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The Phase Out of Indiana Inheritance Tax

In the many years that I have served on the Indiana State Bar Association Probate, Trust & Real Property Section Council, the ISBA Probate Review Committee, and the Probate Code Study Commission for the Indiana Legislature, there have been numerous bills presented in the legislature to repeal the Indiana Inheritance Tax. Every year, the bills have either been defeated or never received a hearing. I believed the inheritance tax would never be eliminated. History changed in March 2012 when Governor Daniels signed Senate Enrolled Act 293 (SEA 293). This Act makes significant changes to the Indiana Inheritance Tax over the course of the next 10 years, with the tax being repealed in 2022. Never say never - hard work and determination pay off.

I will discuss the changes brought about by SEA 293 within the framework of how Indiana's inheritance tax structure currently operates. (Note: changes appear in italics). Indiana Inheritance Tax is imposed on the transfer of property from an Indiana decedent to a beneficiary. While Federal Estate Tax is assessed on a decedent's total combined asset value, Indiana Inheritance Tax is a transfer tax assessed on each separate transfer. The tax is imposed on the recipient of the inheritance, but many estate planning documents provide for the payment of the inheritance tax out of the decedent's estate before assets are distributed.

The inheritance tax is assessed on the fair market value of the transfer at the decedent's death, less the amount of the recipient's exemption (described below). The rate of tax is based upon the beneficiary's class status and those of closer relationship to the decedent pay a lesser tax rate. *Although the tax rates remain unchanged under SEA 293, a 10% credit will be subtracted from the amount of the inheritance tax due for decedents who die in 2013. For decedents who die in 2014, the credit will be 20% and the credit will continue to increase by 10% annually. In 2021, the credit will be 90%, and the tax phases out completely after December 31, 2021.*

Indiana has a three class inheritance tax system and the exemptions and tax rates vary between classes based on the relationship of the recipient to the decedent. The decedent's surviving spouse pays no inheritance tax due to an unlimited marital deduction. There is also an unlimited charitable deduction for inheritance tax purposes. All other beneficiaries are taxed within one of the three classes based upon their relationship to the decedent.

"Class A" beneficiaries include the decedent's parents, children, stepchildren, grandparents, grandchildren, and all other lineal ancestors and lineal descendants. *Under SEA 293 this definition has been expanded for deaths which occur on or after January 1, 2012, to include spouses and surviving spouses of decedent's children and grandchildren and stepchildren.* Before SEA 293 became law Class A beneficiaries were given a $100,000 exemption. *SEA 293 increased the exemption to $250,000, effective retroactively to deaths which occur on or after January 1, 2012.*

"Class B" beneficiaries include the decedent's brothers, sisters and lineal descendants of brothers or sisters (nieces and nephews). *Daughters- and sons-in-law fell into this category prior to SEA 293.* Class B beneficiaries are given a $500 exemption before any tax is due. *This exemption was not changed by SEA 293.* "Class C" beneficiaries includes all beneficiaries who do not fit within the Class A or B definitions. *A spouse, widow or widower of a stepchild fell into this category prior to SEA 293.* Class C beneficiaries are given a $100 exemption before any tax is due. *This exemption also was not changed by SEA 293.*

Another change brought about by SEA 293, effective July 1, 2012, requires the Indiana Department of Revenue to look through a trust or other entity and treat a transfer on death to such entity as a series of transfers, one to each beneficial owner of the trust or entity. Each beneficial owner is taxed for inheritance tax purposes based on their percentage ownership in the trust or entity.

If you have any questions with regards to this new law or would like to discuss your estate planning or probate needs, please contact a member of CGG's estate group. Call (317)573-8888 or email your attorney directly; email addresses for our attorneys appear along with their profile on www.cgglawfirm.com.