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Tips for Handling a Large Inheritance

A large inheritance can be a life-changing event, and with it comes a lot of responsibility. The sudden acquisition of newfound wealth might result in some initial elation but handling an inheritance can also bring stress and uncertainty. In some cases, a large inheritance can even strain family relationships. This is why it's critical to know how to manage a large inheritance.

Here's our guide to frequently asked questions about inheritance management:

Is Inheritance Taxable?

One of the first things to know when inheriting a large sum is whether the inheritance is taxable. [Taxation](#) of inheritances varies depending on the specific laws of your state and the estate's value:

- **Federal Estate Tax** is imposed on the value of the deceased person's estate. It's only applicable to very large estates that exceed the federal estate tax exemption (currently \$13.99 million for 2025). If the estate value exceeds this exemption, a portion of the estate may be subject to federal estate tax of anywhere between 18% and 40%.
- **State Inheritance Tax** is imposed by some states on the recipient of the inheritance. This tax is typically based on the relationship between the deceased and the beneficiary and the value of the inheritance. Not all states have an inheritance tax.

What's the Difference Between Estate Tax and Inheritance Tax?

An estate tax is levied on the estate of the deceased, regardless of who inherits it, and is paid by an estate's executor before any assets are distributed to heirs. An inheritance tax is generally levied by the state on the heirs of the deceased. Only 17 states and the District of Columbia currently levy an estate or inheritance tax.

The specific rules and rates for estate and inheritance taxes can vary significantly from state to state. Consult with an estate planning attorney or tax professional to understand the potential tax implications of an inheritance and how to invest inheritance to minimize tax liabilities.

Step-Up in Basis Provision

While estate taxes can reduce the value of a large inheritance, the step-up in basis provision offers a powerful tax advantage for beneficiaries.

When you inherit property, whether it's stocks and bonds, real estate, or some other asset, the IRS "steps up" the asset's cost basis to its fair market value (FMV) at the date of the original owner's death. This is a significant advantage when you inherit assets because it will minimize your capital gains tax obligation when and if you sell the assets down the road.

How does the step-up basis work?

If one of your parents purchased stock 30 years ago for \$100,000, and when they die, you inherit that stock at an FMV of \$1 million, that \$1 million becomes the "stepped up" basis of the stock. If you decide to sell all the stock five years later when its value is \$1.2 million, your capital gains tax will apply only to the \$200,000 gain in value after your parent's death. The result is a tax bill savings of nearly \$150,000 if you're in the highest income bracket.

What assets are subject to step-up in basis?

The IRS allows for a step-up basis in value on most inherited assets, resetting their value to current FMV at the date of the benefactor's death. Assets subject to the step-up basis include:

- Stocks, bonds, and mutual funds
- Real estate, including primary or secondary homes as well as land
- Business interests, including ownership in private companies, LLCs, or partnerships
- Appraised personal property like jewelry, art, or antiques

What assets are NOT subject to step-up in basis?

Some inherited assets do not qualify for a step-up in basis. Those include the following:

- Retirement accounts like IRAs and 401(k)s
- Irrevocable trust-held assets
- Gifts received before the benefactor's death
- Annuities and life insurance proceeds
- Jointly held property held as joint tenancy with rights of survivorship
(only the deceased's portion is stepped up)

What If I Inherit Real Estate?

Real estate is subject to the step-up basis provision upon inheritance, meaning that if you sell an inherited home or other piece of property, you'll only pay capital gains tax on appreciation in value that happens after you inherit it. Thus, if your parents purchased a second home for \$500,000, and it's worth \$1 million upon their death, when it passes to you and you sell it a few years later for \$1.2 million, you'll only pay capital gains on that \$200,000 in appreciation.

This doesn't mean selling inherited real estate is always a win, however. Inheriting real estate presents both opportunities and responsibilities. Before you decide whether to keep or dispose of inherited real estate assets, assess the properties' condition, income potential, and long-term value. Consider consulting with a real estate agent and property manager to evaluate whether to sell, rent, or hold onto the property or properties. If you choose to rent, carefully vet tenants and establish a clear rental agreement, or have an

agency manage the rental for you. Remember to factor in maintenance costs, property taxes, and potential capital gains taxes when making decisions about your inherited real estate.

What If I Inherit a Retirement Account?

Handling the inheritance of a retirement account also requires careful consideration and strategic planning. As an heir, you'll likely have several options:

- **Roll over:** If you're eligible, you can roll over the inherited funds into your own qualified retirement account [IRA or 401(k)] to defer taxes.
- **Take a distribution:** You can withdraw the funds, but be aware of potential tax implications, including income taxes and possibly early withdrawal penalties if you're under 59 1/2.
- **Establish a beneficiary trust:** Consider setting up a beneficiary trust to manage the inherited funds and potentially avoid probate.

Remember, however, that retirement accounts do not qualify for a step-up in basis because they are subject to income tax, not capital gains tax.

How to Invest a Large Inheritance

If you're wondering how to manage a large inheritance, especially if a significant portion of it is in cash, there are a lot of options. However, it's best to [consult a financial advisor](#) and accountant to understand the tax benefits and implications of your investments as well as to design an investment strategy that aligns with your long-term financial goals.

Here are some options for inheritance management and investment:

- Invest in stocks or bonds
- Invest in real estate
- Open or contribute to a retirement account

- Pay for higher education for yourself or loved ones
- Start a business or other venture
- Give to charity
- Pay off debts or a home mortgage
- Purchase a primary or second home

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When handling a large inheritance, it's important to obtain professional advice on how to invest your inheritance in keeping with your long-term financial goals and any tax considerations you may have. An [experienced wealth advisor](#) can not only offer advice on where to invest assets, but they can also connect you with other fiduciaries who can assist with inheritance management, including estate or tax attorneys and accountants. [Contact a KAR advisor](#) today for professional guidance on handling an inheritance.

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