

Estate Tax Essentials for Maximizing Exemptions

By Sarah B. Bowman

State and federal estate and gift taxes are always an important consideration for estate planning. This is even more important while exemptions against the taxes are at an all-time high.

The federal estate and gift tax exemption reflects the total combined amount any U.S. person may transfer to another person or persons during life or at death, combined, without owing gift or estate tax. Since these exemptions are annually adjusted for inflation, they increased this year by \$860,000 per taxpayer estate to an all-time high of \$12,920,000, or \$25,840,000 for married couples. Any transfers in excess of this amount are subject to a 40 percent federal gift or estate tax.

There may be limited time to take advantage of these high federal exemptions. Under the 2017 Tax Cuts and Jobs Act, the base amounts of the lifetime federal gift and estate tax exemptions doubled. However, unless Congress acts, that increase will expire at the end of 2025. Without Congressional action, in January 2026 the then-existing federal exemptions effectively will be cut in half.

Federal law also imposes a generation-skipping transfer tax (GST tax) on certain transfers of wealth to individuals two or more generations below the transferor to discourage taxpayers from trying to avoid taxes generally imposed at each generation level. The GST tax serves as a second tax when the taxpayer's gift or bequest skips a generation. The GST tax exemption matches the federal gift and estate tax exemption of \$12,920,000 and is also slated to be reduced after 2025.

In addition to the lifetime federal gift, estate and GST tax exemptions, federal law allows an additional annual exclusion to permit gift transfers up to \$17,000 per recipient, or \$34,000 from married couples per recipient, to pass entirely free from gift and estate tax each year. These annual exclusion gifts do not count against the transferor's lifetime exemption described above, and the annual exclusion per recipient is renewed each year.

The annual exclusion allows for federal gift and estate tax exemption to be preserved for gifts in excess of the exclusion amount, and a person can still pass on significant wealth gift tax-free

over a period of years even if his or her lifetime exemption is exhausted. This annual exclusion is also adjusted for inflation. Outright gifts and certain gifts in trust can qualify for the annual exclusion. Careful planning is required where gifts to trusts are intended to qualify for the annual exclusion.

Estate planning opportunities also exist for transfers to surviving spouses and to qualified charitable organizations. Transfers at death to qualifying charitable organizations generally pass free of federal estate tax. Transfers at death to or for the benefit of a surviving spouse generally qualify for a tax-free marital deduction, thereby deferring estate tax until the second spouse's death. It's important to note, however, that transfers to non-U.S. spouses are subject to different rules.

Washington state residents also should consider the impact of state estate tax in updating their estate plans. While Washington doesn't have a gift or GST tax, it does impose an estate tax at death separate from the federal estate tax. In 2023, the Washington state estate tax exemption is \$2,193,000 per taxpayer, with assets in excess of that amount subject to Washington state estate tax at a rate between 10 percent and 20 percent.

The Washington estate tax also applies to estates of nonresidents who own real estate or tangible personal property located in Washington. For nonresidents, the full \$2,193,000 exemption is not applied against the property located in the state. Rather, the exemption is in essence applied against the total value of a nonresident's estate, with the result that Washington tax may be owing even if the value of the Washington assets alone are less than the state exemption.

Like the federal estate tax, Washington state estate tax does not apply to transfers to U.S. spouses or to qualifying charitable organizations.

This year presents an opportunity for healthy, thoughtful estate planning involving transfers that may use federal gift, estate, or GST tax exemption. While the expiration of the increased federal tax exemptions looms at the end of 2025, there is still enough time to carefully consider estate plan updates. Now is the time to dust off estate plans, consider if gifting may be appropriate, and think about using some of the available federal exemptions before they are reduced.

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