Price & Farrington's Estate and Tax Planning *Fast* Faxts

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Estate, Tax, Retirement and Wealth Preservation Planning

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Happy Holidays!

Gifts For Your Family From the IRS:
Opportunities in Real Estate, Cash, Investments

Please share these tips with your clients...

Gift giving is on everyone's mind this time of year, but making monetary gifts in a tax-sensible way is not always easy. Gifts are given out of generosity, but many of us ignore two key tax reasons for making major gifts: ***to reduce future estate taxes*** by removing property from one's taxable estate; and ***to reduce income taxes*** by moving income-producing assets to a family member who is in a low tax bracket.

Gifts to Reduce Estate Tax

Estate tax repeal is not scheduled until 2010-and whether it will ever happen is an open question, given a slumping economy, a vanished surplus and the costs of a war against terrorism. Whether the scheduled exemption increase from $1M in 2002 to $3.5M in 2009 will ever take effect is also uncertain. Tax-wise, it's safest to plan as if the increases and repeal *won't* take place-and to realize that even if they do, you could die before then. *Strategies to consider...*

☑ **Use the annual $10,000-per-recipient gift tax exclusion** to remove large amounts from your estate through a series of tax-free gifts. These gifts can be given to any number of recipients-and not just relatives. In 2002, the exclusion increases to $11,000 per recipient, or $22,000 for a married couple making joint gifts. You can also make additional unlimited tax-free gifts directly to a provider for an individual's college tuition or medical expenses.

☑ **Give away assets now-so they are subject to gift tax instead of estate tax.** Gift tax applies at a lower effective rate than estate tax. Say you are in the 50% estate tax bracket. Transferring $100,000 *by gift* requires $150,000 ($100K for the gift plus $50K for the 50% gift tax). But a *bequest* requires $200,000 (which after the 50% estate tax of $100K leaves $100K for the bequest).

☑ **Make gifts of appreciated property to remove taxable gains from your estate.** If you expect a stock may double before you die, a gift worth $1 today will save $2 being taxed later.

☑ **Leverage your gift using life insurance trusts.** A property bequest may trigger estate tax. An IRA bequest may trigger estate *and* income tax when the account is liquidated. Annual tax-free gifts of $11,000 to an irrevocable life insurance trust can fund an insurance policy on your life that the trust holds for the child. On your death the policy proceeds will benefit the child free of income and estate tax.

☑ **Transfer ownership of a property or a private business in stages.** Minority and lack of marketability discounts can reduce the taxable value of transfers sometimes by as much as 40%. Even if the gifts exceed the annual exclusion, you don't owe tax until you exceed your lifetime exemption amount - $1M in 2002-which applies to gift and estate taxes. By using the exemption early (possibly many years before death) accumulated income and growth from the time of the gift to death which would trigger a huge tax is also removed from the estate.

Strategies to Reduce Income Tax

☑ **Give appreciated securities to someone in a lower tax bracket.** You'll remove future appreciation in value from your estate. The recipient's basis in gift property is the lower of the gift giver's basis or the actual market value at the time of the gift. For example, if you bought shares at $20 and they're now worth $10, the donee takes the gift with a $10 basis and can't deduct any capital loss. You'll probably do better to sell the shares yourself, deduct your loss and then make a gift of the $10 cash.

☑ ***If property has already appreciated in value-but is not expected to appreciate further-bequeath it to eliminate your heir's future income tax bill.*** Why? Because "stepped up basis" applies to inherited property but not currently to gifts. Example: Stock purchased at $100 but worth $1000 some years later is gifted. The donee's basis will be the donor's cost of $100. If the donor transfers cash and holds the stock until death, the donee's basis will be date-of-death value: $1000. This step-up saves the donee capital gains tax and does not cause additional estate tax, assuming the stock doesn't rise further.

Keep Track of Gifts

If you make a gift of property worth less than $10,000, you may want to file a gift tax return-including an appraisal-even though you don't have to. This will start the statute of limitations running and prevent the IRS from challenging the value of the gift more than three years later,which it might be tempted to do if the property appreciates greatly in value. If no return is filed, the IRS will be able to challenge the value of the gift any time. ■

Need to develop a strategy? Contact us.

"Season's Greetings' looks O.K to me. Let's run it by the legal department."

Holiday Ponderings...

❄ ***"And it came to pass in those days, that there went out a decree from Caesar Augustus that all the world should be taxed."*** -New Testament

❄ ***"I once wanted to become an atheist but I gave up. They have no holidays."*** -Henny Youngman