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JOE BIDEN:
The Tax Man Cometh

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KEY POINTS

- Democratic presidential nominee Joe Biden's tax plan is estimated to raise between $3.7 trillion and $4 trillion over a decade by increasing income taxes and applying payroll taxes on earnings above $400,000, raising the capital gains tax on income over $1 million, and increasing the corporate tax rate to 28%.
- There are no new direct taxes proposed on income under $400,000.
- The plan is estimated to reduce the after-tax income of the top 1 percent of earners by 13 to 18 percent and between 2 percent and 3 percent for the 95th to the 99th percentiles.

INTRODUCTION

Democratic presidential nominee Joe Biden has announced the most progressive federal tax plan in over 40 years. The proposal is estimated to raise between $3.7 trillion and $4 trillion over 10 years, or the equivalent of 1.5 percent of GDP. As a percent of GDP, this proposal, if it were to became law, would be the fifth largest tax increase since 1940 and the largest since 1968.

Major tax proposals by the Biden campaign include increasing federal revenue by $1 trillion to $1.2 trillion by raising the top individual tax rate to 39.7 percent, capping itemized deductions at the rate of 28 percent, and reviving the Pease Limitation, as well as treating capital gains as ordinary income for taxpayers with income over $1 million. The tax plan also imposes the full Social Security payroll tax on wages above $400,000, raising an expected $800 million to $1 trillion from high earners.

The plan would also raise $1.6 trillion to $1.9 trillion over a decade from corporations by increasing the corporate tax rate to 28 percent.

While the top 95th income percentile would bear most of the increased tax burden, with those earning over $352,800 paying approximately 85 percent of the new taxes, the proposal's progressive goals concentrate the impact at the very top of the income distribution. The top 1 percent of income earners would shoulder around 74 percent of the increase in taxes, but the top 0.1 percent of income earners would, by itself, bear 46% of the estimated new taxes. The remainder of the revenue will be raised through the increase in the corporate tax rate.

WHAT'S NEXT

Implementation of this plan obviously depends on the outcome of the Presidential election and control of the House and Senate. For Biden to raise taxes, the Democrats need to not only win the White House, but maintain control of the House of Representatives and win a minimum of a net three seats in the Senate. While Biden leads in the national polls, the polling in the swing states remains close.

With over 40 days to go before the final votes are cast, the outcome for the elections remains exceptionally uncertain, but at this time, a Democratic sweep cannot be completely dismissed. Consequently, we recommend that advisors proactively examine the potential tax ramifications for their clients and prepare to take action to minimize risks.

MAJOR ELEMENTS

INDIVIDUAL TAXES

Restore the Top Individual Tax Rate to 39.6 Percent

- A Biden Administration would raise the top individual tax rate to 39.6 percent for filers with more than $400,000 in taxable income, regardless of marital status. This would affect couples and individuals currently in the 35 percent and 37 percent brackets.

Tax Capital Gains and Dividends as Ordinary Income and Eliminate the Step-Up Basis at Death for Taxpayers with Over $1 million in Income

- Biden's plan would tax investment income as ordinary income for those making over $1 million, and tax unrealized capital gains at death.

Phase Out Business Income Deductions Above $400,000 for Pass-Through Entities

- The Biden proposal would maintain the deductibility of 20 percent of qualified business income in pass-through entities for those making under $400,000 per year. The deduction, which under current law is scheduled to expire after 2025, will be phased out completely for higher incomes.

Cap Itemized Deductions on Income Over $400,000

- Under the Biden Proposal, the rate at which itemized deductions can be taken will be capped at 28 percent. For example, someone in the 39.7 percent tax bracket can only deduct 28 percent of the value of a charitable contribution. The proposal would also reinstate the "Pease Limitation," which will further cap the value of itemized deductions.

Apply Social Security Payroll Taxes on Wages Above $400,000

- Currently, the payroll tax of 12.4 percent is capped on income up to $137,700. This level is increased annually at the rate of wage growth. The Biden proposal would subject wages above $400,000 to the payroll tax. The new threshold would be static — allowing the gap with the current level to close slowly over time as wages rise.

BUSINESS TAXES

Increase Corporate Income Tax Rate to 28 Percent

- Biden would increase the corporate tax rate from 21 percent to 28 percent, impacting corporate earnings and valuations going forward.

Impose 15 Percent Minimum Tax on Book Income

- For corporations with at least $100 million in annual income that would otherwise pay low or no corporate taxes, Biden would impose a 15 percent minimum tax on "book profits." Corporations will still be able to deduct loss carryforwards and foreign taxes paid from the new minimum tax.

Double the Minimum Tax on Foreign Income to 21 Percent

- Intangible property, i.e., intellectual property is highly mobile, and profits are easily shifted to low tax jurisdictions. This income is currently taxed at 10.5% under the Global Intangible Low-Taxed Income tax (GILTI). Biden would increase this to 21%.

CONCLUSION

Biden's tax proposal is potentially the largest tax increase since 1968, and it is targeted at raising government revenue from the highest earners, particularly from investment income. We will not know until after election day how viable this plan is, but we do not think it can be dismissed out of hand. Advisors should begin to consider the potential impact for their clients with the Biden proposal and review options to minimize these risks.

BUDGET EFFECTS OF JOE BIDEN'S TAX PLAN
$ Billions, 2021-2030

	Tax Policy Center	Penn Wharton Budget Model	Tax Foundation	AEI	Average
Raise top individual tax rate to 39.6 percent for income above $400,00.	$143	$153	$151	$100	$137
Cap itemized deductions at 28 percent, and Restore Pease limitations for income above $400,000	$376	$263	$357	$312	$327
Tax Capital Gains and dividends at top ordinary income rate (39.6 percent) for taxpayers with income over $1 million and tax unrealized gains at death.	$448	$382	$503	$379	$428
Apply full payroll tax (Social Security) to income over $400,000	$962	$1,035	$808	$797	$901
Phase out 20 percent deductions of QBI for entities earning above $400,000.	$219	$208	$197	$212	$209
Raise Corporate Tax Rate to 28 percent.	$1,300	$1,088	$1,306	$1,297	$1,248
Institute 15 percent minimum "book tax" on companies reporting over $100 million profits in the US but paid zero or negative taxes.	$166	$227	$318	$160	$218
Raise the tax on foreign income of US subsidiaries from intangible assets, i.e. intellectual property (GILTI).	$309	$323	$303	$310	$311
Other provisions	$70	$67	($146)	$281	$68
Total Estimated Revenue	**$3,993**	**$3,746**	**$3,797**	**$3,848**	**$3,846**

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