Estate tax is a tax imposed by a government on the transfer of a person's property after that person dies. The word estate in law refers to the total collection of assets a person owns at the time of death. These assets can include real estate (land and buildings), bank accounts, stocks and bonds, retirement accounts, businesses, vehicles, jewelry, intellectual property, and any other property with financial value. The estate tax is calculated based on the total value of those assets before they are transferred to heirs or beneficiaries.

When a person dies, everything they own becomes part of their estate. Before that estate can be distributed to heirs, the law requires that debts, administrative costs, and certain taxes be paid. Estate tax is one of the possible taxes applied during this transfer process. It is sometimes called a transfer tax, meaning a tax imposed when ownership of property moves from one person to another because of death.

To understand estate tax clearly, it helps to understand the process called estate administration. Estate administration is the legal process through which a deceased person's assets are identified, valued, debts are settled, and property is distributed to heirs. In many cases this process takes place through probate, which is the court-supervised procedure used to verify a will and oversee the distribution of property. If estate tax applies, it is typically calculated during this administration period before assets are distributed to beneficiaries.

The amount of estate tax owed depends on the taxable value of the estate. The taxable estate is calculated by determining the total value of all assets owned by the deceased person and then subtracting certain deductions allowed by law. The starting point is the gross estate, which includes all property owned or controlled by the individual at the time of death. This includes not only property held directly in their name but also certain financial interests such as jointly owned property or certain types of trusts.

From the gross estate, several deductions may be subtracted to determine the taxable estate. Deductions may include debts owed by the deceased, funeral expenses, administrative costs of settling the estate, charitable donations made through the estate, and transfers to a surviving spouse. These deductions reduce the portion of the estate subject to taxation.

Estate tax systems usually include a threshold known as the estate tax exemption. The exemption is the amount of wealth that can pass to heirs without being taxed. Only the portion of an estate that exceeds the exemption level becomes subject to estate tax. In the United States federal system, the exemption amount has changed over time through legislation. When the value of an estate exceeds the exemption, the excess amount is taxed according to a schedule of rates.

The tax rates applied to estates are typically progressive, meaning higher portions of wealth are taxed at higher rates. A progressive tax system increases the percentage of tax applied as the taxable value increases. This structure means that very large estates may pay a larger percentage in tax compared to smaller estates that exceed the exemption threshold by only a small amount.

Estate tax is different from inheritance tax, although the two are sometimes confused. Estate tax is imposed on the estate itself before the assets are distributed. Inheritance tax, on the other hand, is imposed on the individuals receiving the inheritance. Under inheritance tax systems, each beneficiary may owe tax based on the value of what they receive. Some countries use one system, some use the other, and some use both.

The concept of estate taxation is tied to the idea that large concentrations of wealth transfer across generations when individuals die. Governments historically introduced estate taxes as a way to generate revenue from these large wealth transfers. In many countries the estate tax primarily affects only very large estates because the exemption threshold excludes smaller estates from taxation.

In addition to estate tax, many countries also impose a gift tax. Gift tax applies to transfers of property made during a person's lifetime. Governments created gift taxes partly to prevent individuals from avoiding estate tax by giving away all of their assets before death. Gift taxes and estate taxes are often connected within the same legal system and share common exemption limits.

Estate tax systems often interact with trust structures and estate planning strategies. Estate planning refers to the legal and financial preparation for how assets will be managed and distributed after death. Certain types of trusts may remove assets from the taxable estate if they are structured according to legal rules and transferred during the grantor's lifetime.

For example, when assets are placed into some forms of irrevocable trusts, the original owner may no longer legally control or own those assets. Because ownership has been transferred to the trust, those assets may not be counted as part of the grantor's estate at death, depending on how the trust is structured and when the transfer occurred.

Another concept relevant to estate taxation is the step-up in basis. The basis of an asset refers to the value used to calculate capital gains taxes when the asset is sold. When heirs inherit certain assets, the tax basis may be adjusted to the market value of the asset at the time of the original owner's death. This adjustment can reduce future capital gains taxes if the asset is sold.

Estate tax therefore functions as a tax on the transfer of accumulated wealth at death. The government determines the value of the deceased person's estate, subtracts allowable deductions and exemptions, and applies tax rates to the remaining taxable portion. The tax is typically paid before the estate is distributed to heirs, ensuring that government revenue is collected during the process of transferring property from one generation to the next.