

## PECK FINANCIAL ADVISORS

Valerie L. Peck, MBA, CFP® Presents:

# Understanding the Gift Tax Exclusion

*Most of us will never face taxes related to money or assets we give away.*

**“How can I avoid the federal gift tax?”** If this question is on your mind, you aren’t alone. The good news is that few taxpayers or estates will ever have to pay it.

Misconceptions surround this tax. The IRS sets annual and lifetime gift tax exclusion amounts, and this is where the confusion develops.

Here’s what you have to remember: practically speaking, *the federal gift tax is a tax on estates*. If it wasn’t in place, the rich could simply give away the bulk of their money or property while living to spare their heirs from inheritance taxes.

Now that you know the reason the federal government established the gift tax, you can see that the lifetime gift tax exclusion matters more than the annual one.

**“What percentage of my gifts will be taxed this year?”** Many people wrongly assume that if they give a gift exceeding the annual gift tax exclusion, their tax bill will go up next year as a result. Unless the gift is huge, that won’t likely occur.

The IRS has set the annual gift tax exclusion at \$14,000 this year. What this means is that you can gift up to \$14,000 each to as many individuals as you like in 2013 without having to pay any gift taxes. A married couple may gift up to \$28,000 each to an unlimited number of individuals tax-free this year. The gifts may be made in cash, or they can be made in stock, contributions to 529 plans, collectibles, real estate – just about any form of property with value, as long as you cede ownership and control of it.<sup>1,2,3</sup>

So how are amounts over the \$14,000 annual exclusion handled? The excess amounts count against the \$5.25 million lifetime gift tax exclusion. While you have to file a gift tax return if you make a gift larger than \$14,000 in 2013, you owe no gift tax until your total gifts exceed the lifetime exclusion.<sup>2,3</sup>

**“What happens if I go over the lifetime exclusion?”** If that occurs, then you will pay a 40% gift tax on gifts above the \$5.25 million lifetime exclusion amount. One exception, though: all gifts that you make to your spouse are tax-free provided he or she is a U.S. citizen. This is known as the marital deduction.<sup>1,2,3</sup>

**“But aren’t the gift tax and the estate tax unified?”** They are. The gift tax exclusion and the estate tax exclusion are sometimes called the *unified credit*. So if you have already made taxable lifetime gifts that have used up \$3 million of the current \$5.25 million unified credit, then only \$2.25 million of your estate will be exempt from inheritance taxes if you die in 2013.<sup>3</sup>

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However, the \$5.25 million unified credit given to each of us is portable. That means that if you don't use all of it up during your lifetime, the unused portion of the credit can pass to your spouse at your death. So if you only use up \$1.25 million of your unified credit during your lifetime and your spouse has the full \$5.25 million credit remaining, your spouse would have the chance to transfer as much as \$9.25 million tax-free, either through gifts made during your life or after your death.<sup>3</sup>

In sum, most estates can make larger gifts during life without any estate, gift or income tax consequences. If you have estate planning questions in mind, turn to a legal or financial professional well versed in these matters for answers.

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#### **Citations**

- 1 - [www.chron.com/news/article/New-act-clears-up-estate-gift-tax-confusion-4301217.php](http://www.chron.com/news/article/New-act-clears-up-estate-gift-tax-confusion-4301217.php) [2/22/13]
- 2 - [www.nolo.com/legal-encyclopedia/changes-gift-tax-laws-coming.html](http://www.nolo.com/legal-encyclopedia/changes-gift-tax-laws-coming.html) [1/13]
- 3 - [www.forbes.com/sites/deborahljacobs/2013/01/02/after-the-fiscal-cliff-deal-estate-and-gift-tax-explained/](http://www.forbes.com/sites/deborahljacobs/2013/01/02/after-the-fiscal-cliff-deal-estate-and-gift-tax-explained/) [1/11/13]

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## Questions?

We'd Love to  
hear from you  
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