House Ways & Means Committee releases draft tax proposals

15 September 2021

Summary

The U.S. House Ways & Means Committee has released its **draft tax proposals** on 13 September 2021, which is intended to provide the funding for President Joe Biden's USD 3.5 trillion budget reconciliation bill. These are subject to future markups and the final tax proposals are likely to be voted upon by the House Leadership, tentatively by 27 September 2021.

Some of the key corporate tax and personal tax proposals are highlighted in this alert.

Corporate tax proposals

Corporate tax rates

Graduated tax rates have been reintroduced with the peak federal corporate tax rate of 26.5%. The graduated tax slabs are below:

- 18% - Income up to USD 400,0000.
- 21% - Income between USD 400,000 to USD 5,000,000.
- 26.5% - Income exceeding USD 5,000,000.
- Personal service corporations are not eligible for the graduated rates and will be subject to a flat 26.5% rate.
- Changes to the corporate tax rate are proposed to be effective for taxable years beginning after 31 December 2021.
- Fiscal year taxpayers will need to pro-rate their tax rates depending on their tax year end.

Limitations on interest payments

- Certain domestic corporations which are part of an International Financial Reporting Group will have limitations on its interest deductions if the corporation's net interest expense is disproportionate to the share of the corporation's earnings before interest, taxes, depreciation, and amortisation (EBITDA) as compared to the Group's EBITDA.

Global Intangible Low Taxed Income (GILTI)/Foreign Derived Intangible Income (FDII)

- Section 250 deduction reduced with respect to both FDII (to 21.875%) and GILTI (to 37.5%).
- In combination with the proposed 26.5% corporate rate, this works out to an effective 16.5625% GILTI rate and a 20.7% FDII rate.

- GILTI inclusions would be computed on a country-by-country basis and carryovers of tested losses would be permitted.
- Foreign tax credit on GILTI inclusions to be increased from 80% to 95%.
- Qualified Business Asset Investment (QBAI) threshold would be reduced from 10% to 5%.

Base Erosion and Anti-Abuse Tax (BEAT)

- BEAT rates would be applicable as below

Taxable years	Rate
Beginning after 31 December 2021 and before 1 January 2024	**10%**
Beginning after 31 December 2023 and before 1 January 2026	**12.5%**
Beginning after 31 December 2025	**15%**

- Base erosion minimum tax amount is to be determined taking into account tax credits.
- Exception for payments subject to U.S. tax and for payments to foreign parties if the taxpayer establishes that such amount was subject to an effective rate of foreign tax not less than the applicable BEAT rate.
- Exception for taxpayers with low base erosion percentage threshold would only apply to taxable years beginning before 1 January 2024.

Individual tax proposals

Tax rates

- Top marginal rate to increase to 39.6% from the existing 37% and will apply above the following income thresholds for taxpayers:

Category of taxpayer	Income threshold
Single	Income exceeding USD 400,000
Married filing jointly	Income exceeding USD 450,000
Married filing separately	Income exceeding USD 250,000

- 3% surcharge introduced on taxpayers with a modified adjusted gross income exceeding USD 5 million (or USD 2.5 million for married individuals filing separately).
- Net Investment Income Tax (NIIT) scope expanded to cover trade or business income of certain high-income individuals with greater than USD 400,000 in taxable income (single) or USD 500,000 (joint filer).

Capital gains tax

- The peak capital gains rate to increase to 25% from the existing 20% with effect from 13 September 2021 (except for certain binding contracts in effect on such date which may be subject to the old rates)

- For top bracket taxpayers – the effective capital gains rate works out to 31.8% (after including 3.8% NIIT and 3% surcharge)

Estate taxes

- Estate and gift tax lifetime exemption to revert to the erstwhile limit of USD 5 million per individual (indexed for inflation) from the current inflation adjusted USD 10 million per person (USD 11.7 million in 2021).
- The enhanced exemption limits were previously scheduled to revert back to their pre-TCJA[1] level on 1 January 2026.
- The proposed changes would be effective after 31 December 2021.

Individual Retirement Account (IRA)

- For certain high-income taxpayers, the proposed provisions prohibit contributions when the total balance of the contributor's IRAs and other retirement accounts exceeds USD 10 million (determined as of the close of the previous taxable year) and also require such taxpayers to take higher required minimum distributions from such accounts.

Carried Interest

- Holding period for long-term capital gain treatment for carried interest is proposed to be increased from three to five years with effect from taxable year beginning after 31 December 2021.
- The three-year holding period rule would be maintained for real property trades or businesses and taxpayers with adjusted gross income less than USD 400,000.

Qualified Business Income (QBI) deduction

- The maximum QBI deduction to be limited to

Category of taxpayer	Deduction limit
Joint filers	USD 500,000
Single filer	USD 400,000
Married filing separately	USD 250,000
Trust or estate	USD 10,000

The proposed effective date is for taxable years beginning after 31 December 2021.

Modifications to Section 1202 benefits

- Section 1202 provides up to 100% exclusion from capital gains arising from sale of Qualified Small Business Stock (QSBS).
- The new proposals seek to cap this exclusion at 50% for taxpayers with

[1] Tax Cuts and Jobs Acts, 2017

Adjusted Gross income (AGI) exceeding USD 400,000 as well as all estates and trusts.

- For taxpayers with AGI below USD 400,000, the 75% and 100% exclusions will still apply.

The proposed change would be effective from 13 September 2021 (except for certain binding contracts in effect on such date which may be subject to the previous provisions

Our comments

The proposals outlined by the House Ways & Means Committee are likely to undergo further mark-ups in the coming weeks as the Democrats craft the final tax bill that will be presented for a vote.

Some of the key tax rate increases, such as the corporate tax rate and capital gains tax rate are below the 28% (corporate tax) and 39.6% (capital gains tax) that President Biden had initially indicated.

Contact us

To know more, please visit **www.grantthornton.in** or contact any of our offices as mentioned below:

NEW DELHI
National Office
Outer Circle
L 41 Connaught Circus,
New Delhi 110 001
T +91 11 4278 7070

NEW DELHI
6th floor,
Worldmark 2, Aerocity,
New Delhi – 110 037
T +91 11 4952 7400

BENGALURU
5th Floor, 65/2, Block A,
Bagmane Tridib,
Bagmane Tech Park,
C V Raman Nagar,
Bengaluru – 560 093
T+91 80 4243 0700

CHANDIGARH
B-406A, 4th Floor, L&T
Elante office Building
Industrial area, Phase-I,
Chandigarh 160 002
T +91 172 4338 000

CHENNAI
7th Floor, Prestige
Polygon 471, Anna
Salai, Teynampet
Chennai - 600 018
T +91 44 4294 0000

DEHRADUN
Suite No 2211, 2nd Floor
Building 2000
Michigan Avenue, Doon
Express Business Park,
Subhash Nagar, Dehradun
248 002
T +91 135 264 6500

GURGAON
21st Floor DLF Square
Jacaranda Marg,
DLF Phase II,
Gurgaon 122 002
T +91 124 462 8000

HYDERABAD
7th Floor, Block III
White House Kundan
Bagh, Begumpet
Hyderabad 500 016
T +91 40 6630 8200

KOCHI
7th Floor, Modayil Centre
Point, Warriam Road
Junction, MG Road,
Kochi 682 016
T +91 484 406 4541

KOLKATA
10C Hungerford Street
5th Floor,
Kolkata 700 017
T +91 33 4050 8000

MUMBAI
11th Floor, Tower II
One International Centre
SB Marg, Prabhadevi (W)
Mumbai 400 013
T +91 22 6626 2600

MUMBAI
Kaledonia, 1st Floor,
C Wing (Opposite J&J
office) Sahar Road,
Andheri East,
Mumbai - 400 069
T +91 22 6176 7800

NOIDA
Plot No. 19A,
2nd Floor Sector – 16A,
Noida 201 301
T +91 120 4855 900

PUNE
3rd Floor,
Unit No 309 to 312, West
Wing, Nyati Unitree
Nagar Road, Yerwada
Pune- 411 006
T +91 20 6744 8800

For more information or for any queries, write to us at **contact@in.gt.com**

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