PERSPECTIVE

Los Angeles | Daily Journal

THURSDAY, MARCH 2, 2017

# Trump, California At Odds On Estate Tax

**By Robert W. Wood**

California and President Donald J. Trump have a complicated relationship. They are opposites on numerous issues from immigration and sanctuary status to environmental issues. And that difference of opinion extends to taxes, too.

Just as Trump was being elected, California was increasing state income taxes, again. The state's high 13.3 percent individual income tax is only temporary though, just through *2030*. That tax hike was passed by voters in November. Since then, the Golden State is moving to tax estates, even if the feds do not.

If the federal estate tax law is repealed by Trump and Congress, estates in California will still pay, provided that this proposed law is enacted. Last week, State Sen. Scott Wiener, D-San Francisco, introduced Senate Bill 726, which seeks to keep the estate tax in California. The proposal, however, would have to go to voters.

As Wiener put it: “If Donald Trump and congressional Republicans are hell-bent on cutting taxes for our wealthiest residents, we should counter-balance those tax cuts by recapturing the lost funds and investing them here at home in our schools, our healthcare system, and our roads and public transportation systems."

The estate tax remains terribly controversial. It generates emotional fervor that most tax issues do not. Right now, the federal estate tax remains at 40 percent. But, not long ago, Hillary Clinton proposed increasing the estate tax to an astounding 65 percent. Then-candidate Donald Trump vowed to repeal it. And with a Republican House and Republican Senate, he just might.

He is after other taxes, too, of course, such as those enacted as part of Obamacare. But the estate tax can make people's blood boil, even if it is not widely paid. Current law exempts estates worth $5.49 million or less, up from $5.45 million in 2016. Beyond that, you pay 40 percent.

A number of Democrats, including Clinton, called for whittling the $5.45 million figure down to $3.5 million, and upping the 40 percent estate tax rate to 45 percent. Then, as the election drew near, Clinton proposed 50 to 65 percent estate tax rates, depending on your wealth. The proposed 50 percent rate was for estates worth over $10 million per person, 55 percent for estates over $50 million, and 65 percent for estates exceeding $500 million.

Trump wants to repeal the estate tax entirely. More than a few commentators have noted that Trump himself stands to benefit from such a plan, as would his heirs. But it would benefit many others, too. Steadfast proponents of the estate tax are not ready to give up.

They argue that it helps to stop wealthy people from getting even wealthier. But given that income taxes must be paid on earnings that eventually make up the estate's value, opponents claim that the tax is a true double tax having no place in America. Strangely, another argument for the estate tax is that you can plan around it.

Yet that is becoming more and more difficult. It has long been assumed that clever and wealthy people can find ways around the estate tax. But it is far tougher today, with new IRS administrative rules (proposed before President Barack Obama left office) that make valuation discounts scarce and worth less.

In any case, planning to avoid the estate tax is expensive and requires years of planning. Wealthy or not, the estate tax catches many people off guard, after they have worked and paid income tax their whole lives. Small and family businesses can be particularly hard hit. Already, it is hard for many family-owned businesses to stay afloat after the death of a key figure.

Not all of the reasons are managerial. Taxes can prompt sales of family companies and family farms. Ironically, it was only recently — in 2013 — that Americans *finally* got some certainty with a $5 million per person exemption. Indexed for inflation, it now stands at $5.49 million, $10.98 million for a married couple. And the Republicans want it repealed. Conversely, House Democrats want to raise the estate tax materially.

Not long ago, Obama argued that allowing a basis step up for income tax purposes on death was a huge loophole. He proposed *no* basis step up, hoping to raise approximately $200 billion over the next decade. Some figures suggest that this proposal would yield the highest estate tax rate in the world.

Stephen Moore of the Heritage Foundation calculated that by eliminating basis step up, we would end up with the world’s highest estate tax rate. Dick Patten, chairman of the Family Business Defense Council, calculated an effective death tax rate of 57 percent. If you add in state inheritance taxes, the combined tax rate could go as high as 68 percent.

As for California, if the Trump administration succeeds with federal estate tax repeal, California legislators may push for a vote. In most states, votes for tax increases tend to do poorly. But, California has a recent history of approving tax increases, particularly at the upper end of the income spectrum.

If California enacts its own estate tax replacement, it is worth asking if all the billionaires will remain. In the short term, the answer may be yes. But California’s income tax history is worth underscoring. After all, many high-income Californians seem to move away *right before* a big income event, such as an IPO or a career-capping lawsuit recovery.

California tax officials are aggressive in chasing “former” residents. Sometimes, the dispute is not *whether* you moved, but *when* you did. In other cases, California sifts through all your data and can often find sufficient connections to keep you here, *even if you have left*.

If California’s estate tax starts to wallop the wealthy who die here, there could be a whole new set of moves and timing. Californians predicting their demise — soon or down the road — may eye other states, just as they do now for income tax purposes. If that happens, even more than it is already, perhaps California will become the tax lawyer’s state. Now *there’s* a license plate slogan!

**Robert W. Wood** *is a tax lawyer with www.WoodLLP.com, and the author of “Taxation of Damage Awards & Settlement Payments” (www.TaxInstitute.com). This is not legal advice.*