

US ESTATE TAX: LATE PORTABILITY

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US estate tax is imposed if a US citizen or resident's taxable estate exceeds \$5.49 million. That exclusion amount is portable between spouses: any portion not used by the first spouse to die may, via a timely election, be added to the exclusion amount available for the surviving spouse.

Assume that Mr. X, a US citizen or resident, dies in 2017 with an estate worth \$2.49 million. At Mrs. X's death, her exclusion amount increases by Mr. X's \$3 million unused exclusion amount (provided she is also a US citizen or resident), provided that Mr. X's estate files a US estate tax return within 9 months of his death (or within 15 months if a filing extension was obtained) and elects to apply the deceased spousal unused exclusion (DSUE) amount to Mrs. X.

Generally, failure to file an estate tax return in a timely manner means that the DSUE amount is not portable to the surviving spouse; at an estate tax rate of 40 percent, this failure to pass the DSUE to a surviving spouse may result in a significant additional US estate tax liability. However, if an estate is not otherwise required to file a US estate tax return—because the decedent's gross estate, plus adjusted taxable gifts, does not exceed the applicable exclusion amount—Treasury regulation section 20.2010-2(a)(1) provides that the IRS may grant an extension of time to file a return and make a portability election. In those situations, the regulations provide that an extension of time may be requested by using the letter ruling procedures of regulation section 301.9100-3: the IRS grants relief if it is demonstrated that the taxpayer acted in good faith and that the grant of relief would not prejudice the interests of the US government. Thus, if the decedent's estate would file a US estate tax return only for portability purposes but failed to file that return within nine months of death (plus any extensions), the regulations allow the estate to submit a letter ruling request to the IRS for additional time to file the return and make a portability election. No extension is allowed if the decedent's assets (plus adjusted taxable gifts) exceed the applicable exclusion amount (\$5.49 million in 2017).

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Because of what had been the relative obscurity of US estate tax portability and the newness of the underlying statute, the IRS has been inundated with letter ruling requests asking for additional time to make the election. On June 9, 2017, the IRS issued Revenue procedure 2017-34, effective as of that date, which until further notice supersedes the regulations and establishes a new procedure to obtain late portability election relief if the decedent is not otherwise required to file a US estate tax return because his or her gross estate, plus adjusted taxable gifts, does not exceed the applicable exclusion amount. The Revenue procedure provides that a late portability election may be made simply by filing a US estate tax return (albeit otherwise untimely) that is marked as “FILED PURSUANT TO REV. PROC. 2017-34 TO ELECT PORTABILITY UNDER §2010(c)(5)(A).” The Revenue procedure requires the IRS to automatically grant late election relief to any return filed in that manner, provided that (1) the decedent’s gross estate, plus adjusted taxable gifts, does not exceed the applicable exclusion amount; and (2) the return is filed before the later of January 2, 2018 and two years after the decedent’s death.

The IRS is not accepting letter ruling requests made during any period for which a request may be made under Revenue procedure 2017-34, and it is (1) closing out all such letter ruling requests currently in process, (2) directing those estates to comply with the new Revenue procedure, and (3) refunding the \$9,800 letter ruling user fee. The IRS will continue to entertain letter ruling requests if relief under the new Revenue procedure is not available (that is, if the return is not filed before the later of January 2, 2018 and two years after the decedent’s death).

The future of the US estate tax is in question in the current US political landscape. But, even if it is repealed, the US estate tax may later be reinstated under another administration. Thus, irrespective of what may happen to US estate tax in the short term, advisers should plan for the possible continuation of US estate tax, and they should counsel the estate of a US citizen or resident to consider making a portability election whenever a decedent is survived by a spouse who is a US citizen or resident.