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White House 2023 budget raises $2.5 trillion over 10 years

The White House's proposed budget for fiscal year 2023 contains revenue proposals, including taxes targeting billionaires and corporations, that would raise more than $2.5 trillion over the next 10 years.

"The budget includes proposals that reform corporate taxation, encourage housing and urban development, strengthen the taxation of high-income taxpayers, support families and students, close loopholes, and improve tax administration and compliance," the Biden administration states in the Greenbook that outlines and describes all revenue proposals in the fiscal year 2023 budget. The Greenbook was released on March 27, 2022, as a supporting document to the overall budget proposal issued the same day.

High-income individuals

The White House will be targeting high-income individuals by raising the top marginal tax rate to 39.6%, which would apply to taxable income over $450,000 for married couples filing a joint return, $400,000 for unmarried individuals (not including surviving spouses), $425,000 for head of household filers and $225,000 for married individuals filing a separate return. The thresholds would be indexed for inflation following 2023.

Long-term capital gains also would undergo a change.

"Preferential tax rates on long-term capital gains and qualified dividends disproportionately benefit high-income taxpayers and provide many high-income taxpayers with a lower tax rate than many low- and middle-income taxpayers," the Greenbook says. "The rate disparity between taxes on capital gains and qualified dividends on the one hand, and taxes on labor income on the other, also encourages economically wasteful efforts to convert labor income into capital income as a tax avoidance strategy."

Under the White House budget, long-term capital gains and qualified dividends of taxpayers with taxable income of more than $1 million ($500,000 for married filing separately) would be taxed at ordinary rates. Transfers of appreciated property by gift or death would be considered a realization event, with certain exclusions.

For those with wealth greater than $100 million, the White House is proposing a minimum tax of 20% on total income, generally inclusive of unrealized capital gains.

"A taxpayer's minimum tax liability would equal the minimum tax rate (that is, 20%) times the sum of taxable income and unrealized gains (including on ordinary assets) of the taxpayer, less the sum of the taxpayer's unrefunded, uncredited prepayments and regular tax," the Greenbook states. "Payments of the minimum tax would be treated as a prepayment available to be credited against subsequent taxes on realized capital gains to avoid taxing the same amount of gain more than once. The amount of a taxpayer's 'uncredited prepayments' would equal the cumulative minimum tax liability assessed (including installment payments not yet due) for prior years, less any amount credited against realized capital gains in prior years."

Corporate tax changes

Under the White House proposal, the corporate income tax rate would change to 28%, up from the current 21%.

"Raising the corporate income tax rate is an administratively simple way to raise revenue to pay for the Administration's infrastructure proposals and other longstanding fiscal priorities," the Greenbook says. "A corporate tax rate increase can expand the progressivity of the tax system and help reduce income inequality."

The executive branch is also calling for replacement of the base erosion anti-tax abuse liability with an undertaxed profits rule, setting a minimum corporate tax rate of 15% for foreign-parented multinational corporations.

The Biden administration aims to spur job growth in the United States by providing tax incentives for jobs and business activities in the U.S. while removing tax deductions for corporations that move jobs overseas. Businesses would gain a 10% tax credit on eligible expenses for onshoring jobs and business activities.

Housing and urban development support

The Greenbook includes two housing and urban development proposals. The first is making the New Markets Tax Credit permanent. The administration states this credit helps generate investment in low-income communities and would provide greater certainty for investment planning purposes.

The second would allow for selective basis boosts for bond-financed low-income housing credit projects.

"Geographically grounded basis boosts have proved effective in significantly increasing the supply of affordable rental housing, which is in increasingly short supply across the nation," the Greenbook states.

Support for energy policy

The White House proposes to eliminate fossil fuel tax preferences that encourage oil, gas and coal production, including repeal of provisions such as the enhanced oil recovery credit, expensing of intangible drilling costs and capital gains treatment for royalties.

The Biden administration also is proposing to modify oil spill liability trust fund financing and Superfund excise taxes.

Support for families and students

To help lower the cost of adoption, the White House is proposing to make the adoption credit fully refundable, allowing taxpayers to claim the full amount of any eligible credit in the year the expense was first eligible, regardless of tax liability. Additionally, taxpayers with unused carryforward amounts from eligible expenses for earlier adoptions would be able to claim the full amount of any unused carryforward on their 2023 tax return.

Under this proposal, certain guardianship arrangements would also be eligible for a refundable credit for related expenses.

For students, the administration is proposing to make permanent the exclusion of certain forgiven or discharged student loan debt from gross income and thus taxation.

Other changes

Additionally, the Greenbook proposes the following:

- Modification to the income, estate and gift tax rules for certain grantor trusts

- A requirement for consistent valuation for promissory notes
- Improved tax administration for trusts and decedents' estates
- Limiting the duration of the generation skipping transfer tax exemption

It also proposes:

- Closing loopholes related to tax carried interests as ordinary income
- Repeal of the deferral of gain from like-kind exchanges
- Extension of the period for assessment of tax for certain qualified opportunity fund investors
- Establishment of an untaxed income account regime for certain small insurance companies

The White House proposal to improve administration and compliance recommends modernizing certain rules, including digital assets, as well as improving benefits tax administration.

A 20% increase for Treasury

The White House is asking for a 20% increase in the discretionary funding for the Department of the Treasury. The $16.2 billion request represents a $2.7 billion increase from the 2021 enacted level. Of those funds, $14.1 billion would go to the Internal Revenue Service.

"This includes an increase of $798 million to improve the taxpayer experience and expand customer service outreach to underserved communities and the taxpaying public at large," the budget document states. "The budget also provides $310 million for IRS business systems modernization, which is 39% above the 2021 enacted level, to accelerate the development of new digital tools to enable better communication between taxpayers and the IRS."

The White House budget documents say the increase in funding will also "facilitate more effective oversight of high-income and corporate tax returns" but do not specify how those funds would be spent. ◆

Price ESOP paid for company owners' shares did not exceed fair market value

According to a federal trial court in Hawaii, the owners of a company did not breach their fiduciary duties when selling their shares to an ESOP for what proved to be adequate consideration, even though the company stock value fell by $30 million (70%) within a year of the sale. The court explained that the decrease in valuation was a function of the debt incurred when the ESOP purchased the company's stock and the company's guarantee of the ESOP's payment of the purchase price.

The court also ruled that the Department of Labor's suit action was not time-barred, as the filing of the ESOP's Form 5500 did not provide it with actual knowledge of the alleged breach and the government did not act with willful blindness to the ESOP trustee's actions with respect to other ESOPs under investigation.

Owners of an architectural engineering firm sold all 1 million shares of the company to an ESOP for $40 million on Dec. 14, 2012. The ESOP, which had been created specifically for the sale, paid for the shares with funds lent to it by the owners, through a 25-year loan at 7% interest. Pursuant to the sale terms negotiated by the ESOP trustee, whom the owners' attorney had strongly recommended, the company guaranteed the ESOP's continued payment of the purchase price.

In June 2013, an independent appraiser of the company issued a valuation report for the company, as of Dec. 31, 2012 (two weeks after the sale). The company had been valued at $40.15 per share on the Dec. 14, 2012, date of sale. The appraiser's report, reflecting the company's debt obligations related to the sale of the owners' stock to the ESOP, set the value of the company following the sale at $6.53 million ($6.53 per share).

Following the $30 million drop in the company's stock valuation and internal reviews triggered by analysis of the ESOP's Form 5500, the DOL, noting that the owners' desired price was shared ahead of the sale with the ESOP's trustee and greatly exceeded an earlier $15 million valuation of the company (included in a nonbinding indication of interest by another company), brought suit against the owners in April 2018. The DOL charged that the owners violated their fiduciary duties and committed prohibited transactions in manipulating data to induce the ESOP to pay a predetermined price for their shares that exceeded the fair market value of the company. The central issue before the court was whether the sale price of $40 million exceeded the fair market value of the company as of the Dec. 14, 2021, sale (see *Walsh v. Bowers* (DC HI), No. 18-00155 SOM-WRP, Sept. 17, 2021). ◆

Proposed regulations issued on eligibility for premium tax credit

The IRS has released proposed regulations to amend the existing regulations regarding eligibility for the premium tax credit (PTC) (NPRM REG-114339-21). The amendments would provide that affordability of employer-sponsored minimum essential coverage for family members of an employee is determined based on the employee's share of the cost of covering the employee and those family members, not the cost of covering only the employee. A minimum value rule would be added for family members of employees based on the benefits provided to the family members. Further, the proposed regulations would affect taxpayers who enroll themselves or a family member in individual health insurance coverage through a health insurance exchange and who may be allowed a PTC for the coverage.

Background

On Sept. 1, 2015, the Treasury Department and the IRS issued proposed regulations under Code Sec. 36B (REG-143800-14) incorporating the substance of the minimum value rule in the Health and Human Services final regulations. The proposed rule relating to substantial coverage of inpatient hospital services and physician services was not finalized.

On Jan. 28, 2021, President Biden issued Executive Order 14009, *Strengthening Medicaid and the Affordable Care Act (ACA)* (P.L. 111-148). Consequently, the Treasury Department and the IRS reviewed the regulations under Code Sec. 36B, including Reg.§1.36B-2(c)(3)(v)(A)(2), which provides that the affordability of employer coverage for related individuals is based on the employee's share of the annual premium for self-only coverage, not the cost of family coverage. The Treasury and the IRS have tentatively determined that the rule in Reg. §1.36B-2(c)(3)(v)(A)(2) is not required by the relevant statutes and is inconsistent with the overall purpose of the ACA to expand access to affordable health care coverage.

Major amendments

Following are some of the major amendments proposed by the IRS:

- The proposed changes to the affordability rule for related individuals would create greater consistency between the affordability rules in Code Sec. 36B(c)(2)(C)(i) and those in Code Sec. 5000A(e)(1).
- The proposed changes would also promote consistency between the affordability rules in these provisions and 42 U.S.C. 18081(b)(4)(C), which requires exchange applicants to separately provide the required contributions of employees and related individuals in order to determine PTC eligibility.
- Changes would be made only to the affordability rule for related individuals, not for employees.
- Employees will continue to have an offer of affordable employer coverage if the employee's required contribution for self-only coverage of the employee does not exceed the required contribution percentage of household income. Accordingly, under the proposed regulations, a spouse or dependent of an employee may have an offer of employer coverage that is unaffordable even though the employee has an affordable offer of self-only coverage.

The proposed regulations also address situations in which an individual has offers of coverage from multiple employers. Under the proposed regulations, an individual with such offers, either as an employee or a related individual, has an offer of affordable coverage if at least one of the offers is affordable. The proposed regulations would amend Reg. §1.36B-2(c)(3)(v)(B) to provide a part-year period rule for employees based on the employee's required contribution for self-only coverage and a part-year period rule for related individuals based on the employee's required contribution for family coverage.

Minimum value cost of benefits rule for related individuals

These proposed regulations provide in Reg. §1.36B-6(a)(2)(i) that an eligible employer-sponsored plan satisfies the minimum value requirement only if the plan's share of the total allowed costs of benefits provided to related individuals is at least 60%, like the existing rule in Reg. §1.36B-6(a)(1) for employees. Further, to provide minimum value under Reg. §1.36B-6(a)(2)(ii) of these proposed regulations, an eligible-employer sponsored plan must include substantial coverage of inpatient hospital services and physician services.

Minimum value rule regarding inpatient hospitalization and physician services

The Treasury and the IRS have expanded the minimum value rule in Reg. §1.36B-6(a)(2) of the 2015 proposed regulations to apply to related individuals. Thus, Reg. §1.36B-6(a)(2)(ii) of the new proposed regulations states that an eligible employer-sponsored plan provides minimum value to a related individual only if the plan benefits include substantial coverage of inpatient hospital services and physician services in addition to covering at least 60% of the total allowed costs of benefits provided to the related individual.

Premium refunds affecting the PTC computation

The proposed regulations clarify that, in computing the premium assistance amount for a coverage month, a taxpayer's enrollment premiums for the month are the monthly premiums reduced by any amounts refunded in the same tax year the taxpayer incurred the premium liability. ◆

Employment tax relief denied because founder was a statutory employee

A corporation was not entitled to relief from employment taxes pursuant to section 530 of the Revenue Act of 1978, because the founder of the corporation satisfied the definition of a statutory employee under Code Sec. 3121(d)(1). The founder incorporated a Code Sec. 501 tax-exempt corporation to offer seminars on real estate development, serving as a member of the board of directors and a corporate officer. The founder controlled all aspects of the seminars and received compensation pursuant to an unwritten contract. From its incorporation, the taxpayer did not file any employer tax returns reporting payments to the founder as salary or wages for services provided as an employee by or on behalf of the taxpayer.

Statutory employee

At trial, the taxpayer failed to produce credible evidence that the founder worked for or was engaged by the taxpayer other than as an officer. The only items in the record that suggested a separate independent contractor relationships were the Form 1099–MISC reporting nonemployee compensation and the founder's own testimony that he served the taxpayer in a dual capacity. However, the taxpayer failed to carry its burden of establishing that the founder served in a dual capacity, as the court saw no clear distinction between the founder's dual roles as a corporate officer and his provision of services to the corporation.

Additionally, the record was clear that the founder performed significantly more than minor services for the taxpayer. Therefore, the taxpayer was not allowed the exception in Reg. §§31.3121(d)-1(b) and 31.3401(c)-1(f). Further, given the weight of the evidence establishing extensive services the founder provided to the corporation and payments he received as compensation for those services, the court did not accept the taxpayer's characterization of the payments as royalties. Finally, the taxpayer's contention that the founder could not be its employee because the taxpayer could not control him was unpersuasive. The right to control is a common law classification factor, and the taxpayer's attempt to rely on it as determinative of statutory employee status was misplaced.

Penalties

The taxpayer was liable for additions to tax for failure to timely file the required employment tax returns or timely pay the amount shown as tax in the substitute tax returns for three quarters. The taxpayer did not argue that it had reasonable cause and submitted no credible evidence that it exercised ordinary business care and prudence in its failure to file employment tax returns. While the taxpayer made vague references in its post-trial briefs to having previously consulted with tax counsel regarding the tax treatment of the founder's compensation, such statements were insufficient to establish reasonable cause, which was unsupported by evidence (see *The Redi Foundation, Inc.*, T.C. Memo. 2022-34, Dec. 62,038(M)). ◆

"Additionally, the record was clear that the founder performed significantly more than minor services for the taxpayer."

House passes SECURE Act 2.0 with bipartisan approval

On March 29, 2022, the House of Representatives passed the Securing a Strong Retirement Act of 2022 by a vote of 414 to 5. The bill, widely known as SECURE Act 2.0, had been in proposal stage for more than a year. It follows the original SECURE Act, passed as part of the Consolidated Appropriations Act, 2020, in December 2019. The bill enjoys strong bipartisan support and is expected to pass in the Senate.

The SECURE Act 2.0 is designed to build on the provisions of the original SECURE Act and further ensure that more Americans can save an increased amount for retirement. The bill expands on automatic enrollment programs, helping ensure that small employers can easily and efficiently sponsor plans for employees. It enhances credits to make saving for retirement beneficial to both plan participants and sponsors. It also improves investment options for plan participants, streamlines plan administration for fiduciaries and makes important changes to required minimum distributions (RMDs) to help retirees with plan selection and enhance their ability to use their retirement savings.

Increasing plan participation

Automatic enrollment – One broadly applicable provision of the bill requires that, effective for plan years beginning after 2023, 401(k) and 403(b) sponsors automatically enroll employees in plans once they become eligible to participate. Under the requirement, the amount at which employees are automatically enrolled cannot be any less than 3% of salary, and no more than 10%. The amount of employee contributions is increased by 1% every year after automatic enrollment, up to a maximum contribution of 10%. Employees can opt out of the automatic enrollment.

Saver's credit – For tax years beginning after 2026, the saver's credit is simplified from its current three-tier structure based on income amounts to a unified 50% credit amount, with a phaseout for higher incomes. Additionally, the Treasury is directed to increase public awareness of the credit.

Catch-up limits – The annual amount that can be contributed to a retirement plan is limited, generally subject to annual adjustments for inflation. For plan participants age 50 or older, the contribution limit is increased. For 2022, the catch-up contribution is limited to $6,500 for most retirement plans, and $3,000 for SIMPLE plans, subject to inflation increases. Under the SECURE Act 2.0, a second increase in the contribution amount would be available for participants ages 62-64, effective for tax years after 2023. For most plans, this second catch-up limitation would be $10,000, and $5,000 for SIMPLE plans. Like the standard catch-up amount, these limitations would also be subject to inflation adjustment.

The annual limit on contributions to IRAs is also increased for participants age 50 and older. The catch-up limit for IRAs is $1,000. Unlike the catch-up amount for other plans, this amount is not subject to inflation increases under current law. For tax years beginning after 2023, the SECURE Act 2.0 would make the IRA catch-up amount adjusted annually for inflation.

Finally, for tax years beginning after 2022, the bill makes all catch-up contributions subject to Roth (after-tax) rules, rather than only where allowed by the plan.

RMDs

Under current law, enacted as part of the original SECURE Act, plan participants must begin taking RMDs at age 72. Under the SECURE Act 2.0, the age at which participants must begin taking distributions increases over a period of ten years. Starting in 2023, the age increases to 73. The age at which participants must begin taking RMDs further increases to 74 beginning in 2030, and again to 75 beginning in 2033.

The bill would also reduce the penalty on failures to take RMDs from 50% to 25%. The 25% penalty would further reduce to 10% if timely corrective action were taken. The reduction is effective for tax years beginning after 2022.

Annuities

The SECURE Act 2.0 eliminates an actuarial test in the RMD regulations that limits the use of certain annuities in defined contribution plans and IRAs. The modification enables participants to elect to use annuities that provide only a small financial benefit but important guarantees. The change is effective for calendar years after the date of enactment.

The bill also removes statutory barriers to the adoption and growth of qualifying longevity annuity contracts that caused RMD-related regulations to limit their adoption. The provision is effective on the date of enactment. ◆

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2022 Edward Jones tax management opportunities

Although Edward Jones cannot provide tax advice, our financial advisors can use a team approach with you to help investors understand the impact of capital gains and losses on their investments and offer opportunities to use tax management strategies before the end of 2022.

1. Financial advisors can **identify clients** who may have substantial realized gains and/or losses before the end of 2022 and get permission to share this information with you.
2. They can **identify current holdings** these investors own that may have substantial unrealized capital gains and/or losses.
3. They can work together with you to **share tax management opportunities** with these investors.

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Please contact one of our financial advisors today about helping mutual clients.