

## TAX & TRANSACTIONS BULLETIN

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- Effective January 1, 2010, the Federal Estate Tax and the Federal Generation Skipping Transfer Tax (“GST”) are repealed for one (1) year
- The Federal Gift Tax remains in effect during 2010
- The Federal Estate Tax and the Federal GST Tax are scheduled to be reinstated effective January 1, 2011
- Families should carefully review their Estate Plans, with particular emphasis on identifying the beneficiaries of the credit-shelter trust

### A QUICK UPDATE OF THE FEDERAL ESTATE TAX

Effective January 1, 2010, the Federal Estate Tax and the Federal Generation Skipping Transfer Tax (“GST”) are repealed for one (1) year. The Federal Gift Tax remains in effect during 2010. The Federal Estate Tax and the Federal GST Tax are scheduled to be reinstated effective January 1, 2011. It is possible that both Taxes will be made retroactively effective to January 1, 2010.<sup>1</sup> These changes to the Estate Tax may alter or affect a Family’s Estate Plan. Families should carefully review their Estate Plans, with particular attention on identifying the beneficiaries of the credit-shelter trust.<sup>2</sup> The Major Features of the transfer tax system are as follows:

- **Federal Estate Tax:** The federal estate tax is repealed for calendar year 2010. The federal estate tax is scheduled to resume on January 1, 2011, at a 55% maximum rate and a \$1 million exemption.<sup>3</sup>
- **Federal GST Tax:** The federal GST tax is repealed for calendar year 2010. The federal GST tax is scheduled to resume on January 1, 2011, at a 55% maximum rate and an inflation-adjusted exemption of approximately \$1 million.
- **Federal Gift Tax:** The federal gift tax remains in effect during calendar year 2010 at 35% rate and a \$1 million exemption. The annual exclusion of \$13,000 also remains in effect during calendar year 2010. On January 1, 2011, the federal gift tax maximum rate increases to 55% with a \$1 million exemption.<sup>4</sup>
- **Income Tax Basis of Assets:** The adjustment to basis of assets included in a decedent’s gross estate to fair market value (i.e. “Stepped Up Basis Rule”) is repealed effective January 1, 2010. During calendar year 2010, rather than receiving a basis equal to fair market value, inherited assets will take a carryover basis equal to the decedent’s basis. An Executor may increase the basis of a decedent’s assets by up to \$1.3 million. Further, the basis of assets transferred to a surviving spouse may be increased by an additional amount up to \$3 million. On January 1, 2011, the prior Stepped Up Basis Rule resumes so that assets included in a decedent’s gross estate will receive a fair market value basis.
- **State of Illinois Estate Tax:** Technically, the Illinois Estate Tax is also suspended effective January 1, 2010; and then reinstated effective January 1, 2011.



<sup>1</sup>Congress might retroactively reinstate the Federal Estate Tax and GST Tax to January 1, 2010, subject to a constitutional legal challenge.

<sup>2</sup>The credit-shelter trust is also known as the “Family Trust”.

<sup>3</sup>The tax rate will be 60% on Estates valued between approximately \$10 million and \$17 million.

<sup>4</sup>The tax rate will be 60% on Gifts valued between approximately \$10 million and \$17 million.

## ILLINOIS LEGISLATURE ENACTS NEW LAW PERMITTING MODIFICATION OF IRREVOCABLE TRUSTS

Effective January 1, 2010, the State of Illinois revised its Trusts Law. The new Law permits the Trustee and Beneficiaries to enter into a private agreement with respect to any matter involving a Trust. This private agreement – called a “Nonjudicial Settlement Agreement” – is binding and does not require court approval. Matters that may be resolved by a Nonjudicial Settlement Agreement include but are not limited to:<sup>5</sup>

- A. Interpretation or construction of the terms of the trust;
- B. Approval of a trustee’s report or accounting;
- C. Exercise or nonexercise of any power by a trustee;
- D. The grant to a trustee of any necessary or desirable administrative power;
- E. Questions relating to property or an interest in property held by the trust;
- F. Resignation or appointment of a trustee;
- G. Determination of a trustee’s compensation;
- H. Transfer of a trust’s principal place of administration;
- I. Liability or indemnification of a trustee for an action relating to the trust;
- J. Resolution of disputes or issues related to administration, investment, distribution or other matters;
- K. Modification of terms of the trust pertaining to administration of the trust;<sup>6</sup> and
- L. Termination of the trust, provided that court approval of such termination must be obtained.

Thus, the Trustee and Beneficiaries have a broad range of tools at their disposal to achieve Family goals. For instance, the Trustee and Beneficiaries may revise, alter or amend an Irrevocable Trust in order to accomplish a specific goal or objective. The parties could move the Trust’s situs to a different State to reduce State income taxes. The parties could appoint a successor trustee. Moreover, a minor, disabled, unborn, or missing beneficiary may be represented by and bound by an adult beneficiary having a substantially identical interest in the Trust.<sup>7</sup>

<sup>5</sup>See 760 ILCS 5/16.1(d) of the Illinois Trusts and Trustees Act.

<sup>6</sup>Subsection (K) permits modification of terms of the trust. The ability to modify the terms of the trust provides Families with broad latitude to accomplish their goals and objectives. **[Note:** The statutory phrase “administration of the trust” refers to and includes all of the trustee’s powers to manage the trust property and carry out the purposes of the trust, including (a) the power to make investments, (b) the power to make distributions of income or principal, (c) the power to delegate, and (d) the power to incur expenses. *See Restatement (Third) of Trusts, Sections 70 and 86; 760 ILCS 5/4.08; 760 ILCS 5/5.3(e); 205 ILCS 620/1-2; 205 ILCS 620/1-5.05; Campbell v. Albers, 313 Ill. App. 152, 39 NE2d 672 (page 7).]*

<sup>7</sup>760 ILCS 5/16.1.

***Example:*** Grandfather establishes a Trust for his four (4) Grandchildren, with Bank as Trustee. The eldest Grandchild is an adult; the remaining three (3) Grandchildren are minors. The Trust permits the distribution of a maximum of \$2,000 annually to each Grandchild. All four Grandchildren are either currently enrolled in college or plan to attend college within several years. None of the Grandchildren have sufficient funds to pay for college. Pursuant to 760 ILCS 5/16.1(d)(K), the Trustee and the adult Grandchild sign a Nonjudicial Settlement Agreement modifying the terms of the Trust to permit the Trustee to distribute annually to each Grandchild an amount sufficient to pay for his or her college education. The Bank, as Trustee, now has proper authorization to fully pay for each Grandchild's college education. (Note that the adult Grandchild may properly represent the minor Grandchildren and sign the Agreement on those minors' behalf).<sup>8</sup>

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<sup>8</sup>See 760 ILCS 5/16.1(d)(2) regarding the ability of a "representative" to enter into a binding Nonjudicial Settlement Agreement.

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