# How to Reduce Pennsylvania Inheritance Tax

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Did you know that Pennsylvania is one of only six States that still assesses an inheritance tax to beneficiaries who inherit property? Pennsylvania's death tax is the Pennsylvania Inheritance Tax. It is assessed to all beneficiaries of a decedent who was a resident of Pennsylvania at the time of death. However, with advance planning, you can substantially reduce the inheritance tax liability of your beneficiaries.

Some states assess a death tax for property only in excess of a certain value. However, that is not the case in Pennsylvania. In Pennsylvania, all property owned by a resident decedent is subject to inheritance tax unless it is exempt, and only life insurance policy proceeds and real estate located outside of Pennsylvania are exempt from inheritance tax. (Inheritance tax is also assessed on Pennsylvania real estate that is owned by Pennsylvania nonresidents.) Property subject to inheritance tax includes all retirement accounts, annuities, U. S. Savings Bonds, bank and investment accounts, etc. as well as all personal property, which includes, but is not limited to, motor vehicles, jewelry, clothing, furniture and collectibles.

The amount of tax owed by a beneficiary depends upon how closely related the beneficiary was to the decedent. The tax rate between spouses is zero. The tax rate for property passing from a child under the age of 21 years to a parent or from a parent to a child under the age of 21 years is also zero. The tax rate for lineal relatives, for example, from parent to a child over the age of 21 years or to a grandchild, or from a child over the age of 21 years to parent or to a grandparent, is 4.5%. A sibling beneficiary is taxed at the rate of 12% and anyone who is more distantly related than a sibling is taxed at the rate of 15%.

Beneficiaries must pay inheritance tax on property valued as of the decedent's date of death. However, a beneficiary is required to pay inheritance tax only on the property the beneficiary actually inherits. A beneficiary may reduce the amount of inheritance paid by listing deductions on the inheritance tax return for all funeral and burial costs and other expenses that are incurred by the estate, any taxes paid, legal fees and debts the decedent owed at death.

Creating a plan during your lifetime can reduce the inheritance tax liability of your beneficiaries at your death. You can avoid inheritance tax by making outright gifts of your property during your lifetime. Additionally, if you prefer to withhold immediate access to gifts by beneficiaries, you can establish a trust instead of making outright gifts. Such a trust must have specific terms that will avoid inheritance tax upon your death. Please note, however, in Pennsylvania, you must complete your gift or trust plan at least one year before death. If you transfer your property within one year of your death, whether by gift to your family or to a trust, that property will be included in your estate for inheritance tax purposes and inheritance tax will be owed on the property.

Another planning technique to reduce inheritance tax is to add another individual as a joint owner with right of survivorship to your property. If you add one joint owner and live at least one year thereafter, for inheritance tax purposes, your beneficiary is considered to own one-half of the property. Therefore, upon your death, the beneficiary will owe inheritance tax only on the one-half portion of the property owned by you. You can add multiple joint owners to property and inheritance tax will be owed only on your proportionate share of the property. Before undertaking this plan, you should be aware that the joint owners will have access to your property during your lifetime. Additionally, if a joint owner dies before you, you will owe inheritance tax on the joint owner's share of your own property.

Many of our clients utilize a trust in their estate plans, or name beneficiaries to certain accounts, especially retirement accounts, and thereby avoid the requirement of probating a Last Will and Testament in order to distribute property to their beneficiaries at death. It is important to note that avoidance of probate does not necessarily mean avoidance of inheritance tax. In order to avoid inheritance tax a trust must have specific terms that are not present in other trusts. Additionally, the balance of retirement accounts you own at death is subject to inheritance tax, even though the accounts will avoid probate if they have beneficiary designations.

If you are interested in receiving more information about how you can reduce the inheritance tax your beneficiaries will owe at your death, please contact our office and we can discuss a plan for you.