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A 5% wealth tax? Preparing clients for California's Billionaire Tax Act

California's proposed Billionaire Tax Act presents estate planners with significant challenges, including retroactive application, anti-abuse provisions and unresolved questions about its treatment of trusts.

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The proposed 2026 Billionaire Tax Act, which will appear as Proposition 40 on California's Nov. 3, 2026, ballot, would, if approved, impose a one-time excise tax of up to 5% on the net worth of certain individuals and trusts that have assets of at least \$1 billion as of Dec. 31, 2026. The CBTA is concerning for certain ultra-high net worth individuals and trust beneficiaries in California. It is also controversial because, if passed, it would apply retroactively and include anti-abuse provisions. Significant ambiguities and uncertainty remain in the details of the proposed rules, particularly as they apply to trusts, making effective planning challenging in the face of what remains unknown. This article discusses considerations that estate planners and advisors to ultra-high net worth individuals and trust beneficiaries should consider when advising such clients on the potential passage and application of the CBTA.

Grantor trusts

Grantor trusts contain certain powers that the grantor of a trust retains over the trust so that for income tax purposes, the grantor is treated as the owner of the trust. Grantor trusts can be revocable trusts, which the grantor retains full control of and are used to avoid probate, or they



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can be irrevocable trusts that completed gifts are made in order to remove assets from the grantor's estate for estate tax planning.

The assets of a grantor trust are considered part of an individual's net worth calculation to determine if the individual is subject to the one-time excise tax under the CBTA. For revocable trusts, this is logical and unsurprising, as a revocable trust is under the full dominion and control of a grantor. What is surprising about the proposed act is that assets held

in an irrevocable grantor trust that a grantor established for another beneficiary, such as a child, and made a completed gift to for federal estate and gift tax purposes, is includable back in the individual grantor's net worth for purposes of calculations of an individual's net worth and liability under the CBTA. This is a significant deviation from federal wealth transfer tax principles in which such trusts are typically no longer considered part of a grantor's net worth at death.

A client could theoretically have a net worth under \$1 billion personally, but if they transferred assets to an irrevocable grantor trust for their children and the trust has grown significantly, combining the two could put the client over the threshold. Practitioners should evaluate potential exposure to the CBTA when considering the value of grantor trusts that an individual has historically established for federal estate and gift tax planning.

Unless there is a revision to align the treatment of grantor trusts for CBTA purposes with federal wealth transfer principles, the fact that assets are held by a grantor trust, regardless of when transferred, is ineffective to mitigate potential exposure to the CBTA.

Irrevocable grantor trusts are often drafted to allow the grantor or trust protector to turn off the grantor trust status, which turns the trust into a non-grantor trust. This may be a planning opportunity, but should be exercised with caution, so as not to violate the anti-abuse rules.

Non-grantor trusts

A non-grantor trust is a separate tax paying entity that files its own income tax returns. The CBTA potentially implicates non-grantor trusts in two ways:

1. **Applicable trusts:** Any non-grantor, non-tax-exempt trust to which an applicable individual (a California resident as of Jan. 1, 2026,

with a net worth of \$1 billion or more as of Dec. 31, 2026) has transferred property is considered an applicable trust and subject to the excise tax. The tax applies to these non-grantor trusts whether or not the trust is administered in California or subject to California state income tax. Unlike individuals who must meet the \$1 billion net worth threshold themselves, a non-grantor trust is subject to the tax regardless of its size, as long as it received a transfer from a billionaire grantor. Trustees of such trusts should consider whether the grantor meets the individual threshold to be an applicable individual, which would then make the trust an applicable trust for CBTA purposes. If the trust is an applicable trust, the excise tax applies to the trust's net worth. The CBTA gives the applicable individual the option to include the assets of such non-grantor trusts in their net worth for tax purposes. However, the applicable individual should be cautious about doing so, as the payment of a non-

grantor trust's taxes could be treated as a gift from the taxpayer to the trust.

2. Distributable interests to beneficiaries: A trust beneficiary of any trust that is not an applicable trust is deemed to be the owner of trust assets that are "distributable" to the beneficiary. There is currently no guidance on what "distributable" means. Trusts vary widely on their distribution standards. In the absence of clear guidance, it seems reasonable to surmise that the less certain a beneficiary's right to the trust property is, the less likely the trust property is to be treated as distributable to them.

A common structure in estate planning is the pot trust, where one trust is administered for the benefit of a group of beneficiaries. The trustee may make unequal distributions among the beneficiaries. It is unclear under the CBTA whether each beneficiary would be apportioned their pro rata share of the trust. A planning opportunity may

exist to sever the pot trust into separate shares to reduce each beneficiary's distributable share below the \$1 billion threshold, but again, the anti-abuse rules should still be considered.

The application of the CBTA to trusts and beneficiaries remains one of the most complex and uncertain

areas of the proposed act. If the act passes, additional guidance will be needed to resolve these uncertainties. In the meantime, advisors in California should examine each client's unique circumstances to determine exposure to the CBTA, as it is not necessarily intuitive or aligned with federal wealth transfer tax principles.

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