A federal tax is imposed on the value of estates that exceed a statutory exclusion. That threshold of untaxed value is $1,000,000 for individuals dying in 2002 and 2003; $1,500,000 in 2004 and 2005; $2,000,000 in 2006 through 2008; and $3.5 million in 2009. Under current law, the estate tax will expire on December 31, 2009, only to be reinstated on January 1, 2011.

Heirs may choose to determine the value of an estate on the date of death or exactly six months later. Surviving spouses never have to pay federal estate tax on amounts they inherit, no matter how large.

The tax rate starts at 18% and increases to 50% in 2002 (49% in 2003) for taxable estates worth more than $2.5 million. However, any amount that might be taxed in the low brackets is covered by the exclusion discussed in the first paragraph above. As a practical matter, then, the estate tax begins at 41% on amounts over $1 million and goes as high as 50 % on amounts over $2.5 million.

Family-run farms and businesses that are passed on to younger generations may be entitled to a special $1.3 million exclusion of value to reduce the estate tax burden on them. To qualify, the heirs must have been actively involved in running the business. If they do owe estate tax, the heirs who run these enterprises have 14 years to pay.

To keep an estate within the exclusion limit, an individual can give as much as $11,000 a year - tax-free - to an unlimited number of people, from close relatives to strangers. A couple can give $22,000 jointly. Under a 1997 law that ties the tax-free gift limit to inflation, the limit may continue to increase in $1,000 increments when inflation justifies an increase.