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Biden doubles down on corporate, high-wealth tax increases in FY 2025 budget blueprint

Building on the message of tax code "fairness" he laid out in his State of the Union address just days ago, President Joe Biden released a budget blueprint for fiscal year 2025 on March 11 that, like his previous budget proposals, draws heavily on tax increases targeting multinational corporations and other large businesses, the fossil fuel industry, and high-income and high net-worth individuals to pay for tax relief for lower- and middle-class individuals and an array of spending priorities, help ensure the solvency of Social Security and Medicare, and reduce the deficit.

Tax policy at a glance

Some of the administration's proposed revenue offsets are new this year, while others have been carried over from previous White House budget packages. A number of the holdover provisions had been contenders for

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inclusion in the Inflation Reduction Act (P.L. 117-169), which Democrats moved through Congress in 2022 under fast-track budget reconciliation rules—but were left out of the legislation as enacted.
URL: https://www.congress.gov/117/plaws/publ169/PLAW-117publ169.pdf

Corporate and business provisions: On the business side, notable returning proposals include an increase in the corporate tax rate to 28 percent, international reforms intended to move the US toward compliance with the OECD's Pillar Two model rules, and repeal of various deductions and credits currently available to fossil fuel companies.

The president also has renewed his call from last year to strengthen a corporate tax hike that *was* enacted in the Inflation Reduction Act—the excise tax on stock buybacks—by increasing the rate to 4 percent from its current-law level of 1 percent.

Among the new revenue items this year are proposals to deny employers a deduction for salary over $1 million to *any* employee (an expansion of a current limitation that applies only to certain specified high-level corporate officers and highly compensated employees) and eliminate certain tax provisions that the administration contends provide favorable tax treatment for corporate jets compared to commercial aircraft.

High-wealth provisions: Returning proposals targeted at high-income and high-net worth individuals include, among others, an increase in the top marginal income tax rate to 39.6 percent; changes to the tax treatment of capital gains, dividends, and carried interests; and provisions to tighten the estate and gift tax rules. Also hitting the comeback trail this year is a proposed 25 percent minimum tax on ultrawealthy taxpayers.

In addition, the White House proposes once again to tighten the rules around tax-preferred retirement plans to prevent certain wealthy individuals from accumulating multimillion-dollar balances in so-called "mega IRAs" and to bolster the Medicare Trust Fund by increasing the net investment income tax for certain upper-income taxpayers by imposing a higher rate and expanding its application to include additional sources of income.

A new proposal would limit the tax benefits of "private placement life insurance contracts," which the administration contends are primarily investment-oriented products that are marketed exclusively to ultrawealthy individuals and "provide legally minimal life insurance protection relative to the amounts invested."

IRS resources: The White House also has renewed a proposal from last year to extend the mandatory funding stream for the Internal Revenue Service that was enacted in the Inflation Reduction Act to, among other things, allow the agency to strengthen its compliance and enforcement program in an effort to ensure that multinational enterprises, complex partnerships, and high-wealth individuals pay all of the tax they legally owe.

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Find out more

This special edition of *Tax News & Views* discusses the president's budget blueprint in the larger context of the federal debt-and-deficit outlook, highlights the new revenue provisions from the administration as well as some of the significant returning provisions, recaps the Republican response to the president's proposals, and considers whether a substantive tax bill can make it through Congress and be signed into law in 2024.

Descriptions of specific provisions in the budget package and characterizations of the administration's position on various aspects of current law are based on details in what's informally known as "Green Book," which provides the Treasury Department's explanations of the revenue provisions in the blueprint along with estimates of their budgetary effects.
URL: https://home.treasury.gov/system/files/131/General-Explanations-FY2025.pdf

Debt and deficit outlook, budget assumptions

At a high level, President Biden's fiscal blueprint takes a different approach than those of his predecessors, including 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 Barack Obama, whose budget plans generally 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 a share of gross domestic product (GDP).

Anticipating deficits above the historical norm: President Biden's fiscal 2025 budget, by contrast, largely accepts the premise that deficits will be higher than their historical average over the next decade. In dollar terms, the blueprint has deficits increasing from $1.69 trillion last year to $1.86 trillion in fiscal 2024. After a brief reprieve in which deficits fall back to about $1.5 trillion, the fiscal plan projects budget shortfalls rising again in the back half of the 10-year budget window. At that point, deficits would be a bit north of 4 percent of GDP, which exceeds the 3.7 percent average deficit registered over the past 50 years.

Still, the White House estimates that its budget policies would cut deficits, on net, by about $3.2 trillion over the next decade relative to its baseline estimates of revenues and spending over that span.

The blueprint envisions federal spending averaging about 24.4 percent of GDP over the next decade—notably higher than the average level of about 21 percent of GDP registered over the past 50 years. Revenues would also be higher than in the past—amounting to about 19.5 percent of GDP on average over the next decade, which would be a bit more than 2 percentage points higher than its five-decade average.

By the end of the 10-year budget window (fiscal 2034), revenues would be at their 10-year high of 20.3 percent of GDP, a level not seen since the late years of the Clinton administration when the federal budget was briefly in surplus.

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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 99.6 percent of GDP in the current fiscal year to about 105.6 percent of GDP in fiscal 2034.

Modest growth assumptions: In another departure from the budget blueprints of many previous administrations, which often assumed that their proposed policies would be tonic for economic growth—and thus 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 (that is, inflation-adjusted) economic growth will come in at a bit more than 2 percent per year, roughly in line with its level in the years leading up to the coronavirus pandemic.

By contrast, two other economic assumptions in the budget—with respect to projected inflation levels and interest rates—are a bit more optimistic. On inflation, the blueprint assumes that growth in the Consumer Price Index (CPI) will fall from 4.2 percent in 2023 to 2.9 percent this year, and then quickly level out at 2.3 percent per year from 2025 through the end of the 10-year budget window. Meanwhile, rates on short- and medium-term Treasury bills and bonds are projected to decline after this year. (For example, the rate on a 10-year Treasury note is projected to fall from 4.4 percent this year to 3.7 percent by 2029, where it would remain for the rest of the decade).

The administration's assumptions on inflation and interest rates are in the same ballpark as recent projections published by the nonpartisan Congressional Budget Office (CBO)—which, along with the Joint Committee on Taxation (JCT), are Congress's official arbiters of the fiscal outlook—that have inflation falling to about 2.5 percent this year and then returning to a more normal Federal Reserve-targeted level of about 2 percent for the remainder of the budget window. On interest rates, CBO projects that the average rate on 10-year Treasury bonds will remain around 4 percent over the course of the next decade. (For prior coverage of CBO's budget and economic projections, see *Tax News & Views*, Vol. 25, No. 6, Feb. 9, 2024.)
URL: https://dhub.deloitte.com/Newsletters/Tax/2024/TNV/240209_2.html

Of course, the combined effect of elevated deficits and higher interest rates—at least in relation to the record-low rates experienced during the coronavirus pandemic—means that debt service costs will take up a greater share of the federal budget going forward. Under President Biden's budget plan, interest payments would rise from 3.1 percent of GDP this year to about 3.5 percent of GDP by the end of the budget window. In nominal terms, the budget projects the government will incur $1.5 trillion in debt service costs in 2034 alone, roughly 14 percent of spending in that year.

Proposed changes to corporate tax rules

As the president previewed in his March 7 State of the Union address, the budget again proposes tax changes intended to "make big corporations pay their fair share." While increasing the corporate tax rate to 28 percent, quadrupling the excise tax on corporate stock buybacks, and other proposals will look familiar from previous Biden administration budgets, this year's blueprint also includes new revenue-raising proposals that would

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increase the corporate alternative minimum tax rate from 15 percent to 21 percent, expand the denial of deduction for employee compensation greater than $1 million to all employees and to privately held companies, and eliminate a perceived tax preference for corporate jets.

Increase the corporate tax rate: The president 's budget again proposes an increase in the corporate tax rate from 21 percent to 28 percent, retroactive to taxable years beginning after December 31, 2023. This increase would also drive the effective rate on global intangible low-taxed income (GILTI) to 14 percent—but a separate provision would further raise the effective GILTI rate to 21 percent. For taxable years beginning before January 1, 2024, and ending after December 31, 2023, the corporate income tax rate would be equal to 21 percent plus 7 percent multiplied by the portion of the taxable year that occurs in 2024.

In addition to viewing the rate hike as an "administratively simple way to raise revenue," the administration explains that "a significant share of the effects of the corporate tax increase would be borne by foreign investors. Therefore, some of the revenue raised by the proposal would result in no additional federal income tax burden on US persons."

Increase the corporate alternative minimum tax (CAMT) rate to 21 percent: This proposal would increase the rate used to compute the tentative minimum tax for the largest US corporations from 15 percent to 21 percent, effective retroactively for taxable years beginning after December 31, 2023.

According to the administration, the proposed increase is "roughly in line with the proposed increase in the regular corporate tax rate and aligns the CAMT rate with the proposed effective GILTI rate."

When the CAMT was enacted in the Inflation Reduction Act, President Biden and congressional Democrats touted it as a way to ensure the largest US companies would pay their "fair share" of taxes. In a White House fact sheet released in conjunction with the president's budget blueprint, the administration argued that increasing the CAMT rate would ensure that "the biggest corporations pay more of their fair share."
URL: https://www.whitehouse.gov/briefing-room/statements-releases/2024/03/11/fact-sheet-the-presidents-budget-cuts-taxes-for-working-families-and-makes-big-corporations-and-the-wealthy-pay-their-fair-share/

It's worth noting that the CAMT was originally included in the Inflation Reduction Act because Senate Democrats did not have the votes needed to simply increase the corporate tax rate. (The bill was moving under budget reconciliation protections and had no support from Republicans, which meant Democrats, who held only a narrow majority, could only include provisions that had unanimous support within their own caucus.) The president's latest proposal to increase rates for the corporate income tax and the CAMT would represent a one-two punch for those companies impacted by the CAMT.

Increase the excise tax on repurchase of corporate stock: This proposal would increase the 1 percent tax rate on corporate stock repurchases, enacted as part of the Inflation Reduction Act, to 4 percent, retroactive to buybacks made after December 31, 2023. It also would extend the excise tax to the acquisition of stock of an applicable foreign corporation by a specified affiliate of the applicable foreign corporation that is a controlled foreign corporation.

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Tax corporate distributions as dividends: The administration once more argues in this year's budget blueprint that corporations have "devised many ways to avoid dividend treatment under current law"—for example, by entering into "preparatory transactions to eliminate a corporation's earnings and profits or shift the corporation's earnings and profits to a prior or subsequent tax year." Corporations also "enter into transactions (so-called 'leveraged distributions') to avoid dividend treatment upon a distribution by having a corporation with earnings and profits provide funds (for example, through a loan) to a related corporation with no or little earnings and profits, but in which the distributee shareholder has high stock basis," the administration says.

The budget blueprint proposes to amend the tax code in ways the administration contends would ensure that a transfer of property by a corporation to its shareholder(s) better reflects the corporation's dividend-paying capacity. Specifically, the proposal would:

- Amend section 312(a)(3) to provide that earnings and profits are reduced by the basis in any distributed high-basis stock determined without regard to basis adjustments resulting from actual or deemed dividend equivalent redemptions or any series of distributions or transactions undertaken with a view to create and distribute high-basis stock of any corporation, effective as of the date of enactment;
- Treat a leveraged distribution from a corporation (distributing corporation) to its shareholder(s) that is treated as a recovery of basis as the receipt of a dividend directly from a related corporation (funding corporation) to the extent the funding corporation funded the distribution with a principal purpose of not treating the distribution as a dividend from the funding corporation, effective for transactions occurring after December 31, 2024;
- Disregard a subsidiary's purchase of hook stock for property so that the property used to purchase the hook stock gives rise to a deemed distribution from the purchasing subsidiary (through any intervening entities) to the issuing corporation, effective for transactions occurring after December 31, 2024; and
- Repeal the boot-within-gain limitation in reorganization transactions in which the shareholder's exchange is treated under section 356(a)(2) as having the effect of the distribution of a dividend, effective for transactions occurring after December 31, 2024.

Limit tax avoidance through inappropriate leveraging of parties to divisive reorganizations: The administration contends that in the absence of a comprehensive limitation, divisive reorganizations can "provide opportunities for tax planners to structure transactions that economically resemble tax-free cash sales." The budget blueprint again proposes to eliminate what it calls "monetization loopholes" to "increase the integrity" of the tax code. At a high level, these proposals would:

- Eliminate excessive tax-free monetization of divisive reorganizations by modifying the two safe harbors for the tax-free transfer of boot and securities of a controlled entity to creditors of a distributing entity and
- Prevent tax avoidance through the transfer of contingent liabilities to a controlled entity by imposing two additional requirements under section 355 that, if not satisfied, would result in gain recognition by a distributing entity (but not the distributing entity's shareholders).

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Both provisions generally would be effective for transactions occurring after the date of enactment.

Limit losses recognized in liquidation transactions: The administration explains in the Green Book that taxpayers with a built-in loss in the stock of a subsidiary may be able to recognize the loss on a taxable liquidation within a controlled group of corporations under section 331, without exiting their investment. For example, a corporate taxpayer may transfer more than 20 percent of the stock of the subsidiary to a related entity, reducing ownership below the 80 percent threshold, and then cause the subsidiary to liquidate. The liquidation is often accomplished through a "check-the-box" election to be classified as a partnership rather than a corporation, an election which applies only for US income tax purposes. Structuring into such taxable liquidations can also be used to recognize a loss on property held by the liquidating corporation under section 336, such as in cases involving a foreign-owned domestic corporation, the White House explains.

This proposal would modify section 267 to complete liquidations within a controlled group where the assets of the liquidating corporation remain in the controlled group after the liquidation. Where applicable, this would cause losses—both on the stock of the liquidating corporation and the property it holds—to be denied. The proposal would also grant the Secretary and her delegates the authority to allow for the deferral, rather than the denial, of such losses under the principles of section 267(f), as well to address the use of controlled partnerships to avoid these rules. The proposal would apply to distributions after the date of enactment.

Prevent basis shifting by related parties through partnerships: Seeking to "reduce the ability of related parties to use a partnership to shift partnership basis among themselves for the purpose of creating advantageous tax results with no meaningful economic consequences" using a section 754 election, the administration proposes to apply a matching rule that would prohibit any partner in the distributing partnership that is related to the distributee-partner from benefitting from the partnership's basis step-up until the distribute-partner disposes of the distributed property in a fully taxable transaction. The proposal would provide the Treasury Secretary the authority to prescribe regulations necessary to implement the matching rule with respect to related parties, and would be effective for partnership taxable years beginning after December 31, 2024.

Conform definition of 'control' with corporate affiliation test: The administration argues that the control test under section 368(c) "creates potential for taxpayers to improperly achieve desired tax outcomes through structured transactions." The budget renews a proposal from previous years to conform the control test under section 368(c) with the affiliation test under section 1504(a)(2), so that "control" would be defined as the ownership of at least 80 percent of the total voting power and at least 80 percent of the total value of stock of a corporation. The term "stock" would not include certain preferred stock that meets the requirements of section 1504(a)(4). The proposal would be effective for transactions occurring after December 31, 2024.

Expand and tighten rules on excess employee remuneration: A new proposal for fiscal year 2025 would broaden the current limitation on the deduction for excess employee remuneration under section 162(m), which generally disallows a deduction by a publicly held corporation for compensation in excess of $1 million paid to certain employees and former employees ("covered employees") in a taxable year. Specifically, the proposal would expand the scope of the disallowance to *all C-corporations*, both public and private, and to *all employees*. The administration argues that the current limitations of scope "introduce distortions and

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horizontal inequity," potentially distorting a business's decision to remain private or to go public and unfairly favoring the largest businesses by limiting the disallowance to the compensation of only a small number of employees. (Public companies currently are prohibited from deducting more than $1 million in compensation paid to the CEO, CFO, the next three highest-paid officers, and certain other covered employees after 2016. The American Rescue Plan Act of 2021 expanded the list of covered employees to include the next five highest-paid employees, although that provision is not scheduled to take effect until tax years beginning after the end of 2026.)

The budget also renews proposals to tighten the rules of the disallowance to address certain arrangements that, according to the administration, enable employers to avoid the application of the limitation. These proposals would:

- Add an aggregation rule that would treat all members of a controlled group within the meaning of section 414(b), (c), (m), and (o) of the code as a single employer for purposes of determining the covered employees and applying the deduction disallowance for compensation paid to these employees in excess of $1 million.;
- Amend section 162(m) to ensure that otherwise deductible compensation paid to an employee is considered applicable employee remuneration, whether or not paid directly by the corporation; and
- Expand the regulatory authority of the Secretary to issue regulations and other guidance as necessary to carry out the purposes of section 162(m) and to prevent the avoidance of the rule, including through the performance of services other than as an employee or by payment of compensation through a partnership or other passthrough entity.

The proposal would be effective for taxable years beginning after December 31, 2024.

Modify depreciation rules for purchases of general aviation passenger aircraft: Another new proposal in this year's budget blueprint would address what the administration sees as preferential tax treatment of "airplanes not used in commercial or contract carrying of passengers or freight" by aligning the depreciation rules for these airplanes with the existing depreciation rules for aircraft used in commercial contract carrying of passengers (*i.e.*, "chartered" aircraft) or freight as well as helicopters.

Under current law, the recovery period for "airplanes not used in commercial or contract carrying of passengers or freight" is five years under the general depreciation system (GDS) or six years under the alternative depreciation system (ADS). This proposal would change the depreciable life for these types of airplanes to seven years under GDS and twelve years under ADS.

The change in depreciable life would not apply to airplanes primarily engaged in nonpassenger activities (*e.g.*, crop dusting, firefighting, aerial surveying, etc.). These types of aircraft would continue to be depreciated using a recovery period of five years under GDS and six years under ADS.

The proposal would be effective for airplanes placed in service after December 31, 2024.

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(This proposal is a companion to a separate White House proposal related to corporate jets that would reform fuel excise taxes on business aviation. See the discussion of energy tax proposals elsewhere in this edition for details.)

Rents from prison facilities not treated as qualified income for purposes of REIT income tests: This proposal would provide that any amount received or accrued, directly or indirectly, with respect to any real or personal property primarily used in connection with any correctional, detention, or penal facility does not qualify as rents from real property. It would be effective for taxable years beginning after December 31, 2024.

Changes to the tax treatment of multinational corporations

The White House budget blueprint includes many provisions—almost all of which are carried over from previous years—that would tighten current-law tax rules that the administration and many congressional Democrats have argued provide incentives for companies to locate investment in foreign jurisdictions and move US-based jobs and production activities offshore.

Notably, the administration again proposes to move towards implementation of elements of the global tax agreement negotiated through the OECD over the past several years by revamping—and in some instances, eliminating—key international tax provisions from the Tax Cuts and Jobs Act: the global intangible low-tax income (GILTI) regime, the base erosion anti-abuse tax (BEAT), and the deduction for foreign-derived intangible income (FDII).

Revise the GILTI regime: The president's budget once again proposes several changes to the current global minimum tax regime, including eliminating the qualified business asset investment (QBAI) exemption, reducing the section 250 deduction for GILTI inclusion to 25 percent (thus, in conjunction with the proposed 28 percent corporate rate discussed above, increasing the effective GILTI rate to 21 percent), and calculating GILTI on a jurisdiction-by-jurisdiction (also known as country-by-country) basis instead of a global basis.

The proposal also would decrease the 20 percent disallowance of foreign tax credits incurred to 5 percent, allow net operating losses to be carried forward (within a single jurisdiction), and allow foreign tax credits to be carried forward 10 years (within a single jurisdiction). It would repeal the high-tax exemption to subpart F income and its cross-reference in section 951A of the GILTI rules.

The reduction in the section 250 deduction to 25 percent would be effective for taxable years beginning after December 31, 2023. The other elements would be effective for taxable years beginning after December 31, 2024.

This section would also limit the deduction for dividends received from noncontrolled foreign corporations, effective after the date of enactment; limit the ability of domestic corporations to invert; and make several other changes related to foreign income.

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Adopt the undertaxed profits rule: In line with previous budget requests, this proposal would repeal the BEAT and replace it with an Undertaxed Profits Rule (UTPR), intended to be consistent with the UTPR that is described in Pillar Two of the OECD's Model Rules. The administration notes that "[w]hen a UTPR in another jurisdiction comes into effect, the proposal also includes a domestic minimum top-up tax that would protect US revenues from the imposition of UTPR by other countries. Separately, the proposal would ensure US taxpayers would continue to benefit from US tax credits and other tax incentives that promote US jobs and investment, including clean energy tax provisions enacted in the [Inflation Reduction Act]."

The proposal would be effective for taxable years beginning after December 31, 2024.

Repeal the FDII deduction: According to the administration, the deduction for foreign-derived intangible income, which currently is 37.5 percent but is scheduled to decrease to 21.875 percent in tax years beginning after 2025, provides large tax breaks to companies with "excess profits" instead of incentivizing new investment in the US and "disadvantages domestic producers, offering tax incentives only to those companies with high export sales, rather than those with significant domestic sales."

The administration proposes to repeal the FDII deduction effective for taxable years beginning after December 31, 2024, an action that it contends would raise significant revenue that can be deployed to incentivize research and development activities in the US "directly and more effectively." As in previous years, the White House does not specify what those new incentives would be.

Revise the rules that allocate subpart F income and GILTI between taxpayers to ensure that subpart F income and GILTI are fully taxed: According to the administration, current law allows subpart F income, or tested income of a controlled foreign corporation (CFC), to "escape US taxation in certain cases in which stock of the CFC is transferred and the CFC distributes a dividend (including a deemed dividend) to any person other than the US shareholder on the last relevant day."

The White House budget proposes to modify existing pro rata share rules to require a US shareholder of a CFC that owns, directly or indirectly, a share of stock of the CFC for part of the CFC's taxable year, but not on the last relevant day, to include in gross income a portion of the foreign corporation's subpart F income allocable to the portion of the year during which it was a CFC. It also would revise the pro rata share rules for determining a US shareholder's GILTI inclusion with respect to a CFC and authorize the Secretary to issue regulations or other guidance necessary or appropriate to carry out the purposes of the proposal.

The proposal would apply to taxable years of foreign corporations beginning after the date of enactment and to taxable years of US shareholders in which or with which such taxable years of foreign corporations end.

Require a CFC's taxable year to match that of its majority US shareholder: The administration argues that "technological advances have reduced or eliminated the difficulties in obtaining and translating tax information from a foreign entity," obviating the need for the current election CFCs can make to use a taxable year ending one month earlier than that of its majority US shareholder. This year's budget proposes to eliminate the election, which the White House contends has resulted in aggressive tax planning opportunities

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for taxpayers, unnecessary complexity, and significant compliance and administrative burdens. The proposal would be effective as of the date of enactment. CFCs with existing one-month deferral elections would have a short taxable year as of the first taxable year end of its majority US shareholder that is at least 60 days after the date of enactment of the proposal.

Limit foreign tax credits from sales of hybrid entities: This proposal would apply the principles of section 338(h)(16) 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). In addition, because the proposal is limited to determining the source and character of such an item of gain or loss for purposes of applying the foreign tax credit rules, the proposal does not affect the amount of gain or loss recognized as a result of the disposition or the change in entity classification.

The Secretary would be granted authority to issue any regulations necessary or appropriate to carry out the purposes of the proposal, including those applying the proposal to other transactions that have a similar effect and exempting certain transactions among related parties from application of the proposal.

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

Restrict deductions of excessive interest of members of financial reporting groups: The administration argues that the "fungibility of money makes it easy for multinational groups to substitute debt for equity in a controlled entity in order to shift profits to lower-tax jurisdictions."

The budget blueprint proposes to address this by, among other things, limiting the deduction for interest expense by a member of a financial reporting group (as defined in the proposal) if the member has net interest expense for US tax purposes and the member's net interest expense for financial reporting purposes (computed on a separate company basis) exceeds the member's proportionate share of the financial reporting group's net interest expense reported on the group's consolidated financial statements (excess financial statement net interest expense).

The proposal would be effective for taxable years beginning after December 31, 2024.

Conform scope of portfolio interest exclusion for 10-percent shareholders to other tax rules: Because it argues that taxpayers are "often able to avoid (or attempt to avoid) being classified as a 10-percent shareholder" under the Tax Cuts and Jobs Act definition of "US shareholder" for income tax purposes by limiting their technical voting power but retaining substantial interest in the total value of shares, the

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administration proposes to modify that definition. In the case of interest paid on an obligation issued by a corporation, “US shareholder” would mean any person who owns 10 percent or more of the total combined voting power of all classes of stock of such corporation entitled to vote or 10 percent of the total value of shares of all classes of stock of such corporation.

The proposal would apply to payments of US-source interest made on debt instruments issued (including a deemed issuance) on or after the date that is 60 days after enactment.

Treat payments substituting for partnership effectively connected income as US-source dividends: The administration again proposes to treat the portion of a payment on a derivative financial instrument (including a securities loan or sale-and-repurchase agreement) that is contingent on income or gain from a publicly traded partnership or other partnership specified by the Secretary as a dividend equivalent, to the extent that the related income or gain would have been treated as effectively connected income if the taxpayer held the underlying partnership interest.

The Secretary would have authority to prescribe such regulations or other guidance as may be necessary or appropriate to carry out the purposes of, and prevent the avoidance of, this section, including with respect to payments made between foreign persons. No inference is intended as to the application of current law to derivative transactions on interests in partnerships with effectively connected income.

The proposal would be effective for taxable years starting December 31, 2024.

Expand access to retroactive qualified electing fund elections: The administration again proposes to modify section 1295(b)(2) to permit a qualified electing fund (QEF) election by the taxpayer at such time and in such manner as the Secretary shall prescribe by regulations. Taxpayers would be eligible to make a retroactive QEF election without requesting consent only in cases that do not prejudice the US government. For example, if the taxpayer owned a passive foreign investment company in taxable years that are closed to assessment, the taxpayer would need to obtain consent and to pay an appropriate amount to compensate the government for the taxes not paid in the closed years on amounts that would have been includable in the taxpayer’s income if the taxpayer had made a timely QEF election. While it is less common for partnerships and other nonindividual taxpayers to inadvertently fail to make a QEF election, the Secretary would have authority to allow such taxpayers to make retroactive QEF elections in appropriate circumstances.

The proposal would be effective on the date of enactment. It is intended that regulations or other guidance would permit taxpayers to amend previously filed returns for open years.

Reform taxation of foreign fossil fuel income: The budget blueprint once again proposes to repeal the exemption from GILTI for foreign oil and gas extraction income (FOGEI) and to expand the definitions of FOGEI and foreign oil related income (FORI) to include oil shale and tar sands.

The proposal would be effective for taxable years beginning after December 31, 2024.

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Provide tax incentives for locating jobs and business activity in the US and remove tax deductions for shipping jobs overseas: On the incentive side, the budget plan revives a proposal from previous years that 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. Onshoring is defined generally as reducing or eliminating a trade, business, or line of business currently conducted outside the US and starting up, expanding, or otherwise moving the same trade or business within the US, to the extent that the action results in an increase in US jobs.

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

Tax proposals affecting high-wealth and upper-income taxpayers

The White House budget reprises a litany of proposals from previous years aimed at increasing taxes on upper-income and high-net-worth taxpayers and introduces a significant new proposal intended to limit the tax advantages of certain life insurance products that offer investment options that are not typically available to the general public.

Apply the net investment income tax (NIIT) to passthrough business income of upper-income taxpayers: In a proposal that could be viewed as inconsistent with the president's pledge not to increase taxes on individuals with income of less than $400,000, the administration once again calls for ensuring that all passthrough business income of high-income taxpayers ($200,000 for single taxpayers and heads of households, and $250,000 for joint filers) is subject to either the NIIT or self-employment tax, effective for taxable years beginning after December 31, 2023.

Increase the NIIT rate and additional Medicare tax rate for higher-income taxpayers: Also revived from last year's budget is a proposal intended to extend the life of the Hospital Insurance Trust Fund by:

- Increasing the additional Medicare tax rate from 3.8 percent to 5 percent for taxpayers earning more than $400,000 a year. (The 5 percent rate would apply only to income above $400,000; income below that threshold would continue to be taxed at 3.8 percent.)
- Increase the NIIT rate from 3.8 percent to 5 percent for taxpayers with more than $400,000 of income. The administration explains that for taxpayers with positive net investment income, the NIIT would increase to 5 percent on the lesser of (1) net investment income or (2) the excess, if any, of modified adjusted gross income over $400,000. The threshold would be indexed for inflation.

The proposal would be effective for taxable years beginning after December 31, 2023.

Increase in the top marginal tax rate: The administration once again proposes to increase the top marginal tax rate for individuals from 37 percent to 39.6 percent, effective for tax years beginning after December 31, 2023.

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Reform the taxation of capital income: The budget blueprint renews proposals that would tighten the tax treatment of capital income in an effort to prevent more affluent taxpayers from avoiding tax on their appreciated investments. These proposed changes would:

- Tax long-term capital gain and qualified dividend income of at ordinary rates, applicable to taxpayers with taxable income of more than $1 million ($500,000 for married filing separately). The provision would be effective for gains required to be recognized and for dividends received on or after the date of enactment. Income thresholds would be indexed for inflation after 2024.
- Treat transfers of appreciated property by gift or on death as realization events. Thus, "the donor or deceased owner" of an appreciated asset would realize "a capital gain" at the time of the transfer. This provision would be effective for gains on property transferred by gift, and on property owned at death by decedents dying after December 31, 2024, and on certain property owned by trusts, partnerships, and other noncorporate entities on January 1, 2025.

Impose a minimum income tax on the wealthiest taxpayers: The president's budget revives his proposal for a 25 percent minimum tax on the total income of taxpayers with wealth of more than $100 million.

A taxpayer's minimum tax liability would be the minimum rate of 25 percent multiplied by the sum of (1) taxable income and (2) unrealized gains, including on ordinary assets. This product would then be reduced by the sum of the taxpayer's unrefunded, uncredited prepayments and regular tax. The proposal would be effective for taxable years beginning after December 31, 2024.

Prevent excessive accumulations by high-income taxpayers in tax-favored retirement accounts: The budget blueprint includes several proposals—some new, some repeated from previous years—intended to prevent high-income taxpayers from accumulating excessive balances in tax-preferred individual retirement accounts and qualified retirement plans and thus limit what the administration sees as the ability of these taxpayers to use IRAs and other qualified plans as tax planning tools rather than traditional retirement savings vehicles. Specifically, the administration would:

- Require a high-income taxpayer with an aggregate vested account balance under certain tax-favored retirement arrangements that exceeded $10 million as of the last day of the preceding calendar year to distribute a minimum of 50 percent of that excess. This provision would apply to a taxpayer whose modified adjusted gross income in a given taxable year exceeds $450,000 (for a married-joint filer or a surviving spouse), $425,000 (for a head-of-household), or $400,000 (in other cases). This provision generally would be effective for tax years beginning after December 31, 2024.
- Curb so-called "back door" conversions to Roth IRAs, generally by prohibiting Roth conversions for both IRAs and employer-sponsored plans in the case of upper-income taxpayers (defined based on the modified adjusted gross income thresholds outlined above), effective for distributions made after December 31, 2024.
- Clarify that, for purposes of applying the prohibited transaction rules with respect to an IRA, the IRA owner (including an individual who inherits an IRA as a beneficiary after the IRA owner's death) is always a disqualified person, effective for transactions after December 31, 2024.

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- Prohibit an IRA from holding an interest in a domestic international sales corporation (DISC) or a foreign sales corporation (FSC) that receives a payment from an entity owned by the IRA owner, effective for interests in DISCs and FSCs acquired or held after December 31, 2024.
- Extend the statute of limitations in the case of a substantial error relating to valuation of assets with respect to an IRA from three years to six years, and extend the statute of limitations for the excise tax on prohibited transactions from three years to six years, effective for taxes for which the three-year window would end after December 31, 2024.

Limit tax benefits for private placement life insurance and similar contracts: A new proposal in this year's budget blueprint would basically eliminate tax benefits currently offered through so-called private placement life insurance policies (PPLI) and similar contracts (*e.g.*, private placement annuities (PPVA)—products that the administration contends operate primarily as investment vehicles for ultrawealthy individuals and "provide legally minimal life insurance protection relative to the amounts invested."

According to the White House "[m]ost individual PPLI policyholders reportedly have a net worth of $20 million or more, with $10 million or more in liquid assets" and such contracts "allow affluent purchasers to select from an array of investment options that are not accessible generally to purchasers" of traditional life insurance policies. As a result, in the administration's view, such policies should not be eligible for the full suite of tax benefits—such as tax deferral on investment earnings within the contract and exclusion from tax for certain account value withdrawals and benefit payouts—that are available to traditional life insurance.

Specifically, the budget blueprint would define a class of "covered contracts" that are predominantly investment-oriented and ensure that all earnings are ultimately taxable, and that tax deferral is limited and discouraged through a penalty tax, while preserving a tax exemption for the pure life insurance benefits (amounts paid in excess of a contract's cash value).

Covered contracts would include:

- Any PPLI or PPA contract, defined as a variable contract subject to SEC regulation as a security that is not a registered product with the SEC, with respect to which the purchaser, as a condition of purchase, must have sufficient income and wealth to qualify (or can otherwise qualify) as an accredited investor or qualified purchaser under SEC regulations at the time of purchase;
- Any variable life insurance contract any of whose premiums are paid, directly or indirectly, in kind rather than in cash;
- Any variable life insurance contract whose underlying assets include assets purchased, directly or indirectly, from the policyholder, persons related to the policyholder, or a business or other entity in which the policyholder or a related person has more than a *de minimis* ownership interest;
- Any variable life insurance contract that, in combination with contracts owned by persons related (directly or indirectly) to the contract's policyholder, owns an interest in a separate account of an insurance company, and the cash value of the related contracts, in the aggregate, represents at least 5 percent of the value of any distinct investment option whose assets are accounted for in that separate account; and

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- A variable life insurance contract issued outside of the United States, if any of the investment assets supporting the contract, if supporting a contract sold or marketed in the United States, would cause that contract to be salable only to an accredited investor or qualified purchaser and subject to SEC regulation as a security.

The proposal provides, for example, that funds distributed from a covered contract prior to its annuity starting date (if applicable) would be taxed as ordinary income to the extent its investment value exceeds the policyholder's or beneficiary's investment in the contract. Similarly, amounts paid by reason of the insured's death would also be treated as ordinary income to the extent the beneficiary's share of the contract's investment value exceeds the beneficiary's share of the investment in the contract.

Additionally, a 10 percent tax would be applied to any taxable distribution from a covered contract to account for any deferral benefits ("inside build-up") within the contract.

The Secretary would be authorized to require reporting by insurance companies and policyholders as necessary to ensure that payments from covered contracts are identified and taxed appropriately, including information on policy distributions and premiums. Insurance companies and policyholders would be subject to penalties for noncompliance with these reporting requirements.

The proposal would be effective for taxable years beginning after December 31, 2024, for *covered contracts issued under applicable law on or after the day following the date of the publication of the Green Book*. Any substantial modification of an existing life insurance or annuity contract, or exchange of one such contract for another, would be treated as the issuance of a new contract for this purpose.

It's worth noting that PPLI has been under investigation by Senate Finance Committee Chairman Ron Wyden, D-Ore., and his staff. Wyden recently released a report on that investigation and indicated that he will soon introduce legislation intended to curb what he sees as abusive features of PPLI.
URL: https://www.finance.senate.gov/imo/media/doc/ppli_report_final.pdf

Estate, gift tax, and charitable giving proposals

The White House re-upped several proposals to tighten rules around the taxation of estates and gifts to limit the ability of wealthier taxpayers to use generational transfers and other transfer arrangements to delay tax on appreciated assets. These include:

Improve tax administration for trusts and decedents' estates: The budget blueprint includes assorted changes that would expand the definition of "executor," increase the limit on the reduction in value of special use property, extend the 10-year period for certain estate and gift tax liens, require reporting of the estimated total value of trust assets, require that a defined value formula clause be based on a variable that does not require IRS involvement, and simplify the exclusion from the gift tax for annual gifts.

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Limit duration of generation-skipping transfer tax (GST) exemption: This proposal generally would provide that the GST exemption would apply only to: (1) direct skips and taxable distributions to beneficiaries no more than two generations below the transferor, and to younger-generation beneficiaries who were alive at the creation of the trust and (2) taxable terminations occurring while any person described above is a beneficiary of the trust. It would apply on and after the date of enactment to all trusts subject to the generation-skipping transfer tax, regardless of the trust's inclusion ratio on the date of enactment.

Modify income, estate, gift, and generation-skipping transfer tax rules for certain trusts: Building on a proposal from last year, the White House would change the rules around trusts by:

- Generally requiring that the remainder interest in a grantor retained annuity trust (GRAT) at the time the interest is created have a minimum value for gift tax purposes equal to the greater of 25 percent of the value of the assets transferred to the GRAT or $500,000 (but not more than the value of the assets transferred). This provision generally would be effective for transactions on or after the date of enactment.
- Treating a trust's purchase of assets from, or interests in, a trust that is subject to GST tax (regardless of the selling trust's inclusion ratio), as well as a purchase of any other property that is subject to GST tax, as a change in trust principal that would require the redetermination of the purchasing trust's inclusion ratio when those assets (or trust interest) are purchased, effective for transactions occurring after the date of enactment;
- Ignoring trust interests held by additional tax-exempt organizations for purposes of the GST tax, effective for taxable years beginning after the date of enactment;
- Modifying the definition of a guaranteed annuity from a charitable lead annuity trust, effective for trusts created after the date of enactment; and
- Treating loans made by a trust to a trust beneficiary as a distribution for income tax purposes, carrying out each loan's appropriate portion of distributable net income to the borrowing beneficiary, effective for loans made, as well as for existing loans renegotiated or renewed, by trusts after the year of enactment.

Require consistent valuation of promissory notes: This proposal would impose a consistency requirement by providing that, if a taxpayer treats any promissory note as having a sufficient rate of interest to avoid the treatment of any forgone interest on the loan as income or any part of the transaction as a gift, that note subsequently must be valued for federal gift and estate tax purposes by limiting the discount rate to the greater of the actual rate of interest of the note, or (for estate tax purposes) the applicable minimum interest rate for the remaining term of the note on the date of death. It would be effective for valuations as of a valuation date on or after the date of enactment.

Private foundation issues: The budget blueprint also renews "loophole-closing" proposals from last year that would limit the use of donor advised funds to avoid a private foundation payout and exclude payments to disqualified persons from counting toward the private foundation payout requirement.

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Provisions affecting noncorporate taxpayers

The budget includes several policies intended to strengthen the tax rules for noncorporate taxpayers.

Strengthen limitation on loss for noncorporate taxpayers: First proposed by the White House in last year's budget plan, the administration is again proposing to make permanent the limitation on loss deductibility under section 461(l) that is designed to reduce the ability of individual taxpayers to use business losses to offset unrelated income. That annual loss limitation—which under present law is set to expire after 2028—is currently pegged at $610,000 for married couples and $305,000 for all other taxpayers (indexed for inflation).

Under the White House budget plan, this "excess business loss" limitation would be made permanent. Significantly, the proposal would also provide that any loss deduction denied by section 461(l) would not become a net operating loss carryforward in subsequent years—as is the case under current law—subject only to an 80-percent-of-taxable-income limitation under section 172. Instead, those carryforward excess business losses would be treated as current-year losses in subsequent years, again subject to the 461(l) loss limitation.

Other noncorporate proposals: The budget blueprint also includes several additional proposals aimed at noncorporate taxpayers that have appeared in previous Biden fiscal plans. These proposals would:

- Prevent basis shifting by related parties through partnerships: Under current law, a partnership may generally elect, in the case of a distribution of property (section 734), to adjust the tax basis of its partnership property under section 754. This proposal intends to "reduce the ability of related parties to use a partnership to shift partnership basis among themselves for the purpose of creating advantageous tax results with no meaningful economic consequences." It would be effective for taxable years beginning after December 31, 2024.
- Tax carried (profits) interests as ordinary income: Consistent with the Biden administration's fiscal year 2024 budget plan, this proposal would repeal section 1061 (which generally extends the long-term holding period requirement for favorable carried interest taxation from more than one year to more than three years) and change the taxation of certain profits interests for taxpayers with taxable income (from all sources) in excess of $400,000. Specifically, 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 also would be taxed at ordinary rates. This proposal would be effective for taxable years beginning after December 31, 2024.
- Limit deferral of gain from like-kind exchanges: The proposal would limit the deferral of gain from like-kind exchanges of real property to $500,000 for each taxpayer ($1 million for married individuals filing a joint US federal income tax return) for each taxable year, effective for taxable years beginning after December 31, 2024.
- 100 percent depreciation recapture for section 1250 property: In general, this proposal would treat any gain upon disposition of section 1250 property held for more than one year as ordinary income to the extent of the cumulative depreciation deductions taken after the effective date of the provision, which in this case would be taxable years beginning after December 31, 2024.

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Insurance-related provisions

The budget blueprint includes several insurance-related provisions that the administration characterizes as "loophole closers," including proposals to:

- Expand pro rata interest disallowance rules allocable to unborrowed policy cash values of business-owned life insurance policies by eliminating the current-law exception for policies covering the lives of certain employees, officers, and directors. The exception for a policy covering a 20 percent owner of a business would remain. The proposal would apply to contracts issued after December 31, 2024.
- Impose an ownership diversification requirement for the small insurance company election, effective for taxable years beginning after December 31, 2024.
- Modify the rules for insurance products that fail the statutory definition of a life insurance contract, effective for taxable years beginning after December 31, 2024 for life insurance contracts issued under applicable law on or after the day following the date of publication the Treasury Department's fiscal year 2025 Green Book.
- Correct various drafting errors in the taxation of life insurance companies under the Tax Cuts and Jobs Act.

Energy-related tax provisions

The Inflation Reduction Act included significant production and investment tax credits for renewable and alternative energy property, credits for production of certain alternative fuels, incentives to promote low- and zero-emission vehicles, and incentives for energy-efficient building projects. However, that legislation did not repeal any of the deductions or other special provisions in the tax code that, according to the administration, provide distorted incentives to produce fossil fuels. Accordingly, the administration proposes, as it did last year, to eliminate these provisions, including:

- The enhanced oil recovery credit for eligible costs attributable to a qualified enhanced oil recovery project;
- The credit for oil and gas produced from marginal wells;
- The expensing of intangible drilling costs;
- The deduction for costs paid or incurred for any qualified tertiary injectant used as part of a tertiary recovery method;
- The 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;
- Two-year amortization of geological and geophysical expenditures by independent producers, instead requiring amortization over the seven-year period used by major integrated oil companies;
- Expensing of exploration and development costs;
- Percentage depletion for hard mineral fossil fuels;
- Capital gains treatment for royalties on the disposition of coal or lignite;
- The exemption from corporate income tax for fossil fuel publicly traded partnerships;

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- The oil spill liability trust fund excise tax exemption for crude oil derived from bitumen and kerogen-rich rock; and
- Accelerated amortization for air pollution control facilities.

Repeal of these provisions generally would be effective for taxable years beginning after December 31, 2024. In the case of royalties, the proposal would be effective for amounts realized after taxable years beginning after December 31, 2024, regardless of when the property generating those royalties was acquired. 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, 2029.

Reform fuel excise taxes on business aviation: The tax rate on kerosene jet fuel used by private and corporate jets (the noncommercial business aviation segment) is 21.8 cents per gallon. The tax is collected on behalf of and transferred to the Airport and Airway Trust Fund (AATF) to support Federal Aviation Administration (FAA) activity.

The administration argues that business aviation accounts for approximately 3 percent of the FAA's costs while contributing less than 1 percent to AATF revenue. To ensure that private jet users are paying taxes commensurate to the costs they impose on the FAA, the administration has included a new proposal in this year's budget blueprint that would increase taxes on kerosene used for private jet travel, including corporate jets, to $1.06 per gallon, subject to a five-year phase-in. In the first year, the jet fuel tax would increase from 21.8 cents per gallon to 38.64 cents with a 16.84 cent per gallon increase in each subsequent year until 2029.

This proposal would not affect the existing exemptions for certain noncommercial aviation operations, including foreign trade uses, farming uses, nonprofit educational uses, exclusive use by state or local government, and military use.

The proposal would be effective for taxable years beginning after December 31, 2024.

(This proposal is a companion to a separate White House proposal related to corporate jets that would modify the depreciation rules for purchases of general aviation passenger aircraft. See the discussion of corporate tax proposals elsewhere in this edition for details.)

Elimination of drawbacks on certain petroleum taxes: The budget blueprint carries over a revenue-raising proposal from last year that would disallow the rebate of petroleum excise taxes that go to the oil spill liability trust fund or the hazardous substance superfund when products are exported. The provision would be effective after December 31, 2024.

Impose digital asset mining energy tax: Also returning this year is a provision that would impose an excise tax on firms engaged in digital asset mining equal to 30 percent of the cost of electricity used in their activities. This tax would be phased in over three years—starting with taxable years beginning after December 31, 2024—at a rate of 10 percent in the first year, 20 percent in the second, and 30 percent thereafter.

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Define the term ultimate purchaser' for purposes of diesel fuel exportation: This proposal, which was also in the fiscal year 2024 budget blueprint, would define the person entitled to a rebate of federal excise taxes as the last purchaser in the United States for the purposes of diesel fuel and kerosene exportation. It would be effective for diesel fuel and kerosene exported after December 31, 2024.

Tax treatment of digital assets

The administration's fiscal 2025 budget blueprint repeats several prior proposals in the cryptocurrency realm.

- Apply the wash sale rules to digital assets and address related party transactions: This provision would amend section 1091 to add digital assets to the list of assets subject to the wash sale rules, which, under current law, generally seek to disallow losses from the sale of stock or securities if the same or substantially identical stock or securities are purchased within 30 days before or after the sale (a so-called "wash sale"). Additionally, the wash sale rules—for all types of assets—would be modified to defer losses in certain related-party situations. These proposals would be effective for taxable years beginning after December 31, 2024.
- Modernize rules treating loans of securities as tax-free to include other asset classes and address income inclusion: In general, this proposal would expand the securities loan nonrecognition rule in section 1058 to apply to loans of digital assets, provided that such loans have terms that are similar to those currently required for securities loans in section 1058. It would be effective for taxable years beginning after December 31, 2024.
- Provide for information reporting by certain financial institutions and digital asset brokers for purposes of exchange of information: The administration proposes to expand US financial institution reporting obligations on non-US account holders. According to the Green Book, this proposal would result in more robust reciprocal tax information exchanges between the US and jurisdictions with which it maintains reciprocal income tax treaties or intergovernmental agreements under the Foreign Account Tax Compliance Act (FATCA). The rules would require US financial institutions to report (1) account balances for financial accounts maintained in the US that are held by foreign persons, (2) non-US source income payments to accounts held by foreign persons, (3) gross proceeds from the sale or redemption of property held in, or with respect to, financial accounts held by foreign persons, and (4) information regarding passive entities and their substantial foreign owners. The proposal would be effective for returns required to be filed after December 31, 2026.
- Require reporting by certain taxpayers of foreign digital asset accounts: The administration proposes to require individuals and certain domestic entities to disclose digital assets maintained in a "foreign digital asset account," defined as "any account that holds digital assets maintained by a foreign digital asset exchange or other foreign digital asset service provider." This proposal would be effective for returns required to be filed after December 31, 2024.
- Amend the mark-to-market rules for dealers and traders to include digital assets: In general, this proposal would amend the mark-to-market rules under section 475 to include digital assets as another category of assets that may be marked to market by a dealer or trader in such assets. It would be effective for taxable years beginning after December 31, 2024.

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Economic and community development provisions

The budget blueprint includes a slate of provisions aimed at revitalizing economically distressed communities.

Establish a new 'Neighborhood Homes Credit': The administration argues that although the housing market is supported by a number of tax incentives such as the low-income housing tax credit, the mortgage interest deduction, and tax-exempt housing bonds, there currently is no incentive in the tax code designed to directly support the building or renovation of affordable owner-occupied housing, whether by home builders or home owners themselves.

To fill this gap, the budget blueprint includes a proposal from last year to establish a "Neighborhood Homes Credit" (NHC) that would be allocated by state-level Neighborhood Homes Credit Agencies (NHCAs) for the purpose of encouraging: (1) new construction for sale, (2) substantial rehabilitation for sale, and (3) substantial rehabilitation by existing home owners who will remain in their communities. This new credit allocation—which, for each state or US territory, would be capped at the greater of $8 million or $6 multiplied by the state's population (indexed for inflation)—would be effective for taxable years beginning after December 31, 2024.

Expand and enhance the low-income housing tax credit (LIHTC): The budget proposes to make a number of enhancements to the LIHTC, including by increasing the annual "housing credit dollar amounts" (HCDAs) that states are allocated each year for purposes of the 9 percent LIHTC credit rate (effective beginning in 2025), and by reducing the 50 percent private activity bond (PAB) financing requirement (to 25 percent) that enables a building to earn credits at the 4 percent LIHTC rate if the building and land it sits on are financed by PABs subject to a state's volume cap (effective for buildings placed in service after December 31, 2024).

Make the new markets tax credit permanent: The new markets tax credit was last extended by the Consolidated Appropriations Act, 2021 at $5 billion each calendar year 2020 through 2025. The administration's proposal would extend the credit permanently with a new allocation for each calendar year after 2025 at $5 billion, indexed for inflation after 2026. It would be effective after the date of enactment.

Extend the period for assessment of tax for certain qualified opportunity fund investors: Taxpayers who invest in a qualified opportunity fund (QOF) may elect to defer eligible gain from the taxpayer's income for the year the gain is realized. The gain is generally deferred until December 31, 2026. However, if an "inclusion event" occurs (*e.g.*, the fund loses its QOF status), the taxpayer must include the deferred gain in its income for the year in which the inclusion event occurs. The Green Book notes that a longer assessment statute of limitation is needed for taxpayers who defer gain from QOFs because inclusion events "may not be readily identifiable on the taxpayer's return" so the IRS may not know about the inclusion event before the three-year assessment statute of limitation expires. In general, this provision would extend the assessment statute of limitations until "three years after the date on which the IRS is furnished with all of the information that it needs to assess the deficiencies."

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This proposal generally would be effective for inclusions of deferred gains with respect to which deferral elections had been based on investments in QOFs that are made after December 22,
2017. It would not apply in situations where the statute of limitations for assessment has expired before the date of enactment, however.

Modify the work opportunity tax credit to promote longer-term employment: To encourage employers to provide long-term employment opportunities to members of targeted groups under the work opportunity credit program, the administration proposes to increase from 120 to 400 the minimum number of hours worked by an individual in the first year of service to become eligible for the credit. The proposal would be effective for individuals hired after December 31, 2024.

Tax administration and compliance provisions

The Biden administration has argued that it can raise significant revenue, and cut the budget deficit, by reducing what is colloquially referred to as the "tax gap"—the difference between the amount of tax legally owed to the government and the amount actually collected on a timely basis. To that end, the budget blueprint lauds the Inflation Reduction Act's 10-year infusion of roughly $80 billion in mandatory IRS funding (that is, funding above and beyond what the agency will receive as part of the annual appropriations process) as critical to its efforts to "improve customer service, modernize decades-old computer systems, and improve enforcement with respect to complex partnerships, large corporations, and high-income individuals."

At the same time, the administration acknowledges that the Fiscal Responsibility Act of 2023—that is, the debt limit and spending accord struck last year between President Biden and then-House Speaker Kevin McCarthy, R-Calif.—and affirmed in January by a handshake deal between Senate Majority Leader Charles Schumer, D-N.Y., and current Speaker Mike Johnson, R-La., will have the effect of rescinding roughly $20 billion of the mandatory Inflation Reduction Act funding.

Increase and extend mandatory funding provided to the IRS through fiscal year 2034: As a continuation of Inflation Reduction Act policy and in order to backfill the reductions in mandatory funding negotiated in these recent debt limit and appropriations deals, the administration's budget plan proposes to increase and extend the IRS's mandatory funding stream through 2034—that is, for the additional years covered by the 10-year budget window in the fiscal year 2025 blueprint. In total, the agency would be provided $104.3 billion in mandatory funding through 2034, with about half of that dedicated to enforcement, and lesser amounts dedicated to technology and operations support, taxpayer services, and business systems modernization.

Without that increase and continuation of supplemental funding, the administration argues that the IRS's mandatory funding stream will be depleted by 2030 and the deficit will again rise as the agency is forced to curtail its enhanced enforcement activities. (A recent report from the nonpartisan Congressional Budget Office notes that a $20 billion cut to the IRS's mandatory funding stream would reduce revenues by $44 billion over 10 years—the result of forgone tax collections from diminished enforcement resources—and increase the cumulative deficit by $24 billion.)
URL: https://www.cbo.gov/publication/59972

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Maintain discretionary IRS funding at FY2023 level: Additionally, the White House budget plan proposes to maintain the IRS's regular operating budget—that is, funding provided under the annual appropriations process—for fiscal year 2025 at $12.3 billion, a level consistent with its fiscal 2023 level, as enacted, and in keeping with what the president and congressional leaders have agreed to as part of their recent debt-limit and spending accords.

Compliance and administration proposals: In addition to the proposed mandatory and discretionary budget increases for the IRS, the administration's plan also includes several targeted measures—most of which have appeared in prior Biden fiscal plans—that are intended to improve taxpayer compliance and administration. Among these are provisions that would:

- Amend the centralized partnership audit regime to permit the carryover of a reduction in tax that exceeds a partner's tax liability (effective upon enactment);
- Modernize reporting with respect to foreign tax credits to reduce burden and increase compliance (generally effective for taxable years beginning after the date of enactment);
- Authorize limited sharing of business tax return information to measure the economy more accurately (effective upon enactment);
- Require earlier electronic filing deadlines for certain information returns (effective for information returns required to be filed after December 31, 2024);
- Address taxpayer noncompliance with listed transactions (effective for sales of controlling interests in the stock of applicable C corporations occurring on or after April 10, 2014);
- Impose an affirmative requirement to disclose a position contrary to a regulation (effective for returns filed after the date of enactment);
- Require employers to withhold tax on failed nonqualified deferred compensation plans (effective after December 31, 2024);
- Extend to six years the statute of limitations for certain tax assessments (effective for returns required to be filed after the date of enactment);
- Increase the statute of limitations on assessment of the COVID-related paid leave and employee retention tax credits (effective on the date of enactment);
- Impose penalties for inaccurate or fraudulent employment tax returns (effective for claims for which the statute of limitations has not expired as of the date of enactment);
- Expand and increase penalties for noncompliant return preparation and e-filing and authorize IRS oversight of paid preparers (effective on the date of enactment);
- Make repeated willful failure to file a tax return a felony for those with significant tax liability (effective for returns required to be filed after December 31, 2024);
- Expand IRS summons authority for large partnerships (effective after the date of enactment);
- Address compliance in connection with tax responsibilities of expatriates (effective for taxable years beginning after December 31, 2024);
- Define control of the payment of wages (effective after December 31, 2024);
- Rationalize funding for post-retirement medical and life insurance benefits (effective for taxable years beginning after December 31, 2024);

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- Clarify tax treatment of on-demand pay arrangements (effective for calendar years and quarters beginning after December 31, 2024); and
- Amend the excise tax on employment-based group health plans (effective for calendar years and quarters beginning after December 31, 2024).

Tax relief for middle-class taxpayers and working families

The tax increases proposed in the administration's latest budget would help offset the cost of assorted tax cuts intended to support middle-class individuals and working families.

Increase the employer-provided child care tax credit for businesses: The administration proposes to increase the portion of the credit related to qualified care expenses to 50 percent of the first $1 million of qualified care expenses (or 60 percent of the first $1 million of qualified care expenses for small businesses with gross receipts less than or equal to $25 million—adjusted for inflation—for the five-year period preceding the taxable year). The portion of the credit related to referral expenses would be 10 percent of the first $1.5 million of referral expenses. The credit would be limited to $600,000 for employers meeting the small-business receipts threshold and $500,000 for all other employers. This proposal would be effective for taxable years beginning after December 31, 2024.

Expanded child tax credit: Reiterating a key policy priority of the White House and congressional Democrats, the budget blueprint proposes to renew now-expired enhancements to the child tax credit that were enacted in the American Rescue Plan Act of 2021 and expired at the end of that year. Specifically, the administration calls for:

- Extending through 2025 the increased credit amount, higher phase-out thresholds, and the increased age limit for a qualifying child included in the 2021 legislation (effective for taxable years beginning after December 31, 2023);
- Permanently extending provisions that made the credit fully refundable regardless of earned income (effective for taxable years beginning after December 31, 2023) and allowed individuals to claim the credit in advanceable monthly installments (effective for taxable years beginning after December 31, 2024);
- Making other assorted changes to certain definitions and eligibility rules.

Tax credits for certain first-time home buyers and home sellers: The administration contends that the post-pandemic spike in interest rates has made home ownership more difficult for potential first-time buyers, in part because current home owners are more reluctant to sell a residence on which they have a low-interest mortgage. To address that issue, this year's budget blueprint includes two new proposals that would:

- Provide a refundable credit for qualified first-time home buyers: This proposal generally would create a two-year credit equal to 10 percent of the purchase price of a home located in the United States, up to a maximum total credit of $10,000. (The total credit allocated to a married individual filing a separate return would not exceed $5,000.) Half of the maximum credit amount would be applied to the tax

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return for the year the home was purchased; the remaining half would be applied to the tax return for the following year. The credit would phase out as modified adjusted gross income (MAGI) exceeds $100,000 and would phase out completely when MAGI exceeds $200,000 (or $50,000 and $100,000, respectively, for married taxpayers filing separate returns). Various eligibility rules also would apply for claiming the credit. Additional special rules would apply in the case of multiple individuals who purchase a home together. The credit would be available for home purchases after December 31, 2023, and before January 1, 2026.

- Provide a refundable credit for qualified home sellers: This proposal generally would create a one-time credit equal to 10 percent of the sales price of a home located in the US, with the credit amount capped at $10,000 ($5,000 for a married taxpayer filing a separate return). The credit would phase out as MAGI exceeds $100,000 and would phase out completely when MAGI exceeds $200,000 (or $50,000 and $100,000, respectively, for married taxpayers filing separate returns). A separate phase-out would apply beginning when a home's sales price exceeds 80 percent of the area median price and ending at a sales price of 100 percent of the area median price. Various eligibility rules also would apply. A seller would be able to claim the credit on the return for the taxable year in which the property is sold. The credit would be available for homes sold after December 31, 2023, and before January 1, 2025.

Other proposed changes: The blueprint also carries over several tax relief proposals from prior years that would:

- Renew and permanently extend the American Rescue Plan's expansion of the earned income tax credit for workers without qualifying children, effective for taxable years beginning after December 31, 2023;
- Permanently extend enhancements to Affordable Care Act premium subsidies that were enacted under the American Rescue Plan and are currently scheduled to expire at the end of 2025, effective for taxable years beginning after December 31, 2025;
- Make the current-law adoption tax credit refundable and allow certain guardianship arrangements to qualify, effective for taxable years beginning after December 31, 2023;
- Permanently extend the income exclusion for forgiven student loan debt, effective for taxable years beginning after December 31, 2025; and
- Expand tax-preferred treatment for scholarship and loan repayment programs to include certain federal programs dedicated to improving access to medical care for underserved populations, effective for taxable years beginning after December 31, 2023.

Outlook: A second-term wish list

Given the current partisan dynamics on Capitol Hill, where Democrats narrowly control the Senate and Republicans narrowly control the House, the prospects are dim that Congress this year will take up many (if any) of the administration's sweeping tax proposals. Rather, the provisions outlined in the Green Book can best be read as the tax policy agenda President Biden would pursue if he is re-elected to a second term this coming November *and* if Democrats reclaim the majority in the House and retain their majority in the Senate.

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No love from the GOP: Signaling the current partisan divide in Washington, House Ways and Means Committee Chairman Jason Smith, R-Mo., blasted the Green Book proposals in a statement released late on March 11.

"Family farms, ranches, and other generational businesses will be forced to sell off assets to pay well over $100 billion in new death taxes. Biden's war on American energy will continue with over $120 billion in new taxes—and higher prices to fuel cars and heat homes. Middle-class taxpayers will bear the brunt of a super-sized IRS with Biden's proposed $104 billion additional cash infusion to the tax collector—while reneging on the bipartisan agreement he made with Republicans in the Fiscal Responsibility Act to rescind part of the original $80 billion pay raise provided to the agency by congressional Democrats in the . . . Inflation Reduction Act," the statement read in part.

Senate Finance Committee ranking member Mike Crapo, R-Idaho, weighed in with his own set of objections.

"The tax-and-spend regime envisioned by the president would be felt by virtually all Americans," Crapo said in a March 11 statement. "Tax increases that slow the economy would be felt by consumers, retirees, and workers alike. Punitive international tax proposals would make it more attractive for companies to do business overseas, giving our biggest foreign competitors, like China, the upper hand in the global economy."

Reactions such as these are unsurprising given that Republicans already have been sketching out their own vision of a post-election tax policy landscape where the GOP controls the White House and both sides of Capitol Hill.

Several days before President Biden released his budget blueprint, for example, Jason Smith and his Republican colleagues on the Ways and Means Committee approved a budget views and estimates letter for the coming fiscal year indicating that the panel's focus will be on moving legislation that builds on Trump-era tax cuts. Soon thereafter, the Republican-led House Budget Committee approved a fiscal year 2025 budget resolution that appears to support extending those tax cuts while also dismantling certain key provisions in the Inflation Reduction Act. (For additional discussion of how Republicans on these two panels view their tax policy priorities, see *Tax News & Views*, Vol. 25, No. 9, Mar. 8, 2024.)
URL: https://gop-waysandmeans.house.gov/wp-content/uploads/2024/03/FY-25-VE-Letter_3.4.pdf
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URL: https://dhub.deloitte.com/Newsletters/Tax/2024/TNV/240308_4.html

This year, even what should be easy is hard: As evidence of just how difficult it will be to move a tax bill of *any* kind this year, it's worth bearing in mind that the fiscal year 2025 Green Book was released as lawmakers are struggling to advance even a relatively modest—$78 billion—package negotiated over the course of several months by Ways and Means Chairman Smith and Democratic Senate Finance Committee Chairman Ron Wyden that includes provisions that generally enjoy bipartisan support.

The Tax Relief for American Families and Workers Act (H.R. 7024) would, among other things, temporarily reverse certain business-unfriendly tax provisions related to the treatment of research expenditures, bonus depreciation, and the deduction for business interest expenses that were included in the Tax Cuts and Jobs Act

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but did not take effect until several years after that measure was enacted. It also would enhance the child tax credit—although that proposal is far more modest than the one the administration has included in its budget blueprint—and expand the low-income housing tax credit, and would be paid for through new strictures on the pandemic-era employee retention tax credit program.
URL: https://www.congress.gov/118/bills/hr7024/BILLS-118hr7024eh.pdf

The measure cleared the House by a margin of 357-70 on January 31, but that victory was possible only because Speaker Mike Johnson, R-La., opted to bypass objections from members of the ultraconservative Freedom Caucus on the House Rules Committee—the panel that sets the terms for debating bills on the House floor—and bring it straight to the floor under the fast-track process known as “suspension of the rules,” which prohibits amendments, limits debate time, and requires a two-thirds majority for passage rather than the simple majority threshold which normally prevails in the House. (Freedom Caucus members have argued, among other things, that the child tax credit enhancements in the measure essentially amount to a new form of welfare payments.)

The bill currently is languishing in the Senate, where a contingent of Republicans have insisted on an opportunity to propose amendments—for example, in a Finance Committee mark-up or in an eventual floor debate—to address their own concerns about the proposed child tax credit enhancements, among other things. Finance Committee ranking member Mike Crapo wants to eliminate a lookback provision in the proposed child tax credit enhancements that would allow individuals to claim the credit (for tax years 2024 and 2025) based on their prior-year income, arguing that the provision would disconnect the incentive from work. Other Republicans reportedly want to add provisions to the bill that, for example, would make technical corrections to the SECURE 2.0 Act (a retirement security package enacted in 2022) and renew certain expired tax “extenders” provisions.

Finance Committee Chairman Wyden and Ways and Means Committee Chairman Smith remain concerned that any changes adopted in the Senate could upset the careful balance of tax benefits for businesses and families in the current version of the legislation. Moreover, an amended bill would have to go back to the House for another floor vote, which could present a whole new set of challenges if members in either party who stifled their desire to make changes to the measure the first time around decide they want to put their imprint on it when it is brought up for reconsideration.

Regulatory action remains possible: Although opportunities for legislative action on tax policy appear limited this year, we still can expect that the Treasury Department (and other federal agencies) will be active in writing regulations that will have a major impact on businesses and individuals.

In 2022 and again in 2023, for example, Treasury issued notices announcing it would delay the implementation of a provision in the American Rescue Plan Act of 2021 that reduced the dollar-threshold triggering the Form 1099-K reporting requirement for third-party payment processors from $20,000 under prior law to $600 and eliminated the prior-law 200-transaction threshold, effective for reporting for returns filed for calendar years after 2021. (Lawmakers in both parties had tried without success to approve relief of some kind since the new reporting requirement was enacted.)
URL: https://www.irs.gov/pub/irs-drop/n-2023-10.pdf

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URL: https://www.irs.gov/pub/irs-drop/n-23-74.pdf

Indeed, regulatory intervention has been the norm for recent presidencies: when the Congress is unable to produce legislation, policymaking by regulation becomes a major focus. Although Treasury can't administratively raise tax rates, decisions around how to implement previously enacted laws, especially the Inflation Reduction Act, will have major implications for affected taxpayers.

— Alex Brosseau, Michael DeHoff, and Storme Sixeas
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