



Estate Planning & Probate Law Section MCLE Meeting

Location: Attorney Resource Center

Date: June 26, 2019

11:45 AM – Noon

Welcome/Introductions

Michael-Anne Peck, Chair

Case Law Update by Kaitlyn Anne Wild

Noon – 1:00 PM

Program

Common Tax Issues Fiduciaries Need to Know for Estate and Trust Administration

Eric R. Wilen of Brooks, Tarulis & Tibble, LLC.

Speaker's Bio

Eric Wilen is a trusts and estates attorney with over 20 years of experience representing business owners and high net worth families in the areas of estate planning, business succession planning, wealth transfer planning and asset protection planning. Eric Wilen's Fiduciary Practice provides advice and counsel to both corporate and individual fiduciaries in a wide range of issues relating to the administration of estates and trusts whether it is representing an executor or guardian in court proceedings, preparing estate and inheritance tax returns, preparing fiduciary income tax returns, allocating assets to marital QTIP trusts, credit-shelter or family trusts, descendants spendthrift trusts and other successor trusts while preserving generation-skipping tax elections for each trust, resolving disputes among family members and other beneficiaries concerning undue influence and fiduciary actions, or advising on accountings and planning for the final settlement and distribution to beneficiaries.

Eric obtained his bachelor's degree in Finance from the Michigan State University, Eli Broad College of Business, in 1991. After completing his undergraduate studies, Eric attended the Detroit College of Law (which is now known as Michigan State University College of Law) receiving his Juris Doctorate, *cum laude*, in 1994. Eric pursued graduate legal studies at the New York University School of Law receiving an LL.M. in



Taxation in 1995. Eric is licensed to practice in the State of Illinois and the State of Michigan.

Eric is an of counsel with the Naperville Law Firm of Brooks, Tarulis & Tibble, LLC and has been in private practice since 1996 having practiced at law firms in Chicago and the surrounding suburbs. Eric is member of the DuPage County Estate Planning Council serving on the board of directors since 2017. Eric is member of the Illinois State Bar Association, the DuPage County Bar Association and supports the Fox Valley Chapter of the Illinois CPA Society. Eric writes articles and does presentations on topics relating to business, tax and estate planning

Presentation Summary

There are multitude of tax issues in the administration of estates and trusts. Eric will help estate planning attorneys and probate practitioners identify tax issues and learn how to counsel their fiduciary clients regarding these issues. The attendees will learn about what tax filings are most often required in estate and trust administration and how to assist the fiduciary's accountants and tax preparers by providing the information required to generate these filings.

Next Meeting:

Fall 2019

DCBA Events:

July 11th – Ask a Lawyer Help Desk. DuPage Judicial Center, Room 2017. 1:00 p.m. – 4:30 p.m.

July 25th – Ask a Lawyer Help Desk. DuPage Judicial Center, Room 2017. 1:00 p.m. – 4:30 p.m.

Aug. 8th – Ask a Lawyer Help Desk. DuPage Judicial Center, Room 2017. 1:00 p.m. – 4:30 p.m.

Aug. 22nd – Golf Outing, Cantigny Golf Course, Wheaton



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The *DCBA Brief* is looking for substantive law articles over the summer for the September and October issues (and beyond). Due dates to make those issues are July 1 and August 1 respectively. Get a head start on your section's article quota this summer. Ask your speakers, current, past and future to go the extra mile with their topic and turn their speaking notes into an article! Authors may earn up to one half their total required MCLE credits for each reporting period from a single article submitted and published. Check dcbabrief.org for the current Writer's Guidelines and Author Agreement. For questions or to submit an article, contact incoming Editor-in-Chief, Chris Maurer at maurer@aandalaw.com

***North Carolina Dep’t of Revenue v. The Kimberley Rice Kaestner 1992 Family Trust*, 588 U.S. ____ (slip op.) (argued Apr. 16, 2019; decided Jun. 21, 2019).**

In this case, a unanimous United States Supreme Court addressed “the limits of a State’s power to tax a trust.” The respondent, the Kimberley Rice Kaestner 1992 Family Trust (the plaintiff before the state courts), had raised an as-applied Constitutional challenge to a North Carolina income-tax statute, N. C. Gen. Stat. § 105–160.2, by suing the petitioner, the North Carolina Department of Revenue (the defendant in the state courts), which had assessed a tax on the respondent under that statute. All levels of the North Carolina court system ruled in favor of the respondent’s challenge, finding that the petitioner’s assessment of an income tax, under the specific facts of the case, violated the Due Process Clause of the Constitution’s Fourteenth Amendment.

The Supreme Court affirmed, finding that, under the specific facts of the case, the tax imposed under N. C. Gen. Stat. § 105–160.2 failed the first step of the Court’s two-step analysis, applied “to decide if a state tax abides by the Due Process Clause,” articulated in *Quill Corp. v. North Dakota*, 504 U. S. 298, 312 (1992), overruled on other grounds, *South Dakota v. Way-fair, Inc.*, 585 U. S. ____, ____ (2018) (slip op. at 10). The Syllabus of the Court’s decision is as follows:

Syllabus

Joseph Lee Rice III formed a trust for the benefit of his children in his home State of New York and appointed a fellow New York resident as the trustee. The trust agreement granted the trustee “absolute discretion” to distribute the trust’s assets to the beneficiaries. In 1997, Rice’s daughter, Kimberley Rice Kaestner, moved to North Carolina. The trustee later divided Rice’s initial trust into three separate subtrusts, and North Carolina sought to tax the Kimberley Rice Kaestner 1992 Family Trust (Trust)—formed for the benefit of Kaestner and her three children—under a law authorizing the State to tax any trust income that “is for the benefit of” a state resident, N. C. Gen. Stat. Ann. § 105–160.2. The State assessed a tax of more than \$1.3 million for tax years 2005 through 2008. During that period, Kaestner had no right to, and did not receive, any distributions. Nor did the Trust have a physical presence, make any direct investments, or hold any real property in the State. The trustee paid the tax under protest and then sued the taxing authority in state court, arguing that the tax as applied to the Trust violates the Fourteenth Amendment’s Due Process Clause. The state courts agreed, holding that the Kaestners’ in-state residence was too tenuous a link between the State and the Trust to support the tax.

Held: The presence of in-state beneficiaries alone does not empower a State to tax trust income that has not been distributed to the beneficiaries where the beneficiaries have no right to demand that income and are uncertain to receive it. Pp. 5–16.

(a) The Due Process Clause limits States to imposing only taxes that “bea[r] fiscal relation to protection, opportunities and benefits given by the state.”

Wisconsin v. J. C. Penney Co., 311 U.S. 435, 444. Compliance with the Clause’s demands “requires some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax,” and that “the ‘income attributed to the State for tax purposes ... be rationally related to ‘values connected with the taxing State,’ ” *Quill Corp. v. North Dakota*, 504 U.S. 298, 306. That “minimum connection” inquiry is “flexible” and focuses on the reasonableness of the government’s action. *Id.*, at 307. Pp. 5–6.

(b) In the trust beneficiary context, the Court’s due process analysis of state trust taxes focuses on the extent of the in-state beneficiary’s right to control, possess, enjoy, or receive trust assets. Cases such as *Safe Deposit & Trust Co. of Baltimore v. Virginia*, 280 U.S. 83; *Brooke v. Norfolk*, 277 U.S. 27; and *Maguire v. Trefry*, 253 U.S. 12, reflect a common principle: When a State seeks to base its tax on the in-state residence of a trust beneficiary, the Due Process Clause demands a pragmatic inquiry into what exactly the beneficiary controls or possesses and how that interest relates to the object of the State’s tax. *Safe Deposit*, 280 U.S. at 91. Similar analysis also appears in the context of taxes premised on the in-state residency of settlors and trustees. See, e.g., *Curry v. McCannless*, 307 U.S. 357. Pp. 6–10.

(c) Applying these principles here, the residence of the Trust beneficiaries in North Carolina alone does not supply the minimum connection necessary to sustain the State’s tax. First, the beneficiaries did not receive any income from the Trust during the years in question. Second, they had no right to demand Trust income or otherwise control, possess, or enjoy the Trust assets in the tax years at issue. Third, they also could not count on necessarily receiving any specific amount of income from the Trust in the future. Pp. 10–13.

(d) The State’s counterarguments are unconvincing. First the State argues that “a trust and its constituents” are always “inextricably intertwined,” and thus, because trustee residence supports state taxation, so too must beneficiary residence. The State emphasizes that beneficiaries are essential to a trust and have an equitable interest in its assets. Although a beneficiary is central to the trust relationship, the wide variation in beneficiaries’ interests counsels against adopting such a categorical rule. Second, the State argues that ruling in favor of the Trust will undermine numerous state taxation regimes. But only a small handful of States rely on beneficiary residency as a sole basis for trust taxation, and an even smaller number rely on the residency of beneficiaries regardless of whether the beneficiary is certain to receive trust assets. Finally, the State urges that adopting the Trust’s position will lead to opportunistic gaming of state tax systems. There is no certainty, however, that such behavior will regularly come to pass, and in any event, mere speculation about negative consequences cannot conjure the “minimum connection” missing between the State and the object of its tax. Pp. 13–16.

371 N. C. 133, 814 S. E. 2d 43, affirmed.

SOTOMAYOR, J., delivered the opinion for a unanimous Court. ALITO, J., filed a concurring opinion, in which ROBERTS, C. J., and GORSUCH, J., joined.

In its opinion, the Court makes clear that its holding is limited “to the specific facts presented” and “do[es] not imply approval or disapproval of trust taxes that are premised on the residence of beneficiaries whose relationship to trust assets differs from that of the beneficiaries here.” For example, the Court expressly “do[es] not decide what degree of possession, control, or enjoyment [of trust assets] would be sufficient to support taxation.” Further, the Court purposefully “do[es] not address whether a beneficiary’s ability to assign a potential interest in income from a trust would afford that beneficiary sufficient control or possession over, or enjoyment of, the [trust] property to justify taxation based solely on his or her in-state residence.” Justice Alito, in his concurring opinion, explains:

“I join the opinion of the Court because it properly concludes that North Carolina’s tenuous connection to the income earned by the trust is insufficient to permit the State to tax the trust’s income. Because this connection is unusually tenuous, the opinion of the Court is circumscribed. I write separately to make clear that the opinion of the Court merely applies our existing precedent and that its decision not to answer questions not presented by the facts of this case does not open for reconsideration any points resolved by our prior decisions.”

For reference, the citations to the underlying state-court opinions in this matter are as follows:

- Trial court opinion: *Kimberley Rice Kaestner 1992 Family Tr. v. N.C. Dep’t of Revenue*, 12 CVS 8740, 2015 WL 1880607 (N.C. Super. Apr. 23, 2015).
- Appellate court opinion: *Kimberley Rice Kaestner 1992 Family Tr. v. N.C. Dep’t of Revenue*, 789 S.E.2d 645 (N.C. Ct. App. 2016), *writ allowed*, 369 N.C. 189, 793 S.E.2d 683 (2016).
- State supreme court opinion: *Kimberley Rice Kaestner 1992 Family Tr. v. N.C. Dep’t of Revenue*, 814 S.E.2d 43 (N.C. 2018), *cert. granted sub nom. N.C. Dep’t of Revenue v. Kimberly Rice Kaestner 1992 Family Tr.*, 139 S. Ct. 915, 202 L. Ed. 2d 641 (2019).



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Common Tax Issues Fiduciaries Need to Know for Estate & Trust Administration

Presentation by: Eric R. Wilen, Esq.

DuPage County Bar Association / Estate Planning & Probate Section

June 26, 2019

What We Are Going to Cover Today. What Do I Hope You Will Learn From Me.

Best Practices - Developing Your Best Practices to Counsel Fiduciaries
Acquire A Feel or Touch for Handling Tax Issues

Title 26 of United States Code - Tax Law is "Law"
Tax - Go and Speak with Your Accountant About That
How To Work With CPAs and Accountants

Income Taxes - Decedents, Estates and Trusts
Filing Requirements and Exemptions

Federal Estate Taxes and Illinois Estate Taxes
Filing Requirements and Exemptions

Why Income Tax Basis for Assets is Important



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Client Meeting - March 29, 2019:

Male Decedent died of a Heart Attack. Decedent was going to be retiring as a Corporate Executive in the next year or two. Decedent was divorced and had 2 children. Son is Age 35 and Daughter is Age 33. The person you are meeting with in your office is the Decedent's sister. Your client? The Decedent never got around to doing a will.

Sold his house and was renting a Condo. No real estate.

Vanguard IRA - \$850,000 - Beneficiary Ex-Wife

Vanguard Roth IRA - \$250,000 - Beneficiary Son 50% and Daughter 50%

Company 401(k) Account - \$1,250,000 - Beneficiary Ex-Wife

Company Deferred Compensation - \$450,000 - Beneficiary Son 50% and Daughter 50%

MetLife Insurance Policy - \$25,000 Death Benefit - Beneficiary Son 100%

TD Ameritrade Brokerage Account - \$850,000 - TOD Daughter 50%, Son 25%, Sister 25%

Checking Account - \$95,000 - Joint Account with Sister

Savings Account - \$8,500 - No Joint Tenant and No TOD Beneficiary

Sister paid for the funeral and wants to be reimbursed

Question: Do you recommend initiating probate proceedings?



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What Are the Tax Issues? Part 1

Decedent did his own income taxes using Turbo Tax.

Decedent's Date of Death: March 17, 2019

Decedent Had Not Filed 2018 Income Tax Returns - Balance Due?

Who will prepare the 2018 Income Tax Returns?

Who will sign the 2018 Income Tax Returns?

Who will pay the balance due for 2018?

Where are the 2017 Income Tax Returns?

Did we get all of the 2018 tax reporting documents?

Were there Quarterly Estimated Tax Payments?

Transcript - Wage and Income Transcript? IRS Practitioner Priority Service

(866) 860-4259 - Power of Attorney - IRS Form 2848

Do we file for extension (IRS Form 4868) and make a tax payment? How much?



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What Are The Tax Issues? Part 2

Tax Penalties - 5% per month / 4.5% Failure to File / 0.5% Failure to Pay

Will we need to file a tax return for 2019?

Do you need a federal employer identification number for the estate?

Will we need to file a income tax return for the estate?

You advise the sister that no probate proceedings are necessary because all that is required is a Small Estate Affidavit. You quickly prepare an Illinois Small Estate Affidavit and send the Sister to the Bank to close the Savings Account.

Sister calls several weeks later says she had all the mail forwarded the received the following:

State Farm Insurance Check - \$302.25 (Estate of Decedent)

Comcast Check - \$124.19 (Estate of Decedent)

DuPage Medical Group - \$11.43 (Estate of Decedent)

Vanguard Check - \$40,000.00 (Decedent)



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What to do with the checks received? Tax Issues?

Can sister set up a bank account for the Estate of Decedent? What is needed?

Taxable Distribution from the Vanguard IRA? Income 2019?

Are probate proceedings required now?

Who can sign the 2018 (and 2019) individual income tax returns for the Decedent? Sister? Son? Daughter? Ex-Wife? The Personal Representative appointed should sign the tax return. A Personal Representative to the IRS is an Executor named in a Last Will and Testament, even if there is no probate proceedings, an Estate Administrator appointed by the court, usually without a valid will or the person in charge of the decedent's property. Who is in charge of Decedent's property? Sister?

Sister collects 2018 tax reporting documents and goes to see the accountant. Accountant looks at the 2017 tax return and the 2018 tax reporting documents and prepares the 2018 tax return which reflects a balance due. Sister signs the 2018 tax return and sends check for the balance due plus an additional amount for penalties. What happens if Sister overpays and there is refund due?



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How to get a refund for a deceased taxpayer?

Must file IRS Form 1310 (Statement of Person Claiming Refund Due a Deceased Taxpayer).

Did the decedent leave a will? No

Has a court appointed a personal representative for the estate of the decedent? No

As the person claiming the refund for the decedent's estate, will you pay out the refund according to the laws of the state where the decedent was a legal resident? Yes

Who is responsible to pay the Decedent's income taxes? Sister? Son? Daughter? Ex-Wife? Attorney? Look at Transferee Liability. A transferee includes an heir, legatee, devisee and distributee of an estate of a deceased person. Attorney?

Will there be an income return filing requirement for the Estate of Decedent? Depends. Individual Returns are done on Form 1040. Fiduciary Returns are done on Form 1041. The exemption amount for an Estate is \$600.

Where to report the \$40,000 distribution from the Decedent's Vanguard IRA? Follow the Form 1099-R reporting.

Are the fees paid to the attorney deductible? File Fiduciary income tax return attorney fees part of the Excess Deductions. Still deductible not subject to 2% of AGI (TCJA 2017)



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Is the Decedent's Estate Required to file a Federal and/or Illinois Estate Tax Return?

Federal Estate Tax Exemption for 2019 - \$11,400,000

Illinois Estate Tax Exemption for 2019 - \$4,000,000

Do you ask Sister if Decedent ever filed any gift tax returns?

Best Practices - Do a Gross Estate Analysis.

Vanguard IRA	\$ 850,000
Vanguard Roth IRA	250,000
Company 401(k) Account	1,250,000
Company Deferred Compensation Plan	450,000
MetLife Insurance Policy	25,000
TD Ameritrade Brokerage Account	850,000
Checking Account	95,000
Savings Account	8,500
Personal Property	30,000
Checks	40,438
Total - Gross Estate	\$ 3,848,938

Question: Does the Decedent's Estate have to file an Illinois Estate Tax Return?



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More Information from the Sister.

Sister has been continuing to go through the Decedent's papers and finds that the Decedent also owned a condo in Florida with a value of \$400,000.

Does the Decedent have to file an Illinois Estate Tax Return? Florida Estate Tax Return or Florida Inheritance Tax Return?

Illinois Tentative Taxable Estate	\$ 4,248,938
Illinois Estate Tax	71,125
Gross Value of Illinois Situs Property	3,848,938
Gross Value of Wherever Located	4,248,938
Percent of Estate Illinois Tax Situs	91%
Illinois Estate Tax Due	64,724

Question: What else is the Sister going to tell you?



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Client Meeting - June 21, 2019:

Meeting with Daughter (Age 47). Mother just passed away at Age 79. Mother had a Last Will and Testament which poured over to Mother's Living Trust. Daughter has a brother, Son (Age 44), lives out of state. Father passed away in 2004. Father had a Last Will and Testament which poured over to Father's Living Trust. Daughter had Power of Attorney for Property and Health Care. Father's Last Will and Testament and Living Trust were dated in 1996. Daughter describes Mother's assets and properties:

Checking Account - \$25,000 - Joint with Daughter

Savings Account - \$10,000 - TOD to Daughter

Fidelity Brokerage Account - \$250,000 - Mother's Living Trust 100%

Naperville Home Estimated Value - \$600,000 - Father's Living Trust 100%

Southern Illinois Vacant Lot Estimated Value - \$125,000 - Father's Living Trust 100%

MetLife Insurance Policy - \$10,000 - Beneficiary Daughter

Fidelity Brokerage Account Stocks - \$500,000 - Father's Living Trust 100%

Question: Are you considering probate proceedings?



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What are the Tax Issues? Part 1

Father's Living Trust has Successor Trustees being Mother First, Daughter Second and Son Third. Father's Living Trust has an FEIN and files tax returns annually. Upon Mother's death, trust estate one-half to Daughter and one-half to Son.

Mother's Last Will and Testament and Living Trust Amended in 2008. Executors and Successor Trustees are Daughter First, Son Second. Mother's Living Trust leaves trust estate one-half to Daughter and one-half to Son.

Question: Were tax returns filed for 2018?

Mother died May 22, 2019. 2018 tax returns for Father's Living Trust and Mother Personal were prepared by CPA and filed in April 2019.

You look at the fiduciary income tax return (IRS Form 1041) for Father's Living Trust and the box checked on Page 1 is for a "simple" trust. A Schedule K-1 Form 1041 is attached with Mother's name, address and social security number.

A "simple" trust is a trust which is required to distribute income to the beneficiary. A simple trust has a \$300 exemption amount.

A "complex" trust is a trust which is not required to distribute income to the beneficiary. A complex trust has a \$100 exemption amount.



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What are the Tax Issues? Part 2

Father's Living Trust provides for marital deduction and credit shelter planning. There is language for administering the Marital Share in a Marital Trust and federal unified credit equivalent amount passing as the Residuary Share in a Family Trust. The Family Trust provides that the surviving spouse can receive distributions of income and principal as necessary for the surviving spouse's health, education, maintenance and support (HEMS Standard).

What was the federal estate tax exemption in 2004?

The federal unified credit equivalent in 2004 was \$1,500,000.

Which trust was being administered at the time of Mother's death? Marital Trust? Family Trust?

The fiduciary income tax returns would suggest that the trust is being administered pursuant to the terms of the Marital Trust, but trust instrument itself would suggest that the trust is being administered pursuant to the terms of the Family Trust.

Question: Why is important whether the Marital Trust or Family Trust is being administered?

Daughter explains that her plans are to sell the Naperville home, the lot in Southern Illinois and begin selling the stocks in the Fidelity Account. Will there be any taxes?



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How to determine income tax basis?

Internal Revenue Code Section 1014. The basis of any real or personal property acquired from a decedent is generally its fair market value on the date of the decedent's death or on the alternate valuation date. If there is no federal estate liability, the basis of the property is its fair market value as of the date of the decedent's death.

Father died on November 22, 2004.

What date is used to determine the income tax basis for the Naperville Home? The Lot in Southern Illinois? The Stocks in the Fidelity Account?

Mother's Date of Death? Father's Date of Death?

Why Mother's Date of Death?

Why Father's Date of Death?

On November 22, 2004, the assets in Father's Trust had the following values:

Naperville Home - \$300,000

Southern Illinois Lot - \$50,000

Fidelity Stocks - \$100,000



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Whether to Make the Deceased Spousal Unused Exemption (DSUE) Election?

This is often referred to Estate Tax Portability. On the death of the first spouse, the surviving spouse can file an federal estate tax return and make the Deceased Spousal Unused Applicable Exclusion Amount Election. If first spouse dies with a \$1,000,000 estate, make the election and the surviving spouse will now have a their own \$11,400,000 Applicable Exclusion Amount plus \$10,400,000 from the deceased spouse (\$11,400,000 - \$1,000,000) for a total Estate Tax Applicable Exclusion Amount of \$21,400,000.

When to you advise a spouse to make the DSUE Election?

How should this effect attorneys preparing estate plans?

I will stick around and answer questions.



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Questions?



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Practice Areas:

- Estate Planning
- Estate and Trust Administration
- Taxation
- Corporate



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