

## **AVOIDING CONNECTICUT AND FEDERAL ESTATE TAXES THROUGH THE USE OF ESTATE TAX EXEMPTION TRUSTS**

by Neil R. Lubarsky, Esq.

Does your will leave everything to your spouse if your spouse survives you? When you and your spouse add together the value of all of the items included in your taxable estates, including your house, your investments, your pension plan or IRA balances, and the full amount of death benefits payable under your life insurance policies, does the total figure exceed \$2,000,000? If the answer to the two questions posed above is yes, you will be exposing your family to a substantial amount of unnecessary Connecticut estate taxes, and possibly also Federal estate taxes, which can be avoided by changing your will.

Let us look at the following example involving Mark and Linda, a married couple, who have wills leaving everything to the surviving spouse. Such wills are commonly known as "all to spouse" wills. Assume that Mark and Linda own a house worth \$2,000,000, and own investment assets worth \$2,000,000, giving them a taxable estate of \$4,000,000. If Mark, upon his death, left all of his assets to Linda, and Linda subsequently died, owning the couple's house and investment assets, leaving a taxable estate of \$4 million to her children, Linda's estate would have to pay approximately \$200,000 in unnecessary Connecticut Estate taxes.

The reason for Linda's substantial Connecticut estate tax exposure is that the Connecticut estate tax exemption, the amount which she can leave free of Connecticut estate tax to her children, is limited to \$2,000,000. Every dollar in excess of such \$2,000,000 amount which Linda leaves to her children is subject to Connecticut estate tax. Since Linda died with a taxable estate of \$4 million, the second \$2,000,000 left to her children is subject to Connecticut estate taxes in the amount of approximately \$200,000.

Had Mark and Linda properly planned their combined \$4,000,000 estate, the Connecticut estate taxes which they incurred could have been avoided. By changing their "all to spouse" wills, in one of the ways described below, and by dividing their assets equally between themselves, Mark and Linda could have avoided ever having to pay this \$200,000 of Connecticut estate taxes, thereby passing on an additional \$200,000 to their children.

One method of changing "all to spouse" wills in order to minimize estate taxes, is for Mark and Linda to each leave, upon death, their one-half share of the couple's assets, directly to their children.

This approach, however, is often undesirable from the perspective of the surviving spouse, who usually wants to continue to control all of the couple's assets, and who may need to receive the income generated by all of the couple's assets in order to live comfortably.

Fortunately, there is another method of changing "all to spouse" wills which meets the needs of the surviving spouse for control and income while at the same time minimizing the family's estate tax liability.

The solution involves the use of wills containing "estate tax exemption trusts". Under such a plan, assets of the first spouse to die are placed in a trust. During the life of the surviving spouse, the surviving spouse can control the investment of the trust assets. All of the income generated by the assets in the trust is ordinarily paid to the surviving spouse. If desired, the surviving spouse can be given the right to pull additional amounts of assets out of the trust. If a house is placed in such trust, the surviving spouse can be given the right to live in such house for the rest of his or her life without interference and without having to pay any rent.

When the surviving spouse ultimately passes away, all of the assets in the "estate tax exemption trust" pass directly to the couple's children or other beneficiaries without any estate tax being imposed on these assets. The use of wills containing "estate tax exemption trusts", as opposed to the use of "all to spouse" wills, often results in a family avoiding substantial amounts of estate taxes.

Recently enacted federal law has raised the federal estate tax exemption to \$5,250,000. Any household, the members of which have assets which, when added to the face amount of the household's life insurance policies, exceed \$5,250,000, must plan properly in order to avoid losing 50% of the excess in estate tax.

An additional benefit of having a will containing an "estate tax exemption trust" rather than an "all to spouse" will involves the protection that wills containing certain types of "estate tax exemption trusts" can provide, if specifically drafted for such purpose, against all of the couple's assets having to be spent down on long term care costs. Should Mark predecease Linda, leaving his assets to an "estate tax exemption trust" which was specifically structured with an eye towards protecting family assets against long term care costs, and should Linda later need nursing home care, the assets placed in such a specifically structured trust would not have to be spent on Linda's care in order for Linda to qualify for government assistance.

Moreover, using estate tax exemption trusts provides protection against family assets being

transferred outside of the original family unit to a deceptive health care aide or to a new spouse.

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