

SENATE BILL REPORT

SB 6347

As of February 3, 2004

Title: An act relating to the Washington estate tax marital deduction.

Brief Description: Updating the Washington estate tax marital deduction.

Sponsors: Senators Johnson, Brown, Winsley and Roach.

Brief History:

Committee Activity: Ways & Means: 2/4/04.

SENATE COMMITTEE ON WAYS & MEANS

Staff: Terry Wilson (786-7433)

Background: The federal government imposes an estate tax on the transfer of property at death. The state of Washington imposes a tax on the transfer of property at death, which is equal to the amount of tax authorized as a credit against the federal estate tax for state taxes. The federal estate tax was changed in 2001 for persons dying in 2002 and thereafter. However, Washington did not incorporate the federal changes into the state's estate tax. Because of this, Washington's estate tax is calculated in a different manner than the current federal estate tax.

Gifts made to a surviving spouse are exempt from the state and federal estate tax. This marital deduction is also allowed for qualified terminal interest property (QTIP). A QTIP is property placed in trust in which the surviving spouse is entitled to all income from the trust property payable at least annually and no other person has the power to appoint any part of the property to a person other than the spouse. The estate must make an election for property to be QTIP property.

Under the state and federal estate tax, every person receives a unified credit for gifts made during a person's lifetime and at death. The effect of the unified credit is to exempt estates below a certain amount (known as the applicable exclusion amount). The applicable exclusion amount is \$850,000 for the state tax and \$1.5 million for the federal tax for calendar year 2004. This is scheduled to increase to \$1 million by 2006 for the state tax and to \$3.5 million by 2009 for the federal tax.

Most estate tax planning documents for married couples strive to ensure that there is no tax on the death of the first spouse. Many use formulas to fund trusts up to the applicable exclusion amount. Because the applicable exclusion amount is now different for state and federal taxes, a state tax could be due on the death of the first spouse on an amount equal to the difference between the state and federal exclusion amounts. The Department of Revenue has allowed an estate to make a QTIP election in a different amount for the state tax than for the federal tax in order to postpone state tax until the death of the second spouse. However, this election can only be made if the property meets the QTIP requirements.

Summary of Substitute Bill: The Legislature finds that a goal of the Washington estate tax is to provide a reasonable opportunity for a surviving spouse to postpone the Washington estate tax until the surviving spouse dies and declares that this act is needed to provide that opportunity. The Legislature intends this act to create no inference as to any litigation regarding the enactment of the Economic Growth and Tax Relief Reconciliation Act of 2001 and the Washington estate and transfer tax.

An intent to qualify for the marital gift tax deduction is presumed for gifts for which a Washington QTIP election could be made but for which a federal QTIP election is not made.

Trusts are presumed to meet QTIP requirements and qualify for the Washington estate tax marital deduction and Washington QTIP election if:

- (1) The trust is established as a result of the transferor's death and receives an amount determined by reference to the federal applicable exclusion amount or by a formula gift intended to result in no federal estate tax;
- (2) The transferor dies after December 31, 2001;
- (3) The transferor is survived by a spouse;
- (4) Under the terms of a governing instrument, the transferor transfers property in trust for the benefit of the spouse which is includible in the transferor's gross estate for the Washington estate tax and which is subject to Washington estate tax because it exceeds the Washington applicable exclusion amount but bears no federal estate tax because it is less than the federal applicable exclusion amount; and
- (5) The transferor makes the transfer in a manner that does not qualify for the Washington estate tax marital deduction.

This presumption does not apply if (a) a beneficiary of the trust rebuts the presumption; (b) the transferor amended the governing instrument after December 31, 2001, and expressed an intent not to qualify the transfer for the Washington estate tax marital deduction; or (c) the governing instrument states that federal or Washington law as of a particular time prior to January 1, 2002, is to govern.

For purposes of probate and trust law, the reference to the federal Internal Revenue Code is updated to refer to the U.S. Internal Revenue Code of 1986, as amended as of January 1, 2004.

Substitute Bill Compared to Original Bill: The original bill was not considered.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect immediately.