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Making sense of the Sensible Taxation and Equity Promotion (STEP) Act

In late March, a group of U.S. Senators proposed legislation aimed at taxing any appreciated assets that are transferred by gift, transfer to a trust, or at death. If enacted, the STEP Act would eliminate the step-up in basis for appreciated inherited assets included in some estate plans, and impose a tax at the time of some lifetime gifts.

While we don't know if this bill will make its way through both houses of Congress, it's a good idea to consider now how the proposed legislation could affect your estate plan.

What's included in the bill

Under current law, when appreciated assets are transferred at death, the beneficiaries receive a step-up in basis to the asset's fair market value (FMV) on the date of the decedent's death. That means any gains that would have been realized had the original owner sold the asset during their lifetime, are eliminated. The STEP Act would eliminate that step-up in basis, meaning beneficiaries would owe taxes on the gain over and above the basis of the asset when it was originally acquired by the transferor.¹

The Act also proposes to tax any lifetime gifts of appreciated assets. The first \$100,000 of cumulative gain will be able to be passed tax-free to a trust or to any individual other than a spouse. Gifts with cumulative gain above \$100,000 made to a trust or any individual other than a spouse will be subject to tax at the time of the gift.²

\$1 million exemption

It's important to note the bill would allow estates to exclude the first \$1 million in gains, thereby exempting smaller estates from the new tax. Illiquid assets like businesses or farms would be granted up to 15 years to pay the taxes. The current exemption for personal homes of up to \$500,000 would still apply. For larger estates, the gains taxes due could be deducted against estate taxes.³

Implications of the new tax

As a hypothetical example – if an estate included \$10 million in stock that was originally purchased for \$2.5 million (a \$7.5 million gain), the first \$1 million of the estate would be exempt and taxes would be owed on the \$6.5 million gain. That would be a significant change from current tax law, where the estate receives the step-up in basis and taxes would be only on the sale of the asset starting at the FMV when the asset was transferred.

When combined with another proposal making its way through the Senate, the For The 99.5% Act, this bill has significant estate planning implications for high-net-worth individuals. Reach out to your financial professional to discuss strategies that could help protect your estate.

Sources:

1. [Senate Democrats propose capital gains tax at death with \\$1 million exemption](#). CNBC.com, Greg Iacurci, March 30, 2021
2. Sensible Taxation and Equity Promotion Act of 2021, H.S., 117th Congress, March 29, 2021
3. [Wealthy Should Act Now to Prepare for Bernie Sanders's Estate Tax Proposal](#), Kiplinger.com, Jeffrey M. Verdon, Esq., April 18, 2021

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