



CARDINAL ADVISORS

Step Up In Basis-Estate Planning-Income Tax

In the video entitled "Step Up In Basis-Estate Planning-Income Tax" Hans and Tom use the following handout to discuss estate planning.

STEP UP IN BASIS-ESTATE PLANNING-INCOME TAX																								
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Understanding Step-Up in Basis in Estate Planning

I. Introduction

Estate planning isn't just about who inherits your assets—it's also about minimizing taxes. One powerful tool is the 'step-up in basis,' which adjusts the cost basis of an asset to its fair market value (FMV) at the time of the owner's death. This can dramatically reduce capital gains taxes for heirs.

II. The Basics of Step-Up in Basis

- Applies when an asset owner dies
- Adjusts cost basis to FMV at the date of death
- Reduces or eliminates capital gains tax when inherited assets are sold
- Applies to capital assets: real estate, stocks, business interests, etc.

III. Stock Example: Selling Before vs. After Death

Scenario: 1,000 shares of stock bought for \$10,000; FMV at date of death is \$100,000

- A. Sold Before Death:
 - - Sale Price: \$100,000
 - - Original Basis: \$10,000
 - - Capital Gain: \$90,000 (Taxable)
- B. Sold After Death (by Heir):
 - - Inherited Basis: \$100,000
 - - Sale Price: \$100,000
 - - Capital Gain: \$0 (No Tax)

IV. Step-Up in Basis and Married Couples

- Common Law States: Only deceased spouse's half gets stepped up
- Community Property States: Entire property may receive full step-up
- Titling matters (e.g., joint tenancy vs. tenants in common)

V. Home Sale Example After First Spouse's Death

Couple buys home for \$200,000; FMV at first spouse's death is \$600,000; Titled jointly in a common law state.

- - Half of home steps up from \$100,000 to \$300,000
- - New basis = \$300,000 (stepped-up half) + \$100,000 (unchanged half) = \$400,000
- - Sold for \$650,000; Gain = \$250,000
- - Surviving spouse qualifies for \$250,000 home sale exclusion
- - Capital Gains Tax Owed = \$0

VI. Final Step-Up at Second Death

- Assets receive a new step-up at second spouse's death
- Heirs inherit at FMV
- If sold quickly, little or no capital gains tax is owed

VII. Planning Tips

- Understand state-specific laws
- Maintain records of original basis and capital improvements
- Work with a qualified estate planning attorney or tax advisor

VIII. Conclusion

The step-up in basis is a vital strategy in estate planning. It can reduce or eliminate taxes on appreciated assets like homes and stocks. Proper planning ensures your heirs retain more of your legacy.