

## Portability - Clarification on a new Estate Planning Tool

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Portability is a federal estate tax planning tool for married individuals with potentially taxable estates. This past June, the Internal Revenue Service (IRS) passed final regulations (applicable to estates of decedents dying on or after June 12, 2015) clarifying some lingering questions about and specifying how to elect portability.

U.S. residents can transfer an unlimited amount of assets to their spouse during their life and at death, with certain limitations for non-citizen spouses. However, they are only allowed to transfer \$5.45 million (in 2016, indexed for inflation) in assets during their life or at death to a *non-spouse* before paying a gift or estate tax. For those households with assets *over* the \$5.45 million exemption, planning involves minimizing estate taxes through various techniques. For households with assets *under* the exemption, there are still planning options to consider, in particular, portability. So, how do you minimize estate taxes when the surviving spouse dies?

Before portability was enacted by Congress in 2011, any unused portion of an individual's estate and gift tax exemption expired when he or she died. This potentially created the situation where a surviving spouse who received significant assets from his or her deceased spouse ended up with an estate that exceeded his or her own gift/estate exemption and resulted in a high estate tax liability.

In the past, a series of trusts were often used to preserve the deceased spouse's exemption to minimize the estate tax at the time of the surviving spouse's death. Generally, a complex formula in the deceased's will or living trust document would direct the assets, up to the federal estate tax exemption in the year of the death, into a trust or a series of trusts, with the remainder of the assets going to the surviving spouse, either directly or through additional trusts.

Now, with portability, the executor of an estate can elect to have the deceased spouse's unused exemption (DSUE) amount transfer to the surviving spouse to then be further transferred during his or her life and at death to whomever he or she wishes to designate. This irrevocable election is made on a timely filed estate tax return (Form 706) of the first spouse to die. For the election to be timely made, it must be present on an estate return filed within nine months of the date of death or the last day covered by an extension.

What about married couples who want to elect portability, but wouldn't normally need to file an estate tax return? The final regulations eased the compliance burden for estates whose gross asset value is below the exclusion amount of \$5.45 million, by providing an automatic six-month extension of time to file an estate tax return to make the portability election. In addition, only descriptions of assets are needed and specific asset values are not required to be listed on the return for property passing to the surviving spouse or charity. Relief has also been provided for non-citizen surviving spouses. Be warned however, the IRS also confirmed that it will have broad authority to examine the estate return of a deceased spouse when determining the DSUE

amount allowed for the surviving spouse. This potentially extends the time horizon for when the IRS can propose changes on a previously filed estate tax return.