

ESTATE PLANNING & TAX

UPDATE

What is the current status of the federal estate and gift tax?

On January 2, 2013, the American Taxpayer Relief Act of 2012 (the "2012 Tax Act") was signed into law. Under the 2012 Tax Act, the top federal estate, gift and generation-skipping transfer (GST) tax rate is 40%, representing an increase from the prior top rate of 35%. However, the 2012 Tax Act also made permanent the \$5 million federal estate, gift and GST tax exemptions originally enacted in 2010, indexed for inflation. This means that if an individual dies with assets worth less than \$5.34 million in 2014 (\$5 million indexed for inflation) and has made no taxable gifts during his or her life, such person's estate will not be subject to federal estate tax. This rule also means that an individual may make up to \$5.34 million of gifts during his or her life without paying gift tax, though taxable gifts during life reduce the federal estate tax exemption available at death. The inflation-indexed \$5 million exemption is the highest exemption in history. For example, as recently as 2001 the estate and GST tax exemption was \$675,000 per person.

In addition to the 2012 Tax Act changes, the federal gift tax annual exclusion increased from \$13,000 in 2012 to \$14,000 in 2013, where it remains for 2014. As a result, any individual may gift up to \$14,000 to an unlimited number of other persons without having to file a gift tax return or use any portion of the donor's lifetime gift tax exemption (now \$5.34 million).

How have federal income tax laws changed recently?

While the 2012 Tax Act did not change income tax rates for most taxpayers, those individuals with incomes over \$400,000 and married couples filing jointly with incomes over \$450,000 are now subject to a highest marginal rate of 39.6%, up from 35%. A 20% rate now applies to long-term capital gains and dividends of these higher income taxpayers, though taxpayers with incomes below the \$400,000 (for individuals) and \$450,000 (for married couples filing jointly) continue to be subject to 15% and 0% rates on capital gains and dividends, depending on their taxable income. Combined with the new 3.8% Medicare tax on investment income, the maximum rate on long-term capital gains and dividends can now be as high as 23.8%.

The 2012 Tax Act also reinstated the personal exemption phaseout and the so-called "Pease" limitation on itemized deductions. Generally speaking, the reinstatement of these provisions can result in increased income taxes for higher income tax payers.

What about the Washington state estate tax?

The state legislature made significant changes to Washington's estate tax in 2013. Under the new law, the Washington state \$2 million estate tax exemption (the "applicable exclusion amount"), will be adjusted annually for inflation. The legislature also increased the top state estate tax rates by 1%, so that the highest rate (applicable to "Washington taxable estates" over \$9 million) is now 20%, rather than 19%. Very generally, the "Washington taxable estate" equals the decedent's property in excess of the \$2 million (adjusted for inflation) applicable exclusion amount, after any deductions are taken. There is also a new family-owned business deduction, which imposes very specific requirements and potentially exposes heirs to personal liability if the heir fails to materially participate in the family business, or transfer the interest to third parties.

Are there any other changes of which to be aware?

The Washington state legislature also modified certain aspects of the Washington Trust Act, including generally easing annual notice requirements for many trustees. In the most recent session, the legislature enacted a transfer-on-death deed statute, which generally allows real property to be transferred at death under certain circumstances without a probate.

Is there any other reason to contact MPBA?

In many cases, revisions to your estate plan are driven not by changes in law, but by changes in your life. It is generally advisable to review your estate planning documents every few years to make sure you remain satisfied with the proposed distribution of your estate (the persons you have named as your beneficiaries and the shares each beneficiary is to receive), and the persons you have named as your fiduciaries (e.g., the Personal Representative of your estate and your attorney-in-fact). Additionally, changes to your family situation may necessitate further changes to your documents. For example, if you have adopted children or grandchildren, or had children or grandchildren born out of wedlock, your Wills may direct that such persons are not beneficiaries of your estate. Thus, it is critical that you ensure your documents treat such persons as you desire. Please be sure to let us know if this issue (or any other personal issue you feel requires specific attention) applies to you.