



THE SMALL BUSINESS LEGISLATIVE COUNCIL ALERT

DECEMBER 7, 2021

IN THIS ALERT:

- **WHAT'S HAPPENING WITH THE BUILD BACK BETTER ACT?**

WHAT'S HAPPENING WITH THE BUILD BACK BETTER ACT?

On November 19th, the House passed the Build Back Better Act (the “BBB”) (HR. 5376).

In the tax area, many of the provisions which could have been very detrimental to small businesses and their owners were removed from the final House passed version of the BBB.

Specifically, in the final House bill, this is what happened with the proposed tax provisions:

- **No changes to the individual tax rates for the vast majority of Americans.** No change to income tax or capital gains rates. Only those with modified adjusted gross income (“MAGI”) of more than \$10,000,000 will see an increase in income taxes through a new surtax;
- **No change to the estate and gift tax exemption amounts or rates for anyone;**
- **No change to the step up in basis for assets going through an estate.** This provision could have been devastating to many small business owners and had the potential to impose a new capital gains tax on many Americans who are not “wealthy” and could have potentially caused the forced sale of family homes, farms and businesses to pay the new tax;
- **No change to the grantor trust rules.** Earlier versions of BBB contained a provision dealing with grantor trusts which would have eliminated a popular estate planning tool and would have created havoc with almost all existing irrevocable life insurance trusts;
- **No change to the valuation discounts used when transferring interests in most family-owned businesses from an older to a younger generation.** The original proposals would have eliminated the ability to transfer interests in family LLCs and partnerships to the younger generation in a cost-effective manner;
- **A new significant surtax for the super wealthy and non-grantor trusts.**
 - Additional 5% surtax on MAGI in excess of \$10,000,000 (single or married filing jointly) for individuals and in excess of \$200,000 for non-grantor trusts;
 - Extra additional 3% surtax on MAGI in excess of \$25,000,000 (single or married filing jointly) for individuals and in excess of \$500,000 for non-grantor trusts;
- **No change to C corporation tax rates;**

- **Expansion of the 3.8% net investment income tax (NIIT) to apply to active business income from pass-through entities (such as S corporations and partnerships) for those taxpayers earning more than \$400,000 (if single) and \$500,000 (if married filing jointly).** Under current law the 3.8% net investment income tax only applies to passive income. The effective date for this provision in the House bill is January 1, 2022;
- **No change to the very important 20% qualified business income deduction under 199A for pass-through entities.** Though the 199A deduction is still set to sunset at the end of 2025;
- **A number of new IRA provisions for taxpayers most applicable to those who have accumulated more than \$10,000,000 in retirement plan assets.**
 - No new IRA contributions allowed for those who have \$10,000,000 or more in retirement plan accounts, but only for “applicable taxpayers” those making more than \$400,000 filing single or \$450,000 filing jointly. This provision is effective as of January 1, 2029.
 - For applicable taxpayers who have retirement plan accounts valued in the aggregate at more than \$10,000,000, there will be a new Required Minimum Distribution (RMD) requiring a withdrawal equal to 50% of the value over the \$10,000,000 limit. This provision is effective as of January 1, 2029.
 - In addition, applicable taxpayers who have aggregate retirement plan accounts over \$20,000,000 must draw down 100% of any Roth accounts to bring the value down to \$20,000,000. This provision is effective as of January 1, 2029.
 - No after-tax Roth conversions after 2021 (same as the initial proposal). This change affects very few taxpayers who own or are employed by small businesses.
 - No Roth conversion for applicable taxpayers after 2031 (same as the initial proposal). This represents a significant change which is ameliorated by the 10 year delay in the effective date. It is deemed to be a revenue raiser because it will incentivize applicable taxpayers to do a Roth conversion before 2031. When a taxpayer converts all or a portion of a traditional IRA to a Roth IRA, income tax on the entire amount converted is due.
 - One IRA provision from an earlier version of BBB is out – IRAs can continue to invest in private equity. The original version of BBB included prohibitions against IRAs being invested in assets for accredited investors which have been eliminated;
- **Changes to 1202 stock so that there is a retroactive reduction of the 100% or 75% benefit to 50% for individuals with AGI of \$400,000 or more and all non-grantor trusts and estates.** Only change from the original version of the BBB was to clarify the effective date is “after September 13, 2021.”
- **A change to the SALT (state and local taxes) deduction limit increasing it up to \$80,000 until 2031 at which point the deduction would go back permanently to the \$10,000 limitation** brought in by the Trump tax bill. This is a revenue raiser since under the current law, the \$10,000 limitation is set to sunset at the end of 2025 and would revert to prior law with an unlimited SALT deduction as of 2026;
- **No required reporting of banking transactions to IRS;**

Now the action moves to the Senate. It's too soon to judge what the Senate version will look like or even when it will be brought up, however it seems unlikely that any other negative tax provisions will come in, particularly with Senator Manchin having the deciding vote. Senator Bernie Sanders (I-VT) may have a lot to say but the Senators who will be most important are Joe Manchin (D-WV) and Kyrsten Sinema (D-AZ). Based on Senator Manchin's comments, it is possible he will require some of the new social programs in the House passed version of the BBB be pared back or eliminated which will reduce the cost of the bill. He has specifically mentioned having concerns with the paid leave program in the bill, as well as expanding Medicare, creating a methane emission fee and having a larger tax credit for union-made electric vehicles. Senator Sanders, among other things, wants to expand the House version which expanded Medicare to cover hearing, to also include coverage for vision and dental. This will only happen if Senator Manchin is okay with it, which is doubtful. He has already expressed concern that the country cannot pay for Medicare as it stands today let alone afford to expand it. It is also possible that the Senate will cut back the House's SALT provision so the deduction is only available to those taxpayers who are below the \$400,000 filing single and \$450,000 filing jointly income thresholds or some higher threshold. If the Senate did entirely throw out any changes to the SALT deduction, it is quite possible that it would be brought back in conference as the deduction was the critical factor in wooing the votes of a number of House Democrats from high tax states.

Senator Manchin does not seem to be in any rush to do anything that would position Senate Leadership to bring the bill up until at least the end of the year because of his concerns with parts of the bill, inflation, and the Senate's busy schedule, including raising the debt ceiling and getting a defense bill through. If Senator Manchin sticks with this approach, then the conference likely would be in the spring. It is even possible that the Democrats in the Senate will fail to pass the bill. The SBLC anticipates that the Senate will ultimately pass a BBB bill but it will be a skinnier version than the House bill.

You may have noticed that for months Speaker of the House, Nancy Pelosi (D-CA) was trying to get a bill passed in the House that would be able to get through the Senate unchanged. When it became apparent that to get the infrastructure bill through the House, the BBB bill would have to be decoupled from a version acceptable to the Senate, Speaker Pelosi freed the Representatives to pass the version they wanted. The House Democrats know this version will not get through the Senate and basically the House will have to adopt whatever comes out of conference.

It took a lot of work for a number of associations to get rid of the most damaging tax provisions (many of which would have hit upper middle class taxpayers as well as small business owners). For its part, the SBLC was one of the first groups to respond to initial proposals to eliminate the step-up in basis and reduce the estate tax exemption which started to crop up a few years back by starting to educate folks on the Hill as well as the other small business associations as to the damage these provisions could wreak. We also were one of a handful of associations to lead the charge against the potential harmful limitation of the 199A deduction. We also worked with many other associations, including SBLC member, Independent Community Bankers of America, to oppose and eliminate provisions that would have required reporting of numerous banking transactions to IRS.

As of now, BBB went from a bill with many potentially disastrous tax provisions for small businesses to one whose major tax provisions are aimed squarely at the ultra-wealthy. It's probably too early for privately owned and family-owned businesses to breathe a sigh of relief but we'll know soon enough whether they can.

Paula Calimafde
calimafd@paleyrothman.com
301 951-9325

Jessica Summers
jsummers@paleyrothman.com
301 968-3402