

Portability- It's More Complicated Than You Think

Take-Away: Married couples are often misled when their advisors casually say, “you can leave \$15 million free from any federal estate tax.” Glossing over the *portability* filing requirements leads to complacency.

Background: We seem to have fallen into the habit of advising a married couple that they “can leave up to \$15 million in wealth to their children and grandchildren without any federal estate tax.” [IRC 2010.] While that statement on its face is generally accurate, it assumes that the couple will rely on the *portability* of the deceased spouse’s unused applicable exemption amount. While the *portability* rules were not changed with the One Big Beautiful Bill Act (OB3) electing *portability* is a lot more complicated than simply announcing that a surviving spouse may automatically claim the deceased spouse’s applicable exemption amount (DSUEA.)

Portability: The ability of a surviving spouse to use their deceased spouse’s applicable exemption amount, aka *portability*, was made permanent starting in 2013. To take advantage of *portability*, though, requires a formal election.

Election: For the surviving spouse (for ease of reference the *survivor*) to claim *portability*, the personal representative of the deceased spouse’s estate must elect *portability* on a **timely filed** federal estate tax return (Form 706.) [Regulation 20.2010-2(a)(6)(i).] In addition, that estate tax return must be **complete and properly prepared** (which then becomes a trap.) [Regulation 20.2010-2(d) and 20.2010-2(a)(7).] Each year the IRS issues numerous private letter rulings on requests to file a late *portability* election, which suggests that not as much attention is given to the *portability* election as one would assume.

Limitations on Portability: There are a few of limitations on the effective use of *portability* that tend to be overlooked or forgotten, sometimes leading to bad surprises (more on that below).

The Penurious Surviving Spouse: Many surviving spouses are worried about having enough wealth to support themselves for the balance of their lifetime. They are emotional. They are grieving. They are rightfully anxious. As a result, they are not inclined to spend money on pay to prepare and file a Form 706 on which to elect *portability*. Preparing and filing a Form 706 is difficult and expensive, especially if multiple appraisals are required for the decedent's assets. Trying to talk the survivor into incurring an expense that they do not see much, if any, value in is often the challenge their advisors face. This reluctance might also explain why the IRS seems to be inundated with private letter ruling requests asking for the permission to file a late Form 706 on which the *portability* election is made, once after the passing of time the survivor sees value in having access to the DSUEA as his/her estate continues to grow and their initial fear of 'running out of money' dissipates. Today, with the emphasis on saving incomes taxes for heirs, and less so saving federal estate taxes, with the DSUEA, the survivor can still avoid up to \$30 million in federal estate taxes yet obtain a full basis step-up to all of their assets on their death which benefits their heirs.

GST Exemption is Not *Portable*: Often overlooked is that the deceased spouse's generation skipping transfer tax (GSTT) exemption cannot be *ported* to the surviving spouse by an election on Form 706. If the goal is to use the decedent's GST exemption it must be through lifetime gifts where the GST exemption is elected on a Form 709, i.e., a federal gift tax return, (or it is automatically applied using the Tax Code's deemed allocation rules.)

Reverse QTIP Election: The deceased spouse's unused GST exemption amount can be used at death, but only if a qualified terminable interest marital deduction trust (QTIP trust) is used with a 'reverse QTIP election' made by the decedent's personal representative. [IRC 2652(a)(3).] With a reverse QTIP election the assets that pass on the surviving spouse's death will be sheltered from federal estate taxes by the *portability* election (combined with the surviving spouse's own remaining exemption), the transferred assets from the QTIP will be sheltered from GST taxes (using the surviving spouse's own GST exemption and the *ported* GST exemption of the first spouse to die) and all the QTIP trust assets will receive a basis step-up on the surviving spouse's death. However, there often reasons why the married couple are not enamored with the complexity and limitations of a QTIP trust, but that may be the price they have to pay to *port* the deceased spouse's unused GST exemption amount- with a *reverse QTIP election*.

State Estate Tax Exemptions: Of the states that impose state estate taxes, only two, Hawaii and Maryland, have adopted *portability* regimes for any state estate tax exemptions to a surviving spouse. Accordingly, for states that impose estate taxes but do not recognize the transfer of an unused state estate tax exemption amount, that may require more intentional planning to the use of the deceased spouse's state exemption and not rely on the unlimited marital deduction for state estate taxes.

Statute of Limitations Remains Open: There is uncertainty regarding the statute of limitations when it comes to computing the DSUEA. There is no time limit in which the IRS may challenge how the DSUEA amount was initially calculated that binds the IRS. In *Estate of Sower v Commissioner, 149 Tax Court 11 (2017)* the IRS had issued a favorable closing letter for the estate tax return of the first spouse to die. After the statute of limitations had run on that initial federal estate tax return, the IRS adjusted the DSUEA on the surviving spouse's estate tax return. The Tax Court held that the IRS has broad discretion to examine the initial estate tax return and to adjust that DSUEA amount, and because no estate tax was assessed on the death of the first spouse (i.e., the marital deduction was claimed), there was no statute of limitations issue that barred the IRS's examination of the DSUEA that was claimed.

Observation: Because the statute of limitations on the DSUEA remains open, per the Tax Court, it would be wise for a surviving spouse who receives a DSUEA to make lifetime taxable gifts which requires that the DSUEA be utilized *first* by the survivor before the survivor's own applicable exemption amount is used to shelter lifetime taxable gifts. [IRC 6501; IRC 2594(c).]

Timing Requirements: For a valid *portability* election to be made, as noted, the election must be *timely* made. There are four ways to meet the IRS timing requirements. (i) a Form 706 estate tax return is required to be filed, and it filed within 9 months after the first spouse's death; (ii) an estate tax return is required, and an extension to file the Form 706 return is obtained, and the return is filed within the extended period; Note- if the decedent's estate is required to file an estate tax return, the only way to preserve the DSUEA is to make a timely election, which means that by timely filing to do so, and if not, the DSUEA is *lost* and the IRS cannot grant relief (IRC 9100;); (iii) if no federal estate tax return is required to be filed, a simplified method of a late Form 706 may be filed; and (iv) if

no federal estate tax return is required, the estate may seek relief by requesting a private letter ruling (PLR) from the IRS. [Regulation 301.9100-3.]

Revenue Procedures 2017-34 and Revenue Procedure 2022-32: Assume that the first spouse to die did not have a large enough taxable estate that required the filing of a federal estate tax return, but the desire is to transfer the rest of the decedent's DSUEA to his/her surviving spouse who may face a taxable estate at the time of his/her death. The Revenue Procedures outline the requirements for a simplified method for a late filed *portability* election. One Revenue Procedure provides that the IRS will still issue a PLR authorizing a late *portability* election within **five years** after the first spouse's death.

Simplified Form 706: If the deceased spouse's estate size does not require a Form 706 to be filed, but the surviving spouse desires to have *portability* elected, e.g., the decedent's estate plan leaves all of his/her assets to the surviving spouse thus utilizing the unlimited marital deduction, the surviving spouse/personal representative can file a *simplified* (according to the IRS) late Form 706. However, use of the word *simplified* is misleading. Obtaining fair market values can be dispensed with, or relaxed, *only if* the beneficiaries of the decedent's estate are his/her surviving spouse or a charity. If other beneficiaries are to receive a portion of the deceased spouse's estate, then qualified appraisals are still required to support their values on the Form 706. If the *simplified* Form 706 does not comply with all of these reporting rules, then the DSUEA election will be *invalid*, and a later claimed DSUEA will be denied. A current example explains this risk.

Estate of Rowland v. Commissioner: Tax Court Memo 2025-76 (2025): The wife died. Her estate failed to timely file a Form 706. Her estate then filed a late Form 706 under the automatic relief provided by the Revenue Procedures. The Tax Court held that the wife's estate was ineligible to make a late *portability* election because the Form 706 return was "not complete and properly prepared." While some of the valuation reporting rules are relaxed under the Revenue Procedures, that only apply to assets that pass to the surviving spouse or to a charity. In this case, the wife's estate reported unsupported asset values, and it made no meaningful effort to determine the fair market value of the assets, and it included assets without the corresponding proper valuations to recipients (grandchildren) who did not qualify for the marital or charitable deduction. This result occurred when the husband died and, his estate claimed the DSUEA from his late wife's late-filed Form 706. No DSUEA was available to the husband's estate. While his estate argued 'substantial

compliance' with the relaxed reporting and filing rules, the Tax Court pretty much dismissed that argument without much discussion, noting: “ *We are hard-pressed to say that [an estate] can gain the benefit of [the safe harbor] without adhering to the conditions the IRS imposed.*” In other words, the Court’s decision suggests that strict compliance will be required for a late filed *simplified* Form 709. Consequently, on the husband’s death, several million in estate taxes had to be paid because it was denied claiming the DSUEA, which would not have been the result if his late wife’s late filed *simplified* Form 706 had complied with the Revenue Procedure rules and Regulations.

Portability Practicalities: Some interesting aspects apply to who can make a *portability* election. Some practical observations and/or suggestions follow.

Document the Decision Not to File: If the widow or widower does not want to incur the expense of filing a Form 706 on which a *portability* election is made, that should be documented by the estate fiduciaries. It would make sense to obtain a written waiver from the widow or widower.

The Portability Decision- A Direction or Discretion? The decedent’s Will should identify whether the Personal Representative is required to file a *portability* election or is given the discretion to make that election. The Will (or trust) might describe this duty and outline the reasons the fiduciary should consider in making the *portability* decision?

Who Makes the Decision? Who decides *portability* may be more problematic than we think. By way of example, in a second marriage, the deceased’ husband leaves only tangible personal property to his second wife as joint tenants. His children from the first marriage are the beneficiaries of his revocable trust. There is no need for probate and no estate is opened. IRC 2203 says that in the absence of an appointed Personal Representative, anyone in possession of the decedent’s assets if there is no estate proceeding can file the Form 706 and elect *portability*. No ‘priority’ of who can file the Form 706 is provided in IRC 2203. Can the widow who inherits only personal property from her late husband file Form 706 and force the cost of preparing and filing that return onto the decedent’s revocable trust, where only his children benefit?

Who Pays the Cost of Preparation and Filing, Including Appraisal Costs and Audit Fees?

The decedent's Will should describe who is responsible to pay the Form 706 filing fees to assure the timely filed *portability* election. This is important in a second marriage where the surviving spouse has a greater need to claim a DSUEA, but the decedent's children from the first marriage inherit their deceased parent's estate. Probably this directive, i.e., who pays the cost of filing, should be included in the decedent's revocable trust. And as indicated in the Tax Court case above, if there is an audit of a claimed DSUEA, who should pay for the legal and accountings fees associated with that audit should also be addressed in the decedent's Will and trust.

Should *Portability* be Treated as Property? Is a *portability* election property? Normally a tax election is not property in the traditional sense, but clearly a surviving spouse of wealth will consider it the 'next best thing' to property. Often the topic of *portability* is covered in a prenuptial agreement, so presumably the parties to that agreement saw some value in it. Consider, too, that the Oklahoma Supreme Court held that in the absence of specific *portability* provisions in a premarital agreement or the decedent's Will or trust, a surviving spouse was entitled to compel the Personal Representative of the decedent's estate to elect *portability* on the estate tax return, but he was obligated to pay the filing costs associated with the return. In its decision, the Court did not define a *right* to *portability* election except to note that it was not "simple property, but an interest 'created by the federal Tax Code.'" *In re Matter of the Estate of Anne S. Vose v. Lee, Oklahoma Supreme Court (2017.)*

Conclusion: As advisors we tend to take the availability of a *portability* election for granted. We shouldn't. The election can be costly to make, and only the surviving spouse (and his/her descendants) will benefit from the election. And there are plenty of 'hoops to jump through' to claim *portability* and the failure to timely file the Form 706 return can cause it to be lost. And the fact that there is no statute of limitations on the DSUEA calculation means that it can always be revisited by the IRS on the death of the second spouse. In short, the ability to claim *portability* is not a simple decision, and if the election is made, it will probably be expensive, so the decedent's Will (or trust) should clearly identify who should pay for filing an estate tax return that might not be required to be filed.

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