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TO: OUR CLIENTS AND FRIENDS
FROM: JACKSON M. PAYNE
DATE: MARCH 15, 2023
RE: FINANCIAL STRATEGIES FOR YOUR LIVES AND BUSINESSES

JOINTLY-HELD PROPERTY: INCLUSION IN GROSS ESTATE

Clients have recently asked how property you own jointly with another is treated for estate tax purposes.

Right of survivorship. Joint ownership with right of survivorship means that at the death of one co-owner, his or her interest immediately and automatically passes to the other co-owner. The estate tax rule for property owned jointly with your spouse is easy: one-half of its value is included in your estate. If the joint owner is not your spouse, it depends on how the property was acquired. If it was a gift or inherited, again, one-half is included. (If there are three owners, one-third, etc.) If it was purchased, then the amount includible in your estate depends on how much you and your joint owner (or owners) contributed to the purchase price.

For example, say A and B (unmarried) bought investment real estate for \$30,000 back in 1950. A contributed \$20,000 and B contributed \$10,000. The value has risen to \$1 million at the time of A's death. Because A contributed two-thirds of the cost, two-thirds of the value (\$666,667) is included in A's estate. Had B died first, only \$333,333 would have been included in B's estate. This difference of \$333,334 was caused by a difference of only \$10,000 in contributions at the time of purchase.

The effect of debt. If the property owned jointly (not with a spouse) is subject to debt, the debt will have an impact on the estate tax rule described above. Any debt that is outstanding at the time of death is treated as contributed equally by the joint owners. And payments made to pay down the balance of the debt are treated as contributions to the cost of the property.

Example (1). C and D buy investment property that they own jointly with right of survivorship. C contributed \$20,000, D contributed \$30,000, and a \$50,000 mortgage was taken out. C dies when the value of the property is \$150,000. The balance due on the mortgage is still \$50,000 (only interest had been paid on it). C is treated as having contributed \$45,000: the actual contribution of \$20,000 plus half of the outstanding debt. This is 45% of the cost. Thus, at C's death, \$67,500 (45% of \$150,000) is included in C's estate.

Example (2). The facts are the same as in Example (1) except that \$10,000 of the mortgage had been paid off with the \$10,000 in payments made by C. Now, of the \$100,000 cost, C will be treated as having contributed \$50,000: C's original actual \$20,000, C's mortgage payments of \$10,000, and one-half the debt balance ($\frac{1}{2}$ of \$40,000 = \$20,000). Thus, \$75,000 would be included in C's estate.

Tenancy in common. Another form of joint ownership is tenancy in common in which the co-owners do not have any survivorship right. Thus, for example, if there are three equal co-owners and one dies, his or her interest passes to his or her heirs and not to the other owners. Where a decedent dies owning property held in this form of joint ownership, the fraction of the property's value representing the decedent's ownership share is included in his or her estate. It is irrelevant how much each owner contributed to the cost.

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