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Dave DuVal • Jul. 26, 2019



As tax professionals, we are always seeking ways to add value (and maybe even a little more revenue) to our practices. Few taxpayers realize the importance of making an informed decision on how to title their real property. It is a common practice for property owners to add adult children, other family members, or spouses to the title of their homes and investment properties. Many who purchase real estate, whether it is their primary residence, second home, vacant land held for investment, or rental property, ask their real estate agent for a recommendation on how they should title their property as they sign the final paperwork. The customary choice of title for many people who purchase property with another individual or when adding a person to the title of their property is “joint tenancy,” also known as “joint tenants.” While joint tenancy may be a great option, do our clients understand the nuances of this title choice?

Just like our footwear needs depend on the task before us, every person's tax situation

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gift, transfer the property into a trust, complete a transfer on death (available in some states), or make other arrangements, the property may go through probate at this time. The decedent's portion of the property receives a step-up in basis as of the date of their passing. Considering the amount of tax that could be on the line, it is important for the surviving owners to obtain an appraisal of the property from a qualified appraiser. Comps from real estate agents and from online sites as Zillow may not be enough for the IRS if the basis is ever questioned in audit.

In this article, we will be focusing on some of the income tax considerations of joint tenancy, most pointedly, the basis ramifications. The basis rules for joint tenancy property can get a little complicated, as they differ for income tax purposes, estate purposes, and whether the joint tenants are married or not. It's also important to remember that the rules for real estate and how title is held vary from state to state. Be sure to review the rules for your state.

Basis and Income Tax Rules for Joint Tenants that are Married

- *Income Tax Purposes:* If the married couple files separate returns, one-half of the income and deductible expenses will be included on each of the spouse's separate returns. This is true even if one spouse contributed more or all of the proceeds to purchase the property.
- *Estate Tax Purposes:* Each spouse has a 50/50 share in the property, no matter how much each spouse contributed. After the first spouse dies, the fair market value of the decedent's half of the property will be included in their gross estate. The fair market value will either be the appraised value as of the date of death or the alternative valuation date, which is generally six months after the date of death. The decedent's half of the property, which now has a new basis, will automatically transfer to the surviving tenant (the decedent's spouse).^[1] The surviving spouse's new basis in the property will be the original value of their one-half interest in the

property, plus the one-half step-up in basis from the decedent, minus any

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If each spouse decides to give an equal portion of their property interest to another person, such as their child, then each spouse file a separate gift tax return.

- When one spouse is a not a U.S. Citizen: If a spouse gifts half of an interest in real property to their spouse who is not a U.S. citizen, then a gift tax return must be filed if the total value of the property and all other gifts given to the spouse during the year are more than the annual gift exclusion amount for non-U.S. citizens.[\[4\]](#) For 2019, the gift exclusion amount for non-U.S. citizens is \$155,000.

Basis and Income Tax Rules for Joint Tenants that are Not Married

- Income Tax Purposes: Each tenant includes an equal share of the income and deductions from the property on their individual income tax returns. It does not matter how much each tenant originally contributed to the purchase of the property. When the property is sold, each tenant will report an equal share of any gain from the sale on their individual returns. Depreciation is calculated based on an equal percentage share.
- Estate Tax Purposes: Generally, when a tenant passes away, the amount of the fair market value of the property that gets included in the decedent's estate is determined by how much each tenant actually contributed. However, if the surviving tenants cannot prove their personal contributions to the purchase of the property, the entire fair market value of the property will be included in the estate of the first tenant to die.[\[5\]](#) When this happens, the surviving tenants will determine their own basis in the property by equally dividing the total interest in the property. If a property owner gifts an equal share of the property to another person by adding them to the title, the entire fair market value of the property will be included in the donor's gross estate. This is true even if the donor filed a gift tax return for the half that was gifted. For estate tax purposes the gift is set aside. Any gift tax that the donor paid can be used towards the payment of the estate tax.[\[6\]](#) The surviving tenant(s) will automatically inherit the property, and the fair

market value of the property will be divided equally between the remaining

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tenant. The tenant who paid the mortgage is required to include all payments and any other gifts the tenant may have made to the co-tenant(s) during the year are over the gift exclusion amount for the year.^[7] For 2019, the gift tax annual exclusion amount is \$15,000.

There's nothing like a sturdy, insulated boot to keep our feet warm and protected from the gusts of old man winter. Providing the income tax consequences and basis rules of joint tenancy to our clients will help ensure they are on solid footing and their assets weather the unpredictable storms life can bring.

^[1] IRC §2040(b)(1)

^[2] IRC §1014(b)9

^[3] IRC §2523(a)

^[4] IRC §2523(i)(2)

^[5] IRC §2040(a)

^[6] IRC §2013

^[7] Rev. Rul. 78-362

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