Build Back Better Act: Details & Analysis of the $3.5 Trillion Budget Reconciliation Bill

Democratic lawmakers on the House Ways and Means Committee have advanced legislation containing the tax elements of President Biden's Build Back Better agenda. The draft legislation could be modified by the House Rules Committee before moving to the House floor and may differ from what Senators are preparing. This analysis contains estimates of the tax legislation as introduced by the House Ways and Means Committee.

Using the Tax Foundation General Equilibrium Model, we estimate that the House Ways and Means proposals would increase federal revenues by about $2.1 trillion over the next decade, before accounting for $1 trillion in expanded tax credits for individuals and businesses, resulting in a net revenue increase of about $1.06 trillion. Excluding tax revenue from increased tax compliance, the proposals would raise $862 billion over ten years.

We estimate that the Ways and Means tax proposals would reduce long-run economic output by 0.98 percent and eliminate 303,000 full-time equivalent jobs in the United States. It would also reduce after-tax incomes for the top 80 percent of taxpayers over the long-run.

TABLE 1.

Combined Long-Run Effects of Changes Under House Ways & Means Tax Proposals

Long-run Gross Domestic Product (GDP)	-0.98%
Long-run Gross National Product (GNP)	-1.01%
Capital Stock	-1.84%
Wage Rate	-0.68%
Full-Time Equivalent Jobs	-303,000

Source: Tax Foundation General Equilibrium Model, September 2021.

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Major Provisions

The House Ways and Means Committee draft legislation would include the following major changes:

Individual Income Taxes

- Raise the top individual income tax rate to 39.6 percent for single filers making above $400,000, for head of household filers above $425,000, and for joint filers above $450,000
- Create a 3 percent surcharge on modified gross adjusted income above $5 million
- Prohibit Individual Retirement Accounts (IRAs) contributions when balances reach $10 million and accelerate required minimum distributions for those accounts
- Extend the American Rescue Plan Act (ARPA) Child Tax Credit (CTC) expansion through 2025, and make the entire CTC fully refundable on a permanent basis
- Make permanent ARPA's temporary expansion of the Earned Income Tax Credit (EITC) eligibility, phase-in rates, and amount
- Make permanent ARPA's modifications to the Child and Dependent Care Tax Credit (CDCTC)

Capital Gains Taxes

- Increase the top capital gains tax rate from 20 percent to 25 percent, and adjust the top capital gains tax bracket to $400,000 for single filers, $425,000 for head of household filers, and $450,000 for joint filers
- Extend the holding period for carried interest from three years to five years

Estate and Gift Taxes

- Reduce the estate tax exemption beginning in 2022 (currently scheduled to occur in 2026) to $6,020,000, and make related changes to the unified estate tax credit

Pass-through Business Taxes

- Limit the maximum value of the Section 199A passthrough deduction to $500,000 for joint filers and $400,000 for single filers
- Expand the base of the 3.8 percent Net Investment Income Tax (NIIT) to apply to active business income for passthrough firms
- Make permanent the active pass-through loss limitation enacted in the 2017 Tax Cuts and Jobs Act (TCJA)

Corporate and International Taxes

- Return to a progressive corporate income tax rate structure with a top rate of 26.5 percent applying to corporate income above $5 million
- Reduce the deduction for Global Intangible Low-Taxed Income (GILTI) to 37.5 percent, resulting in a tax rate of 16.5 percent; calculate GILTI on a country-by-country basis; reduce the deduction for Qualified Business Asset Investment (QBAI) to 5 percent; reduce the Foreign Tax Credit haircut to 5 percent; allow loss carryforwards for five years and disallow loss carrybacks
- Reduce the deduction for Foreign-Derived Intangible Income (FDII) to 21.875 percent, resulting in a tax rate of 20.7 percent
- Create a new limitation on interest expense deductions for certain multinational corporations

Other Modeled Tax Proposals

- Delay the requirement to amortize research and development (R&D) expenses over five years, instead of taking immediate deductions, to begin after 2025 instead of after 2021
- Accelerate the expanded Section 162(m) limitation on business deductions for highly paid executive compensation to take effect in 2022 instead of 2026
- Increase federal excise taxes on tobacco and vapor products
- Modify, extend, and create a variety of tax credits for green energy, housing, rehabilitation, and other efforts primarily through 2031 or 2033
- Reinstate the Superfund tax on crude oil and imported petroleum at 16.4 cents per gallon (indexed to inflation), and double the reinstated Superfund tax on the sale of chemicals

Significant Proposals Not Modeled

- Extend or make permanent certain ARPA expansions of premium tax credits, including allowing higher-income households to qualify for the credits and boosting the subsidy for lower-income households
- Provide a payroll tax credit for childcare workers and a temporary tax credit for caregiver expenses
- Create a new limitation on foreign company base sales and services income
- Make tax changes targeted at cryptocurrency, including imposing rules related to common control and wash sales
- Make Modifications to the base erosion and anti-abuse tax (BEAT) for multinational corporations
- Change valuation rules for certain transfers of non-business assets

Economic Effects of the House Ways and Means Proposal

The House Ways and Means tax proposals raise tax rates on corporate and pass-through business income, reducing incentives to invest and lowering the long-run size of the economy. We estimate the tax proposals would reduce long-run GDP by 0.98 percent and long-run American incomes (as measured by gross national product, or GNP) by about 1 percent, while also reducing wages by 0.68 percent and eliminating 303,000 full-time equivalent jobs.

The proposed increase in the top corporate tax rate to 26.5 percent has the largest impact, reducing long-run GDP by 0.6 percent and eliminating 107,000 full-time equivalent jobs. Raising the top ordinary income tax rate to 39.6 percent and lowering the threshold for income subject to that rate reduces long-run GDP by 0.1 percent, while the pass-through business tax increases also reduce growth by about 0.1 percent.

The international tax increases imposed on U.S. multinationals (MNEs), including the new limit on interest expense, reduce long-run GDP and GNP by about 0.1 percent and eliminate 12,000 full-time equivalent jobs. There is an additional negative impact on GNP that we have not modeled (due to a lack of empirical studies) arising from the incentive for U.S. MNEs to avoid the higher GILTI taxes by selling foreign assets to foreign competitors not subject to the GILTI taxes.

While the increase in the long-term capital gains tax rate has a very small impact on GDP, it does reduce long-run American incomes as measured by GNP by 0.1 percent. This is because higher capital gains tax rates reduce the after-tax return to saving for U.S. residents, reducing U.S. saving, and increasing the share of U.S. investment financed by foreign savers, with the returns to that investment accruing to foreigners rather than U.S. residents.

For purposes of estimating the proposals' impact on federal budget deficits, interest payments, and resulting changes in GNP, we have assumed $3.5 trillion of spending over the period 2022-2031 inclusive of tax credits. In the years beyond 2031, we assume the proposals have no impact on deficits (to comply with the reconciliation process in the Senate).

We estimate that the higher deficits accumulated in the first decade result in a 0.1 percent reduction in long-run GNP, resulting from additional interest payments to foreign owners of the national debt. We also treat the $2.5 trillion in spending excluding the tax credits as transfer payments, with no associated impact on the economy in the long run.

TABLE 2.

Long-run Economic Effect of House Ways and Means Tax Proposals

Provision	Change in GDP	Change in GNP	Change in Capital Stock	Change in Wages	Change in Full-time Equivalent Jobs
Increase top ordinary rate to 39.6%and adjust the 39.6%bracket threshold downward	-0.1%	-0.1%	-0.1%	Less than -0.05%	-64,000
Increase the top tax rate on long-term capital gains and qualified dividends to 25% and lower the income threshold for the 25% bracket	Less than -0.05%	-0.1%	-0.1%	Less than -0.05%	-6,000
Apply the 3.8% net investment income tax to trade or business income over $400,000	-0.1%	-0.1%	-0.2%	-0.1%	-8,000
Make the active passthrough loss limitation permanent	-0.1%	-0.1%	-0.2%	-0.1%	-16,000
Apply a 3% surcharge on modified adjusted gross income over $5 million	Less than -0.05%	Less than -0.05%	Less than -0.05%	Less than -0.05%	-32,000
Limit IRAs with large balances	Less than -0.05%	Less than -0.05%	Less than -0.05%	Less than -0.05%	Less than 1,000
Require carried interest be held for five years to realize at qualified tax rates	Less than -0.05%	Less than -0.05%	Less than -0.05%	Less than -0.05%	-5,000
Make permanent refundability of the CTC and expansions to the EITC and the CDCTC	Less than -0.05%	Less than -0.05%	Less than -0.05%	Less than -0.05%	-15,000
Reinstate the federal Superfund program	Less than -0.05%	Less than -0.05%	Less than -0.05%	0%	-10,000
Increase tax on certain tobacco products and impose tax on nicotine	Less than -0.05%	Less than -0.05%	Less than -0.05%	0%	-21,000
Raise the top corporate tax rate to 26.5%	-0.6%	-0.5%	-1.1%	-0.5%	-107,000
Make changes to the international tax system, including raising the GILTI tax rate, tightening GILTI rules, and imposing a new limit on interest expense	-0.1%	-0.1%	-0.2%	-0.1%	-12,000
Tighten limits on deducting compensation for highly compensated employees under Section 162(m)	Less than -0.05%	Less than -0.05%	Less than -0.05%	Less than -0.05%	-9,000
Impact of budget deficit on American incomes	0%	-0.1%	0%	0%	0
Total Economic Effect	**-0.98%**	**-1.01%**	**-1.84%**	**-0.68%**	**-303,000**

Source: Tax Foundation General Equilibrium Model, September 2021. Items may not sum due to rounding.

Revenue Effects of the House Ways and Means Proposal

On a conventional basis, the House Ways and Means tax proposals would raise about $1.1 trillion in federal revenue from 2022 to 2031 net of tax credits. This includes about $2.1 trillion in gross revenue raisers, comprised of about $900 billion in corporate tax increases, $950 billon in individual tax increases, and $200 billion from additional IRS tax enforcement. This revenue is reduced by about $1 trillion in tax credits.

Our estimates include about $265 billion in provisions we did not score. For those provisions, we used estimates by the Joint Committee on Taxation (JCT) and the Congressional Budget Office (CBO), including the $200 billion in gross revenue from IRS tax enforcement.

On a dynamic basis (i.e., accounting for the reduced size of the economy resulting from the tax increases), the House Ways and Means tax proposals would raise about $804 billion in revenue net of tax credits.

The largest revenue raisers include raising the top corporate income tax rate to 26.5 percent, raising the top individual ordinary income tax rate to 39.6 percent while adjusting the top income tax bracket downward, raising taxes on passthrough firms by broadly applying the NIIT and extending current limits on deducting certain passthrough business losses, and applying a new 3 percent surcharge on incomes over $5 million. These changes make up about two-thirds of the conventional revenue raisers in the Ways and Means plan.

TABLE 3.

Conventional and Dynamic Revenue Effects of House Ways and Means Tax Proposals (billions of dollars)

Provision	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2022-2031
Individual Provisions											
Increase the top rate on the individual income tax to 39.6% on taxable income above $400,000/$450,000	$30.6	$32.3	$33.2	$35.0	$3.7	$4.1	$4.3	$4.5	$4.7	$4.9	$157.3
Increase the top tax rate on long-term capital gains and qualified dividends to 25% and lower the income thresholds	$6.1	$5.3	$6.8	$7.2	$7.8	$8.5	$8.6	$8.9	$9.2	$9.7	$78.1
Apply the 3.8% net investment income tax (NIIT) to trade or business income over $400,000 not currently subject to the NIIT	$14.5	$15.3	$15.9	$16.8	$17.1	$18.9	$19.8	$20.6	$21.5	$22.8	$183.2
Limitation on deduction for qualified business income (Section 199A) to $500,000 joint/$400,000 single	$18.3	$19.4	$20.2	$21.4	$-	$-	$-	$-	$-	$-	$79.4
Make the Active Passthrough Loss Limitation Permanent	$-	$-	$-	$-	$20.2	$21.0	$21.8	$22.7	$23.6	$24.5	$133.8
Apply a 3% surcharge on modified adjusted gross income over $5 million	$(1.8)	$5.8	$13.9	$14.4	$14.5	$15.7	$16.1	$16.8	$17.4	$18.4	$131.2
Accelerate the scheduled decrease in the estate tax exemption to 2022	$15.1	$15.9	$16.7	$17.5	$-	$-	$-	$-	$-	$-	$65.2
New limitations on high-income taxpayers with large retirement account balances and increasing minimum required distributions	$2.8	$3.3	$1.9	$0.8	$0.1	$(0.3)	$(0.8)	$(1.1)	$(1.1)	$(1.0)	$4.6
Require carried interest be held for five years for the income to be taxed at long-term capital gains tax rates	$1.6	$1.6	$1.6	$1.7	$1.4	$1.6	$1.6	$1.6	$1.7	$1.8	$16.1
Corporate Provisions											
Raise top corporate tax rate to 26.5 percent	$43.6	$46.1	$51.4	$56.3	$78.0	$80.8	$83.5	$85.7	$87.9	$90.2	$703.7
Impose new limitations on interest expenses for certain multinational corporations	$4.6	$4.7	$5.1	$5.5	$5.8	$6.0	$6.2	$6.3	$6.5	$6.7	$57.3
Increase global low-taxed intangible income (GILTI) tax rate, change the GILTI tax base and make changes to foreign tax credit (FTC) calculations	$11.9	$13.1	$12.7	$13.0	$2.9	$0.5	$0.2	$0.1	$0.1	$(0.0)	$54.5
Reduce the deduction value for foreign derived intangible income (FDII)	$6.5	$5.6	$6.0	$5.9	$(0.9)	$0.3	$0.3	$0.2	$0.2	$0.1	$24.2
Other Provisions											
Tighten limits on deducting compensation for highly compensated employees under Section 162(m)	$1.1	$1.4	$1.5	$1.7	$1.7	$1.7	$1.8	$1.8	$1.8	$1.9	$16.3
Delay Sec. 174 R&D amortization until 2025	$(21.8)	$(37.2)	$(34.1)	$(26.1)	$8.5	$33.3	$31.9	$22.4	$12.0	$6.0	$(5.2)
Increase tax on certain tobacco products and impose tax on nicotine	$7.2	$9.5	$9.6	$9.8	$9.9	$10.0	$10.2	$10.4	$10.6	$10.8	$97.9
Net Revenue from Unscored Items (JCT and CBO Estimates)	$35.0	$23.1	$18.5	$20.8	$25.6	$27.6	$28.1	$28.3	$29.0	$28.9	$264.7
Total Reveue Raisers	**$175.1**	**$165.2**	**$180.9**	**$201.6**	**$196.2**	**$229.7**	**$233.5**	**$229.5**	**$225.1**	**$225.8**	**$2,062.5**

TABLE 3.

Conventional and Dynamic Revenue Effects of House Ways and Means Tax Proposals (billions of dollars)

Provision	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2022-2031
Tax Credits											
Extend and modify American Rescue Plan expansion of the Child Tax Credit (CTC)	$(101.7)	$(104.2)	$(109.3)	$(113.9)	$(3.0)	$(2.8)	$(2.7)	$(2.6)	$(2.4)	$(2.3)	$(444.8)
Make Earned Income Tax Credit Expansion in the American Rescue Plan Permanent	$(12.0)	$(12.0)	$(12.1)	$(12.1)	$(15.0)	$(15.1)	$(15.2)	$(15.3)	$(15.4)	$(15.4)	$(139.7)
Make the Child and Dependent Care Tax Credit (CDCTC) Expansion in the American Rescue Plan Permanent	$(8.0)	$(8.3)	$(8.6)	$(9.0)	$(9.4)	$(9.8)	$(10.3)	$(10.7)	$(11.1)	$(11.5)	$(96.7)
Provide Tax Credits for Green Energy, Housing, Rehabilitation, and make permanent the New Markets Tax Credit. Reinstate the federal superfund program	$(8.5)	$(15.0)	$(20.9)	$(28.1)	$(33.8)	$(34.5)	$(39.6)	$(43.9)	$(46.7)	$(47.5)	$(318.5)
Total Tax Credits	**$(130.2)**	**$(139.5)**	**$(151.0)**	**$(163.1)**	**$(61.2)**	**$(62.3)**	**$(67.8)**	**$(72.4)**	**$(75.6)**	**$(76.7)**	**$(999.9)**
Total Conventional Revenue	**$44.9**	**$25.7**	**$29.9**	**$38.5**	**$135.0**	**$167.4**	**$165.6**	**$157.1**	**$149.5**	**$149.1**	**$1,062.6**
Total Dynamic Revenue	**$24.1**	**$2.9**	**$9.3**	**$19.4**	**$116.8**	**$143.8**	**$138.2**	**$125.8**	**$114.2**	**$109.3**	**$803.9**

Source: Tax Foundation General Equilibrium Model, September 2021. Items may not sum due to rounding.

Distributional Effect of Ways and Means Tax Proposals

The House Ways and Means tax proposals would increase the progressivity of the tax code by raising marginal income tax rates faced by higher earners and corporations while expanding several refundable tax credits for low- and middle-income earners.

The proposals would increase the after-tax income of the bottom quintile by about 14.5 percent in 2022 on a conventional basis, which is largely driven by the extended and expanded CTC, first introduced in the ARPA. By contrast, the top 1 percent of earners would experience a 5 percent drop in after-tax income in 2022.

TABLE 4.

Distributional Effect of House Ways and Means Tax Proposals (Percent Change in After-Tax Income)

Income Group	Conventional, 2022	Conventional, 2031	Dynamic, long-run
0% to 20%	14.5%	3.8%	2.6%
20% to 40%	4.2%	0.4%	-0.7%
40% to 60%	1.5%	-0.1%	-1.3%
60% to 80%	0.7%	-0.1%	-1.3%
80% to 90%	0.1%	-0.1%	-1.3%
90% to 95%	-0.2%	-0.2%	-1.4%
95% to 99%	-0.3%	-0.3%	-1.8%
99% to 100%	-5.0%	-2.5%	-4.7%
Total	**0.3%**	**-0.3%**	**-1.7%**

Note: This table omits the impact of additional spending on after-tax incomes.
Source: Tax Foundation General Equilibrium Model, September 2021.

After the expanded CTC expires in 2026, the bottom 40 percent of filers would see a smaller increase in after-tax incomes, reflecting the remaining expanded credits. The bottom quintile would experience a 3.8 percent increase in after-tax income by 2031 on a conventional basis. The top 60 percent of income earners would experience a drop in after-tax income due to higher individual and corporate taxes. The top 1 percent would see a 2.5 percent drop in after-tax income.

On a long-term dynamic basis, the smaller economy reduces after-tax incomes relative to the conventional analysis. The bottom quintile has higher after-tax income, but the top 80 percent of income earners would see their after-tax incomes drop, ranging from -1.3 percent for those in the middle quintile to -4.7 percent for the top 1 percent.

Modeling Notes

We use the Tax Foundation General Equilibrium Tax Model to estimate the impact of tax policies, including recent updates allowing a detailed modeling of U.S. multinational enterprises. The model produces conventional and dynamic revenue and distributional estimates of tax policy. Conventional estimates hold the size of the economy constant and attempt to estimate potential behavioral effects of tax policy. Dynamic revenue estimates consider both behavioral and macroeconomic effects of tax policy on revenue.

The model also produces estimates of how policies impact measures of economic performance such as GDP, GNP, wages, employment, the capital stock, investment, consumption, saving, and the trade deficit.