



Lifetime Gifts

Overview

Many Americans make gifts to their children and other family members. Lifetime gifts may allow a donor to observe how donees will handle the money. Accordingly, the donor can help the recipient learn sound money or business management skills. Making lifetime gifts may require careful planning in light of gift and estate taxes.

Tax Implications

Federal Gift Tax Return

A donor must file a federal gift tax return for any year in which the donor makes a taxable gift. However, not all gifts are taxable for federal gift tax purposes. For example, the Internal Revenue Code excludes the following forms of gifts from a donor's taxable gifts: (1) "annual exclusion" gifts under IRC Section 2503(b); and (2) direct payment of educational and medical expenses under IRC Section 2503(e).

Annual Exclusion Gifts

Each year, a donor can give an unlimited number of donees each up to the "annual exclusion" amount (\$15,000 in 2018) without gift taxes. The amount is subject to increases due to inflation in future years. Through "gift splitting," both spouses can use their annual exclusions for a donee even if only one spouse actually transfers property.

Only gifts of a "present interest" are eligible for the annual exclusion. Gifts of a "future interest" are ineligible. If a recipient receives a gift with no strings attached, the gift is of a present interest. Generally, if there are conditions on the gift or if there is a delay in the enjoyment of the gift, the gift is a future interest gift. A gift to a trust is a gift of a present interest only if: (1) the beneficiary has the present right to trust income; (2) the beneficiary has a right to withdraw the amount of the gift from the trust; or (3) the trust is for the exclusive benefit of a minor and meets certain requirements.

- ◆ **Right to Income.** If a grantor creates a trust and gives a beneficiary a right to income, the gift of the income interest may qualify for the annual exclusion. The value of the gift will be the actuarial value of the income interest based on the term of the income interest, the size of the gift, and the prevailing interest rates. However, if the property transferred is not income producing, the IRS may argue that, for annual exclusion purposes, the value of the income interest cannot be measured, or is zero.
- ◆ **Withdrawal Rights.** In *Crummey v. Commissioner*, the Court of Appeals held that a gift to a trust is a gift of a present interest to the extent the beneficiary has a right to withdraw the gift. Hence, the right to withdraw a gift to a trust has become known as a "Crummey right," and a trust containing withdrawal provisions is referred to as a "Crummey trust." The IRS has agreed to the principle of the Crummey case, but imposes several requirements for a Crummey right to be effective. The courts have been more lenient than the IRS, but each case turns on its facts; therefore, in light of the time and expense of litigation, best practice would be to comply with the IRS's requirements. First, the trustee beneficiary should have actual notice of the contribution and his or her withdrawal right. In addition, the beneficiary must have a reasonable amount of time to decide whether to exercise the right before it lapses. Although there is no set number of days that qualifies as reasonable, the IRS has approved a withdrawal period as short as 30 days. While the withdrawal right should be effective at the time of the gift, the 30-day period typically commences upon the receipt of notice.
- ◆ **Minor's Trusts.** A gift to a trust for the benefit of a minor under age 21 can qualify as a gift of a present interest (and thus qualify for the annual exclusion) even without Crummey rights. The trust must either distribute income to the minor at least annually (as in a so-called "2503(b) Trust," referring to that section of the Code) or distribute principal to the beneficiary upon attainment of age 21 [as in a "2503(c) Trust"].

Gifts for Educational and Medical Expenses

Direct payment to the provider of qualified educational or medical expenses incurred by another does not constitute a taxable gift. The definition of educational expenses only includes tuition paid directly to the educational institution, not room and board, books, etc. As to medical expenses, IRS regulations describe exactly what types of expenses qualify as expenses for medical care.

Applicable Exclusion Amount

The "unified credit" allows a donor to avoid tax on a certain amount of gifts and transfers at death. After computing the tax on gifts in excess of a donor's annual exclusions, the donor can reduce the gift tax due by the amount of any remaining unified credit. At death, the executor of the decedent's estate will then reduce the amount of estate tax due by any unified credit not used during the donor's life.

The amount of assets the credit effectively exempts from federal gift and estate tax is the "applicable exclusion amount." The applicable exclusion amount for federal gift and estate tax purposes is \$11,180,000 during 2018, indexed for inflation thereafter. The entire amount can be gifted during life, if desired.



The Summit Group

Jerry Lorey*, ChFC®

405 Ashley Ridge Boulevard, Shreveport, LA 71106
Phone: (318)629-7500
jhlory@ft.newyorklife.com

*Registered Representative offering securities through NYLIFE Securities LLC, Member FINRA/SIPC, a Licensed Insurance Agency, (405 Ashley Ridge Boulevard, Shreveport, LA 71106). Financial Adviser offering investment advisory services through Eagle Strategies LLC, a Registered Investment Adviser. Member Agent of The Nautilus Group®, a service of New York Life Insurance Company. 0 is not owned or operated by New York Life Insurance Company or its affiliates.

This tax-related discussion reflects an understanding of generally applicable rules and was prepared to assist in the promotion or marketing of the transactions or matters addressed. It is not intended (and cannot be used by a taxpayer) for the purpose of avoiding any IRS penalties that may be imposed upon the taxpayer. 0 as well as New York Life Insurance Company, its agents and employees may not give legal, tax or accounting advice. Individuals should consult their own professional advisors before implementing any planning strategies. The Nautilus Group® is a service of New York Life Insurance Company.

This information was produced by New York Life Insurance Company and provided as a courtesy by Jerry Lorey. © 2015 New York Life Insurance Company. All rights reserved. SMRU 521232 (exp. 4.1.2019)

Jerry Lorey AR Insurance License Number 8032793 CA Insurance License Number 0L92307