

Problems With Joint Tenancy & Other Alternative Probate Avoidance Methods

It Isn't Just The Advantage Of Living Trusts Over A Will And Probate -- It Is The Advantages Of A Living Trust Over Other Alternative Methodologies.

In a single minded quest to avoid probate, people often make the mistake of utilizing alternative probate avoidance methods (other than a Living Trust). If you are to understand how to best handle your assets and estate, then the discussion cannot be confined to the traditional presentation as to the advantages of Living Trusts over Wills and probate; it must include the advantage of Living Trusts over all other alternative techniques. The poor-form methods include the misguided use of Joint Tenancy, adding someone to title of an asset, gift deeds of real property to children (or anyone else), granting signature power, powers of attorney, and other inferior methodologies.

The truly dangerous and insidious aspect to alternative "Probate Avoidance" techniques is how they lull someone into believing what a great thing they are because such alternative methods do often avoid probate with ease. Yet, **one of the biggest mistakes anyone can make is to consider only the probate avoidance aspect of a particular action or strategy while failing to consider other factors and "sleeper" consequences that almost always result**. The pitfalls of these alternative techniques are less obvious and harder to understand because they cut across many complex and distinct areas of tax law, property law, creditor, and liability law -- of which layman and "part-time advisors" are generally unaware or unmindful of.

Hidden Problems & Costs of Alternative Probate Avoidance Techniques

Below is a short list and brief discussion of some of the many negative consequences of alternative techniques. (Subsequent chapters will expand on this more.) Think of them as "sleeper consequences" in that they often are not realized and do not impact or surface until years later when it is way too late and the damage done. Finally, **remember that assets passed through a Living Trust do not suffer any of these grave problems.**

- **Lost Stepped-Up Basis**: Failure to understand or factor the effect on "income tax basis" tops the list as the most typical and expensive blunder. By employing these "poor-form strategies" people are usually forfeiting one of the most generous and valuable tax benefits in all of the tax code -- the "stepped-up income tax basis". If you do not fully understand IRS income tax basis regulations and their typically enormous impact, follow one simple rule: be sure you sit with a tax professional capable of analyzing and explaining this to you before gifting away any asset, adding anyone to title or using joint tenancy during life. Also, as a husband and wife, make sure you understand the generous double stepped-up basis for community property and how joint tenancy destroys this benefit.
- **Gift Taxes**: Put a child on as Joint Tenant to your property and you have just gifted half the value of the property. If the value of that or any gift exceeds \$11,000 the IRS requires the filing of a Gift Tax Return. Failing to file a required return puts you in violation of gift tax law for which there is no statute of limitation.
- **Irrevocable Loss of Ownership & Control**: Add one child as a Joint Tenant and that child is now irrevocably the legal owner of ½ the property in every respect (add 2 children and you only own 1/3rd). There is no legal way to take the gift back and you permanently forfeit the ability to change your mind regarding your estate. (It's theirs now.) You can't sell, you can't gift, you can't move, you can't obtain a loan without them. They can even force a sale and force you out (& collect their share). Too many times clients have come into our office trying to do something with what they perceive as their property and we have to inform them that nothing can be done without all the owners (joint tenants) signatures. They keep repeating that "they don't understand because it is their property" and we have to keep telling them that legally, it is not.
- **Cross Liability & Creditor Exposure**: Since Joint Tenants are legal owners your property is now available for seizure by their creditors. The same can be true with bank accounts and other jointly held assets. If your child has credit problems, becomes entangled in a lawsuit, ends up in divorce court, owes child or spousal support – what was your property before is now all fair game for their debts. They can also give their portion away anytime, to anyone they want -- even lose it in a poker game. You could find yourself co-owners with their ex-spouse or other creditors who by the way want to boot you out, and force the sale, seizure, and collection of property and assets.

- **Watch Out For Amateur Advice To Add Someone To Title In Financing Transactions:** It is bad enough that people on their own, or through “amateur night” advice, are engaging in these risky, tax-negligent, and ill-advised moves. What makes matters worse is that this dangerous practice is also being perpetuated by many in the lending business, including mortgage brokers and title companies. In order to complete some loans, these moves are subtly encouraged with no thought or regard to gift tax law or the many other cascading repercussions and negative consequences of adding someone to title.
- **No Fiduciary Duty:** The trustee of your trust is bound by a high fiduciary duty. On the other hand, none of the alternative techniques afford you the protection of any owed fiduciary duty, meaning if the person wipes you out, you have little or no legal recourse.
- **Medi-Cal Disqualification:** In misguided attempts to deplete their estates and qualify for state paid nursing home, people are often **automatically disqualifying** themselves from any chance of government assistance for 3 years (because of the 36 month “look back period”).
- **No Protection from Conservatorships:** Unlike a trust, alternative techniques afford you no protection from conservatorship. In fact they multiply the chances -- in that the incapacity of any one owner can trigger the urgent need for a conservatorship.
- **End Up In Probate Anyway:** If two sole joint tenants die in a common accident the property will be put through probate with the added complication of contests over who died first.
- **Powers of Attorney Can Be Dangerous, Risky, & Cease To Be Valid At Death:** A power of Attorney has no authority to pass an estate because they cease to be valid immediately upon your death. Further, during life, Powers of Attorney can be a potentially dangerous and risky method of asset management! The person you grant the power of attorney owes little or no fiduciary duty to you or others. You are simply granting them the power to act in your stead. If there is misuse, misrepresentation or misappropriation of the assets there is little recourse available in that it is just as if you did the act yourself. If it is abused or no longer desired, effectively revoking it is quite complex in that it also involves extensive notice to all possible parties where any attempt may be made to use the document.

Why Risk It?

You may think none of this will ever happen to you – except it happens all the time. The point is: Why risk it? Why leave yourself wide open if you don't have to? It should further alarm you that you are not just risking it with your children; the risk potentially extends through to their spouses, their children, their creditors, their whims; and their lives potential disasters and unexpected problems. And risk or not, why would anyone want to destroy the major income tax advantage of stepped-up basis?

Assets Passed Through A Living Trust Do Not Suffer These Grave Problems

Any successful probate avoidance technique needs to also maintain maximum tax advantage as well as maximum protection for you and for those you wish to eventually receive your estate. It is there that alternative probate avoidance methods typically fail in such hidden, miserable and costly fashion. A Living Trust is the only method that will allow you to avoid probate while maintaining maximum tax advantage, flexibility and protection for yourself.

Strategically & Legally Planned Gifting Is Another Matter

There are cases where people consult with their lawyers and accountants to map out a gifting plan. This is usually part of a very carefully crafted advanced estate planning and gifting strategy that takes into account all the income tax, gift tax, as well as other effects and implications. This strategic approach to gifting is an altogether different matter than the non-strategic gifting and asset transfers that usually occur without knowledge or consideration of the numerous unseen consequences.

Methodology that involves extensive planning; experienced awareness and consideration of the issues; and full legal compliance is the only proper approach to any lifetime gifting. Whether it is for the purposes of advanced estate planning, long term care planning, Medi-cal planning, qualifying for government assistance, or simple benevolence; the only intelligent way to go about any lifetime gifting or transfer of assets is with the guidance and assistance of a qualified attorney and CPA. Otherwise you risk a likely host of undesirable, hidden, and costly consequences.