

# Tax legislation update

## New details from White House budget



While legislation has yet to be proposed for any upcoming tax changes, last Friday the White House gave us more details on what they want, when it released its budget proposal along with the Green Book (which provides explanations and more details on the budget proposal).

Think of this as the beginning of negotiations. The final legislation will no doubt look different. It takes the votes of all 50 democratic and independent senators to pass any legislation using the *Budget Reconciliation Method* (versus the usual 60 votes). This gives individual senators more power to dictate changes.

Here are updates on what we've learned from the recent budget proposal and Green Book. *See the May 2021 BMO Proposed Tax Changes Update Article for reference.*

### Effective date — retroactivity for new capital gains tax rate

All of the proposals appear to be effective 1/1/2022 except the new capital gains tax rate. The Administration has proposed taxing capital gains and qualified dividends at 39.6% (plus the existing 3.8% Medicare Net Investment Income tax) for taxpayers with adjusted gross income of more than \$1 million. The Green Book indicates that this one proposal would be retroactive to the “date of announcement.” It is unclear exactly what date that is, but it is most likely either the prior release of the American Families Plan fact sheet on April 28, 2021, or the release of the Budget proposal on May 28, 2021. Keep in mind that it is exceedingly rare to have retroactive tax increases. In addition, it is likely there will be pushback, even among some democratic senators, to this retroactivity, as well as to the tax rate itself.

### 1031 tax deferred real estate changes

The proposals clarified that while they are still pursuing the repeal of Section 1031 tax deferred real estate tax changes, the exception for capital gains on the sale of real estate of \$500,000 or less is per taxpayer. So married couples would have a \$1 million exclusion.

### Triggering of capital gains when assets are transferred

A new provision not seen in the current tax code has been proposed. Lifetime gifts and transfers of assets at death would trigger capital gains on the built-in appreciation of the assets. For example, if Amazon stock was originally purchased for \$200,000 (basis) and was gifted to someone when the fair market value was \$500,000, it would trigger \$300,000 of capital gains income to the gift-giver with the corresponding tax due — even though the stock was not sold. This would not apply to transfers to (1) spouse, (2) charity, (3) grantor transfers to a revocable trust or (4) transfer of certain family business & family farms (where a family member continues to run it).

As mentioned in our prior pieces, there would be an allowance of \$1 million per person that could be allocated to these gains; so now capital gains tax would not be due on \$1 million of appreciation (based on the value as of the date of transfer). Considering our prior example, the \$1 million allowance could be applied to that \$300,000 of gain when the gift was made so no capital gains tax would be due.



**Dave Bensema, CPA, CFP®** is a Managing Director with BMO Family Office, an integrated wealth management provider that serves ultra-affluent individuals, families and family offices across their tax, estate, investment, philanthropic, risk and family capital needs. Dave provides customized financial planning solutions to individuals and families as part of an overall personal wealth management strategy. He joined the organization in 1991 and has over 27 years of experience in the financial services industry.



**Jayne Hartley** is a Regional Leader of Wealth Planning for BMO Wealth Management where she oversees the strategic development and delivery of customized wealth planning services to clients throughout the United States. Jayne is also a key member of the BMO's Business Owner Strategies and Solutions team, a specialized group of professionals that provides sophisticated wealth transfer, estate planning guidance to business owners and corporate executives. She has over 25 years of wealth planning experience.



**Brad Herman, CFP®** is a Senior Wealth Planning Consultant with BMO Private and provides customized financial planning solutions to high-net-worth individuals and families as part of an overall personal wealth management strategy. He joined BMO Private Bank in 2019 and has over 15 years of experience in the financial services industry. Prior to joining BMO Private Bank, Brad held various roles in the independent Registered Investment Advisor and brokerage space as well as over seven years in Private Banking.



**Pratik Patel** is a Managing Director and Head of the Family Wealth Strategies team with BMO Family Office, an integrated wealth management provider that serves ultra-affluent individuals, families and family offices across their tax, estate, investment, philanthropic, risk and family capital needs. Pratik oversees the delivery of integrated wealth management advice and client service for ultra-affluent clients. His expertise includes financial planning, tax planning, wealth transfer planning, charitable and philanthropic planning, family governance and education planning and business owner and corporate executive planning.

However, the person who received the gift would keep the gift-giver's tax basis. The new proposals make it clear that there is portability of this \$1 million allowance for spouses. So, a surviving spouse could claim any of the deceased spouse's unused \$1 million amount. A married couple, therefore, effectively has a \$2 million allowance in total. In addition, there would be a \$250,000 per person allowance for appreciation in any residence; this also would have portability for surviving spouses. A married couple would have a \$500,000 allowance in total, toward any residence.

As part of this expansion of when capital gains are triggered, gain recognition would also be triggered when assets are transferred to, and distributed by, irrevocable trusts and partnerships. If passed, this would have a dramatic effect on some estate tax planning strategies. All the more reason to talk to your advisors and evaluate what gifting you should do in 2021 before this takes effect January 1, 2022.

Lastly, a new "90 year" rule would be added for assets held by a trust, partnership or other non-corporate entity. Gains on unrealized appreciation would be recognized (and capital gains tax would be due) if capital gains had not been paid on the property for 90 years. The initial date for the beginning of the 90-year rule would be 1940, thus the first possible recognition event would be December 31, 2030.

## In Closing:

These provisions are only proposals; we are still waiting to see actual legislation drafted. However, it does give us a clue of where the White House is headed for beginning negotiations.

## Let's start planning!



The information and opinions expressed herein are obtained from sources believed to be reliable and up-to-date, however their accuracy and completeness cannot be guaranteed. Opinions expressed reflect judgment current as of the date of this publication and are subject to change.

This information is being used to support the promotion or marketing of the planning strategies discussed herein. This information is not intended to be legal advice or tax advice to any taxpayer and is not intended to be relied upon. BMO Harris Bank N.A. and its affiliates do not provide legal advice to clients. You should review your particular circumstances with your independent legal and tax advisors.

Certified Financial Planner Board of Standards Inc. owns the certification marks CFP® and CERTIFIED FINANCIAL PLANNER™ in the U.S.

Estate planning requires legal assistance which BMO Harris Bank N.A. and its affiliates do not provide. Please consult with your legal advisor.

"BMO Wealth Management" is a brand name that refers to BMO Harris Bank N.A. and certain affiliates that provide certain investment, investment advisory, trust, banking and securities products and services. Investment Products are:

**Not Insured by FDIC or Any Other Government Agency | Not BMO Harris Bank Guaranteed | Not BMO Harris Bank Deposits or Obligations | May Lose Value**

BMO Private Bank is a brand name used in the United States by BMO Harris Bank N.A. Member FDIC. Not all products and services are available in every state and/or location.

BMO Family Office is a brand delivering family office services and investment advisory services through BMO Family Office, LLC, an investment adviser registered with the U.S. Securities and Exchange Commission; investment management services, trust, deposit and loan products and services through BMO Harris Bank N.A., a national bank with trust powers; and trust services through BMO Delaware Trust Company, a Delaware limited purpose trust company. BMO Delaware Trust Company does not offer depository, financing or other banking products, and is not FDIC insured. Not all products and services are available in every location. Family Office Services are not fiduciary services and are not subject to the Investment Advisors Act of 1940 or the rules promulgated thereunder. Investment products and services: **ARE NOT A DEPOSIT – NOT INSURED BY THE FDIC OR ANY FEDERAL GOVERNMENT AGENCY – NOT GUARANTEED BY ANY BANK – MAY LOSE VALUE.**

Capital Advisory Services are offered by a division of BMO Harris Bank N.A. NMLS #401052

C11# 12924594

© BMO Financial Group (10/21)