GIFTS OF EQUITY

A gift of equity involves the sale of a residence at a price below its current market value, as determined by a professional appraisal. It is a way for homeowners to gift real estate to their children or other relatives, even if they (the buyers) don't have enough cash to cover a down payment or the larger monthly payment that would come from a home sold at market value. Most lenders allow the gift to count as, or toward, a down payment on a home.

How the Gift of Equity Works

The amount of the gift is up to the homeowner. The residence that is changing hands may be either a primary residence or a second home. The difference between the actual sales price and the market value of the home is the actual gift of equity. If a home is appraised at $250,000, and the owners sell it to their child for $220,000, the gift of equity is worth $30,000.

Buyers still must be able to qualify for a mortgage even with a gift of equity changing hands. This means that they'll need to meet the lender's credit score and income requirements. They'll also need to provide all the necessary documentation to get approved for a mortgage.

Lenders will also require a gift of equity letter, stating the facts of the sale, and signed by both the

Lawyers Title

seller and buyer. The letter should include the total amount of the gift of equity while explaining that the buyers are not required to pay back the gift. It should also indicate the relationship between the sellers and buyers and include the address of the property.

Escrow and Closing

There are some requirements that buyers and sellers must meet to close a gift of equity, but the process is relatively simple.

If there is a new loan, the buyer must make sure that their loan is with a lender who will approve the gift of equity on the closing statement, and the gift would appear as a debit and credit. No physical money changes hands.

If the transaction is all cash, the gift would simply show in the instructions that the down payment, or a portion of it, is in the form of a gift of equity between the buyer and seller. The escrow officer will also want to document the relationship between the seller and buyer.

Gifts of equity do not avoid closing costs or other necessary expenses when transferring the title of a property.

Considerations

It's important for sellers to be cautious when giving a gift of equity. If their gift is too large, they may be hit with a gift tax. Buyers, on the other hand, are not required to pay taxes on a gift of equity.

If the gift of equity is large enough, buyers might not have to pay private mortgage insurance, which protects lenders if the buyers don't come up with a down payment of at least 20% of the home's purchase price.

Disclaimer: This information is for general informational purposes only. Before entering into any kind of transaction with a gift of equity, the parties involved should seek the guidance of their tax consultant or legal professional.

Lawyers Title®