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Congress of the United States

JOINT COMMITTEE ON TAXATION
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ROBERT P. HARVEY
DEPUTY CHIEF OF STAFF

November 3, 2023

Honorable Bernard Sanders
United States Senate
SD-332
Washington, D.C. 20510

Dear Senator Sanders:

This letter corrects our response of November 1, 2023, for a revenue estimate of S. 1178 (118th Congress), the “For the 99.5 Percent Act.” Below are descriptions of applicable sections of your bill along with the relevant present law.

Section 2 of the bill

Under present law, the estate and gift taxes are unified with a tax rate of 40 percent and a \$10 million inflation-indexed exemption.¹ Surviving spouses generally are permitted to utilize the unused portion of a predeceased spouse’s estate tax exemption. A separate transfer tax is imposed on generation-skipping transfers in addition to any estate or gift tax that is imposed on such transfers. This tax generally is imposed on transfers, either directly or through a trust or similar arrangement, to a beneficiary more than one generation below that of the transferor. The generation-skipping tax is computed using a flat rate of 40 percent and an exemption equal to the estate tax exemption. For decedents dying in 2026 and thereafter, the estate and gift tax exemption is an inflation-indexed \$5 million.

Section 2 of the “For the 99.5 Percent Act” reduces the estate tax exemption to \$3.5 million and the gift tax exemption to \$1 million. These amounts are not indexed for inflation. The maximum tax rate applied to estates and gifts is raised to 45 percent for taxable amounts greater than \$3.5 million, 50 percent for taxable amounts greater than \$10 million, 55 percent for taxable amounts greater than \$50 million, and 65 percent for taxable amounts greater than \$1 billion.² Surviving spouses continue to be permitted to utilize the unused portion of a predeceased spouse’s estate tax exemption.

¹ For 2023, the inflation-indexed exemption amount is \$12.92 million.

² The 39-percent rate bracket would be extended to cover taxable amounts in excess of \$750,000 but not in excess of \$3.5 million.

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Section 3 of the bill

In general, under present law section 2032A of the Internal Revenue Code (the “Code”), an executor of an estate may elect to use the value of certain farmland and other real property (“qualified real property”) in its use as a farm or other trade or business rather than the fair market value of the property in determining the value of the decedent’s estate. The maximum permitted reduction in value is an inflation-indexed \$750,000. The maximum reduction in value for decedents in 2023 is \$1,310,000. Section 3 of the “For the 99.5 Percent Act” increases the maximum reduction in value to \$3 million and indexes that amount for inflation occurring after 2024.

Section 4 of the bill

Under present law, an executor generally may elect to exclude from the value of the gross estate the lesser of (1) the applicable percentage of the value of land subject to a qualified conservation easement (reduced by the amount of any charitable deduction for a contribution of the easement under section 2055(f)) or (2) \$500,000. The applicable percentage is 40 percent, with certain reductions described in the Code. Section 4 of the “For the 99.5 Percent Act” increases the dollar cap from \$500,000 to \$2 million and the applicable percentage from 40 percent to 60 percent.

Section 5 of the bill

Under section 1014 of the Code, a taxpayer who acquires assets from a decedent generally takes a basis equal to the fair market value of the assets on the date of the decedent’s death. Section 5 of the “For the 99.5 Percent Act” disallows this step-up in basis for property (1) held in a trust of which the transferor is treated as the owner for income tax purposes (*i.e.*, a grantor trust) and (2) that is not includible in the gross estate of the transferor.³

³ Revenue Ruling 2023-2, issued on March 29, 2023, provides that that step-up in basis applies only to assets that are included in the grantor’s estate.

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Section 6 of the bill

Section 6 of the “For the 99.5 Percent Act” includes valuation rules for certain transfers of nonbusiness assets and limits the valuation discount applicable to transfers of minority interests of business assets for estate and gift tax purposes. Generally, in the case of the transfer of any interest in an entity other than an interest that is actively traded, no valuation discount shall be applied to any nonbusiness assets held by the entity, the value of any nonbusiness assets held by the entity shall be determined as if the transferor had transferred such assets directly to the transferee, and the nonbusiness assets shall not be taken into account in valuing the interest in the entity. “Nonbusiness assets” are defined as any assets other than those “used in the active conduct of a trade or business.” Passive assets are not treated as used in the active conduct of a trade or business unless such passive assets are: (1) the stock in trade or inventory of the taxpayer, accounts receivable acquired in the ordinary course of business, or hedges with respect to such property, or (2) “the real property used in the active conduct of one or more real property trades or businesses ... in which the transferor materially participates...” Also, any asset (including a passive asset) held as part of the reasonably required working capital needs of a trade or business shall be treated as used in the active conduct of a trade or business.

The provision also generally disallows discounts for lack of control or lack of marketability if the transferor, the transferee, and members of their families have control of the entity or own the majority of the ownership interests in the entity.

Section 7 of the bill

Section 7 of the “For the 99.5 Percent Act” imposes a minimum term of 10 years for the annuity interest in a Grantor Retained Annuity Trust (“GRAT”) and a maximum term of the life expectancy of the annuitant plus 10 years. Furthermore, the provision prohibits any decrease in the annuity over the term of a GRAT. The provision provides that the remainder interest of a GRAT shall not be less than the greater of 25 percent of the value of the assets transferred to the trust or \$500,000, and not more than the fair market value of the property in the trust.

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Section 8 of the bill

Section 8 of the “For the 99.5 Percent Act” applies certain transfer tax rules to certain grantor trusts. To the extent that the income tax rules treat a grantor of a trust as an owner of the trust (*i.e.*, the trust is a grantor trust), the provision: (1) includes the assets of that trust in the gross estate of that grantor for estate tax purposes; (2) subjects to gift tax any distributions from the trust to one or more beneficiaries during the grantor’s life; and (3) subjects to gift tax the remaining trust assets at any time during the grantor’s life if the grantor ceases to be treated as an owner of the trust for income tax purposes.

The provision also applies to any nongrantor who is deemed to be an owner of the trust for income tax purposes and who engages in a sale, exchange, or comparable transaction with the trust that would have been subject to capital gains tax if the person had not been a deemed owner of the trust. In such a case, the provision subjects to transfer tax the portion of the trust attributable to the property received by the trust in that transaction, including all retained income there from, appreciation thereon, and reinvestments thereof, net of the amount of the consideration received by the person in that transaction.

The provision reduces the amount subject to transfer tax by the value of any taxable gift made to the trust by the deemed owner. The transfer tax imposed by the proposal is payable from the trust. This provision does not apply to any trust that is otherwise includible in the gross estate of the deemed owner.

Section 9 of the bill

Section 9 of the “For the 99.5 Percent Act” provides that generation skipping transfer (“GST”) tax shall apply in the case of a transfer to a any person who is not an exempt person. The GST inclusion ratio for a generation skipping transfer made to a non-exempt person will be one, potentially resulting in the imposition of GST tax on the transfer. An exempt person is a natural person assigned to a generation which is two or fewer generations below the generation assignment of the transferor or a person whose date of birth precedes the date on which the trust was created or a trust in which all interests are held by these persons. Trusts created before 2024 are deemed to have been created on January 1, 2024.

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Section 10 of the bill

Section 10 of the “For the 99.5 Percent Act” modifies the annual exclusion from gift tax under section 2503(b) of the Code. Under present law, a donor can transfer up to \$17,000⁴ (for 2023) of property to each of an unlimited number of donees and exclude the amount of all such transfers from his or her gift tax base. To qualify for the exclusion, the property interests transferred must be present interests, as opposed to future interests (such as remainders). The “For the 99.5 Percent Act” eliminates the present interest requirement for the gift tax annual exclusion. In addition, the Act imposes a new, aggregate *per-donor* limit on certain annual exclusion gifts equal to twice the annual exclusion amount in effect for the year. The following transfers are subject to this new, additional per-donor limit: (1) transfers in trust; (2) transfers of interests through pass-through entities; (3) transfers of interests subject to a prohibition on sale; and, (4) any other transfers of property that, without regard to withdrawal, put, or other such rights in the donee, cannot be immediately liquidated by the donee.

Section 11 of the bill

Section 11 of the “For the 99.5 Percent Act” includes any gift tax paid by a donor on any gift made in a calendar year as an additional taxable gift made in such calendar year.

Section 12 of the bill

Finally, section 12 of the “For the 99.5 Percent Act” moves the definition of the term “executor” from section 2203 to section 7701 of the Code so that it applies for all tax purposes. Additionally, the executor is generally authorized to act on behalf of the decedent, including with respect to any predeath tax liability.

For revenue estimating purposes, we have assumed an enactment date of December 1, 2023. The provisions of the “For the 99.5 Percent Act” concerning rates and exemption

⁴ The statute provides an amount of \$10,000, adjusted in \$1,000 increments for inflation occurring after 1997.

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amounts, special use valuations, and conservation easements are generally effective for the estates of decedents dying and gifts made after December 31, 2023. The provisions concerning valuation discounts and grantor retained annuity trusts are effective for transfers after the date of enactment. Section 8 of the bill, concerning the application of certain transfer tax rules to certain grantor trusts, is generally effective for transfers to trusts on or after the date of enactment. The provision relating to the allocation of GST exemption to a trust is effective on the date of enactment. Sections 10 and 11, concerning the gift tax annual exclusion and the gross up for taxable gifts, are effective for any calendar year beginning after the date of enactment. Finally, section 12, concerning the definition of the executor, is effective on the date of enactment.

While our letter of November 1, 2023, accurately described your policy, we discovered an error in our modelling related to the level of the exemption amounts that reduced the expected revenue gain from your bill. The corrected estimate shows the “For the 99.5 Percent Act” raising more revenue than our 2021 estimate of a similar bill for a variety of reasons, including a different estate and gift baseline that includes fiscal years 2032 and 2033. The corrected estimated effects of the “For the 99.5 Percent Act” on Federal fiscal year budget receipts:

Fiscal Years [Billions of Dollars]											
<u>2024</u>	<u>2025</u>	<u>2026</u>	<u>2027</u>	<u>2028</u>	<u>2029</u>	<u>2030</u>	<u>2031</u>	<u>2032</u>	<u>2033</u>	<u>2024-28</u>	<u>2024-33</u>
7.0	46.9	51.5	44.6	49.4	55.3	61.0	67.9	76.4	85.6	199.5	545.7

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

I hope this information is helpful to you. If we can be of further assistance in this matter, please let me know.

Sincerely,



Thomas A. Barthold