Committee ranking member Kevin Brady, R-Texas, said the plan would "sabotage[e] America's economic recovery with crippling tax hikes that hurt working families and drive jobs overseas. It's the last thing we need right now."

In the Senate, where the president and Democratic leaders would have to gain support from 10 Republicans to avoid a filibuster, Minority Leader Mitch McConnell, R-Ky., said in a release that the White House "wants to jack up taxes in order to nudge families toward the kinds of jobs Democrats want them to have, in the kinds of industries Democrats want to exist, with the kinds of cars Democrats want them to drive, using the kinds of child care arrangements that Democrats want them to pursue."

Some mixed messages from Democrats

The administration also may need to do some work to assuage the concerns of some Democrats – an important consideration given the party's narrow majorities in both chambers.

In the House, where Democrats have an edge of just six seats over the GOP, Ways and Means Committee Chairman Richard Neal, D-Mass., expressed support for the president's plan, commenting in an April 28 news release that "[f]rom major investments in child care and paid leave to fixing our broken tax code and strengthening enforcement at the IRS, this package puts American families first, and will unlock the talent and opportunity our nation needs to thrive."

Neal earlier this week released a discussion draft of his own proposal to provide universal paid family and medical leave, guaranteed access to child care, and permanently extend the family tax credits in the American Rescue Plan that differs in some ways from the president's plan. (For example, it would permanently extend all the components of the enhanced child tax credit while the president would make the refundability component permanent and extend other enhancements to the credit for just four years. Neal's proposal also calls for certain payroll tax credits that are not in the president's plan and does not include revenue offsets.)
URL: https://waysandmeans.house.gov/media-center/press-releases/chairman-neal-unveils-groundbreaking-proposal-reshape-american-economy

Neal acknowledged those differences in his April 28 news release but appeared confident they could be resolved.

"President Biden and I are united by our shared purpose to improve the lives of American families," Neal said. "The committee will explore how to move forward with permanent extensions to the child tax credit, earned income tax credit, and child and dependent care credit, and I think we can do so while still responsibly investing in other top priorities."

SALT problem: But the White House's decision not to address the cap on the SALT deduction in its initial version of the American Families Plan could trigger opposition from a sizeable contingent of House Democrats from high-tax states such as California, New Jersey, and New York who have demanded that the cap be repealed or at least relaxed.

In a letter sent to House Speaker Nancy Pelosi, D-Calif., and House Majority Leader Steny Hoyer, D-Md., earlier this month, 17 of New York's 19 Democratic House members said that they "reserve[d] the right to oppose any tax legislation that does not include a full repeal of the SALT limitation." Separately, 41 House Democrats from California – all except Speaker Pelosi – sent a letter to President Biden on April 15 urging him to restore full deductibility of SALT. And a group of House lawmakers from both parties recently formed a "SALT caucus" whose mission is to advocate for the SALT cap's repeal in the weeks and months ahead. (For prior coverage, see *Tax News & Views*, Vol. 22, No. 20, Apr. 16, 2021.)
URL: https://nadler.house.gov/uploadedfiles/04.13.21_salt_delegation_letter.pdf
URL: https://mikelevin.house.gov/imo/media/doc/2021-04-16%20CA%20Delegation%20SALT%20Cap%20Letter.pdf
URL: https://dhub.blob.core.windows.net/dhub/Newsletters/Tax/2021/TNV/210416_1.html

For his part, House Ways and Means Committee member Bill Pascrell, D-N.J., one of the more vocal critics of the cap, made clear this week that his position has not changed.

“I will be banging my fists onto the table to make New Jersey’s voice heard and do everything in my power to put SALT repeal on the books. I expect certain elements of the [president’s] proposal to shift as it moves through Congress,” he said in an April 28 release.

But any serious effort to include an outright repeal of the cap in an infrastructure package likely would spark opposition from progressive Democrats, who, like many congressional Republicans, argue that doing so would primarily benefit higher-income households. (For prior coverage, see *Tax News & Views*, Vol. 22, No. 21, Apr. 23, 2021.)
URL: https://dhub.blob.core.windows.net/dhub/Newsletters/Tax/2021/TNV/210423_3.html

The president thus far has not taken a position on the SALT deduction cap, although White House officials have said the administration would consider proposals to repeal it if proponents offered acceptable revenue offsets.

Pay-for concerns in the Senate: In the evenly-divided Senate, where Democrats don’t have a single vote to spare if they intend to move a bill without Republican support, the administration may have to address the concerns of some Democratic lawmakers about some of the plan’s proposed offsets.

Democrats Robert Menendez of New Jersey and Mark Warner of Virginia – both members of the Senate Finance Committee – endorsed the notion of increasing the tax rate on capital gain income but suggested that the president’s proposal to tax it at ordinary income rates may be an overreach.

“For me, it is what you’re doing, the totality of the package, and how does it affect the ability of growth to continue to take place. That’s how I’m judging it,” Menendez told reporters this week. “Right now it seems like a rather high rate to me.”

Warner commented to reporters that “there needs to be some differential” in the treatment of ordinary and capital gain income but noted that the current differential “is much too great” and that he is “open to narrowing that.”

Other Democrats, meanwhile, question whether the cost of the president’s latest package needs to be fully offset, according to comments reported by *Axios* ahead of the American Families Plan’s formal release.

Hawaii Democratic Sen. Brian Schatz told *Axios* that he’s “not a big pay-for guy” and that “some investments are worth deficit-financing.”

Connecticut Democrat Chris Murphy likewise commented that “there’s plenty of money in this country to pay for smart investments. But at the same time, if it’s a good investment, I don’t know that it needs to be fully paid for.”

Montana Democrat Jon Tester argued that “we should find a way to pay for half of it upfront and then hopefully with good infrastructure, it’ll create economic growth and pick up the other half.”

Regular order versus reconciliation

These complicated political dynamics will be critical to Democratic leaders' decisions around whether to pursue a bipartisan package that can garner at least 10 Senate Republican votes to overcome a potential filibuster or whether, instead, to again invoke the budget reconciliation process to bypass the GOP and pass a bill with all 50 Senate Democrats plus the tie-breaking vote of Vice President Kamala Harris. (Reconciliation allows for certain tax and spending legislation to clear the Senate with just 51 votes, rather than the usual 60 needed to overcome a filibuster in that chamber. But it also comes with some constraints on what can be included and a statutory requirement that the legislation not increase the deficit in any fiscal year beyond the budget window.)

Democrats opted for budget reconciliation to enact the American Rescue Plan Act late last month and are weighing it as an option for advancing President Biden's American Jobs Plan, although they have not made a final decision.

Democratic leaders appear to have at least two more opportunities to invoke the fast-track budget reconciliation process this year. One path would involve adopting a budget resolution for upcoming fiscal year 2022 (which is set to begin October 1) that includes reconciliation instructions. A second would involve revising the fiscal 2021 budget resolution that Democrats adopted to move the American Rescue Plan in a way that recharges the reconciliation process teed up in that blueprint.

That latter option – which has not been leveraged before by either party – recently became available when a spokesperson for Senate Majority Leader Charles Schumer, D-N.Y., indicated the Senate parliamentarian had given Schumer a favorable ruling in that regard. However, questions persist about just what that ruling said – it has not been made public – and whether it includes any process- or policy-related constraints. (For prior coverage, see *Tax News & Views*, Vol. 22, No. 19, Apr. 9, 2021.)
URL: https://dhub.blob.core.windows.net/dhub/Newsletters/Tax/2021/TNV/210409_2.html

Questions around whether to advance the administration's two expansive proposals separately or in combination provide an additional layer of complexity. Opting to move the American Families Plan separately from the American Jobs Plan presents both opportunities and challenges that Democratic leaders will have to navigate before deciding whether to attempt to move one very large bill or to break it down into two smaller, but still substantial, packages.

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