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Estate Planning | Wills & Trusts

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Estate Planning for Same-Sex Couples

On June 1st of this year, the *Illinois Religious Freedom Protection and Civil Union Act* (the “Act”) went into effect and the State of Illinois began recognizing Civil Unions. As a result, members of Civil Unions should enjoy the same protections and benefits allowed to members of a “spousal relationship” under State law. However, as legislators continue to slowly evolve towards equality, it is important to examine how the State and Federal laws affect your Estate Planning.

There are several laws related to Estate Planning that are directly affected by the Act. Additionally, there are matters of Federal law which continue to restrict their benefits and protections to couples consisting of only a husband and wife.¹ Understanding these laws and planning around them can save a significant amount of time and cost when the time comes to use your Estate Planning documents.

Estate Tax

While Illinois now recognizes same-sex relationships and affords members of a Civil Union the same rights as members of a marriage, the Federal government continues to lag behind.

Under Federal law, one spouse is permitted to transfer an unlimited amount of assets to the other at death without incurring any Estate Tax (the “unlimited marital deduction”). Utilizing this deduction through proper Estate Planning allows a married couple to defer any Estate Tax liability until the second death, allowing the surviving spouse to use or invest the assets during his or her life. On the other hand, if a couple is not recognized under Federal law, then the unlimited marital deduction is not available. The result is that assets exceeding the Federal exemption amount (\$5 million in 2011) that are transferred from one member of a Civil Union to the other are subject to Federal Estate Tax (maximum rate of 35% in 2011).

However, proper planning for a same-sex couple can prevent a double Estate Tax at the second death. One method for accomplishing this tax savings is by retaining assets in trust for the benefit of the survivor rather than giving the assets to the survivor outright, which would cause the assets to be included in the survivor’s taxable estate at his or her death.

While the \$5 million exemption may seem high, keep in mind that it includes life insurance proceeds, retirement accounts and real estate owned by the individual. Also, the exemption for Illinois Estate Tax is only \$2 million, which means that the assets exceeding \$2 million up to \$5 million will be taxed by the State. An additional concern is that due to the current state of the economy, the Federal government may decrease the Federal exemption in order to generate revenue. If Congress fails to act by the end of 2012, the Federal exemption will return to \$1 million with a top maximum rate of 55%.

In addition to the unlimited marital deduction, another Federal benefit that is only available to married couples is the “portability” of the Estate Tax exemption (discussed in detail in the January 2011 Newsletter).² Since portability, which can “bail out” a married couple that fails to plan in certain circumstances, is not available to same-sex couples, members of a Civil Union must maximize their Estate Tax exemptions through proper planning.

When planning for same-sex couples, it is crucial that your counselor recognizes the distinctions between planning for married couples and planning for Civil Union couples and advise you accordingly. If you have an existing Estate Plan, it is important to have those documents reviewed to ensure that they take advantage of the new State law and also take into account the inequalities of Federal Estate Tax laws.

Gift Tax

Similar to the unlimited marital deduction available at death, spouses are allowed to make unlimited gifts to each other during life under Federal Gift Tax law. For this reason, joint purchases between spouses during life, such as the family residence, are generally not a concern for transfer tax purposes. However, since this benefit is also available to married couples only, same-sex couples who make unequal contributions towards a joint purchase may incur Gift Tax if they fail to plan accordingly.

One way to avoid any such tax is to hold the property in proportion to the amounts contributed. Another option is to structure the imbalance as a loan, which may be forgiven using the annual Gift Tax exemption (\$13,000 in 2011).

By consulting an attorney prior to any such purchase, the Gift Tax landmines may be minimized or avoided altogether.

Property Passing Through Probate

Probate is the process by which the court distributes a decedent’s assets based upon (a) the provisions of a Will (testate) or, if the decedent did not have a valid Will at the time of his or her death (intestate), then (b) the laws of the state. Since probate

is a matter of state law, the Act gives the surviving member of a Civil Union the same rights to probate property as a surviving spouse. As discussed in the August 2010 Newsletter, if an individual dies without a valid Will, the surviving spouse is entitled to one-half of the decedent's assets if the decedent had any living descendants or all of the decedent's assets if the decedent did not have any living descendants.

Additionally, the surviving spouse is generally given preference to be named the administrator of the estate if the decedent died without a valid Will. Prior to the Act, the surviving member of a same-sex relationship would not have been granted such priority. As a result of the Act, the surviving member should be granted this preference. However, as is true with most new legislation, until we have case law to rely on, it is best to have a valid Will in place naming the Executor and successors of the creator's choice in order to circumvent any confusion when one of the members passes away.

Elective Share

Illinois protects a surviving spouse from being disinherited by the decedent by allowing the survivor to take an elective share. In other words, if a man dies and leaves everything to his children, his wife has recourse under Illinois law. In Illinois, the fraction to which the surviving spouse is entitled is one-half of the probate estate if the decedent left no surviving descendants and one-third of the probate estate if the decedent did leave surviving descendants.

As a result of the Act, the surviving member of a Civil Union will be afforded this same protection from disinheritance.

Powers of Attorney

When an individual is incapacitated and unable to make decisions for him or herself, a Power of Attorney (Health Care and/or Property) is required to make decisions on behalf of that individual. If the individual did not have a Power of Attorney, then a member of the individual's family must appeal to the court to be appointed Guardian of the individual. This can be a long and costly process and can often result in conflict between family members. Preference is generally given to the spouse or next closest relative to be named Guardian.

As a result of the Act, the courts should give preference to the surviving member of a Civil Union to serve as Guardian of the incapacitated member. However, as stated above, until we have reliable case law to show that the courts will acknowledge the Act in this situation, it is best to have Powers of Attorney in place in case they are ever needed. Even with the Act in place, because the cost and complexity of having a Guardian appointed by the courts is significantly greater than the cost and convenience of having Powers of Attorney prepared for you and your spouse or

partner, it is far more efficient to have these documents prepared while you are healthy and able to make decisions for yourself.

As evidenced by the analyses above, the Act has opened several doors for same-sex couples in terms of Estate Planning. However, until the Federal government recognizes same-sex couples and affords them the same rights and protections that are available to married couples, planning must be done carefully and with proper counseling from an experienced attorney.

1. *Defense of Marriage Act* (“DOMA”), enacted September 21, 1996, by President Bill Clinton, whereby the Federal government defines marriage as a legal union between one man and one woman.
 2. Under the *Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010* if the first spouse dies and does not use all of his or her Federal Estate Tax exemption, the remaining balance can be added to the surviving spouse’s exemption to be used at his or her death.
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Manish C. Bhatia is an Illinois attorney focusing his practice in the area of Estate Planning. Manish has focused his education and practice on Tax Planning, Estate Planning and Business Succession Planning since the first year of law school. He has also added Asset Protection, Elder Law and Nonprofit Organizations/Charitable Giving to his fields of practice. Manish is also a member of the Chicago Bar Association, the Asian American Bar Association of Chicago and the Indian American Bar Association.

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