

IN Brief

SUMMER 2000

BASIC ESTATE PLANNING QUESTIONS AND ANSWERS

by Robert B. Levine

This article will address those questions most often asked of our estate planning attorneys by our clients.

1. What happens if I pass away and I don't have a will?

When a person dies without a will, or intestate, the Connecticut statutes determine how a person's estate will be distributed. If the decedent was married with children, the first \$100,000 goes to the spouse, and, of the balance, one-half goes to the spouse and one-half to their children. If married without children, the first \$100,000 goes to the spouse, and, of the balance, three-fourths goes to the spouse and one-fourth to decedent's living parents, if any.

2. Do any estate taxes have to be paid if my spouse and I leave our estates to each other and then to our children?

Spouses who provide for each other with a will can leave an unlimited amount of assets to each other without having to pay estate taxes, or, if all of a couple's assets are owned jointly, upon the death of the first to die, all assets pass automatically to the survivor without being subject to estate taxes. Upon the death of the survivor, however, the survivor's entire estate in excess of the exemption amount in effect (currently \$675,000, increasing gradually to \$1,000,000 in the year 2006) will be subject to estate taxes. Estate tax rates currently range from a minimum of 34 percent to a maximum of 55 percent.

3. How can my spouse and I shelter our assets from estate taxes and still ensure that we are both provided for?

The simplest way to ensure that a husband and wife fully maximize their ability to shelter their estates from estate taxes and still provide for each other is to use exemption trusts (also known as "A/B trusts," "credit shelter trusts," "family trusts") whereby husband and wife each leave assets worth the exemption amount then in effect to an exemption trust for the benefit of the survivor. The surviving spouse can be the trustee of that trust and can use the trust's assets for his or her health, education, maintenance and support. Upon the survivor's death, the assets previously set aside in an exemption trust will not be taxable, even if those assets appreciate. This structure will ensure that a husband and wife shelter at least twice the exemption amount.

4. Is it appropriate for my spouse and me to own all of our assets jointly?

If all of your assets are owned jointly, upon the death of the first of you to die, all assets pass automatically to the survivor without being subject to estate taxes. Upon the death of the survivor, if his or her estate exceeds the exemption amount, the excess will be subject to estate taxes at that time. If your combined estates exceed \$675,000, and exemption trusts are created in order to utilize both your and your spouse's exemptions, it will be more beneficial for each spouse to own assets in his or her individual name rather than jointly.

(continued on page 6)

If you would like to discuss any of the topics addressed in this issue of *In Brief*, please contact any of the attorneys listed below:

Robert B. Levine
(860) 676-3259
rlevine@ldlaw.com

Lillian B. Miller
(860) 676-3127
lmiller@ldlaw.com

Marvin H. Lapuk
(860) 676-3106
mlapuk@ldlaw.com

George A. Baker
(860) 676-3183
gbaker@ldlaw.com

Howard I. Gross
(860) 676-3102
hgross@ldlaw.com

OVERVIEW OF THE CONNECTICUT PROBATE COURT SYSTEM

by George A. Baker

During my tenure as Probate Judge, I discovered that a vast majority of people had little or no understanding of the probate court system. This article will give an overview of the probate court system and provide a brief summary of the estate administration process.

The Court System

There are approximately 130 individual probate courts located throughout the state. Most courts service individual towns, though several courts service two or more towns. Under the State Constitution, probate judges are the only judges in Connecticut that are elected. Probate judges serve four year terms and must reside within the probate district they serve. Contrary to popular belief, probate judges are not required to have law degrees; in fact, many probate judges have no legal background prior to serving as judges.

In Connecticut, probate courts have jurisdiction over the administration of decedent estates, trusts, conservatorships, guardians for mentally impaired, guardians for minors, parental rights matters (terminations, removals and adoptions), commitment proceedings, name changes, and marriages.

All probate courts are self-funded through the fees collected from the public. A flat fee of \$150.00 per application is usually charged for a non-decedent estate matter; the fee charged for decedent estates is a percentage of the gross taxable estate equal to \$150 for the first \$10,000, .35 percent between \$10,000 and \$500,000 and .25 percent for assets above \$500,000. For example, the fee for an estate having a gross taxable estate of \$500,000 would be \$1,865.00. Fees collected pay the court staff and other administrative expenses, with the balance going to pay the judge's salary.

Administration of a Decedent Estate

When a person dies, his or her estate must be administered in the probate court in the dis-

trict where he or she resided at the time of death. Only "probate assets" (those assets owned by the decedent in his or her individual name for which there is no other means of determining to whom the asset should be distributed) are subject to the probate process. Life insurance policies and retirement plans having beneficiary designations directing distribution upon death and jointly-owned property, for example, are non-probate assets. A bank account owned individually, on the other hand, can only be distributed upon death in accordance with the decedent's will or under the State's intestacy statutes. This is a probate asset.

There are three different types of estates depending on how assets are held at death. The three options are 1) tax purpose only estate; 2) informal estate; and 3) formal estate.

Tax purposes only estate

The tax purpose only estate is used when the entire estate consists of survivorship assets, assets passing directly to a named beneficiary, or assets held in trust. Under the tax purpose only process, even though no assets pass through probate, a Connecticut state succession tax return must still be filed with the local

IN Brief

is published by

Levy & Droney, P.C.

Pond View Corporate Center
74 Batterson Park Road
Farmington, CT 06032
(860) 676-3000 / Fax: (860) 676-3200

Articles in this newsletter are not intended as legal advice, which is dependent upon specific fact situations. Although we do not grant permission to republish these materials without prior consent, you may reproduce articles for personal educational purposes, provided that full credit is given to the authors and to Levy & Droney, P.C.

probate court listing all non-probate assets. It should be noted that the Connecticut succession tax is currently being phased out and will be eliminated completely by the year 2005.

In addition, depending on the size of the gross taxable estate, a federal estate tax return may also be required. Presently, if the gross taxable estate exceeds \$675,000, then the federal Form 706 estate tax return and the Connecticut Form 706 must be filed. The federal estate tax return filing threshold will be increased to \$1,000,000 by 2006.

Today, the *primary* reason to file the tax purpose only estate is to obtain a certificate of no tax for jointly owned real estate. Failure of the joint owner to obtain the certificate of no tax could later impact the ability to sell or mortgage the real estate since the State retains an inchoate lien for succession taxes until a release of the lien is obtained.

The Informal Estate

The informal estate process is used when a decedent owned personal property solely in his or her name and the value of the solely owned personal property is below \$20,000. For example, if a husband and wife owned their home and bank accounts jointly in survivorship, and the husband owned a vehicle having a value below \$20,000 in his name solely, then, at his death, an informal estate must be opened to probate the vehicle. The husband's Last Will and Testament, if he had one, is not formally admitted to probate.

The wife, instead, files an application in lieu of administration, files the will, and also files a request for the transfer of the vehicle with the probate court. She must also file the Connecticut succession tax return and federal estate tax return (if required). Thirty days after filing the Succession Tax Return, if the Department of Revenue Services does not object to the return, then the probate court can issue a Certificate of no tax and a decree to transfer the vehicle to the wife. This process is a simplified version of the formal estate process and can normally be completed with sixty to ninety

days of death. If a person owned real estate solely in his or her name, even if below \$20,000 in value, then the formal estate process must be used.

The Formal Estate

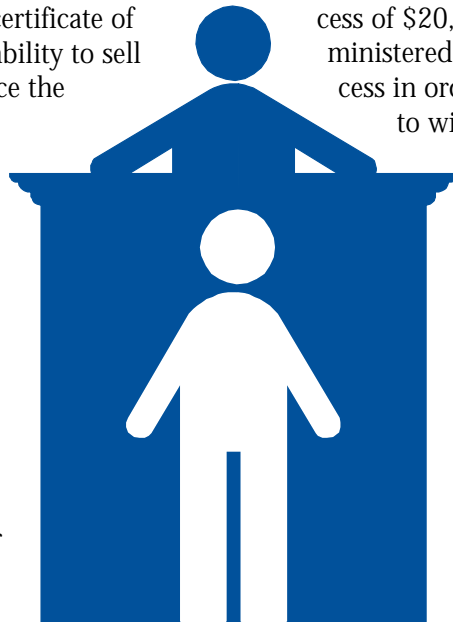
The formal estate administration process must be used if the decedent owned personal property solely in his or her name in excess of \$20,000 or solely owned any real property. For example, husband and wife own their home and bank accounts jointly in survivorship, but husband solely owns a mutual fund worth \$20,500. At the husband's death, because the mutual fund has a value in excess of \$20,000, his estate must be administered under the formal estate process in order to transfer the mutual fund to wife's name. (Remember, the jointly owned assets are not part of the formal estate process.)

The formal estate process begins by filing an Application to Admit the Last Will and Testament or for the intestate administration if he had no will. A hearing is held in the probate court to admit the will and appoint the executor of the estate. Today, a waiver process can be used to avoid a formal hearing if all heirs agree in

writing. Once the will is admitted, the executor is required to gather the solely owned assets and file an inventory of those assets. Normally, the inventory needs to be filed with the probate court within two months from the date of appointment of the executor. The executor also pays any outstanding bills, and files a Return of Claims which itemizes the claims filed and indicates whether the estate paid or denied a claim.

Within six months of the date of death, the executor must file the Connecticut succession tax return listing all taxable assets. The gross taxable estate generally includes solely owned assets, jointly owned assets, and assets that pass outside of probate to a named beneficiary. If any taxes are due, they should be paid within

(continued on page 5)



WHEN A PERSON DIES, HIS OR HER ESTATE MUST BE ADMINISTERED IN THE PROBATE COURT IN THE DISTRICT WHERE HE OR SHE RESIDED AT THE TIME OF DEATH. ONLY "PROBATE ASSETS" ARE SUBJECT TO THE PROBATE PROCESS.

CHARITABLE REMAINDER TRUSTS: NOT NECESSARILY FOR THE CHARITABLE MINDED

by Lillian B. Miller

The name "Charitable Remainder Trust" would seem to indicate a Trust intended to benefit a charitable organization. While it is true that a Charitable Remainder Trust ultimately benefits a charity, this type of trust can have even more economic benefits for a donor and the donor's family. If you have any asset (i.e., stock or real estate) that has substantially appreciated but does not produce enough income, a charitable remainder trust may provide a number of significant economic benefits.

How Does a Charitable Remainder Trust Work?

The owner of the appreciated asset, called the Donor, transfers the asset to a charitable remainder trust. The Donor chooses an amount of income he or she wishes to receive during the Donor's life or for a specific time period. The Donor can also choose to have the trust pay that amount to a surviving spouse or child for life or for a specific time period. (However, naming anyone other than the Donor and the

Donor's spouse could result in a gift tax or the need for filing a gift tax return). The amount paid can either be a fixed amount determined at the start of the trust, called an annuity amount, or a fluctuating amount based on a fixed percentage of the annual value of the asset, called a unitrust amount. The annuity amount guarantees an amount to the

Donor or other beneficiary, while the unitrust amount fluctuates yearly with the value of the asset to compensate for inflation. The amount chosen, however, must be one that, based upon the period of payment and current interest rates, would leave a remainder to the charity.

At the end of the life of the beneficiaries or the specified time period set out in the trust, the remainder of the trust is distributed to a charity as determined by the Donor.

How does the Charitable Remainder Trust Benefit the Donor and the Donor's Family?

When the Donor transfers assets to the Charitable Remainder Trust, the Trustee is able to sell the assets without paying any capital gains tax because the Trust is considered a charity. As a result, the Trust is able to reinvest the full proceeds into other assets which can produce more income. Regardless of the investment, the Trust is required to pay the Donor the specified income stream. Additionally, the Donor receives a charitable deduction against his current income for income tax purposes in the year that the asset is transferred to the Charitable Remainder Trust. The amount of the deduction is based upon the value of the asset, the interest rate at the time of the transfer, and the actuarially determined life expectancy of the Donor which determines the length of time before the charity receives anything from the trust.

Since the trust is required to pay a specified rate of return to the Donor regardless of the performance of the investment, the Donor may use some of the additional income distributed to him or her, that the Donor was not previously receiving, to purchase life insurance through an irrevocable life insurance trust to benefit the Donor's family. In doing so, the Donor will replace the original asset transferred to the Charitable Remainder Trust, which would have been taxable in the Donor's estate, with life insurance proceeds that will pass to his children without being subject to estate taxes.

An example of this is as follows:

Donor has \$500,000 of stock held for more than one year for which he originally paid \$100,000. The stock pays a dividend equal to one percent of the value of the stock (\$5,000). If Donor were to sell the stock, he would pay capital gains tax of 20 percent on the \$400,000 appreciation or \$80,000, leaving \$420,000 to be invested. If the Donor could then achieve a 10 percent annual dividend on his investment,

IF YOU HAVE ANY ASSET THAT HAS SUBSTANTIALLY APPRECIATED BUT DOES NOT PRODUCE ENOUGH INCOME, A CHARITABLE REMAINDER TRUST MAY PROVIDE A NUMBER OF SIGNIFICANT ECONOMIC BENEFITS.

Charitable Remainder Trusts (cont'd)

the Donor would receive \$42,000 per year from this asset. At the Donor's death, this asset is left to his wife, which she then leaves to their children. Depending on other assets in the estate, there could be as much as a 55 percent estate tax on the asset, leaving \$189,000 to the children.

If, instead, the Donor transferred the stock to a Charitable Remainder Trust, no capital gains tax would be payable on the sale of its investments, and there would be \$500,000 to invest. The Donor could choose to receive either a fixed amount (the annuity amount) or a percentage (the unitrust amount) which would be used annually to determine the distribution amount. For this example, the Donor chose an annuity amount of \$50,000 per year to be distributed to him and his wife or the survivor of them regardless of the **actual** performance of the investment. Remember, Donor was only receiving \$5,000 worth of annual dividend income prior to creating the Charitable Remainder Trust. Donor then sets up an irrevocable life insurance trust which will purchase a \$500,000 life insurance policy payable to his children on the death of the Donor and his

wife. The \$500,000 will not be taxable in his or his wife's estate because it is owned by an irrevocable life insurance trust. The Donor gives \$8,000 of his \$50,000 annual annuity amount to the insurance trust to pay premiums on the life insurance.

In summary, regardless of whether Donor is charitably inclined, he has received the following economic benefits in creating a Charitable Remainder Trust:

1. The Donor has replaced an asset worth \$500,000 and taxable in his estate (stock) with a non-estate taxable asset also worth \$500,000 (life insurance).

2. The Donor has converted an asset producing minimal income (one percent) into an asset producing much greater income (10 percent) without paying capital gains tax on the sale of stock.

3. The Donor received a current charitable deduction based on the value of the remainder interest to go to Charity.

Of course, the IRS is very clear as to how both the charitable remainder trust and the irrevocable life insurance trust must be structured. Any of our estate planning attorneys are available to discuss this estate planning strategy with you. **L&D**

Probate Court System (cont'd)

six months to avoid interest and penalties.

If the gross taxable estate exceeds \$675,000 (including life insurance proceeds), then the executor must file the federal estate tax return Form 706 and the state estate tax return Form CT706 within nine months from date of death. Any federal estate taxes owed should be paid within nine months to avoid interest and penalties. Upon review of the tax returns by the taxing authorities, an approval letter is received indicating acceptance of the tax returns.

At that time, the executor submits a final accounting listing the assets initially inventoried in the estate, all payments made from the estate, and proposed distribution to the beneficiaries. If a will was admitted, then the beneficiaries are those individuals, charities, or trusts set forth in the will. Absent a will, distribution is to the heirs according to the laws of intestate succession. Upon approval of the accounting by the probate court, the executor then distrib-

utes the remaining assets to the beneficiaries and files an affidavit of closing to complete the administration process. On average, the administration process can take between nine months and two years to complete.

In short, the probate court serves a vital role in the various matters discussed above. In particular, the probate courts serve as the vehicle by which assets are transferred from one individual to another upon death. In recent years the probate system has undergone a series of changes to streamline and simplify the administration process in order to make the system more user friendly. The phase out of the Connecticut Succession Tax will result in a decrease in revenue for the probate courts which could severely impact the viability of the present probate system in Connecticut. This could result in the further consolidation of probate courts or a complete restructuring of the probate court system. **L&D**

Levy & Droney Speaker's Bureau

If your organization would like an attorney to speak on a legal issue or topic, we would be pleased to offer the talents of an attorney of Levy & Droney. Topics are:

- Workplace Issues
- Family Issues
- Charitable Planning and Giving
- Estate Planning
- Automobile Liability
- Homeowner's Liability
- Condominium Issues
- First-Time Home Buyers

If interested, please contact Attorney Robert B. Levine at rlevine@ldlaw.com or (860) 676-3259.

Estate Planning Q&A (cont'd)

5. Should my spouse be the beneficiary of my retirement plan?

Whether or not a spouse should be the beneficiary on a retirement plan is dependent upon the size of the entire estate and the nature of the other assets that comprise the estate. Retirement assets must be given special attention since they are subject to both estate taxes **and** income taxes. Therefore, it is critical to make the proper beneficiary designation in order to maximize protection from estate taxes while maintaining the opportunity to defer the payment of income taxes that occurs when money is withdrawn from a retirement account.

6. I have a significant amount of life insurance. Are the insurance proceeds taxable in my estate?

Life insurance proceeds, similar to any other asset, are taxable. However, a simple planning technique, an Irrevocable Life Insurance Trust, enables a spouse to benefit from insurance proceeds during his or her life and ultimately transfer the proceeds to children and grandchildren without being subject to estate taxes. Alternatively, a second-to-die policy, which insures the lives of a husband and wife, can be owned by an Irrevocable Life Insurance Trust and the proceeds sheltered from estate taxes for the benefit of children and grandchildren. **L&D**

Please visit our web site at www.lldlaw.com to learn more about estate planning. Featured on our web site this month is an excerpt from a nationally recognized book entitled *The Trustee's Guide, a Handbook for Individual Trustees, Beneficiaries and Advisors*, co-authored by one of Levy & Droney's senior partners, Howard I. Gross.

FIRM HAPPENINGS

COLEMAN LEVY, a new owner of the New Britain Rock Cats minor league baseball team, was featured in an article in the May issue of the *Connecticut Lawyer Magazine*. Attorney Levy was also the featured speaker at the Connecticut Bar Association Sports & Entertainment Section meeting held March 2, 2000.

DANIEL KLEINMAN was elected to the Board of Directors of the Farmington Chamber of Commerce for a three-year term.

KENNETH LEVINE was co-chair of the Hartford County Bar Association's 2000 Law Day, which took place at the Hartford Superior Court on May 1, 2000. Attorney Levine presented the Liberty Bell Award to Evan Dobbelle, President of Trinity College.

MARVIN LAPUK was featured in the Spring 2000 issue of the *UConn Alumni Magazine* in an article called "The Measure of Character" by Jim H. Smith.

ROBIN MESSIER PEARSON spoke on Inland Wetland Regulation and the drafting of land use opinion letters at a May 3, 2000 seminar for practitioners organized by Connecticut Attorneys Title Insurance Com-

pany. She also spoke at the Connecticut Bar Association's Advanced Seminar on Planning and Zoning Issues held in North Haven on March 28, 2000. Her topic was the Connecticut Affordable Housing Appeals Act.

COLEMAN LEVY appeared on April 9, 2000 as the Narrator for the New Britain Symphony Orchestra, performing "A Place Where I Will Always Be Spring," by Fred Sturm.

DORIS E. DESAUTEL was admitted as a member of the Bar on May 18, 2000. Attorney Desautel is a member of Levy & Droney's litigation department and is admitted in Connecticut and Massachusetts.

JOHN ROSE, JR. will be a judge in the annual Kids Court competition at the State House on June 1, 2000. The competition features junior high and high school students who write essays on civil rights issues, then defend them before a panel of judges. It is a statewide competition sponsored by UTC and the State Commission on Human Rights and Opportunities. **L&D**