

## **IRS Explains Rules for Estate-tax Portability**

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the "2010 Tax Relief Act") features the most generous federal estate-tax exemption ever. Furthermore, for the first time, exemptions are deemed to be "portable" between spouses. Now the IRS has issued new guidance for those people who elect to use this provision.

Background: Prior to the 2010 Tax Relief Act, the estate-tax exemption gradually increased from its previous high of \$1 million in 2001 to \$3.5 million in 2009, before the estate tax was effectively repealed for 2010 only. These changes were coordinated with other provisions in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), such as reductions in the estate-tax rates and modified "carryover basis" rules.

The new law reinstates the estate tax repealed by EGTRRA, but also allows a \$5 million exemption for decedents dying in 2011 and 2012. (The IRS recently announced that the inflation-adjusted exemption for 2012 is \$5.12 million.) In addition, exemptions are portable between spouses, so the estate of a surviving spouse may be able to use a portion of the unused exemption from the first spouse to die.

A new notice from the IRS clarifies the portability rules. Significantly, an estate that wants to transfer the unused estate-tax exclusion of a deceased spouse to a surviving spouse must file an estate-tax return, but will not need to make an affirmative election. The estate of the spouse will be considered to have made the portability election as long as it files a timely estate-tax return. In the new notice, the IRS also emphasized that the estates of decedents dying before 2011 cannot transfer an unused exclusion amount.

Note that an estate of a decedent dying in 2011 with assets under \$5 million would not owe any estate tax and would not normally file an estate-tax return. However, under the new notice, these estates must file the return to benefit from the portability provision, even if no estate tax is owed. Normally, the return is due nine months after the date of death. An executor can request a six-month extension.

The 2010 Tax Relief Act also requires the estate making a portability election to compute the deceased spouse's unused exclusion amount. Until the estate-tax return is revised, the IRS says that simply completing the estate-tax return will satisfy this requirement. If the executor of a small estate does not want to make a portability election, he or she does not have to file an estate-tax return. If a return is otherwise required, the executor should

follow the IRS instructions. Finally, the IRS indicated that it will be issuing regulations on implementing the portability provisions.

Caution: The rules in this area are subject to change after 2012. Contact an experienced estate-tax professional for further guidance.