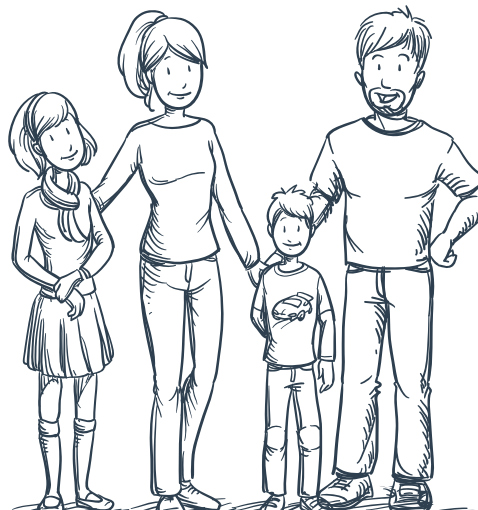




CRAIN & WOOLEY

Death & Taxes



An Introduction

Tax law is difficult, hard to learn, harder to keep up with as rules constantly change, and for many people – is simply a topic that they want to avoid (along with the actual taxes that result). The current tax code is 6,570 standard 8 ½ by 11 inch pages¹. This paper will provide a high level overview of how taxes work at death, which includes discussion concerning the Federal Estate Tax and the Federal Gift Tax with brief comment on State Estate Taxes.

Definition

The Estate Tax is a federal tax on property that is transferred as a result of a person's death. The unofficial term that people use to describe it is the *Death Tax*. The IRS defines the estate tax as, "a tax on your right to transfer property at your death"². The Internal Revenue Code states that,

"(a)Imposition.--A tax is hereby imposed on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States³.

History

Title 26, U.S. Code, the Internal Revenue Code (IRC), is where all of the federal tax laws of the United States can be found. U.S. tax laws began to be codified in 1874, but they were not centrally located in any one code until much later⁴. The first Internal Revenue Code didn't exist until 1939 and was subsequently revised in 1954 and most recently in 1986. The last extensive revisions made to the code were in 1986 and as of the writing of this paper, the current U.S. tax code found at Title 26 is known as The Internal Revenue Code of 1986⁵.

In the United States, the estate tax as we know it today began in 1916 as part of the Revenue Act of 1916⁶. (See Exhibit A – Excerpt from the Revenue Act of 1916)⁷

¹Title 26 – Internal Tax Code can be downloaded at: <https://uscode.house.gov/download/download.shtml>

²<https://www.irs.gov/businesses/small-businesses-self-employed/estate-tax>

³26 U.S.C.A. § 2001, I.R.C. § 2001

⁴https://www.census.gov/history/www/reference/privacy_confidentiality/title_26_us_code_1.html

⁵Pub. L. No. 99-514, § 2, 100 Stat. 2095 [Oct. 22, 1986]

⁶39 Stat. 756

Exhibit A: Revenue Act of 1916

SIXTY-FOURTH CONGRESS. SESS. I. CH. 463. 1916.

777

SEC. 25. That income on which has been assessed the tax imposed by Section II of the Act entitled "An Act to reduce tariff duties and to provide revenue for the Government, and for other purposes," approved October third, nineteen hundred and thirteen, shall not be considered as income within the meaning of this title: *Provided*, That this section shall not conflict with that portion of section ten, of this title, under which a taxpayer has fixed its own fiscal year.

INCOME TAX.
Income under former law not applicable hereto.

Proviso. Designated fiscal year.
Am., p. 766.
Post, p. 1004.

TITLE II.—ESTATE TAX.

SEC. 200. That when used in this title—
The term "person" includes partnerships, corporations, and associations;

Estate tax.

Construction of terms.
"Person."

The term "United States" means only the States, the Territories of Alaska and Hawaii, and the District of Columbia;

"United States."

The term "executor" means the executor or administrator of the decedent, or, if there is no executor or administrator, any person who takes possession of any property of the decedent; and

"Executor."

The term "collector" means the collector of internal revenue of the district in which was the domicile of the decedent at the time of his death, or, if there was no such domicile in the United States, then the collector of the district in which is situated the part of the gross estate of the decedent in the United States, or, if such part of the gross estate is situated in more than one district, then the collector of internal revenue at Baltimore, Maryland.

"Collector."

SEC. 201. That a tax (hereinafter in this title referred to as the tax), equal to the following percentages of the value of the net estate, to be determined as provided in section two hundred and three, is hereby imposed upon the transfer of the net estate of every decedent dying after the passage of this Act, whether a resident or nonresident of the United States:

Tax on transfers of estates of decedents hereafter.
Post, p. 1002.

One per centum of the amount of such net estate not in excess of \$50,000;

Rates.

Two per centum of the amount by which such net estate exceeds \$50,000 and does not exceed \$150,000;

Three per centum of the amount by which such net estate exceeds \$150,000 and does not exceed \$250,000;

Four per centum of the amount by which such net estate exceeds \$250,000 and does not exceed \$450,000;

Five per centum of the amount by which such net estate exceeds \$450,000 and does not exceed \$1,000,000;

Six per centum of the amount by which such net estate exceeds \$1,000,000 and does not exceed \$2,000,000;

Seven per centum of the amount by which such net estate exceeds \$2,000,000 and does not exceed \$3,000,000;

Eight per centum of the amount by which such net estate exceeds \$3,000,000 and does not exceed \$4,000,000;

Nine per centum of the amount by which such net estate exceeds \$4,000,000 and does not exceed \$5,000,000; and

Ten per centum of the amount by which such net estate exceeds \$5,000,000.

SEC. 202. That the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated:

Value of gross estate.

(a) To the extent of the interest therein of the decedent at the time of his death which after his death is subject to the payment of the charges against his estate and the expenses of its administration and is subject to distribution as part of his estate.

Property included. Subject to administration.

(b) To the extent of any interest therein of which the decedent has at any time made a transfer, or with respect to which he has created

Gifts, etc., in anticipation of death.

History, Con't.

The Federal Estate Tax in 1916 taxed the *transfer* of a wealth transaction from an estate to the estate's beneficiaries instead. This approach was different from an *inheritance tax* that would tax beneficiaries directly because the estate tax applied to net estates (defined as the total property owned by a decedent, less deductions). In 1916, there was an exemption of \$50,000 that would prevent the estate tax from applying to estates valued at \$50,000 or less. For estates valued at more than \$50,000, the tax rates were graduated beginning at 1 percent on the first \$50,000 to 10 percent on amounts over \$5 million.

Wealthy people quickly realized that they could gift assets during their life to avoid their estates having a value over \$50,000 and until 1924⁸, there was no gift tax to prevent this type of strategy. In 1926, the gift tax was repealed⁹, but was reintroduced by the Revenue Act of 1932¹⁰ at which time the gift tax became a permanent part of U.S. tax law.

Federal Estate Tax in 2020

The federal estate tax applies to assets of U.S. citizens and U.S. residents (a person domiciled in the United States) following their death. Assets subject to the tax can be located anywhere in the world¹¹. The current estate tax rate is 40%. U.S. citizens and residents receive the full estate tax exclusion amount. However, only U.S. citizens may take advantage of the unlimited marital deduction for transfers to a U.S. citizen spouse. If a person is not a U.S. citizen or resident, the estate tax only applies to assets owned in the United States at their death.

⁸The first gift tax was enacted in the Revenue Act of 1924, 43 Stat. 253.

⁹Revenue Act of 1926, 44 Stat. 9

¹⁰47 Stat. 169

¹¹26 U.S.C. §§ 2001, 2031, and 2051

What Is the Estate Tax Exclusion?

The estate tax exclusion amount is the maximum amount that a person can leave after death, combined with gifts made during life, free of estate tax¹². To determine if an estate is exempt from tax (either partially or fully), the total value of a person's estate when they die should be calculated and added together with the total taxable lifetime gifts that they made. If that total amount is less than the applicable exclusion amount in the year of the person's death, then the estate is exempt from the federal estate tax. For example, a person who dies in 2020 can have their estate value added to the total of the taxable gifts made during their lifetime. If it totals \$11,580,000 or less then the estate will be completely exempted from the federal estate tax. If the total estate **plus** lifetime taxable gifts is over \$11,580,000 in 2020, the 40% estate tax rate would apply to all dollars over the exemption amount for 2020.

What Is the Deceased Spousal Unused Exclusion Amount?

The DSUE is the amount of a spouse's estate tax exclusion amount that was not used on that spouse's death. This amount is considered portable and is available to the surviving spouse¹³. It is important to note that in order to take advantage of portability under current law, an estate tax return must be filed when a spouse dies.

Under previous laws, this was not always the case and spouses had to use difficult and complex tax planning strategies to attempt to allow both spouses to utilize their full estate tax exemption amounts. This resulted in many people executing trusts that would divide their assets during their lifetimes in an attempt to create equal value estates that could best take advantage of the tax law exemptions as written at that time. These are known as bypass or credit shelter trusts. In 2020, these complex tax planning provisions are no longer necessary to ensure that a surviving spouse receives unused estate tax exemptions from their deceased spouse.

¹²26 U.S.C. § 2010(c)(3)(B)

¹³26 U.S.C. § 2010(c)(4)

How Does the Gift Tax Relate to the Estate Tax?

The federal estate tax and the federal gift tax are now part of what is often referred to as the **unified transfer tax system**. This unified tax system combines gifts made during life and after death. To determine if someone owes gift taxes or estate taxes (or both), lifetime gifts and after death gifts must be compared to the current exclusion amount. If the gifts before and after death are less than the exclusion amount, no gift or estate tax is due. The exclusion amount for 2020 is \$11,580,000 (as depicted in Exhibits B and C)¹⁴.

Exhibit B

Year	Estate Tax Exemption	Top Tax Rate
1916	\$50,000	10%
1917	\$50,000	25%
1918-23	\$50,000	25%
1924-25	\$50,000	40%
1926-31	\$100,000	20%
1932-33	\$50,000	45%
1934	\$50,000	60%
1935-39	\$40,000	70%
1940	\$40,000	70%
1941	\$40,000	77%
1942-76	\$60,000	77%
1977	\$120,000	70%
1978	\$134,000	70%
1979	\$147,000	70%
1980	\$161,000	70%
1981	\$175,000	70%
1982	\$225,000	65%
1983	\$275,000	60%
1984	\$325,000	55%
1985	\$400,000	55%
1986	\$500,000	55%
1987-97	\$600,000	55%
1998	\$625,000	55%
1999	\$650,000	55%
2000-01	\$675,000	55%
2002	\$1,000,000	50%
2003	\$1,000,000	49%
2004	\$1,500,000	48%
2005	\$1,500,000	47%
2006-08	\$2,000,000	46%
2009	\$3,500,000	45%
2010	\$5,000,000 or \$0	35% or 0%
2011	\$5,000,000	35%
2012	\$5,120,000	35%
2013	\$5,250,000	40%
2014	\$5,340,000	40%
2015	\$5,430,000	40%
2016	\$549,000	40%
2017	\$549,000	40%
2018	\$11,180,000	40%
2019	\$11,400,000	40%
2020	\$11,580,000	40%

Exhibit B - Historical Estate Tax Rates

Exhibit C

Federal Transfer Tax	2019	2020
Estate Tax Basic Exclusion Amount	\$11,400,000	\$11,580,000
Estate Tax Exclusion for Non-US Persons	\$60,000	\$60,000
Lifetime Gift Tax Exemption Amount	\$11,400,000	\$11,580,000
Annual Gift Tax Exclusion Amount	\$15,000	\$15,000
Annual Gift Tax Exclusion Amount to NonCitizen Spouse	\$155,000	\$157,000
Estate and Gift Tax Rate	40%	40%

Exhibit C Transfer Taxes

¹⁴26 U.S.C. § 2505(a)(1)

Gifts of \$15,000

A person can donate or give \$15,000 per individual each year without tax consequences. The \$15,000 exclusion is officially called the **Annual Gift Tax Exclusion**¹⁵. This means that a person can give up to \$15,000 per year (per person receiving a gift) and not have to report the gift to the IRS. That \$15,000 gift is the maximum gift amount that can be given per person per year that is excluded from gift tax. However, there is also a **Lifetime Gift Tax Exemption**. The Lifetime Gift Tax exemption is \$11,580,000 for the year 2020, this amount is the same as the federal estate tax exemption.

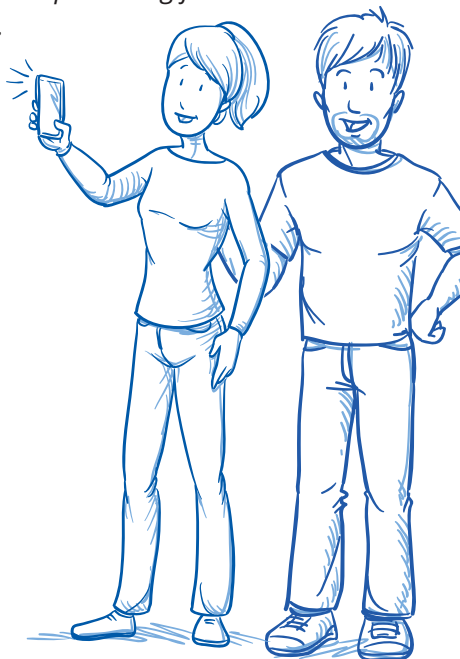
Gifts made over \$15,000 per year (per person receiving a gift) must be reported to the IRS and reduce that person's lifetime gift tax exemption and their federal estate tax exemption. This combination of gift tax and estate tax exclusion amounts is why the exclusion is called a unified credit (meaning the law combines lifetime gift and death gift totals against one exclusion/exemption amount). This means that no gift or estate tax is due until a person gives away more than the total exemption amount, which is \$11,580,000 (or \$23.16 million for married couples). If a person has not gifted more than the Lifetime Gift Tax Exemption, there is no gift tax due. For an overview of estate tax and gift tax exclusion and exemptions, see Exhibit C.



Example of \$15,000 Gifts

Greg gifts \$20,000 to each of his five children and to each of his ten grandchildren for Christmas in 2020 totaling \$300,000. The law in 2020 says that you don't have to report gifts of \$15,000 or less (per individual person you've gifted to). So for each of the children and grandchildren receiving \$20,000 – only \$5,000 has to be reported to the IRS (only the amount, per person, over \$15,000). For fifteen total people, \$5,000 each equals \$75,000 that has to be reported to the IRS (IRS Form 709). Reporting those gifts, however, does not automatically mean that Greg pays any tax because the Lifetime Gift Tax Exemption amount is \$11,580,000. Greg in this example has only used \$75,000 of his total \$11,580,000 exemption which means that he can still gift \$11,505,000 during his life before having to pay any gift tax.

When Greg dies – the total amount of his gifts made during his life must be added together with the gifts made after his death. As long as his lifetime gifts plus his gifts in death total \$11,580,000 or less, there will be no estate tax either. This means that if Greg dies after the gifts he made Christmas of 2020 without having ever given any more gifts and the value of his estate is less than \$11,505,000, there would be no estate tax. (\$11,580,000 exclusion minus the \$75,000 in reportable gifts that he made on Christmas of 2020 equals \$11,505,000).



Calculating How Much Estate Tax is Owed

In order to determine the amount of tax due by taxable estates, the following procedure should be followed:

1. Determine if U.S. estate tax law applies to the estate of a person who died.
2. For assets that are subject to U.S. estate tax law, the gross estate should be calculated by determining what property is subject to U.S. tax law and calculating the total value of that property.
3. The value of the gross estate should be reduced by any allowable deductions.
4. The value of the gross estate should be increased by any taxable gifts made during the person's lifetime.

Steps 1 through 4 result in the Tax Base.

5. Determine the estate tax exclusion for the year in which the person died and add that together with and Deceased Spousal Unused Exclusion Amount that is available. **This is the Total Estate Tax Exemption.**
 6. Compare the Tax Base to the Total Estate Tax Exemption amount. If the value of the Tax Base does not exceed the Total Estate Tax Exemption amount, the estate is exempt from the estate tax and no further calculation is needed. If the estate is not exempt,
 7. The Tax Base which must then be multiplied by the tax rate in 26 U.S.C. Section 2001(c). This result is the **Tentative Tax.**
 8. If the person who died has paid any gift taxes already during their life, those lifetime gift tax payments should be subtracted from the Tentative Tax to find the Gross Estate Tax.
 9. Finally, all available credits from the gross estate, the decedent's applicable credits, and any other credits, should be subtracted from the Gross Estate Tax to determine the **Final Tax Due.**
-

State Estate Tax in 2020

Although the focus of this paper is on the Federal Estate Tax, it is important to understand that multiple states impose state-specific taxes on the transfer of assets at death in addition to, or coordinated with, the federal estate tax. *Exhibit D* outlines the status of each state's laws in regards to a state estate tax and for states with the tax, a reference to the state law is provided for reference.

Exhibit D

State	Estate Tax	Statute
Alabama	No	
Alaska	No	
Arizona	No	
Arkansas	No	
California	No	
Colorado	No	
Connecticut	Yes	Conn. Gen. Stat. Ann. §§ 12-391and 12-392
Delaware	No	
D.C.	Yes	D.C. Code §§ 47-3702 to 47-3703
Florida	No	
Georgia	No	
Hawaii	Yes	Haw. Rev. Stat. §§ 236E-7 and 236E-8
Idaho	No	
Illinois	Yes	35 ILCS 405/2 and 405/3
Indiana	No	
Iowa	No	
Kansas	No	
Kentucky	No	
Louisiana	No	
Maine	Yes	36 M.R.S. §§ 4103and 4104
Maryland	Yes	Md. Code Ann., Tax-Gen. § 7-309(b)
Massachusetts	Yes	M.G.L. ch. 65C, § 2A(e)
Michigan	No	
Minnesota	Yes	Minn. Stat. Ann. § 291.01
Mississippi	No	
Missouri	No	
Montana	No	
Nebraska	No	
Nevada	No	
New Hampshire	No	
New Jersey	No	
New Mexico	No	
New York	Yes	N.Y. Tax Law § 952
North Carolina	No	
North Dakota	No	
Ohio	No	
Oklahoma	No	
Oregon	Yes	Or. Rev. Stat. § 118.010
Pennsylvania	No	
Rhode Island	Yes	R.I. Gen. Laws § 44-22-1.1(a)(2), (3)
South Carolina	No	
South Dakota	No	
Tennessee	No	
Texas	No	
Utah	No	
Vermont	No	32 V.S.A. § 7442a
Virginia	No	
Washington	Yes	RCW 83.100.040
West Virginia	No	
Wisconsin	No	
Wyoming	No	

Exhibit D - State Estate Tax

Conclusion

Taxes are difficult. Failing to evaluate how taxes apply at death or failing to take action on those considerations may result in severe and surprising results. Some important taxes to review are the Federal Estate Tax, Federal Gift Tax, and State Gift Tax. Make sure that you work with someone who is qualified and able to assist you with reviewing and acting on the taxes applicable to you.

Working with Crain & Wooley

Any licensed attorney can write a Will or Trust for you; however, very few dedicated themselves solely to the art and science of estate planning. We do! We practice solely in the area of estate planning thereby providing our clients best-in-class service supported by up-to-date, best practices.

As for online “legal” self-help, it’s typically generic and does not meet state-specific rules nor does it necessarily meet your specific needs and goals as an individual. We can.

Crain & Wooley is a full-service estate planning firm with expertise in Trust Creation, Will Creation, Probate Services, Adult Guardianship, Nursing Home (Medicaid) Qualification, Business Planning, Asset Protection, and Reviewing as well as Updating Existing Plans.

At Crain & Wooley, you will never receive a surprise legal bill. We are upfront with our pricing for proactive estate planning. Learn more about our flat-rate prices on our website www.crainwooley.law/flat-rate-services.



Justin T. Crain

Justin T. Crain has been recognized by the Texas Bar College as one of the best-trained attorneys in Texas. Justin practices exclusively in estate planning and settlement.



Jacob K. Wooley

Jacob K. Wooley’s experience with businesses and families allows him to address a wide range of estate planning issues.

Disclaimer: Information presented is for general educational purposes only and does not constitute legal advice. Crain & Wooley encourages you to meet with a qualified attorney to learn more about your unique situation.

Our Services

Crain & Wooley provides expert service in the following areas:

- Standard and complex Trust creation
- Standard and complex Will creation
- Primary and ancillary probate
- Adult guardianship
- Nursing home qualification (Medicaid)
- Existing document review and update
- Business continuity planning
- Small business formation

Contact Us

Law Office of Justin T. Crain, PLLC
DBA Crain & Wooley

PLANO – PRINCIPAL OFFICE
660 North Central Expressway Ste 210
Plano, TX 75074

972-560-6288

justin@crainwooley.law
joy@crainwooley.law
www.crainwooley.law

Jacob K. Wooley, PLLC
DBA Crain & Wooley

MANSFIELD
1703 Fountainview Dr., Suite 103
Mansfield, TX 76063

682-422-3495

jacob@crainwooley.law
joy@crainwooley.law
www.crainwooley.law



CW
CRAIN & WOOLLY

www.crainwooley.law