

Buying Residence With Partner A Complex Matter

By

You and your significant other - boyfriend or girlfriend, perhaps your fiancée - decide to buy a house or condominium together. You figure it's better to own than to rent and since the monthly mortgage payments will roughly equal the monthly rental payments, it seems like a good idea. Yet whether you know it or not, the two of you are about to enter into a very complex business arrangement and you had better plan and be prepared for the "what ifs" down the road.

The most commonly used document which sets forth your respective rights is a Tenant-in-Common Agreement. Some couples choose to form a limited liability company (LLC), but that can add another layer of expense and limit mortgage loan opportunities. As a general rule, banks and traditional residential mortgage lenders will not make a residential loan to an LLC at prevailing market rates or terms. Even if you find a bank or traditional residential lender willing to make the loan, you will find the quoted interest rate and other terms far less favorable than if you were pursuing the same loan as an individual borrower.

For these and other reasons, the vehicle of choice to document your mutual understanding is usually a Tenant-in-Common Agreement. Here's what you need to think about when buying a house or condo with another person, *other than your spouse*.

How should the property be titled? You have only two choices: either you and your significant other are named in the deed as joint tenants with rights of survivorship or as tenants in common. The first option is generally not used simply because upon the death of one owner, the surviving owner automatically gains 100% ownership of the property. In most cases, the owner who passed away would have wanted his or her ownership interest to go as directed in his or her will. So for that reason among others, ownership as tenants-in-common is usually the preferred option for titling the property.

What will be your percentage of ownership? Will you each own 50% or will there be some other arrangement? This is generally a function of the equity contribution made by each of you. If you put up 60% of the cash and your partner puts up 40%, a 60-40 ownership split seems right, but it does not have to be that way. Regardless of your respective cash contributions, the two of you are free to settle on any percentage arrangement which seems fair.

What goes in the Tenant-in-Common Agreement? Once you agree upon your respective ownership interests, your Tenant-in-Common Agreement can be prepared and should address the following:

MORTGAGE PAYMENTS: Will they be split 50-50 or according to some other arrangement? Suppose you put in 70% of the cash and your partner puts in 30%; should you own the property 50-50 or 70-30? If one of you paid substantially more than the other, shouldn't the one who put in most of the cash have the larger percentage ownership? Yet if both of you are equally liable on the mortgage, how should you adjust for that?

COSTS AND EXPENSES: How will you share the routine costs associated with the house, such as maintenance/repairs, cable or satellite TV, landscape and lawn service, newspaper delivery and all the other customary household expenses? If you own the property 70-30, are the expenses shared according to that same formula?

MAJOR REPAIRS: How will you handle major repairs - and what defines "major"? Is it any repair costing more than \$200 or more than \$2,000 - and who gets to decide? How do you determine whether to replace a failing HVAC system in early April at a cost of \$13,000, or whether to just have it repaired at a cost of \$1,200 and hope it doesn't break down during the hot summer months? And how do you share the costs of any major repair? If one of you owns 70% of the house, should you have to pay 70% of the major repair

cost, even though both of you are equally benefiting from living in the house?

USE OF THE PROPERTY: Is it acceptable for your co-owner to rent out the spare room in the basement? Can your co-owner have overnight guests and, if so, how many and for how long? What about an overnight guest who ends up staying “rent free” for six weeks? Or a friend running a dating service out of the study?

SALE OF THE HOUSE: Suppose you want “out of the deal” or let’s say your co-owner gets engaged to someone else and is moving out of town. There are more than a hundred scenarios which can cause your co-ownership relationship to sour and require some sort of mutual arrangement to deal with the house or condo. Unless you have worked out a mechanism, in advance, for a buy-out, you may find yourself facing a court-ordered “sale in lieu of partition,” which is a court proceeding forcing a sale of the property. That would almost guarantee both of you suffering a substantial loss of equity, not to mention having to pay for attorney’s fees, trustee’s fees, broker fees and expenses of litigation.

HOME EQUITY LOAN. If one of you decides to take out a home equity loan, you will both need to provide signatures. So, what if one of you is not willing to sign?

DEATH: What happens if your significant other passes away? Unless your agreement addresses this issue, another family member is likely to become your partner in the property. That is not a very attractive thought.

FORCED SALE BY JUDGMENT CREDITORS. As far fetched as it may seem, you could find the Sheriff selling your house because, unbeknownst to you, your partner is deep in debt. Although your mortgage is current, your partner may not be current with his or her creditors. If the Sheriff ends up selling your house, or at least your partner’s interest in the house, you could end up with a “replacement” partner you don’t even know. And if your partner owes the IRS back taxes, you may find your house or at least your partner’s interest in the house being sold by the IRS.

TAX CONSIDERATIONS: Some of your decisions will have income tax consequences which need to be identified and considered prior to your purchase of the property. For example, how will you handle the mortgage interest deduction? Suppose your ownership interest is disproportionate to your equity contributions. One of you may have made a gift to the other for tax purposes. What if you agree to rent the property for the summer or for a longer period of time while you and your partner spend a year abroad? You may have unknowingly converted your property to “rental property,” losing the favorable real property tax treatment for owner-occupied property.

Most of these issues can be dealt with through a well-drafted Tenant-in-Common Agreement to be negotiated and entered into well in advance of your purchase of the property. As always, before entering into any sort of agreement, you should consult with competent legal counsel.