



DUNGEY DOUGHERTY PLLC

*Pending Federal Legislation on
Transfer and Wealth Taxes*

(As of November 9, 2021)

Pending Proposals

- **Build Back Better Act—H.R. 5376, Rules Committee Print 117-19 (New November 4, 2021)**
- **Build Back Better Act—H.R. 5376, Rules Committee Print 117-18 (Released November 3, 2021)**
- **Build Back Better Act—H.R. 5376, Rules Committee Print 117-17 (Released October 28, 2021)**
- **House Ways and Means Proposals (Released September 13, 2021)**
 - To Pay for the \$3.5 Trillion Build Back Better Plan
 - Incorporated into House Budget Reconciliation H.R. 5376, reported September 27, 2021
- **For the 99.5% Act**
 - Senators Sanders, Whitehouse, Gillibrand, Van Hollen, Reed, and Warren
 - Representative Gomez
- **American Housing and Economic Mobility Act of 2021**
 - Senators Warren, Markey, Gillibrand, Sanders, Hirono, and Merkley
 - Representatives Cleaver, Khanna, Garcia, Cohen, Shakowsky, Pressley, Moore, Bonamici, Lee, and Delegate Norton
- **The Ultra-Millionaire Tax Act of 2021**
 - Senators Warren, Markey, Gillibrand, Whitehouse, Schatz, Sanders, Merkley, and Hirono
 - Representatives Jayapal and Boyle
- **The STEP (Sensible Taxation and Equity Promotion) Act**
 - Senators Van Hollen, Booker, Sanders, Whitehouse, and Warren
 - Representative Pascrell
- **Biden Administration’s “The American Families Plan”**
- **The Biden Green Book (General Explanations of the Administration’s Revenue Proposals)**

	Build Back Better Oct. 28, 2021 <u>AND</u> Nov. 3/4, 2021	House Ways and Means Proposals Sept. 13, 2021	For the 99.5% Act	American Housing and Economic Mobility Act of 2021	The Ultra- Millionaire Tax Act of 2021	The STEP ACT	The American Families Plan	Biden Administration Greenbook
Reintroduction of prior proposal?	YES but with new ideas	YES but with new ideas	YES	YES	NO	YES but with new ideas	YES	YES but with new ideas
Pure revenue raiser or attached to spending project	Pay for \$1.75+ trillion Build Back Better Plan	Pay for \$3.5 trillion Build Back Better Plan	Only Revenue	Pay for housing legislation	Only Revenue	Only Revenue	Pay for education and childcare plan	Released at the same time as budget
All or part retroactive to January 1, 2021	Part	Part	NO	Part	NO	YES	Unknown	NO
Lowers exemption	NO	YES	YES	YES	NO	NO	NO	NO
Increases Estate/Gift/GST Rates	NO	NO	YES	YES	NO	NO	NO	NO
Limit Valuation Discounts	NO	YES	YES	NO	Allowed limitation through future regulations	NO	YES	YES (for income tax purposes only)
Elimination of perpetual GST exempt trusts	NO	NO	YES	YES	NO	NO	NO	NO (but income tax recognition every 90 years)
Changing rules related to GRATS	NO	NO (but grantor trust changes may eliminate)	YES	YES	NO	NO	NO	NO
Grantor trust includible for Gift and Estate Taxes	NO	YES	YES	YES	NO	NO	NO	NO
Impact on basis step up	NO	NO	NO	NO	NO	YES	YES	YES
Increased enforcement	YES	YES	NO	NO	YES	NO	YES	YES

Transfer Taxes
 Wealth Tax
 Income Taxes

Build Back Better Plan (October 28, 2021, November 3, 2021 November 4, 2021)

- **Increased Income Taxes Will Impact Fiduciary Income Taxes:** *effective for tax years beginning on or after December 31, 2021*
 - Surtax of 5% on modified adjusted gross income of a trust above \$200,000
 - Additional 3% surtax on modified adjusted gross income of a trust above \$500,000

Example for trust with \$1,000,000 in capital gain and \$100,000 of ordinary income:

	2021	2022 (assuming enactment and inflation adjustments)
Ordinary Income Tax	\$35,317.50	\$35,262.50
Capital Gain Tax	\$200,000	\$200,000
Net Investment Income Tax	\$41,288.90	\$41,288.90
Surtax	\$0	\$63,000
Total Tax Liability	\$276,606.40	\$339,551.40

Build Back Better Plan (October 28, 2021, November 3, 2021 November 4, 2021)

- **Qualified Small Business Stock (QSBS)**: *effective for sales and exchanges occurring after September 13, 2021, with binding contract exception*
 - Gain exclusion reduced to 50% of gain from 100% where taxpayer is a trust
- **State and Local Tax Deduction (New to November 4, 2021 version)**: Effective for tax years beginning in 2021, the \$10,000 SALT deduction cap is increased to \$80,000 for individuals who are single or married filing jointly and \$40,000 for estates, trusts, and married individuals filing separately.

Build Back Better: Observations

- **What Didn't Make it In:** Many of the revenue raisers from the House Ways and Means bill related to estate planning did not make it in:
 - No change in exemption amounts (included in the prior House Ways and Means legislative text)
 - No change to valuation discounts (included in the prior House Ways and Means legislative text)
 - No change to estate inclusion of grantor trusts (included in the prior House Ways and Means legislative text)
 - No change to the treatment of sales with grantor trusts (included in the prior House Ways and Means legislative text)
 - No new provisions affecting estate planning
- **Increase in Income Taxes Will Impact Fiduciary Income Taxes:**
 - Low thresholds for trusts and estates will cause the surtax to apply to many estates and trusts
 - Reduced benefit of QSBS, coupled with surtax, may impact non-grantor trust planning

House Ways and Means Proposals (September 13, 2021)

(To Pay for Build Back Better Plan)

- **Lower Exemption**: Estate and gift tax exemption reverts back to \$5 million (adjusted for inflation) in 2022, accelerating the sunset otherwise scheduled to occur in 2026
- **Valuation Discounts**: Disallows the use of valuation discounts in determining fair market value of “nonbusiness assets” held directly or indirectly for estate and gift tax purposes
- **Grantor Trusts**: Effectively reflects Obama Green Book proposal in what would be a new Section 2901 causing inclusion of assets transferred to grantor trust in gross estate, and makes sales to grantor trusts recognition events
- **Increased Income Taxes Will Impact Fiduciary Income Taxes**: The proposal:
 - Surtax of 3% on modified adjusted gross income above \$100,000
 - 39.6% rate for income in excess of \$12,500
 - Capital gains rate increased to 25%
 - Qualified Small Business Stock (QSBS) gain exclusion reduced to 50% of gain from 100%

House Ways and Means Proposals (September 13, 2021) : Effective Dates

- **Lower Exemption**: Starting in 2022
- **Valuation Discounts**: Transfers after date of enactment
- **Grantor Trusts**: Transfers after date of enactment
- **Increased Fiduciary Income Taxes**:
 - Surtax of 3% and return of 39.6% tax bracket applies to tax years beginning *after* December 31, 2021
 - Capital gains tax increase applies to sales or exchanges occurring *after* September 13, 2021
 - Reduction in QSBS gain exclusion applies to sales or exchanges occurring *on or after* September 13, 2021

House Ways and Means Proposals (September 13, 2021) : Observations

- **What Didn't Make it In:** It is notable how many revenue raisers related to estate planning did not make it in such as:
 - President Biden's proposal to make death and gifts an income tax recognition event (including the elimination of the basis step-up)
 - No changes to the rules on GST
 - No changes to structure of GRATs
 - No increase in transfer tax rates
 - No change in SALT deduction
- **Exemption Amounts:** Democratic legislative proposals and the Biden-Sanders Unity Platform from the presidential campaign called for the exemption to be even lower than the \$5 million inflation-adjusted amount in this proposal
- **Valuation Discounts:** The proposal is almost verbatim what Senator Sanders has proposed in his own estate/gift tax proposals (For the 99.5% Act) with one key change. Senator Sanders proposed that there be an automatic disallowance of lack of control and marketability discounts if the entity was owned or controlled by the transferor or related parties to the transferor—that feature is not proposed here.
- **Grantor Trusts:** The proposed new Section 2901, which causes inclusion of grantor trust assets in the grantor's gross estate, can be found in other pending Democratic proposals (i.e. For the 99.5% Act and the American Housing and Economic Mobility Act of 2021). New to this proposal, however, is the creation of a new Section 1062 of the Internal Revenue Code, which would treat sales between a grantor and grantor trust as if between an owner and a third party (that is, as a recognition event for income tax purposes).
- **Increase in Income Taxes Will Impact Fiduciary Income Taxes:** Given the low marginal rates applicable to trusts and estates, these substantial increases will be felt by estates and trusts of all sizes.

Feel the Bern(ie): For the 99.5% Act (March 2021)

- **Lower Exemption**: \$3.5 million estate tax and \$1 million gift tax
- **Higher Rates**: 45% for \$3.5-\$10M, 50% for \$10-\$50M , 55% for \$50M to \$1 billion, 65% for above \$1 billion
- **Valuation Discounts**: Discounts would be largely eliminated
- **GRATs**: Minimum 10 year term and minimum remainder of the greater of 25% of the value of assets or \$500,000
- **GST**: Any trust that will last more than 50 years will have an inclusion ratio of 1 (i.e. would owe tax on distributions to skip persons). For existing trusts that last longer—they will have an inclusion ratio of 1 starting 50 years after the enactment date
- **Annual Exclusion**: \$20,000 cumulative cap on transfers to trusts or gifts of entities with restrictions on them (example: Crummey powers)
- **Grantor Trusts**: Effectively reflects Obama Green Book proposal in what would be a new Section 2901 that would include assets in gross estate
- **Limited Elimination of Basis Step-Up**: No step-up in basis for grantor trusts that are not included in the gross estate (new addition that was not in prior Sanders' proposal)

For the 99.5% Act (March 2021): Effective Dates

- **Lower Exemption**: Starting in 2022
- **Higher Rates**: Starting in 2022
- **Valuation Discounts**: Transfers after enactment date
- **GRATs**: Transfers after enactment date
- **GST**: Transfers after enactment date
- **Annual Exclusion**: Tax year following the year of the enactment date
- **Grantor Trusts**: Transfers after enactment date
- **Limited Elimination of Basis Step-Up**: Transfers after enactment date

American Housing and Economic Mobility Act of 2021

- **Lower Exemption**: \$3.5 million estate tax and gift tax
- **Higher Rates**:
 - 55% for \$0-\$13M, 60% for \$13-\$93M, 65% for above \$93 million
 - 10% surtax on tax owed by estates over \$1 billion
- **GRATs**: Minimum 10 year term and minimum remainder of 10% of the value of assets
- **GST**: Any trust that will last more than 50 years will have an inclusion ratio of 1 (i.e. would owe tax on distributions to skip persons). For existing trusts that last longer—they will have an inclusion ration of 1 starting 50 years after the enactment date.
- **Annual Exclusion**: \$20,000 cumulative cap on transfers to trusts or gifts of entities with restrictions on them (example: Crummey powers).
- **Grantor Trusts**: Effectively reflects Obama Green Book proposal in what would be a new Section 2901 that would include assets in gross estate

American Housing and Economic Mobility Act of 2021

- Lower Exemption: 2021
- Higher Rates: 2021
- GRATs: Transfers after enactment date
- GST: Transfers after enactment date
- Annual Exclusion: Tax year following the year of the enactment date
- Grantor Trusts: Transfers after enactment date

The Ultra-Millionaire Tax Act of 2021

(the wealth tax proposal)

- Proposed Effective Date: 2023
- Who does it apply to—an “applicable taxpayer” which is:
 - Individuals (married couples treated as a single taxpayer)
 - Applies to non-resident/non-citizens on US situs property using estate tax situs rules
 - Trusts (excluding Section 401(a) and 501(a) trusts)
 - Trusts with “substantially the same beneficiaries shall be treated as a single applicable taxpayer”
 - If a trust decants to another trust—those trusts are considered one trust for that year
- Tax Rates
 - 0% for an applicable taxpayer’s net worth from \$0 to \$50 million
 - 2% for an applicable taxpayer’s net worth in excess of \$50 million to \$1 billion
 - 3% for an applicable taxpayer’s net worth over \$1 billion with automatic increase to 6% if universal healthcare with no private insurance becomes law

The Ultra-Millionaire Tax Act of 2021

(the wealth tax proposal)

- Property included
 - All property that would be included in gross estate if the taxpayer died
 - All property in a grantor trust
 - All property gifted to a minor family member until that minor turns 18
 - \$50,000 exclusion for tangible property that are not collectibles or used in business
- Valuation—within 12 months of enactment the Treasury Department must establish valuation rules
 - Specifically authorizes use of valuation methods not currently in use under tax law
 - Specifically authorizes formulaic valuation methods
 - Specifically grants authority to “address the use of valuation discounts”

The Ultra-Millionaire Tax Act of 2021

(the wealth tax proposal)

- Applicable taxpayers who die mid-year—tax is prorated
- Deductibility
 - Not deductible for income tax purposes
 - Is deductible for estate tax purposes
- If you expatriate—40% exit tax
- Reporting and enforcement
 - Treasury must by regulation require reporting of information to substantiate tax liability within 12 months of enactment
 - Will be part of taxpayer's income tax return
 - Regulatory authority granted to require others to provide information
 - Mandatory 30% or greater audit rate

The STEP (Sensible Taxation and Equity Promotion) Act

- Tax unrealized gains:
 - Upon transfer by gift or at death
 - Would not apply to transfers to US citizen/long-term resident spouses, charities, charitable trusts, qualified disability trusts and cemetery trusts
 - \$1,000,000 of exclusion (adjusted for inflation), \$100,000 of which is available during life
 - Taxation of assets in non-grantor trusts every 21 years
 - Transition rule for trusts established in or before 2005 – first tax due in 2026
- Deferral over a 15-year period available for tax on gains other than actively traded assets, that are transferred at death or taxed at 21 years (similar to 6166 but more assets qualify)
- Would add reporting requirement for trusts with more than \$1M in assets or \$20,000 in income to report balance sheet, income statement, trustees, grantors and beneficiaries, including “a full and complete accounting of all trust activities and operations for the year”
- Effective January 1, 2021

The Biden Campaign

- Exemption and Rates
 - Unity Task Force Recommendations called for “Estate taxes should be raised back to the historical norm”
 - Not specific but other indicators that 2009 regime is what is proposed (\$3.5/\$1/45%)
- Elimination of Basis Step Up
 - Explained as a way to pay for \$750 billion over 10 years for post-secondary education
 - The impact on beneficiaries could be greater given proposal to increase capital gains rates over \$1 million to 39.6% (with 3.8% net investment tax a total of 43.4%)

The Biden Administration: The American Families Plan

“Moreover, the President would eliminate the loophole that allows the wealthiest Americans **to entirely escape tax on their wealth** by passing it down to heirs. Today, our tax laws allow these accumulated gains to be passed down across generations untaxed, exacerbating inequality. The President’s plan will close this loophole, ending the practice of “stepping-up” the basis for gains in excess of \$1 million (\$2.5 million per couple when combined with existing real estate exemptions) and making sure the gains are taxed if the property is not donated to charity. The reform will be designed with protections so that family-owned businesses and farms will not have to pay taxes when given to heirs who continue to run the business. Without these changes, billions in capital income would continue to escape taxation entirely..”

-Fact Sheet: The American Families Plan, issued by White House Briefing Room on April 28, 2021

The Biden Green Book

- On May 28, 2021, the Treasury Department released its General Explanations of the Administration's Fiscal Year 2022 Revenue Proposals (a/k/a the Green Book).
- The Green Book provides a comprehensive set of tax proposals the Administration would like to become law.
- The Biden Green Book **DID NOT** include estate and gift tax proposals that were proposed by the Obama Administration and/or included in For the 99.5% Act and American Housing and Economic Mobility Act of 2021, such as:
 - Lowering the exemption
 - Eliminating zeroed-out GRATs
 - Eliminating perpetual GST Exempt Trust
 - Including grantor trusts in decedent's estate
- The Biden Green Book **DOES** propose eliminating the "basis step-up" and makes gifts, death, transfers to and from trusts and partnerships, and having a 90-year holding period, recognition events for income tax purposes.

The Biden Green Book: Lifetime Gifts and Death

- Event Triggering Gain: Transfers of appreciated property as a gift or at death will be treated as a realization event for the donor or donor's estate.
- Exclusions:
 - **Tangible Property**: Tangible personal property (other than collectibles) are not treated as being sold.
 - **General Exclusion**: Biden's proposal provides that in addition to any other exception from gain being recognized that there would be a \$1 million per-person exclusion from gain.
 - **Principal Residence**: In addition to general exclusion, there is an exclusion of up to \$250,000 of gain per taxpayer on the sale of a principal residence.
 - **QSBS**: The gain exclusion for qualified small business stock would continue to be available.
- Transferees Exempt from Recognition:
 - A surviving spouse who is a "U.S. spouse" will receive carry-over basis
 - Charities

The Biden Green Book: Lifetime Gifts and Death

- Donee's Basis: No basis increase for lifetime gifts under the \$1 million exclusion, but other transfers (including tax free transfers at death) will receive a basis adjustment.
- Deferral:
 - 15-year payment plan allowed for non-liquid assets
 - Deferral for family owned and operated businesses available until that business is no longer family owned and operated
- Valuation: The determination of fair market value will be using gift and estate tax valuation principles, but the proposal restricts application of valuation discounts by providing that the value of “a transferred partial interest would be its proportional share of the fair market value of the entire property.”
- Reporting: Deemed recognition would be reported either on 1) the estate or gift tax return or 2) a separate reporting form.
- Effective Date: All gifts and deaths occurring on or after January 1, 2022.

The Biden Green Book: Recognition with Trusts and Partnerships

- Distributions To and From Trusts Partnerships:
 - Recognition Event: Transfers to, and distributions from, a trust or partnership would be recognition events. This applies to both non-grantor trusts and grantor trusts (except revocable trusts).
 - Effective Date: All gifts and deaths occurring on or after January 1, 2022.
- Maximum Holding Period for Assets in Trusts and Partnerships:
 - Recognition Event: “Gain on unrealized appreciation also would be recognized by a trust, partnership... that is the owner of property if that property has not been the subject of a recognition event within the prior 90 years...”
 - Effective Date: The 90-year period would start no earlier than January 1, 1940, meaning that the first potential liability would be triggered in 2030 (90 years after 1940).



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