Financial strategies and future generations

Tax act provided window of opportunity for giving

BY JESSICA GALLIGAN GOLDSMITH

When the federal government enacted the 2010 Tax Relief Act at the end of December, significant changes were made to the estate, gift and generation-skipping transfer (GST) tax laws.

Fortunately, most of the changes were extremely favorable to the taxpayer. However, these changes are temporary and are set to expire at the end of 2012 unless Congress acts to extend the current legislation. As 2010 showed us, Congress cannot be depended on to act, particularly in an election year. Therefore, if you're considering making substantial gifts to your children and grandchildren now may be the time to do it.

What the act does

The 2010 Tax Relief Act increased and unified the federal estate, gift and GST tax exemptions to $5 million per person. A married couple is now able to transfer up to $10 million tax-free to their children and grandchildren either during their lifetimes or at death.

This amount is considerably more than the combined $2 million gift exemption and $7 million estate tax exemption that was available for a married couple in 2009. However, under the law as written, the gift and estate exemptions will decrease substantially to only $1 million per person after 2012, and the GST exemption will decrease to approximately $1.4 million, indexed for inflation.

This can make a very significant difference in the amounts that an individual or married couple can pass to children and grandchildren free of federal transfer taxes.

Tax rates for gifts

The federal estate, gift and GST tax rates for gifts of more than $5 million or estates of more than $5 million will remain at 35 percent for 2011 and 2012 – the lowest rate in decades.

Starting in 2013, these rates are scheduled to increase to 55 percent, which means your children and grandchildren are likely to receive considerably less from your future estate than you can give them today.

If you can't afford to make lifetime gifts of the full $5 million, it is still a good idea to consider making smaller gifts that use only a part of your new exemption.

New York state has no state gift tax, and future appreciation earned on any property given away will be removed from your estate. Everyone now has the opportunity to make substantial new gifts. Even if you have exhausted your prior lifetime gift exemption of $1 million, in 2011 and 2012 you can make up to $4 million in "extra" gifts to children and grandchildren without paying any gift or GST tax.

If you can't afford to make lifetime gifts of the full $5 million, it is still a good idea to consider making smaller gifts that use only a part of your new exemption.

You can also continue to make annual gifts of $13,000 per person, and you can pay any amount of tuition and medical expenses directly to a school, medical professional or medical institution without using any of your gift or GST exemptions.

Undervalued assets

With the increased amounts available for lifetime giving, business owners, as well as investors in real estate and other currently depressed assets, should also consider optimizing the amount that may be transferred through the use of grantor retained annuity trusts and valuation discounts.

Fortunately, these planning tools were not affected by the 2010 Tax Relief Act. The combination of undervalued property, interest rates near historic lows and a vastly increased lifetime gift tax exemption makes this an excellent time to pass undervalued assets to one or more future generations.

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