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Joint Tenancy: Tips And Traps

BC Notaries are faced daily with the joint tenancy topic, advising clients when they purchase an asset or they consider transferring their property to a family member.

When assets are owned jointly, each owner has an equal interest in the property; when one of them dies, title will transfer to the other owner.

If the ownership is not equal, for example one individual owns 40 percent and the other one owns 60 percent, that type of ownership is defined as "tenancy-in-common."

Tax consideration must be given when thinking of joint tenancy, particularly in these areas.

- Investment income
- Property acquired by joint tenants
- Issues related to ending the joint ownership because an asset is sold or transferred, or one of the owners dies

Investment Income

If an asset is jointly owned, the owners must report its income based on the percentage of capital that each owner has contributed. Even though the financial institutions will issue one T5 slip in the name of both owners, the taxpayers must allocate the income based on their contribution.

Acquiring Assets

If an asset is purchased and both owners contribute an equal amount, the acquisition would pose no problem. Both owners own 50 percent and when the asset is sold, they would share the gain or loss. The challenge is when the owners contribute unequal amounts.

When assets are owned jointly, each owner has an equal interest in the property; when one of them dies, title will transfer to the other owner.

In that situation, CRA still considers the owners to own an equal share of the asset. The consequence is that the owner with the larger contribution is deemed to have gifted a portion of the asset to the other owner. In that scenario, the joint tenants would agree to this arrangement if they were related and not dealing at arm's length.

The timing of the joint tenancy becomes very important. If the joint tenancy is entered when the asset is purchased, the deemed gift from one owner to the other will not have any tax consequence. If the asset was owned by an individual for a few years prior to the joint tenancy, however, there will be tax consequences because of the gifting provision.

Let's assume father John purchased a house for $500,000 in 2005 and it is now worth $1,000,000.

In 2011, son Frank became joint owner and paid $250,000 to his father. Father John will have given a gift of $250,000 to his son and he will have a deemed capital gain on the gift to his son, to be reported on his tax return in the year they became joint tenants.

An exception to this rule is when the transfer is made to the spouse or common law partner; there is a tax-free rollover provision and no capital gain is realized at the time of transfer. The transferor, however, could elect to accrue the capital gain if there were capital losses from prior years that could be utilized.

Another important planning point on the transfer happens when transferring title of a home or a cottage to an adult child. The reasons for this type of transfer are usually to avoid probate fees or to transfer a portion of the estate prior to death. The transferor could utilize the principal residence exemption to reduce or totally eliminate the capital gain resulting from the deemed gift on the transfer of title.

Terminating the Joint Tenancy Relationship

Joint tenancy terminates when either one of the owners dies or the asset is sold.

If one of the owners of the property dies, two things happen immediately:

- the property transfers to the surviving owner, and
- the deceased is deemed to have disposed of the property at market value, resulting in a capital gain or loss that is reported on the deceased's final tax return. If the property is transferred to a surviving spouse, the tax-free provision rules apply.

If the property is sold, each owner will calculate his or her capital gain or loss.

It is also possible that the owners no longer wish to be joint tenants but would rather be tenants-in-common. If the owners maintain the original share of ownership—50 percent, there will be no taxable disposition.

Once the owners are tenants-in-common, the title of the property would not transfer automatically to the other owner at time of death. The provisions of the deceased's Will dictate to whom the property will transfer.

Although there are many advantages of joint ownership of property, there are also many consequences that must be considered when making the decision to hold legal title in more than one individual's name.

Some of the Advantages

Reduction or Avoidance of Probate Fees

Probate fees are a provincial levy based on the size of the estate. For example, in British Columbia the probate fee is 1.4 percent on values over $50,000. If the asset is owned jointly, title transfers to the surviving owner and the asset does not become part of the estate.

Assisting the Older Parents

It is normal for a child to assist aging parents with their financial affairs. One strategy is to make the child joint owner of the bank and investment accounts. That allows the child to make financial decisions on behalf of the parents.

Will the child make decisions in the best interest of the parents? We see too many cases of abuse where the child puts his or her own interest ahead of the parent's well-being. The other pitfall is that since the asset transfers automatically to the joint owner, the parent's wishes may not be carried out.

Transferring the Family Cottage

One of the estate planning objectives is to transfer the title of the family cottage to the adult children. Joint ownership is often seen as the best way to deal with the transfer, to avoid probate fees and to determine the tax cost of the transaction with certainty.

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Unless the capital gain on the transfer of the cottage is reduced by claiming the principal residence exemption, the transfer will result in a deemed disposition at market value, and the capital gains tax would be considered a prepayment of the tax that would otherwise be paid at time of death.

Any future increase in the value of the property will accrue to the new joint owners. In many cases, the children do not make any cash contribution to the parents, and it is considered an advance on the inheritance. But depending on the financial situation of the parties, it would be appropriate if the children receiving the property would make a contribution toward the tax liability faced by the parents as a result of the transfer.

Although there are advantages with joint ownership, there are also potential issues; in many cases, the risks outweigh the benefits.

Transferring Title on Death

The issue is whether the person who established joint tenancy wanted to transfer title ownership of the property at time of death. For example, in cases where the family home or cottage is transferred to the adult child, usually it is done with the intention to transfer the title of the property before death.

That may not be the case when an adult child's name is added to the bank or investment account of the elder parent to provide convenience and assistance with the parent's financial affairs. Was it the intention of the parent to transfer the assets at time of death?

For example, an elderly widowed parent from Vancouver has 3 children: 1 living in Vancouver, the other 2 living in Toronto. The child living in Vancouver is in a better position to assist the parent with day-to-day banking and investment decisions. When the parent dies and the joint-owned assets transfer to the child living in Vancouver, it is often unclear whether it was the wish of the parent to leave those assets to that child. There are some active litigation cases to that effect.

Potential Problems with the New Owner

When establishing joint ownership with another individual, there are risks associated with the personal life of that individual. For example, the father transfers an asset to his son as joint owner. Some issues affecting the son could impact on the father; creditors can make a claim against the assets. Another problem is if the son is married and later on gets divorced; the ex-spouse will want the assets to be included as a family asset. All those issues could result in the son having to sell the asset.

Loss of Control

When a party has exclusive control of an asset and decides to enter into a joint tenancy relationship, some control is lost. For example, the asset cannot be sold or remortgaged without the other owner's consent.

Tax Liability

When the asset has increased in value, establishing joint tenancy with a person other than the spouse will trigger a tax liability from the deemed disposition or gifting provisions.

In the end, joint tenancy offers many advantages for estate planning purposes…

Hidden Tax Liability for the New Owner

The new owner in a joint tenancy relationship could become liable for the tax liabilities of the previous owner. Under section 160 of the *Income Tax Act*, in a non-arm's length transaction (that is, transfers between related parties), the new owner can be jointly liable for any taxes that arise on the transfer or for any taxes owed by the previous owner, unless the transfer was made at market value.

Funding Issues with the Estate

If an individual transfers assets to a joint owner prior to his or her death, it could create potential funding issues with the estate.

When an individual dies, there is a deemed disposition of all the assets that are not transferred to the spouse. The estate must pay the taxes on the capital gain from the deemed disposition and distribute the residue of the estate as per the instructions in the Will. Property that is held in joint tenancy may result in capital gain that must be reported in the deceased's final tax return but the ownership transfers to the joint owner. Therefore the asset will not be available for sale to fund the tax liability of the estate.

In the end, joint tenancy offers many advantages for estate planning purposes but there are potential risks associated with it. Unless the parties involved understand the consequences, it is a strategy where considerable caution must be used. ▲

Because of the complex nature of this subject, it is strongly recommended that you consult a legal professional and a tax accountant for assistance with this challenging topic. ▲

Andrea Agnoloni is a BC Notary Public practising in North Vancouver. He is also a Certified General Accountant with EPR – North Vancouver, an Independent Firm of EPR Canada Group Inc.

PRIVATE RECIPE

Red Thai Curry and Coconut Chicken

2 to 3 lbs. selected chicken parts (fresh or frozen)
½ cup combined lime leaves and lemon grass
1 litre chicken stock
1 to 2 envelopes coconut powder
1 to 2 cans coconut milk
2 cups chick peas
Red Thai curry: 1 tablespoon to start
½ cup mixed dried/fried onion and garlic flakes

Garnishes
Fresh raw red onion
Ground cashews
Fresh chopped cilantro
Fresh ground pepper
Toasted coconut flakes

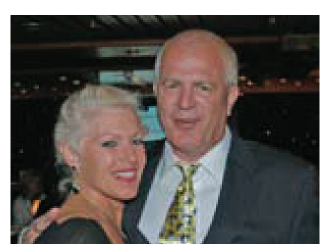
In a casserole dish, pan-fry chicken until brown. Set aside.

In another pot, simmer lime leaves and lemon grass in chicken stock for 1 hour. Remove leaves and grass. Into the chicken stock, combine coconut powder, coconut milk, chick peas, Red Thai curry, and the dried/fried onion and garlic flakes.

Pour this mixture over the chicken and simmer 1 hour or until chicken is cooked.

Garnish as desired with fresh onion, cashews, cilantro, pepper, and coconut flakes.

Serve with rice or noodles flavoured with saffron, sesame, or achiote. Drizzle with sesame oil. ▲



Mary-Ann Mustonen-Hinds and Billy Hinds

Billy Hinds is the husband of Vancouver Notary Mary-Ann Mustonen-Hinds.