

If you've recently inherited artwork, collectibles, or other assets from a loved one, you've probably heard the term **stepped-up basis** tossed around. It sounds complicated, but it really boils down to understanding *how the government values inherited property* and how that affects taxes if you decide to sell it later.

In this blog post, I'll break down the concept of stepped-up basis in a **simple, practical way** you can comfortably share with your siblings. We'll cover how the IRS determines the *fair market value at date of death*, why *qualified appraisals* are crucial (especially for high-value art), what to expect from the *IRS Art Appraisal Services unit* and *Commissioner's Art Advisory Panel*, and how estate tax rules interact with these valuations. Plus, I'll add a *simple timeline checklist* to keep everyone on track for the important IRS deadlines.

What is Stepped-Up Basis? A Simple Explanation

Imagine your parents bought a painting decades ago for \$5,000, and now that you inherit it, its value is \$100,000. The **stepped-up basis** means that, for tax purposes, your basis in the painting is "stepped up" to its *fair market value at the date of your parent's death* (so \$100,000), not the original \$5,000 purchase price.

Why does this matter? Because if you sell the painting immediately for around \$100,000, you pay little or no capital gains tax. But if you sold it later for, say, \$120,000, you'd only pay capital gains on the \$20,000 increase since the date of death.

This reset in basis protects heirs from paying capital gains tax on the entire increase in value during the decedent's lifetime — which can be decades and very substantial.

Key Terms to Know

- **Stepped-Up Basis:** The adjustment of the asset's basis to its fair market value on the date of the decedent's death.
- **Date of Death Value:** The value used for estate tax and stepped-up basis, which typically means the fair market value as of the exact date the person died.
- **Qualified Appraisal:** A formal valuation of an asset conducted by a qualified appraiser following IRS guidelines, essential for high-value estates with valuable art or collectibles.
- **Form 706:** The IRS Estate Tax Return, due 9 months after the date of death, which reports values and may require payment of estate tax.
- **Fair Market Value (FMV):** The price a willing buyer would pay a willing seller for the asset in an arm's-length transaction.

Why Does Fair Market Value at Date of Death Matter?

The *fair market value (FMV) at date of death* is the cornerstone of stepped-up basis. It determines:

1. The value of the estate for estate tax purposes (if the estate exceeds exemption thresholds).
2. The basis you inherit for capital gains tax when you sell the asset.

Fair market value is not just a guess; it is an estimate backed by market data and expert appraisals. For example:

- For a painting, this might involve recent auction prices for similar works, expert opinions, and condition reports.

- For real estate, comparable sales in the neighborhood and appraisals matter.

The IRS expects these values to be reasonable and supported by documentation if the estate value is high enough to require filing Form 706.



The Role of Qualified Appraisals and IRS Scrutiny

When art or collectibles make up a significant portion of an estate—especially if the total estate value surpasses the estate tax exemption threshold—you’ll need a **qualified appraisal** performed by a professional appraiser. This is not optional if you want to avoid headaches with the IRS.

Here’s why:

- **Qualified Appraisal as per IRS Standards:** Must be written, include identity of appraiser, description of the property, the date of valuation, method(s) used, and must be signed under penalty of perjury.
- **Form 706 Requirement:** Estates exceeding the exemption amount must file Form 706 with the IRS within 9 months of the decedent’s death—to report all assets with their FMV, backed by appraisals.

- **Audit and the IRS Art Appraisal Services Unit:** The IRS has a specialized Art Appraisal Services unit that reviews appraisals attached to Form 706 to ensure valuations are accurate.
- **Commissioner's Art Advisory Panel:** If the IRS questions the appraisal, this panel of external independent art experts may review the value.

Without proper appraisals, values can be disallowed or adjusted, which may mean additional estate tax owed, plus potential penalties.

2026 Estate Tax Exemptions and Tax Rates to Know

Year Federal Estate Tax Exemption Maximum Estate Tax Rate 2026 \$12.92 million per individual 40%

For estates under the exemption amount (\$12.92 million for 2026), there is no federal estate tax due, and filing Form 706 may not be required. However, documenting fair market values is still important for establishing the basis of inherited assets.

For estates over the exemption threshold, estate taxes of up to 40% apply on the amount exceeding the exemption. Filing Form 706 on time—with proper appraisals—is critical.

The 9-Month Form 706 Timeline vs. Illiquid Art

One of the biggest challenges heirs face is that **Form 706 must be filed within nine months of the decedent's death**, and any estate tax is generally due then as well. However, artwork and other collectibles are often illiquid and may take time to sell or to obtain thorough appraisals.

Here's a simple timeline:

1. **Date of Death:** The valuation date for fair market value.
2. **3–6 Months:** Begin compiling documentation, secure qualified appraisals of artwork and collectibles.
3. **9 Months:** File Form 706 and pay any estate tax due. The IRS allows a 6-month extension for filing, but extensions *do not* extend the payment deadline.
4. **Later:** Selling assets may occur after tax filing; capital gains calculated based on the stepped-up basis.

Because the IRS expects payment by the 9-month deadline, heirs may need to use liquid assets or estate liquidity planning (like life insurance or loans) to cover estate taxes when <https://fineartshippers.com/what-the-estate-tax-means-for-an-inherited-art-collection/> valuable but hard-to-sell art is part of the estate.

How to Explain Stepped-Up Basis to Your Siblings in Five Simple Points

Here is a straightforward way to summarize this complex topic when family discussions start:

1. **The government resets the value of inherited art or property to what it was worth when our loved one passed away.** This is called the *stepped-up basis*.
2. **This date-of-death value is important because it sets our tax cost basis.** If we sell the asset, capital gains tax only applies to the amount it has risen since then—not all the gains made during their lifetime.
3. **For high-value items, especially art, we need formal appraisals by qualified experts.** The IRS uses these appraisals to check that the values we claim are accurate, so proper documentation is critical.
4. **We must file the estate tax return (Form 706) within 9 months, reporting these values accurately.** The IRS may use specialized units to review complex art valuations.

5. **Sometimes estate taxes are due quickly, even if the art is hard to sell.** It's important we plan ahead to cover these taxes so the estate can handle the payments on time without forced sales.

Final Thoughts: Preparing for Conversations and Tax Steps

Talking about inherited art and taxes with siblings can be stressful, but having a clear, grounded explanation helps. The idea of **stepped-up basis simple explanation** focuses on the *date of death value* as the new starting point for taxes. Appraisals and good documentation protect the estate and the heirs from IRS disputes.

Remember these practical tips:

- Get qualified appraisals done as soon as possible—don't delay until the Form 706 deadline.
- Keep copies of all documentation to support valuations.
- If the estate might owe taxes, explore liquidity strategies early—that helps avoid rushed sales under unfavorable conditions.
- If you or your siblings have questions for experts, make sure to ask: "*What evidence supports this valuation?*" and "*How does this affect potential estate tax and future capital gains tax?*"
- Keep this checklist handy for the nine-month calendar to ensure the estate tax return is filed on time.

Helpful Resources

- IRS Form 706 Estate Tax Return
- IRS Estates and Trusts Overview
- IRS Art Appraisal Services Unit
- Commissioner's Art Advisory Panel (CAAP)