# PORTABILITY IN THE NEW AGE OF ESTATE PLANNING

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**CHAPTER 18**

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## EXPERIENCE

**CAMPBELL & RIGGS, P.C.** **SEPTEMBER 2004-PRESENT**

Shareholder. Represent business owners and other wealthy individuals, charities and corporate fiduciaries. Experience includes preparation of complex wills, trusts, and powers of attorney, health care planning, charitable gift planning, gift and estate tax compliance and planning, creation and transfer of interests in corporations and family limited partnerships, and IRS audits. Assist individual and corporate fiduciaries in complex estate administration, probate proceedings, tax returns, and funding of bequests. Work with charitable organizations including receipt and structuring of gifts and examination of tax issues.

## MEMBERSHIPS

***Board Certified in Estate Planning and Probate by the Texas Board of Legal Specialization***. *Board Member*: Houston Business and Estate Planning Council; The Society of Financial Service Professionals. *Member*: State Bar of Texas Real Estate, Probate, and Trust Law Section; Houston Bar Association Probate, Trust, and Estate Section; Houston Estate and Financial Forum; American Bar Association; Houston Wealth Advisors Forum.

## EDUCATION

**THE UNIVERSITY OF TEXAS AT AUSTIN**
***Doctor of Jurisprudence with Honors*** **1998**

**WASHINGTON UNIVERSITY IN ST. LOUIS**
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## ARTICLES & SPEECHES

**2014 Houston Business and Estate Planning Council**
*"Panel Discussion on Estate Planning with Oil and Gas"* – May 17, 2014

**2013 Houston Bar Association Probate, Trusts & Estate Section**
*"Planning with Oil and Gas Interests: What Every Estate Planner Should Know (But may be Afraid to Ask)"* – May 28, 2013

**2011 Houston Bar Association What the General Practitioner Needs to Know Institute – Civil Day**
*"The Estate Planning Toolbox"* – October 28, 2011

**2011 Houston Bar Association Probate, Trusts & Estate Section**
*"Planning for Spouses in 2011 and 2012: Opportunities and Pitfalls"* – September 27, 2011

**2010 Texas State Bar Advanced Estate Planning Strategies Course**
*"What Do We Do Now That We Have NO Estate Planning Toolbox"* – April 8, 2010

**2009 Houston Bar Association Wills and Probate Institute**
"*The Estate Planning Toolbox*" – February 13, 2009

**2008 Texas Estate Planning and Probate Practice for Paralegals Seminar**
*"Assisting in the Probate Process"* – March 28, 2008

**2006 South Texas College of Law Wills and Probate Institute**
*"The Texas Doctrine of Fraud on the Spouse"* – September 15, 2006

**2002 Texas Bankers Association Estate Administration Seminar**
*"Pre & Post Mortem Planning for Retirement Accounts"* – October 9, 2002

**2001 Houston Bar Association CLE Seminar**
*"Hot Topics in Community Property Issues"* – March 22, 2001

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# PORTABILITY IN THE NEW AGE OF ESTATE PLANNING

## I. INTRODUCTION

The last decade has seen remarkable changes for estate planners. Not so long ago, we lived in a world with a $600,000 exemption equivalent for estate and gift taxes, and a 55% top marginal rate, and today we have a $5 million exemption equivalent (now indexed for inflation, and currently $5.34 million) and a top tax rate of 40%. Along the way, we lost the estate tax for a year, and in its place received a new (albeit temporary) basis regime as an option. Suffice it to say, this period has been both a blessing and a curse for estate planners. A blessing in that it has driven a lot of client interest (and work) to adjust estate plans and take advantage of opportunities afforded by the changes (especially at the end of 2012); a curse in that it has caused us to work overtime to keep up with the changes and taken away something that many of us value in our practice: the ability to rely on tried and true estate planning methods when advising our clients.

Enter into that equation something that has been discussed for a long time as an important addition to the estate tax regime: portability. While seen by many as relief for those married couples who are unwilling or unable to plan for their estates, upon closer inspection, there are a number of confusing provisions and unintended side effects, while at the same time, some opportunities for creative estate planning. While portability may now be permanent[1], that fact does not make the job of the estate planner any easier. What used to be a fairly routine discussion with clients has now become far more complicated by number of factors that we have a difficult time understanding ourselves, much less explaining to clients.

## II. LEGISLATIVE HISTORY OF PORTABILITY

The concept of portability was first introduced on December 17, 2010 as part of the Tax Relief Unemployment Insurance Reauthorization, and Job Creation Act of 2010[2] (the "TRA 2010"). Portability was inserted as revisions to Sections 2010 and 2505 of the Internal Revenue Code of 1986, as amended (the "Code"), as will be discussed in great detail below.

Although portability was a welcome addition to the tax code (even if no one seemed to be clamoring for it), the benefits initially appeared to be short-lived, given some confusing verbiage in the statute and the fact that it would expire on its own terms at the end of 2012. The Staff of the Joint Committee on Taxation added to the confusion by issuing an example that seemed to run contrary to the language in TRA 2010, as discussed later in this outline. However, the IRS did provide some clarity in the form of Notice 2011-42 (stating how the election would be made) and Notice 2012-21 (giving a six-month extension for estates of decedents who died in the first half of 2011).

To the great relief of estate planners everywhere, on June 15, 2012, the Treasury Department issued Temporary and Proposed Regulations to Code Sections 2010 and 2505 that provide much needed clarity and, in some cases, surprisingly taxpayer friendly interpretations of the statute. The Temporary Regulations apply only to the estates of decedents who died after January 1, 2011 and will expire three years from the date of issuance unless final regulations are issues (which is expected).

All of this would have been for naught if portability was allowed to expire on December 31, 2012. However, that did not happen, and the American Taxpayer Relief Act of 2012 ("ATRA 2012") was passed on January 2, 2013 and signed into law on January 4, 2013. In addition to making portability permanent, ATRA also made the recently re-unified exemption amount for estates and gifts $5 million, indexed for inflation, and raised the top rate from 35% to 40%.

While we are still waiting for final Regulations, we did receive some additional good news recently in the form of Rev. Proc. 2014-18, which gives relief to taxpayers who failed to file an extension of time to elect portability. This only applies to the estates of decedents who died after 12/31/2010 and before 12/31/13, so it has limited applicability, but it will be discussed more later.

## III. THE RULES

### A. How to Compute the "DSUE Amount"

Section 2010(c)(2) of the Code defines the "applicable exclusion amount" as the sum of:

1) the basic exclusion amount, and
2) in the case of a surviving spouse, the deceased spousal exclusion amount.

The basic exclusion amount is defined in Code Section 2010(c)(3) as $5,000,000, as adjusted by inflation each year beginning after 2011 (in 2014, it is $5,340,000).

The deceased spousal unused exclusion amount (or DSUE Amount, for short) is found in Code Section 2010(c)(4), which states:

> For purposes of this subsection, with respect to a surviving spouse of a deceased spouse dying after December 31, 2010, the term

[1] That is, until Congress decides to change it again.

[2] Pub. L. 111-312, 111th Cong., 2nd Sess. (Dec. 17, 2010), 124 Stat. 3296.

> "deceased spousal unused exclusion amount" means the lesser of –
>
> a) the basic exclusion amount, or
> b) the excess of –
>
> i) the *applicable* exclusion amount of the last such deceased spouse of such surviving spouse, over
> ii) the amount with respect to which the tentative tax is determined under section 2001(b)(1) on the estate of such deceased spouse.
>
> (emphasis added).

In its most straightforward application, when one spouse dies survived by the other spouse, the surviving spouse's applicable exclusion amount can include the deceased spouse's DSUE Amount, assuming that the proper election is made (which is discussed in great detail below). Assuming the surviving spouse never remarries, he or she can utilize that increased applicable exclusion amount during his or her life through gifts, or to shelter assets from estate tax at death.

1. DSUE Amount Cannot Be More Than Basic Exclusion Amount in Year of Deceased Spouses Death

While the surviving spouse's basic exclusion amount will continue to increase with inflation, the DSUE Amount can never be more than the deceased spouse's basic exclusion amount at the time of his or her death. Temp. Reg. § 20.2010-2T(c)(1)(i).

*Example*. Henry and Casey are a married couple. Henry dies in 2011, leaving his entire estate outright to Casey. Casey's potential DSUE Amount from Henry is $4 million ($5 million basic exclusion, less $1 million in adjusted taxable gifts). Assuming Casey does not make any taxable gifts during her life and dies in 2014, her applicable exclusion amount would be $10,340,000 ($5.34 million, which is Casey's basic exclusion amount in 2014, plus Henry's $5 million DSUE Amount).

2. "Use it or Lose it"

A surviving spouse can only use the DSUE Amount from his or her last deceased spouse. If a surviving spouse remarries and the new spouse predeceases the surviving spouse, the surviving spouse can only use that most recent (deceased) spouse's DSUE Amount. Temp. Reg. § 20.2010-3T(a)(1). In fact, the second deceased spouse has no DSUE Amount, or if the executor of the second deceased spouse's estate fails to make a portability election, then the surviving spouse can see their prior DSUE Amount reduced to $0. Temp. Reg. § 20.2010-3T(a)(2).

*Example*. If Scott predeceases Ramona in 2011 and leaves his $2 million estate to his children, then Ramona's DSUE Amount from Scott would be $3 million, when added to her $5 million, equaling an $8 million estate tax applicable exclusion amount. Ramona then remarries Gideon, who dies and leaves his entire $5 million estate to his children, leaving Ramona with a $0 DSUE Amount. As a result, Ramona's applicable exclusion went from $8 million (her basic exclusion amount plus Scott's $3 million DSUE Amount) to $5 million (her basic exclusion amount).

However, since the DSUE Amount is based on the last deceased spouse, even if a surviving spouse remarries, he or she should keep the DSUE Amount from the last surviving spouse as long as they die before the new spouse. Temp. Reg. § 20.2010-3T(a)(3). Furthermore, divorce does not have any effect on the DSUE Amount, because the ex-spouse's death will not be considered a "last deceased spouse" because they were no longer married. *Id*.

3. Computing DSUE Amount When There are Multiple Deceased Spouses

The computation of the DSUE Amount, while seemingly simple in concept, becomes much more complicated if the surviving spouse remarries. If our newly married surviving spouse (we'll call her SS1) now passes away, survived by her own surviving spouse (we will call him SS2), what amount of DSUE would SS2 be able to claim from SS1's estate? This question was the cause of some concern based on the original language of ATRA 2010, which seemed to limit the DSUE Amount that could be claimed by SS2 to an amount not greater than the basic exclusion amount of SS1, less the taxable estate of SS1 or any lifetime gifts made by SS1. In effect, any DSUE that SS1 might have received from her deceased spouse (DS1) would not count when computing SS1's DSUE Amount. While this may seem confusing (and it is), it is no longer an issue, as the statute was interpreted by the Temporary Regulations, and then modified by TRA 2012. As a result, SS1 is now deemed to have used her DSUE from her deceased spouse first *before* her basic exclusion amount is reduced. Some examples might be helpful.

*Example*. Casey remarries Ron, then Casey dies in 2014. Casey's applicable exclusion amount is $10.34 million. Ron wants to claim Casey's DSUE Amount and add it to his basic exclusion amount. The largest amount Ron can claim is $5.34 million, which is the basic exclusion amount in the year of Casey's death. But what if Casey leaves her $5 million estate to her children? Under TRA 2010, Ron's DSUE

Amount would have been $340,000, but under the modified language of TRA 2012, Ron can still claim a $5.34 million DSUE from Casey (her $5 million taxable estate is absorbed first by the DSUE Amount Casey received from Henry).

Likewise, if Casey made taxable gifts during her life of $5 million, the same result would apply, meaning the taxable gifts use up Henry's DSUE Amount first before using Casey's basic exclusion amount. The ability to use the DSUE Amount has important planning implications that will be discussed below.

4. Adjustment for Gift Taxes Paid

There is one other adjustment to DSUE Amount that is worth mentioning. If the deceased spouse made taxable gifts that required the payment of gift taxes, the amount of the adjusted taxable gifts of the decedent is reduced by the amount of taxable gifts, if any, on which gift taxes were paid for the calendar year of the gift(s). Temp. Reg. § 20.2010-2T(c)(2). This achieves an equitable result where otherwise the DSUE Amount would be reduced by amounts that were taxable and did not actually utilize the deceased spouse's exemption in the year of the gift.

**B. Gifting Strategies – the Ability to Use DSUE Amounts from Multiple Deceased Spouses**

The Temporary Regulations make it clear that applicable exclusion amount will include the DSUE Amount from the last deceased spouse, which may be applied at the surviving spouse's death as well as against taxable gifts made during the surviving spouse's life. Temp. Reg. §§ 20.2010-3T(a)(1), 25.2505-2T(a)(1). While this seems straightforward at the surviving spouse's death, it creates some interesting questions on how this rule is applied to lifetime gifts.

One thing is made explicit, which is that when the surviving spouse who has added a DSUE Amount to her applicable exclusion amount makes a gift, that the DSUE Amount is applied to the taxable gift before the surviving spouse's basic exclusion amount. Temp. Reg. §25.2505-2T(b). This is an incredibly helpful and taxpayer friendly position that, until the Temporary Regulations were issued, was not at all clear from the statute.

1. Effect of Subsequent Remarriage DSUE Amount Gifts

But what if the surviving spouse made gifts during life that used the DSUE Amount, then later remarries, and the new spouse predeceases her, becoming the "new" last deceased spouse?

*Example*. Let's refer to this as the "*Private Benjamin Example*." Judy marries Yale, who dies on their wedding day. Judy claims Yale's DSUE Amount and adds it to her basic exclusion amount. Later, Judy makes a taxable gift to Captain Lewis, which is equal to the DSUE Amount. Judy later marries Henri, who also dies shortly thereafter, leaving his estate to his family and no DSUE Amount is available to Judy. At Judy's death, what happens?

The first deceased spouse's DSUE Amount is replaced by the second deceased spouse's DSUE Amount, but what about the prior gifts that used the first deceased spouse's DSUE? Do those no longer count? Until the Temporary Regulations were issued, no one could be sure of the answer. But, the good news is, in yet another taxpayer-friendly position, the Temporary Regulations give us (mostly) helpful guidance on these complicated questions.

2. The "Last Deceased Spouse"

For gift purposes, the "last deceased spouse" is determined at the time the gift is made. Temp. Reg. §25.2505-2T(a)(1)(i). This special rule can be helpful, because if the surviving spouse remarries in the same year that the first deceased spouse died, and makes gifts before the second spouse dies that same year, those gifts still utilize the first deceased spouse's DSUE Amount. Without the rule, the surviving spouse would not be able to make gifts without some risk of them becoming taxable (although she could also not get remarried). In the absence of this special rule, only the DSUE Amount of the second deceased spouse would apply, since the gift tax unified credit is based on the applicable exclusion amount "if the donor died as of the end of the calendar year." Code Section 2505(a)(1). Of course, the special rule can work to the detriment of the donor spouse as well. Since a DSUE Amount can't be used until a spouse dies, a donor with a terminally ill spouse would not be able to make gifts utilizing the potential DSUE Amount until an actual death occurs.

3. Making DSUE Amount Gifts from Multiple Deceased Spouses

In addition to the foregoing, the Temporary Regulations provide yet another (surprisingly) friendly position for taxpayers: it is possible to make gifts utilizing the DSUE Amounts from multiple deceased spouses. The Regulations state that if a surviving spouse has made lifetime gifts that utilized the DSUE Amounts from prior deceased spouses who are different from the last deceased spouse, the then DSUE Amount to be included in determining the applicable exclusion amount of the surviving spouse that will be applicable at the time of the current taxable gift (or at the surviving spouse's death) is the sum of:

a) The DSUE Amount of the surviving spouse's last deceased spouse…; and

b) The DSUE Amount of each other deceased spouse of the surviving spouse to the extent that such amount was applied to one or more [previous] taxable gifts of the surviving spouse. Temp. Reg. §§ 20.2010-3T(b), 25.2505-2T(c).

In other words, while it is not possible for a surviving spouse to accumulate DSUE Amounts from multiple deceased spouses at her death (due to the "last deceased spouse" rule), it is possible for the surviving spouse to utilize multiple DSUE Amounts so long as she is making taxable gifts prior to the death of any subsequent spouses. While this seems like a morbid planning opportunity (the thought of "black widows" collectively DSUE Amounts comes to mind), it is, nevertheless, a very helpful rule that every estate planner needs to understand.

*Example*. Assuming Judy receives a $5 million DSUE Amount from Yale, she adds that to her basic exclusion amount of $5 million for a total applicable exclusion amount of $10 million. Judy then makes gifts of $10 million to Captain Lewis. Later, Judy marries Henri, and on his death, he has a DSUE Amount of $5 million. Due to the rules, Judy can utilize Henri's DSUE, which she can apply during her life against taxable gifts or at her death.

To underline the application of this rule, the schedules in which the applicable exclusion amount is calculated for gift and estate tax purposes both contain sections dealing with DSUE Amounts from prior deceased spouses used on gifts by the donor/decedent.

4. Timing of Gifts

One word of caution. From a timing standpoint, the surviving spouse is able to utilize the last deceased spouse's DSUE Amount beginning on the date of the deceased spouse's death. However, the election can only be made on the deceased spouse's estate tax return (as discussed below), which is not due until nine months after the date of death (and can be extended an additional six months). Accordingly, it is possible that a surviving spouse will make gifts relying on the portability election being made, but if the executor does not file a return (and the surviving spouse in this situation has no right to file a return because there is an executor), then the gifts could be taxable. Temp. Reg. § 25.2505-2T(d)(1). Furthermore, it is possible for the executor to file a return making the election before the due date, and then file a subsequent return opting out of portability. *Id*.

It is also possible for the DSUE Amount to be reduced by valuation adjustment upon audit. Since the last return filed before the deadline will apply, the surviving spouse would be out of luck. Obviously, this is a non-issue when the surviving spouse is also the executor, but in estates where this is not the case (i.e., second marriage situations), the surviving spouse must be careful to rely on the portability election before it has been made.

**C. Making the Portability Election**

1. The Code

Section 2010 of the Code provides very limited guidance regarding the mechanics of the portability election. The only method by which a surviving spouse can claim a DSUE Amount is if the "executor" of the deceased spouse's estate timely files a U.S. Estate (and Generation-Skipping Transfer) Tax return (Form 706). Code Section 2010(c)(5)(A). Once the election is made, it is irrevocable. *Id*. No election can be made if the return is filed late (although for certain estates, there is some relief for late filed returns under Rev. Proc. 2014-18, discussed below). *Id*. Fortunately, the Temporary Regulations provide additional guidance on these matters.

2. Opting Out; Last Return Controls

In addition to simply not filing a return, the executor can also "opt out" of making the election on the 706. Temp. Reg. § 20.2010-2T(a)(3). Furthermore, the executor can effectively revoke a prior election by filing another 706 before the due date that changes the prior election. Temp. Reg. § 20.2010-2T(a)(4). The last filed 706 before the due date will control, and whatever election is made on that return will be irrevocable. *Id*.

3. Late Filing Relief

The Regulations make no mention of making a "protective" election (for example, in the case of a will contest) or of any relief for filing a late return under Section 9100, however, in light of numerous private letter requests for relief, the IRS promulgated Rev. Proc. 2014-18 in which they set forth a simplified method for filing a late 706 in certain cases. Rev. Proc. 2014-18, 2014-7 IRB 513. In order to qualify,

a) the deceased spouse must have died after December 31, 2010 and on or before December 31, 2013;
b) the deceased spouse must have been a U.S. citizen or resident on his or her date of death;
c) the deceased spouse's estate must not have been required to file a 706 based on the value of the gross estate plus adjusted taxable gifts and did not file a return to elect out of portability; and
d) the 706 must state at the top of the Form that the return is "FILED PURSUANT TO REV. PROC. 2014-18 TO ELECT PORTABILITY UNDER § 2010(C)(5)(A). *Id*.

For estates that do not qualify, the Rev. Proc. provides that, after January 1, 2015, the estate may submit a letter ruling seeking 9100 relief. *Id*.

4. The "Executor" Makes the Election

The Temporary Regulations provide that the "executor or administrator of a decedent (survived by a spouse) that is appointed, qualified, and acting within the United States…may file the estate tax return on behalf of the estate of the decedent and, in so doing, elect portability of the decedent's DSUE amount." Temp. Reg. § 20.2010-2T(a)(6)(i). The executor can also elect out of portability (or simply not file a return if one is not otherwise required).

5. What if There is No Executor?

If no executor is appointed, the portability election can only be made by any person in "actual or constructive" possession of any property of the decedent. Temp. Reg. § 20.2010-2T(a)(6)(ii). If a return is filed by a "non-appointed executor" either electing portability or opting out, then that election cannot be superseded by a contrary election made by another non-appointed executor in the same estate. *Id*.

The important thing to take away is that if there is a court-appointed executor who is not the surviving spouse, there is no way for the surviving spouse to make a portability election if the executor does not. This seems somewhat incongruous to the other, more liberal interpretations applied in the Temporary Regulations. Nevertheless, it becomes critically important in estate plans that involve blended families, where one spouse's children or someone other than the surviving spouse is serving as executor, that that the attorney discusses with the client whether to include some direction (or prohibition) that the executor make the portability election (even if a return is not required) for the benefit of the surviving spouse and how the related costs would be paid.

6. Requirements for Making the Election

While Code Section 2010 made it clear that an election can only be made by filing a Form 706 for the deceased spouse's estate, until recently, it was not clear whether the IRS would permit returns to be filed with less stringent requirements associated with the typical estate tax return.

Fortunately, under certain circumstances, a "full and complete" return is not required. If a return is not otherwise required, and if any property included in the gross estate that qualifies for the marital deduction (under Code Section 2056 or 2056A) or the charitable deduction (under Code Section 2055), the executor does not have to report the value of the asset, only the "description, ownership, and/or beneficiary of such property…" together with information sufficient to support its qualification for the deduction. Temp. Reg. § 20.2010-2T(a)(7)(ii)(A).

There are certain exceptions to this where the property values must be provided. *Id*. For example, if the value relates to amounts passing to other beneficiaries, if any a portion of the property passes to a spouse or charity, if there is a partial disclaimer or partial QTIP election, or if the value is needed to determine the estate's eligibility for alternate valuation, special use valuation or Code § 6166 estate tax deferral. However, even if the procedure applies, the executor must exercise due diligence to estimate the fair market value of the gross estate, and provide a range of values within the executor's "best estimate," rounded to the nearest $250,000. Temp. Reg. § 20.2010-2T(a)(7)(ii)(B).

Presumably, "best estimate" does not include full blown appraisals, but such appraisals may still be required in order to establish any step up in basis of hard-to-value assets. Still, for "simple" estates where most if not all of the assets pass to the surviving spouse outright, the relaxed requirements are a welcome addition as it makes the decision to elect portability less costly to the executor.

However, please note that for estates that include trusts (either Bypass Trusts or QTIP Trusts), a full and complete return (with values and appraisals, if needed) would still be required in order to make the portability election. A good example is a $2 million estate that includes a bypass trust for the surviving spouse (the couple did their wills in 1998 when the exemption was $625,000). If the executor wishes to file a 706 so that the surviving spouse can claim the $3 million DSUE Amount, the executor would be required to file a full and complete return for the estate.

The Instructions to the Form 706 have been revised to reflect the Temporary Regulations. Furthermore, the Form itself contains a new "Part 6" on which the election can be made (or the executor can opt out). A copy of the relevant pages from the Form 706 and its instructions are attached as Exhibit A. Interestingly, certain concepts discussed above, such as the ability to utilize the DSUE Amounts from multiple deceased spouses through lifetime gifts, is clearly reflected in the Form and instructions.

If an estate tax return is filed in which a portability election is made, it appears that the IRS can keep the statute of limitations open on the deceased spouse's estate tax return for the sole purpose of adjusting the amount of the DSUE Amount on the surviving spouse's return. Code Section 2010(c)(5)(B). As a result, the estate tax return of a deceased spouse could be audited for the purpose of determining the correct amount of the DSUE Amount even if the surviving spouse dies decades later. Per the Temporary Regulations, the IRS may adjust or eliminate the DSUE Amount based on the

examination, but it may not assess additional estate tax against a prior deceased spouse's return if the applicable period of limitations for assessment of estate taxes has expired. Temp. Reg. §§ 20.2001-2T(a), 20.2010-2T(d), 20.2010-3T(d) and 25.2505-2T(e).

## IV. PORTABILITY VS. BYPASS TRUSTS

The introduction of portability, along with significantly higher (and re-unified) estate and gift tax exemptions truly are "game changers" in the approach estate planners will need to take going forward. Using a testamentary trust to preserve the estate tax exemption of the first spouse to die (referred to herein as a "Bypass Trust") has long been a staple of estate planners. Understandably, a significant number of clients for whom Bypass Trusts would have been an easy decision must now carefully consider an increasing number of factors that in many cases are impossible to predict. Estate planners must learn how to guide their clients through this complex array of choices and provide them with sufficient (but comprehensible) information to make informed decisions. As an added challenge, now with portability, many potential clients may no longer feel it is even necessary to deal with testamentary planning at all, not knowing all of the potential landmines that await the unsuspecting. Welcome to the new age of estate planning.

### A. Benefits of Portability

Portability offers some clear and unmistakable benefits. Ultimately, whether these are enough to outweigh the benefits of a Bypass Trust will certainly depend on the particular facts at hand. However, from a general standpoint, here are a few noteworthy benefits:

1. Back Stop to Lack of Estate Planning

Just like the GST automatic allocation rules, portability offers a respite (both to estate planners and the IRS who has to review private letter ruling requests) from a lack of planning. For spouses who did not choose to add tax-planned trusts to their wills (or if they have no will at all), a lack of a Bypass Trust at the first spouse's death surely meant that the first deceased spouse's exemption would be partially or completely wasted, unless the surviving spouse was willing to disclaim and let assets pass to the next beneficiaries in line. Now that is no longer an issue, so long as the portability election is made in a timely fashion.

2. Simplicity

A Bypass Trust, despite its numerous benefits (as described below), will always be more complicated than no trust. Estate plans can now be incredibly simple (and flexible) without wasting the first spouse's exemption.

3. Qualified Retirement Plans

For many clients, their traditional IRA or 401(k) is their biggest asset. Unfortunately, these make poor assets for estate planning because of the income tax liability built into the account. Because traditional IRA distributions are subject to ordinary income taxes, the goal is to defer, defer, defer. Typically, the best option from an income tax standpoint is to name the surviving spouse as the primary beneficiary, so he or she can then roll it into their own IRA and defer distributions until he or she is 70½. Because this asset is passing outright to the surviving spouse, it is not available to fund the Bypass Trust under the will. If the tax benefits of using the Bypass Trust are more desired, then it can be named as the beneficiary of the IRA, but then the trust will need to qualify under the minimum distribution rules (which can be tricky) and distributions will need to begin immediately based on the oldest beneficiary's life expectancy, typically the surviving spouse.

Now, with portability, the decision is easier if the surviving spouse is named as the outright beneficiary, as opposed to the trustee of the Bypass Trust. If the deceased spouse's executor makes a portability election on a timely filed estate tax return, the added exemption may fully shelter the IRA upon the surviving spouse's death, without the need for having it pass to a Bypass Trust.

### B. Drawbacks of Portability

1. No GST Equivalent

The DSUE Amount does not apply to the generation-skipping transfer (GST) tax. Unfortunately, a deceased spouse's unused GST exemption cannot be used by a surviving spouse. This means that if the first spouse to die wants to fully utilize his or her GST exemption, the spouse should create a non-marital trust or a reverse QTIP trust for the benefit of the surviving spouse.

2. No Indexing

One of the features of the 2010 Tax Act is that the basic estate tax exclusion amount ($5 million) is now indexed for inflation from starting in 2012. At the first spouse's death, his or her basic exclusion amount may have been indexed for inflation, but once it becomes a DSUE Amount, it will not be subject to future adjustments for inflation after his or her death. However, the surviving spouse's basic estate tax exclusion amount will still be adjusted for inflation at his or her subsequent death. Code Section 2010(c)(3)(B).

3. Election Required

Of course, a DSUE Amount is only available to the surviving spouse if the executor makes the appropriate election by filing an estate tax return for

the deceased spouse. There are a number of potential roadblocks: the cost of preparing the return, filing a return on time, blended family situations, etc., that can make this anything but a straightforward proposition.

**C. Benefits of a Bypass Trust Over Portability**

Despite the clear benefits of portability for a lot of estate plans, it is likely that Bypass Trusts will continued to be recommended by estate planners as a fundamental tool in their toolbox. This is because there are numerous tax and non-tax benefits of Bypass Trusts, as well as the incredible amount of flexibility a trust can provide.

1. Creditor/Divorce Protection

One of the primary advantages of a trust, regardless of any estate tax benefits, is the fact that a trust's assets will be exempt from most creditors under state law. In fact, this is often a bigger factor in persuading a client to use a trust than not. For example, a properly drafted spendthrift trust should protect the surviving spouse from liability for a tort committed by the surviving spouse, contractual claims against the surviving spouse, or claims of a new spouse against the surviving spouse's assets. Furthermore, the assets of the trust should be protected from future spouses of the surviving spouse. Even if the surviving spouse is the trustee, the spouse's interest in the Bypass Trust can be protected from divorce if the trust is properly drafted and will keep separate property interests from being comingled with community property.

2. Allocation of GST Exemption

As mentioned earlier, one of the features not included in the 2010 Tax Act is the portability of a spouse's unused GST exemption. Allocation of a deceased spouse's GST exemption to a Bypass Trust can be an extremely powerful means of avoiding estate and GST taxes for several generations. Using a Bypass Trust at the first death effectively doubles the amount of GST exemption that can be allocated by a married couple to trusts for their children. If a Bypass Trust is not used, the first deceased spouse's GST exemption will be wasted.

3. Protects Appreciation of Assets

The use of a Bypass Trust will protect the enhanced value of the deceased spouse's assets. The income and appreciation generated by the assets in the deceased spouse's estate that pass into a Bypass Trust will escape future estate tax upon the death of the surviving spouse. The DSUE Amount does not change, and in fact, is not even indexed for inflation (unlike the estate tax basic exclusion amount). Finally, by using a Bypass Trust, the surviving spouse will be able to "spend down" his or her assets first (which will be included in his or her taxable estate at death) while preserving the assets in the Bypass Trust for the remainder beneficiaries.

4. Loss of DSUE Amount Upon Remarriage

One of the biggest risks to a surviving spouse who relies on portability instead of a Bypass Trust is the potential loss of the DSUE Amount upon remarriage. If the surviving spouse remarries and he or she outlives the second spouse, the surviving spouse will lose the first deceased spouse's DSUE Amount in favor of the second spouse's DSUE Amount. If the executor of the second deceased spouse's estate refuses to file an estate tax return, the surviving spouse will not only lose the first deceased spouse's DSUE Amount but have nothing to replace it with. On the other hand, use of a Bypass Trust will preserve the first deceased spouse's exemption, regardless of whether the surviving spouse remarries (and, the trust may protect the trust assets from any claims made by the second spouse).

In fact, by utilizing a Bypass Trust, the surviving spouse can acquire multiple DSUE Amounts without having to make any lifetime gifts. If the first deceased spouse's exemption is allocated to the assets of a Bypass Trust, upon the death of the second deceased spouse, the surviving spouse can elect portability and use his DSUE Amount without losing the benefit of the first deceased spouse's exemption (which is still in the Bypass Trust).

5. Avoid Audit of Assets in Bypass Trust Upon Second Death

While it is not unheard of for the estate of the first spouse to die to be audited, it is less likely if no estate tax is due on the first spouse's death. By using a Bypass Trust, the assets in the trust will not need to be disclosed a second time if the surviving spouse dies and files an estate tax return. In fact, since the Bypass Trust assets are not included in the surviving spouse's estate, if the surviving spouse's assets outside the trust (including prior taxable gifts) are less than the exemption amount, the surviving spouse should not be required to file an estate tax return at all. Please note that the threshold for filing a return is based on the surviving spouse's basic exemption amount, without regard to any DSUE Amount.

6. "Locks in" the Estate Plan

If the first deceased spouse is concerned that the surviving spouse will squander his/her assets on the new spouse to the detriment of the children, the Bypass Trust can provide for an independent trustee, strict distribution provisions, and no power of appointment (so that the assets have to pass to the children at the death of the surviving spouse).

### D. Drawbacks of Credit Shelter Trust vs. Portability

Of course, despite the myriad benefits of a Bypass Trust, there are still some important drawbacks that are worth noting. In the past, a Bypass Trust would often be an automatic part of any estate plan over a certain amount, whereas today, it is going to take a lot more discussion to arrive at the best solution for the client.

1. No Stepped-Up Basis

The most compelling tax reason to avoid using a Bypass Trust in favor of portability is the fact that the Bypass Trust assets will not receive a step up in basis when the surviving spouse dies. In the past, the trade off of the loss of a stepped-up basis was easily outweighed by the fact that the estate tax rate (55%, not so long ago) was much greater than the capital gains rate (currently 15% on long term gain). However, two important things have changed. One, the estate tax exemption amount is much higher than it ever was in the past, meaning a lot fewer estates are subject to the tax, and two, the difference between the estate tax rate (40%) and the capital gains rate (23.8%) is not as great as it used to be. If the surviving spouse's estate would not be subject to any estate tax at her death because it is under the exemption (with or without portability), in many cases the spouse's heirs would be better off from a tax standpoint if all of the surviving spouse's assets received a stepped-up basis. Of course, it is impossible to predict what rates will be in the future, and the non-tax benefits of Bypass Trusts are still very compelling, but estate planners can no longer overlook the income tax ramifications of these decisions. Someone said recently that we are all income tax lawyers now, and that is not an incorrect statement.

2. Trusts Are Complicated

While the concept of a Bypass Trust should be pretty straightforward to practicing estate planners, it is a foreign concept to many clients. And for some clients, the hassle of administering the Bypass Trust, including segregating and transferring assets to the trust, keeping track of multiple tax returns, and respecting the distribution provisions of the trust can be intimidating. Although estate planners can offer a lot of help in this area, there are going to be clients who are just not great candidates for Bypass Trusts, and would be better served by relying on portability.

### E. Not an "Either/Or" Choice

It is important to note that the portability election is still available even if a Bypass Trust is used in the will of the deceased spouse. Assuming the deceased spouse's estate is less than the estate tax exemption (including adjusted taxable gifts), then a DSUE Amount would still be available over and above what passes to the Bypass Trust. This DSUE Amount could be used by the surviving spouse during his or her lifetime, preserving that spouse's basic exclusion amount. Of course, an estate tax return would need to be filed for the deceased spouse, and any assets passing to the Bypass Trust would likely need to be disclosed in full, as opposed to the more streamlined option for assets qualifying for the marital deduction. Regardless, it is likely that the number of estate tax returns will rise for this reason, even though the number of estates subject to the estate tax has decreased significantly in the last few years.

## V. PLANNING WITH PORTABILITY

Now that portability appears to be a permanent part of our estate planning toolbox, we need to think about how the advice we give clients in a variety of areas should be adapted to fit this new age of estate planning.

### A. Disclaimer Trusts as an Alternative

Flexibility is more crucial than ever for estate plans. As a planning alternative, in many cases it will be a good idea to recommend using a "disclaimer" Bypass Trust that can be created at the discretion of the surviving spouse after the death of the first spouse. This way, the benefits of a Bypass Trust can still be realized depending on the exemptions in effect at that time and the desires of the surviving spouse. Of course, there are drawbacks, primarily that relying on the disclaimer rules means that the spouse must act within nine months after the first spouse's death and cannot accept the property prior to the disclaimer, and in addition, the surviving spouse cannot have a power of appointment over the Bypass Trust. Still, despite these limitations, the use of disclaimer Bypass Trusts will likely become even more popular in the face of current planning uncertainty.

### B. Will Provisions to Add

In most cases, keeping the Bypass Trust estate plan in place will continue to make sense, even with portability. For flexibility in smaller estates, many will forms include a "disclaimer" option, where the Bypass Trust is created at the option of the surviving spouse after the first spouse's death. Another, less obvious addition to a will form may be a provision regarding the executor's decision to make the portability election. Often, the will strives to deflect as much liability as reasonably possible from the executor. In that case, the will may provide that the executor be absolved from liability for making or failing to make the portability election. That election (or failure to make the election) can have ramifications on the surviving spouse and his or her family, even if they are not beneficiaries of the will. On the other hand, there may be situations in which the executor should be required to make the

election. If cost is an issue, the will can provide that the executor is required to make the election so long as the surviving spouse reimburses the estate for reasonable costs associated with the preparation of the return. Of course, one risk is if the estate is audited, there may be transactions that the family does not want to come to light (think prior gifts that were not fully and adequately disclosed to get the statute of limitations running).

### C. Addressing the Portability Election in Marital Agreements

Spouses who have significant assets may wish to use the other spouse's DSUE Amount if it means they will save significant estate taxes. This has become a negotiating point in Marital Agreements, where the spouse without assets has something valuable to trade in exchange for other rights from the monied spouse. Family law attorneys are likely going to be less aware of these issues, so even if an estate planner doesn't draft marital agreements, he or she may want to have some language handy in case they are asked to review an agreement on behalf of their client.

### D. Using the Increased Gift Tax Exemption

It goes without saying that one of the best opportunities offered by portability is the ability for a surviving spouse to use the DSUE Amount to shelter significant lifetime gifts from gift tax. There are two factors that strongly support this position: one, the fact that the surviving spouse will potentially lose the DSUE Amount upon remarriage and the death of the subsequent spouse, and two, the fact that the DSUE Amount will be utilized first before the surviving spouse's basic exclusion amount when making any gifts. Of course, the surviving spouse would need to have the assets available to make the gifts (and not miss having the use of those assets), but assuming that is the case, it can be a powerful estate planning tool.

### E. Advising the Executor

The executor of an estate in which the decedent died after December 31, 2010 and is survived by a spouse, regardless of the size of that estate and whether the spouse uses a Bypass Trust in his or her testamentary plan, may be eligible to make the portability election on that decedent's estate tax return. Failure to file a return, or failure to make the election, means that the DSUE Amount is not available to the surviving spouse.

Everyone likes to believe they are going to win the lottery one day; failure to make the portability election could, however unlikely, result in more estate tax being owed when the surviving spouse dies. (Of course, the surviving spouse could always find a poor spouse to remarry in order to take advantage of his or her DSUE Amount, but that's another topic).

The question then is when does it make sense to file an estate tax return in order to preserve the first spouse's DSUE Amount, even if the combined estate is well under the exemption amounts?

Please note that the threshold for filing an estate tax return will still be based on the original basic estate tax exclusion amount ($5 million, adjusted for inflation), and is not adjusted based on the addition of a DSUE Amount. Code Section 6018(a)(1). Assuming that the deceased spouse's estate is under the basic exclusion amount, how should an estate planning practitioner advise his or her client about the election?

The downside is primarily the cost of preparing the estate tax return. Given that fewer returns are filed each year, attorneys very often prepare the returns for clients, at an hourly rate. For smaller estates, CPAs may offer a lower cost alternative for preparation, and in many cases, the preparation of a "portability" return will be much easier if all assets are passing outright to the surviving spouse. Another downside is having to disclose assets on a return that may otherwise escape scrutiny. In this case, the client will need to weigh the pros and the cons of filing vs. not filing. At a minimum, the surviving spouse (and the executor, if it is someone else) should be told about the portability and the preparation of an estate tax return should be discussed and documented. Practitioners should consider adding a general discussion in the form letter they send to the executor.

### F. Planning for Non-resident Spouses

1. Nonresidents/Noncitizens

It should be noted that under the Temporary Regulations, if a decedent is a nonresident, noncitizen of the U.S., no portability election can be made and no DSUE Amount is available to the surviving spouse (even if the surviving spouse is a U.S. citizen and/or resident). Temp. Reg. § 20.2010-2T(a)(5). If the decedent is a resident and/or citizen but the surviving spouse is not, then the surviving spouse cannot utilize the DSUE Amount; however, if the surviving spouse subsequently becomes a resident and/or citizen, then they can utilize the DSUE Amount on gifts or at death when that surviving spouse is a resident/citizen. Temp. Reg. §§ 20.2010-3T(e), 25.2505-2T(f). In other words, there may be some benefit to making the portability election when the decedent is a resident/citizen and the surviving spouse is not, just in case.

2. Qualified Domestic Trusts

If the resident/citizen deceased spouse creates a Qualified Domestic Trust (QDOT) under his or her will for the benefit of the non-citizen/non-resident surviving spouse, then the decedent's estate is allowed a marital deduction. Distributions from the QDOT (during the surviving spouse's lifetime or at his or her death) are subject to estate taxes attributable to the

deceased spouse's estate. Therefore, when a portability election is made, the DSUE Amount will need to be decreased based on subsequent distributions from the QDOT, and the surviving spouse will not be able to make use of the DSUE Amount until the date of the event that triggers the final estate tax liability of the decedent under Section 2056A, which would either be at the surviving spouse's death or when there is a terminating distribution from the QDOT. Temp. Reg. §§ 20.2010-3T(c)(2), 25.2505-2T(d)(2).

# Appendix A

Form 706 (Rev. 8-2013)

| Estate of: | Decedent's social security number |
|---|---|
| | |

## Part 6—Portability of Deceased Spousal Unused Exclusion (DSUE)

### Portability Election

A decedent with a surviving spouse elects portability of the deceased spousal unused exclusion (DSUE) amount, if any, by completing and timely-filing this return. No further action is required to elect portability of the DSUE amount to allow the surviving spouse to use the decedent's DSUE amount.

### Section A. Opting Out of Portability

The estate of a decedent with a surviving spouse may opt out of electing portability of the DSUE amount. Check here and do not complete Sections B and C of Part 6 only if the estate opts **NOT** to elect portability of the DSUE amount. ☐

### Section B. QDOT

| | Yes | No |
|---|---|---|
| Are any assets of the estate being transferred to a qualified domestic trust (QDOT)? . . . . . | | |

If "Yes," the DSUE amount portable to a surviving spouse (calculated in Section C, below) is preliminary and shall be redetermined at the time of the final distribution or other taxable event imposing estate tax under section 2056A. See instructions for more details.

### Section C. DSUE Amount Portable to the Surviving Spouse (To be completed by the estate of a decedent making a portability election.)

Complete the following calculation to determine the DSUE amount that can be transferred to the surviving spouse.

| | | | | |
|---|---|---|---|---|
| 1 | Enter the amount from line 9c, Part 2—Tax Computation | 1 | | |
| 2 | Reserved | 2 | | |
| 3 | Enter the value of the cumulative lifetime gifts on which tax was paid or payable (see instructions) | 3 | | |
| 4 | Add lines 1 and 3 | 4 | | |
| 5 | Enter amount from line 10, Part 2—Tax Computation | 5 | | |
| 6 | Divide amount on line 5 by 40% (0.40) (do not enter less than zero) | 6 | | |
| 7 | Subtract line 6 from line 4 | 7 | | |
| 8 | Enter the amount from line 5, Part 2– Tax Computation | 8 | | |
| 9 | Subtract line 8 from line 7 (do not enter less than zero) | 9 | | |
| 10 | DSUE amount portable to surviving spouse (Enter lesser of line 9 or line 9a, Part 2 – Tax Computation) | 10 | | |

### Section D. DSUE Amount Received from Predeceased Spouse(s) (To be completed by the estate of a deceased surviving spouse with DSUE amount from predeceased spouse(s))

Provide the following information to determine the DSUE amount received from deceased spouses.

| A Name of Deceased Spouse (dates of death after December 31, 2010, only) | B Date of Death (enter as mm/dd/yy) | C Portability Election Made? Yes | C No | D If "Yes," DSUE Amount Received from Spouse | E DSUE Amount Applied by Decedent to Lifetime Gifts | F Year of Form 709 Reporting Use of DSUE Amount Listed in col E | G Remaining DSUE Amount, if any (subtract col. E from col. D) |
|---|---|---|---|---|---|---|---|
| | | | | | | | |
| **Part 1 — DSUE RECEIVED FROM LAST DECEASED SPOUSE** | | | | | | | |
| | | | | | | | |
| **Part 2 — DSUE RECEIVED FROM OTHER PREDECEASED SPOUSE(S) AND USED BY DECEDENT** | | | | | | | |
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| | | | | | | | |
| **Total** (for all DSUE amounts from predeceased spouse(s) applied) . . . . | | | | | | | |

Add the amount from Part 1, column D and the total from Part 2, column E. Enter the result on line 9b, Part 2—Tax Computation . . . . . ▶

### Table of Estimated Values

| If the total estimated value of the assets eligible for the special rule under Reg. section 20.2010–2T(a)(7)(ii) is more than | But less than or equal to | Include this amount on lines 10 and 23: |
|---|---|---|
| $0 | $250,000 | $250,000 |
| $250,000 | $500,000 | $500,000 |
| $500,000 | $750,000 | $750,000 |
| $750,000 | $1,000,000 | $1,000,000 |
| $1,000,000 | $1,250,000 | $1,250,000 |
| $1,250,000 | $1,500,000 | $1,500,000 |
| $1,500,000 | $1,750,000 | $1,750,000 |
| $1,750,000 | $2,000,000 | $2,000,000 |
| $2,000,000 | $2,250,000 | $2,250,000 |
| $2,250,000 | $2,500,000 | $2,500,000 |
| $2,500,000 | $2,750,000 | $2,750,000 |
| $2,750,000 | $3,000,000 | $3,000,000 |
| $3,000,000 | $3,250,000 | $3,250,000 |
| $3,250,000 | $3,500,000 | $3,500,000 |
| $3,500,000 | $3,750,000 | $3,750,000 |
| $3,750,000 | $4,000,000 | $4,000,000 |
| $4,000,000 | $4,250,000 | $4,250,000 |
| $4,250,000 | $4,500,000 | $4,500,000 |
| $4,500,000 | $4,750,000 | $4,750,000 |
| $4,750,000 | $5,000,000 | $5,000,000 |
| $5,000,000 | $5,250,000 | $5,250,000 |

### Exclusion — Item 12

**Item 12. Conservation easement exclusion.** Complete and attach Schedule U (along with any required attachments) to claim the exclusion on this line.

### Deductions — Items 14 through 23

**Items 14 through 22.** Attach the appropriate schedules for the deductions claimed.

**Item 18.** If item 17 is less than or equal to the value (at the time of the decedent's death) of the property subject to claims, enter the amount from item 17 on item 18.

If the amount on item 17 is more than the value of the property subject to claims, enter the greater of:

- The value of the property subject to claims or
- The amount actually paid at the time the return is filed.

In no event should you enter more on item 18 than the amount on item 17. See section 2053 and the related regulations for more information.

**Item 23.** Under Regulations section 20.2010-2T(a)(7)(ii), if the total value of the gross estate and adjusted taxable gifts is less than the basic exclusion amount (see section 6018(a)) and Form 706 is being filed only to elect portability of the DSUE amount, the estate is not required to report the value of certain property eligible for the marital or charitable deduction. For this property being reported on Schedule M or O, enter on line 23 the amount from line 10.

## Part 6—Portability of Deceased Spousal Unused Exclusion (DSUE)

Section 303 of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 authorized estates of decedents dying on or after January 1, 2011, to elect to transfer any unused exclusion to the surviving spouse. The amount received by the surviving spouse is called the *deceased spousal unused exclusion*, or DSUE, amount. If the executor of the decedent's estate elects transfer, or portability, of the DSUE amount, the surviving spouse can apply the DSUE amount received from the estate of his or her last deceased spouse (defined below) against any tax liability arising from subsequent lifetime gifts and transfers at death.

**Note.** A nonresident surviving spouse who is not a citizen of the United States may not take into account the DSUE amount of a deceased spouse, except to the extent allowed by treaty with his or her country of citizenship.

### Last Deceased Spouse Limitation

The *last deceased spouse* is the most recently deceased person who was married to the surviving spouse at the time of that person's death. The identity of the last deceased spouse is determined as of the day a taxable gift is made, or in the case of a transfer at death, the date of the surviving spouse's death. The identity of the last deceased spouse is not impacted by whether the decedent's estate elected portability or whether the last deceased spouse had any DSUE amount available. Remarriage also does not affect the designation of the last deceased spouse and does not prevent the surviving spouse from applying the DSUE amount to taxable transfers.

When a taxable gift is made, the DSUE amount received from the last deceased spouse is applied before the surviving spouse's basic exclusion amount. A surviving spouse may use the DSUE amount of the last deceased spouse to offset the tax on any taxable transfer made after the deceased spouse's death. A surviving spouse who has more than one predeceased spouse is not precluded from using the DSUE amount of each spouse in succession. A surviving spouse may not use the sum of DSUE amounts from multiple predeceased spouses at one time nor may the DSUE amount of a predeceased spouse be applied after the death of a subsequent spouse.

### Making the Election

A timely-filed and complete Form 706 is required to elect portability of the DSUE amount to a surviving spouse. The filing requirement applies to all estates of decedents choosing to elect portability of the DSUE amount, regardless of the size of the estate. A timely-filed return is one that is filed on or before the due date of the return, including extensions.

The timely filing of a complete Form 706 with DSUE will be deemed a portability election if there is a surviving spouse. The election is effective as of the decedent's date of death, so the DSUE amount received by a surviving spouse may be applied to any transfer occurring after the decedent's death. A portability election is irrevocable, unless an adjustment or amendment to the election is made on a subsequent return filed on or before the due date.

**Note.** Under Regulations section 20.2010-2T(a)(5), the executor of an estate of a nonresident decedent who was not a citizen of the United States at the time of death cannot make a portability election.

If an executor is appointed, qualified, and acting with the United States on behalf of the decedent's estate, only that executor may make or opt out of a portability election. If there is no executor, see Regulations section 20.2010-2T(a)(6)(ii).

### Opting Out

If an estate files a Form 706 but does not wish to make the portability election, the executor can opt out of the portability election by checking the box indicated in Section A of this Part. If no return is required under section 6018(a),

not filing Form 706 will avoid making the election.

### Computing the DSUE Amount

Regulations section 20.2010-2T(b)(1) requires that a decedent's DSUE be computed on the estate tax return. The DSUE amount is the lesser of (A) the basic exclusion amount in effect on the date of death of the decedent whose DSUE is being computed, or (B) the decedent's applicable exclusion amount less the amount on line 5 of Part 2–Tax Computation on the Form 706 for the estate of the decedent. Amounts on which gift taxes were paid are excluded from adjusted taxable gifts for the purpose of this computation.

When a surviving spouse applies the DSUE amount to a lifetime gift or bequest at death, the IRS may examine any return of a predeceased spouse whose executor elected portability to verify the allowable DSUE amount. The DSUE amount may be adjusted or eliminated as a result of the examination; however, the IRS may only make an assessment of additional tax on the return of the predeceased spouse within the applicable limitations period under section 6501.

### Special Rule Where Value of Certain Property Not Required to Be Reported on Form 706

The temporary regulations provide that executors of estates who are not otherwise required to file Form 706 under section 6018(a) do not have to report the value of certain property qualifying for the marital or charitable deduction. For such property, the executor may estimate the value in good faith and with the due diligence to be afforded all assets includible in the gross estate. The amount reported on Form 706 will correspond to a range of dollar values and will be included in the value of the gross estate shown on line 1 of Part 2-Tax Computation. See instructions for lines 10 and 23 of Part 5-Recapitulation, above, for more details.

### Specific Instructions

**Portability Election.** If you intend to elect portability of the DSUE amount, timely filing a complete Form 706 is all that is required. Complete section B if any assets of the estate are being transferred to a qualified domestic trust and complete section C of this Part to calculate the DSUE amount that will be transferred to the surviving spouse.

**Section A. Opting Out of Portability.** If you are filing Form 706 and do not wish to elect portability, then check the box indicated. Do not complete sections B or C.

**Section B. Portability and Qualified Domestic Trusts.** A *qualified domestic trust* (QDOT) allows the estate of a decedent to bequeath property to surviving spouse who is not a citizen of the United States and still receive a marital deduction. When property passes to a QDOT, estate tax is imposed under section 2056A as distributions are made from the trust. When a QDOT is established and there is a DSUE amount, the executor of the decedent's estate will determine a preliminary DSUE amount for the purpose of electing portability. This amount will decrease as section 2056A distributions are made. In estates with a QDOT, the DSUE amount generally may not be applied against tax arising from lifetime gifts because it will not be available to the surviving spouse until it is finally determined, usually upon the death of the surviving spouse or when the QDOT is terminated.

Check the appropriate box in this section and see the instructions for Schedule M if more information is needed about qualified domestic trusts.

**Section C. DSUE Amount Portable to Decedent's Surviving Spouse.** Complete section C only if electing portability of the DSUE amount to the surviving spouse.

On line 1, enter the decedent's applicable exclusion amount from Part 2—Tax Computation, line 9c. Under section 2010(c)(2), the *applicable exclusion amount* is the sum of the basic exclusion amount for the year of death and any DSUE amount received from a predeceased spouse, if applicable.

Line 2 is reserved.

On line 3, enter the value of the cumulative lifetime gifts on which gift tax was paid or payable. This amount is figured on line 6 of the Line 7 Worksheet Part B as the total of Row (r) from Line 7 Worksheet Part A. Enter the amount as it appears on line 6 of the Line 7 Worksheet Part B

Figure the unused exclusion amount on line 9. The DSUE amount available to the surviving spouse will be the lesser of this amount or the basic exclusion amount shown on line 9a of Part 2—Tax Computation. Enter the DSUE amount as determined on line 10.

**Section D. DSUE Amount Received from Predeceased Spouse(s).** Complete section D if the decedent was a surviving spouse who received a DSUE amount from one or more predeceased spouse(s).

Section D requests information on all DSUE amounts received from the decedent's last deceased spouse and any previously deceased spouses. Each line in the chart should reflect a different predeceased spouse; enter the calendar year(s) in column F. In Part 1, provide information on the decedent's last deceased spouse. In Part 2, provide information as requested if the decedent had any other predeceased spouse whose executor made the portability election. Any remaining DSUE amount which was not used prior to the death of a subsequent spouse is not considered in this calculation and cannot be applied against any taxable transfer. In column E, total only the amounts of DSUE received and used from spouses who died before the decedent's last deceased spouse. Add this amount to the amount from Part 1, column D, if any, to determine the decedent's total DSUE amount.

## Schedule A—Real Estate


*If there are any assets to which the special rule of Regulations section 20.2010–2T(a)(7)(ii) reported on this schedule, do not enter any value in the last three columns. See instructions for line 10 of Part 5–Recapitulation for information on how to estimate and report the value of these assets.*

If the total gross estate contains any real estate, complete Schedule A and file it with the return. On Schedule A, list real estate the decedent owned or had contracted to purchase. Number each parcel in the left-hand column.

Describe the real estate in enough detail so that the IRS can easily locate it for inspection and valuation. For each parcel of real estate, report the area and, if the parcel is improved, describe the improvements. For city or town property, report the street and number, ward, subdivision, block and lot, etc. For rural property, report the township, range, landmarks, etc.

If any item of real estate is subject to a mortgage for which the decedent's estate is liable, that is, if the indebtedness may be charged against other property of the estate that is not subject to that mortgage, or if the decedent was personally liable for that