Joint ownership is an inexpensive way to avoid probate

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Tribune Content Agency

Q: My mom sold her property and put all of the proceeds into a joint account that she, my brother and I are listed on. She wants to purchase a small property for all cash, and it would be titled in her name and in my name. When she passes, I would inherit her half of the house. Will I be heavily taxed on this inheritance? Can I avoid probate? What can I do to avoid paying the most money at that time?

A: If you, your brother and mother are owners of a bank account and own it as joint tenants with rights of survivorship, when any one of you dies the other two become the joint owners of the account automatically. The same thing is true of the house. If the home is in your name and your mother's name jointly, with rights of survivorship, if either of you dies, the other will become the sole owner of the home automatically.

Joint ownership of real estate is an inexpensive way to avoid probate, but as you alluded to, you may encounter tax issues down the line depending on how you set up this arrangement. In general, we're not fans of parents and children owning property together as a way to avoid probate.

Let's break this down: When a parent and a child buy a home together, the parent and child are assumed to be equal co-owners of the home. If the home's purchase price is $100,000, the parent and the child are each assumed to have paid $50,000 for their share of the home. When the parent dies, the child inherits the parent's share of the home at the home's value at or around the time of the parent's death. Let's say the home's value was $300,000 at the time of the parent's death. That would mean the parent's share of the home is valued at $150,000.

For IRS purposes, if the child's cost for his half share was $50,000 and the parent's share that he inherited would be $150,000, the cost basis of the property is now $200,000. If the child then sells the home for $300,000, and he wasn't using his home as a primary residence, he wouldn't have a tax to pay on the parent's share of the home, but he'd have a tax to pay on the profit on the sale of his share of the home, or on the $100,000 of gain he realizes.

If the child had inherited the home entirely and was not a co-owner at the time the parent died, the child would not have this tax problem. This is what is generally referred to as inheriting a home at a stepped up basis, meaning the child would inherit the home at the home's value at the time of the parent's death.

Depending on the estate, the value of the home, and other assets, it could be preferable to put the home in a living trust. The trust would own the home. The parent would be the trustee under the trust and the beneficiary under the trust as well. In essence, the parent would own the home as if it was in the parent's name alone. The difference would be that when the parent dies, the document would spell out that the child would become the successor trustee and the successor beneficiary. Without needing to go through probate, the home would pass from parent to child without the tax issues we described above.

This is how it works in 2017. We don't know what, if any, tax law changes may come down in the future, but having a trust would likely solve the issue about taxes owed and would allow you to avoid probate. Some attorneys will prepare living trust documents for a small fee; and if that is the only asset you are dealing with, it might be to your advantage to consider a living trust in your situation.

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