Office of Chief Counsel
Internal Revenue Service
memorandum

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subject: Connecticut Estate and Gift Tax Deduction under Section 2058

This memorandum responds to your request for assistance. This advice may not be used or cited as precedent.

Section 2058 of the Code allows a deduction for the amount of any estate, inheritance, legacy, or succession taxes actually paid to any State or the District of Columbia, in respect of any property included in the gross estate. You have posed several questions regarding whether the Connecticut estate tax base includes assets other than those included in the federal gross estate. The questions and the answers to them are as follows:

(1) **Are post-2004 Connecticut gifts included in the Connecticut estate tax base?** No, post-2004 Connecticut gifts are not included in the Connecticut estate tax base; rather, they are included in the computation of the Connecticut estate tax to insure that the Connecticut taxable estate is taxed at the highest applicable marginal rate.

(2) **In the case of Connecticut decedents dying after 2014, is the Connecticut gift tax paid on gifts made within three years of death included in the Connecticut estate tax base?** Yes, for deaths after 2014, the Connecticut estate tax base includes Connecticut gift taxes paid on gifts made within three years of death.

(3) **Should the deduction under I.R.C. § 2058(a) be reduced by the Connecticut estate tax attributable to the Connecticut gift taxes paid on gifts made**

within three years of death? Yes, the Connecticut gift tax paid on gifts made within three years of death is not includible in the federal gross estate. The deduction for the Connecticut estate tax must be reduced by the amount of the Connecticut estate tax attributable to the Connecticut gift tax paid on gifts made within three years of death.

Background

The Connecticut gift tax

Connecticut imposes a gift tax on transfers made after September 1, 1991, that are characterized as taxable gifts for federal gift tax purposes. Conn. Gen. Stat. Ann. §§ 12-640, 12-643(1) (West 2018). A progressive rate structure is applied to the value of all taxable gifts to compute the gift tax. CGSA § 12-642(a). There is no exclusion amount; rather the first bracket is taxed at zero percent. For 2018, that bracket exempts transfers up to $2.6 million. CGSA § 12-642(a)(6).

The Connecticut estate tax

Connecticut also imposes an estate tax on the transfer of decedent's estates. For decedents dying after 2014, the "Connecticut taxable estate" includes the sum of:

(1) the value of the federal gross estate less deductions, disregarding the deduction under section 2058 for state death taxes;
(2) Connecticut taxable gifts defined as taxable gifts made after 2004; see CGSA § 12-643(3); and
(3) Connecticut gift taxes paid on gifts made within three years of death.

CGSA § 12-391(c)(1)(C). For any given year, the same progressive rate structure applicable for gift tax purposes is applied to the Connecticut taxable estate to compute a tentative estate tax. CGSA § 12-391(g)(4). A credit is then allowed for gift taxes paid on post-2004 Connecticut taxable gifts. CGSA § 12-391(d)(1)(D). The difference (the tentative estate tax less the credit for the tax paid on the post-2004 Connecticut taxable gifts) is the Connecticut estate tax on the Connecticut taxable estate. There is no exclusion amount; rather the first bracket is taxed at zero percent. For deaths in 2018, the zero bracket excludes from Connecticut tax transfers up to $2.6 million. CGSA § 12-391(g)(4).

Analysis

Connecticut's estate tax regime works in a manner similar to the federal regime in that both apply a progressive rate schedule and both include inter vivos gifts in the computation. The only significant difference is that Connecticut relies on a zero bracket amount while the federal regime relies on a credit against an exclusion amount. Both have the effect of excluding from tax transfers of less than a specific minimum amount.

The federal estate tax regime works as follows:

Step 1. Compute a tentative tax (a tax unreduced by a credit amount) on the sum of the taxable estate and the adjusted taxable gifts, defined as all taxable gifts made after 1976 other than those included in the gross estate. IRC § 2001(b)(1).

Step 2. Compute a hypothetical gift tax (a gift tax reduced by the credit amounts allowable in the years of the gifts) on all post-1976 taxable gifts, whether or not included in the gross estate. IRC § 2001(b)(2). The credit amount for each year during which a gift was made is the tentative tax on the exclusion amount applicable for that year, computed using the tax rates in effect at the decedent's death. IRC § 2001(g)(2). This hypothetical gift tax is referred to as the gift tax payable.

Step 3. Subtract the gift tax payable determined in Step 2 from the tentative tax determined in Step 1 to arrive at the net tentative estate tax. IRC § 2001(b).

Step 4. Compute a credit equal to the tentative tax on the exclusion amount as in effect on the date of the decedent's death. IRC § 2010(a) and (c).

Step 5. Subtract the credit amount determined in Step 4 from the net tentative estate tax determined in Step 3. IRC § 2010(a).

The effect of Step 1 is to compute a tax on the combined taxable estate plus adjusted taxable gifts at the highest applicable bracket of the progressive rate schedule. This tax is then reduced by the tax on the adjusted taxable gifts that is computed at the lower tax rates (brackets) that were applicable to the gifts at the time the gifts were made. This has two effects. First, it removes the adjusted taxable gifts from the estate tax base. Second, it taxes the remaining assets (the taxable estate) at the higher marginal rates (brackets).

The Connecticut estate tax regime works as follows:

Step 1. Compute a tentative tax on the sum of the federal taxable estate plus post-2004 Connecticut taxable gifts plus, for post-2014 dates of death, Connecticut gift taxes paid on gifts made within three years of death. CGSA §§ 12-391(c)(1)(C) and (g)(4).

Step 2. Compute the gift taxes paid on Connecticut taxable gifts made after 2004. CGSA §§ 12-642(a) and 12-643(3);

Step 3. Subtract the gift tax paid in Step 2 from the tentative tax determined in Step 1 to arrive at the Connecticut estate tax. CGSA § 12-391(d)(1)(D).

Connecticut does not use Steps 4 and 5 because the credit they are designed to implement in the federal regime is built into the zero tax bracket of the Connecticut regime. For deaths in 2018, the zero bracket excludes from Connecticut tax transfers up to $2.6 million. CGSA § 12-391(g)(4).

As was the case in the federal computation, the effect of Step 1 of the Connecticut computation is to compute a tax on the combined taxable estate, post-2004 gifts and, in

the case of decedents dying after 2014, Connecticut gift tax paid on gifts made within three years of death, at the highest applicable bracket of the progressive Connecticut rate schedule. This tax is then reduced by the gift tax paid on the post-2004 gifts, which was computed at the lower rates that were applicable as the gifts were made. This has the same two effects as did the federal regime. First, it removes the post-2004 gifts from the estate tax base. Second, it taxes the remaining assets (the taxable estate plus Connecticut gift tax paid on gifts made within three years of death) at the higher brackets of the progressive rate schedule. In short, the Connecticut estate tax base does not include post-2004 Connecticut gifts.

We are aware that Connecticut administers the gift tax on gifts made in the year of death as part of the estate tax. The 2018 Form CT-706/709 (Connecticut Estate and Gift Tax Return) is a combined gift and estate tax return. Gifts made in years prior to the year of death are accounted for as inter vivos gifts. Gifts made in the year of death are accounted for as testamentary transfers. See line 8, including the current year taxable gifts in the estate tax base, and line 14 and Schedule B, reducing the tentative estate tax only by the Connecticut gift tax paid on the gifts made in the prior years. In light of the plain language of CGSA § 12-391(d)(1)(D), however, allowing a credit for gift taxes paid on all post-2004 Connecticut taxable gifts including those made in the year of death, we do not believe that the administrative short cut of the Form CT-706/709 changes the above analysis. Indeed, Form CT-706/709 produces the same result as would a straight-forward application of the Connecticut statutes, which would produce a gift tax on the gifts made in the year of death and an estate tax reduced by the amount of that gift tax.

The same, however, cannot be said of the inclusion in the Connecticut taxable estate of Connecticut gift taxes paid on gifts made within three years of death. While a credit is allowable for the gift taxes paid on these gifts, see CGSA § 12-391(d)(1)(D), that credit serves only to remove the gifts themselves from the Connecticut estate tax base. The credit does not serve to remove the gift taxes from the Connecticut estate tax base. In short, the gift tax paid on gifts made within three years of death is subjected to tax in the Connecticut taxable estate as a testamentary transfer.

Connecticut gift taxes paid on gifts made within three years of death are not includible in the federal gross estate. See § 2035(b), including in the gross estate only the gift tax paid under Chapter 12 (the Federal gift tax) on gifts made within three years of death. As noted above, IRC § 2058 allows a deduction only for the state death taxes paid with respect to property included in the federal gross estate. Accordingly, in the case of decedents dying after 2014 who made taxable gifts within three years of death, the deduction for the Connecticut estate tax must be reduced by the amount of the Connecticut estate tax attributable to the Connecticut gift tax paid on those gifts.

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Please call (206) 946-3602 if you have any further questions.