

Take Full Advantage Of Your Annual Gift Tax Exclusion

Did you know that one of the most effective estate-tax-saving techniques is also one of the simplest and most convenient? By making maximum use of the annual gift tax exclusion, you can pass substantial amounts of assets to the younger generations without any gift tax.

In fact, by giving the maximum gifts in December 2021 and again in January 2022, you can reduce your estate by six figures if you're being generous to multiple beneficiaries.

Maximizing Your Gifts

Despite a common misconception, federal gift tax applies to the giver of a gift, not to the recipient. But gifts can generally be structured so that they're — at least to the degree possible — sheltered from gift tax. More specifically, by the annual gift tax exclusion and, if necessary, the unified gift and estate tax exemption for amounts above the exclusion. (Using the unified exemption during your lifetime, however, erodes the available estate tax shelter.)

For 2021, the annual gift tax exclusion is \$15,000 per recipient. That amount will increase to \$16,000 for 2022. Accordingly, you can give each family member up to \$15,000 a year without owing any gift tax. For instance, if you have three adult children and seven grandchildren, you may give each one up to \$15,000 in December, for a total of \$150,000. Then you can turn around and give each one \$16,000 in January, for \$160,000 more — a grand total of \$310,000.

Furthermore, the annual gift exclusion is available to each taxpayer. If you're married and your spouse consents to a joint gift, also called a "split gift," the exclusion amount is effectively doubled to \$30,000 per recipient (\$32,000 in 2022). Bear in mind that doing this triggers IRS reporting responsibilities (see "Do you have to file a gift tax return?" below). Going back to the previous example of maximizing gifts to a total of 10 family members, a couple could gift up to \$300,000 in December 2021, and \$320,000 in January 2022, for a total of \$620,000, all gift tax free.

Coordinating With The Lifetime Exemption

The lifetime gift tax exemption is part and parcel of the unified gift and estate tax exemption. It can shelter from tax gifts above the annual gift tax exclusion. Under current law, the exemption effectively shelters \$10 million from tax, indexed for inflation. The inflation-indexed amount of \$11.7 million in 2021 is increasing to \$12.06 million in 2022.

However, as mentioned above, if you tap your lifetime gift tax exemption, it erodes the exemption amount available for your estate. For instance, suppose you give \$850,000 to family members in 2021, with \$150,000 sheltered by the annual gift tax exclusion. As a result, the available exemption able to shelter your estate in 2021 is reduced to \$11 million (\$11.7 million - \$700,000).

Exceptions To The Rules

Be aware that certain gifts are exempt from gift tax, thereby preserving both the full annual gift tax exclusion and unified exemption. This includes gifts:

- From one spouse to the other,
- To a qualified charitable organization,
- Made directly to a healthcare provider for medical reasons, and
- Made directly to an educational institution for a student's tuition.

For example, you might pay the tuition of a grandchild's upcoming school year directly to the college. The gifts don't count against the annual gift tax exclusion.

Planning Your Gifting Strategy

The annual gift tax exclusion remains a powerful tool in your estate planning toolbox. Contact your estate planning advisor for help developing a gifting strategy that works best for your specific situation.

SIDEBAR: Do you have to file a gift tax return?

If the total value of your gifts doesn't exceed the annual gift tax exclusion limit, you don't have to file a gift tax return (Form 709). However, to establish the value of gifts of property with the IRS, you can file Form 709.

The bottom line: A gift tax return is required if you exceed the annual exclusion amount, or you give joint gifts with your spouse. Unfortunately, you can't file a "joint" gift tax return. In other words, each spouse must file an individual gift tax return for the year in which they both make gifts.

The deadline for the gift tax return is April 15 of the year following the year of the gift, the same as the due date for income tax returns. Accordingly, for gifts made in 2021, you must file your return by April 15, 2022, or October 17, 2022, if your gift tax return has been extended.

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