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You Can't Take it With You: Giving Now Reduces Tax Liability

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There is a grain of truth in every cliché and that is particularly true of these two:

- **Money. . .You can't take it with you; and**
- **It's better to give than to receive**

In the context of estate planning, I encourage all of my clients to consider these old adages. Whether you are extremely wealthy or only moderately so, it's important that you enjoy the fruits of your labor while you are alive because after you are dead, you have absolutely no use for your money. And you certainly won't be able to enjoy it from the grave.

The larger your estate, the more estate taxes your heirs pay

Now, you may be thinking about your heirs and the fact that you want to leave something for them to enjoy once you've passed on. That's a common consideration for just about all of my clients. But here's the kicker. The larger your estate, the more estate taxes and gift taxes your heirs will have to pay after you die. So, spending some of your money now will actually benefit your heirs by reducing their exposure to estate and gift taxes.

Gifts up to $13,000 per year are tax free

What if I told you there is a way to benefit your heirs and other loved ones now, before you die, and simultaneously reduce their exposure to estate and gift taxes? Well, there is and it's by giving while you are still alive. Under current law, you can give any person up to $13,000 per year, without paying taxes. You can also give an additionl $1 million collectively to all of your heirs without taxes [assuming you're a US citizen – if not, see my articles on international estate planning].

Example

Let me illustrate. Suppose you have 3 chldren and 7 grandchildren. You can make annual gifts to them of $130,000 ($13,000 x 10). If they're married, you can double that amount. Let's assume you also decide to give them an additional one-time gift of $100,000 each ($100,000 x 10 = $1 million). You will have given them $1,130,000 without paying any taxes.

Assume that instead of giving them $1,130,000 that you die in 2011 with an estate worth that amount. Because of the way that the estate tax laws work, they will pay approximately $53,300 in estate taxes and receive only $1,076,700.

Think about it. . .if you leave your heirs $2 million dollars when you die, they will receive only $1,565,000 if the estate tax comes back as scheduled. So, it just makes sense to give as much as you can afford to give while you are alive. By giving now, you benefit your heirs while at the same time reducing your estate, thus reducing your heirs' tax liability.

Gift tax rate expected to jump to maximum rate of 55%

In fact, I advise some of my clients to give more than $13,000 per year. Considering that the current gift tax is relatively low (35%), now is a perfect time to give more than you might ordinarily give and to simply pay the tax. Next year the gift tax is expected to jump to a maximum rate of 55%; therefore, it just makes sense from some clients to give more than $13,000.

GRAT facilitates asset transfers

In addition to making $13,000 gifts, you can use other estate planning techniques to reduce exposure to tax liability. One such technique is the grantor-retained annuity trust (GRAT). The GRAT allows you to transfer assets that you expect will appreciate in value into a trust and to receive periodic payments from the trust for a minimum of two years. Appreciation or gains in the assets placed in the trust go to the trust's beneficiaries tax-free (caution: as they say in certain circles "some restrictions apply")..

There is a strong possibility that the laws governing GRAT's will soon change, making them far less beneficial for avoiding tax liability. If this speculation is correct, Congress may extend the minimum terms to ten years and make the distributions taxable.

Consider the intra-family loan option

Another option that I advise my clients to consider is the intra-family loan. The interest rate on intra-family loans is set by the government and currently stands at 0.53% for loans of three years or less. However, if the government believes that the "loan" is really a gift, it will be taxed as such if it exceeds the $13,000 limit. Therefore, it's important to treat the loan as a loan by putting it in writing and requiring strict adherence to its terms including on-time payments and imposition of late fees when payments are not made on time.

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If you are concerned about asset protection and reducing tax liability for yourself and your heirs, you need a qualified estate planning attorney in your corner who is also very well versed in the estate and gift tax laws – someone who is certified as a specialist in estate planning by the California State Bar Board of Legal Specialization and who has a Masters Degree (LLM) in Tax Law. I have both of those, and also 20 years of experience in estate planning for high net worth clients. I will review your assets and advise you of the best options to help you achieve your estate planning goals while minimizing your exposure to tax liability.

Get started >>

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