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## Estate Tax Portability Election: Congress Expands the Federal Estate and Gift Tax Exemptions for Two Years

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2010 was the year there was no federal estate tax. However, along with that, we were limited in the amount of available step-up in the basis of inherited assets. An estate was limited to a \$1.3 million step-up unless the assets went to the spouse and then a \$3 million step-up was available. The other assets were inherited with a carry-over basis. For example, assume the decedent paid \$19,000 for land in 1920, but it is worth \$800,000 at the time of death. The heir to the property would only receive a \$19,000 basis. Consequently, if they sell the property for \$800,000, they will recognize a \$781,000 taxable gain.

The president signed the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 on December 17, 2010. One part of this major tax bill was the reinstatement of the estate tax exemption. While estates for 2010 decedents were not subject to the estate tax, this bill allows them to elect to use a \$5 million exemption and have a stepped-up basis. For many estates, this is superior to no estate tax and a carry-over basis. The bill also allows the \$5 million exemption for deaths in 2011 and 2013 and caps the top tax rate at 35%. The exemption is scheduled to be reduced to \$1 million for deaths in 2013 and later years with a top rate is 55%.

A major change was made in estate tax planning due to the bill. This is the inclusion of a "portability election" in the bill. This will allow a married couple to exclude up to \$10 million of total assets from federal estate and still have a stepped-up basis. The way it works is:

1. If the first spouse dies in 2011 or 2012, they have a \$5 million exemption. If however, their estate is less than \$5 million, the unused portion of their exemption can be given to the surviving spouse. Assume John dies in 2011 and has a \$2 million estate. The unused \$3 million exemption can transfer to his wife Jane.
2. If the surviving spouse dies in 2011 or 2012, they will have a \$5 million exemption plus the unused amount from the first to die. This means Jane can have a \$8 million estate and no federal estate tax and the assets will receive a stepped-up basis.

The portable exemption amount only applies to the unused exemption from the last spouse. Consequently, if there have been multiple marriages, only the most recent spouse's amount is available.

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In addition, an election must be made in the estate of the first spouse to die to preserve the unused exemption and allow for its use by the last deceased spouse.