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August 5, 2012

## How the portability of federal estate tax may be a benefit

In 2010, Congress temporarily but significantly altered the rules for Federal Estate Tax, Generation Skipping Tax, and Gift tax. The applicable estate tax exclusion was increased to \$5 million with a lower minimum tax rate of 35 percent. The exemption for gifts made during lifetime was also raised to \$5 million, in addition to the annual exclusion amount of \$13,000 (or \$26,000 per couple). "Portability" was also introduced for those who died in 2011 and 2012. This last aspect was likely largely ignored by most widows and widowers, since a federal estate issue seemed to most to be unlikely. However, since the federal estate tax rules are temporary, that are set to expire at the end of 2012, many are predicting that we may drive off the "fiscal cliff" on January 1, 2013. How the federal estate tax rules will be revised is unknown, but may automatically revert to an exemption that is less than \$1 million, and with a much higher minimum tax rate. It is very difficult for lawyers to assist their clients in estate planning with such an uncertain future for the tax laws. Portability may be a good option for widows and widowers to elect this year in light of that uncertainty.

Portability refers to the ability for the surviving spouse to take advantage of the unused portion of the estate tax exclusion that remains after the death of the first spouse, and add it to his or her own applicable exclusion, thus avoiding significant estate tax for his or her eventual heirs. For instance, since the applicable exclusion is \$5 million in 2011 and 2012, and the first to die has a \$1 million estate (which would not trigger the need to file a federal estate tax return), the surviving spouse could elect to file an estate tax return and preserve a \$4 million exclusion in addition to his or her exclusion at the time of her death. The surviving spouse may want to consider this due to the unknowns related to the future estate tax applicable exemption amounts (it may return to \$1 million or less), or due to an unexpected windfall such as a lottery win, an offer on real estate that results in large profits, or oil and gas lease profits to name a few. A widow with a farm that seems to be valued at \$500,000 could later be offered millions which she would have no way to shelter from federal estate tax (this true scenario came up at a recent PBI Elder Law Institute session).

Some couples plan for federal estate tax with credit shelter trusts in their Wills. However, in recent years, these trusts have fallen into disfavor due to the limitations on the surviving spouse's use of the marital assets, and the high exclusion amount which seemed to negate the need for such estate planning. Disclaimer trusts in the Wills often solve this particular problem; however, this has not been standard estate planning in recent years due to the high exclusion amounts after an evaluation of the couple's overall known resources. In any event, for those who died in 2011, or in 2012 without any such planning, portability remains an option to be carefully considered.

A timely filed federal estate tax return is necessary to capture the portability election. The IRS recently developed regulations to simplify the federal estate tax return, making it more affordable to file. Furthermore, for those who died in 2011, the deadline for filing was extended from the normal 9 months (although an extension can be requested) to 15 months where no extension was requested. Consider consulting your attorney for a discussion as to whether a portability election is something that should be considered in your situation.