

Chapter 9:

A Quick Primer on Estate, Gift, and Generation-Skipping Taxes

Taxes are the price we pay for living in a civilized society.

Oliver Wendell Holmes,
U.S. Supreme Court Justice

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IN THIS CHAPTER . . .

you'll discover the levels at which estate, gift, and generation-skipping taxes kick in.

Who Gets Your Money—Your Heirs or the Treasury?

Depending on the size of your estate, a key priority of estate planning may be to minimize the taxes that your heirs will owe upon your death. This chapter briefly introduces some of the taxes that can be levied against an estate. Understanding what these taxes are will help you as you consider the advantages and disadvantages of testamentary Trusts (Chapters 10 through 16) and an array of other issues that can affect how much of your estate goes to pay taxes.

Estate Tax on Gifts at Death

At death, the basic exclusion amount (BEA) \$15 million, plus a yearly inflation adjustment beginning in 2026, minus any reportable gifts made during your lifetime, plus any preserved deceased spouse's unused exclusion (DSUE), passes to beneficiaries free from federal estate tax. As you may surmise, federal estate taxes affect only a tiny percentage of Americans, certainly less than 1%. State estate taxes are discussed later in this chapter.

Tax on Lifetime Gifts

Lifetime gifts to charity and between U.S. citizen spouses are uncapped and not taxable. Other lifetime gifts of up to the BEA can be made without incurring transfer tax. The gift of the entire applicable amount is in addition to the \$19,000 that one person can gift to others every year, but gifts to any nonspouse greater than \$19,000

(or gifts to a non-U.S.-citizen spouse greater than \$190,000) must be reported to the IRS. Gifts reported on an informational gift tax return are subtracted from the individual's BEA remaining at death.

Generation-Skipping Transfer (GST) Tax

Those taking a long view of wealth may consider generation skipping. The government wants to collect transfer taxes at every generation. Both lifetime and testamentary gifts greater than \$15 million to family members two or more generations younger or unrelated individuals more than 37½ years younger face the punitive generation-skipping transfer (GST) tax. The federal GST tax is assessed at the highest rate, 40 percent, after any regular transfer tax has been assessed. This can severely deplete the estate, leaving less for the beneficiaries. As discussed in Chapter 14, GST tax-exempt Trusts can give lasting protection to Trust assets, saving taxes in the estates of your descendants.

Unified System

The transfer tax for estates, gifts, and generation skips is unified. At various times throughout their history, lifetime gifts, testamentary gifts, and generation-skipping gifts all had different tax thresholds, but they currently align at \$15 million. Lifetime gifts to individuals other than a spouse who is a U.S. citizen in excess of the annual exclusion amount deplete the amount of each tax threshold remaining at death. (Chapter 21 further discusses the topic of lifetime gifting). The highest federal estate and gift tax rate, in the absence of GST taxes, is 40 percent.

Gifting to a Spouse during Life or at Death: The Unlimited Marital Deduction

The unlimited marital deduction allows you to make gifts of any size, whether during life or upon death, to your spouse (as long as they are a U.S. citizen) with no tax or reporting requirement. Gifts to a life partner who is not a legal spouse do not qualify for this treatment.

A spousal gift can be made via a testamentary or other irrevocable Trust. To avoid gift and estate taxes, the recipient must unconditionally receive all income generated for life. Even if the surviving spouse remarries, the money is theirs to keep!

As discussed in Chapter 13, there are situations where the overuse of the unlimited marital deduction may result in unnecessary estate tax upon the surviving spouse's death. In those instances, a shelter Trust, automatically created upon the death of one spouse or generated postmortem via disclaimer (Chapter 15), may reduce taxes in the long run.



George Steinbrenner

July 4, 1930–July 13, 2010

Yankees win 7 World Series during his 37-year reign. Times death perfectly: He dies a billionaire in 2010, the one year since 1916 when there was no federal estate tax for people dying.



A Very Brief History of Federal Transfer Tax and Its Political Background

In 1906, when proposing a federal tax on inheritances, Theodore Roosevelt said that a “man of great wealth owes a particular obligation to the State, because he derives special advantages from the mere existence of government.” A decade later, in 1916, Congress implemented an estate tax to help pay the cost of what was then known as the Great War. After an exclusion of \$50,000 (about \$1 million today), the top rate was a 10 percent tax.

Since that time, there have been many ups and downs to federal estate tax thresholds reflecting political battles between Democrats, fighting against wealth concentration, versus Republicans, fighting against “death” taxes. Compromise tax packages over recent decades included various temporary laws that “sunset” after several years. This ping pong system continued until the One Big Beautiful Bill Act (OBBBA), signed into law July 4, 2025, effective January 1, 2026, made the unified system of estate, gift and GST tax permanent. The word “sunset” can finally be retired from estate tax planning.

State Estate Taxes

On top of federal transfer taxes, affecting only the fortunate few, certain states levy their own transfer tax of as much as 20 percent on estates that are much smaller than the \$15 million federal threshold for estate taxes.

A fully funded shelter Trust intended to reduce federal estate taxes may result in substantial state estate taxes upon the death of the first spouse. This problem is usually solved by a shelter Trust that is “Q-Tippable,” essentially requiring that the surviving spouse receive all Trust income and providing that any discretionary principal payments made by the trustee can only be distributed to the spouse.

Although a single asset may not be taxed by multiple states, your estate may owe tax in every state in which you own property. This may be reason enough to sell a rarely used vacation home.

Note that payment of state estate taxes is not federally tax deductible. For wealthy Americans, state estate taxes can be at least as important a consideration as climate and culture as they choose the location of their principal residence.

Estate Tax on Nonresident Noncitizens

Subject to various exceptions, exemptions, and treaties with other countries, the U.S. “situated” estate assets of nonresident noncitizens in the United States, other than spouses, are generally taxed to the extent that their value exceeds \$60,000. A nonresident, noncitizen spouse in receipt of such an estate may benefit from a qualified domestic Trust (QDOT), as discussed in Chapter 13. Nonresident noncitizens may also benefit from annual gifting, as discussed in Chapter 21. Such gifts to a spouse may be in amounts up to \$190,000 per year.

Pearls of Wisdom

If the value of my assets exceeds \$15 million, potential federal estate taxes may be a factor in my estate planning. Likewise, if I live in a state that assesses its own estate tax, that may affect my decision-making and warrant a review of planning done many years ago to ensure mitigation of state estate taxes.

