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SHOULD YOU ADD YOUR CHILD'S NAME TO YOUR HOME?

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A married couple generally owns their homestead as "husband and wife," which creates a tenancy by the entireties. At the passing of the first spouse, the survivor becomes the sole owner of the property. After the passing of the second spouse, the property will go through the probate process to be transferred as directed by that spouse's Will, or by the intestacy law if there is no Will. By adding more names to the deed, as long as the owners take title as joint tenants with rights of survivorship, probate may be avoided to transfer ownership to the surviving owners.

Although this may seem simple, there are several factors to consider before deciding whether the potential to avoid probate outweighs the issues that may arise by adding another owner to your homestead.

Homestead Issues. Florida law affords numerous protections for homestead property, including protection from creditor claims, the Save our Homes Cap which offers savings on property taxes, and restrictions on devise and descent. To the extent that a portion of your homestead will no longer be owned by a person entitled to these protections, creditors may be able to attach liens to your property. Although some transfers may allow the property appraiser to revalue the property thereby removing your Save Our Homes cap, the statute currently allows you to add an owner to your property without requiring the property to be reassessed unless that person applies for a homestead exemption on the property.

Assume Mr. and Mrs. Brown add their son, David, to their deed. Later, David is involved in a serious car accident, is sued, and the injured party obtains a large judgment against David. The creditor could then take steps to attach the judgment to David's interest in the Brown's property. Alternatively, David could lose his job, get behind in paying his bills, and file for bankruptcy protection. The bankruptcy trustee may look to his interest in the property to pay his creditors. As another example, if David is involved in a divorce, his wife may attempt to include his interest in the property as part of the settlement.

Capital Gains. When a person inherits property, he or she receives it with a cost basis set at the date of death value.[1] With a gift, the recipient accepts the donor's cost basis. For example, assume Mr. and Mrs. Brown purchased a home in 1975 for $100,000. The home worth $300,000 at the time of transfer as well as on the date of death of Mr. and Mrs. Brown. If they add their child or children's names to the deed, they are making a life time gift, and should file a gift tax return which may reduce Mr. and Mrs. Brown's estate tax exemption amount.

[1] The current estate tax code eliminates both the estate tax and the step-up in basis in 2010. However, on January 9, 2009, H.R. 436 was introduced into Congress, which will eliminate the estate tax repeal in 2010, eliminate the carryover basis, and set the estate tax applicable exclusion amount at $3.5 million.

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Then, when their child sells the property, he or she will pay capital gains tax based on the selling price, say $300,000, less their basis, which in this example is $100,000. The long term capital gains tax rate is currently 15% (there is no guarantee that Congress will not increase the rate), which would result in a capital gains tax due of $30,000, if the recipient owned the property for over one year. If instead, they inherited the property, there would be no capital gains tax due unless they sold it for more than $300,000.

Gifting Issues. As previously stated, adding another owner to property constitutes a gift of a portion of the property. What if Mr. and Mrs. Brown change their mind and ask David to sign a deed transferring his interest in the property back to them? David would be making a gift, and may need to file a gift tax return. If the family dynamics are good, David may agree to execute a deed transferring his interest back to his parents. However, problems could arise if for some reason David was unable to execute a deed. For example, if David became incompetent, a guardian would have to be appointed to protect David's interests. The guardian may not find transferring his property to his parents to be in his best interest. Perhaps David became insolvent, which could possibly classify a transfer to his parents as fraudulent. Or, maybe David just does not wish to make such a transfer. Any of these outcomes have the potential of complicating the Brown's estate plan. The transfer may require additional costs and complications.

This situation becomes more complicated if there is more than one child. The parents may add only one child to the deed, expecting that child to then sell the property after their passing and share the proceeds with his siblings. There may be reasons why that child is unable or unwilling to do this. Again, this may require that child to file gift tax returns when he distributes the proceeds to his siblings.

Additional Concerns. There may be other concerns or details associated with this transaction. If a mortgage is sought or if the property is sold, then all owners must sign documents. If the property is already mortgaged, then the transfer to the child may violate the terms of the current mortgage. The mortgagee may need to consent to the transfer, and documentary stamp taxes must be paid with any transfer. In addition to these issues, if the parents expect to apply for public benefits such as Medicaid, they will need to make sure this transfer complies with the program's gifting rules.

Most parents do not expect these issues to arise in their families. However, real life statistics suggest otherwise. Before adding another person as an owner of your homestead, you should discuss these issues and any other concerns you have with your attorney who can advise you on how best to structure your estate to meet your objectives.

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