The Importance of Proper Asset Titling

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Overview

For many farmers and ranchers, the land is the most significant asset that is owned, at least in terms of value. Land value often predominates in a farmer or rancher's estate. How the land is titled is important. Holding title in the proper form facilitates estate planning in accordance with expressed goals and can ease the tax burden upon death or upon subsequent transfer of the property by the heir or heirs. Conversely, failing to title property appropriately can undermine estate planning expectations, create family disharmony and result in a higher tax burden.

The distinction between co-tenancy and joint tenancy and why it matters – it's the topic of today's post.

Tenancy-In-Common

A tenant in common holds an undivided interest in property that does not terminate upon the tenant predeceasing surviving co-tenants. Upon the death of a tenant in common, that person's interest passes under that person's will (or in accordance with state law if there is no will (or trust)) to heirs of the deceased cotenant. For federal estate and state inheritance/estate tax purposes, only the portion of the property owned by the deceased tenant in common is included in the decedent's gross estate at death and receives a fair-market basis at death.

Joint Tenancy

The distinguishing characteristic of joint tenancy is the right of survivorship, with the surviving joint tenant or tenants taking all upon the death of a fellow joint tenant regardless of the terms of the deceased joint tenant's will. In other words, when a joint tenant dies, the deceased joint tenant's share in the property passes to the surviving joint tenant (or surviving joint tenants). It does not pass to the heir of the deceased joint tenant (tenants). Upon the death of the last of the joint tenants to die, the joint tenancy is extinguished.

In addition, upon a conveyance of real property, transfer to two or more persons generally creates a tenancy in common unless it is clear in the deed or other conveyancing document that a joint tenancy is intended. A joint tenancy is created by specific language in the conveyancing instrument. That specific language, often referred to as "magic words of conveyance," clearly denotes the survivorship feature of a joint tenancy. In addition, unless the conveyancing instrument is clear in its intent to create a joint tenancy, the legal presumption is against joint tenancy and that a tenancy-in-common was created. For example, assume that O conveys Blackacre to "A and B, husband and wife." The result of that language is that A and B own Blackacre as tenants in common. To own Blackacre as joint tenants O needed to convey Blackacre as required by state law to create a joint tenancy. The language

for creating a joint tenancy is typically to "A and B as joint tenants with rights of survivorship" or to "A and B as joint tenants with right of survivorship and not as tenants in common."

Except for husband-wife joint tenancies, the survivorship feature may generate an unacceptable property disposition pattern upon death. However, on the death of the first of the joint tenants to die, probate may be simplified or eliminated with title obtained by the surviving joint tenant perfected by showing non-liability for taxes and by proving the death of the decedent by affidavit or death certificate. This is possible in most (but not all) states.

When it cannot be determined that two (or more) joint tenants have died other than at the same time an interesting problem may arise. Most states have enacted a simultaneous death statute to handle just such a situation. Such statutes typically provide that the jointly held property is to be divided into as many equal shares as there were joint tenants and that the share allocable to each joint tenant is to be distributed as if such joint tenant had survived all of the other joint tenants.

A major estate planning limitation of the joint tenancy form of property ownership is that the survivorship right of joint tenancy precludes the use of the life estate-remainder arrangement for the nonmarital portion of the estate to reduce the death tax burden upon the survivor's death. The entire property, therefore, will pass to the survivor and may be taxed again in the survivor's estate. In addition, another problem with joint tenancy is that each joint tenant has a right to sever the joint tenancy relationship unilaterally (except for tenancies by the entirety). As a result, a joint tenant furnishing consideration for acquisition of the property in effect grants to the other tenant a revocable interest that could be partitioned and severed at any time. Consequently, each co-owner has the power to amend or destroy the other's estate plan.

For marital joint tenancies, upon the death of the first spouse, one-half of the date-of-death value of the jointly held property is included in the first-spouse's estate. However, the full value of the jointly held property is included in the first spouse's estate (and receives a date-of-death income tax basis in the hands of the surviving spouse) if the marital joint tenancy was established before 1977 and the spouse that bought the property died after 1981 (*Gallenstein v. United States, 975 F.2d 286 (6th Cir. 1992)).*

Joint tenancy is not a cure-all for tax planning but, depending upon the circumstances, it may be a convenient means of owning and passing property. For total estates of each of the husband and wife under $22.8 million (for 2019), there is no federal estate tax liability. Therefore, joint ownership may serve a useful purpose as a will substitute in the first estate for estates that are not potentially subject to federal estate tax. However, since it is not known which joint tenant will die first, the estate of the surviving joint tenant will be subject to probate as an intestate estate (where death occurs without a will), unless the survivor prepares a will or otherwise disposes of the property. For combined spousal estates exceeding $22.8 million (for 2019) in value, joint tenancy ownership may expose a portion of the total estate of the surviving joint tenant to additional taxes, causing an otherwise unnecessary reduction of the estate assets passing to the heirs or other beneficiaries.

Recent Case

A recent case from Texas illustrates the difference between tenancy-in-common and joint tenancy. It also illustrates how misunderstandings about how property is titled can create family problems. In *Wagenschein v. Ehlinger, 581 S.W.3d 851 (Tex. Ct. App. 2019),* a married couple had seven children. The parents also owned a tract of land. Upon the last of the parents to die, each child held an undivided one-seventh interest as tenants in common in the tract. In 1989, the heirs sold the land but executed a deed reserving a royalty interest. The deed reservation read as follows: "THERE IS HEREBY RESERVED AND EXCEPTED from this conveyance for Grantors and the survivor of Grantors, a reservation until the survivor's death, of an undivided one-half (1/2) of the royalty interest in all the oil, gas and other minerals that are in and under the property and that may be produced from it. Grantors and Grantors' successors will not participate in the making of any oil, gas and mineral lease covering the property, but will be entitled to one-half (1/2) of any bonus paid for any such lease and one-half (1/2) of any royalty, rental or shut-in gas well royalty paid under any such lease. The reservation contained in this paragraph will continue until the death of the last survivor of the seven (7) individuals referred to as Grantors in this deed."

An oil and gas company drilled a producing well in 2010 and began paying royalties to the heirs. As each heir died, the credited their royalty interest to the surviving heirs of each deceased heir. That had the effect of increasing the respective royalty payments of the surviving heirs. There were no problems until 2015. In 2015, a child of a deceased heir sued claiming that the deed crediting the royalty reservation to "Grantors and Grantors' *successors"* created a "tenancy in common" and not a "joint tenancy". If the deed created a tenancy in common, the children of the deceased heirs, rather than the surviving heirs, would inherit their parents' royalty interests. The trial court disagreed, noting that while the deed used "successor", it only did so once and clearly and unambiguously reserved the royalty interest to the heirs and the "survivor[s]" of the heirs, rather than their "successors", "heirs" or "beneficiaries." As such, the trial court concluded that the deed unambiguously created a joint tenancy with the right of survivorship, rather than a tenancy in common that the children of the deceased heirs could inherit. Thus, as each heir died, their interest in the tract passed to the surviving siblings, not their children. On appeal, the appellate court affirmed. Further review was denied.

Conclusion

Properly titling property is important for various reasons – not the least of which is to fulfill expectations on property passage. In the Texas case, confusion over how property was titled resulted in a family lawsuit. Regardless of how the case would have been decided, some in the family would not be pleased.