

## Tax Notes

# To Gift or Not to Gift?

## *Planning Under the Increased Lifetime Basic Exclusion Amount*

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The IRS recently issued Proposed Regulation §20.2010-1 which addresses previously raised questions regarding taxpayers who may be interested in taking advantage of the increased lifetime basic exclusion amount (BEA). The BEA is the amount a taxpayer can transfer by way of gift during life or upon death without incurring a gift or estate tax liability.

The Tax Cuts and Jobs Act of 2017 (TCJA) has temporarily doubled the BEA from \$5 million to \$10 million, adjusted for annual inflation increases each year from 2018 through 2025. The BEA is currently set at \$11,180,000 in 2018. These changes are scheduled to sunset after December 31, 2025 and revert back to a BEA of \$5 million adjusted for inflation, as of January 1, 2026.

Due to the temporary nature of the 2017 TCJA there have been concerns that the benefits of the increased BEA could be lost after 2025 if the IRS has the ability to shift pre-2025 gifts back into the gift and estate tax calculations, otherwise known as “clawback.”

The proposed regulation has clarified outstanding questions regarding the impact of the increase and scheduled decrease of the BEA for a taxpayer's previously made gifts and post-2018 gifts. The preamble to the proposed regulation breaks down the gifting issues into four different scenarios in which the first three scenarios are addressed by existing statutory law so no new regulations are needed. The fourth scenario is addressed by the proposed regulation to avoid an adverse effect resulting from the post-2025 scheduled decrease in the BEA.

### **Scenario 1: Gift taxes were actually paid on pre-2018 gifts that exceeded the pre-2018 BEA.**

The current gift tax computation appropriately allows for the increased BEA to be reduced by the amount of BEA allowed against prior gifts but not by gifts for which gift tax was paid. Any pre-2018 gifts where gift taxes were paid will not reduce the increased BEA and will allow the additional BEA to be utilized against gifts made during 2018 through 2025.

### **Scenario 2: The estate tax return of a decedent dying between January 1, 2018 and December 31, 2025 includes gift taxes that were actually paid on pre-2018 gifts that exceeded the pre-2018 BEA.**

The current estate tax computation removes the amount of gift tax liabilities on pre-2018 gifts in determining the tentative estate tax due. The credit for the increased BEA is netted against the tentative estate tax. In this way, the increased BEA is not reduced by the portion of any prior gift on which gift tax was paid.

### **Scenario 3: The BEA decreases and a taxpayer utilized the increased BEA amount between 2018 and 2025 and then makes additional post-2025 gifts.**

The current gift tax computation will avoid the application of the post-2025 BEA to the 2018 through 2025 gifts. However, any gifts made post-2025, when the BEA is lower than the previously gifted amounts, will not have a credit available to offset a gift tax that will be due in that gifting year.

### **Scenario 4: A post-2025 decedent's estate tax return includes gifts that were sheltered under the increased BEA.**

Under the current statutory tax regime, the benefits of the increased BEA would effectively be eliminated for estates that previously utilized the increased BEA for lifetime gifting. In response, the IRS issued Proposed Regulation §20.2010-1(c) to remedy this problem and provide an "anti-clawback" provision. The proposed regulation states that a post-2025 decedent's estate will be allowed to take the **larger of** the current BEA then in effect at the decedent's date of death **or** the BEA utilized in determining the gift tax payable for prior year gifting. In brief, the IRS will allow the increased BEA to shelter gifts made during 2018-2025 instead of those gifts being "clawed back" into the decedent's estate tax calculation.

### **Key Takeaway**

Given such a large increase and the temporary "use it or lose it" nature of the law, PKF O'Connor Davies, LLP sees the time between now and December 31, 2025 as a ripe opportunity for clients to transfer a considerable amount of personal assets without paying gift tax and, consequently, reducing future estate tax.

### **Contact Us**

Please reach out to your PKF O'Connor Davies, LLP tax advisor for more information on how the increased basic exclusion amount could benefit your wealth transfer and planning strategies, or contact either of the following:

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