

Using T.O.D., P.O.D and Joint Ownership Arrangements to Avoid Probate

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What is Probate?

Probate is the court procedure that validates a deceased person's Will and authorizes the passage of assets to heirs of the deceased person. The process involves making an inventory of the deceased person's assets, paying the deceased person's obligations, and distributing assets to heirs. The probate process can take approximately 12 months to complete and involves the payment of filing fees to the court, publication fees to the local newspaper and attorneys fees.

Is Probate Avoidable?

There are several methods that may be utilized to avoid probate. Among them is the use of pay on death, referred to as P.O.D. or transfer on death, referred to as T.O.D. designations and joint ownership arrangements.

Joint Ownership

Joint ownership of an asset carries with it a right of survivorship. When one of the joint owners of an asset dies, the asset passes to the survivor outside of the probate process. Establishing a joint ownership arrangement creates an ownership interest for all persons who are listed as joint owners. Joint ownership arrangements can be used on bank accounts, brokerage accounts and real estate. Care should be used in establishing joint account arrangements for IRAs, Annuities, 401(K) plans and other similar tax deferred investments as changing ownership is likely to create a taxable event. Adding joint owners to CDs may also trigger penalties.

Although joint ownership carries with it the benefit of probate avoidance, it also carries potential problems. In a joint ownership arrangement all joint owners have an ownership interest in the asset; therefore the asset is subject to claims against all of the owners. Consequently if one of the owners of a joint asset is liable to a creditor, the creditor may be able to attach the jointly held asset. Problems may also arise if the original owner of the account desires to sell or liquidate the asset, as all joint owners may be required to agree to any such sale or liquidation.

Additionally, depending on the value of the assets for which joint account arrangements are made, a gift tax return may have to be filed with the Internal Revenue Service. Taxable income may also be reported to all joint owners if the joint asset earns interest or is sold.

Transfer on Death and Pay on Death Designations

Like joint ownership arrangements, P.O.D. and T.O.D. beneficiary designations are another tool that can be used to avoid probate. The owners of bank accounts, brokerage accounts, IRAs, CDs and other similar accounts can arrange for those accounts to be paid to specified individuals on the death of the owner of the account. T.O.D. and P.O.D. designations are fairly simple to accomplish. Generally the bank or company in which the account is held can assist the owners in making P.O.D. or T.O.D. designations at no charge.

A T.O.D. designation can also be made by the owner of real estate. In making a T.O.D. designation relative to real estate, the owner of the real estate files with the applicable Register of Deeds office a deed indicating that the property will pass to designated beneficiaries upon the death of the owner.

Unlike joint ownership arrangements ownership of assets does not pass to the beneficiaries until the owner dies. Therefore, no gift tax return is required, and, during the lifetime of the owner, problems with potential creditors of joint owners are avoided. Additionally all taxable income earned will be reported to the owner and the owner would retain the full and sole right to sell or liquidate the asset.

What are limitations of T.O.D. and P.O.D. designations and Joint Ownership Arrangements?

Although joint ownership arrangements and P.O.D. and T.O.D. designations are an effective tool for avoiding probate, they do not have the level flexibility or as some planning options. For example, a living trust can contain provisions for protection against creditors, trusts for minors, provisions for disabled persons, and contingencies for deceased beneficiaries that cannot be accomplished in joint ownership arrangements and P.O.D. or T.O.D. designations.