

## COMMON INCOME TAX COMPLIANCE FOR ESTATES

*If you have any questions  
about this Advisory,  
please contact:*

**MICHAEL T. CLEAR**  
203.363.7675  
mclear@wiggins.com

**VERONICA R. S. BAUER**  
561.701.8701  
vbauer@wiggins.com

**ROBERT W. BENJAMIN**  
212.551.2602  
rbenjamin@wiggins.com

**DANIEL L. DANIELS**  
203.363.7665  
ddaniels@wiggins.com

**SETH ELLIS**  
561.910.7510  
sellis@wiggins.com

**HELEN C. HEINTZ**  
203.363.7607  
hheintz@wiggins.com

**DAVID W. KESNER**  
203.498.4406  
dkesner@wiggins.com

**LEONARD LEADER**  
203.363.7602  
lleader@wiggins.com

**VANESSA L. MACZKO**  
203.363.7667  
vmaczko@wiggins.com

Income tax reporting obligations do not cease at death. In fact, there may be multiple taxpayers required to file income tax returns after the death of an individual. For example, the decedent, the executor of the decedent's estate and trustees of trusts created by the decedent each has income tax reporting requirements. The basics of income tax compliance in this scenario is best illustrated through the following example:

**EXAMPLE.** Assume a married individual dies on June 30, 2024. His lifetime estate planning included assets in his own name, assets in his revocable trust, and assets in an irrevocable grantor trust. Below is an illustration of the income tax reporting requirements for each.

**Final personal income tax return.** The executor will need to file the decedent's final income tax return to report income and losses for the period from January 1 – June 30, 2024. The return, a Form 1040, will be due and any tax must be paid by April 15, 2025. The return will include any income or loss generated in the decedent's own name, in the name of the revocable trust and from the irrevocable grantor trust. If the decedent typically filed a joint return with his spouse, a joint return can be filed for 2024. The joint return should reflect the spouse's income for January through December and the decedent's income for January through June 30, 2024. Any income earned by the decedent after the date of death should be reported on the estate's income tax return.

**Estate's income tax return.** At the decedent's death, the estate becomes its own tax paying entity and must file a Form 1041 to report income and losses generated by the estate during its tax year. The executor can elect either a calendar year (ending on 12/31 each year) or a fiscal year. A fiscal year cannot extend past the last day of the month before the decedent's date of death. As an example, the longest fiscal year for our hypothetical would end on May 31, 2025. Note that the executor may elect a shorter fiscal year as well – having the fiscal year end at any month selected by the fiduciary. Special consideration should be given when selecting the tax year for an estate. Selecting a long fiscal year has an advantage of delaying the initial filing requirement. Also, in certain situations, the fiscal year may be long enough that the estate can file a first and final income tax return. Selecting a calendar year has the advantage of using a year-end date which matches the timeline for when that tax reporting information like W-2, 1099s and K-1s are issued.

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**ERIN D. NICHOLLS**

203.498.4319  
enicholls@wiggin.com

**CAROLYN A. REERS**

203.363.7668  
creers@wiggin.com

**MATTHEW E. SMITH**

203.363.7639  
msmith@wiggin.com

**WILLIAM M. BROMLEY**

561.910.7530  
wbromley@wiggin.com

**GEORGE R. FREUND**

561.910.7500  
gfreund@wiggin.com

**KATERYNA BAKHNAK**

212.551.2855  
kbakhnak@wiggin.com

**MARY MARGARET COLLEARY**

212.551.2637  
mcolleary@wiggin.com

**RUTH FORTUNE**

203.363.7658  
rfortune@wiggin.com

**ASHTON C. MALKIN**

561.910.7500  
amalkin@wiggin.com

**MARISSA A. O'LOUGHLIN**

203.363.7674  
moloughlin@wiggin.com

**KAITLYN A. PACELLI**

203.363.7635  
kpacelli@wiggin.com

**ANDREW S. PHILBIN**

203.363.7606  
aphilbin@wiggin.com

**MI-HAE K. RUSSO**

212.551.2619  
mrusso@wiggin.com

**Revocable Trust.** Trusts are calendar year tax paying entities, so an income tax return (a Form 1041) would be due for the period July 1, 2024 through December 31, 2024. This return is due and any tax must be paid by April 15, 2025. Note, however, that the executor can elect to treat the estate and the revocable trust as one entity. This election, known as a 645 Election because of the code section that permits it, is made on the estate's first income tax return. If the 645 election is made, all of the revocable trust income is reported on the estate's income tax return.

**Irrevocable Grantor Trust.** The income earned by the irrevocable grantor trust from January 1, 2024 through June 30, 2024 will be reported on the decedent's personal income tax return. Many accountants will file a grantor trust return reporting that the income will be reported on the grantor's personal income tax return. Any income earned from July 1, 2024 through December 31st, 2024 will be reported on a Form 1041 Trust Tax Return. The Trust will always be a calendar year entity and the tax return will be due on April 15 of the following year.

**Tax Identification Numbers.** At the decedent's death, each new entity should get new tax identification numbers: (1) the estate, (2) the revocable trust and (3) the irrevocable grantor trust. EINs are issued by the IRS through its website.

The estate's EIN cannot be received until the executor is appointed by a court, and accounts for the estate cannot be opened until the executor is appointed and the EIN is issued. Therefore, there is a time lag between date of death and when assets are moved into estate accounts and reported under the estate's EIN. During this lag, income and losses should be reported by the estate even if they not reported under the estate's EIN. Therefore, the tax preparer will often need to review accounts and allocate income between the decedent's Form 1040 and the estate's Form 1041.

The Trustee of the revocable trust should apply for an EIN shortly after the decedent's death and move assets into a new account under the new EIN for the revocable trust. Similarly, the Trustee of the irrevocable grantor trust should also apply for a new EIN so that income can be tracked more easily for tax reporting. Sometimes an irrevocable grantor trust will already have an EIN; however, best practice suggests that the trust apply for and receive a new EIN after the decedent's death to avoid confusion on reporting trust income.

**Summary.** Accurate income tax reporting is key during an estate administration process. As discussed above, during this process, the executor will be responsible for filing a final income tax return for the decedent. Additionally, the executor will work to file tax returns for the other entities associated with the estate and trust administration. Working closely with the attorney for the estate and a CPA is often the best route for tax compliance. If you have any questions and would like to discuss this topic further, consider reaching out to your Wiggin and Dana attorney.

*This publication is a summary of legal principles. Nothing in this article constitutes legal advice, which can only be obtained as a result of a personal consultation with an attorney. The information published here is believed accurate at the time of publication, but is subject to change and does not purport to be a complete statement of all relevant issues.*