Treasury 'Green Book' sheds additional light on Biden's tax proposals

The White House released a fiscal year 2022 budget blueprint on May 28 that, as expected, calls for significant tax increases targeting large corporations and high-income individuals to pay for lower- and middle-class tax relief and bankroll trillions of dollars in new spending on the traditional physical infrastructure projects and "human" infrastructure initiatives the administration has proposed in its American Jobs Plan and American Families Plan.

The roster of headline tax proposals in the budget package provides no surprises. President Biden based the economic planks of his 2020 election campaign on the premise that the benefits of 2017's Tax Cuts and Jobs Act (TCJA) are skewed to large corporations and wealthy individuals and that the federal income tax system needs to be retooled to ensure that these taxpayers are contributing "their fair share." To that end, he proposed higher top income tax rates along with "base broadeners" that would limit or eliminate various incentives currently available to these taxpayers. Many of these proposals were previewed during the campaign and then made their way into the American Jobs Plan, which was unveiled in late March, and the American Families Plan, which the administration released last month. Among the more notable provisions are calls to:

- Increase the corporate tax rate to 28 percent and tighten the international tax rules;
- Repeal tax incentives the administration contends unduly benefit the fossil fuel industry (to partially offset the cost of expanded tax benefits to promote development of alternative fuels and energy efficiency);
- Increase the top individual income tax rate to 39.6 percent and tax income from long-term capital gains and carried interest at ordinary rates for certain upper-income individuals; and
- Eliminate the step-up in basis of assets at death for certain inherited assets.

President Biden up to now has addressed these proposals only in a very general way, but his budget blueprint includes a "Green Book," which provides more granular details from the Treasury Department on how they would operate – including their effective dates and their projected impact on federal revenues. All told, the administration projects that its tax proposals would generate a net increase in federal tax receipts of nearly $2.4 trillion between 2022 and 2031.
URL: https://home.treasury.gov/system/files/131/General-Explanations-FY2022.pdf

This special edition of *Tax News & Views* looks at the projected debt and deficit picture under the president's proposed budget, highlights the key details on his tax proposals, and discusses the potential obstacles he may need to overcome to get them enacted into law.

A different kind of fiscal plan: Debt and deficit picture

At a high level, President Biden's first fiscal blueprint takes a markedly different approach than his immediate predecessor, President Donald Trump, whose budgets typically relied on steep spending cuts and strong economic growth assumptions to show sharply declining budget deficits, and then surpluses, over time, and even President Barack Obama, whose budget plans leaned on a mixture of more moderate spending reductions and revenue increases to lower deficits with the primary goal of stabilizing and then gradually reducing the federal debt as share of gross domestic product (GDP).

Biden's fiscal 2022 budget, by contrast, largely accepts the premise that deficits will be elevated over the next decade. In fact, in dollar terms, the blueprint has deficits gradually declining from high points of almost $3.7 trillion in the current fiscal year (fiscal 2021) and $1.8 trillion in fiscal 2022 – reflecting in large part the enactment of several COVID relief bills in the last 15 months, including the $1.9 trillion American Rescue Plan signed into law this past March, and the assumed enactment of Biden's proposed American Jobs Plan and American Families Plan – to a nadir of about $1.3 trillion in fiscal 2027, before they would begin to rise again for the remaining years of the 10-year budget window.

As a share of GDP, the blueprint envisions federal spending averaging about 24.5 percent of GDP over the next decade – notably higher than the average level of about 20.6 percent of GDP registered over the past 50 years. Revenues would also be higher than in the past – amounting to 19.3 percent of GDP on average over the next decade, about 2 percentage points higher than its five-decade average.

By the end of the 10-year budget window (fiscal 2031), revenues would reach a high point of 19.9 percent of GDP, a level not seen since the late years of the Clinton administration when the federal budget was briefly in surplus.

The budget's elevated deficits as a share of the economy means that the federal debt held by the public (that is, debt not held in intragovernmental accounts such as the Social Security and Medicare trust funds) is also projected to rise steadily over the next 10 years, from about 110 percent of GDP in the current fiscal year to 117 percent of GDP in fiscal 2031.

In a bit of a departure from the budget blueprints of many previous administrations, which assumed that their proposed policies would be tonic for economic growth – which can then have favorable secondary effects on projected revenue and spending levels – the Biden administration's growth assumptions are relatively modest. Over the next decade, the budget assumes that real economic growth will come in at about 2 percent per year, roughly in line with its level in the years leading up to the coronavirus pandemic. Real growth would be higher over the next two years, however – between about 3 and 5 percent – reflecting the strengthening of the economy as the impact of the pandemic begins to wane and the assumed early benefits of enactment of Biden's American Jobs Plan and American Families Plan.

28 percent corporate tax rate

The administration's budget proposal would increase the corporate tax rate from 21 percent to 28 percent, citing that change as "an administratively simple way to raise revenue in order to pay for the [its] infrastructure proposals and other long-run drivers of spending growth." This proposal was a centerpiece proposal of then-candidate Biden's tax platform during the presidential campaign and was featured prominently in the American Jobs Plan released at the end March, so its inclusion in the Green Book was widely expected.

The only new light that the Green Book shed on this proposal was a statement that the administration wants to see the rate increase take effect for tax years beginning after December 31, 2021. For non-calendar year taxpayers, for tax years beginning after January 1, 2021, and before January 1, 2022, the tax rate would be equal to 21 percent plus 7 percent multiplied by the portion of the year that falls within 2022.

15 percent minimum tax on book income

The administration also proposes a 15 percent minimum tax on corporations based on worldwide book income, if a corporation has more than $2 billion of worldwide book income. More specifically, the new minimum tax would equal the excess of (1) book tentative minimum tax over (2) regular tax.

The book tentative minimum tax would be equal to 15 percent of worldwide pre-tax book income (calculated after reducing book income by book net operating loss deductions), less general business credits (including R&D, clean energy, and housing tax credits) and foreign tax credits. Under the proposal, taxpayers would be allowed a book tax credit (for a positive book tax liability) against regular tax in a subsequent year, but the credit may not reduce regular tax liability below the book tentative minimum tax for that year. This proposal would be effective for tax years beginning after December 31, 2021.

Like the corporate tax increase, this is a proposal that Biden spoke of often during his run for the White House, and though it has been modified somewhat since then (the original proposal would have applied to companies with incomes above $100 million) and clarified with respect to how tax credits can be used and whether minimum tax liability could be carried forward, the general contours were widely expected to be in the Green Book.

Proposals affecting multinational businesses

The budget blueprint includes proposals to overhaul or eliminate a number of current-law tax provisions that the White House argues provide incentives for companies to locate investment in foreign jurisdictions and move US-based jobs and production activities offshore.

Revisions to the GILTI regime: The administration proposes three changes to the current global intangible low-taxed income (GILTI) regime. First, the QBAI exemption which reduces the GILTI inclusion by 10 percent of the Qualified Business Asset Investment would be eliminated. This would result in a US shareholder's entire net controlled foreign corporation (CFC) tested income being subject to US tax.

Second, the section 250 deduction, which reduces US federal income tax on GILTI inclusion amounts would be reduced to 25 percent. As a result, the US effective tax rate on GILTI would generally be increased to 21 percent, assuming the US corporate income tax rate is increased to 28 percent as the White House has proposed. Finally, the current approach for calculating GILTI, which combines the tested income and tested losses of all of a US shareholder's CFCs would be replaced with a "jurisdiction-by-jurisdiction" calculation. Under the proposed approach, a US shareholder's GILTI inclusion and, by extension, residual US tax on such inclusion, would be determined separately for each foreign jurisdiction in which its CFCs have operations. In addition, a separate foreign tax credit limitation would be required for each foreign jurisdiction, with a similar jurisdiction-by-jurisdiction approach applying with respect to a US taxpayer's foreign branch income. Finally, the budget proposes to repeal the high-tax exception for both subpart F income and for GILTI.

As part of this proposal, the administration would allow a domestic corporation that is a member of a foreign-parented controlled group to take into account any foreign taxes paid by the foreign parent, under an approach that would be consistent with an OECD/Inclusive Framework Pillar Two agreement on global minimum taxation (if such consensus is reached), with respect to the CFC income that would otherwise be part of the domestic corporation's global minimum tax inclusion. The proposal's jurisdiction-by-jurisdiction approach would also apply for this purpose.

The proposal would be effective for taxable years beginning after December 31, 2021

Deduction disallowance for exempt or tax-preferred foreign gross income: The proposal would expand the application of section 265 to disallow deductions allocable to a class of foreign gross income that is exempt from tax or taxed at a preferential rate through a deduction (*e.g.*, a global minimum tax inclusion with respect to which a section 250 deduction is allowed or dividends eligible for a section 245A deduction). The proposal would provide rules for determining the amount of disallowed deductions when only a partial deduction is allowed under section 245A with respect to a dividend or a partial section 250 deduction with respect to a global minimum tax inclusion. The proposal would also repeal section 904(b)(4).

The proposal would be effective for taxable years beginning after December 31, 2021.

Expansion of section 7874: The proposal would broaden the definition of an "inversion" transaction by replacing the 80-percent test with a greater-than-50-percent test and eliminating the 60-percent test. The proposal would also provide that, regardless of the level of shareholder continuity, an inversion transaction occurs if (1) immediately prior to the acquisition, the fair market value of the domestic entity is greater than the fair market value of the foreign acquiring corporation, (2) after the acquisition the expanded affiliated group is primarily managed and controlled in the United States, and (3) the expanded affiliated group does not conduct substantial business activities in the country in which the foreign acquiring corporation is created or organized.

The proposal would also expand the scope of an acquisition subject to section 7874 by including a direct or indirect acquisition of substantially all of the assets constituting a trade or business of a domestic corporation, substantially all of the assets of a domestic partnership, or substantially all of the US trade or business assets of a foreign partnership. Furthermore, a distribution of stock of a foreign corporation by a domestic corporation or a partnership that represents either substantially all of the assets or substantially all of the assets constituting a trade or business of the distributing corporation or partnership would be treated as a direct or indirect acquisition of substantially all of the assets or trade or business assets, respectively, of the distributing corporation or partnership.

The proposal would be effective for transactions that are completed after the date of enactment.

Changes to GILTI and foreign tax credit provisions for foreign fossil fuel income: The proposal would repeal the exemption from GILTI for foreign oil and gas extraction income (FOGEI). The definition of FOGEI and foreign oil related income (FORI) would also be amended to include income derived from shale oil and tar sands activity.

In the case of a dual capacity taxpayer, the proposal would limit the amount of a levy that would qualify as a creditable foreign tax to the amount of tax that the dual capacity taxpayer would have paid to the foreign government if it were a non-dual capacity taxpayer (taxpayers that are subject to a foreign levy and that also receive a specific economic benefit), thereby codifying the safe harbor included in the current Treasury regulations for determining the portion of the levy that is paid in exchange for a specific economic benefit, and making safe harbor the sole method for determining the creditable portion of the levy. The aspect of the proposal that would determine the amount of a foreign levy paid by a dual-capacity taxpayer that qualifies as a creditable tax would yield to United States treaty obligations that explicitly allow a credit for taxes paid or accrued on certain oil or gas income.

Unless otherwise specified, the proposal provisions would be effective for taxable years beginning after December 31, 2021.

Changes to FDII rules: The proposal would repeal the deduction allowed for foreign-derived intangible income (FDII). The resulting revenue would be used to encourage R&D.

The proposal would be effective for taxable years beginning after December 31, 2021.

Replace BEAT with SHIELD: The proposal would repeal the current-law base erosion anti-abuse tax (BEAT) enacted in the Tax Cuts and Jobs Act and replace it with a new rule – known as the Stopping Harmful Inversions and Ending Low-Taxed Developments (SHIELD) – that would disallow deductions to domestic corporations or branches by reference to low-taxed income of entities that are members of the same financial reporting group (including a member that is the common foreign parent, in the case of a foreign-parented controlled group).

Under this proposal, a deduction would be disallowed to a domestic corporation or branch, in whole or in part, by reference to all gross payments that are made (or deemed made) to “low-taxed members.” A low-taxed member is any financial reporting group member whose income is subject to (or deemed subject to) an effective tax rate that is below a designated minimum tax rate.

- **Agreed-upon minimum tax rate:** If SHIELD is in effect before a Pillar Two agreement has been reached, the designated minimum tax rate trigger will be the US global minimum tax rate for GILTI (which is 21 percent under this proposal). If a Pillar Two agreement has been reached, such agreed-upon rate will apply for purposes of SHIELD.
- **Definition of financial reporting group:** A financial reporting group is any group of business entities that prepares consolidated financial statements and that includes at least one domestic corporation, domestic partnership, or foreign entity with a US trade or business. Consolidated financial statements means those determined in accordance with US Generally Accepted Accounting Principles (GAAP), International Financial Reporting Standards (IFRS), or other method authorized by the Secretary under regulations. A financial reporting group member's effective tax rate is determined based on the income earned (in the aggregate, taking into account both related- and unrelated-party income) and taxes paid or accrued with respect to the income earned in that jurisdiction by financial reporting group members, as determined based on the members' separate financial statements or the financial reporting group's consolidated financial statements, as disaggregated on a jurisdiction-by-jurisdiction basis. The rule would apply to financial reporting groups with greater than $500 million in global annual revenues (as determined based on the group's consolidated financial statement).
- **Calculation of denied deduction:** Payments made by a domestic corporation or branch directly to low-tax members would be subject to the SHIELD rule in their entirety. In particular, payments that are otherwise deductible costs would be disallowed in their entirety, while in the case of payments for other types of costs (such as cost of goods sold), other deductions (including unrelated-party deductions) would be disallowed up to the amount of the payment. In addition, payments made to financial reporting group members that are not low-tax members would be partially subject to the SHIELD rule to the extent that other financial reporting group members were subject to an effective tax rate of less than the designated minimum tax rate in any jurisdiction. In such cases, the domestic corporation or branch would effectively be treated as having paid a portion of its related-party amounts to the low-taxed members, if any, of the financial reporting group based on the aggregate ratio of the financial reporting group's low-taxed profits to its total profits, as reflected on the financial reporting group's consolidated financial statements.
- **Grant of regulatory authority:** The proposal includes authority for the Secretary to provide special rules to address differences (both permanent and temporary) between the relevant income tax base and the base as determined under financial accounting, and to provide rules to account for net operating losses in a jurisdiction. In addition, the proposal provides authority for the Secretary to exempt from SHIELD payments in respect of financial reporting groups that meet, on a jurisdiction-by-jurisdiction basis, a minimum effective level of taxation as determined to the satisfaction of the Secretary. Finally, the proposal provides authority for the Secretary to exempt payments to domestic and foreign members that are investment funds, pension funds, international organizations, or non-profit entities, and to take into account payments by partnerships.

The proposal to repeal BEAT and replace with SHIELD would be effective for taxable years beginning after December 31, 2022.

Limit foreign tax credits from sales of hybrid entities: This proposal would apply the principles of section 338(h)(16) (which limits the ability of the deemed asset sale resulting from a section 338 election to impact the source or character of any item for purposes of applying the foreign tax credit rules to the seller) to determine the source and character of any item recognized in connection with a direct or indirect disposition of an interest in a specified hybrid entity and to a change in the classification of an entity that is not recognized for foreign tax purposes (for example, due to an election under the entity classification regulations).

Thus, for purposes of applying the foreign tax credit rules, the source and character of any item resulting from the disposition of the interest in the specified hybrid entity, or change in entity classification, would be determined based on the source and character of an item of gain or loss the seller would have taken into account upon the sale or exchange of stock (determined without regard to section 1248). The proposal would not affect the amount of gain or loss recognized as a result of the disposition or the change in entity classification.

The proposal would be effective for transactions occurring after the date of enactment.

New incentives for 'onshoring'; denial of deductions for 'offshoring': In order to incentivize taxpayers to bring offshore jobs and investments to the United States, the proposal would create a new general business credit equal to 10 percent of the eligible expenses paid or incurred in connection with onshoring a US trade or business.

- **Definition of onshoring US trade or business:** Under the proposal, onshoring a US trade or business means reducing or eliminating a trade or business (or line of business) currently conducted outside the United States and starting up, expanding, or otherwise moving the same trade or business to a location within the United States, to the extent that this action results in an increase in US jobs.
- **Eligible expenses:** Eligible expenses may be incurred by a foreign affiliate of the US taxpayer, notwithstanding the tax credit would be claimed by the US taxpayer. If a non-mirror code US territory (the Commonwealth of Puerto Rico and American Samoa) implements a substantially similar proposal, the US Treasury would reimburse the US territory for the new general business credits provided to their taxpayers pursuant to a plan. Furthermore, the US Treasury would reimburse a mirror code US territory (Guam, the Commonwealth of the Northern Mariana Islands, and the US Virgin Islands) for the new general business credits provided to their taxpayers by reason of the enactment of the proposal.

The administration also proposes to disallow deductions for expenses paid or incurred in connection with offshoring a US trade or business.

- **Definition offshoring US trade or business:** Offshoring a US trade or business means reducing or eliminating a trade or business or line of business currently conducted inside the United States and starting up, expanding, or otherwise moving the same trade or business to a location outside the United States, to the extent that this action results in a loss of US jobs.

- **Impact on taxable income calculation:** In determining the income of a US shareholder of a CFC on its global minimum tax inclusion or subpart F income, no deduction would be allowed in determining such amounts for any expenses paid or incurred in connection with moving a US trade or business outside the United States.

For purposes of both proposals, expenses paid or incurred in connection with onshoring or offshoring a US trade or business are limited solely to expenses associated with the relocation of the trade or business and do not include capital expenditures or costs for severance pay and other assistance to displaced workers. The Secretary may prescribe rules to implement the provision, including rules to determine covered expenses and treatment of independent contractors.

The proposal would be effective for expenses paid or incurred after the date of enactment.

Additional interest deduction limitation for multinational group members: This proposal would add a new interest expense limitation applicable to multinational groups. Taxpayers subject to both this limitation and existing section 163(j) would apply whichever limitation is lower each taxable year. The new limitation would apply to any US subgroup (or stand-alone US entity) that is included in the consolidated financial statements of a multinational group and that reports $5 million or more of net interest expense on US tax returns annually, except that it would not apply to financial services entities.

Interest expense deductions of the US subgroup would be disallowed in proportion to the portion of the subgroup's net interest expense (calculated for financial reporting purposes on a separate company basis) that exceeds the subgroup's proportionate share of the overall group's net interest expense reported on the group's consolidated financial statements. The US subgroup's proportionate share of the group's net interest expense would be based on the subgroup's proportionate share of the group's earnings before interest, taxes, depreciation, and amortization.

Interest expense disallowed under the limitation would be carried forward to subsequent years, and the US subgroup would also carry forward any excess limitation. A US subgroup would be comprised of any US entity that is not directly or indirectly owned by another US entity as well as all direct or indirect subsidiaries (domestic and foreign) of such US entity that are included in the group's consolidated financial statements.

The Treasury Department would be directed to issue regulations providing for the allocation of interest expense disallowance among the members of the US subgroup to the extent they are not all members of a US consolidated group. The US subgroup would also be permitted to elect to limit its interest deductions to its interest income plus 10 percent of its adjusted taxable income (as defined in section 163(j)) as an alternative to applying the new limitation.

Repeal of credits and incentives for the oil and gas industry

The administration proposes to repeal credits and incentives it claims provide undue tax benefits to the oil and gas industry, including:

- The section 43 enhanced oil recovery credit for eligible costs attributable to a qualified enhanced oil recovery project;
- The section 45I credit for oil and gas produced from marginal wells;
- The election to expense intangible drilling costs under sections 263(c) and 291;
- The deduction for costs paid or incurred for any tertiary injectant used as part of a tertiary recovery method under section 193;
- The section 469 exception to passive loss limitations provided to working interests in oil and natural gas properties;
- The use of percentage depletion with respect to oil and gas wells and hard mineral fossil fuels;
- Two-year amortization of independent producers' geological and geophysical expenditures under section 167(h), instead allowing amortization over the seven-year period used by integrated oil and gas producers;
- The expensing of exploration and development costs;
- Capital gains treatment for royalties under section 631(c);
- The Oil Spill Liability Trust Fund excise tax exemption for crude oil derived from bitumen and kerogen-rich rock;
- Accelerated amortization for air pollution control facilities; and
- Elimination of the corporate income tax exception for publicly traded partnerships. A publicly traded partnership is subject to corporate income tax unless at least 90 percent of its income is "qualifying income," which includes, among other things, interest, dividends, rents from real property, income and gain derived from natural resources, and income and gain from certain financial transactions. As part of the Biden administration's effort to prioritize clean energy, the budget proposes to eliminate the corporate income tax exception for any publicly traded partnership that realizes qualifying income or gains from fossil fuels for taxable years beginning after December 31, 2026.

The repeal of these provisions generally would be effective for taxable years beginning after December 31, 2021. In the case of royalties, the provisions would be effective for amounts realized in taxable years beginning after December 31, 2021. The repeal of the exemption from the corporate income tax for publicly traded partnerships with qualifying income and gains from activities relating to fossil fuels would be effective for taxable years beginning after December 31, 2026.

Incentives for renewable energy production and investment, low-emission vehicles

Under the administration's plan, repeal of these fossil fuel provisions would partially offset the cost of production and investment tax credits related to renewable and alternative energy property, credits for production of certain alternative fuels, and incentives to promote low- and zero-emission vehicles.

Renewable electricity production tax credit (PTC): The proposal would extend the full (100 percent value) section 45 PTC for qualified facilities (*i.e.*, wind, open-loop biomass, closed-loop biomass, municipal solid waste, geothermal, hydropower, and marine and hydrokinetic), where construction begins after December 31, 2021 and before January 1, 2027.

Starting in 2027, the credit rate would begin to phase down to zero over five years. The credit rate would be reduced by:

- 20 percent (to 80 percent value) for facilities commencing construction after December 31, 2026 and before January 1, 2028;
- 40 percent (to 60 percent value) for facilities commencing construction after December 31, 2027 and before January 1, 2029;
- 60 percent (to 40 percent value) for facilities commencing construction after December 31, 2028 and before January 1, 2030; and
- 80 percent (to 20 percent value) for facilities commencing construction after December 31, 2029 and before January 1, 2031.

The credit would completely phase out for facilities commencing construction after December 31, 2030.

Taxpayers would have the option to elect a cash payment in lieu of the tax credits (*i.e.*, a direct pay option). The proposal would pair the PTC with certain minimum labor standards and/or incentives.

Renewable energy investment tax credit (ITC): The proposal would extend the section 48 ITC for investments in solar and geothermal electric energy property, qualified fuel cell power plants, geothermal heat pumps, small wind property, offshore wind property, waste energy recovery property, and combined heat and power property. Starting in 2022, the ITC would be expanded to include stand-alone energy storage technology that stores energy for conversion to electricity and has a capacity of not less than five kilowatt hours.

The credit would be restored to the full 30 percent rate for eligible property that begins construction after December 31, 2021 and before January 1, 2027. After 2026, the credit rate will begin to phase down to zero over five years under a similar schedule for the PTC outlined above. Thus, eligible property commencing construction after December 31, 2026 and before January 1, 2028 will receive 80 percent of the full credit, property commencing construction after December 31, 2027 and before January 1, 2029 will receive 60 percent of the full credit, and so on until the credit rate reaches zero in 2031. Taxpayers would similarly have the option to elect a cash payment in lieu of the tax credits (*i.e.*, a direct pay option). The proposal would also pair the ITC with certain minimum labor standards and/or incentives.

Electric transmission infrastructure credit: The proposal would create a new investment tax credit equal to 30 percent of a taxpayer's investment in qualifying electric power transmission property. Qualifying electric power transmission property would include overhead, submarine, and underground transmission facilities meeting certain criteria, including a minimum voltage of 275 kilovolts and a minimum transmission capacity of 500 megawatts. Qualifying property would also include any ancillary facilities and equipment necessary for the proper operation of the transmission facility.

Taxpayers would have the option to elect a cash payment in lieu of the tax credits (*i.e.*, a direct pay option). The proposal would pair the credit with certain minimum labor standards and/or incentives. The proposal would be effective for property placed in service after December 31, 2021 and before January 1, 2032.

Expand and enhance the carbon oxide sequestration credit: The proposal would extend the "commence construction" date for the existing section 45Q credit by five years, such that qualified facilities must begin construction before January 1, 2031.

The credit would also be enhanced for carbon oxide captured from hard-to-abate industrial carbon oxide capture sectors such as cement production, steelmaking, hydrogen production, and petroleum refining. The enhanced credit for industrial capture would not apply to ethanol, natural gas processing, or ammonia production facilities. An additional $35 per metric ton of qualified carbon oxide would be available for qualified carbon oxide that is captured from such sources and is disposed of in secure geological storage. The amount of the $35 per-ton additional credit would not change each year. The total per-ton credit for these projects would be $85 in 2026.

An enhanced credit for direct air capture projects is included as well. An additional $70 per metric ton of qualified carbon oxide would be available for qualified carbon oxide that is disposed of in secure geological storage. The amount of the $70 per-ton additional credit would not change each year. The total per-ton credit for direct air capture projects with secure geological storage would be $120 in 2026.

Taxpayers would have the option to elect a cash payment in lieu of the carbon sequestration credit (*i.e.*, a direct pay option). The proposal would pair the credit with certain minimum labor standards and/or incentives. The proposal would be effective after December 31, 2021.

Electricity generation from existing nuclear power facilities: The proposal would create a new allocated production tax credit (nuclear PTC) for electricity generation from eligible existing nuclear power facilities that bid for the credits. Eligibility to bid for these credits would depend, among other potential requirements, on the taxpayer's ability to demonstrate that (1) the facility has a good operation and safety record, (2) the facility is facing financial operating losses and that future projections include continued losses, and (3) that emissions of various air pollutants would increase if the facility ceased operations.

Eligible facilities would bid to receive credits over two-year windows. A solicitation of bids would be held every two years. In addition to providing all information necessary to determine eligibility, bidding facilities would identify the minimum credit amount per megawatt-hour of their generation that would be sufficient for them to maintain operations during the two-year window. Up to $1 billion in nuclear PTCs would be available in each year to be allocated based on an evaluation of the bids received, with the goal of maximizing the preservation of existing nuclear electricity generation. Eligible facilities would have the option to elect a cash payment in lieu of the allocated tax credits (*i.e.*, a direct pay option). The proposal would pair the credit with certain minimum labor standards and/or incentives. The proposal would be effective after December 31, 2021. The first two-year crediting window would commence on January 1, 2022, and the last crediting window would commence on January 1, 2030.

New credits for qualifying advanced energy manufacturing: The proposal would modify and expand section 48C. The definition of a qualifying advanced energy project would be revised to include: industrial facilities; recycling in addition to production; and expanded eligible technologies, including but not limited to energy storage and components, electric grid modernization equipment, carbon oxide sequestration, and energy conservation technologies. Selection criteria would be revised to include evaluating wages for laborers and additional consideration for projects that create jobs in communities impacted by the closure of coal mines or coal power plants.

An additional $10 billion of section 48C tax credits would be authorized for investments in eligible property used in a qualifying advanced energy manufacturing project. Of the $10 billion allocation, $5 billion would be specifically allocated to projects in coal communities. Applicants would also have the option to elect a direct payment in lieu of the section 48C tax credits.

Applications for the additional section 48C tax credits would be made during the three-year period beginning on the date on which the additional authorization is enacted. Applicants who are allocated the additional credits must provide evidence that program requirements have been met within 18 months of the date of acceptance of the application and must place the property in service within three years of the date of the issuance of the certification.

Tax credits for medium- and heavy-duty zero-emissions vehicles: The proposal would provide a new business tax credit for new medium- and heavy-duty zero-emission vehicles, including battery electric vehicles and fuel cell electric vehicles. These vehicles would be in Classes 3 through 8, as defined by the Federal Highway Administration's vehicle classification system.

Similar to the section 30D (plug-in electric vehicle) tax credit, vehicle manufacturers would submit to the IRS the medium- and heavy-duty vehicles eligible for the credit. To qualify, the vehicle must be acquired for use or lease by the taxpayer and not for resale, the original use of the vehicle must commence with the taxpayer, and the vehicle must be used predominantly in the United States.
Compliance with applicable Clean Air Act standards and federal motor vehicle safety standards would be required for a vehicle to be eligible for the tax credit.

For each vehicle class, the tax credit would be a set amount per vehicle.

For a Class 3 vehicle, the credit would be:

- $25,000 per vehicle purchased between January 1, 2022 and December 31, 2024;
- $20,000 per vehicle purchased between January 1, 2025 and December 31, 2025;
- $15,000 per vehicle purchased between January 1, 2026 and December 31, 2026; and
- $10,000 per vehicle purchased between January 1, 2027 and December 31, 2027.

For Class 4-6 vehicles, the credit would be:

- $45,000 per vehicle purchased between January 1, 2022 and December 31, 2024;
- $40,000 per vehicle purchased between January 1, 2025 and December 31, 2025;

- $35,000 per vehicle purchased between January 1, 2026 and December 31, 2026; and
- $30,000 per vehicle purchased between January 1, 2027 and December 31, 2027.

For Class 7-8 short-haul vehicles, the credit would be:

- $120,000 per vehicle purchased between January 1, 2022 and December 31, 2023;
- $100,000 per vehicle purchased between January 1, 2024 and December 31, 2024; and
- $80,000 per vehicle purchased between January 1, 2025 and December 31, 2027.

For Class 7-8 long-haul vehicles, the credit is:

- $120,000 per vehicle purchased between January 1, 2022 and December 31, 2024 and
- $100,000 per vehicle purchased between January 1, 2025 and December 31, 2027.

Taxpayers would have the option to elect a cash payment in lieu of a general business credit (*i.e.*, a direct pay option). The proposal would pair the credit with certain minimum labor standards and/or incentives.

Extended and enhanced electric vehicle charging station credit: The proposal would modify and expand the section 30C tax credit for electric vehicle charging stations. It would allow taxpayers to claim the tax credits on a per-device basis (*i.e.*, electric vehicle supply equipment, or ESVE, also called a port or a charger), increase the tax credit limit on individual devices to $200,000, and extend the tax credit for five years through December 31, 2026. Taxpayers would also have the option to elect a cash payment in lieu of the general business tax credits (*i.e.*, a direct pay option). The $1,000 tax credit for refueling property installed at a taxpayer's residence would not increase but would also be extended for five years. The proposal would pair the credit with certain minimum labor standards and/or incentives.

Tax credit for sustainable aviation fuel: The proposal would introduce a production tax credit of $1.50 per gallon for sustainable aviation fuel that achieves at least a 50 percent reduction in emissions relative to conventional jet fuel. The credit would be offered for fuel produced after December 31, 2021 and before January 1, 2028. A supplementary credit of up to 25 cents per gallon would be available on a sliding scale depending on the emissions reduction relative to conventional jet fuel. The emissions reduction certification amount would be 1 cent for every 2 percentage points above a 50 percent reduction baseline. Sustainable aviation fuel with a 50 percent emissions reduction relative to conventional fuel would receive the $1.50 per gallon credit, while fuel with a 100 percent emissions reduction would receive a $1.75 per gallon credit. The proposal would pair the credit with certain minimum labor standards and/or incentives.

Credit for low-carbon hydrogen production: The proposal would implement a new low-carbon hydrogen production tax credit. For the purposes of the credit, "low-carbon" refers to hydrogen produced using zero-carbon emissions electricity (renewables or nuclear) and water as a feedstock, or hydrogen produced using natural gas as a feedstock and with all carbon emitted in the production process captured and sequestered.

The credit would apply to each kilogram of qualified low-carbon hydrogen that is: (1) produced by the taxpayer, (2) for an end use application in the energy, industrial, chemicals, or transportation sector, and (3) from a qualified low-carbon hydrogen production facility during the six-year period beginning on the date the facility was originally placed in service. The credit would be indexed annually for inflation measured after the facility is placed into service, based upon the initial amount of $3 per kilogram of hydrogen between 2022 and 2024 and $2 per kilogram between 2025 and 2027. Taxpayers would have the option to elect a cash payment in lieu of the tax credits (*i.e.*, a direct pay option).

The hydrogen may be sold to an unrelated third party or, if directly consumed by the taxpayer that owns the facility, the production must be independently verified. Construction of a qualified facility must have begun before the end of 2026 for the facility to be eligible for the low-carbon hydrogen production tax credit.

Extended and enhanced incentives for energy-efficient building projects

The budget blueprint includes a number of business- and consumer-focused incentives for energy-efficient residential and commercial buildings.

Construction of new energy-efficient homes: The proposal would increase the section 45L tax credit for an energy-efficient home from $2,000 to $2,500 and extend the tax credit five years to December 31, 2026. The proposal would also modify and expand the dwelling units eligible for the credit. For new energy-efficient homes, the required energy savings percentage would increase from 50 percent to 60 percent under the 2006 International Energy Conservation Code (IECC) standards. In addition, certified Energy Star homes would also be eligible for the section 45L tax credit as would dwelling units with annual heating and cooling consumption at least 15 percent below the annual energy consumption level of a comparable dwelling unit under the 2018 IECC standards.

Energy-efficient commercial buildings deduction: The proposal would increase the maximum section 179D deduction per square foot from $1.80 to $3 for qualifying property placed in service after December 31, 2021. The partial deduction rate would be increased from 60 cents to $1 per square foot for qualifying property placed in service after December 31, 2021. The required efficiency standard in relation to the reference building's total annual energy reduction would be adjusted from 50 percent to 30 percent.

Mechanical insulation labor costs credit: The proposal would create a new general business tax credit for qualifying mechanical insulation labor costs. The tax credit would be equal to 10 percent of the mechanical insulation labor costs paid or incurred by the taxpayer during such taxable year. Mechanical insulation labor costs would include the labor cost of installing mechanical insulation property, including insulation materials as well as facings and accessory products, for a depreciable mechanical system that is placed in service in the United States and that satisfies certain energy loss reductions. The credit would be available for labor costs incurred after December 31, 2021 through December 31, 2026.

Consumer-focused energy-efficiency incentives: Incentives targeted specifically to consumers include:

- **Nonbusiness energy property credit:** The proposal would extend the section 25C tax credit five years and increase the lifetime limit to $1,200 for property placed in service after December 31, 2021 and before January 1, 2027. For qualified energy efficiency improvements, the credit rate would be increased to 15 percent and the credit amounts for certain types of residential energy property expenditures would also be increased. The proposal would modify the definitions of eligible qualified energy-efficiency improvements and residential energy property expenditures and update the required energy-efficiency standards for such property. Roofs, advanced circulating fans, and certain equipment, such as water heaters and furnaces, that are powered by fossil fuels would no longer be eligible for the tax credit; however, certain geothermal and load center equipment would be eligible for the tax credit. The proposal would be effective after December 31, 2021.
- **Residential energy-efficiency credit:** The proposal would extend the section 25D residential energy-efficiency credit and expand the definition of residential energy-efficient property to include qualified battery storage technology of at least three kilowatt hours of capacity installed in a residence. Starting in 2022, the credit would return to the full 30 percent rate for property placed in service after December 31, 2021 and before January 1, 2027. The credit would then be phased out over the next five years. The credit would be reduced by 20 percent of the full credit for property placed in service after December 31, 2026 and before January 1, 2028, 40 percent of the full credit for property placed in service after December 31, 2027 and before January 1, 2029, and so on until the credit is phased out in 2031. The proposal would be effective after December 31, 2021.

Superfund excise taxes and Oil Spill Liability Trust Fund

The proposal would reinstate the three Superfund excise taxes at double the previous rates for periods beginning after December 31, 2021 and through December 31, 2031. In addition, the Superfund excise tax on domestic crude oil and imported petroleum products would be expanded to other crudes such as those produced from bituminous deposits as well as kerogen-rich rock. Finally, the eligibility of the Oil Spill Liability Trust Fund for drawback would be eliminated. The proposal would be effective after December 31, 2021.

Economic and community development incentives

The budget package includes several proposals Biden touted during the presidential election campaign that are aimed at revitalizing economically distressed communities.

Expand the low-income housing credit (LIHTC): The proposal would expand the LIHTC by creating an additional type of housing credit dollar amounts (HCDAs), known as an Opportunity HCDA (OHCDA). Housing credit agencies (HCAs) would have a separate ceiling for OHCDAs from their existing allocation ceilings of HCDAs. HCAs would continue to receive annual infusions of regular HCDAs, without change to the allocation and ceilings for those HCDAs under current law. HCAs would be required to allocate the majority of their OHCDAs to projects in Census Tracts of Opportunity (CTOs). The proposal would define a CTO as a tract which is entirely in one or more difficult development areas (DDAs) or which has low poverty or certain other characteristics, as determined by the Secretary of the Treasury in consultation with Housing and Urban Development (HUD).

In each calendar year 2022 through 2026, the aggregate number of new OHCDAs would be 118 percent of the aggregate annual number of new HCDAs under current law. These additional OHCDAs would be made available to all states on a per capita basis, but with a different per capita amount applied to each state. The per capita amount for a state would be determined by a formula established by the Secretary in consultation with HUD that provides higher amounts to states with higher costs of constructing and operating affordable housing, as demonstrated by, for example, larger populations living in DDAs or higher percentages of rent-burdened households. Buildings in DDAs that receive allocations of either HCDAs or OHCDAs would receive “basis boosts” of up to 50 percent. All other “basis boosts” in current law (including those for bond financed buildings in DDAs) would be unchanged. The proposal would be effective for calendar years beginning with 2022. The restrictions on use of OHCDAs would last until all OHCDA ceilings (including unused and returned amounts) had been allocated or had expired. The increased “basis boost” for buildings in DDAs with allocations would be permanent.

Make the new markets tax credit permanent: The proposal would permanently extend the new markets tax credit, with a new allocation for each year after 2025. These annual amounts would be $5 billion, indexed for inflation after 2026. The proposal would be effective after the date of enactment.

Create a neighborhood home investment tax credit: The proposal would create a new tax credit – the neighborhood homes investment credit (NHIC) – to support new home construction for sale, substantial home rehabilitation for sale, and substantial home rehabilitation for existing homeowners. The constructed or rehabilitated residence must be a single-family home (including homes with up to four dwelling units), a condominium, or a residence in a housing cooperative. For each year between 2022 and 2031, inclusive, a specified amount of potential NHICs would be allocated to the 50 states, the District of Columbia, and US possessions (collectively, states). The amount for 2022 would be $2 billion, and this amount would be indexed for inflation for the years 2023 to 2031. The Secretary of the Treasury or her delegate would establish rules to divide the potential NHICs among the states, with an emphasis based on populations living in distressed urban, suburban, and rural neighborhoods. The Secretary, in consultation with HUD, would provide criteria for identifying distressed neighborhoods for this purpose and for purposes of determining where NHIC-supported projects must generally be located (NHIC-qualified neighborhoods). In addition, the Secretary, in consultation with HUD, may establish criteria according to which a limited volume of NHICs may be earned in certain additional rural communities and/or in gentrifying census tracts for owner-occupied rehabilitation.

Each state would create a new agency (or identify a pre-existing agency) to serve as the Neighborhood Homes Credit Agency (NHCA), with authority to allocate potential NHICs to project sponsors. Sponsors seeking potential NHICs would apply on a competitive basis by providing candidate plans for construction or rehabilitation, generally in one or more NHIC-qualified neighborhoods. The NHCA would be responsible for monitoring compliance with all provisions governing NHICs and for reporting violations to the Internal Revenue Service.

Each NHCA would establish a qualified allocation plan (QAP) to guide it in allocating potential NHICs among competing proposals. Every QAP would be required by statute to contain certain factors and preferences. The Secretary could require additional attributes, and each NHCA could add further criteria to address local conditions. NHCAs would also set standards for development costs, building quality, and developer fees. Each NHCA would be prohibited from allocating more potential NHICs than are reasonably expected to be necessary for financial feasibility. If unforeseen matters render an allocation inadequate, the taxpayer may seek an additional allocation. If potential NHICs remain after the sponsor and the sponsor's investors have received their NHICs from a construction or rehabilitation, the unused potential credits would revert to the NHCA for future allocation. The sponsor returning the potential NHICs would receive a preference in the competition for the returned credits.

A taxpayer may claim NHICs only after construction, inspection, and owner occupancy. In the case of a home to be sold to a qualifying new, purchasing owner-occupant, the credit is claimed when that owner-occupant begins residence. In the case of continuing qualifying owner occupants who are rehabilitating their homes, the credit is claimed when construction has been completed and inspected and the owner-occupant is in residence. NHICs can be claimed only if the owner-occupant after construction or rehabilitation is a NHIC-qualified owner. NHIC-qualified owners are those who meet criteria to be established by the Secretary and whose household income does not exceed 140 percent of area/state median income, adjusting for household size as determined by the Secretary of HUD. The method for determining household income shall be established in consultation with HUD. If, within five years of the date of qualification for the NHIC, the purchasing or rehabilitating owner-occupant ceases to the residence's owner-occupant, a portion of the claimed NHIC amount would generally have to be repaid to the NHCA for use in activities that further the purposes of the NHIC. Broadly conceived, the amount of the credit is computed as development costs less the sales price or, in the case of a homeowner rehabilitation, less the amounts paid by the homeowners. The amounts that may actually be claimed, however, are subject to several limits.

The following principles contribute to determining the amount of credit:

- **Necessity:** When sales proceeds meet or exceed development costs, no credit may be claimed.
- **Limited subsidy:** The credit may not exceed 35 percent of the lesser of development costs or 80 percent of the national median sales price for new homes, nor may it exceed the excess of development costs over sales proceeds.
- **Skin in the game:** The taxpayer always has an incentive to sell the residence for a higher sales price. That is, an increase in sales price can result in an increase in the taxpayer's after-tax income. This determination considers both reduction in the credit and reduction in the taxpayer's tax loss on the property. A similar consideration applies to receipt of owner payments toward rehabilitation of an owner-occupant's home.
- **No cliffs:** There is no point at which an additional dollar of sales proceeds precipitously reduces the credit to zero. Instead, the credit smoothly phases out such that it reaches zero at the maximum amount of permitted sales proceeds.

The IRS would be authorized and mandated to collect data relevant to evaluating the socioeconomic effects of the operation of the credit, whether or not that information is directly related to tax administration. The Secretary would be granted strong anti-abuse regulatory authority, including the ability to recharacterize the otherwise applicable tax consequences of a residence seller's original receipt of the NHIC and a passthrough investor's receipt of the credit as part of a distributive share or other passthrough allocation (including an investor that obtained its interest in the original NHIC recipient not long before receipt of the NHIC). The proposal would apply to allocations of potential NHICs to and by NHCAs in calendar years after 2021. Credits could be claimed in taxable years ending after December 31, 2021.

Federally subsidized state and local infrastructure bonds

The administration proposes to expand availability of tax-preferred bonds to finance certain types of infrastructure projects.

School infrastructure bonds: This proposal would create qualified school infrastructure bonds (QSIBs), which would be similar to Build America Bonds (BABs) under prior law. There would be a total national QSIB limitation of $50 billion – $16.7 billion each for 2022, 2023, and 2024. The allocation of this bond authority among states would be based on the proportion of funds that each state receives under Title I, Part A of the Elementary and Secondary Education Act of 1965.

Similar to BABs, interest on QSIBs would be taxable. Either the bondholders' interest would take the form of a tax credit equal to 100 percent of the interest on a QSIB, or the bondholders would receive cash from the bond issuer, and the federal government would make corresponding direct payments to the bond issuer. Each state would have to use no less than 0.5 percent of its total QSIB allocation for outlying areas. Similarly, no less than 0.5 percent of the QSIB allocation would have to be for schools funded by the Bureau of Indian Education.

States could enable local education agencies to issue QSIBs to expand access to high-speed broadband sufficient for digital learning. The local authorization may not exceed 10 percent of the state's total authorization to issue QSIBs and must be competitively allocated among local education agencies based on the poverty level of the schools' student population and the severity of the need to improve school facilities. For QSIBs issued under the 2022 authorization, states would be required to prioritize allocations to finance projects necessary to reopen schools in line with Centers for Disease Control and Prevention guidelines.

Bonds for transportation infrastructure: The proposal would expand the category of private activity bonds created by section 11143 of Title XI of the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU). It would increase the amount of such bonds to be allocated by the Secretary of Transportation by an additional $15 billion. The proposal would also add public transit, passenger rail, and infrastructure for zero-emissions vehicles as qualified activities for which such bonds may be issued. These bonds would not be subject to state private activity bond volume caps.

Both the proposal for QSIBs and the increase in transportation bond volume would be effective beginning with calendar year 2022.

Disaster relief credits

The proposal provides a nonrefundable tax credit for homeowners and businesses equal to 25 percent of qualified disaster mitigation expenditures capped at $5,000. For individual taxpayers, the credit would begin to phase out at an adjusted gross income of approximately $85,000 for single tax filers and approximately $170,000 for joint filers. For businesses, the credit would begin to phase out when the business has gross receipts above $5 million. The credit would only be available to homeowners and businesses in areas where a federal disaster declaration has been made within the preceding 10-year period or in areas adjacent to where a federal disaster declaration has been made within the preceding 10-year period. The credit would be available for taxable years beginning after the date of enactment.

ASC 740 implications

Pursuant to US Generally Accepted Accounting Principles, the tax effects of new tax legislation are accounted for in the interim and annual reporting periods in which a tax law is enacted. In the US, the enactment date generally is the day the President of the United States signs the legislation into law. Because these proposals have not been enacted, they should not directly impact financial statements. If enacted, the proposals may have a material impact on a company's financial statements. As any tax effects would need to be accounted for in the reporting period of enactment, it may be prudent for companies to start to analyze the impact the proposals would have on their tax accounts and disclosures if enacted.

If the change in tax law is enacted subsequent to the balance sheet date, but prior to issuance of the financial statements, it would be considered a nonrecognized subsequent event and companies would need to discuss the new tax law and, potentially, disclose an estimate of its effect on the entity's financial statements and tax accounts. To the extent potential tax law changes could materially affect the company or its business, SEC registrants should also consider possible disclosure requirements under Risk Factors and Management's discussion and analysis of financial condition and results of operations.

State tax considerations for corporate proposals

Most state income tax regimes are affected by federal tax law changes because, for administrative ease, such state regimes tie to the Internal Revenue Code by either incorporating it in whole or in part, or by using federal taxable income as the starting point. States with automatic or "rolling" conformity generally will adopt such changes unless there is specific state legislation enacted to decouple from federal law. Other states adopt the Internal Revenue Code as of a specific date, do not adopt the code provisions in totality, or provide modifications or exceptions to certain adopted provisions.

The administration's corporate income tax proposals likely to have a direct state tax impact will be those that change federal taxable income. Any such impact will be felt first in the rolling conformity states and may be picked up later by the fixed or static conformity states.

The following administration tax proposals are unlikely to have a material direct impact on the computation of state tax, because none change federal taxable income:

- Raising the corporate income tax rate to 28 percent;
- Imposing a 15 percent minimum tax on book earnings of large corporations; and
- Creating federal tax credits.

However, several proposals, discussed below, would potentially have a direct impact on the computation of state corporate income tax due.

Repeal of the high-tax exception and reduction of the GILTI section 250 deduction: Many states currently provide at least a partial subtraction or dividend-received deduction for GILTI income, with a number allowing a full subtraction. For those that do not decouple or provide a 100 percent subtraction, any federal changes that increase the amount of section 951A inclusion would correspondingly increase state taxable income.

As of the date of this publication, there are 10 jurisdictions that impose tax on GILTI net of the section 250 deduction without any subtraction: New Jersey, New York City, Rhode Island, New Hampshire, Vermont, Maryland, Nebraska, Alaska, Delaware, and District of Columbia. The increase in GILTI caused by the proposed repeal of the high-tax exception and the reduction of the GILTI deduction under section 250 would have an outsized state tax impact, both because foreign tax credits are unavailable to offset state tax and most states do not allow full apportionment representation for the GILTI income. The reduction of the GILTI deduction under section 250 would also have an impact in states that allow a less than 100 percent deduction against net GILTI income, as opposed to gross section 951A income.

Repeal of the FDII deduction under section 250: A repeal of deduction under section 250 for FDII would impact state taxable income in the states that currently couple to that provision of the Internal Revenue Code.

Disallowance of deductions made to certain affiliates under SHIELD: The BEAT has not historically affected state corporate income tax due to its nature as a minimum tax that does not affect the computation of federal taxable income. For example, even if a taxpayer paid federal tax under the BEAT, the computation of state taxable income was still based on its federal taxable income as computed under the Internal Revenue Code. The proposed replacement of the BEAT, referred to as SHIELD, would impact federal taxable income and, accordingly, state taxable income.

Certain types of payments that SHIELD was ostensibly intended to target, such as intercompany interest and intangible payments, have long been required to be added back to income in the majority of states under so-called “intercompany addback” statutes which date back to the early 2000s. Intercompany addback statutes often have exceptions that allow a taxpayer to benefit from a deduction where, for example, the payment is made to an entity resident in a country with a US bilateral tax treaty, is subject to tax at a rate similar to the state tax rate (generally under 10 percent), or is paid out to a third party during the tax year. To the extent that the proposal would disallow a deduction in arriving at federal taxable income, there will be no expense “addback” against which to apply to apply the addback exceptions, unless the state enacts a specific subtraction modification. It is unclear whether states will choose to maintain their existing intercompany addback regimes rather than conform to SHIELD or simply conform to SHIELD and thereby avoid the fact-intensive analysis usually required to determine the applicability of addback exceptions.

Limitation of interest expense based on disproportionate borrowing in the US: The proposed additional limitation on interest expense for US members of a multinational financial reporting group may have significant state tax consequences and complexities. Many states do not follow federal consolidated return rules and either tax each entity on a separate-company basis, as if no consolidated return were filed, or require combined reporting of unitary affiliates, defined in such a way that combined group composition can differ markedly from the section 1504 consolidated group. For example, it is common to have a state combined filing group that includes multiple US brother-sister corporations commonly owned by a foreign parent or, conversely, US affiliates may not file as part of the same combined group if they are not part of the same unitary business.

Under the proposal, the determination of a financial group member's excess net interest expense is to be computed on a separate-company basis, but for this purpose, a US subgroup of a multinational financial reporting group is treated as if it were a single member of that group. The proposal would define a US subgroup as a US entity that is not owned by another US entity, and any of its subsidiaries, foreign or domestic. The Green Book does not discuss how the limitation may be allocated between or among members of a US subgroup. For state purposes, this will be a crucial determination, as different members within the US subgroup may have different state tax filing obligations. For example, if a member of a US subgroup is required to file a state tax return on a separate company basis, it is unclear what ought to be its separate company taxable income if the US subgroup of which it is a part had excess net interest expense. Alternatively, these rules could result in a situation where there is a limitation that affects all members of a US subgroup based on the interest expense paid by a corporation that is not included in the combined group for which a return is filed in a particular jurisdiction.

Section 265 expense disallowance: Under the proposed changes, section 265 would be expanded to disallow previously deducted expenses allocable to dividends under section 245A and the deduction under section 250. Due to the ways some states tie state taxable income to federal taxable income, this change may have state tax implications. Many states do not conform to section 245A or section 250 and, instead, allow their own state statutory deductions for foreign dividends or GILTI income. A large number of these states also have their own expense disallowance rules that encompass the types of disallowance contemplated by the proposed revision to section 265. This creates the potential for an outcome in which both federal and state expense disallowance rules could apply to the same income due to the way in which state taxable income is tied to federal taxable income.

Proposals to disallow deductions and repeal favorable amortization of certain expenditures: States generally do not adopt or otherwise follow federal income tax credits, and as a result, the various federal tax credit related proposals are unlikely to have any state tax impact. However, many of the administration's proposals would create or make permanent a tax credit on the one hand while disallowing expense deductions, or eliminating the preferential amortization of certain expenditures, on the other. For example, one proposal would disallow deductions for expenses paid in connection with offshoring a US trade or business. Other proposals would disallow deductions for, or eliminate favorable amortization of, certain expenditures made by taxpayers in the fossil fuel industry. Absent adoption of a state law that decouples from these deduction-related proposals, there would be a state tax impact.

Tax proposals affecting individuals

The budget blueprint includes several proposed tax increases affecting affluent individuals to pay for what the administration has dubbed "human infrastructure" investments such as education, child care, health care, and paid family leave, and offset the cost of certain enhancements to tax incentives benefitting low-and middle-income taxpayers.

Increase the top marginal tax rate for individual and fiduciary taxpayers: The proposal would increase the top marginal individual and fiduciary income tax rate to 39.6 percent. This rate would be applied to taxable income in excess of the 2017 top bracket threshold, adjusted for inflation. In taxable year 2022, the top marginal tax rate would apply to taxable income over $509,300 for married filing jointly taxpayers ($452,700 for single taxpayers). The proposal would be effective for taxable years beginning after December 31, 2021.

Increase tax rate on tax preferential income: Long-term capital gains and qualified dividends of taxpayers with adjusted gross income of more than $1 million ($500,000 for married filing separately) would be taxed at ordinary income tax rates. This proposal would be effective for gains and dividends "required to be recognized after the date of announcement."

Treat carried interest income as ordinary: A taxpayer may provide services to a partnership in exchange for a partnership interest that participates in profits. This type of partnership interest is commonly known as a "profits interest" or "carried interest." Because the character of a partner's distributive share of partnership items is generally determined at the partnership level, a partner that holds one of these interests may receive a distributive share of long-term capital gain even though a taxpayer usually earns ordinary compensation income from the performance of services. As part of the TCJA, Congress also added section 1061, which extends the long-term holding period requirements for certain capital gains resulting from partnership property dispositions and from partnership interest sales from one to three years.

The Biden administration would change the taxation of profits interests for taxpayers with gross income in excess of $400,000 for taxable years beginning after December 31, 2021. The proposal would repeal section 1061 for taxpayers with gross income in excess of $400,000. Instead, if these taxpayers held an investment services partnership interest (ISPI) in an investment partnership, their distributive share of income would be treated as ordinary regardless of the character of the income at the partnership level. Likewise, any gain from a partner's sale of an ISPI would be taxed at ordinary rates as well.

The Green Book defines an ISPI as a profits interest in an investment partnership held by a person who provides services to the partnership. A partnership would be an investment partnership if substantially all of its assets are investment-type assets, but only if over half of the partnership's contributed capital is from partners in whose hands the interests constitute property not held in connection with a trade or business.

If a partner that holds an ISPI also transfers "invested capital" (*e.g.*, money or other property) to the partnership and the partner's invested capital is a "qualified capital interest," the Green Book explains that income attributable to the invested capital would not be recharacterized as ordinary. Likewise, gain from the sale of an ISPI that is attributable to invested capital would not be recharacterized either. In order for a partner's invested capital to be treated as a qualified capital interest, the partnership would have to make allocations with respect to the invested capital in the same manner that it makes allocations to other capital interests held by partners that do not hold ISPIs (and such allocations are significant).

Subject to income thresholds, the proposal also provides an anti-abuse rule that any person who performs services for any entity and holds a "disqualified interest" in the entity is subject to tax at rates applicable to ordinary income on any income or gain with respect to that interest. A "disqualified interest" is defined as convertible or contingent debt, an option, or any derivative instrument with respect to the entity (but does not include a partnership interest, stock in certain taxable corporations, or stock in an S corporation).

The proposal is not intended to adversely affect qualification of a REIT owning a profits interest in a real estate partnership.

A few points are worth noting. First, profits interests in an upper-tier partnership are often granted to management employees of portfolio companies owned by private equity firms. The interest received is arguably for services rendered for the benefit of the partnership, although the individual is employed by the portfolio company. Given the definition of an ISPI, guidance will be warranted as to the application of the proposed carried interest changes to this common management equity incentive plan arrangement.

Second, the definition of a "disqualified interest" includes options; however, it is unclear how the proposed changes would impact a compensatory option arrangement. Generally, the grant of an option does not trigger a taxable event; rather, the exercise of nonqualified stock options triggers compensation that is taxed at ordinary income tax rates. Guidance will be warranted as to whether the proposed changes will cause the shares acquired pursuant to the exercise of an option to be taxed at ordinary income tax rates, as opposed to capital gains rates, upon disposition.

Treat transfers of appreciated property by gift or on death as realization events: Proposals to tax capital income at substantially higher rates are thought to lose money, as asset holders are frozen from selling and instead plan to leave appreciated assets to their heirs. To address this, the budget proposes to limit the ability to use step-up in basis at death. Under the proposal, "the donor or deceased owner" of an appreciated asset would realize "a capital gain" at the time of the transfer. Gain recognition on assets characterized as income in respect of a decedent is not discussed in this proposal.

A gift or transfer at death would be valued using the methodologies used for estate or gift tax purposes, except that a transferred partial interest would be its proportional share of the fair market value "of the entire property."

The Green Book states that "for purposes of the imposition of this tax on appreciated assets," transfers of property into, and distribution in kind from, a trust (including charitable split-interest trusts), partnership, or other noncorporate entity, other than a grantor trust that is deemed to be wholly owned and revocable by the donor, would be recognition events. Special rules would apply to split-interest trusts having a charitable component. Although the language could be clearer regarding scope, the provision appears to be limited to gifts and transfers on death. What that means or how that provision would apply is not clear and additional guidance and clarification would be needed.

"Gain on unrealized appreciation" also would be recognized by a trust, partnership, or other noncorporate entity that is the owner of property if that property has not been the subject of a recognition event within the prior 90 years, with such testing period beginning on January 1, 1940. The first possible recognition event for any taxpayer under this provision would thus be December 31, 2030.

The following exclusions would apply:

- Transfers by a decedent to a US spouse or to charity would carry over the basis of the decedent.
- The proposal would exclude from recognition any gain on tangible personal property such as household furnishings and personal effects (excluding collectibles).
- The $250,000 per-person exclusion for capital gain on a principal residence would apply to all residences and would be portable to the decedent's surviving spouse, making the exclusion effectively $500,000 per couple.
- The exclusion for capital gain on certain small business stock (under section 1202) would also apply.
- The proposal would allow a $1 million per-person exclusion from recognition of "other unrealized capital gains on property transferred by gift or held at death." The per-person exclusion would be portable to the decedent's surviving spouse, making the exclusion effectively $2 million per married couple.

Under the proposal, the recipient's basis in property received by reason of the decedent's death would be the property's fair market value at the decedent's death.

The Green Book states that "[t]he same basis rule would apply to the donee of gifted property; however, the donee's basis in property received by gift during the donor's life would be the donor's basis in that property at the time of the gift to the extent that the unrealized gain on that property counted against the donor's $1 million exclusion from recognition." As written, this implies that one's $1 million exclusion is consumed while the donee must also take carryover basis. This is certainly different than the described treatment at death where the exclusion is consumed and the successor takes a fair market value basis. It is unclear why there would be a variance.

Under the proposal, gain arising by reason of a death would be taxable income to the decedent. How that gain is to be reported is also not entirely clear; however, "the use of capital losses and carry-forwards from transfers at death would be allowed against capital gains income and up to $3,000 of ordinary income on the decedent's final income tax return," and the tax imposed on gains deemed realized at death would be deductible on the estate tax return of the decedent's estate (if any).

Payment of tax on the appreciation of certain family-owned and operated businesses would not be due until the interest in the business is sold or the business ceases to be family-owned and operated.

Furthermore, the proposal would allow a 15-year fixed-rate payment plan for the tax on appreciated assets transferred at death, other than liquid assets and other than businesses for which the deferral election is made.

The proposal also includes authorization for other legislative changes designed to facilitate and implement this proposal, notably: the achievement of consistency in valuation for transfer and income tax purposes; coordinating changes to reflect that the recipient would have a basis in the property equal to the value on which the capital gains tax is computed; and a broad grant of regulatory authority to provide implementing rules.

The proposal would be effective for gains on property transferred by gift, and on property owned at death by decedents dying, after December 31, 2021 and on certain property owned by trusts, partnerships, and other noncorporate entities (S corporations are not mentioned in this proposal) on January 1, 2022.

Rationalize net investment income (NII) and Self-Employment Contributions Act (SECA) taxes: The proposal would ensure that all trade or business income of high-income taxpayers is subject to the 3.8-percent Medicare tax, either through the NII or SECA taxes.

For taxpayers with adjusted gross income in excess of $400,000, the definition of net investment income tax would be amended to include gross income and gain from any trades or businesses that is not otherwise subject to employment taxes.

Limited partners and LLC members who provide services and materially participate in their partnerships and LLCs would be subject to SECA tax on their distributive shares of partnership or LLC income to the extent that this income exceeds certain threshold amounts. The exemptions from SECA tax currently provided for certain types of partnership income (*e.g.*, rents, dividends, capital gains, and certain retired partner income) would continue to apply.

S corporation owners who materially participate in the trade or business would be subject to SECA taxes on their distributive shares of the business's income to the extent that this income exceeds certain threshold amounts. The current exemptions from SECA tax provided for certain types of S corporation income (*e.g.*, rents, dividends, and capital gains) would continue to apply.

To determine the amount of partnership income and S corporation income that would be subject to SECA tax under the proposal, the taxpayer would take the sum of (1) ordinary business income derived from S corporations for which the owner materially participates in the trade or business and (2) ordinary business income derived from either limited partnership interests or LLC's that are classified as partnerships to the extent a limited partner or LLC member materially participates in its partnership's or LLC's trade or business. This sum is the "potential SECA income."

The additional income that would be subject to SECA tax would be the lesser of (1) the "potential SECA income," and (2) the excess over $400,000 of the sum of the potential SECA income, wage income subject to FICA, and 92.35 percent of self-employment income subject to SECA tax under current law.

The proposal would be effective for taxable years beginning after December 31, 2021.

Repeal deferral of gain from like-kind exchanges: The proposal would limit the deferral of gain from like-kind exchanges of real property to an aggregate amount of $500,000 per taxpayer (or $1 million for married individuals filing joint returns) each year. It would be effective for exchanges completed in taxable years beginning after December 31, 2021.

Permanently extend excess business loss limitation of noncorporate taxpayers: The proposal would make permanent the section 461(l) excess business loss limitation on noncorporate taxpayers and would be effective for taxable years beginning after December 31, 2026. Under current law, section 461(l) limits the extent to which passthrough business losses may be used to offset other income. In particular, for taxable years beginning after December 31, 2020 and before January 1, 2027, noncorporate taxpayers may not deduct an "excess business loss" from taxable income. Instead, these losses are carried forward to subsequent taxable years as net operating losses. An "excess business loss" is defined generally as a loss in excess of the sum of gains from business activity and a specified threshold amount ($262,000 or $524,000 for married couples filing jointly in 2021).

Enhance certain family-focused tax credits: Generally, the budget proposal would make permanent the American Rescue Plan's expansion of the expansion of the earned income tax credit for workers without qualified children, and its enhancements to the child and dependent care credit.

The proposal also would extend the child tax credit increase through 2025 and make permanent full refundability effective for taxable years after December 31, 2021. The proposal would also continue the advance payments of the child tax credit each month.

Permanently extend American Rescue Plan's expansion of the premium tax credit: Eligible individuals who purchase health insurance through a marketplace established under the Patient Protection and Affordable Care Act may claim a refundable premium assistance tax credit. The credit may be paid in advance.

Eligibility is based on an individual's household income and family size. Before 2021, individuals with household incomes between 100 percent and 400 percent of the federal poverty line (FPL) were generally eligible for the credit.

An individual's premium tax credit is equal to the amount by which the cost of a specified benchmark health plan exceeds the individual's required contribution (or the actual amount the individual paid for a health plan, if less). The individual's required contribution is a percentage of the individual's household income (referred to as the "applicable contribution percentage"). The applicable contribution percentage varies depending on amount of the individual's household income relative to the FPL and is indexed for years after 2018 to reflect the rate of premium growth relative to the consumer price index.

The American Rescue Plan decreased the credit's applicable contribution percentages (thereby decreasing the percentage of household income individuals must spend on health care) and extended eligibility to individuals with household incomes over 400 percent of the FPL such that the credit for those individuals gradually phases out as household income increases. The American Rescue Plan also froze the indexing of the applicable contribution percentage. The changes made the under the American Rescue Plan are effective for 2021 and 2022.

The budget blueprint would make the changes enacted in the American Rescue Plan permanent, effective after December 31, 2022.

Eliminate fossil fuel tax preferences: The proposal would repeal a number of oil and gas-related tax preferences. (See separate discussion of energy-focused tax provisions elsewhere in this report for details.)

Impose stronger compliance and reporting requirements: The administration would beef up the Internal Revenue Service's enforcement efforts through proposals to significantly expand electronic filing requirements, create a comprehensive financial account information reporting regime, and expand broker information reporting with respect to cryptocurrency assets. (See separate discussion of compliance, information reporting, and tax administration provisions elsewhere in this report for details.)

Notable items *not* in the budget: Although then-candidate Joe Biden called for capping the value of itemized deductions, eliminating the 20 percent deduction for certain passthrough income, imposing FICA tax on income over $400,000, and making other changes to the estate and gift tax rates and exemption during the presidential campaign, those proposals are not included in his budget blueprint. Also not in the budget package is a proposal to ease or repeal the current-law cap on the deduction for state and local taxes that was enacted in the TCJA. (Although the president has never officially taken a position on this issue, proposals to address the cap have support among congressional lawmakers in both parties who represent jurisdictions with high local income and property taxes.)

State tax considerations for individual tax proposals

Questions about the interplay between federal tax law changes and state tax regimes (a concept discussed in the corporate tax section above) also arise with respect to the administration's individual tax proposals.

The following tax proposals are unlikely to have a material direct impact on the computation of state tax, because none change federal adjusted gross income or taxable income:

- Increasing the top marginal income tax rate to 39.6 percent for upper-income earners;
- Taxing capital gain income of upper-income earners at ordinary income tax rates;
- Rationalizing net investment income and Self-Employment Contributions Act taxes; and
- Enhancing various family-focused tax credits.

The proposals discussed below, however, may have a direct impact on the computation of state corporate income tax due.

Treat transfers of appreciated property by gift or death as realization events: Under the proposal, donors or deceased owners of appreciated assets would report gain on the federal gift or estate tax return or a separate capital gains return. As such gains do not appear to increase the taxpayer's federal adjusted gross income or taxable income, as reported on Form 1040, this federal tax change may not have a state tax impact. However, if these gains do increase the taxpayer's federal adjusted gross income or taxable income, the proposal would have a state tax impact. Additionally, it is possible that states could enact similar legislation to tax gains on appreciated assets transferred by gift or death. It should be noted that many states do not currently impose estate or gift taxes, and many of those that do have decoupled from the federal estate and gift tax.

The proposal also provides that gains on unrealized appreciation could be recognized by a trust, partnership, or other noncorporate entity that is the owner of property if that property has not been the subject of a recognition event within the prior 90 years. The proposal does not indicate how these gains are to be reported by the trust, partnership, or other noncorporate entity. If these gains increase the federal adjusted gross income or taxable income of a taxpayer, then states that conform to these changes will also tax these gains.

Tax carried interests as ordinary income: Most states have their own tax rates and are not impacted by changes to the characterization of the income as capital gain or self-employment income. However, there are a few states where the characterization of the income as capital gain or self-employment income may have state tax consequences. For example, certain states that tax partnerships, such as Tennessee, allow a deduction for self-employment income. There are also a few states that have special tax rates or special deductions for capital gains.

Repeal deferral of gain from like-kind exchanges: In states that conform to these changes, taxpayers will pay additional state tax on gains that are recognized in the year of the transfer. In addition, a few states have rules that could result in recognition of the deferred gain if the taxpayer leaves the state and is no longer a taxpayer.

Make permanent excess business loss limitation for noncorporate taxpayers: Many states have conformed to the excess business loss limitations and will probably conform to making these rules permanent. A few states conformed to the excess business loss limitations for certain types of taxpayers, but not for others. For example, Illinois conformed to the excess business loss limitations for individuals, but not for trusts.

Compliance, information reporting, and tax administration provisions

The administration contends that it can raise significant revenue by reducing the so-called "tax gap" – the difference between the amount of tax owed to the government and the amount actually collected. To that end, the budget blueprint proposes to beef up the Internal Revenue Service's enforcement budget to enable the agency to better identify sophisticated tax-avoidance transactions and would expand information reporting and other rules to promote taxpayer compliance.

Provide additional funding for tax administration: The Green Book notes that the IRS's operating budget has decreased by roughly 20 percent between 2010 and 2020. During this same period, the IRS has been required to identify and respond many emerging areas of noncompliance, implement significant tax legislative changes, and stand up several new or expanded programs in response to a global pandemic and economic crisis.

In response to these challenges, the administration is proposing a multi-year increase in discretionary spending for IRS Enforcement and Operations Support accounts in the amount of $6.7 billion over the 10-year budget window. This proposed allocation adjustment for 2022 would fund an additional $417 million in enforcement and compliance initiatives and investments.

The administration also proposes to provide the IRS $72.5 billion in mandatory funding over the budget window to fund improvements and expansions in enforcement and compliance activities – such as enhancing its information technology capability, implementing the proposed financial information reporting regime (more on that below), and strengthening taxpayer service. The proposal would direct these additional resources toward enforcement efforts focused specifically on the highest-income taxpayers.

Additional financial account reporting to improve tax compliance: According to the administration, the annual tax gap for business income (other than for large corporations), which it estimates to be $166 billion, is driven by the lack of comprehensive information reporting. The administration claims this lack of information reporting results in difficulty identifying noncompliance outside of an audit. In an attempt to address this tax gap, the administration proposes to create a comprehensive financial account information reporting regime. The new regime would impose an annual information return requirement on all business and personal accounts from financial institutions, including bank, loan, and investment accounts, except those that meet a *de minimis* threshold. Specifically, the proposal would require financial institutions to report gross inflows and outflows with a breakdown for physical cash, transactions with a foreign account, and transfers to and from another account with the same owner, except for those accounts with a gross flow below a threshold of $600.

Other accounts with characteristics similar to financial institution accounts would be covered under this information reporting regime. In particular, payment settlement entities would collect Taxpayer Identification

Numbers (TINs) and file a revised Form 1099-K expanded form to all payee accounts (subject to the same *de minimis* threshold), reporting not only gross receipts but also gross purchases, physical cash, payments to and from foreign accounts, and transfer inflows and outflows.

Similar reporting requirements would apply to crypto asset exchanges and custodians, as well as to taxpayers who buy and transfer crypto assets from broker to broker and businesses that receive crypto assets with a fair market value of more than $10,000.

The Secretary would be given broad authority to issue regulations necessary to implement this proposal.

These proposals would be effective for tax years beginning after December 31, 2022.

Increase oversight of paid tax return preparers: To ensure that paid tax return preparers are operating in a professional manner, the administration proposes to amend Title 31 of the US Code to provide the Secretary with explicit authority to regulate all paid preparers of federal tax returns, including by establishing mandatory minimum competency standards. This provision would be effective on the date of enactment.

'Ghost' preparers: The administration also would increase the penalty for paid tax return preparers who fail to identify themselves on tax returns (also known as "ghost preparers.") The IRS's penalty assessment authority in the case of ghost preparers is currently limited to $50 per return, not to exceed $25,000 per preparer per year. Under the proposal, the penalty amount would increase to the greater of $500 per return or 100 percent of the income derived per return by a ghost preparer. The limitation period for assessing a penalty would be increased from three years after a return has been filed to six years. The proposed changes would be effective for returns required to be filed after December 31, 2021.

Enhance accuracy of tax information: The Department of the Treasury and the IRS currently have the authority to issue regulations that require electronic filing of certain specified returns if the taxpayer files a minimum number of returns during a year. The IRS also requires backup withholding to a reportable payment if a payee fails to furnish the payee's TIN to the payor in the manner required.

Currently, the IRS may only require that the payee furnish the TIN under penalties of perjury with respect to interest, dividends, patronage dividends, and amounts subject to broker reporting.
The budget proposal would expand the Secretary's authority to require electronic filing for forms and returns to include: (1) income tax returns of individuals with gross income of $400,000 or more; (2) income, estate, or gift tax returns of all related individuals, estates, and trusts with assets or gross income of $400,000 or more in any of the three preceding years; (3) partnership returns for partnerships with assets or any item of income of more than $10 million in any of the three preceding years; (4) partnership returns for partnerships with more than 10 partners; (5) returns of REITs, REMICs, RICs, and all insurance companies; and (6) corporate returns for corporations with $10 million or more in assets or more than 10 shareholders.

Further, electronic filing would be required for the following forms: (1) Forms 8918, "Material Advisor Disclosure Statement"; (2) Forms 8886, "Reportable Transaction Disclosure Statement"; (3) Forms 1042, "Annual Withholding Tax Return for US Source Income of Foreign Persons"; (4) Forms 8038-CP, "Return for Credit Payments to Issuers of Qualified Bonds"; and (5) Forms 8300, "Report of Cash Payments Over $10,000 Received in a Trade or Business."

Return preparers that expect to prepare more than 10 corporation income tax returns or partnership returns would also be required to file such returns electronically. In addition, the Treasury Department and the IRS would also be authorized to determine additional returns, statements, and other documents that must be filed in electronic form.

Separately, in order to improve information reporting for reportable payments subject to backup withholding, the proposal would permit the IRS to require payees of any reportable payments to furnish their TINs to payors under penalty of perjury. The proposal would be effective for payments made after December 31, 2021.

Expand broker information reporting with respect to crypto assets: Under current law, any person doing business as a broker is required to report certain information about their customers to the IRS, such as the identity of each customer, the gross proceeds from sales of securities and certain commodities for such customer, and, for covered securities, cost basis information.

The proposal would require brokers, including entities such as US crypto asset exchanges and hosted wallet providers, to report information relating to certain passive entities and their substantial foreign owners. This would allow the IRS to require a broker to report gross proceeds and other information with respect to sales of crypto assets for customers, and, in the case of certain passive entities, their substantial foreign owners.

The proposal would be effective for returns required to be filed after December 31, 2022.

Address taxpayer noncompliance with listed transactions: The IRS have identified "Intermediary Transaction Tax Shelters" as listed transactions that require disclosure on a tax return to avoid certain penalties. According to Treasury's Green Book, in a typical case of this sort, an intermediary purchases the stock of a C corporation from the C corporation's shareholders, then sells the C corporation's assets. The C corporation does not pay the tax owed from the asset sale. The intermediary does not pay the corporate income tax liability and is judgment-proof, frustrating the IRS's ability to collect taxes that are legally owed. The transaction may yield the selling shareholders a higher sales price for their C corporation stock than could be supported if the corporate income tax liability were to be paid.

The proposal would increase the assessment statute of limitations for returns reporting benefits from listed transactions from three years to six years. The proposal also would increase the limitations period for listed transactions under section 6501(c)(10) from one year to three years.

The Green Book notes that under certain circumstances, the proposal would impose on shareholders who sell the stock of an "applicable C corporation" secondary liability ("without resort to any state law") for payment of the applicable C corporation's income taxes, interest, additions to tax, and penalties to the extent of the sales proceeds received by the shareholders.

The proposed changes above would be effective for sales of controlling interests in the stock of applicable C corporations occurring on or after April 10, 2013. For taxpayers that reported a listed transaction on their tax return, this proposal could reopen the assessment statute of limitations for a year for which the assessment statute had already closed.

Amend the centralized partnership audit regime to address tax decreases greater than a partner's income tax liability: Under section 6226, review year partners compute the changes in tax liability resulting from adjustments to the partnership's tax return and take into account the changes in tax liability on their reporting year tax return. If the calculation results in a net decrease, then that amount can be used by the partners to reduce their reporting year income tax liabilities to zero. The amount of the net negative change in tax that exceeds the reporting year income tax liability does not result in an overpayment that can be refunded nor can that amount be carried forward; rather, it is permanently lost.

Several states have passed legislation in response to the centralized partnership audit regime. However, few of these states, if any, have adopted the federal mechanics for partners to reduce their state tax on the reporting year return. Most states require the partners to amend their state tax returns for the reviewed year and all subsequent years impacted by the change.

The proposal would amend sections 6226 and 6401 to provide that the amount of the net negative change in tax that exceeds the income tax liability of a partner in the reporting year is considered an overpayment under section 6401 and may be refunded.

The proposal would be effective upon enactment.

Requisite supervisory approval of penalty included in notice: Section 6751(b)(1) provides that no penalty under Title 26 shall be assessed unless the initial determination of such assessment is personally approved in writing by the immediate supervisor of the individual making such determination or by a higher-level official as the Secretary of the Treasury or her delegate may designate.

This proposal would clarify that a penalty can be approved at any time prior to the issuance of a notice from which the Tax Court can review the proposed penalty and, if the taxpayer petitions the court, the IRS may raise a penalty in the court if there is supervisory approval before doing so. For any penalty not subject to Tax Court review prior to assessment, supervisory approval may occur at any time before assessment. In addition, this proposal expands approval authority from an "immediate supervisor" to any supervisory official, including those that are at higher levels in the management structure or others responsible for review of a potential penalty. Finally, this proposal would eliminate the written approval requirement under section 6662 for underpayments of tax; section 6662A for understatements with respect to reportable transactions; and section 6663 for fraud penalties.

The proposal would be effective upon enactment.

Authorize limited sharing of business tax return information: Current law authorizes the IRS to disclose certain federal tax information (FTI) for governmental statistical use. Business FTI may be disclosed to officers and employees of the Census Bureau for all businesses. Similarly, business FTI may be disclosed to officers and employees of the Bureau of Economic Analysis (BEA), but only for corporate businesses. The Bureau of Labor Statistics (BLS) is currently not authorized to receive FTI.

This proposal would give officers and employees of BEA access to FTI of those sole proprietorships with receipts greater than $250,000 and of all partnerships.

The proposal would also give BLS officers and employees access to certain business (and tax-exempt entities) FTI including:

- TIN;
- Name(s) of the business;
- Business address (mailing address and physical location);
- Principal industry activity (including business description);
- Number of employees and total business-level wages (including wages, tips, and other compensation, quarterly from Form 941, Employer's Quarterly Federal Tax Return, and annually from Forms 943, Employer's Annual Federal Return for Agricultural Employees, and 944, Employer's Annual Federal Tax Return); and
- Sales revenue for employer businesses only.

BLS would not have access to individual employee FTI.

What's next?

Although the budget gives the president the opportunity to formally lay out his tax policy agenda, these proposals are not binding and the authority for drafting actual legislation lies with members of Congress. But Congress does not speak with one voice and, based on comments from lawmakers in the weeks since President Biden released his American Jobs Plan and American Families Plan, his proposals are likely to be modified to some degree regardless of whether he is able to reach a bipartisan deal on an infrastructure package with congressional Republicans (which would mean winning over at least 10 GOP lawmakers in the Senate to avert a filibuster) followed by a smaller Democrats-only bill under fast-track budget reconciliation protections or decides instead to abandon negotiations with Senate Republicans and enact as much of the American Families Plan and American Jobs Plan as possible using budget reconciliation.

Pushback from Republicans: During the 2020 election campaign and since becoming president, Biden has touted his history as a dealmaker over his 30-plus years in the Senate and his two terms as Barack Obama's vice president. But despite his stated preference for moving major legislation through Congress on a bipartisan basis, efforts to reach an agreement with Republicans on the American Rescue Plan earlier this year fell flat and talks between White House and GOP senators on infrastructure legislation in recent weeks have shown few signs of significant progress.

Discussions over the president's American Jobs Plan have laid bare three fundamental areas of disagreement.

- **Size:** The White House initially proposed an expansive infrastructure package that it estimated would cost as much as $2.7 trillion over eight years, but recently offered to trim that figure to $1.7 trillion. A group of Republican senators led by Shelley Moore Capito of West Virginia this week presented a revised counteroffer of $928 billion (up from an earlier proffer of $568 billion) and Senate Minority Leader Mitch McConnell, R-Ky., indicated that he might be willing to go even higher. Although the White House has indicated that talks with Republicans will continue over the upcoming Memorial Day recess, closing what is still a significant gap between the two plans likely would require major concessions from both sides.
- **Scope:** The White House and Republicans also remain at odds over just what constitutes "infrastructure." Republicans have been adamant that an infrastructure package should focus on traditional projects such as roads, bridges, airports, ports and waterways, and broadband. They have rejected the less traditional proposals in the American Jobs Plan – such as expanding affordable housing and improving home- and community-based care for children, the elderly, and individuals with disabilities – which they see as more akin to social spending programs.
- **Offsets:** Consensus over how to pay for the president's spending proposals also appears elusive. The White House has said that it wants to enact the American Jobs Plan and the American Families Plan without adding to the deficit and has proposed to do that largely by repealing or rolling back significant provisions in the TCJA. Republican leaders regard the TCJA as untouchable, although they have said they are open to funding infrastructure projects through user fees, repurposing unused COVID relief funds that have already been allocated to states and localities, and measures to promote public-private partnerships. The White House so far has rejected user fees, arguing that they would violate the president's pledge not to increase taxes on low- and middle-income taxpayers, and it continues to assert that the tax code needs to be recalibrated so that large corporations and affluent individuals pay "their fair share" of the tax burden. The administration also contends there are not large pockets of unused COVID relief funds that can be repurposed for infrastructure spending without undermining the goals of the original COVID bills.

Pushback from Democrats: As efforts to negotiate a bipartisan accord have continued, some congressional Democrats – particularly in the progressive wing of the party – are pushing for President Biden to abandon talks with the GOP and move forward with a broad Democrats-only bill that could be advanced through both chambers under filibuster-proof budget reconciliation rules, similar to the path Biden ultimately adopted to move the American Rescue Plan in the first months of his presidency. Democratic leaders may have at least two more opportunities to pursue a reconciliation bill this year. One would involve adopting a budget resolution for upcoming fiscal year 2022, which begins October 1, that includes reconciliation instructions. The 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 (although major questions remain as to how that process might work and what limitations it may place upon the majority party, leaving many observers unsure if this "second bite at the apple" is actually available and advisable.)

But taking the route of budget reconciliation would require nearly unified Democratic support in a House where the party has just a single-digit majority and absolute unity in a Senate that's divided 50-50, with the majority hinging on the tie-breaking vote of Vice President Harris. And several factors suggest that the White House may not yet have all the votes it needs for success.

First, some centrist Democrats in the Senate, such as Joe Manchin of West Virginia, have indicated they are not yet ready to abandon bipartisan negotiations. That could leave Democratic leaders short of the 50 votes they would need in that chamber (along with Vice President Harris as the tie-breaker) to authorize a budget resolution with reconciliation instructions and on a subsequent reconciliation bill.

Second, some Senate Democrats have raised specific policy concerns with the president's proposals. Manchin and Virginia Sen. Mark Warner, for example, have said they believe Biden should raise the corporate tax rate to just 25 or 26 percent rather than the 28 percent he has proposed. Moreover, Warner and New Jersey Democrat Robert Menendez recently commented that although they believe the gap between capital gains and ordinary income tax rates needs to be narrowed, they feel the president's proposal to tax capital gains at ordinary rates could be an overreach. And Montana Democrat Jon Tester this week expressed strong reservations about the proposed repeal of stepped-up basis that the administration intends to pair with a higher capital gains rate to counter the lock-out effect that would otherwise cause higher rates to yield less revenue. (It's also worth noting that changes to the president's proposed tax increases could require tweaks on the spending side or potentially additional federal borrowing to address a likely reduction in the estimated revenue score.)

Third, regional considerations may also present obstacles to Democratic unity on certain policy issues. A number of Democrats – particularly in the House – who represent jurisdictions with high state and local income and property taxes have said they would not support any significant tax package that does not include a provision that repeals or substantially alleviates the impact of the TCJA's $10,000 cap on the deduction for state and local taxes. But any serious effort to repeal or relax 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. Other House Democrats whose districts include agricultural regions have indicated that they want any proposed repeal of stepped-up basis at death to also include a robust exception for family farms and small businesses.

Questions about timing: President Biden had initially set Memorial Day as an informal deadline for deciding which legislative path he intends to pursue. In the wake of the GOP's latest counteroffer, however, White House Press Secretary Jen Psaki appeared to back off of that marker, telling reporters on May 27 that the administration "look[s] forward to making progress before Congress resumes on June 7."

For her part, House Speaker Nancy Pelosi, D-Calif., continues to state that she hopes to move legislation through her chamber by the July 4 recess. Senate Majority Leader Charles Schumer, D-N.Y., likewise indicated this week that he expects his chamber to take up a bill in July.

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