Gift Loans

Prepared for: Sample

Prepared by: Brentmark

Gift Loans

Loan Date:	10/2022
Principal of Note:	$2,500,000
Interest Rate:	3.50%
Term of Note:	10
Type of Note:	Amortized
Payment Period:	Annual
Balloon Payment:	Yes
Amortization or Principal-Recovery Period:	10
Applicable Federal Rate:	4.00%
Present Value of Loan Payments:	$2,438,163.01
Amount of Gift (Principal less PV of Payments):	$61,836.99

Payment	Principal Balance	Interest 3.500%	Principal Payment	Total Payment	Present Value 4.00%	Foregone Interest
1	$2,500,000	$87,500	$213,103	$300,603	$289,042	$12,500
2	$2,286,897	$80,041	$220,562	$300,603	$277,925	$11,434
3	$2,066,335	$72,322	$228,282	$300,603	$267,235	$10,332
4	$1,838,053	$64,332	$236,272	$300,603	$256,957	$9,190
5	$1,601,781	$56,062	$244,541	$300,603	$247,074	$8,009
6	$1,357,240	$47,503	$253,100	$300,603	$237,571	$6,786
7	$1,104,140	$38,645	$261,959	$300,603	$228,434	$5,521
8	$842,182	$29,476	$271,127	$300,603	$219,648	$4,211
9	$571,055	$19,987	$280,617	$300,603	$211,200	$2,855
10	$290,438	$10,165	$290,438	$300,603	$203,077	$1,452
		$506,034	$2,500,000	$3,006,034	$2,438,163	$72,291

This scenario is a hypothetical illustration based on the assumptions you entered via the inputs inside the program. It is to be used solely as a conceptual guide to understand and quantify your planning needs. It would be wise to consider this illustration together with all other information you deem necessary in making your investment decisions. This illustration is not a guarantee of the performance of any specific investment. Actual performance from your investments and assets may vary. This illustration is not legal or tax advice. You should consult with your attorney and accountant to review this information and determine its appropriateness for your particular situation. The provider of this illustration provides no guarantee and assumes no responsibility or liability for the accuracy of the information provided (including whether the interest rate you have selected is in fact "reasonable") or for your reliance based on this information.

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Under section 7872 of the Internal Revenue Code, a loan can result in an immediate gift if (a) the loan is for a fixed term (and not payable on demand), (b) the loan is a "below-market loan" because the interest rate is less than the applicable federal rate (defined by section 1274(d) of the Internal Revenue Code), and (c) the foregone interest (the difference between the rate of interest charged on the loan and the applicable federal rate) is in the nature of a gift. For a gift loan, the amount of the gift is the difference between (a) the amount received by the borrower and (b) the present value of all future payments to be made, based on the applicable federal rate in effect at the time the loan is made. For income tax purposes, each year's foregone interest is treated as received by the lender on the last day of the calendar year.

Given the amount of the loan, the term of the loan, the frequency of the payments (monthly, quarterly, semiannually, or annually), whether the loan is amortized, level principal, or interest-only, the interest rate for the loan, and the applicable federal rate, the future payments can be calculated, along with the present value of those payments, the amount of the gift, and the future amounts of foregone interest.

In an amortized loan, the payments are calculated so that the periodic payments of combined interest and principal are equal amounts over the term of the loan. The interest is always calculated on the principal balance owed, but the interest amount goes down (and the principal amount goes up) as the principal of the loan is paid. So, early in the loan, the payments will be mostly income with very little principal paid, while towards the end of the loan the payments will be mostly principal with very little interest payable on the declining loan balance.

In a level-principal loan, the principal payment is fixed as the amount needed to pay off the principal amount over the stated term, and if there is no "balloon" payment, then the principal portion of each loan payment will be the principal amount of the loan divided by the number of payments to be made. The interest portion of each payment is calculated on the principal balance remaining, so the interest amount goes down as the principal of the loan is paid. Because the principal portion of each payment is a fixed amount, and the interest portion goes down over the course of the loan, each loan payment will be different, and the payments will go down over the term of the loan.

In an interest-only loan, no principal is paid until the end of the term. Because the principal of the loan remains the same throughout the term, the interest payments also remain the same.

A compromise between an interest-only loan and an amortized or level-principal loan is a loan in which some principal is paid during the term and the balance is paid as a "balloon" at the end of the term. So, for example, the periodic payments on a loan can be calculated based on an amortization over 30 years even though the term of the loan is only 15 years, in which case the balance of the principal is payable as a lump sum "balloon" at the end of the 15 years. A level-principal loan can also be calculated with a principal-recovery period that is longer than the actual term of the loan, also resulting in a balloon payment at the end of the term.

The "annual percentage rate" or "APR" is a useful number to know in comparing the true costs of different kinds of loans, and the APR is not necessarily the same as the interest rate used to calculate the loan payments. If the payments are monthly, quarterly, or semiannual, the APR will not be the same as the interest rate that is entered for the note because payments that are more frequent than annual have the effect of compounding the interest rate, so the APR (or effective interest rate) is higher.

The present value of future loan payments is calculated by discounting the future payments back to present value by applying the applicable federal rate.

The foregone interest is the difference between the interest actually payable under the loan and the interest that would have been payable using the applicable federal rate.