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Biden Administration Releases Budget and Green Book, Providing Details on Corporate and Individual Tax Proposals that Would Have Significant Impact on Private Equity Industry

02 June 2021

On May 28, 2021, the Biden administration released its fiscal year 2022 budget proposal, which includes two major legislative plans previously released by the administration, the American Jobs Plan (focused on corporate tax reform) and the American Families Plan (focused on individual tax reform). On the same day, the Treasury Department released its highly anticipated "Green Book," which provides additional detail around the administration's tax proposals.

The tax proposals in the two plans would have far-reaching effects on private equity sponsors, their principals and their portfolio companies. We highlight below what we view as the most significant proposals. Generally, these proposals have prospective effective dates, though the proposal to tax capital gains and qualified dividends at ordinary income rates is proposed to be effective for gains recognized "after the date of announcement" (presumably either April 28, 2021, the date the Biden administration released the American Families Plan, or May 28, 2021).

We note that the Biden administration's budget is only the first step in the legislative process, and it would not be surprising if there were significant changes made to these proposals as the process plays out on in the coming months.

A more detailed description of the proposals is available in the accompanying Kirkland *Alert*, which you can access by clicking here.

Individual Tax Increases

- Increase the top ordinary income tax rate to 39.6% from 37%.
- Tax capital gain and qualified dividends at ordinary income rates for taxpayers with incomes over $1 million (but only to the extent the taxpayer's income exceeds $1 million).
- Tax carried interest (including current income allocations as well as gain on sale of a partnership interest) as ordinary income subject to self-employment tax for taxpayers whose income (from all sources) exceeds $400,000.
- Impose self-employment tax on the distributive shares of limited partners, LLC members and S corporation owners who materially participate in their businesses and whose income generally exceeds $400,000, subject to current exclusions for certain types of income such as dividends and capital gains.
- Limit gain deferral on "like-kind exchanges" of real property to an aggregate amount of $500,000 per year, per taxpayer ($1 million for married individuals filing jointly).
- Make permanent the limitation on deductibility by non-corporate taxpayers of net excess business losses (non-passive business losses) above a certain threshold.
- End non-taxable stepped-up basis at death for appreciated assets, subject to certain exceptions (such as transfers to charities).
- Treat the donor of an appreciated asset as realizing capital gain on date of gift, subject to certain exceptions (such as transfers to charities).

Corporate Tax Increases

- Increase the corporate tax rate to 28% from 21%.
- Impose a new 15% minimum tax on book income of large corporations with worldwide pre-tax book income of at least $2 billion.
- Revise the global minimum tax regime by increasing the tax on so-called "GILTI" income of non-U.S. subsidiaries from 10.5% to 21%, eliminating the exemption for a 10% return on foreign tangible assets and calculating a U.S. shareholder's minimum tax (and foreign tax credit limitation) on a jurisdiction-by-jurisdiction basis.
- Replace the BEAT (a corporate minimum tax focused on "base-eroding" payments) with "stopping harmful inversions and ending low-tax developments" (SHIELD), a

deduction disallowance regime that would disallow deductions for certain payments to low-tax members of the same financial reporting group.
- Tighten existing anti-inversion rules by expanding the circumstances in which a non-U.S. acquiror of a U.S. business is treated as a U.S. corporation.
- Repeal the FDII deduction, which currently provides a reduced tax rate for certain export income.
- Restrict deductions of "excessive" interest of members of financial reporting groups for "disproportionate borrowing" in the U.S.
- Restrict the deduction of expenses related to "offshoring jobs" and provide a new general business credit to support "onshoring."

Repeal of Certain Oil and Gas Tax Benefits

- Repeal several tax credits, deductions and other special provisions targeted to benefit oil, gas and coal producers, and their equity owners.
- In particular, eliminate the election to expense intangible drilling costs (IDCs), remove the passive loss limitation exception for losses on working interests and repeal ability to take percentage depletion.
- Treat income from activities relating to fossil fuels as non-qualifying income for publicly traded partnerships, beginning after 2026.

Clean Energy Incentives

- Allow taxpayers to make an election to receive a cash payment in lieu of the existing renewable energy tax credits and many other related tax credits.
- Restore the full production tax credit and investment tax credit for wind, solar and certain other qualified facilities and add an investment tax credit for stand-alone energy storage, in each case, that begin construction by the end of 2026, with a 20% phasedown each year thereafter.
- Extend the beginning of construction deadline for carbon sequestration credit eligibility to January 1, 2031, and provide an enhanced credit for certain technologies, including direct air capture.
- Extend, increase and create tax credits for various other clean energy initiatives.

Housing and Infrastructure Support

- Expand low-income housing tax credits through a new program allocating housing credit dollars to projects in "Census Tracts of Opportunity" and an increase to the existing subsidies for difficult development area projects.
- Make permanent the New Markets Tax Credit, currently scheduled to expire in 2025.
- Create new qualified School Infrastructure Bonds and expand transportation private activity bonds to allow for additional federally subsidized financing for infrastructure projects.

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