Debunking Six Gift Tax Myths

By: Stephen H. Gariepy

Everyone makes gifts, whether it's a birthday present motivated by love and affection or stock in the family business motivated by tax planning goals. The gift tax, when it applies, is a flat rate of 40%. But few know the ins and outs of the gift tax rules. Six prevalent myths deserve debunking.

Myth #1: The recipient of a gift must pay income tax on the gift. Generally, not true. There's a specific exclusion of gifts from income tax. And it makes no difference whether the gift is in the form of real estate, an automobile, jewelry, stock or cash. However, a gift by an employer to an employee is taxable income unless made entirely for personal reasons not related to past or future services.

Myth #2: The donor pays gift tax if annual gifts to a recipient exceed $14,000. Almost never the case. Although a donor is limited to an annual exclusion of $14,000 per recipient per year, a donor is also entitled to a large lifetime exemption, currently $5,490,000. For example, if a donor makes a $100,000 gift, the donor uses the $14,000 annual exclusion and $86,000 of the lifetime exemption. Further, the annual exclusion and lifetime exemption can be doubled for married donors if both spouses take the required steps to "split" their gifts. There's also an unlimited gift tax deduction for qualifying gifts to a spouse. So there's no excuse for skimping on your next anniversary present.

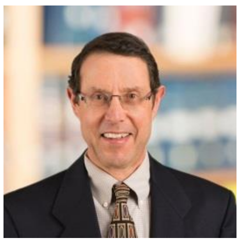
Myth #3: The lifetime gift exemption is a hard ceiling. The ceiling can be punctured. There are sophisticated estate planning strategies that can leverage the exemption many times over. There are even devices that can zero-out the gift tax on the future appreciation on large holdings. Just ask Sheldon Adelson (Las Vegas Sands), Mark Zuckerberg (Facebook), Lloyd Blankfein (Goldman Sachs), and Charles Ergin (Dish Network), who have transferred millions, even billions, free of gift tax.

Myth #4: A gift always saves estate taxes. Not with an estate exemption that matches the lifetime gift exemption of $5,490,000. Only one-tenth of one percent of estates are subject to estate tax in the first place. Moreover, if a donor dips into the lifetime exemption it's a wash because it reduces the estate exemption dollar-for-dollar. Ways a donor can come out ahead include leveraging the exemption, paying gift tax (the same 40% rate as the estate tax but it's tax-exclusive), taking advantage of valuation discounts for lack of marketability and control, shifting ownership but not income tax responsibility, and gifting assets that appreciate in value between the date of the gift and the date of death.

Myth #5: There's no tax disadvantage to making a gift. A trap for the unwary. In the case of a gift of an appreciated asset, such as stock, the recipient takes over the donor's low cost basis and the recipient pays capital gain tax on a later sale. On the other hand, if there is no gift and the stock passes on the donor's death to the recipient, the recipient takes a stepped-up basis equal to the stock's then market value and all pre-death appreciation escapes capital gain tax. Always compare the projected estate tax savings to the income tax cost.

Myth #6: The most important gifts are material. Not if we step back to look at the big picture. The most valuable gifts – family, friendship, health, the wonders of nature, peace – are priceless - and tax-free.

*Previously published in *Cleveland Jewish News*.



STEPHEN H. GARIEPY
HAHN LOESER & PARKS LLP
200 Public Square | Suite 2800 | Cleveland, Ohio 44114
p: 216.274.2224 | e: sgariepy@hahnlaw.com