

Determining the “true” value of your gifts and bequests

Whether it’s making gifts to loved ones or to charity, or bequeathing your assets to your heirs in your will, it’s especially important to have a clear understanding of the value of what you are transferring.

For one, if you are trying to equalize your gifts among your beneficiaries, placing an accurate price tag on your gift will help to keep peace in the family. Second, and always an issue when you make substantial gifts, is to value them accurately for tax purposes.

Fair market value

The standard benchmark for assigning a value to property is “fair market value.” The IRS defines fair market value as “the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.”

Although determining fair market value is simple enough for securities traded on an exchange, the value of the stock of a family-owned or closely held business is more difficult. In that instance, it may be possible to apply a discount to the value of the stock, thereby reducing the size of the gift or bequest and, ultimately, the tax that will be owed. Discounts may be permitted for several reasons, including: lack of marketability of the shares, ownership of a minority interest and restrictions that might exist on the sale of the stock.

The tax facts

There are no taxes on lifetime gifts, made outright with no strings attached, as long as the gifts do not exceed \$12,000 per donee. (Married couples may “split” their gifts, doubling that figure to \$24,000, even if the gift comes from only one of the spouses.)

In addition there are estate and gift tax exemptions available. For 2008, the maximum estate tax exemption is \$2 million; for gifts, \$1 million. Once the exemption is used up, bequests and gifts are taxed at a maximum rate of 45%.

Alternate value

Although property at death is usually valued as of the exact date of death, the executor of an estate may choose a date that is six months later. If the executor elects to use the alternate valuation date, *all* estate assets must be valued as of that date. An executor will choose the later date only if it results in an overall decrease in tax liability for the estate. For example, if an estate consists mainly of stock, and its value has dropped significantly in the six months after death, then the executor will chose the alternate valuation date.

Special use value

Very often a family farm or business may be situated on real estate that might be better utilized for purposes that would make more valuable use of the property (dubbed “its highest and best use”). Yet valuing property at its highest and best use for estate tax purposes could well lead to a forced sale of the land to pay taxes. An executor may make an election to take advantage of a special use valuation technique that will put a lower price tag on the property. The special valuation rules are complex, and rigid adherence to these rules is required in order to avoid a disallowance of the valuation and the imposition of a “recapture tax.”

The art of appraisal

When establishing the value of a gift for tax purposes, it's essential to obtain an accurate, written appraisal from a reputable individual or firm. In order to pass muster with the IRS, the report must be more than just an opinion. All of the facts that led to the appraiser's conclusion as to the property's fair market value must be detailed in the appraiser's report.

How favorably the IRS will view the appraisal will depend also upon the method used to arrive at the property's value. Using established or more traditional methods increases the likelihood that the IRS will accept the appraised value included on a tax return.

Copies of appraisals of your real estate, business and personal property should be distributed to anyone who is involved with your long-term financial planning: your attorney, accountant, executor and trustee, for instance. Finally, because the value of most property is likely to fluctuate, make sure to update your appraisals regularly.

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