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Dear Clients and Friends,

We are excited to announce
that our office has moved to the landmark Monadnock Building!

As of September 21, 2023, our new address is:

Rothman Law Group
53 West Jackson Boulevard
Suite 1201
Chicago, Illinois 60604

In addition to advising you of our change of address, we are writing to discuss (i) the status of Federal and Illinois gift and estate taxes, (ii) the proper implementation of estate planning documents, including ownership of investment assets by revocable trusts, and updates to retirement account beneficiary designations and (iii) the importance of regular review of estate planning documents.

I. Federal and Illinois Gift and Estate Tax Updates.

Under current laws, each individual has available a Federal applicable exclusion amount which can be applied (i) during the individual's lifetime, to exempt from gift tax liability property transfers of up to $12,920,000 (indexed for inflation) and (ii) upon the individual's death, to exempt from Federal estate tax liability property transfers also up to $12,920,000, indexed for inflation and reduced by any portion of the $12,920,000 gift tax exclusion amount applied to lifetime taxable gifts. It is anticipated that on January 1, 2024, this Federal applicable exclusion amount will increase to $13,610,000, and the gift tax annual exclusion amount per donor/donee will increase to $18,000 from $17,000.

Under current laws, however, unless Congress takes additional action, on January 1, 2026, the Federal applicable exclusion amount will be reduced by one-half of the otherwise then applicable inflation adjusted amount for both lifetime transfers and transfers at death. The gift tax annual exclusion amount will not be impacted.

For married couples, a 'portability election' can be made on the estate tax return of the first spouse to die. If a portability election is made, any Federal applicable exclusion amount that remains unused as of the death of the first spouse will be added to the Federal applicable exclusion amount available for use by the surviving spouse.

Separately, however, Illinois imposes its own estate tax on the estates of Illinois residents and on Illinois real estate and tangible personal property owned by estates of non-residents of Illinois. The amount of transfers upon death which may be exempted from Illinois estate tax is limited to $4,000,000. This amount is not indexed for inflation. Illinois does not impose a gift tax and does not offer a portability election following the death of the first spouse.

The amount of Illinois estate tax is determined using a complicated calculation based on a 2001 Federal tax law that is no longer in force. While the marginal rates provided in the 2001 law range from 0.80% to 16%, the actual tax calculation is complex and can result in effective tax rates well over 16% for amounts in excess of $4,000,000. For example, an Illinois taxable estate of $4,100,000 results in an Illinois estate tax of $28,571, an effective tax rate of nearly 29% of the amount above of the Illinois exemption amount.

Many clients with residences in both Illinois and another state which does not have an estate tax are electing to change their legal domicile to the state with preferential tax laws. Please contact a Rothman Law Group attorney if you would like to discuss this possibility.

II. Implementation of Estate Planning.

Current estate planning documents are only one part of an effective estate plan. The full benefits of an estate plan cannot be achieved without the recommended ownership of investment assets and beneficiary designations of retirement benefits, life insurance policies and annuity contracts.

A. Ownership of Investment Assets by Revocable Trusts.

There are several benefits to transferring ownership of investments (other than retirement accounts) to revocable trusts. These benefits include (i) providing for an efficient transfer of responsibility for the management of financial matters to the acting co-trustee or the designated successor trustee of the revocable trust in the event of incapacity, (ii) avoiding the additional costs and delays from the need for probate at death, (iii) maintaining privacy with respect to the value of the decedent's assets or the decedent's beneficiaries, and (iv) for married couples, reducing or avoiding estate taxes and capital gain taxes by optimally dividing assets between both spouses' revocable trusts.

For example, if the combined net worth of a married couple is $6,000,000 and all assets are owned jointly with rights of survivorship, instead of being divided between their revocable trusts, the jointly owned investments will all pass to the survivor without any estate tax. However, when the surviving spouse subsequently dies, the survivor's taxable estate will presumably also be $6,000,000. Because the survivor's Illinois estate tax exemption is only $4,000,000, an Illinois estate tax of $456,071 will be owed by the surviving spouse's estate. **The tax in this example could be completely avoided with proper documents and titling of assets.**

In addition, continuing the example above, if the cost basis of the investment assets with a value of $6,000,000 is only $4,000,000 at the death of the first spouse, the assets will all receive a one-half adjustment in cost basis to their date of death values for capital gain purposes. That is, the 'stepped up' cost basis with respect to all the assets would be only $5,000,000. If the surviving spouse sells some of the inherited assets after the first death, there will be a capital gain tax on the difference between the sale price of each asset and the partially adjusted cost basis of each asset. On the other hand, if one-half of the assets were titled to the revocable trust of the deceased spouse, the assets owned by the revocable trust of the deceased spouse would receive a 100% 'step-up' in cost basis and could potentially be sold and reinvested in other assets by the surviving spouse ***without any capital gain tax***.

B. Updating Retirement Account Beneficiary Designations.

Proper beneficiary designations are crucial for tax deferred retirement accounts, such as IRA, Roth IRA, 401(k), 403(b) and similar accounts. Following the enactment of the SECURE Act in 2019, we updated our recommended planning for distributions from tax deferred retirement accounts for estate planning purposes to beneficiaries *other than surviving spouses*.

Our office continues to recommend that a surviving spouse be named the primary beneficiary of retirement accounts to preserve the ability of the surviving spouse to 'roll over' the benefits and pay out ('stretch') required minimum distributions from the retirement accounts over the surviving spouse's lifetime.

Prior to the SECURE Act, retirement benefits for beneficiaries, other than a surviving spouse, could be paid out ('stretched') over the beneficiary's entire life expectancy. Our prior recommendations, therefore, directed retirement benefits for non-spouses to be paid to separate trusts created under the decedent's revocable trust (generally called 'Descendant Trusts' or 'Beneficiary Trusts') which would be treated as 'conduit trusts'. In essence, any minimum required distributions made to a conduit trust are required to be immediately distributed to the beneficiary of the trust. The preservation of the ability to stretch the retirement distributions over the beneficiary's life expectancy was presumed to be more valuable than the creditor and estate tax benefits of keeping the distributions in the trust.

Since the enactment of the SECURE Act, however, the requirement that retirement accounts for beneficiaries, other than surviving spouses, must be fully distributed within 10 years changed our recommendation to treat separate trusts for each beneficiary as 'accumulation trusts', rather than 'conduit trusts'. With an accumulation trust, a more discrete decision can be made by the trustee of each beneficiary's trust whether (i) to retain part or all of each distribution in the trust to preserve the protection of the proceeds from potential claimants and to exclude the net proceeds from the beneficiary's taxable estate, or (ii) to pay out some or all of the distribution to the beneficiary in order to reduce the overall income taxes paid on the distribution.

The 'bottom line' is that for estate planning documents prepared by our office prior to 2020, if there are significant retirement accounts involved, we strongly recommend arranging for a review of the documents for updates to the retirement planning and other updated estate planning provisions.

III. **Importance of Regular Review of Estate Planning Documents.**

In addition to changes in our forms to address the SECURE Act, there have been other, less significant changes in state laws and in our preferred drafting provisions. For these and other reasons, it is worthwhile to regularly review estate planning documents and beneficiary designations.

We also generally recommend reviewing your current estate planning every ten years or so, or whenever there have been changes in financial or family circumstances.

Please contact a Rothman Law Group attorney if you have any questions or wish to arrange a review of your existing estate planning documents.

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It is our hope that this brief discussion has provided you with information that will help you make informed and proactive estate planning decisions. As always, we are available to assist with any of the matters discussed in this letter and welcome all inquiries.

Kindest personal regards,

Rothman Law Group

Rothman Law Group is a Chicago-based law firm with an emphasis 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.