

# Doing Good and Doing It Right: Los Altos CF Class #3



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# Los Altos CF Class Series



- ***1- Estate Planning Basics*** – The Basic Documents and Why You Need Them.
- ***2-Fine-Tuning Your Estate Plan*** – Distributions at Death.
- ***3-Doing Good and Doing it Right*** – Distributions During Life- June 27, 2017



# Today's Topics



- Understanding gift and estate taxes.
- Learning about smart ways to give to loved ones.
- Learning about smart ways to give to charities.

# Gift and Estate Taxes



- **Gift Tax** applies to gifts made during life.
- **Estate Tax** applies to gifts made after death.



# Estate and Gift Taxes Are Connected



- ▶ Estate and gift tax exemption equal to passing \$5.49 million/per person **during life or at death** (indexed to inflation).
- ▶ This only includes gifts made during life that exceed \$14,000 per year.
- ▶ Reported gifts count towards your lifetime exemption.



# Gifts Are Cumulative



- ▶ Gifts can be made during life or after death: reported gifts are cumulative.
- ▶ No gift or estate tax is due until you use up the exemption amount.

*Think of the exemption like a sports clock with a lot of time.*

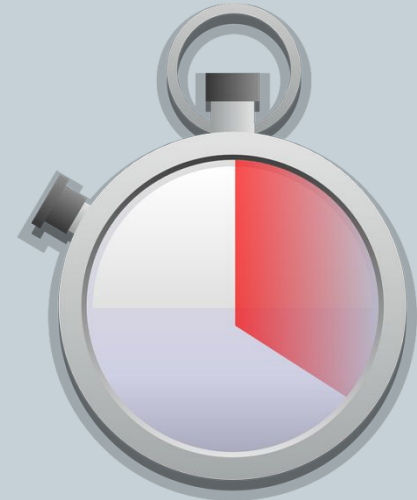


# At Death We Add Up Prior Gifts



- ▶ When someone dies, we total up their reported lifetime gifts to see what exemption amount is left.

Reported Gifts	
2014	\$100,000
2016	\$200,000
Total Exemption Used	<b>\$300,000</b>
Total Exemption Left 2017	<b>\$5.19 Million</b>



# Annual Gifts Don't Count



- ▶ You can make annual gifts during life that don't use up *any* time on that clock.
- ▶ ANNUAL GIFTS of \$14,000 per donee do not have to be reported.
- ▶ Like a checkbook each year for gifts up to \$14,000.





# You Don't Report Gifts Under \$14K



- ▶ **Example:** Donna gives each of her three grandchildren and their two parents \$14,000 in 2017. The gifts totaled \$70,000. Because none of the gifts exceeded \$14,000, Donna did not have to report any of them. She still has a \$5.49 million exemption.



# You Do Report Gifts Over \$14K



- ▶ **Example:** Donna gives her son \$84,000 to help with a down payment on a condo in 2017. Because that gift exceeds the annual gift tax limit, Donna must report a gift of \$70,000 on a gift tax return the following year. (The first \$14,000 is free of tax). Now she has a tax exemption of \$5.420 million.



# You Have A Lot of Exemption to Use



- ▶ The BIG POINT:
- ▶ If \$5.49 Million is more than enough to cover your estate, you aren't limited to the annual gift amount, it is OK to use up some of the time on that clock!



# Make Gifts When They Really Count



- ▶ **Example:** Clifford gave \$314,000 to his daughter Claire to help pay for college for her twin sons in 2012. He reported that gift in 2013 on a gift tax return.
- ▶ When Clifford died in 2017, he had an available exemption amount of \$5.19 million (\$5.49-\$300k)
- ▶ Clifford's total estate was \$3 million.
- ▶ No estate tax was due.



# Things Have Changed A Lot



- People used to worry about using up that exemption.
- But today, many people do not need to worry.
- Be generous, if you want to be generous.



# Exemption Rising; Tax Rates Falling

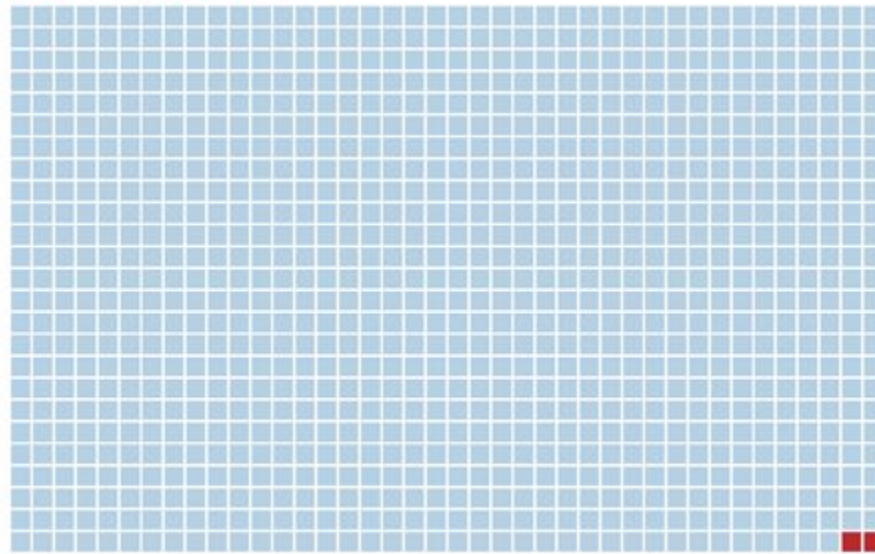


<b>Taxes</b>	<b>2001</b>	<b>2009</b>	<b>2017</b>
Maximum Gift Tax Rate	55%	45%	40%
Maximum Estate Tax Rate	55%	45%	40%
GST Tax Rate	55%	45%	40%
Gift Tax Exemption	\$675,000	\$1,000,000	\$5,490,000
Estate Tax Exemption	\$675,000	\$3,500,000	\$5,490,000
Portability	No	No	Yes

# 99.8% of Estates Aren't Taxable



**Only 2 Out of Every 1,000 Estates Will Owe Federal Estate Tax in 2015**



Source: Joint Committee on Taxation

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# More Smart Gifts



Direct payments for education.

Direct payments for medical expenses.

Can exceed annual exclusion.

The “Ed/Med Exclusion.”





# Ed/Med Exclusion



**Example:** Steven pays for his grandson's high school tuition by sending a check directly to the school.

The tuition of \$17,000 does not need to be reported on a gift tax return and does not reduce Steven's \$5.49 million exemption.



# Ed/Med Exclusion



## Rules:

1. **Only for tuition, not books etc.**
2. **Paid directly to the institution.**
3. **For primary, secondary, preparatory, high schools, colleges, and universities.**
4. **Pre-school is fact-specific. 😊**



# Ed/Med Exclusion



**Example.** Hilda pays her grandson's medical insurance premiums and pays for his prescriptions for an expensive drug not covered by insurance. That \$22,000 is gift tax free. Hilda still has a \$5.49 exemption from gift and estate tax.



# Ed/Med Exclusion



## Rules:

1. **Qualifying medical expenses only: such as diagnosis, cure, treatment, insurance.**
2. **Must be paid directly to provider.**



# Small Gifts/Big Impact



- A gift doesn't have to be large to have a **BIG IMPACT**
- Consider gifts with tax-free growth
- Help young people leverage their best asset: **TIME**



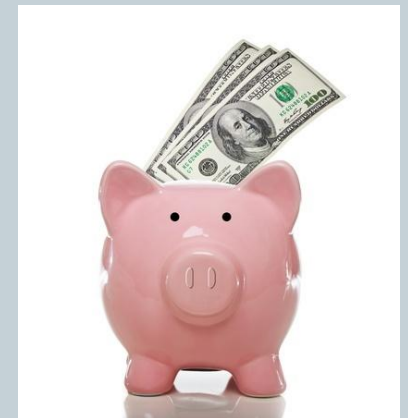
- **Ideas**

- Start a Roth IRA/Contribute to a 529 Plan**

# Roth IRA Match: Another Smart Gift



- Give kids an incentive to save early.
- Earlier the better for compound growth.
- People who wait to save for retirement have to save more.
- Help young adults develop good financial habits.



# Roth IRA: Lifelong savings



- You can contribute up to \$5,500 or amount of earned income, whichever is less.
- If a child is under 18, you can open a custodial Roth IRA in child's name.



# Roth IRA: Early Money is Better



- Example: To save \$1 million by age 65, you'd have to save **\$2,000/month** if you started at age 45.
- If you start at age 20, you would only have to save **\$361/month** to reach that goal.





# 529 College Savings: Yet Another Smart Idea



- 529 Plans allow tax-free growth for college/grad school expenses.
- Can be used for tuition and books and room and board.
- Can make 5 years of annual gifts all at once (\$70,000): front-loading—good for tax-free growth.
- Can be used for other family members.



# 529 College Savings Plans



- 529 Plans count as parental assets for financial aid (better than a child's assets): 5.64% contribution/parent versus 20% contribution/student.
- 529 Plans owned by grandparents impact financial aid a lot: when money is withdrawn, that money is counted as child's money for financial aid (50% contribution)



# 529 College Savings Plans



- ***What to do?***
- Plan ahead: consider making gifts to a parent's/kid's 529, rather than set a new one up.



# 529 College Savings Plans



- ***Great Resource:***

- **[www.Savingforcollege.com](http://www.Savingforcollege.com)**



# Smart Idea: Convert IRA to Roth IRA



- Pre-pay income tax for heirs.
- No RMD's in your lifetime.
- Control your income tax in future years.
- Reduce your taxable estate.
- *May not make sense if you are in a higher tax bracket than your heirs.*



# Smart Idea: Convert IRA to Roth IRA



- **Example:**
- Karen, age 60, converts part of her IRA to Roth IRA.
- Roth IRA has no RMD, but Karen can take tax-free withdrawals if she needs to do so.
- Balance in her Roth IRA passes income tax free to her heirs at her death.
- If she left an IRA, heirs would have to pay income tax on withdrawals.



# Giving to Charity



- Now we are switching gears from gifts to loved ones to gifts to charities. There are lots of good ideas here, too!



# Charitable IRA Rollover



- Individuals 70 1/2 or older
- Donate up to \$100,000k/year
- From their IRA to charities
- Satisfies RMD (so your taxes are lower)
- Charity gets tax-free gifts.





# Charitable IRA Rollover

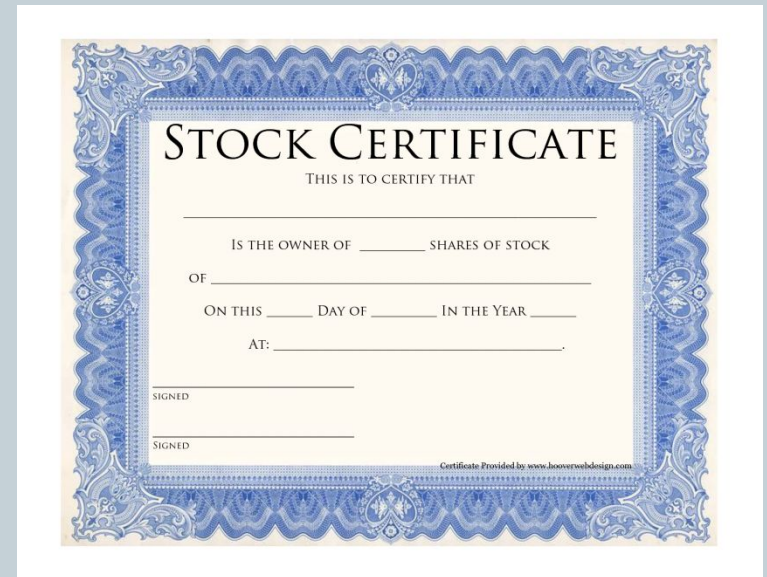


- **Example:** Russell, age 91, has to take out an RMD of \$15,000 in 2017.
- He doesn't want the income.
- He donates \$15,000 to Los Altos CF directly from IRA.
- Russell's income is reduced.
- Los Altos CF is thrilled.



# Gifts of Highly Appreciated Stock

- Highly appreciated stock is a GREAT GIFT to charity!
- You get a charitable deduction (if you itemize).
- Charity pays no capital gains tax on sale of stock.
- Applies to stock with low basis or unknown basis.

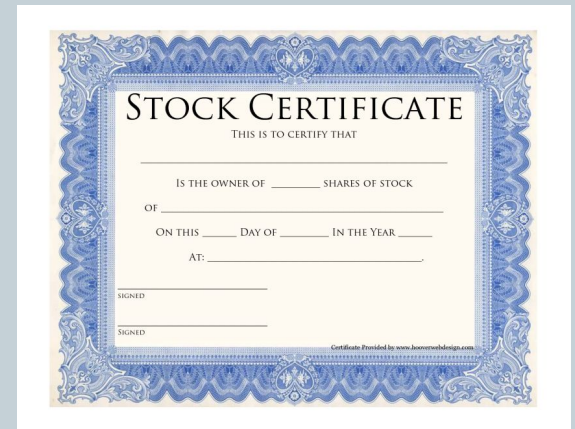


# More Smart Gifts to Charity



- **Rules:**

1. Must own stock for more than one year.
2. You give stock to a charity.
3. You get an income tax deduction equal to fair market value of stock up to 30% of AGI (carry forward five more years).
4. Charity sells stock and pays no capital gains tax.



# Gifts of Appreciated Assets



- **Example:** Mary wants to give a gift of \$10K to charity. Her tax rate is 28% and she itemizes deductions.
- She has low-basis stock, but not a lot of cash.
- She donates stock worth \$10K to the Sierra Club with a cost basis of \$4K.
- Sierra Club sells stock. No one pays capital gains taxes.
- Mary gets a \$10K charitable deduction, which saves her \$2800 in taxes.



# Donor Advised Funds



- Donor Advised Funds are like private foundations, but with less paperwork and expense.
- Community Foundations and investment companies offer them.
- You set up account and fund it with low basis stock.
- You get deduction in year of donation.
- You can recommend grants to charities in that year or future years.



# Charitable Gift Annuities



- You fund it with highly appreciated/low basis stock.
- You get income for life.
- Charity gets balance at your death.
- You get a charitable deduction based on value of ultimate gift.
- Spreads out recognition and taxation of capital gains.



Available on my website  
[www.lizahanks.com](http://www.lizahanks.com)



# The Family's Guide to Wills & Estate Planning

- Protect Your Family
- Create Peace of Mind
- Maximize Your Estate



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# Thanks for Listening!



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