

MINNESOTA • REVENUE

ESTATE TAX & GIFT TAX Unified Transfer Tax

March 11, 2014

Department of Revenue
Analysis of H.F. 2108 (Lenczewski)
As Proposed to be Amended (H2108DE1)

	Yes	No
DOR Administrative Costs/Savings	X	

	Fund Impact			
	<u>F.Y. 2014</u>	<u>F.Y. 2015</u>	<u>F.Y. 2016</u>	<u>F.Y. 2017</u>
	(000's)			
Estate Tax	\$0	(\$6,100)	(\$8,800)	(\$9,400)
Gift Tax	(\$700)	\$3,000	\$3,300	\$3,900
General Fund Total	(\$700)	(\$3,100)	(\$5,500)	(\$5,500)

The estate tax is effective for estates of decedents dying after December 31, 2013.

The gift tax is effective for gifts made after June 30, 2013, provided that the maximum rate of tax is 10% for gifts made before January 1, 2014.

EXPLANATION OF THE BILL

The current Minnesota estate tax is determined by calculating two different tax amounts based on two different tax rate tables found in pre-2001 federal estate tax statutes. The resulting Minnesota estate tax is the minimum of those two different tax amounts. In most cases, the resulting marginal tax rate structure looks like the current tax rates in the table below. The high 41% rate, which comes from one of the old federal tables, is known as “the bubble”.

The proposal eliminates the “bubble” and creates a stand-alone estate tax rate structure. In effect, the exclusion amount is raised from \$1 million to \$1.5 million. Some rates are increased. The current and proposed rate structures are as follows:

----- Taxable Estate Range -----		Current	Proposed
Over	But Not Over	Tax Rate	Tax Rate
\$0	\$1,000,000	0%	0%
\$1,000,000	\$1,093,785	41.0%	0%
\$1,093,785	\$1,100,000	5.6%	0%
\$1,100,000	\$1,500,000	6.4%	0%
\$1,500,000	\$1,600,000	6.4%	12%
\$1,600,000	\$2,100,000	7.2%	12%
\$2,100,000	\$2,600,000	8.0%	12%
\$2,600,000	\$3,100,000	8.8%	12%
\$3,100,000	\$3,600,000	9.6%	12%
\$3,600,000	\$4,000,000	10.4%	12%
\$4,000,000	\$4,100,000	10.4%	14%
\$4,100,000	\$5,100,000	11.2%	14%
\$5,100,000	\$6,000,000	12.0%	14%
\$6,000,000	\$6,100,000	12.0%	16%
\$6,100,000	\$7,100,000	12.8%	16%
\$7,100,000	\$8,100,000	13.6%	16%
\$8,100,000	\$9,100,000	14.4%	16%
\$9,100,000	\$10,000,000	15.2%	16%
\$10,000,000	\$10,100,000	15.2%	18%
\$10,100,000		16.0%	18%

EXPLANATION OF THE BILL (Cont.)

The maximum small business and farm property deduction is reduced from \$4 million to \$3.5 million.

Currently, Minnesota statutes require that adjusted taxable gifts made by the decedent after June 30, 2013, and made within three years of death, be included in Minnesota taxable estate. This provision is changed to require that all Minnesota taxable gifts made by the decedent after June 30, 2013, be included in Minnesota taxable estate.

The proposal also authorizes a Minnesota QTIP (Qualified Terminable Interest Property) which should have no fiscal impact since it is intended to simplify the way in which a QTIP is elected, eliminating the requirement to file a federal estate tax return when a federal return would not otherwise have to be filed.

If a qualified work of art owned by a nonresident is on loan to a 501(c)(3) organization located in Minnesota, the situs of the art is deemed to be outside of Minnesota.

The proposal changes the way the estate tax is calculated for resident decedents who had property located outside of Minnesota. Currently, a ratio of Minnesota gross property to total gross property is calculated. That ratio is then applied to the tentative estate tax resulting from applying the tax tables to the total taxable estate, resulting in a reduced tax owed to Minnesota. Under the proposal, the ratio is no longer applied to the tentative estate tax. Instead, the tentative tax is reduced by a credit for estate tax paid to the other state for the decedent's property in that state.

In 2013 a gift tax was enacted, effective for gifts made after June 30, 2013. Currently, the gift tax is equal to 10% of Minnesota taxable gifts. There is a lifetime credit of \$100,000 that can be used to offset any gift tax that would otherwise be owed to Minnesota. For property sited in Minnesota, Minnesota recognizes the definition of federal taxable gifts. For 2014, the first \$14,000 of total gifts given to one individual by a donor in one year would not be considered taxable. Anything over \$14,000 would be considered taxable.

Under the proposal, the gift tax rates would be changed for gifts made in 2014 or later to be the same as the proposed estate tax rates. The rates would be applied to the aggregate of Minnesota taxable gifts made by a donor during the donor's lifetime. A credit would be allowed against the tax for any gift tax paid on gifts included in Minnesota taxable gifts on any prior Minnesota gift tax return. This results in the unification of the gift tax and the estate tax into a unified transfer tax.

EXPLANATION OF THE BILL (Cont.)

The gift tax rates are as follows:

----- Taxable Gift Range -----		Proposed
Over	But Not Over	Tax Rate
\$0	\$1,500,000	0%
\$1,500,000	\$4,000,000	12%
\$4,000,000	\$6,000,000	14%
\$6,000,000	\$10,000,000	16%
\$10,000,000		18%

For gifts made before January 1, 2014, the maximum gift tax rate is 10%.

The proposal authorizes a penalty if a Minnesota gift equals or exceeds \$100,000 and a Minnesota gift tax return is not filed. A penalty of up to \$25,000 is imposed if a gift tax return is required to be filed even if the amount of the gift tax would have been equal to zero.

Grantor retained annuity trusts (GRATs) are included in the definition of taxable gifts.

The proposal also enacts various administrative provisions that are necessary to implement a unified transfer tax. In addition, a number of provisions are repealed.

REVENUE ANALYSIS DETAIL

Estate Tax

- A database of estate tax returns filed in 2012 and 2013 was created and used for this analysis.
- Returns received for the twelve months from July 2012 through June 2013 were used.
- Because the estate tax statutes were changed during the 2013 legislative session, the estate taxes for returns in the database were recalculated to reflect those 2013 changes.
- The proposed tax rates were then used to recalculate the estate taxes for the returns in the database.
- One hundred percent of adjusted taxable gifts were included in the taxable estate.
- Using the proposed rates, the total estate tax for returns in the database decreased by 6.6%.
- Using the returns in the database, it was estimated that the proposed change in the way the estate tax would be calculated for deceased residents with non-Minnesota property would change the above decrease to 4.1%. That percentage change was applied to the estate tax estimates in the February 2014 estate tax forecast.
- It is assumed that the estate tax is paid nine months after the death of the deceased.

REVENUE ANALYSIS DETAIL (Cont.)

Gift Tax

- Information on gifts subject to the federal gift tax was obtained from the IRS website for returns filed in 2009, 2010, and 2011. Included in the data was information (counts and amounts) based on the size of the taxable gifts. The data for the three years was averaged and used for the base year of 2010 instead of the actual 2010 data.
- This analysis assumes that the Minnesota pattern of giving will be similar to the federal pattern of giving.
- The Internal Revenue Service, Statistics of Income (SOI) Division website contains state information on wealthy individuals in the United States. The 2007 data was for individuals with a net worth of at least \$2,000,000. Based on the data in the table, 1.3% of the wealthy individuals were in Minnesota. They had 1.36% of the wealth. Using the data from the SOI Division website, the federal gift tax data was apportioned to Minnesota.
- The amount of taxable gifts was assumed to increase at 2% per year.
- The federal data was also used estimate the percent of repeat donors. For this analysis it was assumed that the percentage of repeat donors in years two through four will be 12.5%, 25%, and 37.5% respectively.
- The federal data for the highest amount category (\$1,000,000 and above) was extrapolated to better estimate the effect of gifting at higher amounts.
- Using the proposed rate structure, the proposed Minnesota gift tax was estimated.
- This proposed Minnesota gift tax was then compared to the gift tax estimate in the February 2014 forecast.
- For purposes of this analysis, it is assumed that taxable gifts made and gift taxes paid will have no effect on the estate tax during the period of this analysis.

Source: Minnesota Department of Revenue
Tax Research Division
[www.revenue.state.mn.us/research_stats/Pages/
Revenue-Analyses.aspx](http://www.revenue.state.mn.us/research_stats/Pages/Revenue-Analyses.aspx)