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You Just Inherited Some Stock. Now What?

Financial advisers say not to rush a move, and be aware of the tax implications

When stocks are inherited, there is a mix of the emotional with the financial, advisers say. *ILLUSTRATION: GARY TAXALI FOR THE WALL STREET JOURNAL*

By CHARLIE WELLS

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Most people have a pretty good idea of how to handle inheriting a family member's heirlooms, cash or even real estate. But when stocks are inherited, it can get a little more complicated.

Be they securities in a large public company or private equities in a small family firm, the heart of the issue with stocks is they mix the emotional with the financial, advisers say.

Some may inherit shares in a deceased parent's longtime employer, for instance, and feel a sympathetic attachment that beclouds a sound financial decision. Others may have no idea how, when or where to sell the stocks, and what the tax implications of doing so may be.

Here are four things financial advisers recommend for people feeling confused about a recent stock inheritance.

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1. First, do nothing

Some who inherit stocks might feel the urge to act quickly. The market moves at a rapid pace, after all, so selling right away could be a natural impulse, especially for those who have never owned stocks before.

But fight this feeling, says Nick Holeman, a financial adviser for robo-advisory firm Betterment.

"It can take some time for the estate to settle," Mr. Holeman says. "and you have a lot of other things going on aside from the finances—maybe a funeral, dealing with relatives and wills."

The early phase of an inheritance can be a financially vulnerable one, too. Mr. Holeman warns that while a sudden injection of assets is great for your financial situation, it is also an attractive moment for commission-based salespeople to pressure you into selling your stocks and buying financial products that don't have your needs as a central focus.

"If a salesman or a so-called financial adviser seems to be hounding you to 'get on this really quickly,' be careful," he says.

2. Then, figure out your tax liabilities

An important early step is to calculate what the potential tax liability of selling inherited stocks may be, advisers say. A common misconception: Some people fear that they will be taxed significantly on the appreciation of the asset over the lifetime of the benefactor.

This is incorrect. Federal capital-gains taxes take into account the growth of a stock—one that is not in a retirement account—only from the benefactor's date of death, not the date the benefactor purchased the stock, says Kathleen Campbell, founder of Campbell Financial Partners, a fee-only financial advisory in Fort Myers, Fla.

"The person inheriting just needs to look up the high and low prices on the date of death, average those, and that is the basis," she says.

Some investment companies may not automatically calculate this basis, which can result in an incorrect—and possibly higher—tax liability. Advisers recommend that a beneficiary check with the executor of the will to make sure the basis has been updated.

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>
> —Financial adviser Nick Holeman

Estates subject to the estate tax—currently, those over $5.45 million—have another option for calculating the cost basis. Instead of valuing the estate at the date of death, they may value it six months after, says Vic Hess, president of ButtonWood Advisors in Tucson, Ariz.

"If the estate in total is less than it was at the date of death, you can use the alternate date," says Mr. Hess. "But you can't just pick a couple assets out of it. It's got to be the whole estate, both the ups and the downs."

3. Make a plan to sell

After calculating tax consequences, advisers say that in general, it will probably be a good idea for most people to sell stocks they have inherited.

"Especially if you aren't a sophisticated investor and don't have individual stocks in your portfolio," says Christine Benz, director of personal finance at fund researchers Morningstar Inc.

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Inheriting only one stock, as sometimes happens, or a portfolio of stocks dominated by shares of a single company, comes with the danger that holding on to that one particular stock can overexpose an investor to the fate of that company. Most investors need to diversify, which could mean buying into a product that involves a broad basket of securities, says Ms. Benz.

4. Then, fit the money in with your larger goals

A big mistake that beneficiaries make with stocks is selling them, and then failing to incorporate the cash into a larger set of financial goals.

Regrettably, some will spend it all, says Mr. Holeman of Betterment. What inheritors of stock should do instead, he says, is ask themselves a set of questions, such as: "What are your goals right now? Do you have an emergency fund? Do you have high-interest debt to pay off? Have you not maxed out your retirement contributions for this year?"

It will probably be a good idea for most people to sell stocks they have inherited. *PHOTO: ISTOCKPHOTO/GETTY IMAGES*

Addressing these types of issues should be every inheritor's priority, Mr. Holeman says. If there are still individual stocks left after taking care of these needs, he says, then think about incorporating the stocks into a portfolio.

The thing to remember, he says, is that the inheritor's financial plan is likely very different from that of the person who left them the stocks.

"From what I've seen, a lot of times when you inherit money, unfortunately your parents or friends probably didn't have as well-organized a financial plan as I would recommend," he says. "A lot of times it's a smattering of random stocks and bonds that when you look at it cohesively, don't really match any sort of strategy."

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