BEYOND 'I DO' · WEEK 4 OF 8

A Generous Spouse, a Surprise *Tax Bill.*

Given with love. Taxed at sale.



Written by Akshaya Senthil Kumar

Last week, a blended family planned intentionally so that no one is paid by accident. This week, a husband gives his wife a gift, and the tax bill arrives years later, addressed to her.

Meet Marcus and Helen, married thirty years. In 1996, Marcus bought stock for $40,000. Today it is worth $1 million. For their anniversary, he transfers all of it into Helen's name.

On the day of the gift, nothing happens. Gifts between spouses who are both U.S. citizens qualify for an unlimited marital deduction, so there is no gift tax (I.R.C. § 2523(a)). The transfer is not a sale, so there is no income tax (I.R.C. § 1041(a)).

The surprise is what travels with the gift.

The gift carries its history. Every asset has a basis, usually what the owner paid for it. When Marcus gives Helen the stock, she takes his basis: $40,000 (I.R.C. § 1041(b)). If she sells for $1 million, she is taxed on $960,000 of gain. At the top federal rates, that is more than $225,000, before New York takes its share.

This principle is nearly a century old. In *Taft v. Bowers*, 278 U.S. 470 (1929), a father gave his daughter stock that had grown in his hands. When she sold, she argued that she could be taxed only on the growth after the gift. The Supreme Court upheld the rule Congress had written: the person who receives a gift takes the giver's cost basis, and the gain that comes with it.

The inheritance would not have (step-up in basis). Had Marcus kept the stock and left it to Helen at his death, her basis would have been its value on that date (I.R.C. § 1014(a)). She could have sold the next morning with almost no gain. It is the same stock and the same spouse, and the only thing that changed the tax bill was the timing.

The deathbed version does not work. Some couples try the reverse: give appreciated property to a dying spouse and inherit it back with a fresh basis. Congress closed that door. If the spouse dies within one year and the property returns to the giver, the old basis stays (I.R.C. § 1014(e)).

A gift in trust needs paperwork. If Marcus gives the stock to a trust that pays Helen income for life, the marital deduction is not automatic. He must make a QTIP election on a timely filed gift tax return (I.R.C. § 2523(f)). If he misses the deadline, the gift is taxable.

A gift is not a private matter in divorce. In New York, the property one spouse gives to the other is marital property, not the recipient's separate property (Dom. Rel. Law § 236(B)(1)(d)(1)). The gift is still on the table if the marriage ends.

What I tell clients and colleagues

- Giving your spouse an appreciated asset? Do you know its basis, and does your spouse?
- Planning to sell soon? Have you compared a gift now with an inheritance later?
- Giving to a spouse who is seriously ill? Have you checked the one-year rule?
- Funding a trust for your spouse during life? Who is filing the gift tax return, and by when?
- Adding your spouse to the deed? Do you know that only half of a jointly owned home generally receives a new basis at the first death (I.R.C. §§ 2040(b), 1014)?
- Is your spouse a U.S. citizen? If not, the unlimited deduction does not apply, and tax-free gifts are capped at $194,000 for 2026 (I.R.C. § 2523(i)).

What is the most valuable thing you have ever put in your spouse's name, and did anyone mention basis?

Akshaya Senthil Kumar, Attorney
akumar@mpl-law.com
717-845-1524