Chapter 14

Sole and Joint Ownership Considerations

Sole Ownership

Owning property in one name usually is the simplest method and gives the holder the most complete ownership possible. Transfers are relatively easy because, under most circumstances, the holder of title to the property has the absolute right to dispose of it as he (she) wishes—although in some States, one spouse may have to consent to the transfer of real property owned solely by the other because of the dower right available under State law. At death, solely owned property passes under provisions of the will, or if the decedent died intestate, according to the provisions of State law. Federal estate and State death taxes generally apply to the total value of the property held in sole ownership. Outright ownership of property is referred to as “fee simple,” the nearest thing to absolute and complete ownership. For business purposes, sole ownership, also called sole proprietorship, means an unincorporated business owned by a single individual.

Advantages of Nonspousal Co-Ownership

In many States, the probate procedure is perceived to be so cumbersome, time consuming, and expensive that joint property holding (termed joint tenancy in most States) is common. Joint property holding tends to express the common feeling of joint endeavor and mutual accomplishment enjoyed by owners of farm, forest, and other rural properties. It commonly has been utilized as a substitute for more complex business organization arrangements.

Survivorship property ownership arrangements can offer each owner the emotional and financial security of knowing that the mutually acquired property cannot be lost by the survivor, in whole or in part, upon the death of the other. Additional advantages include the ease of understanding and implementing the concept, and the uncomplicated and inexpensive transfer process.

Disadvantages of Nonspousal Co-Ownership

Individuals often become involved in co-ownership without fully realizing what it means in terms of loss of freedom and control and the costs involved. Before or upon death, sales may be difficult to accomplish. One co-owner may want to sell, while the other(s) may not. If a partial sale of an undivided interest is made, the price realized may be less than the sale property’s proportionate share of the fair market value of the property as a whole.

Unintentional termination—In some States, joint tenancy ownership may be severed by a contract to sell to third parties or even by the placing of a mortgage on the property. As a result, the parties may fail to achieve their purpose through an unintentional termination of the survivorship feature.

Limitation on using a disclaimer—The role of disclaimers (see chapter 7) as a postmortem estate planning tool for jointly held property is extremely limited. Only a few States permit a disclaimer of the interest in joint-tenancy property that has been transferred to the survivor. Thus, this highly desirable method of postmortem tailoring of property ownership is not available if not provided for by State statute, and the resultant after-death tax planning generally is denied to the surviving joint tenant.
In general, for Federal estate tax purposes, an individual must make a qualified disclaimer of the interest to which the disclaimer succeeds on creation of a joint tenancy within 9 months after creation of the tenancy [Treasury Regulation 25.2518-2(c)(4)(i)]. It does not matter that a later disclaimer may be valid under State law. This position is based on the fact that the potential disclaimant accepted the property when the joint tenancy was created (Private Letter Rulings 7829008, April 14, 1978, 7911005, November 29, 1978, and 7912049, 1979); therefore it must be disclaimed within the statutorily required 9-month period.

In any case, a qualified disclaimer of the survivorship interest can be made no later than 9 months after the death of the first joint tenant to die. The timing for disclaiming the survivorship interest is not affected by the power of the disclaimant to unilaterally sever the tenancy under local law.

**Post-Death income tax considerations**—Another disadvantage of joint tenancy involves post-death income tax considerations. There are a great many advantageous income tax options available to the estate of a decedent. Because survivorship property passes to the survivor immediately upon the death of the decedent, however, there is no intervening estate to act as a taxable entity. Thus, the surviving joint tenant cannot take advantage of the postmortem tax options generally available to estates, although the non-spousal surviving tenant does receive a “stepped-up” basis for the deceased tenant’s share of the property.

**Real property considerations**—Most States with joint tenancy statutes now permit the creation of joint tenancies in real property by a conveyance to the joint tenant(s) that sets forth the existence of the survivorship feature. Income realized from such property is treated in most States as the separate property of the joint tenants in proportion to their ownership interests. Once established, however, ownership of the income resulting therefrom sometimes becomes an issue. The status of the income is critical to the tax consequences associated with it, particularly with respect to proof regarding contributions by a nonspousal donee or surviving joint owner.

**Federal estate tax aspects**—The estate tax consequences of the death of an individual who has an interest in a joint tenancy are governed by Internal Revenue Code (IRC) section 2040. Section 2040(a) applies to all situations involving nonspousal joint interests. The value of any such joint interest is to be included in the decedent’s gross estate to the extent of his (her) fractional share of the property in cases where: (1) the property was acquired by gift, bequest, devise, or inheritance, or (2) the property was acquired by other means, such as purchase, to the extent that it cannot be determined that the surviving tenant(s) provided consideration for the acquisition of the property. Because it sometimes can be difficult to determine the amount of consideration provided by each tenant, it is very important that accurate records be kept when using nonspousal joint property holding arrangements.

**Spousal Co-Ownership**

A key estate planning element for family-owned forest land is the manner in which the property is held by husband and wife. Typically, the spouses have worked together to accumulate and manage the forest land. The result is a feeling of commonality of ownership, and the intent that the property be controlled by and applied to the use of the survivor as long as he (she) lives.

It is beyond the scope of this book to provide a detailed discussion of the various methods of interspousal property holding among the 50 States. A basic analysis of the application of estate and gift taxes to property transfers within the marital community will, however, be presented.

**Legal Development**

The traditional English concept of jurisprudence was that as long as both spouses lived, they represented a single unit of ownership, with this ownership being represented by the surviving spouse after the death of the other. A blending of this common law concept of the legal unit of husband and wife with the common law theory of joint ownership of property led to the development of tenancy by the entirety.

**Tenancy by the entirety**—Tenancy by the entirety is the joint ownership of real property by spouses with the right of survivorship. Its distinguishing feature is that no partition or severance of the survivorship can be achieved by the unilateral action of either spouse. Many States have abolished this concept as a form of holding real property; others have continued it, sometimes with modification.

**Abolishment of tenancy by the entirety**—Where tenancy by the entirety has been abolished, common law joint tenancy generally may be utilized to create property holdings between husband and wife that have the survivorship feature. Joint tenancy resembles tenancy by the entirety in that both entail a right of survivorship. Unlike tenancy by the entirety, however, joint tenancy additionally permits partition of the property at the will of any of the co-tenants.

**Federal Estate Tax Aspects**

IRC section 2040(b) establishes the concept of a “qualified joint interest.” This concept is defined as “any interest in
property held by the decedent and the decedent’s spouse as (1) tenants by the entirety; or (2) joint tenants with right of survivorship, but only if the decedent and his (her) spouse are the only joint tenants.” For such an interest in property, the value to be included in the decedent’s gross estate is one-half of the value of the interest.

Disadvantages of Spousal Co-Ownership

Several of the disadvantages discussed above with respect to non-spousal joint interests also apply to spousal joint ownership. These include limitations on using a disclaimer and the absence of an intervening estate to take advantage of favorable income tax provisions. In addition, there is the particular disadvantage discussed in the next paragraph.

Basis limitations—Despite the valuable uses of joint property holding arrangements between spouses, there can be problems with respect to basis—particularly for those estates that have values greater than the applicable exclusion amount. Regardless of which spouse provided the consideration, when spouses are exclusively joint tenants in property, one-half of the value of the property is included in the gross estate of the first spouse to die. Although no Federal estate tax is paid on property passing to the surviving spouse because of the unlimited marital deduction, in non-community property States the surviving spouse may receive a stepped-up basis only in that property included in the gross estate of the decedent spouse, depending on how the joint ownership was structured. If the first spouse to die had owned all of the property, a full step-up would have been obtained.

Community Property

Nine States—Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin—derive their concepts of property holding between husband and wife from the civil law rather than from common law. These are the so-called “community property States.” The basic community property concept is that all property acquired by the spouses from the efforts of either during the marriage belongs in common to both. Separate property generally is that owned prior to the marriage or received individually through inheritance or gift.

Generally, in community property States, the surviving spouse is protected to a greater degree in succession to community property than in succession to separate property. At the death of the first spouse, the entire community property receives a stepped-up basis. As well, the profits and earnings from community property, and in some cases from separate property, are considered community property.

Life Estates

A life estate is a limited property interest. The life tenant transfers title of the property to the remainder person, with retention by the transferor of the right to use, enjoy, and perhaps receive income from the property transferred for a term of years or for life. The life tenant has the right to possession of the property. His (her) responsibilities include such things as paying mortgage interest, paying property taxes, and keeping the property in good condition and protecting it. Many States have statutory provisions that require a life tenant whose tenancy includes forest land to practice sustainable forest management on the property. Acting alone, the life tenant generally cannot sell or mortgage the property except with the approval of the remainder person.