

[TAXES - The Tax Magazine \(2006 to Present\), THE KNIGHT WATCH—Tax Reform Update for High-Net-Worth Individuals, \(Nov. 20, 2024\)](#)

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“A tax loophole is something that benefits the other guy. If it benefits you, it is tax reform.”

– Russell B. Long

I. Introduction

With the impending 2024 Presidential election and the imminent sunset of many provisions of the law known as the Tax Cuts and Jobs Act of 2017 ^[1] (TCJA), it is important for high-net-worth (HNW) individuals and their advisors to understand what is at stake. The TCJA includes changes to the estate, gift, and generation-skipping tax (GST) taxes doubling the amounts taxpayers can transfer free of transfer tax. Understandably, many practitioners are advising clients to take advantage of these provisions while they still can but concerned about “crying wolf,” others are more circumspect in their advice. Helping clients reach the right decision requires a better understanding of how the TCJA came to be, what really has to happen in the 2024 election to “move the needle” on a so-far gridlocked government, and what positions each party is taking in the leadup to November.

II. The Political Landscape

A. The Legislative Process

Elections have consequences. Federal tax changes will depend on who controls the White House and Congress. Both parties are preparing for tax reform as if they will control both the White House and Congress. According to all of the reliable polling, neither party will have commanding control of the Senate to avoid a filibuster. The margins of control will likely be narrow, which will dictate the process for tax reform in 2025.

The Senate comprises 100 senators, and if 40 or more senators vote against a cloture motion to end a filibuster, then the legislation cannot move forward. For certain tax, spending, and debt limit legislation, though, there is a workaround—budget reconciliation. Created by the Congressional Budget Act of 1974, reconciliation is a special subset of legislation that affects spending, revenue, and the federal debt limit. ^[2] The filibuster does not apply to reconciliation bills and, under Senate rules, amendments—which, under normal circumstances, can be used to indefinitely stall a bill—are greatly limited. ^[3]

There are important limitations on reconciliation bills. First, the budget committees in both houses must set reconciliation instructions as part of the budget for the fiscal year. For example, the budget committees set a reconciliation instruction of \$1.5 trillion of deficit spending within the 10-year budget window for the TCJA. ^[4] Of course, the price of extension of the TCJA with no further modifications has increased to \$4.6 trillion over 10

years. ^[5] If all of the offsets are removed (e.g., the deduction for state and local taxes is fully restored), then the cost would exceed \$8 trillion over 10 years.

Congress may pass only up to three reconciliation bills, one on each of the permissible subjects of reconciliation: spending, revenue, and the debt limit. ^[6] In practice, though, there is typically only one per year. ^[7] The Byrd Rule—named for the late Senator Robert Byrd of West Virginia—imposes both a procedural advantage and substantive constraint for reconciliation bills. ^[8] Procedurally, the Byrd Rule streamlines the legislative process by precluding non-germane or “extraneous provisions” from being added to a reconciliation bill. ^[9] This becomes a substantive constraint because any provision that raises the deficit in any year after the 10-year window is considered “extraneous.” ^[10] Additionally, Congress is limited to the amount set in the reconciliation instruction. That limitation can force Congress to adopt additional offsets or create expirations within the budget window, as is evident in the TCJA. For example, the current deduction for research expenses expired for tax years beginning after Dec. 31, 2021. Instead, taxpayers are required to amortize research expenses over five years (domestic research) or 15 years (foreign research). Finally, any modifications to Social Security are extraneous.

The TCJA was structured as a reconciliation bill due to opposition from Senate Democrats—and, for that reason, many of its most impactful provisions are subject to a sunset clause after 10 years. ^[11] If one party controls the White House and Congress after the 2024 election, it is likely that the party will use reconciliation to pass tax legislation in 2025. For that reason, practitioners should consider the tax proposals advanced by each party in light of the opportunities and limitations inherent in the reconciliation process. Tax legislation is less certain in a divided government, and it is possible that the TCJA could expire. ^[12]

B. The 2024 Election

In 2024, 34 Senate seats and all 435 House seats are up for election. ^[13] Currently, Democrats control the Senate, even though they hold only 46 seats to the Republican party’s 49, due to the four Independent Senators who caucus with the Democratic party and Kamala Harris’s tie-breaking vote. ^[14] Meanwhile, Republicans control the House, with 219 seats held by Republicans, 213 seats held by Democrats, and three vacancies. ^[15]

Of the Senate seats up for election this year, 10 are held by Republicans and 19 are held by Democrats. ^[16]

Some sources predict that Republicans will gain control of the Senate, ^[17] while others state that it is too early to tell. ^[18] Further, as of the writing of this column, the House ^[19] and White House are tossups. ^[20] In any scenario, the 2024 election will be close and may take weeks to determine which party controls each part of government.

Functionally, the path forward for any tax legislation is narrow given these realities. As discussed in Section III, *infra*, if one party controls the government, then tax reform 2025 will look very different depending on who is in charge. If Democrats are in charge, then the focus will be on providing tax relief to the lower and middle classes by raising taxes from high-net proposals, which would be geared toward increasing revenue from HNW individuals and corporations. If Republicans control government, then a tax bill will likely lose revenue in the 10-year budget window. It is unclear whether the Republicans in the 119th Congress would make the same trade-offs as their predecessors. Most of the current members of the House Committee on Ways and Means were not on the committee (or even in Congress) during the drafting and passage of the TCJA. Further, the Republican party is more populist than it was in 2017. The Republicans in 2017 were focused on addressing the high corporate income tax rate and the lock-out effect of our worldwide tax system with deferral, which led to the creation of a quasi-territorial tax system, or global intangible low-taxed income.

III. Tax Changes

A. Overview of the TCJA

1. The TCJA and the Federal Deficit

The TCJA made several significant changes in the federal tax laws, including the following:

1. Lowered the corporate income tax rate from 35% to 21%;
2. Lowered most of the income tax bracket percentages and increased most of the income levels for each bracket; [\[21\]](#)
3. Eliminated the deduction of miscellaneous itemized expenses;
4. Created a deduction of up to 20% of qualified business income for owners of passthrough entities and sole proprietorships ([Code Sec. 199A](#)); and
5. Raised the estate and gift tax basic exclusion and the GST exemption to \$10,000,000, adjusted for inflation (currently \$13,610,000).

All of these changes are set to expire after Dec. 31, 2025, except for the lower corporate income tax rate, which is permanent. It was estimated that the TCJA would increase the deficit by almost \$1.5 trillion over a decade. [\[22\]](#) Of this \$1.5 trillion, only 8.3 billion (0.55%) is attributable to the double estate, gift, and GST tax exemption amount. [\[23\]](#) The largest portion (74.6%) of the estimated deficit increase is attributable to changes to the individual income tax. [\[24\]](#) To put those figures in perspective, consider them in the context of the country's overall "deficit spending." For example, the deficit in 2023 was \$1.7 trillion, [\[25\]](#) and according to the Joint Committee on Taxation (JCT), the projected deficit from the TCJA in 2023 was \$137.9 billion, [\[26\]](#) or roughly 8.11% of the U.S. deficit.

However, that was then and this is now. As discussed above, the cost of extension of the TCJA (including the built-in offsets) has ballooned from \$1.5 trillion to \$4.6 trillion, assuming no additional modifications to the current law.

It is projected that estate and gift tax revenue for 2026, the last year in which the federal government will collect estate and gift taxes under the TCJA, will be approximately \$28 billion, which is estimated to be 0.58% of the U.S.' projected total revenue. [\[27\]](#) In 2027, the first year in which the federal government will collect estate and gift taxes under the lower exemption, the projected estate and gift tax revenue is \$40 billion (0.78% of revenue). These figures highlight two key points. First, the rather stark mismatch between the revenue impact of the income tax provisions of the TCJA as compared to the transfer tax provisions. Second, the drastic impact of the TCJA on transfer tax revenue (a 43% increase following sunset).

Put another way, the TCJA has a marginal impact on an ocean of income tax revenue while it has a massive impact on a pond of transfer tax revenue. At the same time, for wealthy families, the TCJA's impact is reversed: the income tax benefits are marginal while the transfer tax benefits are massive. Understanding this dichotomy is central for practitioners looking to counsel clients about navigating the sunset clauses of the TCJA.

2. The TCJA and Family Offices

The TCJA also eliminated the deductibility of investment advisory fees under [Code Sec. 67\(g\)](#), by suspending all miscellaneous itemized deductions subject to the 2% adjusted gross income (AGI) floor from 2018 through 2025. This change spurred the rise of family offices, leveraging the *Lender Management LLC* [\[28\]](#) case, which allowed these expenses to be treated as ordinary business expenses under [Code Sec. 162](#). This approach provided a more favorable tax treatment by classifying the expenses as fully deductible business expenses rather than expenses for the production of income under [Code Sec. 212](#), which became non-deductible.

Even if the deductibility of investment advisory fees returns after the TCJA provisions sunset at the end of 2025, many HNW individuals would not be able to take advantage of the deduction because they likely will be subject to the Alternative Minimum Tax (AMT) regime. The AMT regime is a parallel tax system designed to ensure that high-income individuals pay a minimum level of tax by, among other measures, disallowing many deductions, including miscellaneous itemized deductions. The TCJA significantly increased the AMT exemption amounts and

phaseout thresholds, reducing the number of taxpayers affected by the regime. These changes, however, also are scheduled to sunset, reverting the AMT exemption amounts and phaseout thresholds to pre-2018 levels, thereby potentially subjecting more HNW individuals to the AMT regime once again.

As a result, even after the sunset of the TCJA provisions, the family office structure will remain highly relevant. This structure will continue to allow HNW individuals to treat investment advisory fees as ordinary business expenses under [Code Sec. 162](#), providing a valuable tax planning strategy that remains effective regardless of the AMT's impact.

Family offices also benefitted from [Code Sec. 199A](#), or the 20% deduction for qualified business income from a partnership. [Code Sec. 199A](#) was designed to mimic the reduction in the corporate income tax rate such that the combined rate of the corporate income tax and the second level of tax on dividends should be equivalent to the income tax rate on individuals who conduct their affairs in partnerships. [Code Sec. 199A](#) was expensive—the cost was \$414.5 billion over 10 years. It is possible Republicans will seek to make [Code Sec. 199A](#) permanent, which could require offsetting revenue raisers.

B. Additional Changes Discussed by Parties

1. Democrats

It is unclear how Democrats would modify the TCJA to reflect their priorities, as they were shut out of the process in 2017. As a presidential candidate, Vice President Harris's tax plan includes the following:

1. Increase the corporate income tax rate to 28%;
2. Increase the tax deduction to \$50,000 for new small business start-up costs;
3. Increase the long-term capital gains rate from 20% to 28%;
4. Increase the net investment income tax (NIIT) to reach 5% on income above \$400,000;
5. Minimum tax of 25% on top earners' income and unrealized capital gains (for individuals who have more than \$100 million in assets); and
6. Restore the top income tax rate to 39.6%.

Democrats would likely look to the Treasury's Green Book, the in-depth discussion of the tax provisions in the president's budget. The Treasury fiscal year 2025 budget proposals [\[29\]](#) include the following:

1. Reporting requirements for trusts administered in the United States;
2. Eliminate income tax basis step-up at death;
3. Require trusts to recognize capital gain every 90 years, including a look back to Jan. 1, 1940;
4. Eliminate lack of control and lack of marketability discounts for intrafamily transfers of closely held entities; and
5. Because the TCJA sunset will happen automatically, no action needs to be taken for the rollback of its changes to transfer tax and individual income tax.

The other proposed changes would, as a practical matter, require Democratic control of government. President Biden first proposed these changes in 2021, and they have failed to gain traction when Democrats controlled government. Vice President Harris has not released proposals regarding modifications to [Code Sec. 199A](#) or transfer taxes.

If Rep. Richard Neal (D-Mass.) becomes chairman of Ways and Means, he will likely start with the Build Back Act (BBA). [\[30\]](#) While the energy provisions and a few of the offsets became the core of the Inflation Reduction Act of 2022, most of the offsets are available. The following provisions from the BBA could potentially affect HNW individuals:

1. Application of NIIT to trade or business income of certain high-income individuals;
2. Limitations on excess business losses of noncorporate taxpayers made permanent, with a carryforward modification;

3. Surcharge on high-income individuals, estates, and trusts (initial surtax on AGI of 5% in excess of \$10 million and additional surtax of 3% on AGI in excess of \$25 million); and
4. Limitations on high-income taxpayers with large retirement account balances.

Senate Committee on Finance Chairman Ron Wyden (D-Ore.) recently held a hearing on the taxation of high-income and high-wealth taxpayers. ^[31] JCT prepared background materials for the hearing. ^[32] JCT publication notes that the distribution of [Code Sec. 199A](#) and the preferred capital gains rate is regressive. In other words, HNW taxpayers receive more of benefits. ^[33]

Based on the issues in the JCT publication, it is likely Chairman Ron Wyden (D-Ore.) will pursue the following issues in a unified government:

1. Broader scope of the NIIT;
2. Mark-to-market on accumulated assets of HNW individuals;
3. Limitations on private placement life insurance and annuity contracts;
4. Modifications to carried interest; and
5. Modifications to transfer taxes as they apply to trusts.

Chairman Wyden has a history of introducing legislation and announcements that would also affect HNW taxpayers. The Modernization of Derivatives Act of 2021 ^[34] would modify the tax treatment of derivatives to require mark-to-market treatment on an annual basis, and the character of gain or loss would be ordinary. In 2021, Chairman Wyden announced a new draft bill, the Wyden Pass-through Reform Discussion Draft, that would “remove optionality that is unnecessary for business ends and close certain tax loopholes that allow investors and corporations to pick and choose when to pay tax.” ^[35] According to news reports, the Wyden proposal would raise \$172 billion over 10 years. ^[36]

2. Republicans

Republican’s focus will be on improving the TCJA. Due to the cost, it will be challenging for a Republican-unified government to make the TCJA permanent. Reconciliation would also prevent Republicans from deficit spending outside of the budget window, which means significant offsets would be required to offset revenue losses after the 10th year.

Former President Trump proposed the following tax proposals as part of his campaign:

1. An additional cut to the corporate income tax rate from 21% to 20% potentially decreased to 15% for those corporations that produce in the United States;
2. A new 10% tariff on all imports to the United States (60% for imports from China);
3. Permanence of TCJA rates for individuals;
4. “End taxes” on tips for service workers and Social Security;
5. Reversal of state and local tax (SALT) deduction limitations;
6. Eliminate worldwide taxation for individuals; and
7. Elimination of Inflation Reduction Act (IRA) green energy provisions.

Former President Trump’s proposals would cost at least \$7.5 trillion over 10 years (and growing). ^[37]

The groundwork for tax reform is underway at Ways and Means. Chairman Jason Smith (R-Mo.) and Tax Subcommittee Chairman Mike Kelley (R-Pa.) created 10 tax teams, each tasked with a subject matter (e.g., U.S. Innovation, Main Street, and New Economy). These Republican-only teams are tasked with creating roundtables and site visits with stakeholders. To date, these tax teams held more than 90 events with the goal of obtaining tax proposals for legislation in 2025. ^[38] Stakeholders could submit written comments by Oct. 15, 2024. It is unclear how the tax teams will process the comments and whether they will be made public.

As noted above, the majority of Ways and Means members were not on Ways and Means in 2017, and the tax teams provided an opportunity for the members to gain an education regarding the TCJA.

Senate Finance Committee Republicans, led by Senator Mike Crapo (R-Idaho), are preparing for tax reform as well. Unlike their counterparts in the House, Senate Finance Republicans are meeting in private to determine what they would like to achieve in tax reform.

IV. Divided Government

Currently, both parties are planning as if they have control of Congress and the White House. But what happens in a divided government? Hopefully, the current status of the Tax Relief for American Workers and Families Act (TRAWFA) ^[39] is not a preview of things to come. TRAWFA is a compromise bill that would address some of the TCJA cliffs and expand the child tax credit. As of the writing of this column, the House passed the bill with overwhelming support, while Senate Republicans are filibustering the bill. TRAWFA is a small bill—under \$100 billion and fully offset. Nevertheless, the houses and the parties are not fully aligned on a compromise bill.

The issues and revenue at stake for 2025 are magnitudes greater than TRAWFA.

In a divided government, compromise will be required to avoid the TCJA cliffs. The extension of [Code Sec. 199A](#) and the transfer tax provisions will create deep divisions between the parties. It is hard to predict which party will have leverage in the negotiations, and divided government could delay tax reform, pushing it into 2026.

V. IRS Enforcement

The other side of the tax policy coin is enforcement by the IRS. Congressional budgeting impacts whether the IRS has funds to support robust enforcement. The IRS' budget was cut by 24% between 2010 and 2022. ^[40] For example, IRS budget cuts reduced the audit rate from 3.8% in 2010 to 0.1% in 2019. ^[41] Also, the IRS has been tasked with doing more, including involvement in healthcare, clean energy, and onshoring microchip manufacturing. These new assignments require additional resources.

In 2022, the IRA provided the IRS with an additional \$80 billion over the next decade. ^[42] The IRS has stated that it plans to use these additional funds, in part, to “increase scrutiny on high-income taxpayers” to “reverse the historic low audit rates.” ^[43] It was anticipated that this would increase estate and gift tax return audit rates, which in 2019 were 7% for estate tax returns and less than 1% for gift tax returns. ^[44]

However, House Republicans began advocating for cuts to IRS funding after retaking the House in 2022. In Jun. 2023, Congress and the Biden Administration cut the IRA funding by 27%. If Republicans have a unified government, it is likely they will advocate for cutting funding that supports enforcement, while supporting funding to improve taxpayer user experiences (*e.g.*, more employees for phone lines and improved IRS websites).

In contrast, Democrats were able to obtain revenue from the JCT, and it is likely they will continue to support innovation and additional enforcement resources if Democrats control the government.

VI. Conclusion

Due to the impending sunset of many provisions of the TCJA, significant tax changes proposed by both Presidential candidates, and the work underway at the tax-writing committees, the outcome of the 2024 election will have a major impact on the Internal Revenue Code. For those interested in engaging with Congress, now is the time to begin meeting with members and their staff. Buckle up, as tax reform in 2025 is going to be as wild as Mr. Toad's Wild Ride. ^[45]

Footnotes

- ¹ The Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018, Pub. L. 115–97 (2017).
- ² Congressional Budget and Impoundment of Control Act of 1974, Pub. L. No. 93-344, 88 Stat. 297.

- 3 2 USC §§ 641(d) and (e).
- 4 Congress considers revenue over a 10-year window. The Joint Committee on Taxation, the official revenue estimator for Congress, provides revenue estimates by year for 10 years, as well as totals for 5 and 10 years.
- 5 Congressional Budget Office, *Budgetary Outcomes Under Alternative Assumptions About Spending and Revenues* (May 2024). www.cbo.gov/publication/60271.
- 6 Richard Kogan & David Reich, *Introduction to Budget "Reconciliation"*, CTR. ON BUDGET & POL'Y PRIORITIES (May 6, 2022), www.cbpp.org/research/introduction-to-budget-reconciliation.
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- 8 See generally CONG. RSCH. SERV., *THE BUDGET RECONCILIATION PROCESS: THE SENATE'S "BYRD RULE"* (2022), sgp.fas.org/crs/misc/RL30862.pdf.
- 9 2 USC § 644. Under the rule, a provision is extraneous if it does not change the level of spending or revenue (or if that change is "merely incidental"). 2 USC § 644(b)(1)(A).
- 10 *Id.* The ten-year window is due to that being the current budget window. Naomi Jagoda, *Rift Opens in GOP Over Budget Strategy*, THE HILL (Jun. 28, 2017, 6:00 A.M.), thehill.com/policy/finance/339767-rift-opens-in-gop-over-budget-strategy. Any Senator can object to an extraneous provision. The Senate parliamentary rules whether a provision in a bill violates the Byrd rule, and if it does, she determines how the provision is struck from the bill. See Congressional Research Service, *The Budget Reconciliation Process: The Senate's "Byrd Rule"*, crsreports.congress.gov/product/pdf/RL/RL30862 (updated Sep. 28, 2022).
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