

# **Don't overlook tax apportionment when planning your estate**

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If you expect your estate to have a significant estate tax liability at your death, be sure to include a well-thought-out tax apportionment clause in your will or revocable trust. An apportionment clause specifies how the estate tax burden will be allocated among your beneficiaries. Omission of this clause, or failure to word it carefully, may result in unintended consequences.

## **Apportionment options**

There are many ways to apportion estate taxes. One option is to have all of the taxes paid out of assets passing through your will. Beneficiaries receiving assets outside your will — such as IRAs, retirement plans or life insurance proceeds — won't bear any of the tax burden.

Another option is to allocate taxes among all beneficiaries, including those who receive assets outside your will. Yet another is to provide for the tax to be paid from your residuary estate — that is, the portion of your estate that remains after all specific gifts or bequests have been made and all expenses and liabilities have been paid.

There's no one right way to apportion estate taxes. But it's important to understand how an apportionment clause operates to ensure that your clause is worded in a way that your wealth will be distributed in the manner you intend.

Suppose, for example, that your will leaves real estate valued at \$5 million to your son, with your residuary estate — consisting of \$5 million in stock and other liquid assets — passing to your daughter. Your intent is to treat your children equally, but your will's apportionment clause provides for estate taxes to be paid out of the residuary estate. Accordingly, the entire estate tax burden — including taxes attributable to the real estate — will be borne by your daughter.

One way to avoid this result is to apportion the taxes to both your son and your daughter. But that approach could cause problems for your son, who may lack the funds to pay the tax without selling the property. To avoid this situation while treating your children equally, you might apportion the taxes to your residuary estate but provide life insurance to cover your daughter's tax liability.

### **Omission of apportionment clause**

What if your will doesn't have an apportionment clause? In that case, apportionment will be governed by applicable state law (although federal law covers certain situations).

Most states have some form of an "equitable apportionment" scheme. Essentially, this approach requires each beneficiary to pay the estate tax generated by the assets he or she receives. Some states provide for equitable apportionment among all beneficiaries while others limit apportionment to assets that pass through the will or to the residuary estate.

Often, state apportionment laws produce satisfactory results, but in some cases they may be inconsistent with your wishes.

### **Avoid surprises**

If you ignore tax apportionment when planning your estate, your wealth may not be distributed in the manner you intend. We can answer your questions about taxes and estate planning.

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