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Gifts in 2013

As we approach the end of another year, we have been asked by clients whether 2013 should be a year in which they make gifts. Gifting is usually thought of as a tax saving strategy, but whether it should be implemented to reduce future estate tax liability or for some other purpose, gifting and the manner in which gifts are made requires careful consideration.

Currently, there are two separate gift and estate tax schemes – federal and state. For federal gift tax purposes, this year an individual can gift up to \$14,000 to an unlimited number of persons. Spouses can each make these gifts. Gifts to any one person in excess of \$14,000 (\$28,000 for married couples) require the filing, by the gift-giver, of a federal gift tax return. However, each individual can gift up to \$5.25 million in excess of the \$14,000 limit without any gift tax consequence. At the individual's death, the balance of the \$5.25 million can be used to avoid federal estate tax, applied against the value of his or her estate. New York does not impose a gift tax on the value of any gift. However, only \$1 million avoids estate taxes at death.

An example demonstrates the interplay between the federal and state schemes. John has an estate of \$2,200,000. In 2013 he gifts \$14,000 to each of his 4 grandchildren (\$56,000). If he makes no other gifts in 2013, he will not have to file a federal gift tax return. However, John also makes gifts of \$514,000 to each of his 2 children. Because the gifts to his children exceed \$14,000, John has to file a gift tax return. However, rather than paying any federal estate tax, John allocates \$1 million of his \$5.25 million unified credit to the gifts exceeding \$14,000 - \$500,000 per child. As a result, John has no gift tax to pay in 2013 and, at his death, there is \$4.25 million remaining of his federal estate tax credit, well in excess of the value of his remaining estate, \$1,116,000.

Now let's consider the effect John's gifts have on his New York State estate tax liability. There is no NYS gift tax and, by reducing the size of his estate, from \$2,200,000 to \$1,116,000, John has significantly reduced his estate tax liability.

Gifts can provide benefits besides tax savings. It is a strategy that can be used to financially qualify a person for Medicaid benefits. Aside from the benefit to the gift-giver, the recipient derives benefits from the gift permitting, for instance, payment for goods, services or education, which might not otherwise be affordable, and allowing the recipient to improve his or her quality of life. Gifting can also have unintended

consequences. Thus, for instance, assets like stock or real property that would qualify for a step-up in basis if inherited at the giver's death do not qualify for that tax treatment if gifted during the giver's lifetime. In the earlier example, John's gift to his children would disqualify him from receiving Medicaid nursing home benefits for 5 years.

If a gifting strategy is something you wish to implement, it is important to consider the manner in which the gift(s) will be made. Is the recipient a minor child, financially irresponsible or otherwise unable to manage the gift? Is there a possibility that the recipient will have marital issues that place the assets at risk? If the intended beneficiary ultimately predeceases you, who will benefit from your gift? In any of these cases, the implementation of a trust as the repository for the gift(s) may enable the gift to be effectively managed and utilized for the benefit of your intended beneficiary.

Gifting is an excellent strategy. It can accomplish very different goals but it can also create complications. It is best to consult with an attorney experienced in this area of the law to help you evaluate the most effective gifting strategy for your circumstances. To avoid the pressure that end-of-year gift planning can cause, we recommend that you contact us as soon as possible for a consultation to discuss the merits of this estate planning strategy.