

MSF CLIENT ALERT

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New Tax Proposals Could Shake Up Estate Planning for Generations

Members of the Senate majority have proposed two pieces of legislation intended to tax high net worth families. The two bills, the “For the 99.5 Percent Act”, sponsored chiefly by Sen. Bernie Sanders, and the “Sensible Taxation and Equity Promotion (STEP) Act”, led by Sen. Chris Van Hollen, stand to upend some of the most commonly used estate planning tools and raise billions in revenue for the Federal government.

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Sen. Sanders’ 99.5 Percent Act would lower the current estate tax exclusion amount from \$11.7 million per individual (\$23.4 million for married couples) to \$3.5 million per individual (\$7 million for married couples), annually adjusted for inflation. The bill also abandons the current 40% universal estate tax rate for a progressive tax rate ranging from a minimum of 45% to a maximum marginal rate of 65% for decedents leaving estates in excess of \$1 billion. The proposal would also severely limit the use of Grantor Retained Annuity Trusts (GRATs) to shelter growth from income tax, eliminate the use of many valuation discounts commonly used by closely held businesses, and amend the rules relating to annual exclusion gifts.

Sen. Van Hollen’s STEP Act focuses on capturing unrealized capital gains that have long been exempt from taxation in the United States. Under current law, heirs who inherit non-retirement assets from a decedent are allowed to take what is known as a “step-up” in basis - that is, the basis of an asset becomes its market value as of the decedent’s date of death. If an heir decides to sell that asset soon after death, only the growth that occurred since the decedent’s death would be subject to tax, not the growth that occurred during the decedent’s life. Under the proposed legislation, however, heirs would be required to use the decedent’s basis in the asset to determine their realized gains. For high growth capital assets, this change has the potential to cause significant income tax liabilities for high net worth individuals despite an attempt to limit the burden by permitting an exemption of \$1 million of gains and allowing payments to be made in installments over a fifteen year period.

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Both bills contain various additional provisions, principally surrounding transfers to trusts, designed to protect their main goals of preventing long-term generational wealth which avoids taxation. A major consequence of these provisions includes the limitation on the use of “dynasty” trusts designed to last for generations. Under the proposed legislation, any trust designed to be in existence for more than 50 years after the Trust’s creation will be prohibited from allocating GST Tax exemption to such trust, subjecting all transfers to the 40% GST Tax.

While it remains uncertain whether either of the proposed bills will be enacted into law in their current form – or at all – these bills highlight the need for high-net worth families to contact their estate planning teams now to take advantage of current tax rules. If passed, the majority of the 99.5 Percent Act’s provisions would become effective immediately, with exemption amounts lowering for decedent’s dying after December 31, 2021; the STEP Act’s provisions, on the other hand, would apply to any transfer taking place after December 31, 2020, meaning its provisions have the potential to retroactively affect transfers made prior to its enactment. This alert outlines the key provisions of the proposed tax changes, however there may be additional provisions that apply to each client’s specific planning needs.

Please contact an attorney in the Taxation & Estates practice if you need assistance with respect to this information.



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