

## Life Estates

**Life estate** - an interest whereby the person possessing the life estate interest may use, reside in, and benefit from a piece of real estate – such as receiving rent from the property (whether a residence, commercial property, or vacant land) for a specific person’s lifetime (usually the same person’s lifetime).

**Life estate pur autre vie** - where the life tenant’s interest is not based on his/her life (but based on the lifetime of another person).

**Life tenant** - the person who has the life estate interest

**Remainderman** - the person(s) or entity(ies) who will be 100% owner(s) of the property after the life estate interest ends (normally when the life tenant dies). Usually, the remainderman is the title owner, who owns the property subject to the life estate.

**If you own real property and wish to transfer it to your children or someone else (common reasons are to start the five year look back period for Medicaid planning or to have the property not be subject to probate), the benefits of keeping a life estate interest for oneself are...**

(a) to be able to reside in the property (if it is residential property).

(b) to be able to collect the rent money (if the property is rented out),

(c) to be able to farm the land (if it is farmland), or collect a fee (or percentage of crops) if the life tenant allows another person to farm the land.

(d) to be able to receive the real estate tax benefits that a homeowner of residential real estate qualifies for when residing in the property as one’s principal residence. New York State Department of Taxation & Finance recognizes the life tenant as the “owner” for purposes of STAR and Enhanced STAR. The life tenant may also qualify for other property tax exemptions, such as for veterans.

(e) to be able to receive some of the sales proceeds if all of the parties, including the life tenant, agree to sell the property during the life tenant’s lifetime. The Internal Revenue Service has a table that provides how the sales proceeds are to be apportioned between the title owner(s) and the life tenant(s). The age of the life estate owner is a factor. The ages of remaindermen aren’t factors.

(Unless the deed transferring the property subject to the life estate prohibits selling of the property, the title owner may sell the property subject to the life estate, in which case it would not require the life tenant’s permission nor would it provide sale proceeds to the life tenant.)

(f) to know that the property will pass at death not subject to one's debts (subject to possible Medicaid claim if five years had not passed from transfer, and possibly also subject to a creditor's claim if the creditor can show that the transfer was a fraudulent conveyance).

(g) to know that retaining a life estate does keep the "step-up basis" in the property upon one's death. This is because the full value of the property at the time of death is still included in the estate for estate tax purposes (even though the property is not subject to probate or administration). The "step-up" basis at the owner's death is equal to the fair market value of the asset.

For example, if a parent buys a home for \$18,000.00 in 1960 and the property is worth \$300,000.00 at the time of the parent's death, the fact that the parent had transferred the property to his/her children subject to the parent's life estate, means that the children's basis in the property is \$300,000.00. The children could sell the property for \$300,000.00 and have no capital gain, and hence no capital gains tax to pay. If the children sell the property for more, they would pay taxes on the amount over \$300,000.00 (assuming that the extra amount isn't due to improvements they have made to the property).

If the parent had not retained a life estate, the children's basis in the property would be equal to the parent's basis at the time of transfer. In other words, the \$18,000.00 the parent paid for the property plus all improvements.

**Note that transfers of real property subject to mortgages have limitations. Check that the grantee falls under the provisions of 12 U.S. Code § 1701j-3 - Preemption of due-on-sale prohibitions, so that the mortgage company cannot demand payment of the mortgage in full upon the transfer. (The Garn/St. German Depository Institutions Act of 1982.)**

Further, as a general rule, you should not transfer your home to your children until you have resolved any considerations of selling the property, wanting to obtain a reverse mortgage, or obtaining free or low-cost home repairs available to homeowners.

#### **Responsibilities/duties of life tenant.**

- (a) The life tenant protects and maintains the property, and keeps insurance on the property.
- (b) The life tenant pays the real estate taxes on the property (unless otherwise specified by the document granting the life estate interest).
- (c) The life tenant pays association dues, utilities, and makes necessary repairs (unless otherwise specified by the document granting the life estate interest).
- (d) The life tenant pays the interest on any mortgages (unless specified otherwise specified by the document granting the life estate interest. Often, the life tenant also pays the principal.)

**Can the life tenant take out any loans/mortgages against the property?** A lender would most likely want the life tenant and the remaindermen to all sign for a mortgage. A life tenant alone should not be able to get a loan or mortgage against the property. If somehow a life tenant is able to do that, the life tenant and her interest is solely liable for the debt. It does not encumber the remainderman's interest/ownership. Whether or not the lender can foreclose and force a sale of the property, with the remainderman receiving payment for his/her interest, is questionable.

### **What happens if a person has a life estate interest and applies for Medicaid benefits?**

If you are later in a nursing home or assisted living facility, and you are receiving Medicaid benefits:

(a) if the home is sold during your lifetime, then you are entitled to receive some of the sales proceeds (and you will have to repay the state for the Medicaid benefits you have received, and if there is any money remaining, then you will have to privately pay the nursing home until the money is gone).

(b) if the home is rented out, then the rent money can be used to pay the costs of maintaining the home (real estate taxes, homeowner's insurance), with any excess going to the nursing home as a partial payment towards your nursing home expenses.

The above assumes that the five year look back period had passed, as you are receiving Medicaid benefits.

Currently, New York State does not require the home to be sold or rented out. That is solely the choice of the remainderman. Nevertheless, language can be put in the deed that restricts the life tenant's interest from being transferred or sold.

### Sample Life Estate Clauses for Deeds

The grantor reserves the right to the exclusive use and occupancy of the premises during her lifetime, with the Grantor to pay all maintenance and repair costs, water and sewer charges, insurance charges, and taxes relating to said premises. Said life estate shall be personal to the Grantor, and shall not be subject to assignment or lease, except as otherwise provided in the following paragraph.

The grantor reserves life use and occupancy of the premises during her lifetime and reserves the power to appoint the remainder and/or her life use in the premises to any one or more of her issue. This power of appointment shall be exercisable or may be relinquished during the grantor's lifetime by a deed to the grantee herein or to any other person or persons making express reference to this power and executed and recorded in the Otsego County Clerk's Office prior to the grantor's death. No exercise of this power of appointment shall be deemed to release the grantor's life estate unless such release is explicitly made in a deed. The exercise of this power shall not exhaust it, and unless the power is specifically released in such a deed, the deed last recorded shall control.

The Grantors herein reserve life use and occupancy of the premises.

The Grantors herein reserve a limited power of appointment to appoint the property by deed recorded prior to death or by last will and testament referring specifically to the power of appointment and appointing the property back to themselves jointly, or as tenants in common or to either grantor individually.

Excepting and reserving to \_\_\_\_\_ and \_\_\_\_\_, Grantors herein, for and during their natural lives, the use and occupancy of the premises hereinabove described, provided, however, that the life estate of \_\_\_\_\_ and \_\_\_\_\_ shall terminate upon such time as they have been confined to a residential health care facility for a period of sixty (60) consecutive days.

No abstract of Title examined and no certification as to Title, Taxes or Description made.

Reserving however to party of the first part NAME, an estate measured by and meaning the duration of the said estate, the life of NAME, or until six (6) months after a medical doctor certifies that said NAME can no longer live in the subject premises, or until six (6) months after the date that the said NAME permanently vacates the subject premises, whichever of the above is sooner, AND during the term of the said reserved estate, it is expressly agreed and acknowledged that the parties of the second part shall maintain said premises in their present condition or better, including, lawn care, snow removal and all other items of maintenance, upkeep and repair.

For example, the grantor would provide that I devise and bequeath my residence, X, to my wife for her life use and possession without any bond or security... My wife shall have the power to sell X without the joinder or consent of the remaindermen and, if she elects to do so, she may from the net proceeds purchase such other residence as she may desire. In the event any excess remains from the proceeds of the sale of X or my wife elects not to purchase a new residence, the entire net proceeds of such sale shall be distributed to my Trustees as principal for a separate trust for the benefit of my wife, income for life, remainder to my issue, *per stirpes*.

Parties of the first part reserve for themselves for the term of their natural life or for as long as they shall continue to reside in the premises, whichever occurs first, a life use of the premises. Parties of the first part hereby relinquish the right to allow any other person to use the property, reserving this use strictly for \_\_\_\_\_ and \_\_\_\_\_. During the said life use of the premises, the parties of the second part shall pay the taxes, insurance and maintenance for said property.

Parties of the second part, \_\_\_\_\_ and \_\_\_\_\_, may not sell or transfer title to this property, nor make any modification nor make any changes whatsoever to the furnishings and/or the décor of any existing structure on said property, without the prior written permission and consent of parties of the first part, \_\_\_\_\_ and \_\_\_\_\_. Said transfer of ownership will include all furnishings and appliances.

The Party of the First Part, \_\_\_\_\_, reserves to herself for the term of her natural life, a life use of the premises. This life use is personal to the Party of the First Part and is non-transferable. Provided, however, that if the Party of the First Part, \_\_\_\_\_, becomes unable to live independently, and moves into a nursing home, assisted living facility, or other facility for a term that exceeds six (6) months, then this life estate shall terminate and the Parties of the Second Part shall hold title to this property free and clear of the life estate.

If life tenant fails to reside in the said property for a continuous period of one hundred eighty (180) days, she will be deemed to have changed principal residence, and her interest therein shall terminate.

The Party of the First Part reserves life use and occupancy of the premises during her lifetime and reserves the power to assign her life estate in the premises to any one of her choosing.

SUBJECT TO AND RESERVING UNTO the party of the first part, an estate in and to said premises during her lifetime such that the party of the first part reserves the right to the use and possession of the premises during her lifetime. The party of the first part shall pay for all maintenance and repairs, water and sewer charges, insurance charges and taxes related to the premises. The party of the first part reserves any and all real estate tax exemptions available to her including, but not limited to, the STAR, Senior Citizens' or Veterans' exemptions.

**Sample for Life Estates in Wills/Trusts:**

(A) The beneficiary shall be required to pay all costs of maintenance, assessments, insurance premiums, taxes, water charges, and repairs to the property. Upon failing to pay any such charge, any one or more of the remaindermen may pay the same, and in such event, the person or persons shall be entitled to reimbursement from the beneficiary, and shall have a lien against the property for the amount so expended plus interest at nine (9%) percent per annum. If the property is sold to a bona fide purchaser for value, such lien shall be deemed extinguished as to the real property, but shall follow the proceeds, payable first from the beneficiary's share of the proceeds, if any.

(B) The beneficiary shall obtain and keep in force a policy of insurance (at her own expense) with sufficient fire insurance coverage to represent the replacement value of all structures from time to time; and personal injury liability coverage in a minimum amount of \$150,000. Such policy shall include the remaindermen as additional insureds.

(C) No bond or other security shall be required of the beneficiary.

(D) Upon the termination of the interest of the beneficiary in the said property, I give and devise it to my then living children, equally per capita and not be representation.

(E) If any beneficiary under this Article is a minor, the property distributable to the minor may be delivered to the guardian or other person with whom the child resides, without further responsibility to the child. Any cash proceeds due a minor may be paid or held as otherwise provided under the terms of this Will.