

**Portability**  
-  
**Panacea? Pariah? Placebo?**  
-  
**Plethora of Possibilities!**

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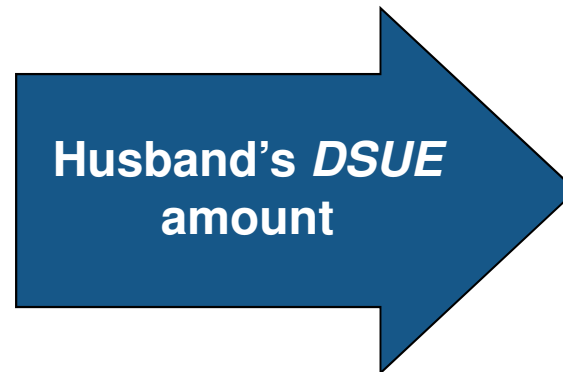
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*Estate Planning Council  
of Greater Miami*

*November 15, 2012*

# Portability

*“**Portability**” refers to the estate tax concept of being able to transfer (or “port”) a deceased spouse’s unused exclusion (“DSUE”) amount over to the surviving spouse (Note: there is no portability of the GST exemption).*



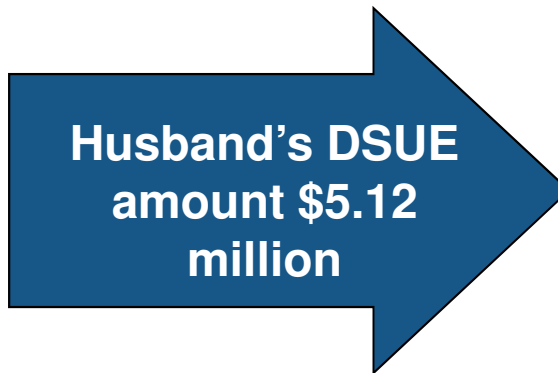
# Portability

*To take advantage of Portability, the executor must make the portability election on a “complete and properly-prepared” estate tax return which is timely-filed.*



## Example #1:

*Husband (H) dies in 2012, having made no inter vivos gifts and leaving his entire \$10 million estate to his wife (W). Thus, at his death, H's DSUE Amount is \$5.12 million.*



*If H's executor elects portability on H's timely filed estate tax return, then, as of H's death, his DSUE amount is ported to W.*

**Example is for illustrative purposes only.**

## *New Terms –*

- **Basic Exclusion Amount** = \$5.12 million (in 2012); it was \$5 million (in 2011).
- **Deceased Spouse Unused Exclusion (“DSUE”) Amount** = Deceased spouse’s unused **applicable exclusion amount** at the time of the decedent’s death that can be ported over to the surviving spouse.
- **Applicable Exclusion Amount** = BEA + ported DSUE amount.

## *New Regulations –*

- Temporary Regulations –
  - Enactment date June 15, 2012 for some, but most as of January 1, 2011.
- Proposed Regulations
  - Duplicate of Temporary Regulations
  - Comment Period
  - Hearing in Washington, D.C.



## *Huge Changes Made by New Regulations –*

- Making the election
- No Election – No DSUE amount ported
- How DSUE amount is computed
  - Clarified Joint Committee on Taxation’s *Example 3*
  - When decedent made taxable gifts and paid gift tax
  - QDOT’s
- Identifying the “Last Deceased Spouse”
- Multiple Deceased Spouses and “previously applied” DSUE amounts
- New Order (ing rule)

### *Making the Election*

- Must file a “timely-filed” estate tax return, without regard to size of gross estate and taxable gifts. Generally, timely-filed is 9 months after death with a 6-month extension.
- Once election is made and time for filing is expired, then portability is “irrevocable”. Can revoke up to the 9-month (or, if extended, 15-month) period.
- No election; No portability.
- No election for Non-Resident Non-Citizens permitted.
- Clarified who is the “executor,” and implemented new rules, if no “probate” executor.

### *Making the Election*

- Requirements for the return
  - “Complete and properly-prepared” – if in accordance with Instructions for filing estate tax return and Treasury’s other regulations
  - Special Rules if estate is a “smaller estate”
    - Simplified filing requirements
    - Rounding \$250,000
    - May not be of much help with certain plans and those in states with estate taxes.
- Computation of DSUE required; however, transitional rule.

No Election = No DSUE amount ported



### *Making the Election*

- Two ways **NOT** to make the Election
  - Failure to timely file –§ 301.9100 relief (maybe for smaller estates)?
  - Opt out on a timely filed estate tax return

Q: Why would executor **NOT** make the election?

A: Cost / Benefit analysis

### *How DSUE amount is computed*

- “Interpreted” the Internal Revenue Code to change how DSUE amount is calculated in two ways:
  - Changed the “first limitation” from “surviving spouse’s BEA” to the “last deceased spouse’s BEA”; and
  - Changed the second limit from the surviving spouse’s BEA to the surviving spouse’s AEA (adopting the Joint Committee on Taxation’s position in Example 3)

### *How DSUE amount is computed*

Q: What is the impact of the first limitation?

A: Arguably, Treasury misread the statute. However, the benefit is that the likelihood of “Portability Clawback” or “Portability Recapture” is eliminated.

Q: What is the impact of the change from using the last deceased spouse’s BEA versus using the AEA.

A: You eliminate the “privity” issue, so you can port from H1 to W to H2. In other words, H2 could literally use H1’s unused exclusion amount. Thus, larger DSUE amount.

***Example #2:*** *H1 and W were married and H1 dies in 2011, having left his entire \$15 million estate to W. H1 and W made no lifetime taxable gifts. Portability is properly elected on H1's timely filed estate tax return. Subsequently W marries H2, and W dies in 2012, predeceasing H2. W leaves 1/2 of her estate to H2 and 1/2 to her children. H2 makes no lifetime taxable gifts and dies in 2012 after W.*

### *H2's DSUEA*

<b><i>Result under the Internal Revenue Code</i></b>	<b><i>\$0</i></b>
<b><i>Result under the New Temporary Regulations</i></b>	<b><i>\$2.62 million</i></b>

**Example for illustration purposes only.**



### *How DSUE amount is computed*

- Also ...
  - Clarified that if the decedent made taxable gifts and paid gift tax, that the amount that you don't lose the benefit if the exemption goes up.

***Example #3:*** *H1 and W are married and both are U.S. citizens. In 2003, when the unified credit was \$1 million, H1 made a taxable gift of \$3 million, paying gift tax on \$2 million. Thereafter, and until H1's death in 2011, no other taxable gifts were made by H1 or W. H1 leaves his entire \$10 million probate estate (which was his gross estate, too) to W. Assume that H1 and W were residents of State X, that has no state death tax. W, as H1's executor, properly and timely makes a portability election.*

*Q: How much of H1's DSUE amount ports to W?*

*A: \$4 million. Disregard the \$2 million on which H1 paid gift taxes, so it is as if his total taxable gifts were \$1 million; thus, \$5 million less \$1 million of taxable gifts.*

Q: Who is the **Last Deceased Spouse**?

A: Clarified that it's the last person that the decedent was married to at the time of the decedent's death.

A: Also clarified that if the decedent married and divorced a person, that it would have no effect on the last deceased spouse.



H1 is the Last Deceased Spouse



*Example: H1 was married to W. H1 dies. W marries and subsequently divorces H2. H2 dies (after the divorce). H1 is W's last deceased spouse.*

**Example for illustrative purposes only**

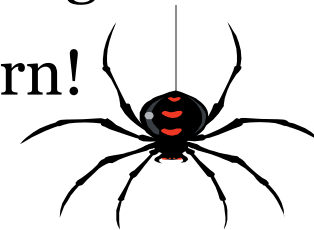
Q: What’s the difference between the “Last Deceased Spouse” and “Prior Deceased Spouse”?

A: New concept –

Last Deceased Spouse – Last spouse of the decedent who was married to the decedent at the time of such spouse’s death.

Prior Deceased Spouse - A spouse of the decedent who was married to the decedent at the time of such spouse’s death, however, such spouse was not the “last” deceased spouse of the decedent. Relevant only if the decedent used any of such prior deceased spouse’s DSUE amount during life.

Concept – ignored the “Black Widow” concern!

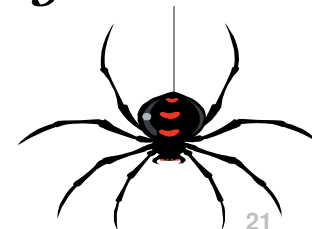


## Portability – Regulation Changes

**Example #4:** H1 and H2 are married. They make no taxable gifts during H1's lifetime. H1 dies in 2011 leaving his \$10 million estate to H2 (outright). W then makes a gift in 2011 of \$5 million to her children. W marries H2 in 2011 after the gift. H2 dies in 2012 leaving his entire \$10 million estate to W. W then makes another \$5 million gift to her children in 2011. W marries H3 in 2011. H3 dies and leaves his \$10 million estate to W. W dies later in 2011, leaving her \$20 million estate to her children. W, was executor of H1, H2 and H3's estate and made portability elections).

*Result: W gets to use H1's and H2's DSUE amount (because H1 and H2 are W's prior deceased spouses and she made lifetime taxable gifts of such DSUE amount. And W gets to use H3's DSUE amount as W's last deceased spouse.*

**Example for illustrative purposes only**



### *How DSUE amount is computed*

- New Rule ...
  - Add the DSUE amount of “prior” deceased spouses, if the decedent used such prior spouse’s DSUE amount for lifetime gifts!
- New Regulations DSUE amount =
  - DSUE amount from Last Deceased Spouse; **PLUS**
  - DSUE amount from prior deceased spouses, if there were used against prior taxable gifts made by the decedent.

### New Order (ing rule)

- Use the ported DSUE first, before using the surviving spouse's BEA.

***Example #5:*** H1 and W were married having made not taxable gifts during their married life. H1 dies in 2011, and H1's executor makes a proper, timely portability election. H and W had \$30 million owned as joint tenants with right of survivorship. Later in 2011, W makes a gift of \$7 million to her children.

Result: W uses up H1's ported DSUE amount of \$5 million, and then uses \$2 million of her BEA.

### Who is the Executor?

- If there is a probate executor, then that is the person who makes the election.
  - Executor, same meaning as in the Internal Revenue Code § 2203 (i.e., person in possession of property may be the executor).
- If there is no executor, then someone who is “in possession of property” can make an election. Another person “in possession of property” can not override the election made by someone else.



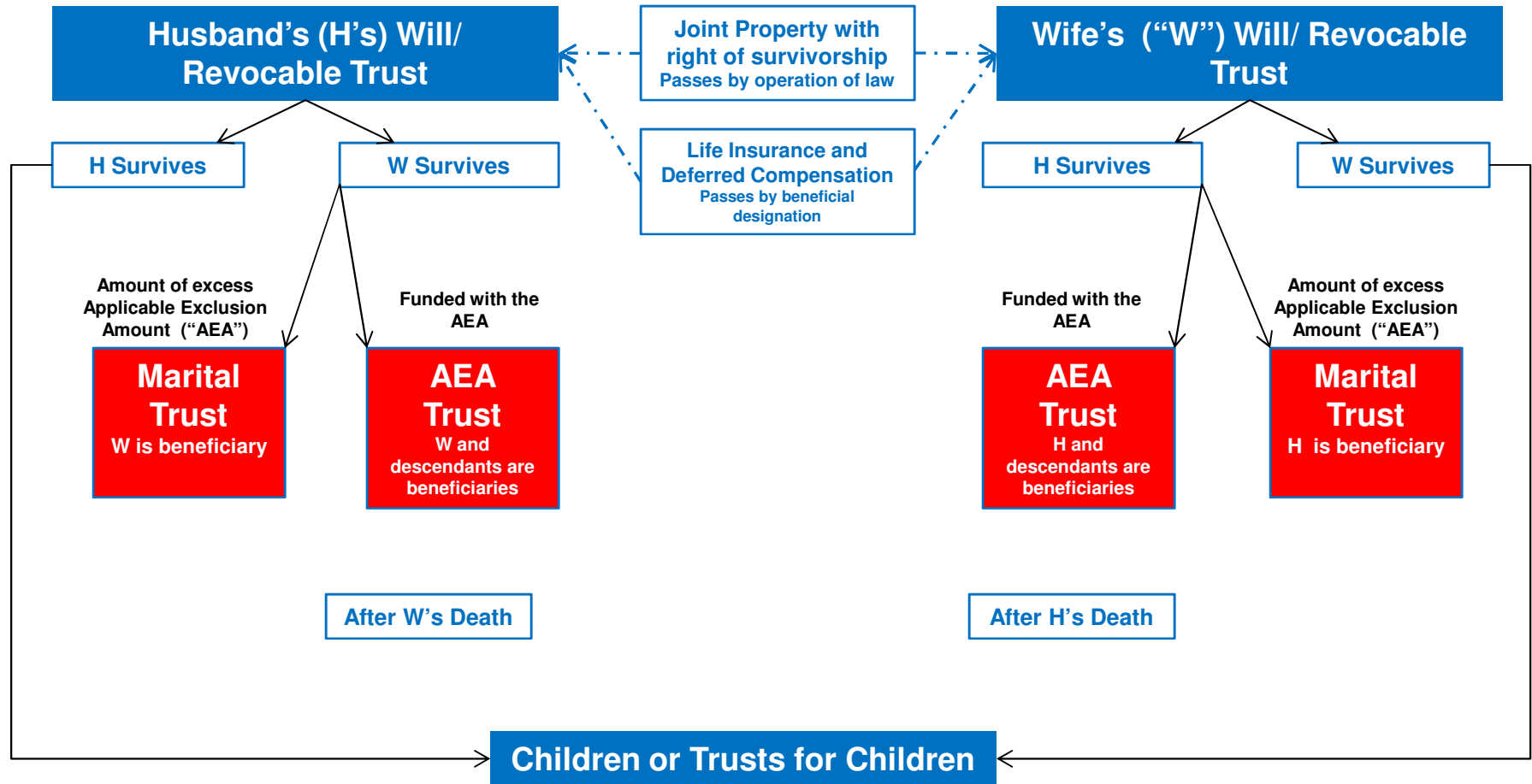
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# Comments to Treasury

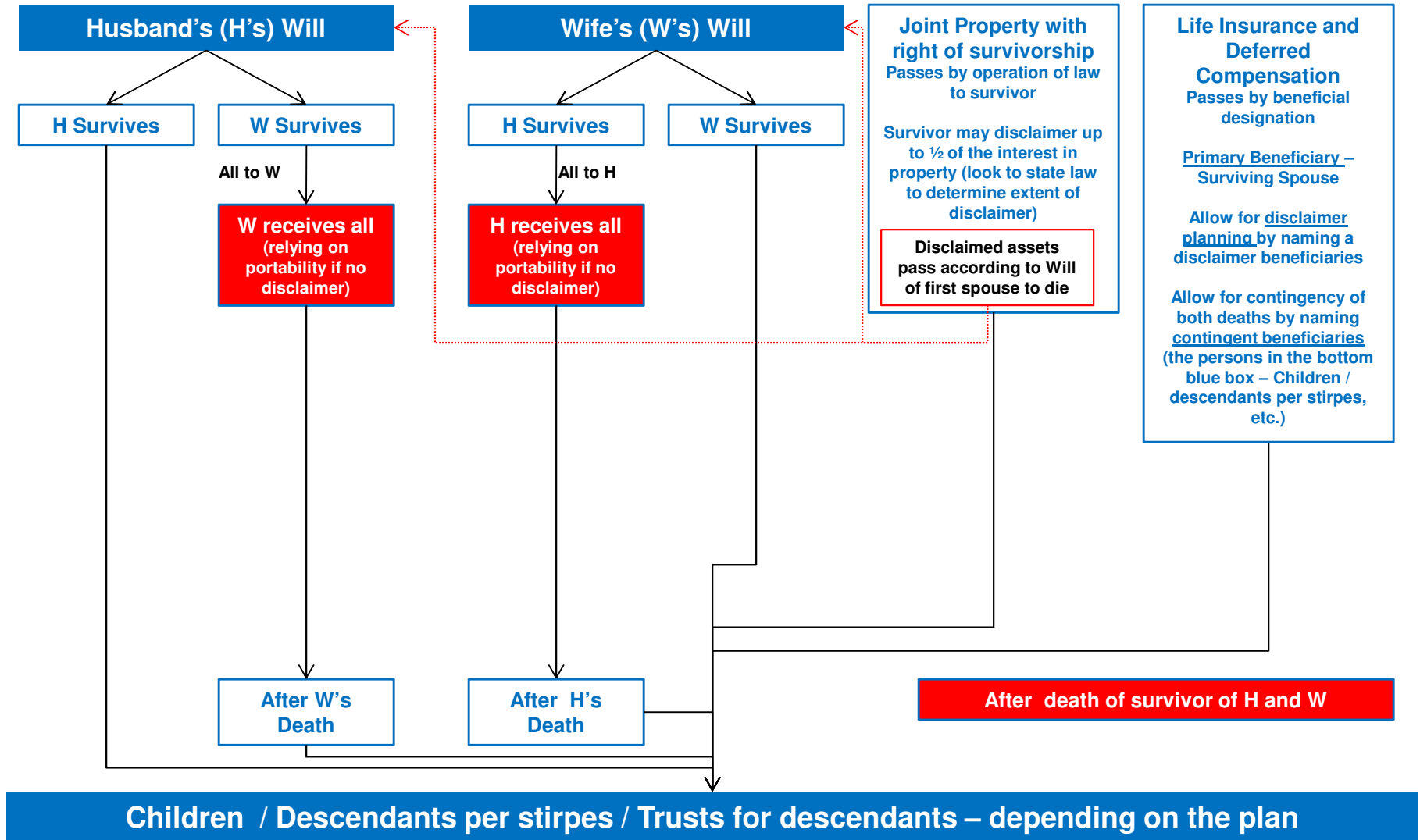
*On October 5, 2012, the ABA-RPTE Section sent Comments to Treasury on the New Temporary and Proposed Regulations. Here is a link to the Comments (posted on the ABA-RPTE's website:*

[http://meetings.abanet.org/webupload/commupload/RP512500/relatedresources/2012\\_10\\_04\\_comments\\_on\\_portability\\_of\\_transfer\\_tax\\_exemptions.pdf](http://meetings.abanet.org/webupload/commupload/RP512500/relatedresources/2012_10_04_comments_on_portability_of_transfer_tax_exemptions.pdf)

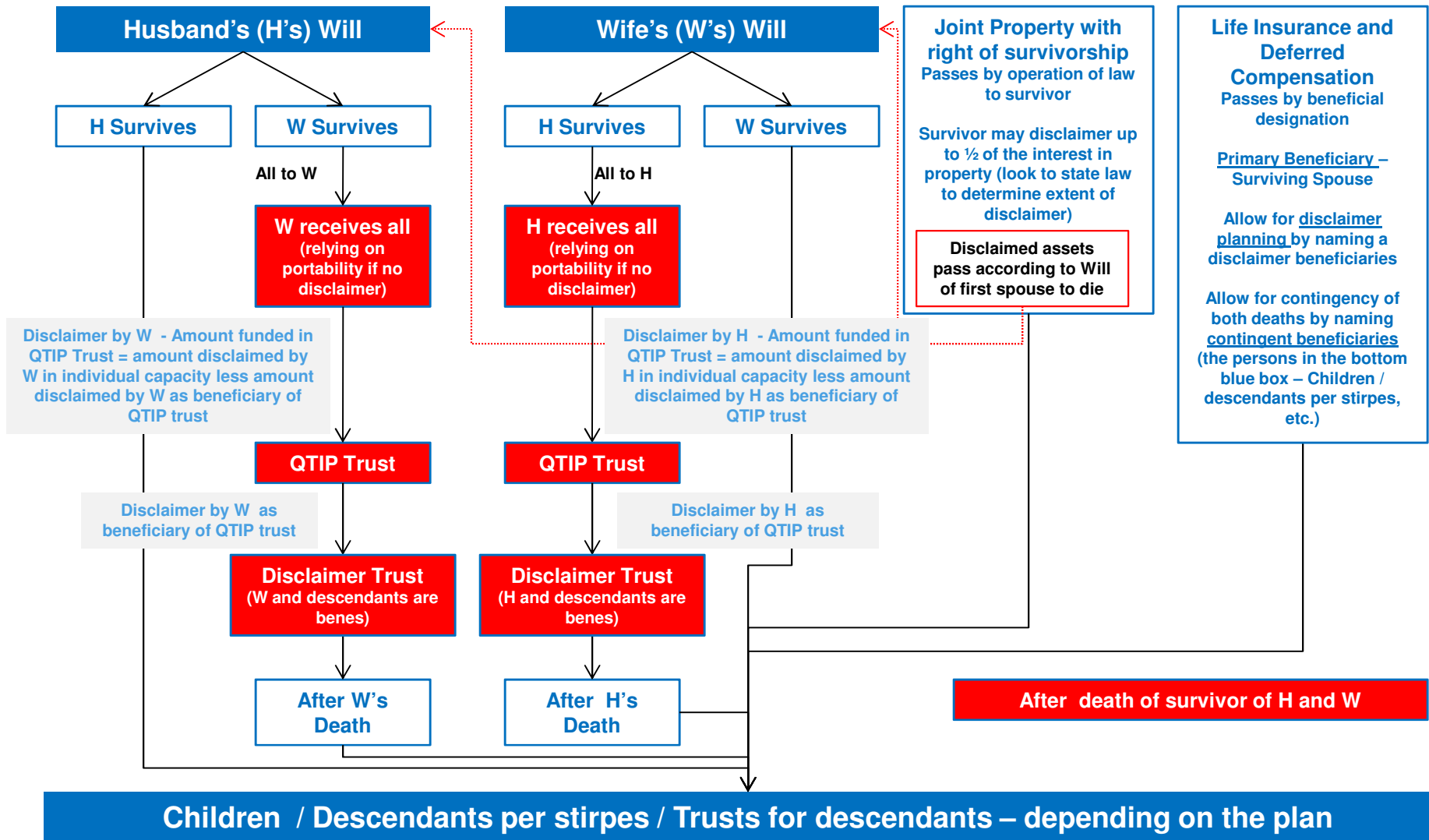
- “Traditional Plan” *v.* “Portability Plan”
  - Common Thinking about a Portability Plan
- Forward thinking with Portability
  - Traditional Planning with a Twist
    - Use of Disclaimer Trust planning
    - Use of Testamentary QTIP Trust planning
      - Caveat – Rev. Proc. 2001-38
- Portability’s Continuance
- Other Thoughts
  - Premarital Planning
  - Planning Today



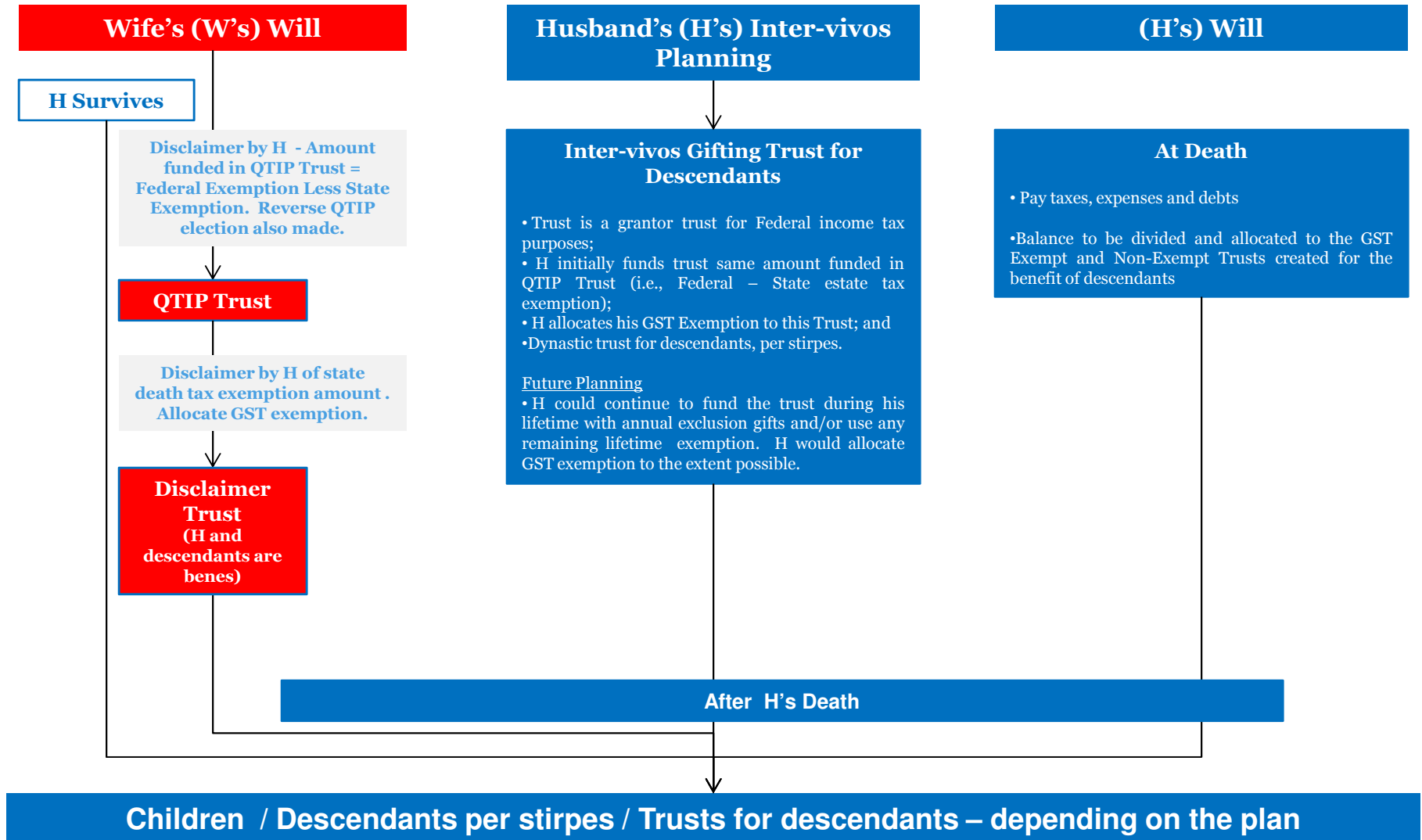
# Disclaimer Planning – Will / Revocable Trust – with QTIP Trust (page 1)



# Disclaimer Planning – Will / Revocable Trust – with QTIP Trust (page 1)



# Disclaimer Planning – Will / Revocable Trust – with QTIP Trust (page 2) – assume W dies



# Disclaimer Planning – Will / Revocable Trust – with QTIP Trust (page 3) – assume W died

## Wife's (W's) Will

### RESULT #1 – (after W's death)

Husband fully utilizes W's unused GST Exemption

- By funding the GST Exempt QTIP Trust to the extent of the excess of the Federal Estate Tax Exemption over the State death Tax Exemption (i.e., fully utilizing W's GST Exemption).

### RESULT #2:

H fully utilizes the state death tax exemption and uses part of W's GST exemption (see Result #1, where all of the unused GST Exemption is utilized).

- In doing this, there is no state death tax that is triggered (for states with state death taxes).

## Husband's (H's) Inter-vivos Planning

### Inter-vivos Gifting Trust for Descendants

### RESULT #3 – (soon after W's death)

#### H's gift to Gifting Trust:

1. Fully utilizes W's ported exemption.
2. By making a gift, except for one state (i.e., CT, FYI: TN just got rid of their gift tax), H avoids state gift tax (on the amount passing into the trust (which is effectively a substitute for a Credit Shelter Trust for descendants).
3. Allocates part of H's GST exemption to this trust.
4. Since this is a grantor trust, with proper planning, H can get some (if not all) step-up in basis at time of his death (by using a substitution power).

## (H's) Will

### At Death

### RESULT #4 – (when H dies)

When H dies, effectively H and W would have:

1. Used all of W GST exemption (at her death).
2. Used all of W's unused estate tax exemption at her death and when H makes the gift to the gifting trust.
3. Used some of H's GST exemption when he made gifts to gifting trust.
4. Used the balance of H's unused GST exemption and estate tax exemptions at his death.
5. Effectively had a grantor trust that served like a credit shelter trust during H's life.
6. Avoided state death tax on W's amount passing into the gifting trust.

Children / Descendants per stirpes / Trusts for descendants – depending on the plan

- Big 5
  - Current Administration's View
  - Non-partisan provision
  - Viewed as middle class benefits
  - The Democrats even put out a bill to continue Portability
  - Service has it as a priority item



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## Portability – Other Thoughts

Need to review and revise premartial agreements for portability.

The DSUE Amount may be a valuable asset

Portability is a game changer!

Thus, planning with portability requires:

- New and different ways to think about it;
- New and different ways to plan for it; and
- New planning techniques.

# QUESTIONS?