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How gifting can create tax-saving opportunities

Ideas to explore with your tax advisor

By Michelle Tucker
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Year end is a time for sharing with those we love and care about. At the same time, it's time to think about how much we will share with the IRS. Can you reduce your taxes by gifting to those you love? Here are some ideas to explore with your tax advisor.

Gifts to Your Family to Reduce Estate Tax

If your estate will be subject to estate tax, lifetime gifts will reduce both the size of your estate and your estate tax. There is a limit to this strategy. Each year, you can give no more than $12,000 to any one person. If you don't use the exclusion allowance for 2008, you lose it. Consequently, it might be wise to make a gift before the end of this year.

You can gift cash or property such as real estate and stocks. Gifting property other than cash has additional advantages.

Gifting property that will continue to appreciate during your lifetime will shift future appreciation to the next generation estate-tax free.

The capital gains tax consequences of property gifts should be carefully considered in light of the following rule: the recipient of gifted property will retain your tax basis for capital gains tax purposes, whereas the tax basis of inherited property is the date of death value. By retaining low basis property until you pass, the property's tax basis will step-up. While you are alive, it makes sense to gift high-basis property, particularly if your health is poor, and keep your low-basis property until you pass. If, on the other hand, you have assets that are worth less than your cost, the basis will step-down at your death. Consider selling these before you pass so you don't waste the loss deduction.

Gifts to Your Family to Help with Their Needs

Perhaps your gifts are not motivated by estate tax savings, but instead by a desire to help your children and grandchildren and parents. In this case, there are capital gains tax-saving considerations.

Often, family members who receive gifts are in a lower tax bracket. For the years 2008-2010, taxpayers whose marginal tax rate is 15 percent or below will pay ZERO tax on long-term capital gains. Here is your opportunity to gift appreciated property to a lower-income recipient who can sell the property to help pay for education or medical expenses, and pay zero federal capital gains tax. The threshold for the 15 percent bracket is a respectable taxable income of $65,100 for married taxpayers filing jointly.

You may have to limit this strategy to gifts to adult children and parents. Children under 19 and full-time students under 24 are subject to the "Kiddie Tax," which subjects their unearned income in excess of $1,800 to their parents' tax rate.

Remember this "Kiddie Tax" when deciding how to invest monies gifted to minor children and grandchildren. If their annual unearned income might exceed $1,800, consider tax-deferred investments instead of those that produce current income. Another college savings option is a 529 plan, which is not subject to the "Kiddie Tax." Earnings within a 529 plan escape both income and capital gains tax if the money is used properly.

The $12,000 annual gifting limit does not apply to qualified education expenses for your children or grandchildren or for their medical expenses and for those of your parents. You may have to make the payment directly to the educational or medical institution. Don't forget to claim the educational expense tax credits. You can deduct the medical (and nursing home!) expenses even if your child or parent is not your dependent.

Before making sizable gifts to children or parents, keep in mind that these gifts may some day make a student ineligible for college financial aid.

Gifts to Charity

Your appreciated property offers tax saving opportunities for charitable contributions. If you donate appreciated stock, you can deduct the full fair market value, but you have to have owned the shares for more than a year and you must give the stock certificates directly to the charity. Do not donate stock that has fallen in value — sell it, take the loss and donate the proceeds.

A tax advantage that expired at the beginning of this year has been reinstated. If you are age 70-1/2? or over, you can transfer up to $100,000 in income tax free directly from your IRA to a qualified charity. This contribution counts towards your RMD allowing you to reduce or even eliminate the tax that would normally be due (at ordinary income tax rates) on your RMD.

MICHELLE TUCKER Bio

Michelle Tucker is a Certified Financial Planner™, an attorney and a certified public accountant/Personal Financial Specialist. She is the first attorney in Hawaii to be certified by the American Bar Association (ABA) accredited Estate Law Specialist Board, Inc. as an estate planning law specialist, and is so certified by the Supreme Court of Hawaii. The Supreme Court of Hawaii grants Hawaii certification only to lawyers in good standing who have successfully completed a specialty program accredited by the ABA.

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