

MINNESOTA • REVENUE

ESTATE TAX Conform to Federal Exclusion Change Tax Rate Structure

January 28, 2015

Department of Revenue
Analysis of H.F. 82 (Loon) / S.F. 198 (Koenen)

	Yes	No
DOR Administrative Costs/Savings	X	

	Fund Impact			
	<u>F.Y. 2016</u>	<u>F.Y. 2017</u>	<u>F.Y. 2018</u>	<u>F.Y. 2019</u>
General Fund	(\$68,400)	(\$101,900)	(\$98,300)	(\$93,700)

Effective for estates of decedents dying after December 31, 2014.

EXPLANATION OF THE BILL

Current Law: In the 2014 legislative session, the Minnesota estate tax was changed to a stand-alone tax. In conjunction with those changes, the amount of taxable estate excluded from taxation increases incrementally by \$200,000 per year from \$1.2 million for decedents who died in 2014 to \$2.0 million for decedents who die in 2018 and later. The tax rates vary from a low of 9% (2014) or 10% (2015 and later) to a high of 16%.

An estate is required to file a Minnesota estate tax return if it is required to file a federal estate tax return or if the value of the federal gross estate plus federal adjusted taxable gifts made within three years of death exceeds the Minnesota exclusion amount. Federal law requires an estate to file a federal estate tax return if its combined gross assets plus the decedent's prior taxable gifts exceed \$5.43 million for estates of decedents dying in calendar year 2015. The \$5.43 million amount is increased for inflation in later years.

The maximum small business and farm subtraction was reduced incrementally by \$200,000 per year from \$3.8 million for decedents who die in 2014 to \$3.0 million for decedents who die in 2018 and later. If an estate makes use of the small business and farm subtraction and if a qualified heir of the estate disposes of qualified small business or farm property within three years of the death of the decedent, a recapture tax is imposed. The amount of the recapture tax is 16% of the amount of the small business and farm subtraction claimed when the estate tax return was filed.

Proposed Law: The proposal changes the filing requirement so that an estate is required to file a Minnesota estate tax return only if it is required to file a federal estate tax return.

The subtraction for small business and farm property is repealed, as is the associated recapture tax.

EXPLANATION OF THE BILL (Cont.)

A subtraction is created that is equal to the amount of the decedent's applicable federal exclusion, which is defined in federal law. The applicable federal exclusion consists of the basic exclusion amount (\$5.43 million in 2015, increased for inflation in later years) plus the deceased spousal unused exclusion. This exclusion is the amount of the federal exclusion that was not used by the decedent's last spouse, provided that the spouse died after December 31, 2010, and the spouse's estate elected to transfer the unused amount on a federal estate tax return.

The bill also changes the estate tax rate structure. Under current law, the tax rates apply to Minnesota taxable estate. The annual amount excluded (for example, \$1.4 million in 2015) is not subtracted to arrive at Minnesota taxable estate, and a 0% rate applies to the excluded amount. Under the proposal, the definition of Minnesota taxable estate is changed to be the amount after subtracting the federal exclusion. For 2015, the proposed tax rates apply to a taxable estate amount that is generally \$5.43 million lower than the taxable estate under current law. Under current law, the 16% rate applies to the taxable estate over \$10.1 million. Under the proposal, the 16% rate applies to the taxable estate (before subtracting the exclusion) over \$15.53 million.

REVENUE ANALYSIS DETAIL

- A database of estate tax returns filed in 2012 through 2014 was created and used for this analysis.
- The estate tax statutes were changed in 2013. The estate taxes for returns in the database were recalculated to reflect those 2013 changes because most of the returns were filed before the 2013 changes were in effect.
- The proposed amount excluded from taxation and the proposed tax rates were then used to recalculate the estate taxes for the returns in the database.
- The basic exclusion amount is increased based on Consumer Price Index projections published by IHS Global Insights, Inc., in December 2014. Basic exclusion amounts are assumed to be \$5.44 million for deaths in 2016, \$5.55 million for 2017, and \$5.66 million for 2018.
- Using the exclusion amounts along with the proposed rate structure, the total estate tax for returns in the database decreased by 68.5% in 2015 and 2016, 69.0% in 2017, and 69.4% in 2018. These percentage changes were applied to the estate tax estimates in the November 2014 estate tax forecast.
- While the long-term impact of the portability of the exclusion amount will probably be significant, the impact for the duration of this analysis should be small. For purposes of this analysis, an additional impact of two percentage points was assumed.

REVENUE ANALYSIS DETAIL (Cont.)

- Because the returns in the database reflect the estate tax before the 2014 law changes, appropriate adjustments to the calculation were made in order to apply the percentage reduction factors.
- It is assumed that the estate tax is paid nine months after the death of the deceased.

Number of Taxpayers: It is estimated that approximately 1,500 estates will file estate tax returns under current law for 2015, with about 800 of these owing tax. This proposal is expected to reduce the number of filers to approximately 160 for 2015, with less than 100 owing tax.

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)