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Progressive States Coordinate Wealth Tax Proposals

Did you know that seven states account for 60% of US household wealth? These states include California, New York, Illinois, Hawaii, Maryland, Minnesota, Washington, and Connecticut. Last week, these states introduced wealth tax bills in a coordinated effort to address what progressive Democrats view as historic levels of American economic inequality. A "wealth tax" typically refers to a tax based on net worth rather than income.

On the federal level, proponents of a wealth tax have not had much success. Recently Senator Elizabeth Warren of Massachusetts introduced the Ultra-Millionaire Tax Act, which aimed to impose a 2% tax on the net worth of households and trusts between $50 million and $1 billion and 1% on those over $1 billion. The Act never passed. Drafts of the Build Back Better (BBB) Act included other forms of wealth tax, such as a tax on unrealized gains. The BBB Act failed to pass in 2021. Now that Republicans control the house, progressive Democrats most likely understand that the chances of passing a wealth tax at the national level are even lower today.

Democrats are re-focusing their efforts at the state level. The proposed taxes target the ultra-wealthy. California's bill would require a 1.5% annual tax on worldwide assets of $1 billion and up. The tax is scheduled to take effect between 2024-2026, depending on when and if the bill is passed. One of New York's proposals adds a long-term capital gains tax. The bill mandates a 7.5% tax on long-term capital gains for taxpayers with income above $550,000 and 15% for taxpayers with income above $1.1 million. The current highest marginal rate in NY state is 10.9%, and the new tax increases the cap gains rate to approximately 26%. NY city residents pay a local tax, and their combined rate may be closer to 30%.

Critics of wealth taxes assert that they have a negative effect on the economy and encourage tax avoidance and offshoring of assets. A recent example of this behavior is when more than 2,000 millionaires fled NY during the pandemic. The migration followed a Covid relief budget tax increase where the marginal rate for those earning more than $1 million increased from 8.82% to 9.65%. An additional challenge to implementing a wealth tax is valuing assets regularly. Many sophisticated taxpayers own properties, business interests, and a variety of other illiquid assets that are difficult to value.

We will continue to monitor state-specific wealth tax proposals and keep you apprised of any that pass. If you have questions, please reach out to your wealth manager.