



How Should Non-Traditional Partners Hold Title to Property?

By: Tanya D. Simpson, JD, MBA



In my July 2009 article in the WealthCounsel Quarterly entitled *Special Considerations in Planning for Non-traditional Families*, I briefly addressed the topic of how non-traditional partners should hold title to property. This article takes an expanded look at the ways non-traditional partners can take and hold title to property, and some of the advantages, disadvantages, tax consequences and potential pitfalls of each.

Joint Tenancy With Right of Survivorship

As stated in my previous article, non-traditional partners typically come to the table with the assumption that joint tenancy with right of survivorship (JTWROS) is the obvious and best way for them to hold title to their shared property to ensure efficient transfer of the property at their death. Frequently, a real estate or title agent will suggest the partners choose this form of ownership because of the survivorship benefit, but seldom have the partners considered the implications of this type of ownership beyond the right of survivorship.

Most non-traditional partners are aware that JTWROS allows property to pass to the surviving owner by operation of title, thereby avoiding probate. This can be particularly beneficial when one or both non-traditional partners have family members who may not agree with their choice of partner, since this method of passing property at death is not subject to challenge.

JTWROS, however, is not a complete answer to avoiding probate and passing property at death. This method of planning only looks one step ahead to when the first partner dies. When the second partner dies, if no additional planning has been done, the property will be subject to probate. The property will also pass through probate if both partners die simultaneously.

If no additional planning has been done, JTWROS can also pose a problem if one partner becomes incapacitated.

Since this method of ownership requires the signature of both partners to transfer the property, the property cannot be sold while one partner is incapacitated. Absent a durable power of attorney, the incapacity of one partner could necessitate time consuming and expensive guardianship or conservatorship proceedings if the property is to be sold while the partner remains incapacitated.

JTWROS can also be unilaterally severed by one partner without consent of the other by transfer or encumbrance of that owner's separate share. Such action automatically converts the JTWROS to tenancy in common, and the other partner has no recourse to prevent this conversion.

JTWROS also exposes the property to the creditors of each individual partner. With JTWROS, each partner is considered to own a separate share of the property. Thus a creditor of one partner may attach that partner's portion of the property to recover that partner's individual debt.

Another potential pitfall is that when one owner of property that is held JTWROS by unmarried partners dies, §2040 of the Internal Revenue Code requires inclusion of 100% of the fair market value of the property in the estate of the first partner to die, unless the surviving partner can prove contribution to the acquisition of the property. To overcome this presumption, the surviving partner must provide evidence as to his or her contribution to both the down payment and the mortgage payments.

JTWROS is also only available to partners who wish to own equal percentages of the property. If one partner contributes a greater share to the down payment, mortgage payments, or improvements, that partner has made a taxable gift to the other. A taxable gift also occurs when one partner adds the other partner to the title of the first partner's existing property – a commonly overlooked issue among non-traditional partners. It is very important to counsel non-traditional partners who wish to add their

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partner to the title of their existing property that doing so creates a permanent gift that cannot be revoked if they later have a parting of the ways.

Tenancy in Common

Non-traditional partners may choose to hold property as tenants in common (TIC) to avoid some of these potential pitfalls. As TIC, partners can own different percentages of the property, and that percentage can be defined and can change over time by separate agreement. For example, one partner can gift a share of the property equal to his or her annual exclusion amount each year until one half of the property has been gifted. The value of the gifted shares may be reduced by a fractional share discount, due to the reduced marketability of undivided interests in real property. Use of a fractional share discount can allow the partners to equalize their ownership more quickly without exceeding their annual gift exclusion amount.

One partner can also sell a percentage of his or her existing property to the other partner as TIC, either in installments or in contract for proceeds of a future sale. The sale of shares to the partner need not be for fair market value; however, if the shares are sold at an egregious discount, a taxable gift may be inferred. If the sale of shares of property to the second partner reflects an appreciation in property value from the selling partner's initial acquisition cost, the selling partner may incur capital gains tax. If the property in question is the selling partner's principal residence, the selling partner may exclude capital gains up to the allowable amount (currently \$250K). The partners must keep in mind, however, that when the property is eventually sold, whatever capital gains exclusion the original selling partner previously claimed on that property will have been already used up to the extent of the previous exclusion amount. The partners should still be able to claim the unused balance of the then available capital gains exclusion at the time of the later sale.

With TIC, on the death of the first partner, only that partner's share of TIC property will be included in his or her estate. A fractional share discount should also be allowed, since §2040 does not apply to TIC property. Compare *Ellie B. Williams v. Com'r*, 75 T.C.M. 1758 (1998) (fractional discount allowed for estate tax value of share of TIC prop-

erty) with *Estate of Young v. Com'r*, 110 T.C. 297 (1998) (no fractional discount allowed for estate tax value of JTWROS property under §2040).

Unlike JTWROS, with TIC, some estate planning is required to pass title upon death of the first partner. However, probate can still be easily avoided by placing the TIC shares in the partners' revocable living trusts.

Tenancy By the Entireties

Tenancy by the entireties (TBE) is a form of joint ownership with survivorship benefits plus additional asset protection benefits. TBE is not available in all states, and it is only available to married couples. However, with same-sex marriage laws constantly evolving, TBE is available to same-sex married couples in Massachusetts and presumably now in Vermont, with other states likely to come on board in the future.

Unlike JTWROS, where each partner is considered to own a separate share of the property, with TBE, the spouses as a spousal entity own the entire property, thus one TBE owner cannot unilaterally sever his or her property interest. In Massachusetts, creditors may still attach TBE property for the debts of one spouse; however, if the non-debtor spouse survives the debtor spouse, the creditor takes nothing. Creditors may attach TBE property for any debt which is the joint debt of both spouses. Keeping this in mind, to the extent that the spouses are careful to keep their debt separate, TBE affords a level of asset protection that JTWROS does not.

One Partner's Name Only

Depending on the partners' circumstances, there may be situations where it is advantageous for only one partner to hold legal title to the partners' shared property. Some examples include where one partner may own the entire property to begin with and the relationship may be too new for joint ownership to be appropriate. Or one partner may have credit problems that the property may be needlessly subjected to by adding that partner to the title. Or perhaps one partner may earn most or all of the income and thus the partnership would benefit from that partner taking the entire income tax deduction.

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The danger of this method of ownership is that if the second partner contributes to the acquisition or improvement cost of the property and there is no documentation of this contribution, the second partner will have no way to recoup his or her contribution in the event of a break up.

Shared Property Agreements

Regardless of how non-traditional partners hold title to property, a shared property agreement is always a good idea. Such an agreement can detail what percentage each partner owns, what each has contributed and will contribute in the future to the acquisition, maintenance and improvement of the property, and whether and how the ownership percentage will change over time. For the purposes of documentation or equalization of contribution, the value of non-monetary consideration – such as labor to improve the home – can be detailed in the agreement. (Practitioners should take care not to draft any phraseology that could possibly be interpreted as using sex for consideration.)

Non-traditional partners should expressly document their agreed understanding in writing at the time they take title to shared property, or as soon thereafter as possible. While there is a great body of family law that has created known precedent for the disposition of property in a dissolution of marriage, the law regarding disposition of property in a break up of non-traditional partners is sparse and unpredictable. If issues of disagreement about the partners' shared property arise, these issues are much more easily resolved at the time the partners take title to property together, while the relationship is good and minds are not clouded by the emotions of a break up.

Other Considerations

When re-titling property, it is important to look to the laws of your state to determine how issues such as documentary stamp tax, property tax assessment and homestead laws apply. In some instances, these issues are a mild to moderate annoyance. In other instances, these issues have the potential to defeat the goals of the partners' plan. For example, in Florida, persons having minor children are prohibited from devising their homestead property. Thus, if a partner has a minor child from a past relationship or marriage and now has a new partner, the first partner may not devise his or her

homestead property to the new partner, even if the minor child is living full time at the other parent's homestead property. Thus, if the first partner wishes to ensure that the second partner receives the first partner's homestead property upon the death of the first partner, then a vehicle of devise, e.g. a will or a revocable living trust, would not be an appropriate choice to achieve the partners' goal as to that specific property.

Conclusion

There are many options available to non-traditional partners when deciding how to take or hold title to shared property. The most important concept to take away from this article is that, contrary to popular misconception, there is no one right way for non-traditional partners to hold title to their shared property. What is best for any particular partners depends on their unique circumstances, including their finances, their goals, their family situation, and the laws of their state.

Tanya D. Simpson established The Manors Law Firm to help Florida's diverse individuals and families plan ahead to protect and secure themselves and their loved ones in today's rapidly changing legal, political and economic climate. Ms. Simpson holds a Juris Doctorate from Florida State University College of Law, where she was a member and twice-published author of the college's prestigious Law Review, and a twice-competing member of the college's award-winning Moot Court team. She also holds a Master of Business Administration from the University of San Diego, and had a successful career since 1987 in the business and investing fields prior to entering the field of law. For further information or to contact Ms. Simpson, please visit her website at www.ManorsLaw.com.