Life estate and gift annuity keeps retirees in their homes

InsuranceTimes™ Copyright © by M&S Communications, Inc. September 2, 2003, Vol. XXIII, No. 18

by the Associated Press

Usually, when someone trades an asset for income, he gives up rights to that asset.

But a homeowner is able to swap his house for a lifetime of checks, while continuing to live in the same house — all for charity.

The strategy for senior citizens with a valuable home and insufficient retirement income is known as a "life estate and gift annuity," and is offered by a handful of charities around the country.

The only thing comparable is the reverse mortgage — a commercial product that lets elderly people swap their homes to a mortgage company for similar benefits.

But it can be hard to find a charity willing to support this strategy. Most charities don't have the cash to pay an annuity before they sell the donated asset, said Lance Jacobson, development officer at medical research organization Mayo Clinic in Scottsdale, Ariz.

Also, charities stand to lose money if the donor lives longer than expected or the house drops in value, he said.

For those reasons, the charities that do this tend to be large, and picky about who and what they accept. Many limit this charitable giving option to people well above 70 years old, and to those with expensive homes in neighborhoods where the values are expected to rise.

Some people expect an annuity — or the lifetime income stream — from a home to be based on the full value of the house. But it doesn't work that way. The charity will slice and dice the home's value to protect their interest, which is one reason that charities often limit such transactions to people well advanced in age, and to homes of high value.

Here's how it works: You donate your home and the charity divides the value between the two parties based on a formula that calculates how long you might live. You might own 40 percent, and the charity will take 60 percent.

The charity will then calculate your tax deduction and your annuity based on the 60 percent.

Also, expect the charity to shave a percentage off the top — often 10 percent to 20 percent — to cover costs and hedge other risks.

How much that leaves you with is hard to tell. The older you are, the higher your annuity payment will be. Likewise, the greater the value of the home, the greater the chance that you will have enough to live on after it's all divvied up.

Consider: A 75-year-old with a million dollar home might expect a tax deduction on about $218,000, or less than a quarter of the home's value. He might also expect an annuity payment of $42,000 a year, or roughly 4.2 percent of the donated value, according to calculations provided by the UCLA Office of Planned and Major Gifts.

If the income is equally important as the charitable gift, compare the annuity you'll get to a reverse mortgage. Keep in mind that the reverse mortgage company will also divvy up the value of the home to hedge against risk and to cover costs.

It's not always obvious which solution will pay more, especially after the tax deduction, said Judith Pillon, director of UCLA Office of Planned and Major Gifts. Often, people who compare the foundation's annuity to one from a reverse mortgage "come back to us," she said. ❐