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Guiding clients toward financial success.

# ESTATE AND GIFT TAXES

## WHAT YOU NEED TO KNOW

Income tax, payroll tax, capital gains tax – there are many divisions in the Internal Revenue Code, including one you might not have focused on lately: estate, gift, and generation skipping transfer taxes. Here's what you need to know about how these taxes might affect you.

## WHAT ARE THE CURRENT RULES? ■ ■ ■ ■ ■

■ **FIRST A LITTLE BACKGROUND.** A law passed back in 2001 gradually reduced estate tax rates and increased exemption amounts over a ten-year period, finally eliminating the estate tax in 2010, but only for that one year.

Late in 2010, Congress passed a law setting the estate tax exemption at \$5 million and the maximum estate tax rate at 35% through the end of 2012.

Finally, Congress made the rules “permanent” in the *American Taxpayer Relief Act of 2012*, passed in January 2013. This law set the amount exempt from tax at \$5 million with a top tax rate of 40%.

■ **THE ESTATE AND GIFT TAX EXEMPTION.** The estate and gift tax systems, which were temporarily severed during the last decade, are unified for 2013 and beyond. You can transfer, either during your lifetime or via your will after your death, a certain amount before estate or gift tax is due. The basic exemption amount is \$5 million. This amount is adjusted annually for inflation, resulting in a \$5,250,000 exemption for 2013 and \$5,340,000 for 2014.

The basic exemption is per person; thus a couple's exemption is twice that amount.

■ **PORTABILITY RULES.** Also made permanent in the law is the portability of unused exemptions. Under prior law, couples frequently performed complex estate planning to take full advantage of both spouses' exemptions. Now the law allows a deceased spouse's estate to transfer any unused exemption to the surviving spouse without all the complex planning.

Executors make this “portability” election by filing an estate tax return, even if an estate is not taxable and might not otherwise need to file.

■ **BASIS RULES.** The law now provides for a step-up in basis to fair market value for all assets passing through an estate, even assets below the basic exemption amount. Later sales of such assets create taxable gain only to the extent the sales price exceeds the fair market value in the decedent's estate.

The basis of gifts made during one's lifetime does not change in the transfer. Instead, the basis is the same in the recipient's hands as it was in the donor's hands.



## SHOULD YOU MAKE LIFETIME GIFTS? ■ ■ ■ ■ ■

■ **UNIFIED ESTATE AND GIFT TAXES.** Lifetime gifts made to your children and others also factor into the exemption threshold, and in effect can lower the exclusion amount available to your estate. For example, if you give away \$2 million during your lifetime, your estate tax exemption in 2014 would be only \$3,340,000.

■ **TAX-FREE GIFTS.** In addition to the lifetime gifting limit, the IRS allows annual tax-free gifts of up to \$14,000 per recipient (\$28,000 on joint gifts made by married couples). The annual limit is subject to adjustments for inflation. As long as your gifts remain under the annual exclusion amount, they have no impact on your basic estate tax exclusion.

You can also make unlimited payments for unreimbursed medical expenses and tuition, gift-tax-free, when you pay the fees directly to the medical care provider or qualified school. Gifts between spouses are also excluded from gift tax, though an annual limit applies when your spouse is not a U.S. citizen.

■ **SKIPPING GENERATIONS.** The generation skipping tax (GST) is coordinated with other estate tax provisions. The GST can be assessed when someone gives or bequeaths to their grandchildren an amount in excess of their basic exclusion. Congress uses the GST to make sure that each generation is taxed when passing on their estate.

## DO YOU NEED A PLAN? ■ ■ ■ ■ ■

■ **WHAT SHOULD YOU DO NOW?** First, estimate the size of your estate to determine if you may be subject to estate tax.

If your estate is under the tax threshold, don't assume that you can just ignore estate planning. A plan is not just about reducing federal estate taxes; don't overlook state tax rules that could vary from federal law.

Also, there's more to estate planning than just taxes. An estate plan can help assure your family of financial security after your death. It can cut taxes, administrative costs, and red tape. It allows you to dispose of assets as you wish, with consideration given to your heirs' individual needs and desires.

If you don't have an estate plan, establish one as soon as possible. At a minimum you need the following:

- A will or trust to specify who will inherit your assets and to appoint a guardian for any minor children.
- A medical directive or "living will."
- A financial power of attorney.
- Updated beneficiary designations for insurance and pension assets.

Once you have a plan in place, you should review and update it whenever your financial situation changes or there are changes among your heirs or beneficiaries.

*For help calculating the value of your estate, or to learn more about estate planning options, please contact our office and your attorney.*

*Information presented in this brochure is of a general nature and should not be acted upon without further details and/or professional assistance.*



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