DESCRIPTION OF BUDGET RECONCILIATION LEGISLATIVE RECOMMENDATION RELATING TO REPEAL OF THE NET INVESTMENT INCOME TAX

Scheduled for Markup
by the
HOUSE COMMITTEE ON WAYS AND MEANS
on March 8, 2017

Prepared by the Staff
of the
JOINT COMMITTEE ON TAXATION

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INTRODUCTION

The House Committee on Ways and Means has scheduled a committee markup of a Budget Reconciliation Legislative Recommendation Relating to Repeal of the Net Investment Income Tax on March 8, 2017. This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a description of the legislative recommendation.

[1] This document may be cited as follows: Joint Committee on Taxation, *Description of Budget Reconciliation Legislative Recommendation Relating to Repeal of the Net Investment Income Tax* (JCX-12-17), March 7, 2017. This document can be found also on the Joint Committee on Taxation website at www.jct.gov. All section references herein are to the Internal Revenue Code of 1986, as amended, unless otherwise stated.

A. Repeal of Net Investment Income Tax

Present Law

In general

A tax is imposed with respect to the net investment income of certain high-income individuals, estates and trusts.[2] In the case of an individual, the tax is 3.8 percent of the lesser of net investment income or the excess of modified adjusted gross income over the threshold amount.

The threshold amount is $250,000 in the case of a joint return or surviving spouse, $125,000 in the case of a married individual filing a separate return, and $200,000 in any other case.

Modified adjusted gross income is adjusted gross income increased by the amount excluded from income as foreign earned income under section 911(a)(1) (net of the deductions and exclusions disallowed with respect to the foreign earned income).

In the case of an estate or trust, the tax is 3.8 percent of the lesser of undistributed net investment income or the excess of adjusted gross income (as defined in section 67(e)) over the dollar amount at which the highest income tax bracket applicable to an estate or trust begins.

The tax does not apply to a nonresident alien or to a trust all the unexpired interests in which are devoted to charitable purposes. The tax also does not apply to a trust that is exempt from tax under section 501 or a charitable remainder trust exempt from tax under section 664.

The tax is subject to the individual estimated tax provisions. The tax is not deductible in computing any tax imposed by subtitle A of the Internal Revenue Code (relating to income taxes).

Net investment income

Net investment income is investment income reduced by the deductions properly allocable to such income.

Investment income is the sum of (i) gross income from interest, dividends, annuities, royalties, and rents (other than income derived from any trade or business to which the tax does not apply), (ii) other gross income derived from any business to which the tax applies, and (iii) net gain (to the extent taken into account in computing taxable income) attributable to the disposition of property other than property held in a trade or business to which the tax does not apply.[3]

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[2] Sec. 1411.

[3] Gross income does not include items, such as interest on tax-exempt bonds, veterans' benefits, and excluded gain from the sale of a principal residence, which are excluded from gross income under the income tax.

In the case of a trade or business, the tax applies if the trade or business is a passive activity with respect to the taxpayer or the trade or business consists of trading financial instruments or commodities (as defined in section 475(e)(2)). The tax does not apply to other trades or businesses conducted by a sole proprietor, partnership, or S corporation.

In the case of the disposition of a partnership interest or stock in an S corporation, gain or loss is taken into account only to the extent gain or loss would be taken into account by the partner or shareholder if the entity had sold all its properties for fair market value immediately before the disposition. Thus, only net gain or loss attributable to property held by the entity which is not property attributable to an active trade or business is taken into account.[4]

Income, gain, or loss on working capital is not treated as derived from a trade or business. Investment income does not include distributions from a qualified retirement plan or amounts subject to SECA tax.

Description of Proposal

The proposal repeals the 3.8-percent tax on net investment income.

Effective Date

The proposal is effective for taxable years beginning after December 31, 2017.

[4] For this purpose, a business of trading financial instruments or commodities is not treated as an active trade or business.

B. Estimated Revenue Effect

Fiscal Years [Billions of Dollars]											
2017	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**	**2017-21**	**2017-26**
-1.5	-10.5	-7.5	-16.7	-17.8	-18.7	-19.7	-20.7	-21.7	-22.7	-54.1	-157.6

NOTE: Details do not add to totals due to rounding.