DHG

ALERT

December 2021

The Latest Evolution of the Build Back Better Act

Since its introduction, the Build Back Better Act (BBBA) has evolved through multiple versions of the legislation. The most recent version was released by the Senate Finance Committee on December 11, 2021. With the BBBA still being debated in the Senate, the current version of the bill could still be changed.

The following is a summary of the significant domestic tax proposals included in the most recent version of the BBBA under consideration:

CORPORATE TAX

- **15% corporate minimum tax**—For C-Corporations with a three-year average of $1 billion in profits reported to shareholders, an additional 15% corporate alternative minimum tax would apply for tax years beginning after December 31, 2022.
- **1% excise tax on stock buyback**—For domestic, public corporations with stock traded on a securities market, if the corporation repurchases its stock, an excise tax would be levied. This excise tax would generally be equal to 1% of the fair market value of the corporation's repurchased stock. These changes would be effective for repurchases occurring after December 31, 2021.

INDIVIDUAL AND BUSINESS TAX

- **Expansion of net investment income tax (NIIT)**—Nonpassive income from trades or businesses of high-income individuals, estates and trusts would generally now be subject to the NIIT. The high-income threshold would be modified adjusted gross income (MAGI) over $500,000 for married filing jointly or head of household individuals, $250,000 for married filing separate individuals, $400,000 for all other individuals, and, for estates and trusts the income level whereby income would be taxed at the top tax rate. This income would include gains from sales not previously subject to the NIIT. Trade or business income that is treated as self-employment income and subject to self-employment tax would not be further subject to NIIT. Overall, pass-through income regardless of entity type would be subject to a 3.8% tax whether passive or nonpassive. These changes would be effective for taxable years beginning after December 31, 2021.
- **Limitation on excess business losses**—An excess business loss (EBL) is the amount by which business losses exceed business income plus a threshold amount. EBLs would no longer be considered NOLs carried forward indefinitely. Instead, prior year EBLs would be considered for limitation alongside current-year business losses. The provision would also make permanent the disallowance of excess business losses in any given tax year. These changes would be effective for taxable years beginning December 31, 2020.
- **New surcharge on high-income individuals, trusts, and estates**—A 5% surtax would be applied to modified adjusted gross income (MAGI) over certain thresholds. The MAGI threshold would be $10 million for all individuals except those filing married filing separately which would have a $5 million threshold and $200,000 for estates and trusts. An additional 3% surtax for a total of 8% would be applied to MAGI over a higher second threshold ($25 million for all individuals except those filing married filing separately which would have a $12.5 million threshold, and $500,000 for estates and trusts). The new surcharge would be effective for taxable years beginning after December 31, 2021.

- **Modification of business interest expense limitation**— The section 163(j) business interest expense limitation would be calculated at the partner or shareholder level, rather than partnership or S-corporation level. The partner or shareholder would not take into account entities exempt from section 163(j) as a small business. This change would be effective for taxable years beginning after December 31, 2022.
- **State and local tax (SALT) cap modification**—Currently, there is a $10,000 itemized deduction available for state and local taxes. The amount of this “cap” on state and local tax deductibility was proposed to be changed in the version of the BBBA passed by the House. However, in the Senate’s December 12, 2021, version, there is simply a placeholder for a future compromise related to the state and local tax “cap”. Therefore, no specific changes are currently enumerated. DHG will inform you as updates are released.
- **Child tax credit**—The current increased credit would be extended to 2022, with unchanged income thresholds. Monthly advance availability would be extended through 2022 as well. Refundability of the credit would be made permanent.
- **Limitation on gain exclusion for qualified small business stock**—The sale or exchange of qualified small business stock by high-income taxpayers would result in a 50% exclusion of gain from income instead of the potentially higher 75% of 100% exclusion rates. This applies to taxpayers with adjusted gross income equaling or exceeding $400,000. This also applies to all trusts or estates, regardless of income level. These changes would apply to sales and exchanges occurring after September 13, 2021.
- **Common control rule**—Grouping activities are often required when electing methods or calculating limitations. For example, if two trades or businesses are considered to be under common control, their activities are grouped when calculating the section 163(j) business interest expense limitation or determining if the cash method of accounting is available. The BBBA would generally expand the definition of trades or businesses for these purposes to include activities under section 212, which include investment companies and activities related to the production of income. Potentially affected would be private equity groups or other investment entities not previously subject to these rules. These changes would apply to taxable years beginning after December 31, 2021.
- **Expansion of wash sales**—Consideration of your related parties’ activities would be required when applying the wash sale rules. Related parties would generally include spouses, dependents, other related individuals under section 267(b), and entities controlled by the taxpayer as well as individual retirement plans and 529 or Coverdell education savings accounts. Further, cryptocurrencies, commodities, and foreign currencies would generally now be considered a specified asset subject to the wash sale rules. Further, the basis adjustment generally associated with the wash sale rule would only apply to assets acquired by the taxpayer or the taxpayer’s spouse. Related parties would not see a basis adjustment and therefore a disallowed loss could be permanently disallowed instead of simply deferred. These changes would apply to sales, dispositions, and terminations occurring after December 31, 2021.
- **Research and development expenses**—The requirement to capitalize and amortize research or experimental expenditures over 5 years would be delayed from taxable years beginning after December 31, 2021, to taxable years beginning after December 31, 2025.

RETIREMENT PLANS

- **Contributions limits to “Mega” IRAs**— “Mega” IRAs are defined as retirement accounts, including Roth and traditional IRAs, exceeding $10 million in value as of the end of the previous tax year. No contributions would be allowed to such accounts for individuals with income over certain thresholds. The single or married filing separate threshold would be $400,000, the married filing joint threshold would be $450,000, and the head of household threshold would be $425,000. “Mega” IRAs do not include SEP plans or simple retirement accounts.

In addition, new reporting requirements would be added for certain accounts with a balance of more than $2.5 million. These changes would be effective for taxable years beginning after December 31, 2028.

- **Increase to required minimum distributions (RMD)**—If retirement accounts exceed a $10 million threshold, additional RMDs would be required for high-income taxpayers. This requirement would be effective for tax years beginning after December 31, 2028.
- **Roth conversions and rollovers**—The only way to contribute to a Roth account would be to either directly contribute to the Roth account or roll one Roth account into another. The ability for high-income individuals to be able to contribute to a Roth IRA by first making a nondeductible contribution to a traditional IRA and then converting the IRA would no longer be allowed. These changes would apply to contributions, distributions, or transfers that are made after December 31, 2021. In addition, rollovers or conversions from IRAs or employer-sponsored retirement plans would no longer be allowed for high-income individuals beginning in 2032.
- **Prohibited investments by IRAs in DISCs and FSCs**—Either directly or indirectly holding an interest in a Domestic International Sales Corporation (DISC) or a Foreign Sales Corporation (FSC), would generally no longer be allowed. This change would apply to stock or other interests that are acquired or held after December 31, 2021.

CREDITS

- Favorable changes to incentives for housing, renewable energy, and electric vehicles are included in this version of BBBA. Further detail will be provided in a subsequent tax alert.

With the end of the calendar year quickly approaching, lawmakers are being pressured to examine the BBBA and to consider its effect on the nation's budget. The Senate's goal remains to pass the BBBA by year end, though changes to the current version may alter this timeline. DHG will continue to monitor this legislation as any adjustments arise.

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