**8548. What is “tax basis” and how is it used in determining the amount of a taxpayer’s capital gain or loss?**

 “Tax basis” is a taxpayer’s after tax investment in property. In other words, when a taxpayer acquires property for money, it is presumed to be his or her after tax investment in such property.[[1]](#endnote-1) So when property is sold or exchanged, for purposes of computing gain, the difference between the amount received less the taxpayer’s basis in the property is the taxable gain.[[2]](#endnote-2) Similarly, for purposes of computing a loss (meaning the taxpayer received less than its original cost), the difference between the taxpayer’s basis in the property and the amount received is the taxable loss.[[3]](#endnote-3)

*Example:* In 2012, Asher purchased Apple stock for $1,000. In 2014, Asher sold the stock for $1,500. Asher’s taxable gain is $500, or the difference the amount received and his basis in the stock ($1,500 minus $1,000). Obviously, there would be no tax on the $1,000 received because it would simply be the recovery of Asher’s initial after tax investment in the property, i.e., his basis.

In the alternative, if Asher sold the Apple stock for $500, his taxable loss would be $500, or the difference between his basis in the stock (what he paid for it) and what he received in the sale ($1,000 minus $500). In this case, Asher has a loss because the amount he received is less than what he originally paid.

If the taxpayer acquires property other than by purchase, basis is determined pursuant to different rules. For example, if the taxpayer acquires property from a decedent by inheritance or bequest, the basis in the property is its date of death fair market value.[[4]](#endnote-4)

With respect to the gift of property, the general rule is the donee taxpayer takes the donor’s basis in the property.[[5]](#endnote-5)

*Example:* Asher gifts Apple stock he purchased for $1,000 to his friend Ashley. At the time of the gift, the stock had a fair market value of $1,500. Ashley’s basis in the stock is $1,000, the same as Asher’s. So if she sold the stock for $1500, she would have a $500 gain.

 On the other hand, there is an exception to the rule that the donee taxpayer takes the donor’s basis in the property. This occurs when at the time of the gift, the donor’s basis is greater than the fair market value of the gifted property. In that case, the donee taxpayer’s basis is the fair market value of the property.[[6]](#endnote-6)

*Example:* Asher gifts Apple stock he purchased for $1,000 to his friend Ashley. At the time of the gift, the stock had a fair market value of $500. Because Asher’s basis of $1,000 is greater than its $500 fair market value, Ashley’s basis in the stock is $500. So if she sold the stock for $500, she would have no gain or loss. The reason for this rule to prevent one taxpayer to shift a taxable loss to the other taxpayer. If Ashley had taken Asher’s $1,000 basis, she would have reported a $500 loss rather than Asher.

1. IRC Sec. 1012. [↑](#endnote-ref-1)
2. IRC Sec. 1001(a). [↑](#endnote-ref-2)
3. IRC Sec. 1001(a). [↑](#endnote-ref-3)
4. IRC Sec. 1014. [↑](#endnote-ref-4)
5. IRC Sec. 1015(a). [↑](#endnote-ref-5)
6. IRC Sec. 1015(a). [↑](#endnote-ref-6)