



## IRS Guidance on Estate Tax Portability *by Bruce A. Rawls*

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 amended the Internal Revenue Code to allow the estate of a decedent who is survived by a spouse to make a "portability election" which allows the surviving spouse to apply the decedent's unused exemption amount (known as the "DSUE amount") to the surviving spouse's lifetime gifts or transfers at death (*i.e.*, to transfers which may be subject to the federal gift tax if made during the surviving spouse's lifetime or subject to the federal estate tax if made at the death of the surviving spouse). The portability provisions were scheduled to expire on January 1, 2013, but Congress permanently extended the portability provisions in the American Taxpayer Relief Act of 2012.

The Internal Revenue Service has just released Revenue Procedure 2014-18 (2014-7 IRB) which provides guidance on the means by which estates of decedents who died before January 1, 2014, may elect to take advantage of the estate tax "portability" election if the value of the estate is below the threshold required for the filing of a federal estate tax return. The effect of making the "portability" election can be illustrated as follows:

Fred Jones died on February 17, 2011, survived by his wife, Martha. The assets includible in Fred's gross estate for federal estate tax purposes amounted to \$2,000,000, all of which were left to Martha under Fred's Will. Fred made no taxable gifts during his lifetime. Given the value of Fred's estate, Fred's executor was not required to file a federal estate tax return. Martha dies on December 20, 2013, and at the time of her death her taxable estate is valued at \$8,000,000, and, like Fred, Martha made no taxable gifts during her lifetime. Martha's executor will file a federal estate tax return on or before its due date of September 20, 2014. Absent the ability to claim the unused portion of Fred's federal estate tax exemption, Martha's executor will be required to pay estate tax on the \$2,750,000 in excess of Martha's estate tax exclusion amount, which is \$5,250,000. Had Fred's executor filed a federal estate tax return and made a "portability election" Fred's unused estate tax exemption would have become "portable" and could have been used on Martha's estate tax return, in which case Martha's estate would have totally avoided the tax.

In order for Martha's estate to get the benefit of portability described in the example above, the executor of Fred's estate must file a federal estate tax return on which a portability election is made. That tax return must also include a calculation of Fred's DSUE amount. Not only does an estate tax return have to be filed, but a portability election is effective only if made on an estate tax return that is filed on a timely basis, which is determined including any extensions for filing such return. The due date of an estate tax return required to elect portability is nine months after the decedent's date of death or the last day of the period covered by an extension (if a filing extension has been obtained).

**Automatic extension.** In Revenue Procedure 2014-18 the IRS has provided some welcome relief to taxpayers who have failed to make a portability election because the value of the estate of the first spouse to die was not large enough to require the filing of a federal estate tax return. If the criteria prescribed in Revenue Procedure 2014-18 are met, the IRS has announced that it will provide an automatic extension of the time to elect portability. The requirements that must be met to qualify for the automatic extension are:

- 1) the decedent (a) has a surviving spouse; (b) died after December 31, 2010, and before January 1, 2014; and (c) was a citizen or resident of the U.S. on the date of death;
- 2) based on the value of the gross estate, the decedent's estate is not required to file an estate tax return;
- 3) the decedent's estate did not file an estate tax return within the time prescribed for filing an estate tax return required to elect portability;
- 4) a person permitted to make the election on behalf of a decedent must file a complete estate tax return on or before December 31, 2014; and
- 5) the person filing the estate tax return must state at the top of the return that the return is "FILED PURSUANT TO REV. PROC. 2014-18 TO ELECT PORTABILITY UNDER CODE SEC. 2010(c)(5)(A)."

If it is ultimately determined that the decedent's estate was required to file an estate tax return (because, for instance, the decedent's estate had a higher value than thought), the grant of an extension under Revenue Procedure 2014-18 becomes void.

Taxpayers who are not eligible for relief under Revenue Procedure 2014-18 because they do not meet the requirements listed above or because the decedent died after December 31, 2013 can request an extension to make a portability election by requesting a letter ruling as provided in regulations prescribed by the IRS. The IRS has provided, in Revenue Procedure 2014-1, the procedural requirements for requesting a letter ruling.

**Limitations period for claim for credit or refund by surviving spouse.** Generally, if a taxpayer has made an overpayment of tax, the taxpayer must file a claim for credit or refund of the overpayment within three years from the date of filing the tax return, or within two years from the date of payment of the tax, whichever period expires later. Accordingly, to obtain a credit or refund of an overpayment of tax by reason of a portability election made pursuant to a grant of relief under Revenue Procedure 2014-18, the surviving spouse (or the executor of the estate of the surviving spouse) of the decedent must file a claim for credit or refund of tax before the expiration of the limitations periods prescribed above. Revenue Procedure 2014-18 included the following example:

Predeceasing Spouse (S1) dies on January 1, 2011, survived by Surviving Spouse (S2). The assets includable in S1's gross estate consist of cash on deposit in bank accounts held jointly with S2 with rights of survivorship in the amount of \$2,000,000. S1 made no taxable gifts during life. S1's executor is not required to file an estate tax return and does not file such a return.

S2 dies on January 14, 2011. S2's taxable estate is \$8,000,000, and S2 made no taxable gifts during life. S2's executor files a Form 706 (a federal estate tax return) on behalf of S2's estate on October 14, 2011, and includes payment of the estate tax on the \$3,000,000 in excess of S2's applicable exclusion amount.

Pursuant to Revenue Procedure 2014-18, S1's executor files a Form 706 on behalf of S1's estate on November 1, 2014, reporting a DSUE amount of \$5,000,000. In 2015, IRS (i) determines that S1's estate has met the requirements for a grant of relief under this revenue procedure and is deemed to have made a valid portability election, (ii) accepts S1's return with no changes, and (iii) issues an estate tax closing letter to S1's estate.

To recover the estate tax paid, S2's executor must file a claim for credit or refund of tax by October 14, 2014, even though a Form 706 to elect portability has not been filed on behalf of S1's estate at that time. Such a claim filed in anticipation of the filing of the Form 706 by S1's executor will be considered a protective claim for credit or refund of tax. Accordingly, as long as the claim of S2's estate for credit or refund of tax was filed by October 14, 2014, IRS can consider and process that claim for credit or refund of tax once S1's estate is considered to have elected portability pursuant to Revenue Procedure 2014-18.

**For assistance, please contact:**

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