CHAPTER 7

Classification of Property Interests as Present Interests, Contingent Future Interests, or Vested Future Interests

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Because an understanding of vocabulary is important to any communication, let's start by defining our terms:

Property refers to the thing to which certain rights (or interests) are attached. Property is classified as either real or personal. Real property is land and things attached to the land (houses, for example). Personal property is everything else.[1]

Interests are the rights in the thing (the property). Sometimes referred to as a "bundle of rights," interests include the right to possess, use, encumber[2], transfer[3], and exclude others.

Property interests are classified as either present interests or future interests, as follows:

> A **present interest** is an interest that can be presently exercised (that is, the interest holder can presently possess, use, encumber, transfer, or exclude others).
>
> A **future interest** is an interest that can only be exercised upon the happening of a future event, at which time it becomes a present interest.

Future interests are further classified as either contingent future interests or vested future interests, as follows:

> A **contingent future interest** is a future interest where the future event IS NOT certain to occur.
>
> A **vested future interest** is a future interest where the future event IS certain to occur.

There is no such thing as a contingent present interest. A present interest, by its very definition, is an interest that can be presently exercised. It is not contingent on anything, and if it were, it would be a future interest.

TYPES OF INTERESTS

Common types of interests include a fee simple, leasehold, life estate, remainder, and reversion:

A **fee simple** is sometimes referred to as absolute ownership. You have a fee simple if you have all of the bundle of rights.

A **leasehold** is an interest bound by time. It terminates at some point in the future.

A **life estate** is an interest that exists only so long as a person lives. A life estate can be based on the interest-holder's life or the life of another.

A **remainder** is a future interest that another holds (either contingent or vested) after the termination of a prior interest (for example, after a life estate).

A **reversion** is a future interest the grantor holds (either contingent or vested) after the termination of a prior interest (for example, after a life estate where no remainder interest is specified).

Consider the following conveyances (assume the grantor had a fee simple):

"To Adam." That's about as simple as it gets. Adam has a fee simple. The grantor has nothing.

"To Adam for 10 years." Adam has a present interest called a leasehold. The grantor has a vested future interest called a reversion.

"To Adam for life, then to Baker." Adam has a present interest called a life estate. Baker's interest is clearly a future interest because Baker can only exercise his rights in the property upon the happening of a future event (Adam's death). But is it contingent or vested? It is contingent because if Baker is dead when Adam dies, the property reverts to the grantor.

"To Adam for life, then to Baker or Baker's heirs." Adam still has a present interest but now Baker has a vested future interest because Adam is sure to die. Once Adam dies, Baker or Baker's heirs will have a fee simple. Before Adam dies, Baker can convey his future interest during life or at death. After Adam dies, it is no longer a future interest. It is a present interest.

"To Adam for life, then to Baker if he has reached age 25." Again, Baker's interest is clearly a future interest because Baker can only exercise his rights in the property upon the happening of a future event (Adam's death). Actually, there are two future events that must occur before Baker can exercise his rights — reaching age 25 and Adam's death. Until Baker reaches age 25, he has a contingent future interest, because the future event of reaching age 25 is not certain to occur. After he reaches age 25, it is a vested future interest because the contingency of reaching age 25 has been satisfied, and the remaining future event (Adam's death) is certain to occur. But what if Adam dies before Baker reaches age 25? The property reverts back to the grantor. The grantor is said to hold a reversionary interest called a possibility of reverter.

"To Baker, so long as the property is not subdivided." Baker has a present interest in fee simple, but because it is subject to a condition subsequent (that it not be subdivided), it is said to be a defeasible fee simple. Further, because "so long as" are words determining when the fee simple will terminate, it is said to be a fee simple determinable. And if it terminates, the property will revert to the grantor. The grantor has a contingent future interest (a reversion) called a possibility of reverter.

"To Baker, if the property is not subdivided." Notice the difference from the last example. Using "if" instead of "so long as" makes a world of difference. The law looks at "if" as a word allowing the grantor to defeat Baker's interest, but the grantor must take some action. It is not automatic as it is with "so long as." If the grantor does not take action within a reasonable time, the grantor's interest is terminated. Here, Baker still has a defeasible fee simple, but we call it a fee simple subject to condition subsequent, rather than a fee simple determinable. The grantor has a contingent future interest (a reversion) called a power of termination (or right of entry).

Well, that's all fine and good, but how is classifying property important to estate planning? It is important for understanding the value of a person's estate. Since estate valuation is based on a willing buyer, willing seller standard, there is a significant difference in what a willing buyer will pay for a contingent future interest versus a vested future interest, depending on the contingency and the extent of the future interest.

Property interests can be very complex, and valuing a property interest that has not met the light of the free market often requires the expertise of an appraiser who specializes in estate valuation appraisals.

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1. As an historical note, the term "property" did not refer to the thing itself, but to the rights (or "interests") a person has in the thing. Therefore, historically, one would refer to "property" rather than its modern equivalent "property interest." So, in modern usage, "property" refers to the thing, and "property interests" refers to the rights in the thing.

2. "Encumber" means to allow another person to attach a legal right to the property. There are two types of encumbrances, those affecting title, and those affecting physical condition. A lien on property to secure a loan is an example of an encumbrance affecting title. An easement allowing someone else to cross the property is an example of an encumbrance affecting physical condition.

3. "Transfer" means to convey one's interest to another. This can be confusing when we consider present and future interests. You could have the present right to transfer a future interest, but such does not give you a present interest in the property. In order to have a present interest in the property, you must have the power to presently exercise at least one of the other property interests.