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'Tis the season to give assets to loved ones ... and dodge estate taxes

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The economy is in a temporary mess with home prices diminishing and the stock and bond market falling. Yet, for anyone with a federal estate tax issue potentially at his or her death, this is a good time to give as many assets as one can. This is one of the best opportunities to transfer wealth to younger generations, without incurring the federal estate tax in the process.

The federal system for estates and gifts is a combined system. A person is able to give an annual gift of $12,000 per donee (or $24,000 if that person's spouse shares the gift). If the value of the gift exceeds the $12,000 amount, the portion above that amount uses up part of the lifetime exemption amount.

In 2001, Congress had changed the law in this area, which increased the amount that an individual could leave to someone other than their spouse without incurring the federal estate taxes. This amount is $2 million today, which is scheduled to increase to $3.5 million in 2009.

The federal estate tax, according to the 2001 law, is scheduled to disappear in 2010 (estates will not receive the stepped-up basis of fair market value as of date of death, and thus pay capital gains taxes instead), and will reappear in 2011 with a $1 million amount. There is also one additional rule in which you cannot give more than $1 million during your lifetime without incurring a tax on the gift.

This is the current state of the law, which will be changed by the new Congress when they are sworn in next year. During the political campaign, both candidates stated they wished to leave this lifetime exemption at a higher amount than $1 million. President-elect Barack Obama said he wished to make the lifetime exemption at $3.5 million and leave the tax rate at the current rate of 45 percent.

As no tax professionals believe the federal estate tax system will be abolished anytime soon, most planning involves the transfer or gift of property from one generation to the next with the least tax cost. Because of the temporary diminished prices on stocks, bonds and real estate, this is a great time to consider making gifts of those assets, which will allow the recipient of the gift to enjoy the rebound in price when it occurs.

Another thing you can do is to pay the tuition and medical bills for your children or grandchildren with no tax consequences to federal gift or estate taxes.

In addition, as the interest rates are down now, this makes many other techniques in giving more to your heirs much more attractive. It is more appealing now to use family loans, grantor retained annuity trusts, an intentionally defective grantor trust or a charitable lead trust, which will allow you to give more to your heirs than you would have been able to when rates were higher. These tax techniques rely on an interest rate that the government sets monthly, called the applicable federal rate, which is set lower than the rates that you might see for a 30-year mortgage.

Because of the above, there are great opportunities to transfer your wealth to the next generation. If you are one of the people who may otherwise have to pay federal estate taxes at your death, consider contacting your estate planning attorney to determine your best course of action to limit your exposure to this tax.

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