Risks of joint bank accounts

By Roxanne Hawn • Bankrate.com

Highlights

- No one can stop a joint account owner from withdrawing all funds.
- An account is at risk from creditors or liens against either owner.
- There are better ways to achieve the same goals with less risk.

Most consumers sock away cash into bank accounts -- checking, savings, certificates of deposit -- to maintain liquidity. But opening a joint bank account, whether with family members or business associates, has potential pitfalls even as it offers convenience.

While pooling your money may imply love or trust, the ramifications of joint accounts can elude both parties. Here's what you need to know.

Rights of ownership

Drama most often crops up during marital discord, but the same drawbacks apply to joint banks accounts held by:

- Minor children and parents.
- Elderly parents and adult children.
- Cohabitating couples.
- Roommates.
- Business partners.

"You can have a joint account with anyone in the world, but once we're jointly on that bank account, once we sign the papers, both of us have 100 percent rights to that account," says Sandra M. Radna, a family attorney with Radna & Androsiglio in New York.

No matter who started the account or who put in more money, she says, "In the eyes of the law, you're equal holders."

Account co-owners enjoy the right to spend, give away or transfer funds to other accounts, without the consent or knowledge of other account holder(s). In many cases, the "wronged" party can get back some of the money, but legal action is required.

"There is no protection for either party with a joint account," says Brent Adams, senior vice president at Private Bank of Buckhead in Atlanta. "There is nothing (the bank) can do to protect either party if the other person comes in and withdraws all the money."

Rights of survivorship

In addition, most joint accounts carry rights of survivorship. "So, if one of the joint holders dies, there is nothing the surviving joint owner has to do to get that money," says Radna.

That can be an upside, but there may be unexpected consequences. Mahlia Lindquist, an estate lawyer in Boulder, Colo., says, "You may unintentionally subject your assets to the claims of someone else's creditors, disrupt your estate plan and trigger higher taxes."

In many cases involving families, the added co-owner of the account upholds wishes for financial sharing upon the other's death. However, when you give money outside the normal estate settling process, "gift" taxes can come into play.

Risk of tax triggers

If someone other than a spouse is co-owner of a bank account while all parties remain alive, additional tax issues may arise.

"When you put money into an account, it isn't necessarily a gift, but if that person takes money out of the account in excess of the $13,000-a-year limit, then that would be treated as a gift, and you might have a gift tax filing requirement," says Benjamin C. Sullivan, an associate with Palisades Hudson Financial Group, in Scarsdale, N.Y.

Risk of debt collection, credit damage

Joint bank accounts lay open to:

- Overdraft charges.
- Debt collection.
- Liens.
- Judgments or garnishments.
- Divorces.

Even in cases where joint account holders are not married (or perhaps not even related), what happens in one person's life can affect the other's financial stash.

Here are a few examples:

- An elderly parent puts an adult child as a co-account owner. If that adult child gets divorced, the account can be considered part of the adult child's assets, even though the implicit understanding is that it's the parent's money.
- A grandparent opens a joint bank account with a grandchild to save for college, but sometime later, the grandparent faces a lawsuit or goes bankrupt.
- Either party uses the account as collateral for a loan, then defaults.

"In most cases, if it's with a child or an elderly relative or maybe a casual business associate, we think there are much better ways to structure your assets than just to have a joint bank account with those people," says Sullivan.

How to protect your joint account

Financial advisers suggest you can do a few things to make the account a bit safer.

- Keep minimal amounts of money in joint bank accounts for day-to-day use.
- While they are more common with commercial accounts, set up criteria for account transactions requiring two signatures through the bank.
- Use online banking alerts to monitor account activity.

The motivation for joint bank accounts is often rooted in "wanting to take care" of someone -- just in case. But, you can do essentially the same thing in other ways.

- For spouses or other people you want as direct beneficiaries: Set up the accounts to "pay on death."
- For elderly parents, spouses or family members: Set up durable powers of attorney, which give access to accounts in certain circumstances (illness, incapacitation, etc.).
- For minor children: Set up accounts in trust or UTMA -- Uniform Transfer to Minors Act -- where you can serve as custodian, but the money is legally the child's.