



Understanding federal transfer taxes

Transfer taxes are a set of federal taxes that apply when wealth is transferred from one person to another, whether during life or at death. While the rules are complex, it is helpful to have a working knowledge of the three types of transfer taxes — gift tax, estate tax, and generation-skipping transfer (GST) tax. Below is an explanation of the way these closely related taxes work together as part of the same system. The application of the rules will vary depending on specific circumstances, which is why it is important to have a knowledgeable advisor guide your estate planning.

Gift tax: Transfers during life

The gift tax applies to most transfers of property to individuals during your lifetime. If you give money or other assets to someone without expecting anything in return, that transfer may be considered a gift for gift tax purposes. The gift tax ensures that individuals do not avoid estate taxes by giving away all their assets during their lifetime.

Each individual has a lifetime gift tax exemption, and any taxable gifts you make during your lifetime using that exemption will reduce the amount of estate tax exemption that is available at death (see below). In this way, the gift and estate tax exemptions are unified. In 2026, the federal gift and estate tax exemptions are \$15 million per person. Thereafter, the exemption amounts will be adjusted for inflation each year. You report any taxable gifts and the use of your lifetime gift tax exemption on a gift tax return for the year any such gifts are made. If you use all of your gift exemption during life, the gift tax rate is 40% on any additional gifts.

The Internal Revenue Code excludes certain transfers from being treated as taxable gifts. These exclusions allow you to make “tax-free” gifts to or for the benefit of any individual without reducing your lifetime gift tax exemption.

- **Annual exclusion gifts:** Each year, you can give up to a certain amount to as many individuals as you wish without the gift being treated as a taxable gift. In 2026, the annual exclusion amount is \$19,000 (\$38,000 for married couples).
- **Medical expense and tuition exclusion:** In addition to annual exclusion gifts, you can make unlimited payments to cover qualified medical and educational expenses for others, but you must make payments directly to the providers or institutions.

Estate tax: Transfers at death

The estate tax applies to the transfer of property at death. It is a tax on the value of the property in your estate, reduced by your allowable deductions (your “taxable estate”). The property in your estate for estate tax purposes generally consists of those assets which you own or control at death. Some deductions that may be allowed to reduce the value of your taxable estate include your outstanding debts, expenses of the estate administration, and gifts to a spouse or charity.

Under current law, your taxable estate will be subject to an estate tax only to the extent it exceeds your estate tax exemption, determined after reducing the estate tax exemption by the amount of your lifetime gift tax exemption you used (your “remaining exemption amount”). This means that if the total value of your taxable estate is below your remaining exemption amount at death, no federal estate tax is owed. On the other hand, if the total value of your taxable estate exceeds your remaining exemption amount, then the exemption is subtracted from your taxable estate and a 40% estate tax rate is applied to that balance.

GST tax: Transfers to “skip persons”

The GST tax is a separate tax designed to ensure that a transfer tax is imposed at every generation. The GST tax applies when assets pass to individuals who are more than one generation younger than the grantor. These recipients are called “skip persons” since the generation directly below the grantor is skipped. For example, a grandchild is a skip person as to a grandparent. For non-family members, a skip person is anyone more than 37-1/2 years younger than the grantor.

Like the estate and gift taxes, there is an exemption for the GST tax, which is \$15 million per person in 2026. This amount is tracked separately and is not unified with the estate and gift exemptions. The GST tax rate is imposed at a rate of 40% on transfers to skip persons to the extent they exceed the grantor’s remaining GST exemption at the time of the transfer.

You can use your GST exemption by making direct gifts to skip persons during life or at death. In addition, you can use your GST exemption for a gift in trust, which should allow that gift to be held for the benefit of multiple generations for decades without incurring additional transfer taxes at each generation. Therefore, GST exempt trusts are very powerful tools for transferring wealth from generation to generation.

To use GST exemption for a gift in trust, GST exemption can be affirmatively allocated to that trust by filing a gift tax return. Even if GST exemption is not affirmatively allocated or a gift tax return is not filed, there are automatic allocation rules that may apply to transfers in trust that benefit a skip person.

Tracking the use of GST exemption is generally more complicated than tracking the use of estate and gift tax exemptions. In addition, the tax implications of the GST exempt character of a trust may only become relevant many years after the trust is created. Therefore, good record-keeping of each GST allocation during life and at death is important. For this reason, any use of GST exemption (whether reported or not) should be tracked and all gift tax returns and estate tax returns should be kept indefinitely.

Conclusion

There are many nuances and complexities to consider when determining how the transfer taxes may apply to a certain situation. Working with a qualified estate planning attorney will help you determine how the rules apply to you and your circumstances as well as how to best plan for these transfer taxes.

For more information, visit our [CIBC Private Wealth](#) page.

Example estate tax calculation

In 2025, Andrew made taxable gifts of \$5 million and he later died in 2026. Under his estate plan, his assets were distributed to named charities and his nieces and nephews.

Here is an explanation of the calculation of his estate tax:

Estate tax exemption in 2026:
\$15 million

Use of exemption for lifetime gifts: **\$5 million**

Remaining exemption amount at death: **\$10 million**

Value of assets Andrew owned at death: **\$25 million**

Less deductions for debts and charitable gifts: **\$5 million**

Less remaining exemption amount: **\$10 million**

Taxable Estate: **\$10 million**

Estate tax at 40% rate:
\$4 million