



# THE ILLINOIS ESTATE TAX & LIFETIME GIFTS

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# Reducing IL Estate Taxes Through Gifts

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- Current Gifting Environment

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- Calculation of the Illinois Estate Tax

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- Gifts = IL Estate Tax Savings

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- Quantifying the Loss of Stepped-up Basis

# The Current Estate Tax Environment

- **The 2010 Tax Act (Federal)**

- EGTRRA \$1M “Sunset” Postponed to 12/31/2012
- \$5M Estate & Gift Tax Exclusion (Surprise!!!)

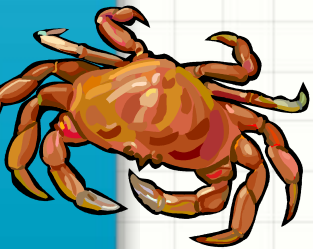
- **PA 97-0636 (Illinois) Permanent Provision**

- \$3.5M Exclusion (2012); \$4M for 2013 & thereafter

- **The Gifting “Clawback” Controversy**

- If \$1M Exclusion in 2013, are prior Gifts (for example \$4M) added back to Donor’s Estate at Death?
- Possible estate tax upon 1<sup>st</sup> to die for married couple

- **Uncertain Laws = Planning Challenges**



# Combined Federal & IL Estate Taxes

Tentative Taxable Estate	2012 <b>Federal Credit = \$5.12M</b>		2013 - NO SUNSET <b>Federal Credit = \$5.24M (estimated)</b>		2013 - SUNSET <b>Federal Credit = \$1M</b>
	IL Rates over <u>\$3.5M</u>	Fed & IL Rates over <u>\$5.12M</u>	IL Rates over <u>\$4M</u>	Fed & IL Rates over <u>\$5.24M</u>	Fed & IL Rates over <u>\$1M</u>
\$2,000,000	N/A		N/A		43.5%
\$3,000,000	N/A		N/A		47.25%
\$4,000,000	25.93%		N/A		49.83%
\$5,000,000	23.48%		25.93%		54.04%
\$5,120,000	22.48%		25.93%		54.41%
\$5,240,000	21.63%		25.93%		54.76%
\$6,000,000		68.69%		74.01%	56%
\$7,000,000		54.56%		55.89%	56.66%
\$8,000,000		50.36%		51.03%	57.16%
\$9,000,000		48.42%		48.85%	57.57%
\$10,000,000		47.35%		47.66%	57.91%
\$20,000,000		45.04%		45.12%	61.52%

# QUIZ: Which Year (2011-2013) Triggers the LOWEST Illinois Estate Taxes for a \$6M Estate???

	2011	2012	2013
IL TENTATIVE TAXABLE ESTATE	\$6,000,000	\$6,000,000	\$6,000,000
IL ESTATE TAX EXCLUSION	<u>(\$2,000,000)</u>	<u>(\$3,500,000)</u>	<u>(\$4,000,000)</u>
“Excess”	\$4M	\$2.5M	\$2M

IL ESTATE TAX	<b>\$456,071</b>	<b>\$456,071</b>	<b>\$456,071</b>
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# IL Estate Taxes - A Complicated Calculation

- Based on Repealed State Death Tax Credit (Code Section 2011)



- The Lesser of:
  - Code Section “**2011 Table**”
  - The “**Hypothetical Federal Estate Tax**”
    - calculated with a 35% top rate & a \$3.5M Exclusion in 2012
- Circular Computations



# IL Estate Tax Exclusion Amount Maxims



- \$3.5M for 2012; \$4M thereafter...
- For the Majority of Estates over the IL Estate Tax Exclusions
  - The 2011 Table produces the Lowest Tax and is the “default” calculation
  - This makes the IL Exclusion Amounts (\$3.5M & \$4M) **Meaningless!!!**
- The IL Estate Tax Exclusions only Benefit
  - Estates below IL Exclusion Amounts
  - Estates marginally above IL Exclusion Amounts

# IL Attorney General Estate Tax Calculator

<http://illinoisattorneygeneral.gov>

- **Input Screen Calculator:**

- IL Tentative Taxable Estate (“ITTE”)
- “ITTE” + Adjusted Taxable Gifts

- IL Estate Tax is LESSER OF:

- “Code Section 2011(b) Table” – **Excludes Gifts**
- “Hypothetical Estate Tax” – **Counts Gifts**



*Beware: Calculator may not show alternate calculation if it is not relevant (i.e., in 2011, no Hypo Tax calculations for Estates over \$2.5M)*



# The “AHA” Moment



***The 2011 Table’s Exclusion  
Of Taxable Gifts from its  
Estate Tax Base Encourages  
Lifetime Gifts to Reduce  
Illinois Estate Taxes...***

# Appendix B – Example #4; \$6M Taxable Estate

## IL Estate Tax Saving related to Gifting

Tentative Taxable Estate (2012)	Gifts	Computations		Lowest Amount	IL Estate Tax Savings Related to Gifts	Net Savings <small>(reduced 35% for Federal estate tax benefit, if any)</small>
		2011 Table	Hypo Estate Tax			
\$6,000,000	\$0	\$456,071	\$648,148	\$456,071	N/A	N/A
\$5,500,000	\$500,000	\$402,518	\$648,148	\$402,518	\$53,553	\$34,809
\$5,000,000	\$1,000,000	\$352,158	\$648,148	\$352,158	\$103,913	\$67,543
\$4,500,000	\$1,500,000	\$301,799	\$648,148	\$301,799	\$154,272	\$100,277
\$4,000,000	\$2,000,000	\$253,986	\$648,148	\$253,986	\$202,085	\$131,355
\$3,500,000	\$2,500,000	\$209,124	\$648,148	\$209,124	\$246,947	\$160,516
\$3,000,000	\$3,000,000	\$167,279	\$648,148	\$167,279	\$288,792	\$187,715
\$2,500,000	\$3,500,000	\$128,518	\$648,148	\$128,518	\$327,553	\$212,909
\$2,000,000	\$4,000,000	\$92,910	\$648,148	\$92,910	\$363,161	\$236,055
\$1,500,000	\$4,500,000	\$60,526	\$648,148	\$60,526	\$395,545	\$257,104
\$1,000,000	\$5,000,000	\$31,439	\$648,148	\$31,439	\$424,632	\$276,011
\$500,000	\$5,500,000	\$9,690	\$648,148	\$9,690	\$446,381	\$290,148
\$0	\$6,000,000	\$0	\$648,148	\$0	\$456,071	\$296,446

# The “Trip Wire Effect” of Adjusted Taxable Gifts

- The IL Calculation ADDS:

- Tentative Taxable Estate
- Adjusted Taxable Gifts



- An IL Estate Tax is Triggered:

- If SUM Exceeds \$2M (2011)
- If SUM Exceeds \$3.5M (2012)
- If SUM Exceeds \$4M (2013 & thereafter)

- “Adjusted taxable gifts may cause the Illinois estate tax to apply as the “trip wire” is crossed, yet the calculation of such tax often is based on the 2011 Table which excludes such gifts from its tax base and does not take into account the Illinois estate tax exclusion amounts.”

## Appendix B – Example #1; \$4M Taxable Estate

### *Beware of Gifts Marginally above the IL Exclusion Amounts*

Tentative Taxable Estate (2012)	Gifts	Computations		Lowest Amount	IL Estate Tax Savings Related to Gifts	Net Savings (reduced 35% for Federal estate tax benefit, if any)
		2011 Table	Hypo Estate Tax			
\$4,000,000	\$0	\$253,986	\$129,630**	\$129,630	N/A	N/A
\$3,500,000	\$500,000	\$209,124	\$129,630**	\$129,630	\$0	N/A
\$3,000,000	\$1,000,000	\$167,279	\$129,630**	\$129,630	\$0	N/A
\$2,500,000	\$1,500,000	\$128,518	\$129,630	\$128,518	\$1,112	N/A
\$2,000,000	\$2,000,000	\$92,910	\$129,630	\$92,910	\$36,720	N/A
\$1,500,000	\$2,500,000	\$60,526	\$129,630	\$60,526	\$69,104	N/A
\$1,000,000	\$3,000,000	\$31,439	\$129,630	\$31,439	\$98,191	N/A
\$500,000	\$3,500,000	\$9,690	\$129,630	\$9,690	\$119,940	N/A
\$0	\$4,000,000	\$0	\$129,630	\$0	\$129,630	N/A

- **\*\*The Hypothetical Estate Tax is lower than the 2011 Table Amount**
- **No IL Estate Tax Savings of Gifting until Gifts Exceed about \$1.5M**

# #3 Gifts = IL Estate Tax Savings (2012)

Example #1

Tentative Taxable Estate	Gifts	Total	IL Estate Taxes	IL Estate Tax Savings*	2011 Table
\$5M	\$0	\$5M	\$352,158	N/A	YES
\$0	\$5M	\$5M	\$0	\$352,158	YES
\$500,000	\$4.5M	\$5M	\$9,690	\$342,468	YES
\$1.5M	\$3.5	\$5M	\$60,526	\$291,632	YES

\*Presumes no Federal Deduction (Form 706) of IL Estate Taxes

# Gifts = IL Estate Tax Savings (2012)

Example #2

Tentative Taxable Estate	Gifts	Total	IL Estate Taxes	Estate Tax Savings*	2011 Table
\$6M	\$0	\$6M	\$456,071	N/A	YES
\$0	\$6M	\$6M	\$0	\$296,446	YES
\$1.5M	\$4.5M	\$6M	\$60,526	\$257,104	YES
\$2.5M	\$3.5M	\$5M	\$128,518	\$212,909	YES

\*IL Estate Tax Saving decreased 35% for benefit of Federal Deduction (Form 706) of IL Estate Taxes



# Gifts = IL Estate Tax Savings (2012)

Example #3

Tentative Taxable Estate	Gifts	Total	IL Estate Taxes	Estate Tax Savings	2011 Table	Hypo Tax*
\$4M	<b>\$0</b>	\$4M	\$129,630	N/A	NO	YES
\$3.5M	<b>\$500k</b>	\$4M	\$129,630	N/A	NO	YES
\$3M	<b>\$1M</b>	\$4M	\$129,630	N/A	NO	YES

\*The Hypothetical Estate Tax Amount is the correct measure of Illinois Estate Taxes, as it is lower than the 2011 Table Amount

# #4 Quantifying the Loss of Stepped-up Basis

- Best to Gift High Basis Assets
- Gift of Appreciated Assets

Are

**Estate Tax Savings**

Greater than

**Income Tax Costs**

(No Stepped-up Basis)

???

- Case by Case Analysis
  - **Future Appreciation?** (Wildcard)
  - Amount of Built in Gain?
  - Ordinary Income or Capital Gains Property?
  - Whether Asset will be Sold?

# LIQUIDATION ANALYSIS

## Transfer Tax Savings Versus Income Tax Costs of Gifting

	<u>No Gift</u>	<u>Cash Gift</u>	<u>Sale by Donee of Gifted Property (\$700,000 Basis)</u>
<b>Gift Before Death</b>	N/A	\$1,000,000	\$1,000,000
<b>Combined Federal &amp; IL Taxes- (20%)</b>	N/A	N/A	(\$60,000)
<b>Tentative Taxable Estate</b>	\$6,000,000	\$5,000,000	\$5,000,000
<b>Illinois Estate Tax</b>	(\$456,071)	(\$352,158)	(\$352,158)
<b>Federal Estate Tax</b>	<u>(\$148,375)</u>	<u>(\$184,745)</u>	<u>(\$184,745)</u>
<b>Net Value to Family</b>	\$5,395,554	\$5,463,097	\$5,403,097
<b>Total Tax Savings (Costs) (compared to “No Gift” scenario)</b>		<b>\$67,543</b> =====	<b>\$7,543</b> =====

### “Break-Even” Point Analysis

- \$67,543 divided by 20% Income Tax Rate = \$337,715
- Equates to \$662,285 Basis (\$1M less \$337,715)
- Minimum Basis of Gifted Property Needed to “Break Even” under Liquidation Analysis

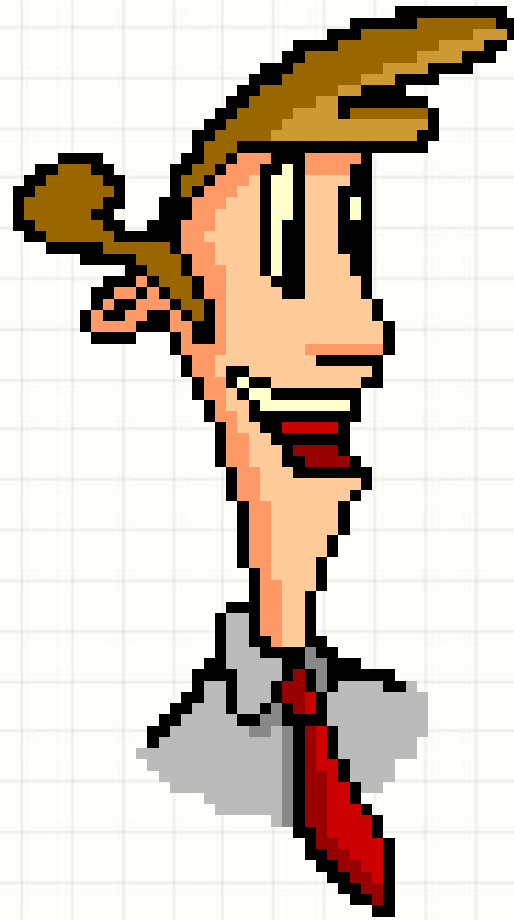
# APPRECIATION “WILD CARD”

How much Post-Gift Appreciation is Needed to Create Positive Transfer Tax Savings?

	<u>No Gift</u>	<u>Gift of Property with \$300,000 “Carryover Basis</u>
<b>Gift Before Death</b>	N/A	\$1,000,000**
<b>Combined Federal &amp; Illinois Income Taxes- (20% x \$700,000)</b>	N/A	(\$140,000)
<b>Tentative Taxable Estate</b>	\$6,000,000	\$5,000,000
<b>Illinois Estate Tax</b>	(\$456,071)	(\$352,158)
<b>Federal Estate Tax</b>	<u>(\$148,375)</u>	<u>(\$184,745)</u>
<b>Combined Value to Family</b>	\$5,395,554	\$5,323,097
<b>Total Tax Savings (Costs) (compared to “No Gift” scenario)</b>		<b>(\$72,457)</b> =====

\*\*\$330,000 of Post-Gift Growth Needed to Reach “Break-Even” Point

# THE END



Questions?