

## The Tax Counselor

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### **Should You Consider a Change of Residency to Avoid State Taxes?**

Late in 2010, Congress increased the federal gift and estate tax exemptions to \$5 million per person. Although the federal estate tax exemption is now \$5,000,000, the Illinois estate tax exemption remains only \$2,000,000 per person. This means that an Illinois married couple with a combined estate of \$10 million could owe no federal estate tax, but \$704,316 in Illinois estate taxes, when the second spouse dies. In addition, Illinois has recently increased the Illinois personal income tax rate from 3% to 5% of gross income. To avoid these taxes, individuals who own or lease residences in more than one state may be considering changing their residency to a state other than Illinois.

Before making this decision, you should understand that changing your state residency can be fairly complicated. Each state makes its own determination of who qualifies as a state resident and looks at a number of factors to make this determination. Common factors that states consider include the amount of time actually spent in the state, home and/or business ownership in the state, state driver's licenses, state voter registration and state income tax filings. In addition, many state tax laws include rebuttable presumptions of residency based on a certain amount of time spent in the state. In Illinois, an individual is presumed to be a state resident if he or she spends more than nine (9) months here. If an individual is absent from Illinois for one (1) year, there is a presumption that the individual is no longer an Illinois resident. Of course, these presumptions may be overcome depending on your particular facts and circumstances.

Even a successful change of residence to a state other than Illinois may not completely eliminate Illinois income tax liability. Non-residents must still pay Illinois income taxes on Illinois source income, such as from businesses they own in Illinois or from salary from employment by an Illinois company. Of course, you will receive a credit for the Illinois tax payment in your state of residence. Similarly, if you own property in Illinois and move to a state with no estate or inheritance tax, you would still have some estate tax exposure at your death because Illinois (like most states with an estate tax) taxes real property located there.

A change of residence can also impact the amount of your real estate tax liability, as some states, such as Michigan, Florida and South Carolina, provide substantial real estate tax savings for residents.

It is also possible that, if you divide your time between two or more separate states, each state will treat you as a local resident. For example, Florida has no rebuttable presumption of state residency based on time spent in the state, so as long as you spend a significant amount of time there and have other badges of residence such as home ownership, driver's license, etc., you may be considered a resident there. However, a second state where you own property may also take this position, if you are spending significant time each year in the second state.

If you wish to consider a change of residency for yourself or for someone for whom you act as agent, you should consult with us before proceeding.

Illinois residents who are not going to change their residence to another state should consider having their estate plans reviewed to be sure that they properly account for the discrepancy between the federal and Illinois estate tax exemptions. Older plans of married couples may only take into account federal tax planning, which could result in some Illinois estate tax being owed at the death of the first spouse to die. With the increase in the federal exemption to \$5 million, other changes in your planning may be appropriate. We would be happy to discuss these issues with you.

### **Increases in Tax Exemptions**

The IRS recently announced an increase in the federal estate, gift and generation-skipping tax exemptions for 2012 based on an automatic inflation adjustment contained in the Internal Revenue Code. Those exemptions will increase by \$120,000 each, to \$5,120,000. However, the annual gift tax exclusion will remain at \$13,000. With interest rates at historic lows, asset values still down, and uncertainty as to what Congress will do with these exemptions, this remains an excellent time to utilize the gift and generation-skipping exemptions. We can work with you to help minimize the transfer taxes that will otherwise be owed by your estate.

### **Illinois Civil Union Law**

The new Illinois Religious Freedom Protection and Civil Union Act went into effect on June 1, 2011. It creates a new status that is analogous and equal to marriage under Illinois law for both same-sex and different-sex couples, each of whom are at least 18 years old. Couples who enter into a civil union will have all of the same benefits and protections, and be subject to the same responsibilities, as a married couple. The Act incorporates the provisions of the Illinois Marriage and Dissolution of Marriage Act for many purposes, including in the event of a dissolution of the civil union.

Persons in a civil union are entitled to the same rights as spouses wherever those rights are granted under Illinois law. So, for example, that should include the ability to (1) hold property as tenants-by-the-entirety, which can be useful for creditor protection, (2) elect spousal inheritance rights, (3) make medical decisions for each other when one of them is unable to do so for him or herself, absent a health care power of attorney to the contrary, and (4) file joint Illinois income tax returns. However, the civil union will have no impact on rights granted under federal law, such as the unlimited marital deduction for gift and estate tax purposes, ERISA or social security benefits, or the ability to file joint federal income tax returns.

This new law may impact not only the estate plans of parties in civil unions, but of others, such as parents, who may want to provide for or exclude a party in a civil union. There also may be status issues for couples who own residences in or move to a state that does not recognize civil unions. These and other issues should be considered as you update your estate plans.

### **Revisions to the Illinois Power of Attorney Acts**

On July 1, 2011, amendments to the Illinois Power of Attorney Act went into effect. Although these changes are mostly incremental, they serve as a reminder that you should review your powers of attorney periodically to be sure they continue to reflect accurately your wishes.

Powers of attorney technically do not expire because of lapse of time, but, as a practical matter, a medical or financial institution may have reservations about relying on a power that is many years old. Given that, and given the new change in the language of the statutory health care power of attorney form, it may be a good time to consider reviewing your existing powers to see if any changes are appropriate.

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