

CASE IN POINT

Sales Tax Estate Planning Underwriting & Product Newsletter

Probate or Capital Gains: A peril of joint ownership



People sometimes go to great lengths to avoid probate costs. The focus can blind them to much bigger costs that may be created by passing assets outside of the estate. I wrote about one of them recently.

I was asked about a case recently concerning an elderly gentleman. Let's call him Joe. Joe was recently widowed and has an only son. We'll call him Nick. Nick is single and is not even seeing anyone. Nick owns his own home. He is the only heir of his father's estate.

Joe wanted to place his home into joint ownership with rights of survivorship, naming Nick as the joint owner. That way, estate settlement would be easier and probate/estate administration taxes would be avoided. What about capital gains considerations?

Nick already owns a home so he would need to declare one of the two homes as his principal residence when he sells one of the properties. Gains on the other home would trigger some capital gains taxes when it is eventually sold. Which home would Nick choose?

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Peter works with independent advisors and other professionals raising awareness on issues and concerns faced by affluent individuals, professionals and business owners. He supports efforts in researching and developing optimal solutions for clients aimed at improving their financial well-being and supporting their personal wishes and lifestyles. He annually provides 100's of workshops, seminars and technical support throughout the country on tax, retirement income and estate planning issues, concepts and strategies to both advisors and consumers. As a Registered Financial Gerontologist, a good deal of his time is spent on building awareness and educating people of all professions who work with or specialize in the needs, expectations and issues of elders. Comprehensive lifestyle planning is an important element of these processes.

The Sales, Tax, Estate Planning, Underwriting & Product (STEPUP) team provides internal and broker support, including seminars, education, advanced concept illustrations & Client case technical consultations.

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Nick thought that Dad's home would be the secondary home and would trigger capital gains on sale. After all, Nick felt he would only own half of it on the transfer now and would trigger a capital gain only on that portion when he eventually sold that house. No big deal, right?

Let's look at this more closely.

Joe and Nick are trading a probate tax of about 1.5% of the value of Joe's home in exchange for a capital gain on 50% of the increased value of that home. If Nick waited awhile to sell the home after Joe, his dad, passed away, the capital gain would apply to the increased value on Joe's 50% as well. In many housing markets, home prices are increasing, some dramatically. The capital gains then could be a lot more than the probate fees avoided.

If Joe were to have a change of heart about where his house was going to go after he passed away, he would find it difficult to unwind a joint ownership transaction. Joe may wish to leave a large amount of money to a favourite cause. He may meet someone, fall in love and get involved in a common law relationship or even get married. Joe may wish to leave the house or a life interest in the house to the new love in his life.

Even if Joe remains single, his son, Nick, could become involved with someone for an extended period of time, including cohabitation or marriage using Dad's home as the residence. Joe's former home could be caught in any division of property or dependency claim dispute. If Nick were to run into financial difficulties or be sued for damages, then Joe's home could get caught in the settlement.

This started as a brief question about using joint ownership to bypass probate. There are lots of actual and potential problems here. The considerations are extensive. The advisor was glad he called me and perhaps a little surprised as well by what he learned.

Probate doesn't have to be the monster some people make of it. Joint ownership is not the fairy dust that makes problems go away. The reality is frequently the reverse.

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