



STEP-UP BASIS VS. GIFTING ASSETS: THE TRANSFER DECISION

How families with appreciated assets can evaluate the hold, gift, or transfer decision under current tax law and the OBBBA framework.

Palmer Wealth Group™ | 2 April 2026

Imagine a commercial property your family purchased in 1987 for \$400,000. Today it is worth \$3.2 million. The choice facing your estate attorney and financial advisor is whether to gift it to your children now or hold it until death. That decision will determine whether your heirs receive a \$2.8 million tax-free inheritance or inherit a \$560,000 capital gains obligation alongside the building itself.

This is not a hypothetical. It is the conversation we have with business owners, executives, and multi-generational families across Texas with increasing frequency. It is also one of the most consequential decisions in wealth transfer planning.

THE DECISION MOST FAMILIES GET WRONG ABOUT APPRECIATED ASSETS

According to Cerulli Associates' June 2025 research, an estimated \$124 trillion in assets is projected to transfer across generations through 2048. Approximately half of that total will originate from high-net-worth households, a group that represents just 2% of all families in the United States. The families PWG serves sit squarely in that group.

The scale of what is at stake has grown significantly in recent years. Between 2020 and 2023, real estate values surged by approximately 39% and equity markets grew by roughly 27%, according to data cited in the Cerulli report. For families who have held appreciated property or a closely held business for decades, these gains have deepened the unrealized gains problem substantially, creating embedded capital gain exposure that has accumulated quietly across portfolios for years, sometimes decades. Baby boomers alone control approximately \$78.55 trillion in total U.S. wealth, making the transfer decision a generationally urgent one for a very large number of families.

We examine how estate plans commonly fall short on this specific decision in our article on [why your estate plan might not protect your legacy](#).

The difficulty is that most families approach this decision with one of two equally flawed assumptions. The first is that gifting assets during life is the generous and smart move, putting wealth into heirs' hands sooner while reducing the taxable estate. The second is that the stepped-up basis (the IRS rule that resets the cost basis of inherited assets to their fair market value at death) will always save the day. Neither

assumption holds in every situation. The right answer depends on three variables: the magnitude of embedded appreciation, the tax situation of the intended heir, and the size of the estate relative to today's exemption thresholds.

Why the Hold-Gift-Transfer Choice Matters More Than Most Families Realize

The \$124 trillion wealth transfer projection is not simply a statistic about the future. For any family holding a \$2 million piece of commercial real estate, a \$3 million block of founder stock, or a closely held business built over thirty years, the federal income tax embedded in that asset is a live liability, one that is triggered the moment the asset is sold and one that a thoughtful transfer strategy can eliminate, reduce, or inadvertently multiply.

The families Cerulli identifies as the source of approximately 50% of all future transfers (those with net worth above \$10 million) are precisely the families for whom the decision carries the greatest financial consequence. At this wealth tier, differences of \$500,000 or more in unrealized gains across a portfolio are not unusual, and the cost of transferring those gains to heirs through a poorly timed gift can rival years of investment returns.

The Two Competing Tax Outcomes and Why They Are Not Equal

Federal tax law treats a lifetime gift and a testamentary transfer (one that occurs at death) very differently for the recipient.

When an asset is gifted during life, the recipient inherits the donor's original cost basis, commonly called "carryover basis." If a parent purchased stock for \$100,000 and gifts it to an adult child when it is worth \$300,000, the child's basis remains \$100,000. When the child eventually sells at \$320,000, they owe capital gains tax on \$220,000 of gain, the full weight of the prior owner's unrealized gains now falling on the next generation.

When the same asset is held until death and transferred as part of the estate, the recipient receives what practitioners call the cost-basis step-up under Internal Revenue Code Section 1014(a). The stepped-up basis resets the recipient's cost to the asset's fair market value on the date of death. If that stock is worth \$300,000 at death, the heir inherits it with a \$300,000 stepped-up basis. A subsequent sale at \$320,000 produces only \$20,000 of taxable gain.

The difference is not cosmetic. It is real money. In high-appreciation scenarios, it is often a six- or seven-figure difference. These outcomes depend on individual circumstances, applicable tax rates, and future changes in the law, which is why every transfer decision should be reviewed with qualified tax and legal counsel.

THE FEDERAL RULES THAT GOVERN EVERY TRANSFER DECISION

Two sections of the Internal Revenue Code anchor this decision. Understanding them is not optional for families in the \$5–30 million range. These rules are the foundation upon which every other planning conversation rests.

How the Step-Up in Basis Works at Death (IRC § 1014)

Under IRC Section 1014(a), the basis of property acquired from a decedent is generally set to its fair market value on the date of death. This adjustment, known as the cost-basis step-up, applies to a wide

range of directly held assets: real estate, publicly traded stocks and bonds, interests in pass-through entities, and assets held in a revocable living trust, because the IRS treats revocable trust assets as owned by the grantor until death.

For a long-held asset, this provision effectively erases decades of unrealized gains for the recipient. The heir who sells within a reasonable time after inheritance may owe little to no capital gains tax on appreciation that accumulated over an entire lifetime of ownership. The IRS also grants inherited assets a long-term holding period automatically, meaning even a sale shortly after inheritance qualifies for the more favorable long-term capital gains rate.

How Carryover Basis Works on Lifetime Gifts (IRC § 1015)

Lifetime gifts follow a different rule entirely. Under IRC Section 1015, the recipient of a gift takes the donor's adjusted basis as their own starting point. The built-in gain does not disappear. It simply transfers from one taxpayer to the next, carrying all accumulated unrealized gains intact.

There is one narrow exception. When a donor has actually paid federal gift tax on the transfer, the recipient may add a pro-rata portion of that gift tax (specifically, the amount attributable to appreciation) to their carryover basis under IRC § 1015(d). This adjustment can modestly reduce the recipient's eventual gain, but it requires filing Form 709 and is best reviewed with tax counsel to calculate correctly.

One additional nuance: when a gifted asset has declined in value, the carryover basis rules change. For calculating a loss on a subsequent sale, the recipient's basis is the lower of the donor's original basis or the fair market value at the time of the gift. In practical terms, the embedded loss disappears at the point of the gift, which is one more reason to think carefully before gifting an asset in any direction.

The Two Exceptions That Catch Families Off Guard

Two important exceptions to the stepped-up basis rule create planning traps for families who assume the step-up applies universally.

The IRD exception. IRC Section 1014(c) explicitly excludes "income in respect of a decedent" (income the decedent earned but had not yet collected before death) from the step-up. Traditional IRAs, 401(k) accounts, deferred compensation arrangements, and installment sale gain receivables all fall into this category. These assets carry their full ordinary income tax obligation through to the heir. There is no basis reset at death. A beneficiary who inherits a \$500,000 IRA will still pay ordinary income tax on every distribution. This is one reason we typically recommend that clients consider IRD assets as first candidates for charitable bequests, reserving stepped-up basis-eligible assets for individual heirs.

The irrevocable trust exception. In April 2023, the IRS issued Revenue Ruling 2023-2, which clarified that assets held in an irrevocable grantor trust (a structure widely used for estate planning, including Intentionally Defective Grantor Trusts, or IDGTs) are not includable in the decedent's gross estate and therefore do not receive a cost-basis step-up at death. This ruling has significant implications for clients who have transferred appreciated assets into irrevocable structures expecting a stepped-up basis. The specific treatment of any particular trust arrangement should be confirmed with qualified legal counsel.

The boomerang rule. IRC Section 1014(e) denies the stepped-up basis for appreciated property that was gifted to a decedent within one year of death if that same property then passes back to the original donor

or their spouse. The rule was designed to prevent deathbed gift-and-inherit strategies designed solely to manufacture a cost-basis step-up.

WHAT THE OBBBA CHANGED AND WHAT IT LEFT INTACT

The One Big Beautiful Bill Act (OBBBA), signed into law on July 4, 2025, made sweeping changes to the federal estate and gift tax framework. For families and advisors focused on the stepped-up basis, the most important headline is what the law did not change.

The \$15 Million Exemption and Its Practical Effect on the Hold-vs.-Gift Calculus

Effective January 1, 2026, the OBBBA permanently increased (absent future legislative change) the unified lifetime estate tax exemption to \$15 million per individual (\$30 million for a married couple), with annual inflation indexing beginning in 2027. This replaced the TCJA provisions that were scheduled to sunset at year-end 2025, which would have reverted the estate tax exemptions to approximately \$7 million per person. For clients who were accelerating gifts in anticipation of that reduction, the OBBBA removed the urgency, though it did not remove the planning opportunity.

According to analysis from Faegre Drinker and Nelson Mullins, this increase represents a significant shift in the estate planning landscape. The annual gift tax exclusion remains \$19,000 per donee (\$38,000 per donee for married couples electing gift-splitting), and the top estate, gift, and generation-skipping transfer tax rate remains 40%.

For families with taxable estates below \$15 million, federal estate tax is no longer the primary planning concern under current law. It is important to note that “permanent” in this context means there is no automatic sunset. A future Congress could reduce the estate tax exemptions through legislation, and advisors across the country are recommending that plans remain flexible. Every planning recommendation in this article should be understood as applicable under current law, subject to potential legislative change.

The Step-Up in Basis Survived the OBBBA: Why It Matters

The OBBBA made no changes whatsoever to IRC Section 1014. The stepped-up basis at death remains fully intact. Heirs continue to receive assets with a basis equal to their fair market value on the decedent’s date of death, regardless of how large those unrealized gains may be.

According to estate planning attorneys at Pierce Atwood and other leading practices, this combination of higher estate tax exemptions and a preserved cost-basis step-up shifts the primary wealth transfer planning question from estate tax avoidance to income tax minimization. For families comfortably below the \$15 million threshold, the most valuable transfer planning tool available is often not a trust structure or a gifting program. It is the disciplined decision to hold highly appreciated, basis-eligible assets until death.

The IRS also issued corrected final regulations in March 2026 (T.D. 9991) on basis consistency reporting requirements. These regulations are recent and their operational details, including any changes introduced by the March correction, should be confirmed with legal counsel before any reporting positions are taken.

For families who have the technical framework right but face challenges with multi-generational coordination, see our analysis of [the governance gap that causes 90% of family wealth plans to fail by the third generation](#).

ASSET CLASS BREAKDOWN: REAL ESTATE, BUSINESS INTERESTS, AND CONCENTRATED STOCK

The hold-vs.-gift decision plays out differently across the major appreciated asset classes our clients hold. Understanding the distinctions by asset type is essential before making any transfer decision.

Real Estate: The Asset Class Most Vulnerable to Gifting Errors

Real estate is the single most common context in which families make costly gifting mistakes. The scenario is familiar: a property purchased decades ago has appreciated dramatically in value, and a parent wants to simplify their estate by transferring it to their children now.

The tax math, however, almost never favors this approach for low-basis real estate. A building purchased for \$500,000 that is now worth \$3 million carries \$2.5 million in unrealized gains. Gifted during life, those gains pass to the children under the carryover basis rules, creating a deferred capital gains tax obligation the heirs will eventually bear. Transferred at death under IRC § 1014, the cost-basis step-up resets the basis to \$3 million and eliminates the embedded gain entirely.

Texas families have an additional planning tool worth discussing with their estate attorney: the community property advantage. Texas is one of nine community property states, and both halves of community property may qualify for a stepped-up basis at the first spouse's death, not just the decedent's half. For a married couple holding a highly appreciated property as community property in Texas, this may significantly reduce or eliminate the capital gains tax on the full unrealized gains, depending on how the assets are titled and classified under Texas law. The specific application of community property rules requires confirmation with a Texas estate attorney.

Closely Held Business Interests: Complexity Amplified

Business interests add another layer of complexity. For clients who have transferred a business interest into an irrevocable grantor trust (a common and otherwise sound planning technique) will not receive a cost-basis step-up at death under Revenue Ruling 2023-2. All unrealized gains embedded in the business interest at the time of the grantor's death remain in the hands of the trust and its beneficiaries. This is a significant planning consideration that is frequently overlooked when clients review existing trust structures.

For business owners whose equity may qualify as Qualified Small Business Stock (QSBS) under IRC Section 1202, the OBBBA brought meaningful changes: the holding period was shortened from five years to three years, and the maximum capital gains exclusion was raised from \$10 million to \$15 million for sales occurring after the law's effective date. The QSBS rules apply specifically to qualifying C-corporation stock and involve a multi-factor eligibility test. For business owners evaluating how QSBS interacts with their transfer planning, the analysis requires careful review – we address the QSBS rules in depth in [Why Your Practice Exit Won't Qualify for the New QSBS Tax Exclusion – And What to Do Instead](#).

Nelson Mullins and other estate planning practices have observed a broader planning trend: for clients with illiquid business assets, the post-OBBBA conversation has shifted toward control, asset protection,

liquidity, and family governance, not just tax minimization. Basis planning must be coordinated with the business succession plan, not treated as a separate exercise.

Concentrated Stock Positions: When Holding for the Step-Up Conflicts With Portfolio Risk

For corporate executives and business founders holding concentrated stock positions, the basis planning decision intersects with a different kind of risk. Holding a large, undiversified position until death preserves the stepped-up basis opportunity, but it also concentrates portfolio risk and creates potential sequence-of-returns exposure if the position declines significantly before death.

Fidelity's planning guidance acknowledges this tension directly: for highly appreciated stocks, bequeathing at death is generally the most tax-efficient outcome, but when a recipient is in a materially lower income tax bracket, the carryover basis on a lifetime gift may produce a comparable after-tax outcome once the reduced capital gains rate is applied to a smaller gain. That analysis requires knowing the recipient's tax situation, the magnitude of the unrealized gains, and the likely holding period after transfer. Under current law, the capital gains rate applicable to a lifetime gift may be 0% or 15%, though rates are subject to legislative change.

One additional planning note: tax-deferred assets (IRAs, 401(k) accounts, and annuities) are not eligible for the stepped-up basis under the IRD rules discussed above. Practitioners recommend treating these accounts as candidates for gifting or charitable giving, reserving cost-basis step-up-eligible equities for testamentary transfer where possible. This kind of asset-by-asset coordination is precisely the work of a comprehensive wealth transfer review.

WHEN GIFTING APPRECIATED ASSETS IS THE RIGHT MOVE AND WHEN IT IS NOT

The general rule of holding low-basis appreciated assets until death is correct for most clients in the \$5–30 million range under current law. But it is not universal. There are legitimate scenarios where gifting an appreciated asset makes financial sense even at the cost of the stepped-up basis.

Four Scenarios Where the Carryover Basis Trade-Off Is Worth It

According to analysis from Signature Estate & Investment Advisors and Charles Schwab's wealth planning team, four situations warrant a closer look at lifetime gifting for appreciated assets.

First: when the taxable estate is likely to exceed the \$15 million exemption threshold, removing future appreciation from the estate, even at the cost of carryover basis, may reduce the eventual estate tax exposure meaningfully. The trade-off between income tax cost and estate tax savings requires a quantitative comparison. **Second:** when the asset has already been transferred into an irrevocable trust ineligible for the cost-basis step-up under Rev. Rul. 2023-2, the basis argument for holding evaporates; the stepped-up basis is already off the table. **Third:** when the intended recipient is in a meaningfully lower income tax bracket, the capital gains tax cost upon a future sale is lower in the heir's hands than it would be in the donor's, potentially offsetting the carryover basis disadvantage. **Fourth:** when the donor is young and the asset is expected to appreciate substantially before death, the future estate tax on that additional appreciation may ultimately outweigh the income tax cost of gifting now.

None of these scenarios produces a simple answer. Each requires individual analysis in consultation with a qualified tax advisor.

The Strategies That Try to Capture Both, and Their Limits

Two advanced strategies attempt to engineer the stepped-up basis in situations where it would not otherwise arise.

Spousal basis optimization, analyzed in detail by financial planning researcher Michael Kitces, involves transferring appreciated assets into the name of the spouse who is statistically more likely to die first, which may allow those assets to receive a full cost-basis step-up while remaining within the family, provided the one-year holding requirement under IRC § 1014(e) is satisfied and the assets remain in the decedent's estate. Timing certainty is obviously not available, which limits this approach to situations with sufficient lead time.

Upstream gifting, outlined by Charles Schwab's planning team, involves transferring an appreciated asset to an older-generation family member (typically a parent or grandparent) who then designates the intended heir as beneficiary. When the older family member dies, the asset receives a full stepped-up basis and passes to the intended recipient with all prior unrealized gains eliminated. Additionally, once an asset is transferred to the older family member, the original transferor has no legal claim to the asset or its ultimate disposition. The strategy depends entirely on the older family member's intent and estate documents remaining aligned with the plan. This strategy also requires genuine family alignment, careful trust drafting, and an honest assessment of the older family member's financial security and creditor situation.

Both strategies involve real legal and tax complexity and require coordination with an estate planning attorney. We recommend them only as concepts to explore in a comprehensive planning review, not as do-it-yourself techniques.

For families where neither holding nor gifting to heirs is optimal, donating appreciated assets to charity offers a third path that eliminates the embedded gain entirely — a strategy we cover in our guide to [charitable giving tax optimization](#).

A DECISION FRAMEWORK FOR FAMILIES IN THE \$5–30 MILLION RANGE

For most families in the range we serve, the decision framework is more straightforward than the complexity of the underlying rules suggests. The default position, clearly articulated by estate planning attorneys at SSB LLC and supported by Fidelity's planning guidance, is this: gift assets with little or no embedded capital gain, or gift cash. Retain highly appreciated, cost-basis step-up-eligible assets until death whenever possible.

This default holds most strongly when: the unrealized gains are large relative to the asset's current value; the taxable estate is comfortably below the \$15 million federal exemption; and there is no irrevocable trust structure already removing the stepped-up basis eligibility. Under the OBBBA's current framework, a married couple in Texas with a combined taxable estate under \$30 million can, in many cases, focus almost entirely on income tax minimization rather than estate tax reduction, and the cost-basis step-up at death is among the most significant income tax minimization tools available under current law.

Three Variables That Drive the Decision

Fidelity's estate planning framework identifies three questions that should anchor the analysis for every appreciated asset in the portfolio.

How large are the unrealized gains? The greater the ratio of current fair market value to original cost basis, the stronger the argument for holding until death and capturing the stepped-up basis. A stock purchased at \$50,000 and now worth \$2 million is a fundamentally different planning situation than one purchased at \$1.5 million now worth \$2 million.

What is the heir's likely tax rate upon sale? If the intended recipient is in a low-income bracket (a younger family member early in their career, for example), the capital gains rate applicable to a lifetime gift may be 0% or 15% under current law, narrowing the after-tax gap between carryover and stepped-up basis outcomes.

Will this asset likely push the taxable estate above the exemption threshold? For clients approaching or exceeding the \$15 million individual threshold, the estate tax exposure on continued appreciation may make current gifting, despite the carryover basis cost, the more efficient outcome overall. The interaction between estate tax exemptions and unrealized gains is precisely the analysis a comprehensive wealth transfer review is designed to perform.

What Texas Families Should Know About Community Property and the Step-Up

Texas's community property classification can significantly enhance the stepped-up basis available to surviving spouses. In community property states, both the decedent's half and the surviving spouse's half of a community property asset may receive a cost-basis step-up at the first spouse's death, compared to only the decedent's half in a separate property state.

For a married couple holding a \$3 million piece of commercial real estate as community property in Texas, the surviving spouse's entire interest in the property (not just the decedent's 50%) may receive a new stepped-up basis at the first death. This may significantly reduce or eliminate the capital gains tax on the full unrealized gains when the surviving spouse eventually sells.

Because community property classification depends on how and when assets were acquired, titled, and potentially commingled, we recommend confirming the community property status of significant appreciated assets with a Texas estate attorney before making any transfer decision.

The transfer decision also intersects with how and when heirs gain unrestricted control of inherited assets – a dimension we address in [The Countdown to Control: Preparing Your Family When Custodial Accounts Reach Termination](#).

FREQUENTLY ASKED QUESTIONS

Q: Is it better to gift assets to my children now or let them inherit them?

For highly appreciated assets (real estate, business interests, or concentrated stock with a low cost basis), it is generally more tax-efficient to allow heirs to inherit them at death rather than receive them as lifetime gifts. Under IRC Section 1014, the stepped-up basis resets the recipient's cost to fair market value on the date of death, potentially eliminating decades of unrealized gains that would otherwise be taxable upon sale. When assets are gifted during life, the recipient inherits the original cost basis under IRC Section 1015 and will owe capital gains tax on all prior appreciation. Consult a qualified tax advisor before making any transfer decision, as individual circumstances and applicable rates vary.

Q: Do all inherited assets get a step-up in basis?

No. Not all inherited assets receive a stepped-up basis. IRC Section 1014(c) explicitly excludes “income in respect of a decedent” (IRD) assets, which include traditional IRAs, 401(k) accounts, deferred compensation plans, and annuities. These assets carry their full ordinary income tax liability to the beneficiary with no basis reset at death. By contrast, directly held real estate, publicly traded stocks, bonds, and revocable living trust assets generally do qualify for the stepped-up basis under IRC Section 1014(a). Because the tax treatment differs substantially by asset type, every estate plan should include a systematic review of which assets are basis-eligible and which are not before any transfer decisions are made.

Q: Do assets in a trust get a step-up in basis when the grantor dies?

It depends on the type of trust. Assets in a revocable living trust are generally treated as owned by the grantor for tax purposes, are included in the gross estate, and typically receive the stepped-up basis at death under IRC Section 1014(a). Assets in an irrevocable grantor trust are treated differently: in Revenue Ruling 2023-2 (IRS, April 2023), the IRS clarified that assets held in irrevocable grantor trusts are not includable in the decedent’s gross estate and therefore do not receive a cost-basis step-up at death, meaning all embedded unrealized gains remain intact and taxable to the trust or its beneficiaries. If you hold appreciated assets in an irrevocable structure, review that trust with qualified legal counsel. The treatment of specific trust arrangements varies and should be confirmed with qualified legal counsel.

Q: What happens to the capital gains tax if I gift appreciated stock to my kids?

When you gift appreciated stock to your children during your lifetime, they inherit your original cost basis under IRC Section 1015, not the stock’s current market value. Every dollar of unrealized gains that accumulated during your ownership becomes taxable to your child when they sell. For example, stock purchased for \$50,000 and currently worth \$500,000 carries a \$450,000 embedded capital gain that transfers with the gift. If instead you held those shares until death, your child would inherit them with a stepped-up basis equal to the fair market value at the date of death, and the prior appreciation may owe no capital gains tax at that point under current law. Gifting cash or assets with minimal unrealized gains is generally preferable to gifting highly appreciated securities.

Q: Did the One Big Beautiful Bill Act change the step-up in basis rules?

No. The One Big Beautiful Bill Act (OBBBA), signed into law on July 4, 2025, made no changes to IRC Section 1014. The stepped-up basis at death remains fully intact under current law. What the OBBBA did change significantly are the estate tax exemptions: according to Pierce Atwood and confirmed by IRS Revenue Procedure 2025-32, the unified lifetime exemption was permanently increased to \$15 million per individual (\$30 million per married couple) effective January 1, 2026, with annual inflation adjustments beginning in 2027. The annual gift tax exclusion remains \$19,000 per donee. “Permanent” means no automatic sunset, but a future Congress could reduce the exemption through legislation. Consult a qualified advisor to evaluate how your estate plan reflects these changes.

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Research Methodology: This article was researched using primary regulatory sources (IRS publications, United States Code), secondary legal and financial analysis (Pierce Atwood, Faegre Drinker, Nelson Mullins, Kitces.com), and industry research (Cerulli Associates, Fidelity Investments, Charles Schwab). All sources were retrieved and verified in March–April 2026. Regulatory thresholds reflect the law as of April 2, 2026.

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