

A Gift from the IRS? A Holiday Miracle

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The holidays are nearly upon us, and for many, this means holiday cheer, baking, and our endless gift lists. What should also come to mind is the “gift” that the IRS bestows upon all of us, which is the ability to make many gifts to our loved ones free of taxes, together with the benefits that accompany making those gifts. Below is a handy list of gifts that should be considered as we close out 2023.

1. **Annual exclusion gifts:** In 2023, an individual can make annual gifts of up to \$17,000 per recipient to an unlimited number of individuals free from any gift tax. Married couples can double this gift to \$34,000 per recipient to an unlimited number of individuals. This benefit is called the “annual exclusion amount” because the gift is *excluded* from gift tax for the calendar year in which the gift is made. The annual exclusion is a “use it or lose it” benefit, meaning that your ability to gift for that year ends after the year has passed.

Not only are annual exclusion gifts an effective way to pass wealth to family members and others, free from estate or gift taxes, but these gifts also have the added benefit of reducing the gift-giver’s taxable estate that would otherwise be subject to an estate tax upon his death.

These annual exclusion gifts can be made “outright” and paid directly to the recipient to qualify for the annual exclusion. Certain gifts can even be made to the recipient in a trust if it is properly structured.

2. **Lifetime gifts:** Gifts exceeding the annual exclusion amount are sometimes referred to as “lifetime gifts.” When “lifetime gifts” exceed the \$17,000 or \$34,000 annual exclusion amount in the case of a married couple, it reduces the federal estate tax exemption of the gift-giver. For example, the current federal estate tax exclusion is \$12.9M for each person. This means that at the federal level, the gift-giver can either gift during their life or die with \$12.9M. Therefore, if the gift-giver gifts \$117,000 to a recipient in 2023, \$17,000 of the gift will qualify for the annual exclusion amount for 2023. The remaining \$100,000 gift will reduce the gift-giver’s lifetime estate tax exclusion by \$100,000, thus reducing his available estate tax exclusion credit from \$12.92M to \$12.82M at death.

The other benefit of making more significant lifetime gifts that exceed the annual exclusion amount is that it removes the value of the gifted assets from the gift-giver’s estate. Removing assets from the gift giver’s estate can be particularly useful when the gifted asset is expected to appreciate in the future. By gifting those highly appreciable assets out of the gift-giver’s estate now, the gift-giver’s estate will pay a reduced estate tax at their death.

Lifetime gifts should be strongly considered at the present time as the federal estate tax exclusion of \$12.92M is set to “sunset” at the end of 2025. This means the amount of assets you can die with that will *not* be subject to an estate tax will plummet from \$12.92M free of estate tax to only approximately \$6.8M free of estate tax. Therefore, making gifts now to take

advantage of the current \$12.92M estate tax exemption is something to consider.

3. **Charitable Giving:** Most appreciate the many benefits of gift-giving to a favorite charity: it feels good to make a positive impact while simultaneously supporting a cause that is meaningful to the gift-giver. Many are unaware, however, that there are trusts that can be established to provide the gift-giver with an income stream, a tax break during the gift-giver's life, *and* a gift to one's favorite charity at death.

A charitable remainder trust does just that: it allows the gift-giver to make a contribution to the trust for the charity while simultaneously providing a partial tax deduction for the gift and an income stream to the gift-giver or her loved ones.

The tax deduction the gift-giver receives from funding a charitable remainder trust is based on the type of charitable remainder trust created. The deductions, depending on the type of charitable remainder trust, are then calculated by several factors, including the present value of the charity's interest, the assets "donated" to the trust, how long the trust will likely remain and/or the annual "payout" rate to the income beneficiary.

In addition to the present tax benefit enjoyed by the gift-giver, the gift-giver can also name herself or a loved one as the beneficiary of the present income stream from the assets donated to the trust. Based on how the trust is set up, the gift-giver (or nominated income beneficiary) can receive income annually, semi-annually, quarterly, or monthly. The IRS requires that the annual income stream must be at least 5% but no more than 50% of the trust's assets.

After the specified term of the trust or upon the death of the last income beneficiary, the remaining trust assets are then distributed to the designated charitable beneficiaries. The charitable beneficiary (or beneficiaries) can be public charities or private foundations. Moreover, the trustee can be provided the power to change the trust's charitable beneficiary (or beneficiaries) during the lifetime of the trust, if necessary.

Gifting can be an integral part of one's estate plan. Gift planning, especially involving trusts, can be complex and highly individualized. It is crucial to consult a knowledgeable estate planning attorney to ensure that the gifts made are properly structured and comply with tax laws at the state and federal levels, especially as the tax laws change over time. Please get in touch with me directly to discuss these or other gift-giving options before the end of 2023.