Estate Planning and Wealth Preservation Practice Group

By: John S. King

Welcome to the Estate Planning and Wealth Preservation practice group of the Scolaro Law Firm. We are pleased that you have chosen to work with us to design and implement your estate plan.

Since our firm's inception more than 35 years ago, we have focused our practice largely on assisting our clients

- ✓ as they accumulate assets and grow their estates,
- ✓ as they develop and grow their businesses or professional practices,
- ✓ as they plan for the eventual disposition of their estates,
- ✓ as they plan for retirement,
- ✓ as they work to preserve their estates in light of the ever changing rules governing the imposition of income taxes as well as gift, estate and generation-skipping taxes,
- ✓ as they seek to protect their assets from the potential claims of creditors, and
- ✓ ultimately, as their estates are passed on to later generations or other beneficiaries.

Estate Planning and Wealth Preservation comprises the accumulation, conservation, and eventual transfer of one's wealth through the design and implementation of a comprehensive estate plan. Our overall purpose is to work with our clients and their other financial advisors to develop a plan that maintains the client's financial security and that of their families while at the same time facilitating the management of their assets during lifetime and the orderly and efficient transfer of their estates at death.

Many members of the firm's Estate Planning and Wealth Preservation practice group overlap their practices with our Business Practice Group and Employee Benefits Group. Estate Planning and Wealth Preservation practice group members are often involved in structuring new businesses, creating and implementing business succession plans and designing and establishing employee benefit plans.

Charitable Giving is often an important component of our clients' estate plans. Members of the Estate Planning and Wealth Preservation practice group have developed an expertise in all types of charitable giving including the creation of Charitable Remainder Trusts, Charitable Lead Trusts, Private Foundations and the use of Donor Advised Funds through local Community Foundations.

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ESTATE PLANNING BASICS

An Introduction to Estate Planning. The following is designed as a preliminary introduction to a number of important concepts and terms involved in the estate planning process. We hope that this information will provide you with an insight into the planning process as well as the vehicles and techniques that may be utilized in developing an overall estate plan for you and your family. This information is not, however, intended to be a substitute for specific legal advice which takes into account your unique financial and personal situation.

Probate and Non-Probate Property

For many people, the idea of "estate planning" means getting your Last Will and Testament (your "Will") in order. However, before beginning any conversation about estate planning it is important to understand that your Will controls the disposition of only certain of your assets (your "Probate" assets). In order to have a comprehensive estate plan it's important to consider the disposition of your other assets (your "Non-Probate" assets) since they are controlled by documents or legal arrangements other than your Will.

Examples of "Probate" assets might include: Assets owned by *you, alone,* such as Marketable Securities, a Bank or Brokerage Account, your Home, an Automobile or an interest in your Closely-Held Business. In most cases, these assets make up your "probate estate" and are disposed of in accordance with the terms of your Last Will and Testament.

Most of us, however, also own assets that are disposed of under the terms of a document other than our Will or by some other legal arrangement. Examples of "Non-Probate" assets might include a policy of Life Insurance on your life that is controlled by a *beneficiary designation*, a parcel of Real Estate or a Bank Account that is owned jointly with someone else and which passes to the surviving owner by a *right of survivorship,* or an IRA or other Retirement Plan that is also controlled by a *beneficiary designation.* Another increasingly common type of non-probate asset is a *Revocable Trust* (sometimes referred to as a "Living Trust") to which you may have transferred some or all of your probate assets during your life. Revocable Trusts will be discussed in greater detail below.

Proper estate planning requires that your advisor have a thorough understanding of all of your assets, including both probate and non-probate assets.

Potential Pitfall – Joint Ownership of Bank Accounts

For decades, people have titled bank accounts in joint names with a child or other trusted individual as a way of making sure that some funds remain readily available in the event of the original owner's death or to facilitate the management of the funds upon the original owner's incapacity. Keeping a modest bank account in joint names with a trusted child or friend can be very helpful during lifetime and at death. However, such joint ownership has the potential to create significant problems and should not be considered an adequate substitute for a well thought out and implemented estate plan. Understand that *legally*, upon the death of the original owner, the other individual now owns and controls the bank account *and can do with it whatever they choose*. If the funds are used by the surviving owner (a child, for example) to pay the decedent's funeral bill or other estate administration expenses there may not be a problem. However, the child may take the position that the joint bank account was intended as an inheritance, left to him or her because Mom or Dad wanted to say "thank you" for helping out and instead of paying the funeral bill buys a new car.

Potential Pitfall – Informally Prepared Beneficiary Designations

Properly prepared beneficiary designations - for life insurance and retirement plans in particular - are an important component of any estate plan.

In the past several years, however, it has become possible to name a beneficiary of assets that traditionally have not been disposed of through a beneficiary designation. In particular, individually owned securities accounts can now have a beneficiary designation (often referred to as a "transfer on death" designation). While this may be an appropriate way of disposing of one's assets, the addition of a beneficiary to a securities account typically occurs when the account is opened and without the account owner giving much, if any, thought to the effect a "transfer on death" designation will have on his or her estate plan.

As part of your overall estate plan, you should confirm whether you have named a beneficiary or included a transfer on death designation on any securities accounts you own. If you have, then as part of your estate plan we should confirm that this disposition remains appropriate and is consistent with your overall plan.

Even when your beneficiaries recognize that joint ownership, a beneficiary designation or transfer on death instruction was inadvertent and they wish to "do the right thing" and abide by what they believe to be your estate plan (as evidenced by your Will) it may be very costly and time consuming to accomplish the necessary changes after your death.

IMPORTANT ESTATE PLANNING DOCUMENTS

Last Will and Testament. For many clients, the bedrock document governing their estate plan is their Will. Your Will directs the disposition of your probate assets upon your death. Your Will can identify individuals or organizations that you want to single out to receive a specific bequest or other legacy. Your Will disposes of your personal effects along with all of the remaining assets of your probate estate, outright to the beneficiaries, in further trust for the beneficiaries or in some combination of the two. Your Will is the document in which you designate a Guardian for minor children, appoint Executors to administer your estate and appoint Trustees to manage any continuing trusts created by your Will.

Your Will does nothing to control your assets while you are alive. So long as you are competent you can change your Will at any time and for any purpose. *Remember, however, that your Will does not control the disposition of your non-probate property.*

<u>Revocable Trust or Living Trust</u>. In many respects, a revocable, or living trust takes the place of or works in conjunction with your Will. It is a useful tool that can simplify estate administration, avoid the probate process and ease the lifetime management of your property if you become incapacitated. By avoiding the probate process, Revocable Trusts also offer a level of privacy that Wills do not. When a person dies, his or her Will is submitted to the Court for probate at which point it becomes a public document, available for review by anyone at any time. Moreover, through the probate process certain family members must receive notice of the probate proceeding – whether or not they have any financial or other interest in the decedent's estate. A Revocable Trust does not require court involvement at your death so, generally, it does not become a public document and in most cases only those family members or others who benefit receive information about your estate. It is important to note that a Revocable Trust offers no tax advantages over a Will, and that you must transfer all of your probate property to your Revocable Trust during your lifetime in order to effectively avoid probate.

Revocable Trusts are typically designed for your benefit alone during your lifetime. You may *revoke, modify* or *amend* the trust so it remains an extremely flexible instrument. *However, because you retain complete ownership and control of the Trust, it does not provide any protection from creditors nor are the assets of the Revocable Trust ignored or exempted in determining your eligibility for governmental benefits such as Medicaid.* Nevertheless, with proper planning and lifetime funding, a Revocable Trust is a convenient tool for managing property at death as well as during life, especially in the cases of incapacity or a long illness.

In conjunction with a Revocable Trust, a "pour-over" Will is recommended. A pour-over Will is the common term for a simple Will which, upon death, controls the disposition of you *probate* property by directing such property be given to the Trustees of your Revocable Trust to be disposed in accordance with the provisions of such trust. The pour-over Will is a necessary tool designed to "catch" any assets which may not have been transferred to your Revocable Trust during your lifetime.

<u>ANCILLARY ESTATE PLANNING DOCUMENTS</u>

<u>Durable General Power of Attorney</u>. A Durable General Power of Attorney is a document in which you designate someone

(your "Agent") to help manage your legal and financial affairs during your lifetime. A Power of Attorney can be designed so that it is effective immediately upon signing or, alternatively, so that it is effective only if you become incapacitated. Under a Power of Attorney you can grant to your Agent the authority to do virtually anything that you can do including modify your estate plan and transfer your assets. Obviously, the choice of Agent(s) and the powers they are given is an important aspect of your overall plan. You can appoint multiple Agents and you can direct that they must work together or permit them to act independent of one another. If you don't have a Durable Power of Attorney and become unable to handle your own legal and financial affairs it may be necessary to go through a lengthy Guardianship proceeding in order to have the Court appoint a Guardian to act on your behalf.

<u>Health Care Power of Attorney or Health Care Proxy</u>. Like a General Power of Attorney, a Health Care Power of Attorney or Health Care Proxy permits you to designate an Agent to make Health Care decisions on your behalf when you are unable to make such decisions for yourself. By naming a Health Care Agent you are arranging your affairs so that if you become incapacitated someone of your choosing (typically a spouse, child or other close family member) is making health care decisions for you rather than having the Court appoint a Guardian for you to make these decisions. Only one Agent should be appointed at a time under your Health Care Proxy so that your treating physician or medical facility can deal with a single individual rather than a "committee".

<u>Living Will</u>. A Living Will is the document which, in conjunction with your Health Care Proxy, gives your Agent guidance as to your wishes regarding end of life decisions.

<u>PLANNING FOR LONG-TERM CARE</u>

One question that comes up more and more frequently in our estate planning practice is: "If I have to go into a Nursing Home does my Will/Revocable Trust protect my assets from Medicaid". The short answer for most of our clients is "No"; a typical estate plan does nothing to help you qualify for Medicaid. Your plan may, however, minimize Medicaid issues for your heirs.

Traditional Medicaid Planning ("How can I qualify for Medicaid?") is an area of the law separate from, although in many ways quite similar to, estate planning. It involves the transfer of assets and many of the same documents (such as Wills, Trusts, Powers of Attorney etc.) but is designed so that you intentionally impoverish yourself in order to qualify for governmental assistance, usually to help pay the costs of a Nursing Home or other long-term medical care.

Few of our clients come to us to undertake traditional Medicaid Planning. Instead, those who have a Medicaid issue are usually concerned about an aging parent, or are looking to protect a particular asset (such as a generations old family farm or vacation home), provide for an already disabled spouse or child, or to add a layer of additional protection to assets that they are passing on to a surviving spouse or children who may become disabled in the future.

For our younger, healthier clients, *Long-Term Care Insurance* may be an appropriate way to provide funds to help defray the cost of a Nursing Home stay or other long-term medical care. Although considered by many to be expensive, long-term care insurance may provide a level of security and flexibility that makes it well worth the price.

If you have Medicaid Planning concerns they should be brought up early on in the estate planning process since they may significantly impact how we can implement your estate plan.

TAXES

THE FEDERAL ESTATE, GIFT AND GENERATION-SKIPPING TAX

Over the past 30 years or so our federal Estate and Gift tax system has gone from taxing a decedent's "taxable estate" *in excess of $600,*000 at rates of up to *55 percent* to now imposing a *40 percent* tax on taxable estates once they exceed *$5,430,000 (or $10,860,000 for a married couple)*. Not surprisingly, the possibility of federal Estate or Gift tax being imposed on any particular estate has become less likely and, in many cases is no longer the driving force behind estate planning.

Federal Applicable Exclusion Amount (or "Unified Credit"). The federal tax law provides for a transfer tax credit which currently has the effect of allowing an individual to transfer property worth $5,430,000 during lifetime or at death.[1] Unlike under previous law, assets worth this entire amount can be transferred during your lifetime without paying any gift tax. This figure is referred to as the "applicable exclusion amount" or sometimes the "unified credit". Each person is entitled to this exclusion. Therefore, in the case of a husband and wife, property valued at more than $10,800,000 can be transferred free of federal estate and gift taxes. Under prior law, if an individual failed to utilize his or her exemption amount it was lost. However, since 2011, the amount of the applicable exclusion amount not otherwise used by the first spouse (either during lifetime or at death) is transferable to the surviving spouse to be used during his or her remaining lifetime or by the survivor's estate. This so-called "portability" has made it easier to avoid the loss of the unified credit in the "less wealthy" spouse's estate if he or she is the first to die.

Generation Skipping Transfer Tax. Operating in conjunction with the federal estate and gift tax system is a second tier of tax called the generation-skipping transfer tax ("GST"). As the name implies, this system imposes a tax on transfers made during lifetime or at death that "skip" generations. When applicable, the GST is imposed at a flat rate equal to the highest federal estate tax rate -- currently 40%.

The GST system was designed to plug perceived "loopholes" in the estate and gift tax system. It is the intent of Congress that transfers of property be taxed once at each generational level. To illustrate, if a parent makes a transfer to a child, that transfer is subject to estate or gift taxation at the parent's level. If the child subsequently makes a transfer to a grandchild, the transfer is again subject to estate or gift taxation at the child's level. If, however, the grandparent makes the transfer directly to the grandchild (thereby *skipping* the child) the transfer, prior to enactment of the GST system, would be subject to tax only at the grandparent's level. As a result of the enactment of the GST, if the grandparent transfers assets to a grandchild, an estate or gift tax *and* a GST tax potentially apply at the grandparent's level.

In an attempt to "soften the blow" of the GST for less wealthy individuals the GST system is designed with several exceptions, the most important of which is the Generation-Skipping Transfer Tax

[1] Note that this amount is indexed for inflation and has grown by nearly $100,000 per year since the exclusion amount was first increased to $5,000,000.

exemption (currently equal to the applicable exclusion amount of $5,430,000 and indexed for inflation). Using the GST exemption, an individual can make generation-skipping transfers of assets worth $5,430,000 to grandchildren or lower generation individuals (or to trusts for the benefit of such individuals) without incurring the GST. *It should be noted that unlike the applicable exclusion amount for estate and gift tax, there is no "portability" of the GST exemption between spouses.*

Unlimited Marital Deduction. In addition to the applicable exclusion amount, an unlimited estate or gift tax deduction is allowed for qualified transfers to a spouse. This is known as the "marital deduction". The marital deduction allows transfers of assets between spouses without concern that a transfer tax may be imposed and to allow a couple to postpone the imposition of transfer taxes until the death of the second spouse to die. The unlimited marital deduction is available for lifetime gifts as well as transfers occurring at the first spouse's death.

In effect, the unlimited marital deduction allows one spouse to transfer to the other his or her entire estate free of any estate tax at the first death. In a situation where the combined assets of the husband and wife are not likely to exceed the applicable exclusion amount for either spouse (or, with "portability", the combined exclusion amount for both), from a purely "estate tax" standpoint an estate plan that leaves everything outright to the surviving spouse may be appropriate. Before implementing such a plan, we recommend that you consider a number of *non-tax* issues, such as the plan's effect on the ability to minimize the costs of long-term medical (or Nursing Home) care or the exposure of individually owned assets to the claims of potential creditors.

Under current law, if the applicable exclusion amount and the unlimited marital deduction are properly incorporated in the estate plan, property worth more than $10,800,000 can ultimately be transferred to the children or others free of federal estate tax.

NEW YORK ESTATE AND GIFT TAX

New York's Limitation. The state of New York limits the applicable exclusion amount to $3,125,000. Thus, at the present time, the federal and New York exemption amounts do not coincide. However, the New York exemption amount is scheduled to increase over the next several years so that it will coincide with the federal applicable exclusion amount by January 1, 2019. There is no so-called "portability" of the New York exemption amount so the tax planning for a married couple with assets greater than the New York exemption amount but less than twice the federal exemption amount is more complex. New York does not have a gift tax as such although gifts made within three years of death and before January 1, 2019 will be brought back into the decedent's estate for purposes of calculating the New York tax.

INCOME TAX vs TRANSFER TAX

Until recently, a well-designed estate plan often involved a tradeoff between the desire to minimize estate, gift and generation-skipping taxes and the eventual imposition of income taxes. At a time of relatively low transfer tax exemption amounts and when federal transfer tax rates reached a maximum of 55 percent while ordinary income tax rates were around 40 percent and the tax on capital gains was only 20 percent or less, such a tradeoff seemed appropriate and was acceptable to most.

As recently as 2011, there was real concern that the federal estate and gift tax applicable exclusion amount would return to the prior level of $1,000,000. However, with the "permanent" introduction of an indexed $5,000,000 applicable exclusion amount and with similar increases in the New York exemption, estate tax concerns have disappeared for many. At the same time, federal income tax rates may again exceed 40 percent and there is also the recent enactment of the 3.8 percent "net investment income" tax so that the prior tradeoff may no longer be worthwhile.

Perhaps the most important income tax distinction to make between various planning opportunities is the potential capital gains tax consequences of any proposed plan.

Under current law, if an individual dies owning an asset which is later sold by his beneficiaries, for purposes of computing the capital gain recognized on the sale the beneficiaries look to the value of the asset at the deceased owner's date of death and compute the gain as the difference between that value and the amount realized on the sale. Alternatively, if that same asset had been given to the beneficiaries during the deceased owner's lifetime and sold *before or after* the prior owner's death, the beneficiaries look to the amount paid for the asset by the prior owner and compute the gain as the difference between that value and the amount realized on the sale.

As an example, if Dad purchased 100 shares of stock for $10 per share, his *basis* for determining gain or loss when he sells the stock is $10 per share or $1,000 ($10 x 100 shares). If at Dad's death the stock is worth $50 per share and is *inherited* by his children who later sell it for $50 per share, the children will have no capital gain since their basis in the stock is "stepped-up" to $50 (the stock value at Dad's death). If, instead, Dad had given the stock to his children while he was alive their basis would be $10 per share and when they eventually sell it for $50 per share they will have a capital gain of $40 per share ($50 sale price minus $10 basis) or $4,000.

Assuming Dad's estate is large enough to pay estate tax at the current 40% federal rate and that the children will pay capital gains taxes at a 20% federal rate, there may is still be a significant tax savings to be realized if Dad gives the stock away during his lifetime despite the fact that the children will pay a capital gains tax when they sell the stock. At 40%, the stock would be subject to estate tax of $2,000 ($5,000 estate tax value x 40%) in Dad's estate. If Dad gives the stock to the children who later sell it for $5,000 they would have a gain of $4,000 ($5,000 sale price minus $1,000 basis) and would incur a capital gains tax of $800 ($4,000 gain x

20%). Compared to the estate tax, this is a tax savings of $1,200. Moreover, the estate tax is due 9 months following the decedent's death whereas the capital gains tax only becomes due after an asset is sold. In effect, the beneficiaries have no control over when the estate tax must be paid but they generally have complete control over when or if they want to recognize the capital gain and pay the capital gains tax.

On the other hand, if in the above example it is unlikely that Dad's estate will be subject to estate tax (presumably because it will be below the federal and/or New York exemptions) a lifetime gift of the stock would be inappropriate from a purely tax standpoint because the basis adjustment available at Dad's death would eliminate the capital gain when the children sell the stock, thus saving $2,000. With the advent of the 3.8% additional tax on net investment income it is possible that capital gains will be subject to federal tax alone at 23.8% making the basis adjustment a death even more valuable.

The basis adjustment at death also has the beneficial consequence of giving *depreciable* property new basis that can again be depreciated by the new owners thus reducing their income taxes

In choosing the appropriate estate planning strategies and the assets to be utilized in the planning, it is important to consider the potential income tax consequences and weigh them against the transfer tax benefits of the proposed plan.

OTHER ESTATE PLANNING ISSUES

Transfers of an Inheritance "In Trust". There are substantial tax and non-tax benefits to having your heirs receive all or a substantial portion of their inheritance in trust.[2] To briefly note the major items, consider the following:

Non-Tax Advantages of an Inheritance in Trust:

1. The assets in a trust are not subject to the claims of the creditors of the beneficiary.

2. The assets in a trust are not subject to marital division in the event of divorce, separation or, in most circumstances, other financial settlements between beneficiaries and their spouses.

3. In the event the trust beneficiary dies, you can, if you wish, direct that the trust assets will pass to particular beneficiaries according to your wishes. For example, if a beneficiary dies, you can provide that the trust fund will continue for the benefit of that beneficiary's children, and the assets may not be diverted to the spouse of a beneficiary who may subsequently remarry or wish to provide for later born children. Similarly, you can grant to the beneficiary the authority to direct how the remaining assets will be distributed at his or her death, within the constraints you determine.

4. The assets in a trust can provide a financial security net for the beneficiaries. Thus, even though a beneficiary may have invested his or her own assets imprudently or have poor experience in business, the assets in the trust continue to be available to provide for basic needs such as food, clothing and shelter.

Tax Benefits of an Inheritance in Trust:

1. A trust can be designed so that no estate tax or generation-skipping tax is imposed upon the Trust assets at your beneficiary's death and at the deaths of beneficiaries in subsequent generations.

2. Distributions from a trust can be made among several generations of beneficiaries such as to a child *or* grandchild whereas if the assets are given outright to the child, later transfers to the grandchild could constitute taxable gifts from the child to the grandchild.

Subject to fairly narrow constraints designed to protect trust assets from creditors and transfer taxes, a trust can be designed to give the beneficiary as much *or as little* control over the trust as you wish.

Choice of Fiduciaries. The development of an estate plan not only involves the analysis of your assets and family situation, but also the identification of individuals or institutions capable of seeing to it that your wishes are observed. Typically, an individual will name one or more *Executors* to handle estate administration as well as one or more *Trustees* to handle the administration of any ongoing trusts. In addition, if you have minor children the appointment of one or more *Guardians* is typically handled through your Will or Revocable Trust.

[2] Note that the type of trust referred to here is not a Revocable Trust as described above and thus has tax and other consequences that are much different from those described in the section on Revocable Trusts.

Executor. The job of an Executor is to "settle" your estate. Your Executor collects your assets, pays any outstanding debts, files any necessary tax returns (including income, estate and gift tax returns), pays any tax due and, upon termination of the estate, distributes the remaining assets of the estate as you directed under your Will or Revocable Trust.

Generally, individuals name as Executors close family members (such as a surviving spouse or child), close friends, business associates, professional advisors and/or financial institutions. As a general rule it is not necessary to appoint an individual who possesses all of the technical expertise needed to settle an estate. The named executor may hire the professional advice needed to guide him or her with respect to the requirements of appropriate estate administration.

We recommend that you name a successor Executor in addition to the primary Executor in order to avoid the necessity of a court proceeding in the event the first named Executor is unable to serve.

If you use a Revocable Trust, you are often the sole Trustee during your lifetime. However, it is important, at the time the trust is created, to designate a "successor Trustee" to administer the trust upon your death or incapacity. Many times, the person you would name as Executor is the logical person to be named as successor Trustee of your Revocable Trust.

Trustee. The job of a Trustee is to "administer" a trust in accordance with its terms. Usually, the Trustee is responsible to oversee the investment of trust assets and to make decisions regarding the distribution of trust income and principal to or for the benefit of the trust's beneficiaries.

Trustees may be given narrow or broad discretion in deciding how, when and in what amounts distributions will be made from a trust. Accordingly, it is important to name individuals or institutions in whose judgment you have a great deal of confidence. We recommend that you also provide a mechanism for the removal and replacement of Trustees in the event a Trustee becomes disabled or is unresponsive to the needs of the trust's beneficiaries. Moreover, since many trusts are designed to last for a period that may extend well beyond any one individual Trustee's lifetime, a mechanism to provide for long-term Trustee succession is important.

Trust Protector. Frequently, a Trust Protector is named so that there is someone in place who can facilitate Trustee succession without the necessity of an extended Court proceeding. A Trust Protector may be granted the authority to remove a Trustee, to designate an additional Trustee or successor Trustee in order to fill a vacancy in the office of Trustee if one arises. In most circumstances, the Trust Protector has no responsibilities unless and until a problem arises with a Trustee, between the Trustees or between the Trustee(s) and a beneficiary.

For example, if a disagreement arises between a beneficiary and a Trustee over access to or investment of trust funds, without a Trust Protector the beneficiary's only recourse might be to seek judicial intervention and the removal of the

Trustee. This can be a costly, time consuming and public action, and the results may not be to the beneficiary's liking. It is unusual for a court to remove a Trustee unless the Trustee has acted dishonestly or in bad faith. If a Trust Protector is appointed, however, he or she can remove and replace the Trustee without court involvement or may intercede as a moderator in an effort to settle the disagreement between the beneficiary and Trustee.

We recommend that a successor Trust Protector be named and/or that a procedure be put in place whereby someone or some group of people are authorized to name a successor in the event of a vacancy in the Trust Protector's office.

The design of the Trustee and Trust Protector succession provisions depends in large part on your willingness (and the appropriateness) of empowering one or more of your beneficiaries in this respect.

<u>Lifetime Gifts – the "Annual Exclusion"</u>. An important method of reducing the exposure to the estate tax is by making lifetime gifts.

Annual Exclusion Gifts. Under current gift tax law, you can make annual gifts of cash or other assets worth up to $14,000 per donee to as many people as you desire. A married couple can double this amount by either each making gifts or by one making the gift and the other, on a properly filed gift tax return, agreeing to "split" the gift so that it is treated as having been made one-half by each spouse. Whether through direct or "split" gifts, a husband and wife may give up to $28,000 a year to each of their children and grandchildren or to anyone else to whom they wish to make gifts. A regular program of gifting over a period of years can significantly reduce your taxable estate. These gifts can be made outright or, with proper planning, to a trust for the benefit of one or more donees.

Annual exclusion gifts fall entirely outside of the estate and gift tax system, and, in certain circumstances, the GST tax system. Thus, through the use of lifetime annual exclusion gifts, you can reduce the exposure of your estate to transfer taxes without using your applicable exclusion amount. Moreover, by gifting assets that generate income or that you expect will appreciate in value, you have also removed the future income and/or appreciation from your estate. Recall, however, that gifted assets will not receive a "step-up" in basis at your death so your beneficiaries may eventually pay a larger capital gain tax if and when the asset is sold. If your estate is not likely to be subject to estate tax (federal or New York) the potential for negative income tax consequences resulting from lifetime gifts of low basis assets may outweigh any reason to make the gift.

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