TIPS FOR CHANGING RESIDENCY

- Declaration of domicile
- Acquire personal residence in new state
- Sell Illinois residence
- If Illinois residence not sold, do not claim homestead exemption for property tax
- New state driver's license
- New state voter registration and actual voting
- Register school age children for school in new state
- Move most valued possessions – including pets!
- Homestead application
- Use new state address on correspondence
- Bank account in new state
- Receive mail in new state – change post office address
- Move safe deposit box to new state
- Revise estate planning documents
- Register cars, bonds, airplane(s) in new state
- Join clubs/other membership organizations in new state and reduce or eliminate involvement in Illinois
- Subscribe to local newspapers
- Establish relationships with new state medical professionals
- Get a mobile phone number using the new state area code
- Use credit cards in new state
- File income tax returns in new state (if required) or other required returns
- Count days using mobile app
- Keep good records

CHANGING RESIDENCY FROM ILLINOIS FOR BUSINESS OWNERS, EXECUTIVES AND RETIREES

The Chicago Estate Planning Council

March 13, 2019

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AGENDA

I. **Income Taxation of Individuals**

II. Income Taxation of Trusts

III. Estate Taxation

IV. Procedural Matters

I. INCOME TAXATION OF INDIVIDUALS

Illinois income tax applies to the entire net income of an Illinois **resident**, regardless of whether the income was earned in Illinois.

I. INCOME TAXATION OF INDIVIDUALS

Illinois income tax applies only to the Illinois-source income of a **non-resident**.

I. INCOME TAXATION OF INDIVIDUALS

Statutory definition of residence:

A resident is defined as "an individual (i) who is in this State for other than a **temporary or transitory** purpose during the taxable year; or (ii) who is domiciled in this State but is absent from the State for a **temporary or transitory** purpose during the taxable year." 35 ILCS 5/1501(a)(20)(A).

A nonresident is "a person who is not a resident." 35 ILCS 5/1501(a)(14).

I. INCOME TAXATION OF INDIVIDUALS

What is a **temporary or transitory purpose**?

Fact-specific inquiry. 86 Ill. Admin. Code § 100.3020.

I. INCOME TAXATION OF INDIVIDUALS

Regulatory examples of a **temporary or transitory** purpose:

- Just passing through on way to another state
- Brief rest or vacation
- To accomplish a transaction or perform a short-term contract

I. INCOME TAXATION OF INDIVIDUALS

Regulatory examples of presence for "other than" a **temporary or transitory** purpose:

- In Illinois for health reasons and illness requires "long or indefinite" period to recuperate.
- Permanent or indefinite Illinois employment.
- Retiring from employment and moving to Illinois "with no definite intent of leaving shortly thereafter."

I. INCOME TAXATION OF INDIVIDUALS

A presumption of Illinois residence arises in two circumstances:

- Claiming a homestead exemption for Illinois property.
- An Illinois resident one year is presumed to be resident for next year if she/he spends more time in Illinois than any other state.

86 Ill. Admin. § 100.3020(f).

I. INCOME TAXATION OF INDIVIDUALS

Timing presumption: To avoid the presumption, an individual must spend more time in *one other state* than she/he spends in Illinois. Time spent in two other states cannot be added together to avoid this presumption.

I. INCOME TAXATION OF INDIVIDUALS

Residency Presumption Example:

Individual A relocates to Florida in Year 1.

In Year 2, A spends 5 months in Florida, 3 months in Michigan and 4 months in Illinois.

Is A presumptively an Illinois resident?

I. INCOME TAXATION OF INDIVIDUALS

Domicile

- Not defined by statute.
- "The place where an individual has his or her true, fixed, permanent home and principal establishment, the place to which he or she intends to return whenever absent." 86 Ill. Admin. Code § 100.3020(d).

I. INCOME TAXATION OF INDIVIDUALS

Domicile - A question of **intent**

- Locating elsewhere with **intention** of establishing the new location as your domicile.
- Abandoning any **intention** of returning to Illinois.

86 Ill. Admin. Code § 100.3020(d).

I. INCOME TAXATION OF INDIVIDUALS

An individual must physically leave Illinois to change domicile to another state.

I. INCOME TAXATION OF INDIVIDUALS

Persons **domiciled** in Illinois normally retain Illinois **residency** until they acquire **domicile** in another state.

Recently, questions of intent related to domicile have prevailed over bad residency facts.

I. INCOME TAXATION OF INDIVIDUALS

Recent taxpayer victory #1:

Cain v. Hamer, 2012 IL App (1^{st}) 11 2833

- Affirms summary judgment for taxpayers.
- Intent to change domicile to Florida controls despite fact that these taxpayers split time between Illinois and Florida after relocation.

See also Grede v. IDOR, 2013 IL App. (2d) 12073-§9; *Edmund Sweeney v. IDOR*, No. 2010 L 50524 (Cook County Cir. Ct., June 26, 2013); and *Corbin v. IDOR*, 14 TT 9 (2015)

I. INCOME TAXATION OF INDIVIDUALS

Recent taxpayer loss:

Dep't of Revenue v. John Doe, IT 14-03 (2/4/2014) (Department of Administrative Hearings)

- Taxpayer did not abandon residency while working overseas; work was temporary
- Illinois contracts maintained

I. INCOME TAXATION OF INDIVIDUALS

Proof of change in domicile/residency:

- Acquire personal residence in new state
- Sell Illinois residence
- If Illinois residence not sold, do not claim homestead exemption for property tax

I. INCOME TAXATION OF INDIVIDUALS

Supporting Facts:

- New state driver's license
- New state voter registration and actual voting
- Register school age children for school in new state
- Move most valued possessions – including pets!
- Homestead application
- Declaration of domicile

I. INCOME TAXATION OF INDIVIDUALS

Additional supporting facts:

- Use new state address on correspondence
- Bank account in new state
- Receive mail in new state – change post office address
- Move safe deposit box to new state
- Revise estate planning documents
- Register cars, bonds, airplane(s) in new state

I. INCOME TAXATION OF INDIVIDUALS

Additional supporting facts:

- Join clubs/other membership organizations in new state and reduce or eliminate involvement in Illinois
- Subscribe to local newspapers
- Establish relationships with new state medical professionals
- Get a mobile phone number using the new state area code
- Use credit cards in new state
- File income tax returns in new state (if required) or other required returns

I. INCOME TAXATION OF INDIVIDUALS

Location of charitable contributions may not be considered.

86 Ill. Admin. Code § 100.3020(g)(2).

I. INCOME TAXATION OF INDIVIDUALS

Other proof tips:

- Consider location apps to track days in state
- Document and retain records showing new state contacts

I. INCOME TAXATION OF INDIVIDUALS

Illinois-source income for individuals

- Income earned in Illinois is subject to Illinois income tax regardless of residency.
  - Example: Wages from a person or organization that transacts business in Illinois

    - An employee's services must be "localized" in Illinois

    - Services provided outside of Illinois are incidental

I. INCOME TAXATION OF INDIVIDUALS

Illinois-source income for individuals

- Wage Income
  - If no state in which services are localized; Illinois income when:
    - Base of operations is in Illinois
    - [If no base of operations] Place from which services are directed is located in Illinois

I. INCOME TAXATION OF INDIVIDUALS

Illinois-source income for individuals

- Capital gains from sale of partnerships interest
  - Business income (apportioned) v. non-business income (allocated)
  - IT 09-6033-GIL

I. INCOME TAXATION OF INDIVIDUALS

Illinois-source income for individuals

- Capital gains income cases of interest
  - *Corrigan v. Testa*, 149 Ohio St. 3a18 (2016); *but see T. Ryan Legg Irrevocable Trust v. Testa*, Slip Op. No. 2016-Ohio-8418 (Dec. 2016)
  - *Comm'r of Revenue v. Dupee*, 670 N.E.2d 173 (1996)

AGENDA

Fleeing Illinois: State Income and Estate Tax Overview for Individuals and Fiduciaries

I. Income Taxation of Individuals

II. Income Taxation of Trusts

III. Estate Taxation

IV. Procedural Matters

II. INCOME TAXATION OF TRUSTS

A. Illinois Statutory Provisions

- An Illinois resident trust must pay tax on its entire income, regardless of source.
- 35 ILCS 5/1501(a)(20): Purports to tax the income of any "resident" trust.
- "Resident" trust includes "[a] trust created by a will of a decedent who at his death was domiciled in this State" and "[a]n irrevocable trust, the grantor of which was domiciled in this State at the time such trust became irrevocable. For purpose of this subparagraph, a trust shall be considered irrevocable to the extent that the grantor is not treated as the owner thereof under Sections 671 through 678 of the Internal Revenue Code."

II. INCOME TAXATION OF TRUSTS

A. Illinois Statutory Provisions (cont'd)

- PLR IT97-0006-PLR (CCH Admin-Rul. Feb. 15, 12997): "…[T]he Department is obligated to follow the Illinois Income Tax Act."
- Result: Illinois tax rules require the permanent taxation of a "resident" trust's income in Illinois.
- However, must consider constitutional implications when the trust later has few or no connections to Illinois.

II. INCOME TAXATION OF TRUSTS

A. Illinois Statutory Provisions (cont'd)

- The following trusts are <u>not</u> resident trusts:
  - Trust created by nonresident designating an Illinois resident trustee, regardless of whether the trust is testamentary or inter vivos.
  - Irrevocable inter vivos trust created by an Illinois resident, provided that grantor trust status is terminated <u>after</u> the grantor becomes a nonresident of Illinois.
- If a grantor of such a trust is considering moving out of Illinois, consider terminating grantor trust status after moving out of Illinois. Likewise, if a grantor of an irrevocable grantor trust is considering moving to Illinois, consider terminating grantor trust status prior to becoming an Illinois resident.

II. INCOME TAXATION OF TRUSTS

B. *Linn v. Dep't of Revenue*, 2 N.E.3d 1203 (Ill. Ct. App. 2013)

- Illinois Fourth District Appellate Court ruled that the Due Process Clause limited Illinois' power to impose income taxes on an *inter vivos* trust, despite meeting the statutory definition of a resident trust.
- Trust established in 1961 by A.N. Pritzker, an Illinois resident.
- The trust initially was administered by Illinois trustees pursuant to Illinois law.
- In 2002, pursuant to powers vested in the trustee under the trust instrument, the trustee distributed the trust property to a new trust in Texas.
- Starting in 2006, no non-contingent trust beneficiary resided in Illinois, no trust officeholder resided in Illinois, all trust assets were outside Illinois, and Illinois law was not referenced in the trust instrument.

II. INCOME TAXATION OF TRUSTS

B. *Linn* (cont'd)

- The Department reclassified the trust as a resident trust, in accordance with the Illinois statute, and issued a notice of deficiency.
- Circuit court granted Department's motion for summary judgment, and trustee appealed, arguing that Illinois taxation was unconstitutional under Due Process Clause and Commerce Clause.
- Noting that the Texas trust had no Illinois beneficiaries, the Appellate Court found that a grantor's residency within a state at the time the trust is created is not itself a sufficient connection to satisfy due process in the context of an *inter vivos* trust.

II. INCOME TAXATION OF TRUSTS

C. Where does *Linn* Leave Illinois Testamentary Trusts?

- No Illinois cases since *Linn.*
- Illinois DOR strict construction may be challenged.
- Recent cases to watch and consider:
  - *South Dakota v. Wayfair, Inc.*, 138 S. Ct. 2080 (June 21, 2018)
  - *Kaestner 1992 Family Tr. v. N.C. Dep't of Revenue*, 814 S.E.2d 43 (N.C. 2018)
  - *Fielding v. Comm'r*, 916 N.W.2d 323 (Minn. 2018)

II. INCOME TAXATION OF TRUSTS

D. Other Recent Cases

- *Kaestner*
  - Kaestner trust was created in, and governed by the laws of, New York.
  - Trustee was a resident of Connecticut.
  - Trust assets were held by a custodian in Massachusetts.
  - Only connection with North Carolina was the residence of beneficiary.
  - NC court have held that such “minimal contacts” do not constitute “purposeful availment” for purposes of Due Process Clause.

II. INCOME TAXATION OF TRUSTS

D. Other Recent Cases (cont'd)

- *Kaestner*
  - Split between nine state supreme courts on relevant issue.
  - California, Missouri, Connecticut and Illinois: Critical link between a state and trust is residence of the beneficiary.
  - NC, NY, NJ, Michigan, and Minnesota: Mere residence of a trust beneficiary or a trust settlor within the state is not sufficient.
  - U.S. Supreme Court will hear the Kaestner case on April 16, 2019.

II. INCOME TAXATION OF TRUSTS

D. Other Recent Cases (cont'd)

- *Fielding*
  - Trusts were created by Minnesota domiciliary, and grantor was Minnesota domiciliary when the trusts became irrevocable
  - Trusts funded with shares of a Minnesota S-Corp.
  - Trusts had filed Minnesota state income tax returns prior to the tax year at issue.
  - End result in *Fielding* was same as in *Kaestner* – lack of sufficient contacts precluded state income taxation – a review of *Fielding* would have potentially far greater significance than a review of *Kaestner*.

II. INCOME TAXATION OF TRUSTS

D. Other Recent Cases (cont'd)

- *Fielding*
  - First, *Fielding* would be more likely to force the Supreme Court to analyze the types of trust contacts with a state do and do not constitute minimum contacts for purposes of Due Process Clause.
  - Second, the domicile of the grantor – the key issue in *Fielding* – is a far more common basis for taxing trusts than the residence of a trust beneficiary – the key issue in *Kaestner*.

AGENDA

Fleeing Illinois: State Income and Estate Tax Overview for Individuals and Fiduciaries

III. ESTATE TAXATION

A. Illinois Estate Tax Statute

- Illinois estate tax imposed on taxable transfers of property having a situs within Illinois
- 35 ILCS 405/3(a)
  - If decedent was an Illinois "resident" at death, all transferred property has an Illinois tax situs, other than real or tangible property located in another state.
  - If decedent was a nonresident, the transferred property having an Illinois tax situs only includes the real and personal property located in Illinois.

III. ESTATE TAXATION

B. The terms “resident” and “domicile”

- “Resident” is not defined in the Illinois estate tax statute, and the term “domicile” is not used in the Illinois estate tax statute.
- Illinois estate tax statute (35 ILCS 405/2) does not refer to Illinois Income Tax Act definitions.
- No Illinois cases appear to address the meaning of “resident” under the current Illinois estate tax statute.
- “Resident” has been used synonymously with “domicile” in other contexts.

III. ESTATE TAXATION

C. Different Tests for Income and Estate Tax

- Illinois estate tax statute does not define residence by cross reference to the Illinois Income Tax Act, but it does refer to the Illinois Income Tax Act to define resident trust and nonresident trust.
- Logical to conclude that “resident” for estate tax purposes means something different than “resident” for Illinois income tax purposes.

III. ESTATE TAXATION

C. Different Tests for Income and Estate Tax (cont'd)

- Further, the Illinois Income Tax Act defines a "resident estate" as the estate of a decedent who was "domiciled" at death in Illinois, <u>not</u> a decedent who was an Illinois resident at death.
- The Illinois Income Tax Act also defines a "resident trust" by referencing the "domicile" of the decedent or grantor, <u>not</u> by referencing the income tax residence of the decedent/grantor.
- These distinctions are consistent with conclusion that domicile is the relevant test for death-related events and fiduciary arrangements, including the Illinois Estate Tax.

III. ESTATE TAXATION

D. Change of Domicile for Estate Tax Purposes

a) Physical abandonment,

b) No intent to return,

c) Physical presence in new domicile, and

d) Intent to be domiciled in new domicile.

Cain v. Hamer, 975 N.E.2d 321 (Ill. App. 2012)

III. ESTATE TAXATION

D. Change of Domicile for Estate Tax Purposes (cont'd)

- Physical presence is simple to determine.
- Intent for the purposes of domicile is more complicated factual issue.
- Factors include:
  - Filed a declaration of domicile for a certain location
  - Location of permanent resident identification cards or driver's license
  - Voting records and jury summonses
  - Private club memberships
  - Credit cards
  - Charitable donations
  - Newspapers
  - Burial plots.

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IV. PROCEDURAL MATTERS

Initial Department Review

- IDOR Processing Unit Review
- Approach to filing returns
- Getting to the right form of denial
  - From Return Correction Notice to Notice of Denial
- Deadlines for appeals are statutory

IV. PROCEDURAL MATTERS

Options for Review of Adverse Department Determination

Illinois Protest Monies Act (30 ILCS 230/2a, 2a.1)

- Requires payment under protest.
- Guarantees right to constitutional review by trial court.
- Avoids state agency as fact finder.
- Funds placed in special fund, refunded with interest to prevailing taxpayers.

IV. PROCEDURAL MATTERS

Options for Review of Adverse Department Determination

Illinois Independent Tax Tribunal (35 ILCS 1010/1-1, et seq.)

- No "pay to play"
- Constitutional review limited to "as applied" challenge
- $15,000 jurisdictional threshold
- Appeals go directly to Illinois Appellate Court
  - Do not make assumptions based on title

IV. PROCEDURAL MATTERS

Options for Review of Adverse Department Determination

Illinois Administrative Hearing (86 Ill. Admin. Code § 200.101, et seq.)

- Disputes less than $15,000; property tax
- No constitutional review before Administrative Hearing officer
- Director of Revenue is decision maker in administrative hearing
- Appeals go to Circuit Court, then Appellate Court.
- Standard of review

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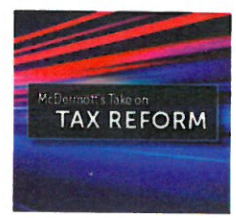

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QUESTIONS