Joint Account & Estate Planning

The purpose of this article is to outline the most common forms of joint ownership and to discuss the advantages and disadvantages of holding assets jointly as an estate planning tool.

The two most common forms of joint ownership are Joint Tenancy with Rights of Survivorship (JTWROS) and Tenants-in-Common (TIC).

What is the difference between JTWROS and TIC?

If properties are held as JTWROS, each joint tenant has an undivided interest in the whole property. When one of the joint tenants dies, that person's interest is automatically transferred to the remaining joint tenants, in equal shares. Since the assets do not form part of the estate, they are not included in the probate calculation.

Note: *Laws in Quebec are significantly different from other parts of Canada and estate planning strategies involving the concept of JTWROS are not applicable in Quebec.*

If properties are held as TIC, each joint owner has an equal right to possess and dispose of their ownership interest without the consent of the other owners.

If one of the owners dies, that person's share of the asset is transferred according to the instructions in their Will. Unlike JTWROS, the ownership interest of each joint owner in a TIC need not be equal.

If an individual owns an asset jointly with one or more individuals, they should state clearly whether the asset is to be held as joint ownership with right of survivorship or as tenants-in-common.

How do I create a JTWROS?

Joint ownership can be accomplished by transferring property that you currently own outright to yourself and another person. Be aware that creating a joint tenancy is the same as making an immediate gift, in that you have given up part of the value and control over the property. There are possible tax consequences at the time of transfer and afterwards. (See the section "Is JTWROS an effective estate planning tool?" for a more detailed discussion.)

When is a JTWROS severed?

Severance of a joint tenancy can occur by mutual agreement or unilateral action. Severance of a joint tenancy can also occur by operation of law. For example if one of the joint owners becomes bankrupt, the share of the bankrupt joint owner may pass to the trustee in bankruptcy and the JTWROS becomes a tenancy-in-common.

Financial implications on death of a JTWROS owner

Assets held in JTWROS generally do not form part of the deceased joint owner's estate and therefore are generally not subject to probate.

As for potential tax implications at death, if the asset was held in JTWROS with a spouse or common-law partner (hereinafter collectively referred to as the "Partner") there would be no immediate tax consequences on the death of the joint owner. The surviving Partner would simply inherit the deceased's interest and adjusted cost base (ACB).

If the asset was held in JWROS with anyone other than your Partner, the deceased would be deemed to have disposed of his or her interest in the joint account immediately before death, and his or her estate will be responsible for any taxes as a result.

Is JTWROS an effective estate planning tool?

A key advantage to holding properties JTWROS is the avoidance of probate, making it easier and faster to administer the estate on the death of one joint owner.

However, there are many potential disadvantages to using JTWROS, namely:

1. Immediate tax consequence if an asset is transferred to a joint account with anyone other than your Partner.
2. Claims by creditors of new joint owner.
3. Loss of full control.
4. Problems with true intention of transferor.
5. Creating taxes on principal residence.
6. Family law implications: deemed severance of matrimonial home.
7. Loss of opportunity to utilize testamentary trusts.

Each of these issues is examined below in greater detail.

1) Immediate tax consequence if the asset is transferred into a joint account with anyone other than your Partner

<u>Adding someone other than your Partner as joint owner:</u>

If you own an asset and later transfer that asset into joint names with another person (for example, your adult child), you are effectively making a gift of one-half interest in the asset to that person. Under the Income Tax Act, you are deemed to have disposed of a one-half interest in the asset at fair market value, and any accrued capital gains (fair market value in excess of your adjusted cost base) on that half of the asset will become immediately taxable.

Example:

Mrs. Rich owns an investment account in which she holds 2000 XYZ shares with a FMV of $100,000. Her ACB is $50,000. If Mrs. Rich decides to add her son, Neil, as a joint owner of the account, the tax consequences are that:

Mrs. Rich is deemed to dispose of a 50% interest in the investment account. She is deemed to receive proceeds of disposition of $50,000 for her 50% interest. The ACB of that interest is $25,000

As a result: Mrs. Rich has a capital gain of $25,000 and hence a $12,500 taxable capital gain, in the year she adds Neil as a joint owner.

Adding your Partner as joint owner:

There is no immediate capital gain tax liability if the new joint owner is your Partner, since the transfer is deemed to be on a rollover basis, unless the Partners jointly elect otherwise. The spousal rollover applies where both you and your Partner are resident in Canada at the time of the transfer. However, be aware that the income attribution rules apply, so that all income and capital gains from the transferred property will still be taxable in the hands of the Partner who originally owned the asset.

2) Claims by creditors of new joint owner

With a new joint owner on title, the asset may be exposed to claims arising out of the financial problems of that new owner, specifically, bankruptcy and divorce (i.e. former sons-in-law and daughters-in-law).

3) Loss of full control

Once you transfer the asset to joint ownership, you no longer have full control of the asset. Financial institutions often require joint investment accounts to be joint and several, meaning that one joint owner's instructions will be sufficient to operate the account.

Also, where assets are held as JTWROS, at the death of one joint owner, the asset may be given to the surviving joint owner regardless of a different intention in the Will of the deceased joint owner. You should therefore ensure, before transferring your assets to a joint account, that you indeed intend your new co-owner to be the beneficiary of the asset when you die.

4) Problems with true intention of transferor

Often, aging parents transfer property to their children for no other reason than to avoid probate tax or enable them to help manage their affairs. This is usually done without adequate documentation of their intentions. This can result in costly and acrimonious estate litigation, as family members dispute whether the transfer to the donee (i.e. the recipient of the transfer) was truly intended as a gift or whether it was only to avoid probate.

In Ontario, the case of *Saylor v. Brooks* involved these very issues: the deceased person provided for his three children equally in his Will. One of the children, however, was the joint owner of certain bank accounts and investments with her father and, upon her father's death, claimed ownership over those assets through the right of survivorship. The court held that:

- Where the donee is the independent adult child of the donor, as was the case, there is no "presumption of advancement" (that is to say, the presumption that a gift was intended).
- Rather, there is a presumption of resulting trust (that is to say, no gift was intended).
- Therefore the donee is required to prove that her father had intended to gift the joint investment to her.
- Since she was unable to successfully prove that intention, she was ordered to pay to the estate on account of the joint bank account and investments.

Planning Tip

If a parent wishes to add a child as a joint owner for ease of administration of an account, but does not truly wish to transfer ownership of the account, then he or she should consider using a power of attorney for property instead. A power of attorney for property can be limited to managing a specific account.

5) Creating taxes on principal residence

Often, a parent places his or her home in joint tenancy with an adult child for the purpose of avoiding probate. By adding the child as a joint tenant, the parent may be creating an unexpected future tax burden in that, rather than being able to claim his or her entire home as tax-free under the principal residence exemption, the parent is limited to claiming this exemption on his or her one half interest going forward.

The remaining one half interest, now owned by the child, may become taxable on a future sale, either because the child could not use his or her principal residence exemption (i.e. the child did not live in the home), or the child may own another home in which case the principal residence exemption can only be applied to one of the homes.

6) Family law implications: deemed severance of matrimonial home

We mentioned earlier that a joint tenancy may be severed by operation of law. One situation when this can occur is where a matrimonial home is owned in joint tenancy by one spouse with a person who is not their spouse. In Ontario, for instance, if a spouse dies owning an interest in a matrimonial home as a joint tenant with a third person and not with their spouse, the joint tenancy shall be deemed to have been severed immediately before the time of death.

Consider this scenario:

Mrs. Smith, a widow, adds her adult child Taylor as joint owner on her home to avoid probate when she dies. Taylor’s spouse Casey moved into the home to live with Mrs. Smith. Two years later, Taylor dies. What are the consequences?

- On Taylor’s death, half of the home will form part of Taylor’s estate and be subject to claims by Casey, the surviving spouse.
- Mrs. Smith now finds herself a tenant in common with Casey. This may not be what Mrs. Smith envisaged at all!

7) Loss of opportunity to utilize testamentary trusts

Perhaps the biggest disadvantage of all is that by placing assets in JTWROS, you cannot avail yourself of the potential tax advantages that could otherwise benefit your heirs by placing those assets in a testamentary trust. In a lot of situations, the ongoing tax savings that would result from bequeathing the assets to a testamentary trust might be considerably greater than the one-time saving from avoiding probate taxes through a JTWROS.

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