US Office of Public Policy

Special Washington Update

Biden and Tax Policy

20 July 2020

Former Vice President Joe Biden has secured enough delegates for the Democratic nomination for President of the United States. He is poised to accept the nomination at the Democratic National Convention in August and face off against President Trump in November.

Biden and congressional Democrats have a long list of policy priorities they will be looking to advance if they win in November. That list includes major changes to tax law. Democrats in the House and Senate unanimously opposed the 2017 tax law supported by President Trump, which reduced taxes for businesses and individuals in all tax brackets. They opposed the law for a variety of reasons, but their primary argument was that it provided large and unfunded tax cuts for wealthier taxpayers and corporations. It is unlikely that Democrats would repeal that entire law, but they certainly would try to rewrite many of its major components.

What can we expect from a Biden presidency on tax policy? Vice President Biden has laid out several components of a broad tax plan, and we highlight a few below. We focus on investment-related tax provisions in this publication.

If Biden is elected president, we believe the House and Senate also likely would be controlled by Democrats. However, any Democratic majority in the Senate would be small, perhaps only an advantage of a seat or two. A majority of 50, 51 or 52 would make it difficult for Democrats to pass their legislative priorities given that current Senate rules require a super majority of 60 votes to advance most legislation (60 votes are needed to end debate and overcome a filibuster). However, tax changes can be advanced through an alternative process called "budget reconciliation," which allows a measure to pass the Senate with a simple majority under certain limited circumstances. Notably, this process was used by Republicans to pass the 2017 tax law (and by Democrats to pass the Affordable Care Act in 2010).

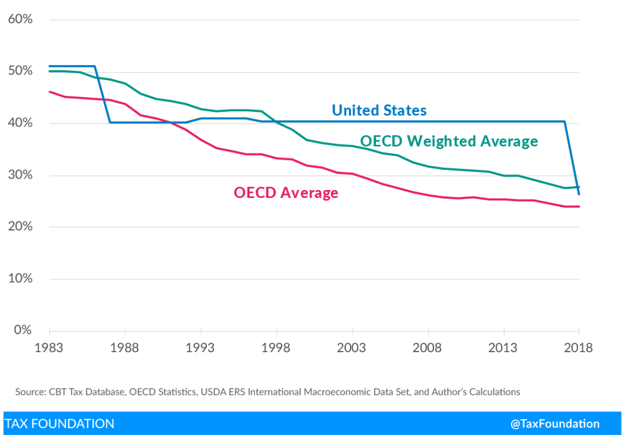
A more drastic move would be simply eliminating the 60-vote requirement for legislation and effectively striking down the filibuster practice entirely. Only a majority is needed to change Senate rules, but the filibuster has been a longstanding and defining feature of the Senate, even as it has been scaled back over the years. While the 60 vote requirement dates back to 1975 (it previously was a two-thirds threshold), the Senate in more recent years (under both Democratic and Republican majorities) have taken steps to eliminate the 60 vote requirement for nominations. Democrats could take a quantum leap and eliminate it for legislation as well, but that would be a risky and controversial move. Such a move likely would be opposed by a few moderate Democrats and be considered a last resort, particularly given that tax and certain budget changes can be advanced through the aforementioned reconciliation process.

A Biden win also would usher in a new Treasury Secretary that will take a very different approach than that of current Secretary Steve Mnuchin. In particular, a Biden administration would issue and implement much tougher regulations that would focus on wealthier taxpayers and corporations. For example, the Trump administration is rolling back the Obama administration's regulations targeting inversions, which involve companies moving their headquarters overseas for tax purposes. These rules, which had an impact on a wide range of companies, may be one of many areas that a Biden administration would seek to take a different tact than the Trump administration and Treasury Secretary Mnuchin.

Corporate Tax Rates. The 2017 tax law lowered the corporate tax rate to 21%, down from 35%. Biden's plan would increase the corporate tax rate to 28%. Biden has also embraced a new minimum tax in the form of requiring certain corporations to pay at least 15% tax on their reported "book income." If Democrats win control of the White House, House and Senate, an increase in corporate taxes will be low hanging fruit.

A rate of 28% is the likely target, however that may change depending on a number of factors, including the amount of revenue needed to fund Democratic spending priorities and the makeup of the House and Senate (moderates vs. more progressive members). As such, it could be higher or lower than that 28% level. *A tax increase on corporations is a strong likelihood under Democratic control.*

Top Corporate Income Tax Rate, United States vs. OECD, 1983 – 2018



Income Tax Rates. Biden and congressional Democrats uniformly agree that the 2017 tax cut for top earners should be reversed. Democrats would keep most of the income tax brackets intact but would seek an increase in the top income tax bracket back to 39.6% (up from 37%). *This too is low hanging fruit and will be a cornerstone to any Biden tax plan.*

2020 Tax Brackets and Rates

Rate	For Single Individuals, Taxable Income Over	For Married Individuals Filing Joint Returns, Taxable Income Over	For Heads of Households, Taxable Income Over
10%	$0	$0	$0
12%	$9,875	$19,750	$14,100
22%	$40,125	$80,250	$53,700
24%	$85,525	$171,050	$85,500
32%	$163,300	$326,600	$163,300
35%	$207,350	$414,700	$207,350
37%	$518,400	$622,050	$518,400

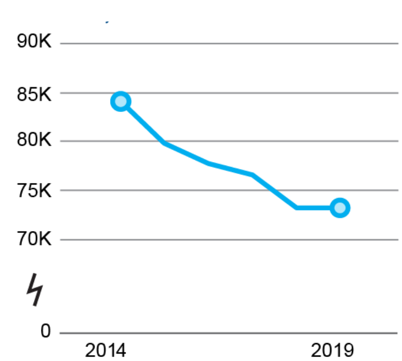
Source: Internal Revenue Service.

Investment Taxes. Biden has adopted the apparent orthodoxy in the Democratic Party that capital gains (and dividends) for the wealthy should be taxed as ordinary income. As noted, ordinary income tax rates under Democratic control could increase to 39.6%. That would mean that capital gains and dividend tax could almost double from 20% to 39.6% for investors in the top tax bracket. This of course does not account for the 3.8% net investment tax, which will remain in place and could even be increased. Additionally, Senator Ron Wyden (D-OR) is the lead Democrat on the Senate Finance Committee, and he is pursuing a plan known as "mark to market" that would annually tax unrealized capital gains on high-income earners. *Under a Biden win scenario, there is a good chance that taxes on investment will rise significantly for certain Americans.*

International Tax. This is a sleeper issue that needs to be taken seriously by international corporations and those investing in them. The 2017 tax law devised a new mechanism to tax corporations with international revenue and profits. US companies are now subject to the Global Intangible Low Tax Income (GILTI) regime that acts as a minimum tax with a 10.5% tax rate. Biden has proposed doubling the GILTI to 21%. Many Democrats who are influential on tax issues also support increasing the GILTI tax. This may be one of the more impactful changes to corporate taxes. *Investors need to appreciate what impact this policy would have on their investments.*

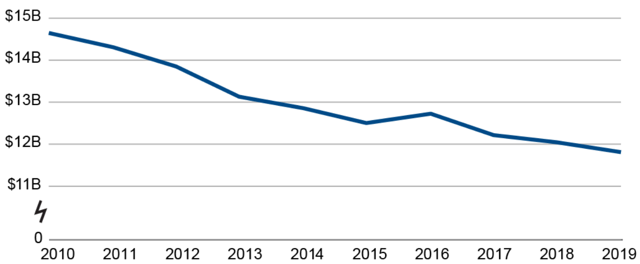
IRS Enforcement. The IRS's enforcement budget fell from $5.5 billion in 2010 to $4.7 billion in 2018. The agency's workforce in 2018 was 22 percent smaller than in 2010, and its enforcement staff was down by about one-third. This has led to fewer enforcement actions (audits). In 2018, the IRS audited 0.5 percent of the 196 million tax returns filed. This was down 10 percent from the previous year, with the drop in the audit rate of upper-income earners being particularly pronounced. *Democrats will push for more funding for the IRS to focus on enforcement, especially on those in higher income brackets.*

Full-time Equivalent Positions Realized, Fiscal Years 2014 – 2019



SOURCE: *IRS Data Book* Table 32

Operatings Costs (Constant 2019 Dollars), Fiscal Years 2010 – 2019

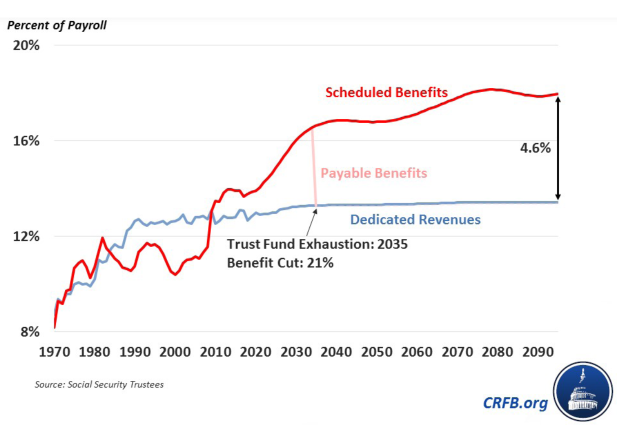


NOTE: Inflation-adjusted amounts were calculated using the U.S. Bureau of Economic Analysis, Nondefense Gross Domestic Product Chain-type Price Index with a 2019 base year.
SOURCE: *IRS Data Book* Table 31

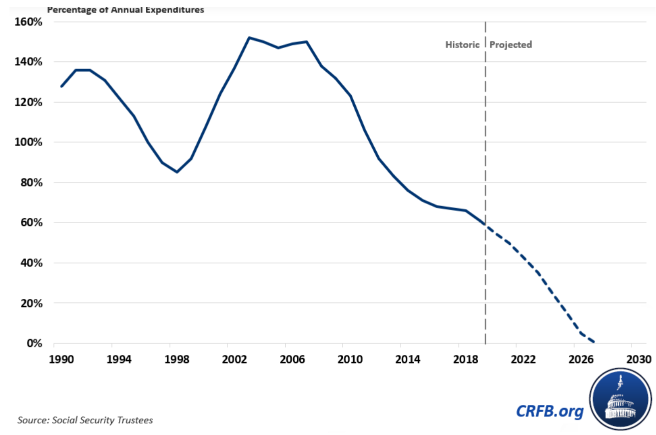
Estate Tax. Congressional Democrats almost uniformly believe that the estate tax should revert back to the pre-2017 tax law exemption level of $3.5 million. Biden has been silent on this policy. Perhaps more notable is Biden's support for a change in the tax treatment for "step-up basis." Currently, capital gains on an inherited investment are based on its value at the time it was inherited (not its value when the original investment was made). Biden would like to change this to when that asset was originally acquired, which would lead to a much larger tax being paid. Such a change would have a potentially significant impact on estate planning. *If Biden and Democrats win in November, there is a good chance that changes will be made to estate taxes.*

Payroll Taxes (Social Security). It is no secret that both Social Security and Medicare are facing insolvency in the coming years. Biden has proposed lifting the cap on Social Security payroll taxes for those earning wages over $400,000. While we believe an increase in taxes will be part of the eventual solution to save Social Security, such a change is not likely until we get much closer to insolvency, which is 2035 for Social Security and 2026 for Medicare. Keep in mind that these dates may move up due to lower revenues due to the economic impact of COVID-19. *With that said, we don't believe there will be movement on taxes in 2021 or 2022.*

Social Security Revenue and Benefits in Trustees Report



Medicare Hospital Insurance Trust Fund Ratio



Wealth Tax. During the presidential primary election, several Democratic presidential candidates such as Senators Elizabeth Warren (D-MA) and Bernie Sanders (I-VT) proposed a wealth tax. Under such a plan, a tax would be imposed on the wealthy based on assets, not income. Biden and many Democrats have not embraced these proposals. At the end of the day, a tax on assets like individual retirement savings (not income) makes Republicans and many Democrats uneasy. *Despite the likely focus on it, we do not envision a wealth tax being instituted if Biden is elected president.*

"Wall Street" Tax. Pitting Wall Street versus Main Street makes for good politics and will be a theme this fall during the campaign. Several Democratic presidential candidates (but not Joe Biden) proposed a financial transaction tax (FTT) that would tax trades of financial instruments (stocks, bonds and derivatives). While there are several versions of this proposal, the most prominent has been estimated to raise almost $800 billion. A recent study suggested that a FTT of 0.1% would cause individuals to work two and half years longer, as it would result in a 19% decline in retirement savings over a 20-year investment. *While this tax has support from the left wing of the Democratic Party, many moderate Democrats oppose such a proposal, making it unlikely that a FTT would gain traction and be implemented.*

The above tax issues are only a few of those that would be debated in a Biden-era tax plan, but they are those that would be most impactful to investors. We will assess other provisions later as they become more relevant. If you have any questions, please contact Shane Lieberman (*shane.lieberman@ubs.com*).