President Biden's American Families Plan and what it means for you

As promised throughout his campaign, President Joe Biden is planning to end the preferential tax treatment of investment income for wealthy Americans. He used his first joint address to Congress to outline his two-part economic plan that calls for higher taxes on corporations and the wealthy. He also wants to boost IRS enforcement efforts on the wealthy to drive tax revenue. The administration plans to use the extra revenue to fund various initiatives, such as addressing climate change, providing free education, and up to 12 weeks of paid family and medical leave. Here are the key points to consider as you think about your personal tax situation:

- **A new top tax rate of 39.6%**
  President Biden is proposing a top tax rate of 39.6%, up from 37%. The new rate is only expected to apply to the top 1% of taxpayers. It is not yet clear at what level of income the new rate will apply or when it will be put in place.

- **A doubling of the capital gains tax rate**
  Biden proposed almost doubling the capital gains tax rate for both individuals and couples earning $1,000,000 or more each year. With the Obamacare tax factored in, this would send the top federal rate soaring to 43.4%. Currently, the top rate on capital gains is 23.8%. For taxpayers living in high taxing states, such as New York and California, total tax rates on capital gains would be over 50%.

- **Capital gains at death**
  The proposal will also change how large estates will pay tax on appreciated assets at death. Under Biden's proposal, the step-up in basis for capital gains purposes at death will no longer apply for any gains of more than $1 million. At this point, there is no proposal to reduce the current $11.7m estate tax exemption.

- **Limiting the use of Like Kind Exchanges**
  Like Kind exchanges are frequently used by real estate investors to defer gain on real estate sales, sometimes indefinitely. Biden is proposing that this tax break be eliminated for transactions with gains of over $500,000.

- **Close the Carried Interest Loophole**
  Biden wants to eliminate the carried-interest tax break altogether. It's an idea the private equity industry is expected to fight vigorously. This loophole could also be endangered by the increase in the capital gains tax rate, at least for wealthy taxpayers.

Keep in mind, the American Families Plan is currently just a proposal, and will be debated over the coming weeks. Some Democrats have refused to pass the proposal unless the 2017 TCJA limitation on SALT deductions is repealed. It is likely that some revised version of the above changes to the tax code will pass, and will likely take effect 1/1/2022. It has been discussed that these changes could apply retroactively, but that is unlikely.

The best advice for taxpayers at this point, is that taxes are almost certainly going up. If you expect to recognize large capital gains in the near future, it may make sense to recognize in 2021, if possible. It may also make sense to defer deductions to next year, when your overall tax rate is higher. If the capital gains increase passes, contributions of appreciated stock to donor advised funds will become even more attractive. It may also be a good time to review your estate planning, especially if you intend to pass on assets with large unrealized gains.

Disclaimer: The American Families Plan is currently just a proposal, and will be debated and possibly changed as it moves through Congress. Therefore, we don't recommend making any significant planning moves until we have a final version of the bill. Please reach out to your MAI advisor to discuss how this could impact you and if any mitigation techniques are in order.

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