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Timely Tax Tips: Smart Gifting Ideas

By Cynthia Hatfield

So, your grandson Johnny is graduating from High School and you want to buy him a car. Or maybe you are just getting older and you are thinking of passing on a few baubles to your children and grandchildren. Let's review the gifting rules on the impact of these types of transactions.

In general, each person has two gift exclusions of which they can take advantage. The annual exclusion is the value of cash and non-cash gifts that may be made on an annual basis tax-free. This exclusion is currently $11,000 per donor to another person. If you are married, you could choose to gift up to $22,000 jointly, and split the gifts with your spouse.

The lifetime exclusion, currently one million dollars, is the amount of gifts a person can make in total over their entire life, in excess of the annual exclusion, without incurring tax.

So back to our first example, if Johnny wants a new BMW at $30,000, you and your spouse could gift him the car, but you would have a gift tax-reporting situation. You would utilize your joint annual exclusions on the car for Johnny, and the excess $8,000 would be applied against your lifetime exclusion.

When you make a gift across generations, to grandchildren, great-grandchildren, grandnieces and nephews, etc, you are additionally subject to the generation skipping tax (GST). The good news here is that there is also a lifetime exclusion amount for the GST, and it is currently $1,120,000.

Why should you report these gifts to the government, you may wonder? Well, gifting is an excellent way to remove assets from your estate on an annual basis, tax-free. However, if you do not document the value of the gifts you have given, other than cash, at the time of the gift; it is entirely possible that, upon examination of your estate return many years later, the IRS could include these gifts in your estate at their then fair market value. The fact of the matter is that many gifts, such as stock, jewelry, business interests, real estate, etc., appreciate over time. Therefore, it is important to correctly value, document the value, and report the gift when it is transferred.

Our second example involves your daughter, who is getting married to a nice, but currently low-income guy. You decide to give the happy couple three acres of prime real estate in Auburn, so they can build a new home. This gift is clearly in excess of the $11,000 or ($22,000 joint) annual exclusion. In addition, it is a non-cash gift, which is likely to continue to appreciate in value. This is a perfect example of a gift that should be appraised, and reported to the IRS on Form 709.

As usual, with the tax law, there are a few exclusions from the rules. If you want to pay for your grandchild's college tuition, you can do so in any amount as long as you make the payments directly to the educational institution. The same rules apply for any type of medical payments.

The gift and estate law is complex and this article covered just a few of the basic gifting rules. Many more planning opportunities are available through the use of trusts, family limited partnerships, and other tools, which may include the use of formal valuations or discounting techniques. Please do not rely solely on the information I have presented to you here. Contact your financial advisor or attorney or myself for additional guidance with gifting or estate planning.

If you have questions or comments regarding this article, please direct them to Bainbridge resident Cynthia Hatfield, CPA Tax Manager at Zinner & Co. LLP chatfield@zinnerco.com, or call her at 216-831-0733.