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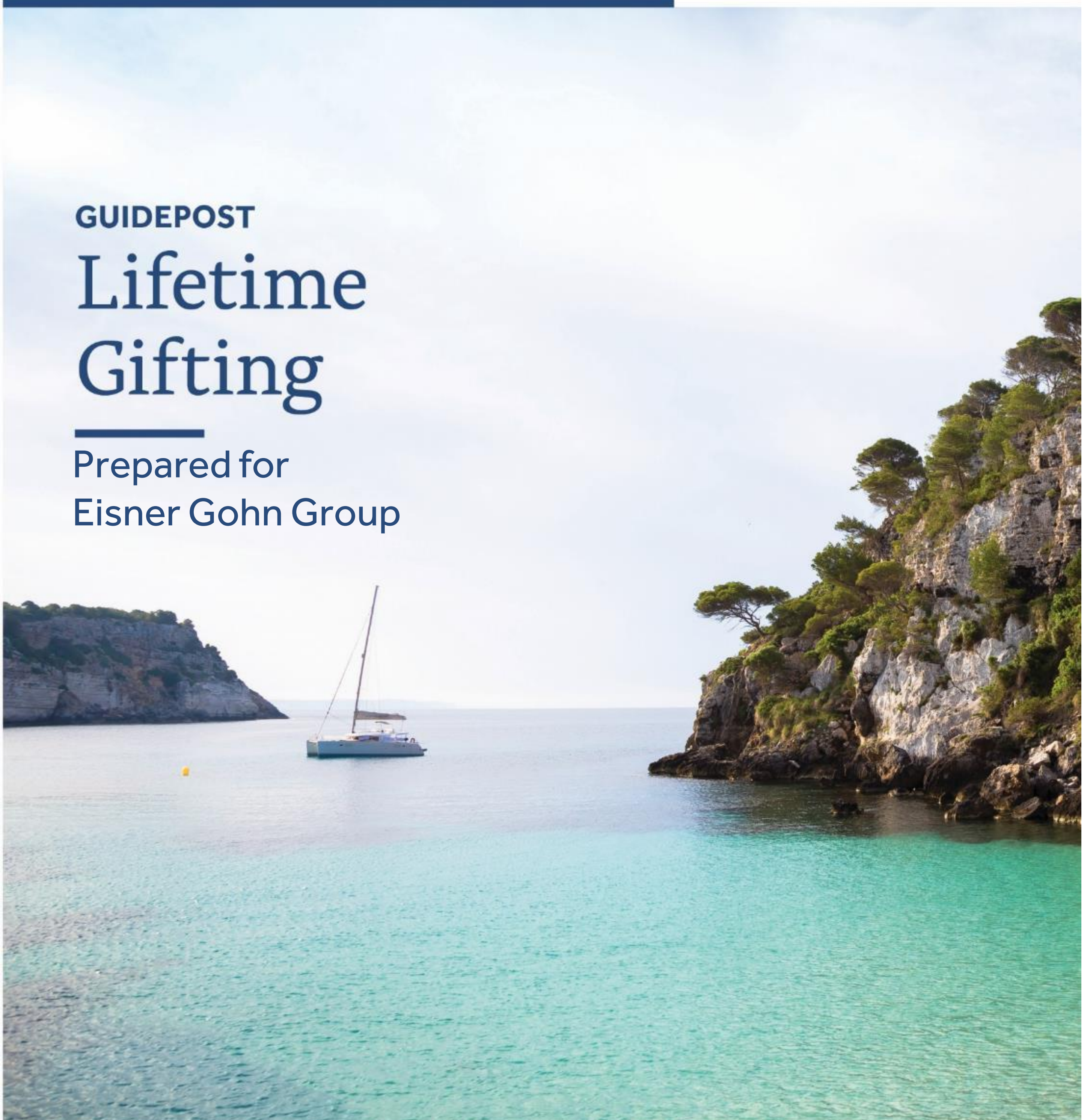

GUIDEPOST

Lifetime Gifting

Prepared for
Eisner Gohn Group

Lifetime Gifting

A lifetime gift is a transfer of assets from one individual to another for less than full and adequate consideration. Many individuals utilize lifetime gifting to facilitate reduced income or estate tax liability. Prior to determining whether lifetime gifting is appropriate, an individual should consider income, gift and estate tax ramifications, long-term income needs and otherwise available resources, and asset protection planning needs and objectives.

Lifetime gifting and the federal gift tax

Internal Revenue Code (IRC) §2501 provides that gift tax is imposed annually on gifts made by an individual. A gift is a transfer of assets for no consideration or for consideration worth less than the transferred asset's fair market value. The gift tax rate is 40% (in 2025) and gift tax is paid by the donor (as opposed to the donee).

IRC §2503 defines certain transfers that are not to be considered as "taxable gifts" for the purposes of computing gift tax liability.

- **Annual gift tax exclusion**. IRC §2503(b)(2) enables a donor to gift a certain amount of assets to an unlimited number of donees every year without imposition of gift tax. In 2025, the annual gift tax exclusion amount is $19,000 per donee. Married couples can utilize the annual gift tax exclusion to gift $38,000 (in 2025) gift tax free to each donee. The annual gift tax exclusion is often adjusted for inflation in increments of $1,000. For a gift to qualify as an annual exclusion gift, it must be a "present interest" gift, which means the recipient has an unrestricted right to the immediate use and possession of the gifted property. For this reason, if annual exclusion gifts are made to an irrevocable trust, trust beneficiaries must be given withdrawal rights over the gifted amount (often referred to as "Crummey" withdrawal rights).

  The annual gift tax exclusion amount can be used to make tax-free gifts to a 529 education savings account since contributions to a 529 account are treated as completed present interest gifts from the donor to the account beneficiary. In fact, a donor can make an election on a U.S. Gift Tax Return Form 709 to have contributions to a 529 account treated as if made ratably over a five-year period. This means that a donor can utilize five years of annual gifting capacity in one year to fund a 529 account. In 2025, a donor could contribute up to $95,000 (or, $190,000 for a married couple) to a 529 account without the imposition of gift tax liability since the contribution will be treated as made over the next five years.

  The annual gift tax exclusion amount can generally be utilized to fund Uniform Transfers to Minors Act accounts if the account terminates when the beneficiary attains the age of 21. Similarly, the annual gift tax exclusion amount can be used to fund a "2503(c) trust" if the trust provides that trust assets may be used for a beneficiary prior to attaining age 21 and trust assets will be distributed to the beneficiary at age 21 (or the beneficiary is given the right to withdraw trust assets at age 21, typically, for a reasonable period such as 60 days), and, if the beneficiary dies prior to age 21, trust assets are payable to the beneficiary's estate or as the beneficiary appoints.

- **Education and medical expenses**. IRC §2503(e) provides that a "qualified transfer" to an educational organization or to a provider of medical care will not be treated as a gift for the purposes of computing gift tax liability. This allows an individual to spend an unlimited amount of money on another's education expenses or health care costs without being treated as having made a gift. For education expenses, payments must be made directly to the educational organization to avoid being treated as a gift. Also, payments must be for tuition only and not books, supplies, room and board or meal plans. Payments for medical expenses must be paid directly to the medical provider to avoid being treated as a gift.

All other lifetime gifts will be deemed taxable gifts for the purpose of computing gift tax liability. However, various credits and deductions are allowed when computing gift tax liability.

- **Using the exclusion amount to offset gift tax liability**. Individuals can utilize the basic exclusion amount to reduce gift tax liability. The exclusion amount shields a defined amount of assets from estate tax upon an individual's death. In 2025, the exclusion amount is $13.99 million. The exclusion amount can be used during lifetime to make tax-free gifts above and beyond the annual gift tax exclusion amount. Of course, any exclusion utilized during lifetime reduces the exclusion amount available at the donor's death.

  Note that the Tax Cuts and Jobs Act of 2017 doubled the then effective exclusion to achieve a $13.99 exclusion in 2025; however, the increased exclusion was not made permanent. Accordingly, the exclusion amount is scheduled to sunset on December 31, 2025, to $5 million, as made permanent under the American Taxpayer Relief Act of 2012, adjusted for inflation. This means that, under the current law, the amount of assets an individual can gift during lifetime without imposition of gift tax will be significantly reduced in 2026. This provides a limited window for high-net-worth individuals or for individuals who live in a state with state level estate tax but no state level gift tax to utilize lifetime gifting to make use of the temporarily increased exclusion amount to reduce exposure to estate tax liability.

- **Charitable gifts**. Certain gifts made to qualified charities can be deducted for the purposes of determining gift tax liability.

- **Transfers between spouses**. When an individual makes a gift to his/her U.S. citizen spouse, the gifted amount can be deducted for the purposes of determining gift tax liability.

Even where lifetime gifts will expose the donor to gift tax liability, considerable tax savings still may be achieved since the gift tax is tax exclusive. The gift tax calculation is based on the value of taxable gifts made in any given year. The gift tax calculation does not include the value of assets used by the donor to pay gift tax liability. In contrast, the estate tax is calculated on the value of a deceased's estate, including the value of assets the estate will use to pay estate tax liability.

Advantages of lifetime gifting

- Gifts can reduce the impact of estate tax on an individual's estate since the value of the gifted asset, and its anticipated ongoing appreciation, will be removed from the donor's taxable estate.
- For donors living in a state that imposes a state level estate tax but has no state level gift tax, exposure to state estate tax can be substantially reduced, or even eliminated, by making lifetime gifts.
- Gifting income producing property to beneficiaries in a lower income tax bracket reduces the impact of income tax on the asset's income (subject to the "kiddie tax").
- Gifting assets to an irrevocable trust for the benefit of the donor's beneficiaries can protect the assets from the claims of creditors (both the donor's creditors and the creditors of the trust beneficiaries, assuming no creditor has a claim to the gifted assets at the time of the gift).
- Lifetime gifts can provide greater personal satisfaction than testamentary transfers since the donor can witness the benefit a donee receives from a gift.
- If business interests or other family legacy assets are gifted during lifetime, successor generations can become involved in the management and operation of those assets while the donor is still alive and able to provide guidance.
- If transferred assets are subject to certain restrictions (lack of control and lack of marketability), gifted assets can be transferred at a discounted gift tax cost.

Disadvantages of lifetime gifting

- Generally, most (but not all) assets owned by an individual receive a basis step-up to fair market value upon the owner's death. The basis step-up reduces the amount of income tax liability due if assets are later sold. However, if an individual gifts assets during his or her lifetime, the donee receives a carry-over basis in the gifted assets (the donee's basis will equal the donor's basis, plus increases for improvements). As such, lifetime gifts eliminate the basis increase that may otherwise occur if the donor retained the gifted assets until death.
- If gifted assets decline in value, any exclusion used to facilitate the gift could be wasted.
- A donor's circumstances could change after a lifetime gift is made, resulting in insufficient assets (post gift) to support the donor's needs. In such an event, the donor has no right to reclaim possession of the gifted assets.
- Where a donor may wish to apply for certain government benefit programs, a lifetime gift of assets could trigger a "look-back" period during which the donor will remain ineligible.

As a result of the Tax Cuts and Jobs Act of 2017 (TCJA) the estate, gift and generation skipping transfer (GST) tax exemption amounts increased to approximately $11.18 million per person (approximately $22.36 million for a married couple). For assets transfers in excess of the applicable exemption amount and otherwise subject to such taxes, the highest applicable federal tax rate remains at 40 percent. While the exemption amounts are indexed for inflation, current law provides for an automatic sunset of these increased exemption amounts after 2025. As a result, the exemption amounts available in 2026 and beyond could be reduced to a level provided under prior law ($5.49 million/single and $10.98 million/couple in 2017, indexed for inflation) absent further action by Congress. In addition, under different rates, rules and exemption amounts (if any), there may be state and local estate, inheritance or gift taxes that apply in your circumstances.

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