

Michigan Inheritance Tax

By **Ralph E. Hepp and Myron P. Kelsey, Extension Specialists**
 Department of Agricultural Economics, Michigan State University

For most families, an objective in estate planning is to minimize the amount of death taxes to be paid. At death, Michigan imposes a transfer tax upon the market value of the heirs' share of an inheritance.¹ All real and personal property owned by a Michigan resident decedent and all real property located in Michigan but owned by a non-resident decedent is subject to the tax. Because of various personal exemptions and property exclusions, the tax may or may not be important for your estate. You must understand the law's provisions to make this determination. This bulletin explains major provisions of the law and gives estate planning pointers to help Michigan families manage the tax.

Transfers Subject to the Tax

Property transfers are subject to the tax when made by:

—Will or intestate laws of Michigan (Michigan laws which govern the distribution of estates of persons dying without leaving a valid will). Examples of property ownership that passes through the terms of the will or intestate laws are property owned solely by the deceased and the decedent's share of tenancy-in-common property. Tenancy-in-common exists when two or more persons each own an undivided share in property. Each tenant has the right to mortgage, sell, assign or convey his undivided share. At death, a tenant's fractional share in the property is included in the taxable estate. For example, if two individuals own equal shares in farmland, only one-half the value of the farm is included in the deceased tenant's estate.

—Grant or gift made within two years of death that is made in contemplation of death.

—Grant or gift made during lifetime which takes effect at or after death. Retained life estates, trusts or other lifetime transfers whereby a person transfers property by gift and retains possession, enjoyment or right to income from the property are included in the taxable estate. A similar result occurs if the decedent had the

right to designate the person who shall possess the property or receive the income from the property. Transfers intended to take effect at death are also included in the taxable estate.

Property transfers not subject to the tax are:

—Jointly held property, whether joint tenancy with rights of survivorship or tenancy by the entirety. Joint tenancy with rights of survivorship exists when two or more persons own an undivided share in property together. Jointly, the tenants have the right to mortgage, sell, assign or convey their ownership rights. Tenancy by the entirety is a special type of joint tenancy with rights of survivorship between husband and wife. Upon the death of one joint owner, the survivors do not take ownership by descent, distribution or transfer but by right of survivorship, and there is no transfer and no inheritance tax. The fact that one owner contributed all the property or had the right to revoke the joint ownership does not make the property taxable.

—Life insurance proceeds paid to the estate are subject to the tax, but proceeds paid to named beneficiaries are not subject to the tax.

—All property transfers to a spouse that otherwise would be subject to the tax are exempt. The marital deduction for property passing to the decedent's spouse has been effective for all estates since December 31, 1982.

Deductions

Items that reduce the value of the inheritance are allowed as deductions before the tax is determined. Common deductions are:

- Funeral expenses.
- Estate administration expenses (legal fees, executor's fees, probate court costs).
- Debts and claims owing at the time of death.
- Mortgages and liens.

Classes of Heirs

Persons taxed by the Michigan inheritance tax fall into two classes:

Class I—Grandfather, grandmother, father, mother, husband, wife, child, legally adopted child, step-child, brother, sister, wife or widow of a son, husband or widower of a daughter, a person to whom the decedent stood in the mutually acknowledged relation of a parent if the relationship began at or before the child's seventeenth birthday and continued until the death of the decedent and a lineal descendent of the decedent.

Class II—All other heirs not included in Class I.

The exemptions and tax rates are unique to each class of heirs.

Exemptions

Personal exemptions for each class of heirs are:

Class I—\$10,000 for a decedent who dies after 12/31/91 but before 1/1/93; \$15,000 for a decedent who dies after 12/31/92 but before 1/1/94; \$25,000 for a decedent who dies after 12/31/93 but before 1/1/95; \$50,000 for a decedent who dies after 12/31/94.

Class II—None. There is no tax on the share of any beneficiary if the value of the share is less than \$100.

Charitable exemptions—Property transfers to charitable, religious, educational or public institutions are exempt if the recipient is exempt from property taxation and one of the following:

—A Michigan corporation specifically organized for the above purposes.

—A Michigan unincorporated foundation for the above purposes, but only if it was in existence prior to May 15, 1949.

—A foreign corporation for the above purposes if the state in which that corporation was organized grants similar exemption from inheritance taxes to a resident of the state who leaves money to a similar Michigan corporation.

For the estate of a decedent who dies after 12/31/92, no tax is imposed on a transfer of any property of a family-owned business or the transfer of the ownership of a family-owned business to a qualified heir or heirs. A family-owned business is defined as participation by the decedent or a qualified heir for not less than 500

hours in 5 out of 8 years immediately preceding the decedent's death and either the business is 100 percent owned by the decedent and qualified heirs, or the business is 49 percent owned by the decedent.

For the estate of a decedent who dies after 12/31/92, the transfer of qualified farm real and personal property to a qualified heir is exempt from taxation.

Qualified farm real and personal property is property that meets the criteria for a family-owned business as defined above. A qualified heir is any Class I beneficiary or farm business partner.

For the estate of a decedent who dies before 1/1/93, 50 percent of the market value of transferred qualified farm real property that is enrolled in P.A. 116 is exempt from tax.²

Tax Rates

As Table 1 illustrates, the graduated tax rates vary, depending on both the value of the inheritance and the relationship of the beneficiary to the decedent.

Table 1. Michigan inheritance tax rates for classes of heirs.

II Value of inheritance	Class I	Class
	heirs	heirs
—Percent—		
0 to \$50,000	2	12
\$50,000 to \$250,000	4	14
\$250,000 to \$500,000	7	14
\$500,000 to \$750,000	8	17
\$750,000 and over	10	17

The value of the inheritance is the market value of the property reduced by unpaid mortgages, debts or liens on the property. The inheritance tax is determined by: (1) separating the heir's share into the appropriate tax brackets, (2) assessing the rate for each range, and (3) summing up the parts to yield the total inheritance tax due for the heir. The heir's personal exemption is deducted from the lowest tax brackets rather than from the entire value of the transfer.

Inheritance Tax Example

This example assumes that a married decedent leaves jointly held property, life insurance and solely owned property to his spouse. The jointly owned property is not subject to the inheritance tax. Other property, solely owned by the deceased, is part of the taxable estate and has a net value of \$140,000. The property is transferred to the following heirs and taxed according to the calculation in Table 2.

The exemption for each child is taken from the lowest tax bracket and the 2 and 4 percent rate applied to the remaining taxable inheritance. The exempt charity has a complete exemption for the property transferred. The neighbor has no personal exemption and the inheritance is taxed at the 12 percent rate.

Additional Tax

An additional Michigan inheritance tax may be due on an estate that must pay a federal estate tax. The federal estate tax has a tax credit for state taxes based upon a schedule according to estate size. If the federal estate tax credit for state taxes is larger than the inheritance tax paid to Michigan, the difference is paid by the estate as an addition to the inheritance tax. Inheritances or transfers not subject to the additional tax shall receive a credit for 10 percent of the Michigan inheritance tax imposed.

The county treasurer collects an additional tax of one-half of 1 percent on the Michigan inheritance tax

paid and credits the fee to the general county fund.

The inheritance tax is also imposed on a generation-skipping transfer made by a decedent dying after 12/31/92 if the transfer is subject to a tax under the Internal Revenue code.

Filing Requirements

If property is subject to the Michigan inheritance tax, an inheritance tax order must be obtained from the Probate Court. The Probate Court, having jurisdiction over the decedent's estate, has authority to determine the inheritance tax.

The inheritance tax must be paid within 105 days after the date of death. A penalty of 8 percent of the tax will be added for late filing, plus 5 percent for each fraction of a month the return is late up to a maximum of 25 percent, plus interest at the rate of three-quarters of 1 percent per month. The person to whom the property is transferred and the personal representative of every estate are liable for the tax until its payment.

Planning Pointers

The Michigan inheritance tax has low tax rates for property subject to the tax for close family members. In most cases, married couples (first marriage) own their property jointly and have retirement benefits and life insurance that transfers directly to the named beneficiary or transfers property to the surviving spouse. Property owned and transferred by these methods is not subject to the inheritance tax.

A couple with a medium (\$250,000 to \$500,000) or large estate (\$500,000 or more) should obtain tax counsel in estate planning because the inheritance tax

Table 2. Inheritance tax on a \$140,000 taxable estate for a person dying during 1994.

Heir	Value of taxable inheritance	Exemption	inheritance taxed	Tax rate %	Inheritance tax
Son	60,000	25,000	Exempt	2	—
			25,000	2	500
			10,000	4	400
Daughter	60,000	25,000	Exempt	2	—
			25,000	2	500
			10,000	4	400
Exempt charity	10,000	10,000	Exempt	—	—
Neighbor	10,000	—	10,000	12	1,200
Total	\$140,000	\$60,000	\$80,000		\$3,000

and federal estate tax on the surviving spouse's estate may be large if all property is transferred to the surviving spouse. In large estates, transfers to the surviving spouse may minimize the inheritance tax on the first transfer, but the second transfer may be expensive to the surviving spouse's heirs.

Second marriages, especially when there are children from a previous marriage, have issues to be considered other than tax planning. Obtain legal counseling in planning the estate so property is transferred to heirs whom you want to receive the property. Then consider tax issues.

Widows, widowers and single individuals have other issues that need to be considered when transferring their estates. Owning property jointly with their heirs has inheritance tax implications, and the process of adding an heir's name to property may have federal gift tax impacts and property control and ownership implications. Single individuals and their heirs should hold property jointly only in special situations. Obtain legal counsel before changing the way property is owned so you understand the consequences during your lifetime and the way the property will be taxed.

Summary

The above discussion was limited to some of the major provisions of the Michigan inheritance tax law. Each of the new provisions, and the law itself, is detailed and complicated enough that competent counsel is needed to plan and settle estates. Individuals who established estate plans under the prior law should review present plans and determine whether the amended law should result in some changes. Those who have done little or no planning should start now.

¹ Public act NO. 188 of 1899 as amended. The latest amendment is Senate Bill NO. 1 of 1991, passed in June 1992. Property transfers at death are also subject to the federal estate tax. Information on the federal tax may be found in Extension Bulletin E-1231, "Federal Estate and Gift Taxes," Cooperative Extension Service, Michigan State University.

² An explanation of the Farmland and Open Space Act (P.A. 116) may be found in Extension Bulletin E-792A, "Farmland and Open Space Preservation Act," Cooperative Extension Service, Michigan State University, November 1978.

**MICHIGAN STATE
UNIVERSITY
EXTENSION**

MSU is an affirmative-action, equal opportunity institution. Cooperative Extension Service programs and materials are available to all without regard to race, color, national origin, sex, handicap, age, or religion. Issued in furtherance of Cooperative Extension work in agriculture and home economics, acts of May 8 and June 30, 1914, in cooperation with the U.S. Department of Agriculture. Gail L. Imig, Director, Cooperative Extension Service, Michigan State University, E. Lansing MI 48824.

Major revision-11:92-3M-IJ-BP-25¢ (single copy free to Michigan residents)
Printed on recycled paper using vegetable-based ink

Other Available Publications

There are many other publications about estate planning that are available from your Cooperative Extension Service. Some of these are listed below.

E-0451 Record of Important Family Papers, 8pp	50¢*
E-1231 Federal Estate & Gift Taxes, 6pp	50¢
E-1345 Trust Uses in Estate Planning, 8pp	75¢
E-1346 Life Insurance Uses in Farm Planning, 4pp....	20¢*
E-1619 Estate Planning Tools for Farm Corporation Owners	65¢
E-1684 Insurance for Your Family, 6pp.....	25¢*
E-2120 Wills, Probate & Estate Planning, 16pp.....	\$1.00

* Single copies free to Michigan residents