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Greetings,

In September, I covered the proposed tax plan released by Democrats on the House Ways and Means Committee, which would help pay for the $3.5 trillion Build Back Better Act through changes to corporate, personal and other taxes, as well as retirement plans.

On Thursday, October 28th, a new draft of the bill was released, and that $3.5 trillion price tag was cut in half to $1.75 trillion as a host of provisions – including paid family leave and an expansion of Medicare (however some Medicare provisions remained) – were dropped from the bill. That lower price tag also means a lot of those tax and retirement planning changes needed to fund a more expansive spending plan were cut. Still in the proposal is expanded school spending, clean energy initiatives, expanded home care provisions, more child care credits and funding for other hard infrastructure expenditures.

As with the last draft of the bill, this proposal is still not final. Democrats in the Senate plan to pass the bill through the budget reconciliation process, which means they need all 50 of their members on board. That could mean a few last-minute changes are still in store ahead of a final vote because it's not clear that there are enough votes yet for this bill to pass.

Furthermore, just because certain provisions were cut, especially around retirement plans, **it does not mean that they won't come back in another bill like in the retirement focused bill being called**

the SECURE Act 2.0 bill, which also has a decent chance of being modified and passed by end of year.

Let's dive into what's changed from the last draft of the bill, as well as some new additions to this version.

What's Changed from the Previous Bill

Retirement Plan Changes

Before: The previous draft of the BBB Act had numerous changes to retirement accounts, including limits on traditional IRA contributions, changes to required minimum distributions for high-income earners, limits on Roth conversions and an end to so-called "back-door" Roth conversions.

Now: All of these retirement planning changes have been scrapped. And with back-door Roth conversions still being allowed, it may make more sense for individuals with large retirement accounts to convert assets to Roth IRAs over time so that their estates will not be subject to the 10-year withdrawal rule.

Estate Tax Returns to Old Levels

Before: The estate and gift tax exemption would return to $5 million ($10 million for married couples) in 2022, after the 2017 Tax Cuts and Jobs Acts signed by President Donald Trump pushed that number to $11.7 million ($23.4 million for married couples). No change would be made to the step-up in basis rule.

Now: The estate and gift tax exemption would remain at $11.7 million for individuals ($23.4 million for married couples). As before, no change would be made to the step-up in basis rule.

Increased Income Tax for Top Earners

Before: The highest personal income tax bracket would jump from 37% to 39.6%. The proposal also added a 3% surtax on individuals with modified adjusted gross income over $5 million.

Now: The top personal income bracket would remain at 37%. However, there would be a 5% surtax on annual modified adjusted gross income over $10 million for all individuals except married filing separately ($5 million). There would then be an additional 3% surtax on income over $25 million. This would directly impact only the wealthiest 0.02% of Americans.

An Increased Capital Gains Tax

Before: The top rate for taxes on capital gains and dividends tax would increase from 20% to 25%.

Now: The capital gains tax rate would remain at 20%.

A Higher Corporate Tax Rate

Before: The top federal corporate tax rate would increase from 21% to 26.5% starting in 2022.

Now: The top federal corporate tax rate would remain at 21%, but large companies would now face a minimum 15% rate. That minimum rate would apply to corporations with more than $1 billion in profits annually over a three-year period, and would put a floor on how much they could lower their tax rate through loopholes. For instance, Amazon has reported $45 billion in profits over the past three years and paid an effective tax rate of 4.3%.

Additionally, the bill would impose a 1% surcharge on stock buybacks by large corporations.

What Stayed from the Previous Bill

'Wash Sale' Rules for Cryptocurrency

Starting in 2022, cryptocurrencies like bitcoin and ethereum would be subject to anti-abuse rules that currently apply to stocks, bonds and other securities. “Wash sale” rules are intended to prevent investors from taking advantage of tax benefits after selling a losing investment, then immediately buying back that same investment at a lower cost.

Currently, crypto investors can sell currency for a loss and claim a tax benefit, then buy the same currency back shortly after, potentially at a lower price than it was sold. **Under the proposal, crypto investors would have to wait 30 days before rebuying that currency to avoid penalties.**

International Tax Overhaul

International taxes on U.S. multinational companies have been a strongly debated topic for the past few years, preceding even the changes that took place in 2017 as part of the Tax Cuts and Jobs Act. The new changes would increase the taxes on foreign profits from U.S. multinational companies.

The goal here is to not allow companies to side-step U.S. taxes by claiming they pay low taxes in other countries that essentially serve as a tax haven. The change would, in essence, create a minimum tax for certain international companies operating in the U.S. It’s projected this could raise hundreds of billions of dollars in new revenue and potentially even have incentives in its structure to move more operations to the U.S. While there was a proposed minimum corporate tax in the earlier BBB draft, this was modified a bit in this version of the bill.

What’s New in This Bill

Though much was changed from the last version of the BBB Act, a few new proposals were added.

Additional Taxes on Large Trusts and Estates

The new tax on money taken from trusts or estates starts at a 5% rate for anything in excess of $200,000, with an additional 3% for anything over $500,000. **You may not be able to avoid this tax if you inherit a**

large IRA or other retirement account from a non-spouse, because the SECURE Act requires you to withdraw the money within 10 years. So if you inherit a $5 million IRA, you're looking at $500,000 withdrawals each year (plus any market gains), and you could get pushed into the full 8% tax rate depending on your modified adjusted gross income (MAGI).

Child Tax Credit

The enhanced credit – passed in March through the American Rescue Plan – will continue through 2022. **It provides $3,000 for children ages 6 to 17 (up from $2,000), with an additional $600 for children under the age of 6.** The credit begins to phase out above certain income levels – $75,000 for individuals or $150,000 for married couples.

IRS Funding

The bill calls for an $80 billion increase in funding for the IRS – several projections show that the IRS, if it were properly funded, could raise more money by just enforcing current laws. One CBO report suggested that with this $80 billion increase, the IRS could raise roughly $200 billion in new revenue.

What Could Still Be Added to the Bill?

This version of the BBB Act doesn't include any **changes to the cap on state and local income tax (SALT) deduction. That amount – which allows filers to reduce their federal tax burden by the amount they pay in state and local taxes – was capped at $10,000 as part of 2017's Tax Cuts and Jobs Act, and that cap will remain in place through 2025.**

Democrats had debated several changes to the cap – one proposal was to suspend the $10,000 limit for two years, reinstate it in 2024 and then remove it entirely starting in 2026 – but nothing made it into this version of the bill. It's possible some kind of change could make it into the bill before it's finalized.

What's Next?

The Biden administration and Democrats in Congress are pushing to pass the Build Back Better Act relatively quickly, and the current framework will likely be close to the final version.

And though many of the previously proposed changes to personal taxes and retirement planning were dropped from this bill, they may still make it into the SECURE Act 2.0 – though, much like with the BBB Act, there's no guarantee they'd survive negotiations among the Democrats' narrow Senate majority.

Please let us know if you have any questions or if we can be of any assistance.

Debbie

Thanks and Regards,

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