RYAN WILSON'S

GOLDEN BULLETS

Wealth & Estate Planning Strategies

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SHIFTING WEALTH EARNS BIG TAX SAVINGS

The annual gift tax exclusion is one of the most simple, yet powerful, of all the tools available to the financially successful individual. The privilege of totally excluding gifts from taxation is an extremely valuable one. Gift tax rates are equal to estate tax rates — and those rates are — once the gift becomes taxable — high! The right to totally exclude a gift from such rates can be very advantageous.

An incredible amount of wealth can be shifted, gift tax free, through the use of the (currently) $12,000 exclusion. The annual exclusion can be taken each year — for each gift — to each donee — with the number of potential donees virtually unlimited! Here are a few examples:

1. A 70 year old widower with four single children and six married grandchildren (16 donees) could divest himself of $192,000 ($12,000 x 4) plus ($12,000 x 12) — each and every year for the rest of his life. Assuming a 45% federal estate tax bracket, each year's gifts save $86,400! In 10 years the donor will have given away $1,920,000 — saving $864,000! Remember, (a) no out of pocket tax cost has been incurred and (b) no use of the unified credit was necessary.

   If the donor makes gifts for the remaining 16 years of his life expectancy, the amount of total gifts amounts to $3,072,000 with a potential estate tax savings of $1,382,400.

   But of course, that's not the whole story. If the donees invest the annual gifts at merely 4% after tax, the total value of the gifts at that time will be $4,190,310 — resulting in a potential estate tax savings of $1,885,639!

2. A married couple could double the amount of annually excludable gifts made to third persons such as children — from $12,000 to $24,000 — each — by "splitting" the gift. In other words, if the nondonor spouse consents to the gift, it may be treated as if each spouse made one half of the gift. This enables the spouse owning most of the property to take advantage of the other spouse's annual exclusion. In the example above, a married couple could — over a 16 year period give away $6,144,000 with a potential estate tax savings of $2,764,800! The projected value of those gifts — if the donees enjoy a 4% after tax return on the gifts — would be $8,380,620 — resulting in a potential estate tax savings of $3,771,279! (A 50 year old donor with 10 donees making $12,000 annual gifts who splits the gifts with her husband and makes those gifts in a planned program for life (expectancy 33.1 years) would give away $8,160,000 with a potential estate tax savings of $3,672,000. But if the donees invest at 4% net aftertax, the money will grow to $16,765,898 over the 50 year old donor's life expectancy — resulting in potential estate tax savings assuming a 45% federal rate — of $7,544,654!

3. Annual exclusion gifts can be made even on the donor's deathbed — and if made in the form of cash, securities, real estate, or even art or collectibles, will not be brought back into the donor's gross estate. Such gifts will not be brought back into the donor's estate — regardless of how close to death they were made — or the reasons motivating the gift. However, the gifts must be "completed" gifts. Thus, the check must be cashed and cleared through the bank, not simply delivered to the donee.

4. Annual exclusion gifts do not form part of the base used to compute the rate of tax when calculating federal estate taxes, i.e., they are not considered “adjusted taxable gifts.” So, unlike taxable gifts, annual exclusion gifts are not added back to push up the rate the remaining estate is taxed. So annual exclusion gifts have no adverse impact on estate tax costs.

THE BOTTOM LINE

The annual exclusion is a highly useful and significant estate planning tool that can be used to minimize or eliminate the cost of shifting an estate from one generation to another. Through careful planning, it is possible to obtain an annual exclusion — even for gifts in trust. Another valuable aspect of lifetime giving is the ability to see how the donee uses the gift. How the gift is used may change the way the donor disposes of his or her remaining assets. Also, there is an advantage to seeing the donee have the benefit of the gift during his or her lifetime, and not have to wait until the donor’s death. For example, many donors enjoy knowing that their gift made the purchase of a home possible.

A donor must also keep in mind that once the gift is completed, the gifted property is no longer available to support the donor. Thus, you do not want to gift if you cannot afford it. Finally, gifted property has a carry-over tax basis. So, a donor must keep this in mind if appreciated property is gifted. It is advisable to consult with a lawyer or a tax professional before you initiate a gifting program.

Ryan M. Wilson is an attorney with Fraser Trebilcock Davis & Dunlap, P.C., specializing in Estate Planning. If you have any questions regarding the topics in this issue or estate planning in general, you may contact me at (517) 377 0897 or by email at rwilson@fraserlawfirm.com

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“Golden Bullets” is provided as a source of general information about current developments in the practice of estate planning and related topics. If you have questions regarding this issue or estate planning in general, please contact Ryan Wilson prior to taking action.

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