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What Is the Gift Tax?

Greetings Golden Club!

I am often approached about what considerations one should make while gifting assets to loved ones. Namely, many are concerned about the gift subjecting them or the recipient to gift taxes. The federal gift tax applies to gifts of property or money while the donor is living. The federal estate tax, on the other hand, applies to property conveyed to others (with the exception of a spouse) after a person's death.

The gift tax applies only to the donor. The recipient is under no obligation to pay the gift tax, although other taxes, such as income tax, may apply. The federal estate tax affects the estate of the deceased and can reduce the amount available to heirs.

In theory, any gift is taxable, but there are several notable exceptions. For example, gifts of tuition or medical expenses that you pay directly to a medical or educational institution for someone else are not considered taxable. Gifts to a spouse who is a U.S. citizen, gifts to a qualified charitable organization, and gifts to a political organization are also not subject to the gift tax.

You are not required to file a gift tax return unless any single gift exceeds the annual gift tax exclusion for that calendar year. The exclusion amount (\$14,000 in 2015) is indexed annually for inflation. A separate exclusion is applied for each recipient. In addition, gifts from spouses are treated separately; so together, each spouse can gift an amount up to the annual exclusion amount to the same person.

Gift taxes are determined by calculating the tax on all gifts made during the tax year that exceed the annual exclusion amount, and then adding that amount to all the gift taxes from gifts above the exclusion limit from previous years. This number is then applied toward an individual's lifetime applicable exclusion amount. If the cumulative sum exceeds the lifetime exclusion, you may owe gift taxes.

The 2010 Tax Relief Act reunified the estate and gift tax exclusions at \$5 million (indexed for inflation), and the American Taxpayer Relief Act of 2012 made the higher exemption amount permanent while increasing the estate and gift tax rate to 40% (up from 35% in 2012). Because of inflation, the estate and gift tax exemption is \$5.43 million in 2015. This enables individuals to make lifetime gifts up to \$5.43 million in 2015 before the gift tax is imposed.

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