

Death Taxes in Pennsylvania

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Most people are familiar with the quote attributed to Benjamin Franklin: "...in this world nothing can be said to be certain, except death and taxes."

Another equally true quote, although not quite as familiar, is from Will Rogers: "The difference between death and taxes is death doesn't get worse every time Congress meets."

And although both quotes are true, and both death and taxes are inevitable, "death taxes" are relatively misunderstood by most. On top of that, taxes can be quite confusing generally, and even more so during the grieving process.

Since we know that "no one gets out of here alive", let's delve in to the topic of death taxes and see exactly what they include.

Federal Estate Tax

Everyone has heard about Federal Estate taxes. Most folks also know that the concept of an "estate" becomes relevant when a person dies and leaves his or her "stuff" to beneficiaries. But while estate taxes seem to get all the headlines, the reality is that very few, if any, estates will owe federal estate taxes. Why?

Because the value of an individual's net worth that is exempt from the tax is incredibly large. In fact, in 2019 the federal estate tax exemption is \$11.4 million per person, and if that person is married, the exemption can be doubled to \$22.8 million! This may be accomplished by using something called the portability election, which means that a surviving spouse may claim any unused portion of the deceased spouse's exemption and add it to their own exemption. Additionally, the individual exemption amount will only continue to increase annually based on inflation, at least until 2025, when the individual exemption is set to return to \$5.49 million per person.

If, by some chance, the decedent's estate was valued at \$11.4 million or more, the Personal Representative (Executor or Executrix) of the estate would have to file a Federal Estate Tax return using IRS Form 706, which is officially called the *United States Estate (and Generation-Skipping Transfer) Tax Return*.

Pennsylvania State Inheritance Tax

If the deceased was a resident of Pennsylvania but did not have enough net worth to have to pay Federal Estate Tax, the state of Pennsylvania still wants to make sure Ben Franklin's quote holds true! Accordingly, Pennsylvania requires payment of a State Inheritance Tax, starting with the first dollar (no exemptions). The Pennsylvania inheritance tax is not based on how much the decedent was worth at

death, but instead is based on who receives the deceased person's property. If you are not a lifelong resident of Pennsylvania or have never lost a loved one who lived in Pennsylvania, you are probably not familiar with this tax. Why? Because Pennsylvania is one of only six states that collect a state inheritance tax.

So which beneficiaries of an estate may have to pay state inheritance taxes and how much is the tax? Some good news is that any portion of the decedent's estate that passes to the deceased person's surviving spouse or to a charity generally will be exempt from the state inheritance tax.

The Pennsylvania inheritance tax rates are as follows:

- 0 percent on transfers to a surviving spouse, to a parent from a child aged 21 or younger or to a charity generally;
- 4.5 percent on transfers to direct descendants and lineal heirs;
- 12 percent on transfers to siblings; and
- 15 percent on transfers to other heirs, generally.

Inheritance tax payments are due upon the death of the decedent and become delinquent nine months after the individual's death. If inheritance tax is paid within three months of the decedent's death, however, a 5 percent discount is allowed. As you can see, the likelihood of an inheritance being subject to Pennsylvania State Inheritance Tax is far greater than the likelihood that the estate will be subject to Federal Estate Tax.

State Estate Taxes

Pennsylvania does not have a State Estate Tax, but that does not mean that Pennsylvania residents can completely ignore the possibility this tax may be owed. If the deceased person owned real estate in Connecticut, Delaware, the District of Columbia, Hawaii, Illinois, Maine, Maryland, Massachusetts, Minnesota, New Jersey, New York, Oregon, Rhode Island, Tennessee, Vermont or Washington, it is possible that the estate may end up owing State Estate Taxes too.

Gift Taxes

Although Gift Tax is not automatically owed at death at the state level in Pennsylvania, there are certain scenarios for which a Federal Gift Tax Return may need to be filed. If the decedent gave away assets during the last year of his or her life, and the gift exceeded the Federal Gift Tax exemption of \$15,000 in 2019 (or \$30,000 for a married couple), then the Personal Representative will have to file a federal gift tax return using IRS Form 709, officially known as the *United States Gift (and Generation-Skipping Transfer) Tax Return*.

Income Taxes

One often overlooked tax return that must be filed has to do with the decedent's income in the last year of life and is called "Income in Respect of a Decedent", or IRD. The Personal Representative will be responsible for filing a deceased person's final income tax return at the federal level and at the state level. Pennsylvania treats "Income in Respect of a Decedent" quite differently from the federal income tax treatment of IRD. Tax experts are keenly aware of the differences and Julian Gray Associates recommends that the Personal Representative work with their own tax preparer to file the decedent's Income Tax return.

Income earned by an estate or a trust is reported on IRS Form 1041, officially known as the *U.S. Income Tax Return for Estates and Trusts*, for federal income tax purposes. For state estates and trusts, income is reported on the *PA-41 Fiduciary Income Tax return*.

So, what does it all mean? The attorneys at Julian Gray Associates stand ready to assist families with the process of settling their loved one's affairs. Our goal is to relieve families of the burdens of worry, uncertainty, confusion and pressure so that the family can focus on one another and the memory of the loved one throughout the grieving process.

If you are not sure if your loved one's estate or trust will be subject to any taxes, or if you are not sure if what you have inherited will be subject to any taxes, please contact us at Julian Gray Associates.