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Is joint ownership with your child risky?



Financial Thoughts

by John Schooler

Parents often want to name a child as a joint owner of a house or other property to avoid the probate process. However, that may not be such a good idea.

Since the probate process can be time-consuming, costly and is public record, people will do just about anything to avoid it.

One of the most popular ways parents try to avoid probate is by naming a child as joint owner of a property, bank account or house. However, many attorneys say this is a mistake. Here is why:

Gift Tax Concern – For example, let's say that a surviving spouse has \$150,000 in CDs in a joint account with Ann, a daughter who lives nearby. There are two other children. The surviving spouse tells Ann to divide the cash equally with her siblings. Ann is a devoted daughter and transfers \$50,000 to each of her siblings. However, by doing so, she's made a gift that's potentially subject to gift taxes.

Circumstances Beyond Your Control – Even if there are no other siblings, joint ownership with a child can become a nightmare because of circumstances beyond your control. For example, if your child has creditor problems, the creditor may go after your jointly held property. Even if your child has perfect credit and handles money well, his or her assets could be targeted someday because of an accident or some other catastrophic event. Your jointly held property may also be at risk if the child is involved in a divorce.

Tax Consequences – For example, let's say you purchase a home and sign a joint ownership agreement with your child. Your child now owns half the house. Under the federal tax law, when someone passes away, the property receives a new basis. This new or "stepped-up basis" is equal to the fair market value of the property at the date of

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death. Thus, the surviving joint tenant (your child) receives a stepped-up basis only on the portion of the property owned by you. On the other hand, if your child were a beneficiary (not a joint tenant on the title), your child would receive a stepped-up basis on the entire property, which could result in a lower capital gain tax.

There are alternatives to joint ownership. One alternative is that if you have a bank account that you want to pass onto a child and avoid probate, consider a pay-on-death designation or, in the case of stocks, a transfer-on-death account.

Another alternative is to establish a revocable trust. Your assets can pass seamlessly to your child through a revocable trust. While you're alive, the assets are yours and are not subject to the claims of your child's creditors. A house or other property can also be left to a child in a revocable trust – with no probate, and the benefit of a stepped-up basis.

Please contact me if you are interested in discussing the above issues in greater detail. We can refer you to a law firm that can help you analyze your situation and find alternatives that are best for you.

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John is a Certified Financial Planner®