First Quarter 2023

Giving Away Money Needs to Start with a Plan

One of the more pleasant surprises in life is to discover you have more money than you will be able to spend, and you can afford to make financial gifts to family, friends, causes, and charities. But before you do so, you need to talk with your financial and tax advisors about the pros and cons of gifts and whether you risk running out of money you might need later.

There are two tax realities that make gifting over the next three years more attractive.

1. The recent inflation adjustments increased the estate and gift tax exemption to $12,920,000 over an individual's life before federal gift taxes take effect. The amount that can be given to any individual without gift tax implications has increased to an all-time high of $17,000. If couples choose to work together in making gifts, those amounts double.
2. Unless Congress acts to extend provisions of the 2017 Tax Cuts and Jobs Act (TCJA), the estate tax exemption reverts to the 2017 inflation-adjusted exemption of about $7 million at the end of 2025. Taking advantage of today's higher exemption could reduce future estate taxes if the estate tax provisions are allowed to expire. In that situation, even if one has already exceeded their gift tax exemption, gifting now and paying gift tax at 40%, could potentially save future taxes by decreasing the size of the estate.

On the downside, there is a potential disadvantage to giving gifts such as stock, property, collectibles, etc., before you die, rather than as an inheritance from your estate. When the recipient liquidates the gift, the individual will owe taxes on the appreciated value from when you first purchased the gift. An inherited asset generally receives a step-up in income tax basis to the value at the time of death, eliminating any capital gains prior to your death. Of course, that is if future tax law changes don't eliminate the step-up in basis, as was proposed in 2021. There's always the risk that strategies put in place today may be undone by tax rules in the future.

The $17,000 per individual per year is a different matter altogether. You can gift as many individuals as you would like over the course of a year, but there can only be one annual gift to each individual. This might be a way to offset college tuition, help make a down payment on a home, buy a used car, or hundreds of other ways to offer a helping hand. As long as the gift is under $17,000, there are no gift tax ramifications or taxable events. Naturally, there is a catch. You can't expect the money to be repaid. That would make it a loan and if you decide to forgive a loan, it could be considered taxable income to the borrower.

Gifting can also be a way to avoid future family arguments over your estate by legally transferring assets to another before you die.

If you think you might someday want to apply for Medicaid long-term-care benefits, however, you need to be careful because giving away money or property can interfere with your eligibility. To qualify for Medicaid, individuals cannot have income or assets above a certain level. Under federal Medicaid law, transferring certain assets within five years before applying for Medicaid, can make you ineligible. This includes gifts to charities and gifts to individuals up to $17,000 that federal law allows without a gift tax. Medicare considers them to be transfers.

It is important to work with a knowledgeable financial advisor and make plans that consider different future scenarios and how gifting might affect your net worth, future estate, and tax liability as well as your eligibility for federal programs.

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