TAX

The move that protects everyday millionaires from the estate tax hit in 2026

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Surviving spouses now have more time to lock in the exclusion of a deceased partner.

The amount of wealth that rich Americans can shield from estate taxes is at historic highs — just over $12 million for individuals and double that for married couples. But the tax benefit will do a 180-degree turn come 2026 when the protected amounts revert to half those levels.

The shift will slam ultrawealthy taxpayers who are over the current exclusion hurdles. But for well-heeled taxpayers who aren't hit by the 40% estate tax now but could get caught in three years, it's now easier to lock in the current benefit for a surviving spouse long after it falls by half.

When one spouse passes away, the surviving partner typically inherits a chunk, if not all, of the deceased person's estate. The windfall is tax-free, regardless of its size. When the surviving spouse later dies, the inherited assets are included in her own estate and the whole pot can be subject to estate taxes. While her separate assets may be under $12 million, the prior addition of the inherited amount can swell the pot enough for the excess to get hit with the 40% levy.

The means for potentially avoiding that just got smoother, thanks to a July ruling by the Internal Revenue Service that gives a surviving spouse five years to lock in for their own benefit the unused exclusion of a deceased spouse. The previous time limit, established in 2017, was two years; before that it was 15 months.

Known under IRS rules as "portability," the locking-in process is available only to taxpayers who don't have to file an estate tax return because their estates aren't large enough. What's confusing to many financial advisors and their clients is that to activate portability, an estate has to file an estate tax return, even if it's a smaller one that isn't required to.

Electing portability effectively doubles a surviving spouse's individual exemption in place when the partner died. All of this means that wealthier married couples who don't think they need to file an estate return — because their individual net worth is below $12.06 million — should nonetheless plan for the estate of a futurely deceased spouse to file one and elect portability to lock in the surviving spouse's exclusion. A person has to have died by Dec. 31, 2025, which is when the current exemption levels, boosted under the 2017 tax cuts, will fall by roughly half. The surviving spouse must instruct the executor of the deceased spouse's estate to file a return in which portability is elected.

"Even if you're not tripping up against the exemption levels, if you're close to them, you should file an estate tax return anyway," said Justin Miller, the national director of wealth planning at Evercore in San Francisco.

A dual Romanian-U.S. citizen has been fighting an IRS contention that he owes $2.7 million for failing to submit FBAR forms.

Say a husband dies today and leaves his wife $8 million and the wife has $8 million of her own assets. If portability is elected within five years, she can add the husband's $12 million exclusion — even if she makes a portability election in, say, 2027, when the inflation-adjusted individual exclusion will be around $7 million.

Without portability, the wife's estate would owe the 40% estate tax on nearly $9 million of assets ($18 million minus $7 million), or $3.6 million. The scenario, said Marc Stern, a partner in the private client services group at Greenberg Glusker in Los Angeles, assumes that neither spouse has used up any part of their lifetime exclusion by making gifts to heirs.

So why should people who are below or near their exemption level plan to file the document? It's not only that a deceased spouse can leave the survivor amounts that exceed her exemption, Stern said. There's also the possibility that the surviving spouse may inherit additional money from other relatives.

Steve Wittenberg, the director of legacy planning at SEI Investments in Oaks, Pennsylvania, said that he recommended all people with a net worth of $10 million to $20 million file an estate tax return and elect portability. Once exemption levels fall by half in 2026, the same move should be made for any surviving spouse whose estate is expected to exceed $3 million, according to The Pollock Firm, a law firm in Princeton, New Jersey, and Boca Raton, Florida, that's focused on trusts, wills and estates.

It sounds simple enough to do. But steep costs and awkward timing have meant that many taxpayers haven't filed an estate return electing portability within the old time limit of two years. In 2020, 3,441 estates filed returns, according to IRS data. Less than one in 10, or 326, were for estates valued at less than $10 million, while more than half, or 1,859, were for estates with a gross value between $10 million and under $20 million.

The returns — what Miller called "one of the most complicated and expensive tax returns" — can cost tens of thousands of dollars. Plus, nobody in the throes of grieving a lost spouse wants to think about tax documents.

"You're dealing with distributions, burials, funerals and all the psychological and emotional stuff, so oftentimes the No. 1 thing on their list isn't to file this 706," said Miller, referring to the estate tax form.

With the new five-year limit, the IRS isn't creating a bigger benefit for people seeking to transfer assets to heirs. "Somebody still has to die" to lock in the exemption in existence when you pass, Stern said. The IRS made the change because it was overwhelmed with requests from taxpayers who missed the two-year deadline for a so-called private letter ruling — an individual blessing from the nation's tax collector — authorizing portability.

Advisors say that the advantage comes from having more time to make a money-saving move.

"It gives people more time to think about using it and [to] take those administrative steps," Wittenberg said. By doing so, he added, "you can move more money out of your taxable estate."

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