HOUSE RESEARCH
Bill Summary

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Overview

This bill substantially restructures the estate and gift taxes. The changes include:

- Unifying the two taxes to providing one (that is, a combined) exemption of $5 million for both taxes (rather than separate $1 million exemptions under each of the taxes as under present law).
- Modifying the rate structures to be a unified stand-alone tax (rather than being based on the old federal credit for state death taxes for the estate tax or a flat 10 percent rate for the gift tax) with rates ranging from 16 percent to 20 percent.
- Making technical and administrative changes, particularly to make the gift tax administrative and compliance provisions consistent with the estate tax.

The estate changes generally are effective for decedents dying after December 31, 2013, and for gifts the bill is retroactive to imposition of the gift tax (gifts made after June 30, 2013).

<u>**Section**</u>

1 **Transferee liability.** Extends the transferee liability under the estate tax to the gift tax. This makes the recipient of a taxable gift liable for the tax, if the donor fails to file and pay. It replaces a provision in section 292.17, which is eliminated in section 26. The obligation of a personal representative to pay, if the donor dies before paying, parallels federal law. These provisions replace similar provisions in section 292.21, which is repealed by section 33.

2 **Tax administration.** Adds the gift tax to chapter 289A, the general tax administration chapter that also applies to the estate tax, as well as the individual income, corporate, sales,

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and mining occupation taxes.

3 **Definitions.** Adds a reference to the gift tax chapter's definitions in chapter 289A.

4 **Return requirement.** Modifies the return filing requirement to reflect the increase in the exemption amount in section 22 and to include all lifetime taxable gifts (present law is limited to taxable gifts made within three years of death) and transfers the gift tax return filing requirement from chapter 292, the gift tax chapter, to chapter 289A, the general tax administration chapter.

5 **Gift tax return; documents required.** Adds gift tax to the commissioner's authority to specify what documents must be filed with the tax return.

6 **Gift tax return; definitions.** Provides definitions under the gift tax chapter apply to the estate and gift tax return section.

7 **Estate tax return.** Eliminates obsolete language relating to estate tax returns for deaths during 2010.

8 **Gift tax return, filing deadline**. Specifies gift tax returns must be filed by April 15 of the year following the year in which the gift was made. (This is transferred from section 292.19, which is repealed by section 33.)

9 **Estate tax returns, extensions.** Makes nonsubstantive changes in the language providing for extensions of time to file estate tax returns.

10 **Gift tax returns, extensions.** Provides that the federal extensions to file gift tax returns also apply to Minnesota gift tax returns.

11 **Gift tax payment date.** Specifies gift tax must be paid by April 15 of the year following the year in which the gift was made. (This is transferred from section 292.21, which is repealed by section 33.)

12 **Extensions to pay estate tax.** Makes nonsubstantive changes in the language providing for extensions of time to pay estate tax.

13 **Extensions to pay gift tax.** Authorizes the commissioner to extend the time to pay gift tax for good cause and extends the time to pay, if a federal extension applies.

14 **Audit and assessment authority.** Provides that the commissioner's authority to audit and assess estate tax also applies to the gift tax. This replaces authority now in chapter 292, which is repealed by section 33.

15 **Statute of limitation extension; omissions of 25 percent or more.** Provides the extension of the statute of limitations to 6-1/2 years applies to omissions of taxable gifts of 25 percent or more. This parallels the similar provision under income, sales, and estate taxes.

16 **Notification of federal changes.** Adds gift tax to the statute requiring taxpayers to notify the commissioner of changes reported to, agreed to or ordered by the Internal Revenue

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Service on the federal return. This requirement is currently in chapter 292.

17 **Refunds of gift tax.** Adds gift tax to the chapter 289A provision providing for refunds of overpayment of taxes. This requirement is now in section 292.21, which is repealed by section 33.

18 **Interest on gift tax refunds.** Provides interest on refunds will be paid from the latest of (1) the overpayment, (2) the due date of the return, or (3) the date the original return was filed.

19 **Penalty, failure to pay gift tax.** Applies the late payment penalty applicable generally to other taxes to the gift tax.

20 **Estate tax definitions.** Eliminates the definition of "adjusted taxable estate" to reflect that section 21 changes the tax computation to be based on the Minnesota taxable estate.

The restriction on the definition of personal property with a Minnesota situs to that given within three years of death is eliminated. This reflects that computations will take into account all taxable gifts made after June 30, 2013, the effective date of the gift tax, and makes the estate and gift taxes consistent.

The exemptions for qualified small business and farmland property are repealed, since the general exemption increase to $5 million equals the current combination of the general exemption and the special exemptions.

Expands the look-through provision that applies to Minnesota property owned by a pass-through entity to apply to the gift tax, as well as the estate tax, by striking the limitations to property owned by a decedent. (The estate tax definitions also apply to the gift tax.)

21 **Minnesota taxable estate.** Defines Minnesota taxable estate, the tax base to which the rates under section 22 apply, as:

Federal taxable estate, plus

1. The deduction for state and foreign death taxes
2. The amount of taxable gifts made after June 30, 2013 (i.e., gifts subject to the Minnesota gift tax)
3. Any Minnesota gift tax paid by the decedent within three years of death (this parallels the similar computation under the federal estate tax for federal gift tax); less

22 **Estate tax computation.** Creates a stand alone estate tax rate schedule and increases the estate tax exemption from a *de facto* $1 million amount (which is not a true exemption because estates with values just above the exemption amount are subject to higher effective tax rates) to a true exemption of $1.5 million:

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Minnesota taxable estate	Tax rate
$5 million or less	0
$5 million up to $7 million	16%
$7 million up to $10 million	18%
Over $10 million	20%

Under present law, the tax rate schedule is based on the intersection of the repealed federal credit for state death taxes, the old federal estate tax rate schedule, and the old federal unified credit. These complex computations result in a rate schedule that imposes no tax on estates (including taxable gifts made within three years of death) of $1 million or less; a 41 percent tax on the value of the estates between $1 million and about $1,094,000, and rates ranging from 5.6 percent to 16 percent (with the top rate applicable to estate values over $10,100,000).

23 **QTIP election.** Provides that Minnesota taxable estate reflects the value of qualified terminable interest property (QTIP) elections allowed under federal law. An estate may make this election for Minnesota purposes, even if it is not required to file a federal return. (Under present law, Minnesota only recognizes QTIP elections made under the federal estate tax.) If the estate is required to file a federal return, the QTIP election must be made consistently for federal and Minnesota purposes.

Background. QTIP trusts are a standard estate tax planning tool for married couples. They allow electing the amount of the trust that will qualify for the marital deduction. The value of the QTIP property qualifies for the marital deduction (avoiding estate tax on the death of the first spouse), although only a limited income interest is provided to the surviving spouse. To be QTIP property:

- The property must be owned by the decedent.
- The surviving spouse must have a right to all of the income, payable at least annually, from the property for life.
- No one else may have a power of appointment over the property until the surviving spouse dies.
- A QTIP election must be made.

24 **Credits.** Allows the following credits against estate tax:

- Minnesota gift tax paid on gifts included in the taxable estate, unless the property was deductible as qualified farm or small business property
- Inheritance or estate tax paid by the estate of a nonresident decedent to another state on property subject to Minnesota estate tax because the property is owned by a pass-

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through entity (This credit is allowed under present law, section 291.03, subdivision 1c, which is repealed by section 33, and moved to the new general credit section of the estate tax.)

25 **Gift tax definitions.** Adds a definition of Minnesota taxable gifts that excludes gifts of tangible property located outside of Minnesota when the gift is made by a nonresident. (This is currently provided by an exclusion from the tax base, which is repealed by section 33.)

This section also:

- Changes the definition of resident by eliminating the cross reference to the income tax and specifically providing that residency is based on domicile when the gift was made.
- Clarifies that donations to section 527 political organizations are not subject to tax and that contributions to 529 Plans receive the same treatment as under the federal gift tax. (Both of these confirm administrative guidance provided by DOR.)

26 **Imposition.** Eliminates the ten-percent tax rate, which is replaced by the graduated rate structure in section 27, and eliminates the specification of liability, which is replaced by the provision in section 1 and amendments to chapter 298A.

27 **Tax rates.** Replaces the flat ten-percent rate of the gift tax under present law with graduated rates equal to the estate tax rates under section 22.

28 **Application of federal rules.** Provides that the commissioner has authority to apply federal gift tax rules in administering the tax. This language is moved from section 292.21, which is repealed by section 33.

29 **QTIP election.** Allows a Minnesota QTIP election for gift tax purposes under rules similar to those provided in section 23 for the estate tax.

30 **Credits.** Provides the following gift tax credits:

- Gift tax paid on prior returns – this ensures that the graduated rates apply on a lifetime basis to the sum of the donor's gifts over the lifetime exemption amount.
- Nonresident tax credit – this is similar to the nonresident estate tax credit as described in section 24 that ensures that a gift of Minnesota property held in a pass-through entity that is subject to both Minnesota gift tax and that of another state is not double taxed. (At present, only Connecticut imposes a gift tax; however, a number of states include gifts made in contemplation of death or a short time before death in their estate or inheritance taxes.)

31 **Appraisals of property.** Makes a cross reference change to reflect the changes in section 25.

32 **Definition of taxable gift for decedents dying before January 1, 2014.** Provides a definition of taxable gift for estate tax purpose for decedents dying in 2013, parallel with the

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bill's provisions in section 25. This confirms DOR's administrative policies.

33 **Repealer.** Repeals the following statutes (most of which are replaced by provisions moved to chapter 289A):

Statute	**Description**
290.01, subd. 20e	Obsolete income tax provision related to federal elections
291.03, subd. 1b	QTIP property for decedents dying in 2010 – obsolete
291.03, subd. 1c	Nonresident decedent estate tax credit – replaced by section 24
291.03, subd. 8	Definitions used in the small business and farmland exemptions
291.03, subd. 9	Qualified small business property
291.03, subd. 10	Qualified farm property
291.03, subd. 11	Recapture tax under the qualified small business and farm property exemption
291.41 – 291.47	Uniform act to resolve interstate disputes over domicile – this statute has never been used by DOR
292.17, subds. 2 and 3	Gift tax's lifetime credit and exclusion for out-of-state gifts – this is replaced by the tax rate schedule and the allowance of a credit for gift tax paid in prior years under sections 27 and 30
292.18	Gift tax return requirement, replaced by sections 8 and 5
292.19	Gift tax filing requirements, replaced by sections 8 and 10
292.21	Gift tax administrative provisions, replaced by various amendments to chapter 289A