

COMPARISON OF DRAFT OF NEW UNIFORM ESTATE TAX APPORTIONMENT ACT WITH THE CURRENT ACT

The current version of the Uniform Estate Tax Apportionment Act is set forth at §3-916 of the Uniform Probate Code. The major differences between the current version and the draft of the proposed new version of that Act are set forth below.

1. The current version of the Act apportions the federal estate tax and any additional inheritance tax imposed by designated states plus interest and penalties imposed on those taxes. §3-916(a)(5). The current version does not apply to foreign taxes nor to the federal or state generation-skipping tax.

The proposed new version of the Act will apportion all domestic and foreign taxes imposed because of an individual's death, and all interest and penalties associated with those taxes, except that it does not apportion any inheritance taxes, income taxes, or a generation-skipping tax on an event other than a direct skip. The proposed new version reaches foreign death taxes, and generation-skipping taxes on a direct skip, neither of which are covered by the current version. The proposed version does not cover inheritance taxes because an inheritance tax is borne by the recipient of the property that generated the tax, and so no apportionment is needed.

Both the current and the proposed new versions of the Act adopt an equitable apportionment scheme which treats equally the recipients of probate and nonprobate assets, and makes no distinction between residuary and other beneficiaries.

2. The current version apportions taxes according to the persons interests in the gross estate. Under IRC §2035(b), any gift tax paid on a gift made by the decedent within three years of his death is added to the decedent's gross estate. No person has received or will receive the portion of the gross estate that is attributable to the addition of a gift tax payment.

The proposed new version of the Act deletes the gift tax added to the gross estate from the computation of the amount to be apportioned. The proposed new version also subtracts from the gross estate the amount of deductible claims against and expenses of the estate.

3. The current version of the Act provides that an apportionment chosen by the decedent in a will, and only in a will, overrides the statutory apportionment scheme.

The proposed new version permits the statutory scheme to be overridden by the will, a revocable trust, or other dispositive provision. In the case of a conflict of apportionment provisions among two or more instruments, the proposed Act establishes an order of priority as to which instruction will control.

4. Under the present version of the Act, if one or more parties has a "time-limited interest" in a fund or property (such as a term interest, a life interest, or an annuity interest), any tax

apportioned to such interest and to the remainder interest is to be paid from the principal of the property or fund. §3-916(f). The payment is to be made from principal even if the remainder interest qualifies for a marital or charitable deduction. §3-916(e)(2), (f).

Under the proposed new version of the Act, the payment of taxes attributable to property or a fund in which there are time-limited interests depends upon whether the property or fund is unavailable for payment of the tax because of obstacles making collection impossible or impracticable. Such property is referred to as “Insulated property.” If collection from property or a fund is not impracticable or impossible, the property or fund is referred to as “Uninsulated property.” If the property or fund is Uninsulated property in which there are time-limited interests, the tax apportioned to interests in that property will be paid from principal. Section 6(b). The treatment of Uninsulated property is the same in the new version of the Act as it is in the old version. However, if the property is Insulated property in which there are time-limited interests, the treatment in the new version of the Act is more refined. The tax attributable to interests in the Insulated property is paid by persons owning interests in Uninsulated property in proportion to the values of their interests, and those payments constitute advancements to the persons having interests in Insulated property who otherwise would be required to pay the tax. Section 6(c). As a consequence of that advancement, the beneficiaries of interests in Uninsulated property who pay that tax will effectively own a fraction of the Insulated property for which the tax payment was made. When a distribution is subsequently made from the Insulated property, the distributee is required to pay a portion of the distribution to the beneficiaries of Uninsulated property. Section 6(c). In effect, the beneficiaries of Uninsulated property pay the tax allocable to Insulated property which is subject to a time-limited interest, and the Uninsulated beneficiaries thereby involuntarily acquire a percentage interest in the Insulated property. That general rule of advancements can be altered by a court if the court determines that it would be more equitable for the beneficiaries of the Insulated property personally to pay the tax allocated to that interest. Section 6(d).

5. The current version of the Act allocates the benefits from estate tax credits for gift taxes and foreign estate taxes paid by the decedent or his estate to all persons interested in the decedent’s gross estate. § 3-916(e)(3). The proposed new version makes a similar allocation. Section 5(c). However, the current version of the Act makes no reference to the allocation of credits for such taxes when paid by the recipient of the property on which the tax was payable. The proposed new version allocates the credits in such circumstances to the persons who paid the tax. Section 5(c).

6. The Internal Revenue Code has several provisions that, in certain circumstances, permit an election to be made that either provides a reduced valuation of certain property included in the gross estate, provides a special deduction for a “qualified family-owned business, or an exclusion of a portion of the value of land subject to a qualified conservation easement. See IRC §§ 2031(c), 2032A, and 2057. If conditions following the decedent’s death do not comply with statutory requirements, all or part of those special benefits will be recaptured. The current version of the Act does not state how the benefits derived from those special provisions are to

be allocated among the beneficiaries of decedent's property, nor does it state how the taxes incurred if any of those special benefits are recaptured in a subsequent year are to be allocated. The proposed new version of the Act addresses those issues in Section 7.

7. The Internal Revenue code provides an election for a deferral of payment of the federal estate tax in certain circumstances and requires that interest be paid on the deferred amount. See IRC §§ 6161(a), 6163, and 6166. The current version of the Act does not state how the tax benefits from the deferral are to be allocated among the beneficiaries, nor does it state how the interest expenses incurred from that deferral are to be allocated. Section 5(d) of the proposed new version addresses those issues.