



Fiscal Note 2025 Biennium

Bill information:

SB0555 - Provide for special spousal trusts with property treated as community property (Hertz, Greg)

Status: As Introduced

- | | | |
|---|---|--|
| <input type="checkbox"/> Significant Local Gov Impact | <input type="checkbox"/> Needs to be included in HB 2 | <input type="checkbox"/> Technical Concerns |
| <input type="checkbox"/> Included in the Executive Budget | <input checked="" type="checkbox"/> Significant Long-Term Impacts | <input type="checkbox"/> Dedicated Revenue Form Attached |

FISCAL SUMMARY

	<u>FY 2024</u> <u>Difference</u>	<u>FY 2025</u> <u>Difference</u>	<u>FY 2026</u> <u>Difference</u>	<u>FY 2027</u> <u>Difference</u>
Expenditures:				
General Fund	\$0	\$94,651	\$93,013	\$94,253
Revenue:				
General Fund	\$0	(\$853,000)	(\$1,034,000)	(\$1,176,000)
Net Impact-General Fund Balance:	\$0	(\$947,651)	(\$1,127,013)	(\$1,270,253)

Description of fiscal impact: HB 555 allows married taxpayers to transfer property to a Special Spousal Trust. Property transferred to the trust has its value stepped up when one of the spouses dies. This step-up will reduce capital gains income.

FISCAL ANALYSIS

Assumptions:**Department of Revenue**

1. HB 555 will allow married taxpayers to create a Special Spousal Trust (SST). Property placed in a SST would be treated as community-property. The SST functions as an option for Montana taxpayers to treat property contributed to the trust as community property.
2. SSTs allow a surviving spouse to receive step-up in basis on all property contributed to the trust when the other spouse passes away. With the step-up in basis, no capital gains would be realized on the increase in value of the property subject to the step-up in basis upon disposition of the property by the surviving spouse.
3. An example is if a couple owns a property equally, with a basis of \$1,000. Without contributing the property to an SST, the surviving spouse receives full ownership of the property, but the step-up in basis applies only to the decedent's share. The surviving spouse basis is now \$1,500. If the property was contributed to an SST, the surviving spouse receives a step-up in basis of \$1,000, with a new basis of \$2,000. If the property is sold shortly after the date of death, no capital gain is realized on the additional \$500 by which the basis is increased.

4. The federal government does not recognize the community property opt-in created by this bill. Because of this, placing property in an SST will not have any direct impact on the federal tax liability of taxpayers.
5. SB 555 does create state personal income tax exemptions for the new step-up in basis, and associated capital gains, for property held in the trust. This state specific step-up are expected to reduce Montana taxable income and state income tax liabilities.
6. In TY 2021, married returns where a spouse died during the year reported nearly \$75,000,000 in taxable capital gains income.
7. While most taxpayers will not create a trust for when a spouse dies, taxpayers with the most capital gains income are more likely to create a trust to reduce their capital gains liability. It is assumed that 1/3 of the capital gains reported by the taxpayers in assumption #4 would have placed their property in the trust created by SB 555 if the trust had been available.
8. As the step-up in basis for the property continues in the years after the spouse dies, it is assumed that 10% of the \$75,000,000 in capital gains continues to be exempted from capital gains taxation in future tax years.
9. HJ 2 revenue assumptions assume that capital gains income will decrease by 25% in TY 2022 and 4.8% in TY 2023. For TY 2024 and TY 2025, capital gains are expected to increase by 5% and 11.2% respectively.
10. It is assumed that capital gains continue to increase at 5% each year after TY 2025.
11. Based on 2021 capital gains, capital gains growth rates, and a 1/3 participation rate, it is assumed that \$18,742,500 in capital gains will be in a Special Spousal Trust when a spouse dies, and has its basis stepped up, in TY 2024. For TY 2025, the capital gains stepped-up is estimated to \$20,841,660. For TY 2026 and TY 2027, qualified capital gains are estimated to be \$21,884,000 and \$22,978,000, respectively.
12. With 10% of capital gains being exempted in each future year, the total amount of capital gains that is expected to not be taxable at the state level is estimated to be \$18,742,500 in TY 2024, \$22,715,910 in TY 2025, \$25,842,189 in TY 2026, and \$29,124,720 in TY 2027.
13. It is assumed that 30% of the capital gains would have been exempted from taxation under current law, due to the capital gains deduction. It is also assumed that the remaining 70% of income will be taxed at the state's top tax rate of 6.5%.
14. In total, stepping-up the basis for the property in the trusts is estimated to reduce Montana tax liability by \$853,000 ($\$18,742,500 \times 70\% \times 6.5\%$) in FY 2025, \$1,034,000 in FY 2026, and \$1,176,000 in FY 2027.

DOR Administrative Costs

15. The Department of Revenue requires 1.00 FTE to administer the taxation of capital gains with this trust in place. The 1.00 FTE will increase Department of Revenue expenditures by \$94,651 in FY 2025, \$93,013 in FY 2026, and \$94,253 in FY 2027.

Fiscal Impact:	FY 2024 Difference	FY 2025 Difference	FY 2026 Difference	FY 2027 Difference
Department of Revenue				
FTE	0.00	1.00	1.00	1.00
Expenditures:				
Personal Services	\$0	\$83,096	\$84,153	\$85,225
Operating Expenses	\$0	\$8,397	\$8,860	\$9,028
Equipment	\$0	\$3,158	\$0	\$0
TOTAL Expenditures	\$0	\$94,651	\$93,013	\$94,253
Funding of Expenditures:				
General Fund (01)	\$0	\$94,651	\$93,013	\$94,253
TOTAL Funding of Exp.	\$0	\$94,651	\$93,013	\$94,253
Revenues:				
General Fund (01)	\$0	(\$853,000)	(\$1,034,000)	(\$1,176,000)
TOTAL Revenues	\$0	(\$853,000)	(\$1,034,000)	(\$1,176,000)
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):				
General Fund (01)	\$0	(\$947,651)	(\$1,127,013)	(\$1,270,253)

Long-Term Impacts:

- The tax liability impact of the proposed change depends on the amount of property placed in the trust, and the taxpayers who have a spouse die. The revenue impact of this bill will significantly increase in future years when taxpayers with significant property and capital gains income die and the property that is placed in this trust has its basis stepped up. Because of this, the revenue impact of this bill is likely to change significantly in future tax years. For example, full-year resident taxpayers with capital gains income in excess of \$25 million in TY 2021 reported an average of \$168 million in capital gains income. Stepping up this income could reduce Montana’s income tax revenue by \$7.644 million (\$168,000,000 X 70% X 6.5%).

NO SPONSOR SIGNATURE

_____ 3/29/23 _____ AO _____ 3-29-23
 Sponsor’s Initials Date Budget Director’s Initials Date