CHAPTER SEVEN – Gift Strategies

Reasons for and against making lifetime gifts:

**Pro:** Tax savings (federal income, gift and estate taxes); possible state income tax savings (in other jurisdictions than Texas)?

Shifting wealth to younger generation(s).

**Con:** Loss of control over the funds or property; possibly “inadequate” (?) resources to enable the donor to pay expenses in later life, e.g., expenses of one’s “last illness;” concern of the behavior of donee.
Choosing the Gift Property

Strategies in picking the potential gift property:
1) High tax basis property (including cash).
2) High appreciation potential property.
3) Discount/reduced valuation possibilities –

Note the Pierre case (2009) where a single member LLC was created and funded and then the LLC interests were transferred (gifts & sales) to trusts for child/grandchild; discounted values on the LLC interests for gift tax purposes. Beneficial use of an “LLC wrapper.”
Income Tax Basis Considerations

Code §1015 specifies a transferred tax basis for gifts, except for loss property (in certain situations). Why?

How choose loss property for making gifts?

What treatment if the property appreciates significantly after the gift transfer?

Note the Code §1015(d)(6) adjustment for gift tax attributable to the appreciation portion.

What order for gifts? Cash first (if § 1015(d)(6) is applicable)? No tax basis increase for cash.
Identifying a “Gift” for Gift Tax Purposes
See Reg. §25.2511-1(a) & (c)(1) re gratuitous transfers of wealth & gift tax exposure.
Reg. §25.2511-1(g) re no donative intent necessary to complete a gift. Cf., objective facts.
Determining amount re formula – permissible?
See Wandry case, note 6, p. 5.
Cf., “gift” concept for income tax & Duberstein.
Rev. Rul. 77-372, p. 5 – transfer to equalize estate distributions (i.e., “hotchpot”); gift treatment when equalization contribution made (i.e., in excess of the state law requirement).
Identifying a “Gift” for Gift Tax, cont.

Family settlement arrangement?
Cancellation of debt.
Payment of another’s liability, including on a life insurance policy.
Interest free loan - §7872 - low/no interest debt.
Excessive salary to child-employee.
Gift by a closely-held corporation to children?
Payment for child’s wedding?
Excessive trustee’s fees paid to children?
Contributions to a §501(c)(4) organization?
Gift Completion Considerations

Non-trust transfers, e.g., a check or negotiable instrument – when is the transfer complete? See Rev. Rul. 67-396, p. 10; RR. 84-25, p.11.

Gift of a U.S. Treasury bond?

Joint checking or savings account?

Gift of corporate stock or mutual fund shares?

Is a record transfer necessary to complete gift?

Does a gift occur when one spouse pays all the FIT liability for a particular year? P.11

Gift of a promissory note (whose note)?
Gifts made Under Durable Power of Attorney p.12

Can a gift be made on behalf of a principal by an “attorney in fact” for that principal?

How document the capacity to make a gift?

What federal estate tax effect results if no legal capacity exists to make the gift? Code §2038.

What is the responsibility of the executor?

See Texas Estates Code §1162.001 (p.14) re possible Texas court authorization for a guardian to make gifts for federal gift tax and estate tax planning purposes.
Transfers into a Trust & Gift Completion Issues

Rev. Rul. 77-378, p. 15 – completed gift occurs even where the independent trustee can distribute P&I to the grantor in the trustee’s discretion; cf., Rev. Rul. 62-13 (p.17).

See Reg. §25.2511-2(c) (p.17) - an incomplete gift results when the donor has power to change interests among beneficiaries in the trust.

Cf., Reg. §25.2511-2(d) where donor’s retention of only a right to determine time when a beneficiary is to receive from trust. Cf., Lober.
Gift Transfers to a Grantor Trust (IDGT) p.18

Completion of a gift for gift tax purposes but not for income tax purposes. Three situations re Grantor’s income tax: 1) No reimbursement; (2) Required reimbursement; (3) Discretionary reimbursement by Trustee.

Rev. Rul. 2004-64 – holding payment of income tax by the grantor is not a gift to the trust. But, inclusion in the gross estate (under Code §2036(a)) if the grantor retains right to be reimbursed by the trust (Situation 2 in ruling).
Notice 2010-19
p.22

IRC §2511(c) provides that a transfer in trust is treated as a gift transfer unless the trust is treated as wholly owned by donor under Subpart E.

What does §2511(c) and this IRS Notice accomplish?
Annual Donee Gift Tax Exclusion  p.23

Code §2503(b) – annual donee exclusion in amount of $14,000 (for 2014, i.e., the $10,000 amount as indexed for inflation).

Limited to gifts of a “present interest.” Must be a right to a substantial present economic benefit. What about a gift of a growth stock paying no current dividends?  P. 23.

See Rev. Rul. 76-360, p. 24, re effect of a “restrictive agreement” after a “statutory merger.” Note the possibility of an annual donee exclusion for only the “income interest” component (p.25).
Other Possible “Present Interest” Limitations

1) Older shareholders forgive debt owing to them from a closely held corporation – thereby enhancing the value of all shares, including those owned by younger minority shareholders. Stinson case, p. 25.

2) Gift of limited liability company (LLC) or LP interests to younger generation donees (where restrictions apply on the transfer of the ownership interests). P.26 (Hackl)
Rev. Rul. 77-358
p.26

Transfers to irrevocable trusts where the trustee could:
1) Apportion receipts and disbursements;
2) Allocate gains and losses to income;
3) Invest in current income assets.

Gift of income interest only; reversion to the grantor.

Problem with the potential diversion of income to the corpus with the loss allocation power. The income right was not ascertainable & no “present interest.”
Use of a “Crummey” Power  

Does a right of withdrawal, even though not exercised, facilitate “present interest” status for a property transfer?

How can a donor “leverage” the annual donee exclusion? Are contingent interests OK for the exclusion? See the Cristofani case, p. 28.

Note the “reciprocal gift” limitation, p. 28.

What is the appropriate treatment for enabling annual donee exclusions? See the JCT “Options” paper (2005), p. 29, with choices re restricting the Crummey power.
Gift Splitting Between Spouses

Code §2513 authorizes gifts made by one spouse to be treated as made ½ by each spouse. How stagger gifts to other beneficiaries when one spouse has more assets than the other? Is Code §2513 even relevant in a community property jurisdiction (e.g., Texas)? If so, under what circumstances?
Gift Tax Marital Deduction

p.33

Code §2523 provides for an unlimited marital deduction for gifts to a spouse.

Code §2523(b) provides that the deduction is not available when a “terminable interest” is transferred to the spouse. Why?

Exception for transfer to QTIP trust. §2523(f).

See Code §2523(i) re $100,000 limit (indexed) on marital deduction gift to non-U.S. citizen spouse. Why this limit? Why not an unlimited deduction?
Gifts within Three Years of Death

Code §2035(a)(2) inclusion in gross estate where termination (within 3 years of death) of a “retained power” (see §§2036-2038 & 2042).

What about transfers made from a “revocable trust” made within 3 years of death? See PLR 9343003, p. 34. Characterized as withdrawals for this rule? See treatment under §2035(e).

And, inclusion of the gift tax amount in the gross estate – Code §2035(b). P. 37.