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ASK ENCORE

A Stock Gift? The Tax Is in the Size of the Giving

By KELLY GREENE

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If I give an appreciated stock to my sister, age 66, which I purchased at \$1,000 a few years ago, and it is currently worth \$5,000, is there any capital-gains tax involved? Do I have to pay the tax, even though I haven't sold the stock? If not, does my sister have to pay tax? Or does the stock simply pass to her without tax with her basis being the market value the day of the transfer? If she has to pay the tax, is her basis and date of purchase my original date and cost?

--Ron Earhart, Dayton, Ohio

No one pays tax when you give the stock to your sister. She would assume your basis in the stock, and -- since it's a gift from you -- she would tack your holding period onto her own for tax purposes.

Your sister would be on the hook for capital-gains tax when she sells the stock. But since you held it for more than a year and she gets to add your holding period to her own, the capital gain would be considered long term, and taxed at a maximum federal rate of 15%, as opposed to the 35% maximum rate for short-term capital gains, says Nick Crocetti, a tax director with CBIZ Inc. in Plymouth Meeting, Pa.

So, continuing with this example, if she sold the stock for \$5,500 almost immediately after you gave it to her, she would have a long-term capital gain of \$4,500.

The situation would be different if the stock you gave your sister was worth more than \$12,000. In that case, you might have to pay federal gift tax, says Mark Nash, a personal finance services partner with PricewaterhouseCoopers in Dallas. And "if gift tax is paid, there might be an adjustment to the basis of the stock" in your sister's possession.

Then again, adds Mr. Crocetti, you might not have to pay the tax, because "we all have a lifetime gift-tax credit, which is equivalent to about \$1 million in gifts that we can give above that \$12,000 limit." And some states levy their own gift taxes using different rules.

"Everyone assumes it's a great idea to give appreciated stock to your family members, and that's not always true because you're saddling them with this built-in gain," Mr. Nash says. "Sometimes people will say, 'But I really want her to have the stock.' You could give her \$5,000 in cash, and she could go out and buy the stock in the open market with a basis of \$5,000."

If an even larger chunk of stock is involved -- worth, say, \$100,000 to \$1 million -- you might consider waiting to pass it to your sister through your estate, Mr. Crocetti says. That way, the stock would be valued at its price the day of your death, rather than the day you bought it.

You also may want to consider giving the stock to charity, because the charity wouldn't have to pay tax on the gain, and you would get an income-tax deduction for the fair-market value of the stock at the time you gave it away, he adds.

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