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Tax Planning in 2023: Biden's Budget for Next Year

The fiscal year for the White House runs from October 1 to September 30 each year. That means that FY2023 will begin in October 2022. To prepare for the new year, President Biden recently announced his budget plans for the United States.

In total, the budget has spending plans for $5.8 trillion, including strategies to reduce the national deficit by roughly $10 trillion over the next 10 years. Plans to increase revenues are primarily based on increasing the corporate tax rate to 28% (from 21%). Plans for introducing a minimum tax on billionaires are also a crucial part of the budget. Below is a summary of some of the major provisions of the budget.

Increased Taxes on High-Income Households

Biden's "billionaire" tax would tax those worth over $100 million (roughly 0.01% of American households) a minimum of 20%. This tax would include income based on unrealized investment income, which is currently untaxed. According to the White House, this revenue stream alone could cut the deficit by roughly $360 billion over the next 10 years.

The increased tax does not just affect billionaires, however. Any household making over $450,000 (if married filing jointly) may see increased taxes. The proposal includes increasing the top marginal tax rate for these high-income earners to 39.6%. This increase would go into effect for tax year 2023, with adjustments for inflation in the coming years.

Capital income could also see a huge tax increase. The new budget includes a proposal to tax high-income earners' capital income at their ordinary tax rates. However, this rate hike would only apply to those with taxable income of more than $1 million.

Increased Funding for the IRS

The new budget proposed an increase in funding for the IRS of $798 million, for a total of $14.1 billion. The extra funds are projected to help expand customer service functions and provide more outreach to underserved communities.

The budget also sets aside $310 million for IRS Business Systems Modernization, which helps facilitate better digital communication between the IRS and taxpayers. These funds are specifically targeted at helping the IRS provide more effective oversight of corporate tax returns and those filed by high-income individuals.

Adoption of the Undertaxed Profits Rule

The undertaxed profits rule would replace the base erosion anti-avoidance tax starting in 2024. This is a "top-up" tax targeted specifically at multinational companies. Essentially, it makes changes to ensure that these larger companies pay taxes of at least 15%.

This change specifically applies to foreign-parented companies operating in a low-tax jurisdiction and financial reporting groups with global revenues of $850 million or more for at least two of the prior four years in operation.

Incentives for Domestic Businesses and Jobs
A portion of the budget provides incentives for keeping businesses and jobs in the United States. It includes a 10% tax credit for providing jobs and business activity in the United States to offset costs related to reducing a line of business that is currently up and running outside of the country.

The provisions also disallow deductions for costs related to moving a trade or business outside of the United States.

Low-Income Tax Changes
The budget sets out some tax reductions for lower-income families. The Low-Income Housing Tax Credit would allow state housing credit authorities more flexibility to allow “basis boosts” regardless of geography. It applies to new construction and substantial rehabilitation projects that are financed with private activity bonds.

The budget also expands funding for Housing Choice Vouchers, which help people who need rental assistance. The increase is roughly 17%, or $4.8 billion. The program also increases funding for homeless programs and public housing.

“Deemed Sale” Transfers: Capital Income Reform
Long-term capital gains and qualified dividends will be taxed as ordinary income for those who have a taxable income of more than $1 million (married filing jointly).

The budget also changes transactions so that some are “deemed sales,” triggering a taxable event. Examples include:

- Transfer of appreciated property by gift or death
- Unrealized appreciation on property held in trust or in a partnership or other non-corporate entity (if the property has not been the subject of a recognition event in the past 90 years)
- Property transfers into or from certain trusts (other than revocable trusts), partnerships or other non-corporate entities

There is a $5 million lifetime exclusion, which can be passed to a surviving spouse. There are also exceptions for transfers to a spouse or charity.

This “deemed sale” provision could have a huge impact on estate and gift tax planning. It effectively eliminates the step-up in basis benefit for large estates and increases the overall cost of gifting. If this plan moves forward, investors may need to change their existing plans.

The Bottom Line: Implementing Tax Planning Strategies
While the proposed budget has a number of changes, it is unclear whether any of these provisions will pass. Nonetheless, keeping an eye on these proposals is a good idea for those who have existing tax plans and who are currently creating tax planning strategies.

If you have any questions please contact any of our professionals at Frankel Zacharia, LLC, 402.496.9100.