# THE NEW LEGISLATIVE LANDSCAPE

## WAYS & MEANS PROPOSALS OF INTEREST TO FAMILY OFFICES

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# SPEAKERS

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# STATUS & LIKELIHOOD

- Two bills pending
  - Infrastructure bill
    - Bipartisan
    - Passed Senate
    - Held up by Democratic progressives in House
  - Reconciliation bill
    - Partisan – would pass only with 50 votes plus VP in Senate
    - Proposed $3.5 trillion cost more than some Democrats will accept
    - Contains Ways & Means tax provisions paying for entire $3.5 trillion
    - If a deal reduces the size of the bill, there would be room to cut back the tax provisions

# STATUS & LIKELIHOOD, *CONTINUED*

# STATUS & LIKELIHOOD, *CONTINUED*

- Tax proposals for the Reconciliation bill
  - Released by Ways & Means September 13 and approved September 15
  - 368 pages of legislative language
  - 293 page Joint Committee Technical (JCT) Explanation
- Must still be included in a House bill and passed by the House
- Ways & Means proposals will not be enacted as is, but need to be monitored
  - Further along in the process than previous proposals or the Wyden proposals – legislative language, JCT technical analysis, revenue estimates
  - Historically, once provisions reach this stage, the chance that they will be enacted in this or a future legislative cycle is increased

# TRANSFER TAXES

- Basic Exclusion (Lifetime Estate & Gift + Generation-Skipping Transfer Tax (GST) Exemption)
  - Current law $11.7 million scheduled to reduce to approximately $6.2 million in 2026
  - Proposals would accelerate reduction to 2022
  - Internal Revenue Service (IRS) has announced that the use of excess exemption by current gifts will not later be recaptured
- Valuation Discounts
  - Not allowed for nonbusiness assets
  - Transfers after date of enactment

# TRANSFER TAXES, *CONTINUED*

- Grantor Trusts
  - Current law permits certain irrevocable grantor trusts to be completed gifts but ignored for income tax purposes (intentionally defective grantor trusts or IDGT's)
    - Not included in grantor's estate
    - Trust distributions are not taxable gifts from the grantor
    - Grantor pays the taxes on the trust's income without making an additional gift to the trust
    - Sales to grantor trusts are disregarded for income tax purposes
    - Note payments can be made in kind without triggering gain
    - A Grantor Retained Annuity Trust (GRAT) is a special type of IDGT
    - Congress and Treasury are the source of these tax advantages and the grantor trust rules no longer serve their original purpose because of adverse income tax rules applicable to trusts

# WAYS & MEANS HOUSE PROPOSAL

- Irrevocable Defective Grantor Trusts
  - Would be included in grantor's estate (first time since Section 2036(c) was repealed and replaced by Chapter 14 Congress imposed an "estate tax solution to a gift tax problem")
  - Trust distributions to beneficiaries other than grantor would be treated as gifts
  - Because initial funding of trust would remain a gift, complex double-counting rules would be needed
  - Because of estate inclusion rule drastically altering transfer tax treatment of these trusts, IDGT's created before date of enactment would not be affected by these transfer tax changes
  - Contributions after date of enactment to grandfathered trusts would be subject to the new transfer tax changes
  - Sales to grantor trusts other than revocable trusts would be recognized (unclear what other transactions would be recognized)
  - Leaves beneficiary grantor trusts untouched (use of 5X5 power)

# INCOME TAXES

- Rate Increases – Individuals & Trusts
  - Capital gains and qualified dividends: 20% increased to 25% for sales and dividends received after September 13, 2021
  - Ordinary income: 37% increased to 39.6% starting in 2022
  - 199A 20% pass-through deduction limited to $400,000 of pass-through income
    - Top pass-through rate would increase from 29.6% (80% of 37%) to 39.6%
  - 3% surtax beginning in 2022
    - Individual – on Adjusted Gross Income (AGI) over $2.5 million
    - Joint return – on AGI over $5 million
    - Taxable trusts unless all beneficiaries charitable – on AGI over $100,000
    - 163(j) disallowed interest allowed for this purpose
    - Not considered a regular tax for Alternative Minimum Tax (AMT) purposes

# INCOME TAXES, *CONTINUED*

- Rate Increases – C corporations
  - Regular rate 21% to 26.5% effective in 2022
  - Global Intangible Low-Taxed Income (GILTI) rate 10.5% to 16.5625%, and country by country
  - Foreign Derived Intangible Income (FDII) rate 13.125% to 20.7%

# INCOME TAXES, *CONTINUED*

- 3.8% loopholes plugged
  - Active income added to NII for taxpayers over $400,000
  - So, S corporation and Limited Partnership (LP) exceptions to 1402 don’t help
  - Existing 1411(c)(6) prevents double inclusion with 1402 for general partners and Limited Liability Company (LLC) members
- 461(l) excess business losses – discussed later
- Worthless stock – date of worthlessness rather than year-end
- Worthless partnership interests – capital loss
- Portfolio interest exemption from withholding tightened

# INCOME TAXES, *CONTINUED*

- 1061 Carried interest changes – covered in later presentation
- 1202 Qualified Small Business Stock (QSBS)
  - 100% exclusion reduced to 50% for taxpayers over $400,000
  - Sales after September 12, 2021
  - No grandfathering for investments made in reliance
- 1259 constructive sales
  - Applied to digital assets
  - Cryptocurrency and Non-Fungible Tokens (NFTs)

# INCOME TAXES, *CONTINUED*

- 52(b) common control
  - Applies to 212 activity
- 1091 wash sales expanded to:
  - Securities as defined in 475
  - Foreign currency
  - Commodities
  - Digital assets
- S Corporation Liquidation
  - If an S corporation on May 13, 1996, and all times, thereafter, can convert to domestic partnership tax-free in 2022 or 2023
  - May 13, 1996, is the date the proposed check-the-box regulations were issued

# RETIREMENT PLANS

- Required minimum distribution 50% of balance over $10 million
  - Applies if AGI over $400,000
  - Aggregate Individual Retirement Accounts (IRAs) and 401(k)s
  - Roth IRA (Roth) distributions taxable if <59 ½
- No further contribution to IRA over $10 million if individual over $400,000
  - Aggregate regular IRAs and 401(k)s
- Backdoor Roth not allowed
  - Roths limit contributions more than regular
  - “Backdoor” means contribute to regular (after tax), then convert to Roth

# RETIREMENT PLANS, *CONTINUED*

- IRA investments in related entities
  - Current rule that IRA cannot invest in entity 50% owned by beneficiary
    - changed to 10%
    - Applicable if IRA owner is an officer, regardless of percentage
    - Changed from a prohibited transaction to a disqualifying event
- IRA investments requiring accredited investor status
  - Disqualifies the IRA
  - Two years to divest existing holdings

# THANK YOU!

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