



Joel S. Rothman

Christopher R. Fleck  
Burt C. Binenfeld  
Seth J. Mersky

*Of counsel*

Stuart A. Cohn  
Robert G. Evans  
Mark T. Neil  
Lorri E.K. Otis  
Michel Winkelstein

September, 2013

## **Federal and Illinois Law Update –**

Dear Clients and Friends:

From all of us at the Rothman Law Group, we hope this letter finds you well.

We are writing to discuss significant changes to the Federal and Illinois gift, estate and generation-skipping transfer tax laws, as well as to briefly summarize the recent Supreme Court decisions regarding the rights afforded to individuals in a same-sex marriage. We will also review the available estate planning opportunities under the current tax code and the important non-tax reasons to review current estate plans.

Before we begin, we would like to introduce our newest associate, Seth J. Mersky. Seth joins us via The George Washington University and the University of Miami School of Law, where he earned a Juris Doctor, *cum laude*, and a Master of Laws (LL.M.) degree in taxation. A New Jersey native, Seth is a member of both the Illinois and Florida bars, and he has a broad knowledge of all aspects of domestic and international tax law. By adding Seth to our group, we are enriching our ability to continue providing the high-quality, sophisticated tax and estate planning that has come to be expected from us.

### **I. Federal Estate and Gift Tax.**

#### **A. Gift Tax Changes.**

This year began with the passage by Congress of the American Taxpayer Relief Act of 2012 (“the Taxpayer Relief Act”) which was signed into law by President Obama on January 2, 2013. Under the Taxpayer Relief Act, the lifetime gift tax “Applicable Exclusion Amount” increased substantially. As a result, each person may now make a total of \$5,250,000 in lifetime gifts without paying gift tax (the “Lifetime Gift Tax Exclusion Amount”). The gift tax rate on gifts in excess of \$5,250,000 is now 40%, which is an increase from the prior rate of 35%. The new Lifetime Gift Tax Exclusion Amount is indexed to increase each year for inflation.

September, 2013

Page 2

The *annual* gift tax exemption, which is the amount each person can give each year to an unlimited number of beneficiaries before using any of his or her Lifetime Gift Tax Exclusion Amount, is now \$14,000 per donee per year. This exemption will continue to be indexed annually for inflation.

#### **B. Estate Tax Changes.**

The amount each person is able to exclude from Federal estate taxation upon death has also been increased to \$5,250,000 (the “Estate Tax Exclusion Amount”) and will be indexed for inflation. It is important to note, however, that the Lifetime Gift Tax Exclusion Amount and Estate Tax Exclusion Amount remain “unified,” which means that gifts made during one’s lifetime will reduce the Estate Tax Exclusion Amount available upon one’s death. For example, if a person gives \$1,250,000 of taxable gifts during his or her lifetime, he or she will have a remaining Estate Tax Exclusion Amount of \$4,000,000 available at death in 2013. The tax rate on estates in excess of the Estate Tax Exclusion Amount is now 40%.

As you may be aware, a concept called ‘portability’ allows a surviving spouse to elect to take advantage of any unused portion of the Estate Tax Exclusion Amount of his or her deceased spouse. Portability was added to the estate tax laws in 2011 and has been made ‘permanent’ by the Taxpayer Relief Act. Portability enables a married couple to transfer up to \$10,500,000 in 2013 before paying any estate taxes, even if the first spouse to die did not have an optimum estate plan. **It is important to note, however, that (i) portability must be elected on a timely prepared and filed Federal estate tax return following the death of the first spouse; (ii) as discussed more fully below, portability is not available with respect to the Illinois estate tax; and (iii) there is no portability of the Generation-Skipping Transfer Tax (“GST Tax”) exemption.**

#### **C. GST Tax Changes.**

The GST Tax is imposed on certain transfers to an individual’s grandchildren, later descendants, or other persons at least 37.5 years younger than the donor (“skip persons”). The amount each person is able to exempt from GST Tax has also been increased to \$5,250,000. Proper use of this exemption enables a person to transfer up to \$5,250,000 in trust for the lifetime benefit of a child or other beneficiary without that amount being subject to tax again at that person’s death when the assets pass to the next generation. This exemption amount will also be indexed for inflation in future years.

### **II. Illinois Estate and Gift and Taxes.**

Illinois imposes its own estate tax that is separate and distinct from the Federal estate tax. For Illinois residents, the tax is imposed on the value of all assets, wherever located, other than real estate outside of Illinois. For non-Illinois residents, the tax is imposed only on real estate and

September, 2013

Page 3

personal property physically located in Illinois. Estates that exceed \$4,000,000 in value are subject to Illinois estate tax at rates between 8% and 16%.

**The Illinois estate tax law does not have a portability provision.** As a result, if the first spouse to die does not take full advantage of his or her own \$4,000,000 Illinois estate tax exclusion amount, it will be ‘lost’ and the surviving spouse will have only his or her own \$4,000,000 amount available. Because of the absence of Illinois portability and the lower exclusion amount of \$4,000,000 rather than the Federal Estate Tax Exclusion Amount of \$5,250,000, **special planning must be undertaken in order to minimize, to the extent possible, the application of the Illinois estate tax.** Illinois does not currently impose a gift tax.

### **III. Same Sex Marriage.**

On June 26, 2013, the United States Supreme Court declared Section 3 of the Federal Defense of Marriage Act, which had defined marriage as between one man and one woman, to be in violation of the Equal Protection Clause of the Fifth Amendment to the United States Constitution. The effect of this decision is to give to same-sex married couples the same rights as opposite-sex married couples. Since there are more than 1,000 Federal laws and regulations that exclude same-sex partners from the definitions of “marriage” and “spouse,” sweeping changes will have to be made across a broad array of laws and regulations.

At the present time, Illinois permits civil unions but does not permit same-sex marriage. Therefore, the Court’s ruling is not likely to directly impact parties who have entered into an Illinois civil union. However, it is anticipated that the Illinois legislature will vote on a same-sex marriage bill later this year. **We will provide an update as soon as greater clarity is provided by the Illinois legislature or the courts.**

### **IV. Planning Considerations - How permanent is permanent?**

The Taxpayer Relief Act does not contain a “sunset” provision as did other recent gift and estate tax laws. This means that the laws will not automatically expire at a set date. For this reason, many people have assumed, perhaps erroneously, that the gift and estate tax laws (and the current \$5,250,000 Applicable Exclusion Amount) can never be reduced.

Little more than four months after signing the Taxpayer Relief Act into law, the President proposed the following gift and estate tax law changes in his 2014 budget proposal:

1. Return estate, gift and GST Tax rates and exemptions to 2009 levels. This would increase the top tax rate to 45%, reduce both the Estate Tax Exclusion Amount and GST Tax Exclusion Amounts to \$3,500,000, and reduce the Lifetime Gift Tax Exclusion Amount to \$1,000,000;

September, 2013

Page 4

2. Outlaw a widely-used and extremely effective estate planning technique called the “Grantor Retained Annuity Trust,” or “GRAT,” which currently allows significant amounts of appreciation to escape gift and estate taxes;
3. Limit the duration of the GST Tax Exclusion Amount (meaning that trusts that pass assets to grandchildren may be subject to additional tax); and
4. Tax the benefits currently available from the creation of certain favorable estate and gift tax trusts called “irrevocable grantor trusts.”

In the past, the Obama Administration has also advocated eliminating the ability to discount the value of transferred assets in the arena of estate and gift taxation. “Discounting” has provided significant tax benefits over the years.

Because the permanence of the gift and estate tax laws and the Applicable Exclusion Amounts are far from certain, and because the laws have been in a constant state of flux over the past decade, **only a proper estate plan can protect from unpredictable changes in the law and ensure that assets are not unnecessarily taxed at death.**

#### V. Non-Tax Reasons to Review and Revise Estate Plans.

Planning to avoid taxes is only one reason why an up-to-date estate plan is essential. Aside from the many tangential benefits an estate plan offers, such as avoiding probate court proceedings and simplifying the administration process in the event of disability, *an up-to-date estate plan provides important peace of mind. As the sole expression of final wishes, an estate plan determines who will make decisions in the event of incapacity, who will care for children, and who will receive life’s possessions and material wealth after death.*

An out-of-date estate plan can unintentionally lead to disorder, frustration among beneficiaries, and increased administration costs, not to mention potential litigation and family disputes. Many people often forget how many years have passed since they last had an estate planning attorney review their documents. Simply having an estate plan is not enough: ***an estate plan must reflect current wishes and the current law.***

As a rule of thumb, all individuals should have an attorney review their estate planning documents every three to five years. As one’s personal and financial circumstances change, and as the law evolves, so too must an estate plan.

The following are just a few of the many situations that would necessitate a review of one’s estate planning documents:

1. ***Significant changes in financial situation.***
2. ***Significant changes in family situation.***

September, 2013

Page 5

3. *Significant personal or business event occurrences.*
4. *A desire to change all or a portion of the estate plan.*
5. *Moving to another state or owning property in another state.*
6. *Major changes in the law.*

\*

\*

\*

**We continue to urge our clients to follow the fundamental estate planning principles that have always guided our practice:**

- **Plan based upon current laws, assuming the worst while hoping for the best;**
- **Allow for the greatest possible flexibility to address future changes in the tax laws as well as in financial and family circumstances; and**
- **Review estate planning documents regularly to assure that 1) they accurately reflect present goals and wishes, and 2) title to assets such as beneficiary designations for insurance policies and retirement plans are correct and current.**

**As always, if you have any questions, or if we can be of any assistance, please do not hesitate to call our office.**

**Kindest personal regards,**

***Rothman Law Group***

**Rothman Law Group** is a Chicago-based law firm specializing in estate planning, business planning and trust and estate administration. We combine the most sophisticated planning techniques with the ability to find practical solutions to individual problems. Our legal expertise coupled with strong relationship skills enables us to effectuate our clients' goals while providing tax and other cost-saving strategies.

To comply with certain U.S. Treasury regulations, we advise you that any discussion of Federal tax issues in this communication is not intended or written to be used, and cannot be used by you, (i) to avoid any penalties imposed under the Internal Revenue Code or (ii) to promote, market or recommend to another party any transaction or matter addressed herein.