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What to Do with an Inherited House

by **Barbara Strapp Nelson, Esq.**

So you have inherited a family residence. What do you do next?

First you will want to maintain property insurance and make sure real estate taxes are paid on a timely basis. Importantly, you will need to determine if there is a mortgage loan outstanding against the property. If so, mortgage payments will need to be made to avoid the property going into foreclosure.

Most residential mortgages have a "due on sale" clause that provides that if title to the property transfers without the lender's consent, the lender has the option of calling in the mortgage, causing it to be due and payable in full. However, depending on your family relationship to the decedent, and/or how you inherited the property, the "due on sale" clause may not apply. By a federal law known as the Garn-St. Germain Act (12 U.S. Code §1701j-3), a lender is prohibited from exercising its "due on sale" clause for a number of reasons, two of which are: if the transfer is to a relative resulting from the death of the borrower; or if the transfer is by devise, descent, or operation of law on the death of a joint tenant or tenant by the entirety.

(Other situations to which this exemption from the "due on sale" clause applies include a transfer from the borrower to a spouse or children, a transfer pursuant to a divorce to a spouse of the borrower, or a transfer into an inter vivos trust which does not include a transfer of rights of occupancy in the property).

If you inherit property and do not fall into the above categories that prohibit the lender's exercise of its "due on sale" clause, then you will need to make arrangements to refinance the mortgage or sell the property.

Inherited real estate may be subject to liens for the payment of possible New Jersey Transfer Inheritance Tax, New Jersey Estate Tax, Federal Estate Tax, and debts of the decedent. These are generally addressed by the decedent's estate before title is transferred, although the obligation for payment of the New Jersey Inheritance Tax on inherited property is actually an obligation of the beneficiary. Depending on the beneficiary's relation to the decedent, there may be a tax, no tax, or a reduced tax. Real estate left to children or parents of a decedent will pass free of New Jersey Inheritance Tax.

If you decide to sell the property, you may be obligated to pay income taxes on any capital gain resulting from the sale. Capital gain, generally speaking, is the difference between the sale price and the property's basis. The basis of an inherited property is usually its value as of the decedent's



date of death, assuming no capital improvements have been made since then. If you sell the inherited house for the date of death value, there will be no capital gain, but if you sell it for more, there may be a gain.

If, however, you live in the inherited house as your residence, you may qualify for a capital gain exclusion of up to \$250,000 for individuals or \$500,000 for married couples filing a joint return. Generally, you have to reside in the house as your principal residence for two out of the most recent five years before the house is sold to take advantage of this exclusion.

While inheriting a house may be a benefit, it comes with obligations as well.

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