

Tax Talk Today

Specialty Taxes: Estate and Gift, and Employment Taxes

May 12, 2009

Q&A, Part I – Estate Taxes

Question

The common reasons given for high estate exemptions are that small businesses and family farms have to liquidate to pay estate taxes. Does the service keep any records on liquidations and are there alternatives for families to still pay a fair share of estate tax but not lose the farm in the process?

Answer

The Service does not maintain any records on liquidations. The special use election (IRC Section § 2032A) is available to estates comprised of farm real property or property used in a trade or business. IRC Section 2032A was enacted to alleviate the estate tax burden for farmers and other business owners whose business property/farm has a highest and best use value (fair market value) that exceeds its value in actual use (special use valuation).

Question

If a donor gives, say, \$28,000 in checks written to a husband and \$20,000 to the wife, and they have two kids, and the money is for the family's benefit, can the amount be reported on the gift tax return as \$12,000 to each of the 4 family members? Or must it be reported as gifted to the person(s) to whom the checks were written?

Answer

The amounts of the checks must not be reported on the gift tax return as \$12,000 to each of the 4 family members, but instead must be reported as \$28,000 to the husband and \$20,000 to the wife. Generally, the children will be entitled to the applicable annual exclusion if the checks are written to the minors or to their custodian under the Uniform Transfers to Minors Act (formerly known as the Uniform Gifts to Minors Act).

Question

A family friend, who died two years ago, left me \$72,000.00 per her will which I will receive sometime this summer. What kind of taxes will I have to pay on this?

Answer

Generally, if you receive a gift or a bequest, you will not have to pay any federal gift tax or estate tax. Also, you will not have to pay income tax on the value of the gift or inheritance received.

Question

How do you deal with estate taxes that come about from a wrongful death suite?

Answer

Wrongful death suit proceeds are included in the calculation of a decedent's gross estate under IRC section 2033 only if the proceeds are related to decedent's pain, suffering or related expenses during the decedent's lifetime.

Question

If a taxpayer makes a contribution to an irrevocable life insurance trust that is less than the threshold (\$13,000) must they file a gift tax return?

Answer

Generally, any individual who makes a gift must file a gift tax return for the year in which the gift is made. A transfer in trust constitutes a gift to the trust beneficiary/ies. Whether or not a return is required to be filed in this case depends on a number of factors including the number of trust beneficiaries, whether the trust beneficiary/ies have a present interest in the trust, the total amount of annual gifts to each beneficiary/ies and whether spouses are splitting gifts.

Question

Upon the death of a taxpayer with funds invested in an IRA, taxes are automatically withheld at 10% on the federal level prior to disbursement to a beneficiary, could these funds be claimed as part of the estate and therefore the withheld portion refunded once a tax return is filed?

Answer

A gross estate includes the fair market value of all of the decedent's property; accordingly, IRAs are part of the gross estate. The beneficiaries of inherited IRAs will report the proceeds as taxable income in the year they receive distributions.

Question

If an IRA is split into separate accounts for each child after a parents death within six months of death, do you use the six month date or the date the IRA was split for alternate valuation purposes.

Answer

Generally, the alternate valuation election pertains to the valuation of the property. The election does not permit a redetermination of what property is to be included in the gross estate. Thus, the value of the IRA to be included on the

Form 706 is its full value as of the date of death and its full value 6 months after the date of death.

Question

Are IRA's and/or 401k's included as taxable on the 706? If so, are Roth IRAs treated different from regular IRAs?

Answer

A gross estate includes the fair market value of all of the decedent's property; accordingly, IRAs are part of the gross estate. Beneficiaries of inherited IRAs report the proceeds as taxable income in the year they receive distributions. For purposes of inclusion in the gross estate, the Roth IRA is not treated differently from a regular IRA.

Question

Does this apply on stock by stock item or in total (all or nothing?)

Answer

Generally, stock in which decedent has an interest is also included in the gross estate and should be listed by each stock item.

Question

Can the alternate valuation date be used instead of date of death value to value assets in estates or trusts that are not required to file the estate tax return (i.e. smaller estates)?

Answer

No.

An estate tax return, Form 706, must be filed if the gross estate, plus any adjusted taxable gifts and specific gift tax exemption, is more than the filing requirement for the year of death. The valuation of the properties which comprise the gross estate is as of the date of death. Alternate Valuation may be elected if the value of the gross estate at the alternate valuation date is less than its value at the date of death and if the sum of estate tax liability and GST tax liability will be reduced as a result of the election. The alternate valuation date values must not be used to determine whether an estate tax return should be filed.

Question

Please explain the gift tax implications of a \$20,000 contribution to a 529 plan. Must this distribution be allocated evenly over 5 years, or can \$13,000 be allocated to the current year, with the remaining \$7,000 allocated evenly to the 4 subsequent years? Is a gift tax return only required for the year of the gift, assuming it exceeds the annual limit?

Answer

If a taxpayer elects to treat the \$20,000 contribution made in one year as being made ratably over five years then the taxpayer is treated as making a completed gift of \$4,000 in each of the five years and must file a gift tax return for each of the five years.

Question

What happens when a taxpayer dies and upon preparing the 706 we find that a gift tax return was filed but it missed reporting one of many gifts? Can we amend an old (2001) gift tax return after the decedent has died? If not how do we handle it on the 706 since we know the gift tax return was filed incorrectly?

Answer

Pursuant to IRC section 2001, post-1976 taxable gifts not included in a gross estate must be added to the taxable estate. The estate's fiduciary may amend the gift tax return and include the amended total amount of post-1976 taxable gifts on Line 4 of the Form 706.

Question

If you file a late gift tax return and the unified credit offsets the tax - do you not have to pay the interest and or penalty on the amount of tax offset because it was not offset timely? (by the due date of the return)

Answer

If no gift tax is due as a result of the application of the unified credit then no interest or penalty will be assessed; however, if it is later determined that gift tax is due, failure to file penalties may be applicable.

Question

Does the gift have to be cash to be subject to the threshold? For example, if you pay off a loan that your child has in their name, is that considered a gift?

Answer

A gift does not have to be in cash to be subject to the annual exclusion threshold. The gift tax applies to transfers by gift of property. You make a gift if you give property (including money), or the use of or income from property, without expecting to receive something of at least equal value in return. If you sell something at less than its full value or if you make an interest-free or reduced-interest loan, you may be making a gift.

Question

If a taxpayer transfers the deed to their home to children during their lifetime, have they potentially triggered a gift tax return requirement? If they learn this and transfer the deed back to themselves, so they relieve that filing requirement.

Answer

The gift tax applies to transfers by gift of property. You

make a gift if you give property (including money), or the use of or income from property, without expecting to receive something of at least equal value in return. In this case, if the transfer exceeded the applicable annual exclusion to which each child is entitled or if the taxpayer's total amount of annual gifts to each child exceeded the applicable annual exclusion then a gift has been made to each child and the taxpayer is required to file a gift tax return (Form 709). If the children transfer the deed to the parents, a gift tax return may be required to be filed by each child if the transfer exceeds the applicable annual exclusion to which each parent is entitled or if each child's total amount of annual gifts to each parent exceeds the applicable annual exclusion.

Question

Adult sister/daughter died. Her 401k named father as beneficiary but her will said it should be split among sisters and father. Form 1099R issued to the father. How should this be reported?

Answer

401k proceeds generally pass to the designated beneficiary regardless of what a will provides. Because the father was designated as the beneficiary of the IRA, the Form 1099R was properly issued to the father. If the decedent is required to file Form 706, US Estate Tax Return, the 401k proceeds are includable as an asset of the estate. Additionally the proceeds of the 401k should be reported as income on the Father's individual income tax return.

Question

If an individual has a trust and all assets are within this trust, is a 1041 estate return also required? Is the trust included in the 706 return?

Answer

Form 1041 is required. The fiduciary (or one of the joint fiduciaries) must file Form 1041 for a domestic trust taxable under section 641 that has:

1. Any taxable income for the tax year,
2. Gross income of \$600 or more (regardless of taxable income), or
3. A beneficiary who is a nonresident alien.

All transfers (other than outright transfers not in trust and bona fide sales) made by the decedent at any time during life must be reported on Schedule G of Form 706.

Question

What if a client has been giving gifts to his children and grandchildren over the past 5 years? Does a form 706 have to be filed even if he stayed under the maximum amount allowed?

Answer

For decedent's dying in 2008, Form 706 must be filed by the executor for the estate of every US citizen or resident whose gross estate plus adjusted taxable gifts is more than \$2,000,000 (\$3,500,000 for decedents dying in 2009).

Question

Does a one time monetary gift to children be reported as income?

Answer

Gifts are not subject to income tax.

Question

If Mary has 2 minor children and I make a gift of \$13,000 to each child, have I made a \$26,000 gift to Mary?

Answer

Most states have laws governing gifts to minors under the Uniform Gifts to Minors Act. If your state has a provision for gifts to minors, transfers to such minors are not considered transfers to their parents.

Question

If a retirement account such as a 401(k), SIMPLE, or Roth or Traditional IRA has a qualified charity as the only one, or as one of the beneficiaries, is that portion excluded from the estate evaluation?

Answer

Retirement Accounts such as a 401(k), SIMPLE, Roth and Traditional IRAs are generally included as an asset of a decedent's estate. If a qualified charity is the beneficiary of such an account, the estate will generally be entitled to a charitable deduction.

Question

If Grandma writes a \$52,000 check to her son for the benefit of his family, which includes his wife and two kids – does it need to be reported as a \$52,000 gift to her son, or can it be considered a \$13,000 gift to each of the 4 family members and therefore all within the exclusion?

Answer

A check written to an individual will generally be treated as a gift to that individual. In the above example, a \$52,000 check to son would be treated as a \$52,000 gift to one individual. If she wanted to give each family member \$13,000, Grandma would need to write an individual check to each family member.

Question

Can a gift from a parent to a child result in a Generation Skipping Tax if the parent is more than 37 ½ years older than the child? i.e. Mom was 40 years old when the child was born

Answer

No. Generally, for purposes of Generation Skipping Tax, the generation of a transferee is determined along family lines. A gift to one's child will never be subject to Generation Skipping Tax regardless of how old the mother was when the child was born.

Question

Is it true that in an estate tax return, spouse deduction is 100% but that a single parent (or a divorced person) can not will their estate to their children 100% tax free?

Answer

Yes, a deduction is available for most bequests to a surviving spouse. There is no deduction available for bequests to children.

Question

When using alternate valuation, should we still reflect date of death value for cash assets?

Answer

Yes. Income earned on cash assets would not be included in the gross estate as a result of an election to use the alternate valuation method.

Question

Are life estates included in a decedent's estate?

Answer

The answer depends on who created the life estate. A life estate in an asset created by another would generally not be includable as an asset of a decedent's estate. A life estate in an asset that was once wholly owned by the decedent will generally be includable as an asset of the decedent's estate.

Question

Please explain the gift tax regarding tuition. Question: Can a grandparent pay tuition to a private grade school (K-12) and escape the gift tax rules?

Answer

The gift tax does not apply to an amount paid on behalf of an individual to a qualifying domestic or foreign educational organization as tuition for the education or training of the individual. A qualifying educational organization is one that normally maintains a regular faculty and curriculum and normally has a

regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on.

The payment must be made directly to the qualifying educational organization and it must be for tuition. No educational exclusion is allowed for amounts paid for books, supplies, room and board, or other similar expenses that do not constitute direct tuition costs. To the extent that the payment to the educational institution was for something other than tuition, it is a gift to the individual for whose benefit it was made, and may be offset by the annual exclusion if it is otherwise available.

Question

Is the value of a trip on a company jet where the parents are officers or directors or the purchase of an airplane ticket for a child constitute a taxable gift?

Answer

The federal gift tax applies to any transfer by gift of real or personal property, whether tangible or intangible, that you made directly or indirectly, in trust, or by any other means to a donee. The gift tax applies not only to the gratuitous transfer of any kind of property, but also to sales or exchanges, not made in the ordinary course of business, where money or money's worth is exchanged but the value of the money (or property) or money's worth received less than the value of what is sold or exchanged. The gift tax is in addition to any other tax, such as federal income tax, paid or due on the transfer.

The first \$12,000 (2008) of gifts of present interests to each donee during the calendar year is subtracted from total gifts in figuring the amount of taxable gifts.

Question

QDOT-

When is this required to protect the marital exclusion in an estate? I have friends living in Paris and it seems if the husband dies without this, his wife may not benefit from the exclusion? Is there estate given the \$3.5 million exclusion on the estate even if living overseas in 2009, but not in 2010 as the law is currently written?

Answer

The marital deduction is allowed for transfers to a surviving spouse who is not a U.S. citizen only if the property passes to the surviving spouse in a qualified domestic trust (QDOT) or if such property is transferred or irrevocably assigned to a QDOT before the decedent's estate tax return is filed.

A QDOT is any trust:

1. That requires at least one trustee to be either an individual who is a citizen of the United State or a domestic corporation;

2. That requires that no distribution of corpus from the trust can be made unless such a trustee has the right to withhold from the distribution the tax imposed on the QDOT;
3. that meets the requirements of any applicable regulations; and
4. For which the executor has made an election on the estate tax return of the decedent.

The applicable exclusion amount for 2009 is \$3,500,000. The estate tax has been repealed for 2010 as the law is currently written.