# Biden, tax, and how family offices will allocate their wealth

by **Michael Foster** 27th April 2021

President Joe Biden's plan to double US capital gains tax rates will have a big impact on the way family offices allocate their wealth.

The proposal will be fiercely fought, but if it is passed in its current form it could knock trading in assets like bitcoin and growth stocks while producing a tilt to long-term investment.

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Billionaire Tim Draper of Draper Associates warned the move would hit revenues at Silicon Valley and cut investment in new ventures, bringing job creation to a halt.

It could force private equity and venture capital to retain their portfolio investments for a longer period of time until the rate of CGT falls back.

Law firm Withers US-based partner William Kambas says: "I believe we shall see more capital invested in family businesses because they are a classic long-term enterprise. "

Jimmy Chang, CIO at Rockefeller Global Family Office, said the measure could trigger an exodus from US equities as investors seek to lock their gains at a lower rate before a new CGT rate becomes law.

Bitcoin fell sharply when reports of Biden's plan appeared in the media on 22 April but recovered on Monday, along with a string of growth stocks.

Thomas Hayes, chairman of Great Hill Capital, said the recovery took place because the current proposals would fail: "If it had a chance of passing, we'd be down 2,000 points."

Paul Nolte, portfolio manager at Kingsview Investment Management argued investors would start buying again, when they had crystallised their losses. Matthew Keator, managing partner of Keator Group, the family-owned adviser, expects stock sales but adds this could lead to a "tremendous amount" of M&A.

But securities traders said the market mood is a crucial factor. Stocks are still being pushed to record levels by low interest rates and investors are not in the mood to worry about CGT just yet.

According to new data from FINRA, debt taken out of buy stocks on margin has soared 71% in a year to hit a record $822 billion in March. Activist short-seller Nate Anderson tweeted: "This is a lurking disaster."

Biden is due to confirm his plan on Wednesday 28 April.

If he is not forced to compromise, consultant Steve Martiros of Martiros Strategies, says the new CGT rate should lead to a greater use of separate managed accounts (SMA).

He said: "In a co-mingled fund you have no ability to separate your tax requirements from everyone else. In an SMA your adviser can look after you in that respect, and invest your cash on a buy and hold basis, as required."

Biden is expected to limit the rise in corporation tax from 21% to 28%, against a pre-Trump level of 35%, which puts family businesses on a relatively good footing.

Biden intends to double CGT on individuals earning more than $1 million, taking the rate to 39.6%, in line with a higher level of income tax.  Obamacare contributions would take the total to 43.4%. This is close to 50%, particularly if you take account of state taxes, a level at which investors pay more for good tax advice.

One suggested proposal on inheritance tax could particularly impact property because it could require a tax liability on its original purchase price, rather than allowing the capital to "step up" to its current market value at the time of transfer.

Biden has separately said that individuals earning more than $400,000 could pay the new, higher rate of income tax.

The increase in CGT would mean that private equity firms whose partners get paid via carried interest would end up paying the doubled rate of CGT. According to one private equity manager: "I think most of us would see higher CGT as inevitable. But I am less convinced the proposed rate will come to pass. "

According to Kambas, private equity and venture capital partners will need to decide whether their portfolio holding periods of, say, five to seven years for their portfolio companies would still be tax efficient.

Further complications could result from private equity firms with a 5 to 7-year strategy overseas, if this leads to US investors in the fund suffering a tax hit.

Michael Sonnenfeldt founder of networking group Tiger 21 agrees that people sensitive to higher levels of tax tend to invest for longer periods of time.

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Tax sensitivity will also lead to a stronger focus on where family offices choose to base the businesses, according to Martiros. States which levy local CGT, such as New York and California, could suffer migrations to the likes of Texas and Nevada, which do not. Of course, that migration is already happening regardless of tax rises.

Active mutual funds which often incur CGT will lose more ground to passive managers because ETF are more tax efficient.

The situation could benefit philanthropy, according to Martiros, because individuals would prefer to give their money away than pay big tax bills.

Buy and hold strategies, as practised by Warren Buffett, are an even better bet, Martiros says, because they do not incur an annual CGT charge which chips away at capital available to invest, year by year.

The new regime could attract more investors to income stocks, as long as they can shelter their income.

In theory, real estate could also benefit as long-term investment, but Kambas warns the Democrats could try to close off a
of tax loopholes in the sector.