



WHAT ARE TWO GIFTING TECHNIQUES THAT CAN BE IMPLEMENTED IN A HIGHER INTEREST RATE ENVIRONMENT?

Although interest rates remain low from a long-term historical perspective, interest rates are considerably higher than a few years ago. While some tax planning strategies are more effective in lower interest rate environments, others are more attractive when interest rates increase. Below are two techniques which provide better tax results, all else being equal, when interest rates are higher.

A Qualified Personal Residence Trust (“QPRT”) is a tax-efficient means of transferring a personal residence to intended beneficiaries. The concept of a QPRT is relatively simple - the owner of the personal residence transfers it to a trust but retains the right to live rentfree in the residence for a specified number of years. In order to be successful, the original owner must survive the specified number of years. If the original owner is alive at the end of that period, ownership of the residence is transferred to the beneficiaries (or to a trust for their benefit) and the value of the residence is removed from the estate of the original owner. At that time, the original owner can rent the property from the beneficiaries (or trust) if he or she wishes to continue to use the residence.

The primary tax advantage of the QPRT comes from the way in which the value of the residence transfer is calculated for gift tax purposes. The value of the gift is not the full value of the residence on the date of the gift but rather the present value of the beneficiaries’ right to receive the residence after the specified number of years and only if the original owner survives that term. This is calculated by reducing the value of the residence transferred to the QPRT by the value of the original owner’s retained right to live in the property for a period of years using the IRS assumed interest rate on the date of the transfer.

In a high interest rate environment, the value of the original owner’s retained interest increases, thereby reducing the value of the gift. For example, if a 60 year old transferred a \$2,000,000 residence to a 15-year QPRT in March 2022 when the IRS assumed interest rate was 2.0%, the taxable gift would have been roughly \$1,560,000 while this same gift in September 2025 when the assumed interest rate was 4.8% resulted in a taxable gift of \$770,000. Assuming a federal gift and estate tax rate of 40%, the tax savings resulting from the higher IRS assumed interest rate alone is \$316,000.

A Charitable Remainder Trust (“CRT”) is a trust which pays a percentage of the trust assets annually to the Grantor or to other noncharitable beneficiaries for a set period of time and, at the end of that period, pays whatever property remains in the CRT to one or more charities. Funding a CRT has a number of tax benefits for the Grantor including:

- The Grantor is entitled to an immediate income and gift tax charitable deduction equal to the present value of the charity’s right to receive the assets remaining in the trust at the end of the trust term. As interest rates increase, CRTs become a more attractive gifting option as the higher interest rate provides the Grantor with a larger charitable income tax deduction.
- The CRT itself generally is exempt from income taxes. Accordingly, appreciated property can be transferred to the CRT and then sold without the CRT paying any immediate capital gains tax. Instead, a portion of the capital gain will be deemed distributed to the Grantor or noncharitable beneficiary each year as part of the annual payment, thus spreading the tax liability over multiple years.