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“Sweetheart Deals in High Demand”

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08-01-2011

## **Cohabitation agreements create rights and obligations for unmarried couples.**

**Arlene G. Dubin**, a partner at Moses & Singer, writes that many people think of cohabitation agreements as the same as prenuptial agreements, but without the “nup.” But there are important distinctions: living together agreements have no specific statutory requirements and are governed by contract principles; and there are potential tax issues not presented by prenups.

Unmarried couples made up 12 percent of U.S. couples in 2010, a 25 percent increase in 10 years, according to a recently released U.S. census report.<sup>1</sup> The result has been a corresponding surge in the demand for cohabitation or living together agreements. “Cohabs” are fast becoming as popular as “prenups,” and thus an increasingly important part of family law practice.

Cohabitation has increased for many reasons. An oft-cited practical reason is the reduction of household expenses. Cohabitation is widely accepted and promoted via celebrity role models, such as Governor Andrew Cuomo and Sandra Lee, Angelina Jolie and Brad Pitt, and Goldie Hawn and Kurt Russell. An astounding 40 percent of U.S. adults say they have lived with a partner without the benefit of marriage.<sup>2</sup>

Cohabitation is often a stepping stone for parties headed for marriage. Studies have found that more than 70 percent of couples who marry today lived together first.<sup>3</sup> And often it is a choice for older couples who do not want to upset their family or friends or lose Social Security or other benefits. According to the AARP, there are 266,600 seniors (65 years and above) who live together without being married.<sup>4</sup>

Finally, the increase in cohabitation agreements correlates with the increase in formalization of same-sex relationships. Although same-sex marriage has now been legalized in New York, five other states and the District of Columbia, it can be expected that many same-sex couples will choose cohabitation over matrimony for the same reasons that heterosexual couples do.<sup>5</sup>

Cohabitants often want agreements, sometimes called “dating pre-nups” or “pre-prenups” for the same reasons that marrying couples want prenups: to provide the financially less secure partner an equitable settlement, to properly compensate a party for his or her role as caretaker, to allow the financially more secure person to limit exposure in the event of a breakup, and to disclose the expectations of the relationship, both financial and personal.

Arguably, the reasons for a cohab are more compelling than for a prenup. A common-law marriage cannot be established in New York,<sup>6</sup> and New York does not recognize implied-in-fact

remedies, which are implied from the course of behavior and circumstances of the relationship.<sup>7</sup> Although New York does recognize some equitable remedies, such as quantum meruit,<sup>8</sup> unjust enrichment,<sup>9</sup> constructive trust, and joint venture,<sup>10</sup> such remedies are very difficult to prove.

With married couples, if there is no prenuptial agreement, the default rules of the domestic relations and estates laws apply in the event of a divorce or death. If parties are married, certain rights are automatic under the law, such as a right to receive a property settlement and support in the event of divorce, a right to file joint tax returns, a right to obtain family health insurance, dental insurance, bereavement leave and other employee benefits, a right to receive distributions from estates free of estate tax, a right to receive survivor's benefits from retirement plans and Social Security, and a right to share property in the event a partner dies.

With unmarried couples, if there is a breakup of the relationship or a death, the couples are often treated as legal strangers. Affirmative steps must be taken to assure available rights, not only upon the death of one of the parties or termination of the relationship, but also during the period of the relationship.

Accordingly, the most effective way to create rights and obligations upon death or breakup is to enter into an express contract, a cohabitation agreement.

### **Contract Principles**

Express cohabitation agreements are generally permitted in New York.<sup>11</sup> General contract principles apply to cohabitation agreements, so in order to be upheld, the contract must be entered into freely and voluntarily and must be free of fraud and duress, and both parties must possess the requisite capacity.<sup>12</sup> However, some special considerations apply to a cohabitation agreement.

First, a cohabitation agreement may be voided upon public policy grounds if one party is married to a third party at the time of entering into the agreement.<sup>13</sup> Second, sex cannot be the sole consideration for the contract. It is acceptable to recite in a contract that a person will be a business partner, homemaker, housekeeper, or social director, but not "lover."<sup>14</sup>

A cohabitation agreement can cover one or more areas or it can cover the full gamut of relationship issues. A popular single-issue cohabitation agreement is a tenants-in-common agreement governing a principal residence or other real estate.

### **Key Issues**

An obvious key issue to consider when drafting a cohabitation agreement is the fair distribution of property upon dissolution of the parties' relationship. Not as obvious, however, is the inclusion of a clear and unambiguous definition of "termination of relationship." The term can be defined to mean when one party delivers to the other a written notice of intent to terminate the relationship, or when a party vacates the parties' principal residence or requests in writing that the other party vacates such residence.

The agreement should specify which property is separate and which is shared (and on what basis), and distinguish between property that is inherited and property that is received as a gift.

The agreement also should determine what happens to the increase in value on pre-relationship property that occurs during the period of the relationship. It is usually beneficial to draft specific provisions relating to the ownership and occupancy of the parties' principal residence and contents therein. All debts should be identified and a determination made as to who is responsible for each.

Also of crucial importance, the agreement should state if and the extent of any obligation to contribute to the support of the household and, upon dissolution of the relationship, the payment and duration of any financial support by one party to the other. Provisions regarding support, custody or visitation of minor children also may be included, but they are non-binding and always subject to judicial review "in the best interests of the child."<sup>15</sup>

In the event of the death of one of the parties prior to a termination of the relationship, the agreement can spell out survivorship rights, such as the right to inherit property and receive retirement, life insurance and other benefits, as well as set forth directives for burial and funeral services. The agreement also may include the right of a party to be an agent on a durable power of attorney, serve as a guardian or conservator in the event of incapacitation of the other party, make medical decisions on behalf of a party's partner, and participate in health, disability, life and long-term care insurance plans.

Extrinsic to the cohabitation agreement and in conformity therewith, it may be necessary to register real property as joint tenants with a right of survivorship, designate one's partner a beneficiary in wills, retirement plans, insurance policies and other estate planning documents, and appoint one's partner to certain fiduciary positions.

Even so-called "lifestyle" provisions, which deal with non-financial issues such as who will do which household chores, walk the dog or do the dishes, may be included. As is the case in prenuptial agreements, provisions of this ilk often serve as moral imperatives, rather than legally enforceable obligations.

As with any comprehensive contract, in our increasingly mobile society, it is prudent to include a choice of law provision that determines what state law will govern. Lastly, clients also may wish to provide for a method for resolving disputes, such as collaborative law, arbitration or mediation.

### **Same, but Different**

Many people think of cohabitation agreements as the same as prenuptial agreements, but without the "nup." But there are important distinctions.

First and foremost, a prenuptial agreement is governed by specific statutory requirements,<sup>16</sup> while a cohabitation agreement is governed almost exclusively by contract principles. For example, the statute requires that a prenuptial agreement be in writing and acknowledged in the form required for a deed to be recorded in New York. As a matter of prudence, practitioners often follow the stricter rules applicable to prenuptial agreements when drafting cohabitation agreements. These include full and fair financial disclosure, separate and independent counsel, and acknowledgement in the form required for recording a deed.

Often clients want a cohabitation agreement to do double duty as a prenuptial agreement in the event that they ultimately do decide to marry. Certainly, practitioners can follow the rules applicable to prenuptial agreements when representing the client in a cohabitation agreement. But other issues present themselves.

On a substantive level, terms that may be acceptable in a cohabitation agreement may not be acceptable for a prenuptial agreement, because in a cohabitation agreement no marital rights are being waived. Consideration is required for a cohabitation agreement as in any contract, whereas in a prenuptial agreement the consideration is the marriage itself.<sup>17</sup>

On a procedural level, financial disclosure in a prenuptial agreement must be current, and the disclosure used at the time of the execution of a cohabitation agreement may not be accurate at the time of marriage.

Thus, the safest course would be to provide in the cohabitation agreement that the cohabitation agreement terminates in the event the parties marry, and in such case, the parties will enter into a prenuptial agreement incorporating the same terms as the cohabitation agreement, or that the parties will renegotiate the terms in a prenuptial agreement, as the case may be.

### **Tax Pitfalls**

It is crucial that a practitioner be aware of potential tax issues lurking in cohabitation agreements, which do not present themselves in prenuptial agreements.

For example, payments made by one partner for shared living expenses may constitute taxable income or taxable gifts above the exemption amount.<sup>18</sup> Transfers above the exemption amount into joint names may give rise to gift tax if the parties do not contribute equally.<sup>19</sup> Health care coverage under an employer plan is a taxable benefit.<sup>20</sup> Support at the termination of a relationship may constitute taxable income or taxable gifts above the exemption amount.<sup>21</sup> Gain or loss may be recognized on the transfer of appreciated property at the termination of the relationship.<sup>22</sup> Estate tax may be triggered on estates greater than the exemption amount.<sup>23</sup>

Given the current change in the trusts and estates law for 2011 and 2012, which increased the federal exemption amount to \$5 million,<sup>24</sup> some issues have been ameliorated at least for those years, although the New York state exemption amount remains at \$1 million.<sup>25</sup>

Non-spousal beneficiaries were given some tax parity in the Pension Protection Act of 2006.<sup>26</sup> Following the death of a participant in an employer-sponsored plan, a plan of such type may require that a benefit be distributed in a lump sum to a designated beneficiary. Under the law, non-spousal as well as spousal beneficiaries can roll the benefit over into an IRA. Prior, non-spousal beneficiaries had to take the benefit as a lump sum and suffer immediate tax consequences. However, there is a very long way to go in the future for cohabitants to achieve tax parity with married couples.

### **Debunking the Myth**

Despite a widespread misperception among clients, if they live together in New York, they are not married under common law. Parties must enter into a ceremonial marriage to be considered

married in New York. If they do not enter into a ceremonial marriage, they are legally considered single.

Nine states and the District of Columbia recognize common-law marriage.<sup>27</sup> In addition, five states have “grandfathered” common-law marriage, allowing those marriages established before a certain date to be recognized.<sup>28</sup> Generally, these states require the parties to agree orally or in writing to enter into a husband and wife relationship, to hold themselves out as married, and to acquire a reputation as a married couple. If a state recognizes a couple as married under common law, the couple is legally considered married to the same degree as if they had a ceremony.

However, many states, including New York,<sup>29</sup> that do not recognize common-law marriage formed within their borders will recognize a common-law marriage formed in another state as a matter of full faith and credit. Accordingly, it is critical that if the parties live or possibly may live in a state that recognizes common-law marriage, they should include a provision in their cohabitation agreement that they do not intend to be considered married unless they enter into a ceremonial marriage.

### **Same-Sex Agreements**

On June 24, 2011, New York passed the Marriage Equality Act and became the sixth and largest state to legalize same-sex marriage.<sup>30</sup> Prior to this, although New York recognized same-sex marriage legally performed in other jurisdictions, it did not recognize same-sex marriage performed within its borders.<sup>31</sup> As a result, many same-sex couples who could not marry in New York entered into cohabitation agreements, often with the hope that their agreements would be transformed into prenuptial agreements once the law changed. In a recent study by the American Academy of Matrimonial Lawyers, 30 percent of surveyed attorneys said a majority of the cohabitation agreements they draw up are for same-sex couples.<sup>32</sup>

Practitioners must review cohabitation agreements that were drafted prior to July 24, 2011, the date the bill became effective, to ensure that the agreement reflects the couples wishes and satisfies all the requirements necessary to be enforced as a prenuptial agreement if the couple desires to marry.<sup>33</sup> It may be necessary to amend the cohabitation agreement or replace it in its entirety with a prenuptial agreement.

Likewise, going forward, drafters of cohabitation agreements for same-sex couples should advise their clients on the effect marriage may have on their agreements and draft accordingly. In order for a cohabitation agreement to be upheld after marriage, it must meet the standards required for a prenuptial agreement.

Furthermore, even though same-sex couples may now legally marry within the state, the federal government currently does not recognize such marriage, so the tax consequences on the federal level would not be the same as for married heterosexual couples.<sup>34</sup> Accordingly, cohabitation agreements for same-sex couples should reflect such economic realities. Specially tailored financial and estate planning also may be required.

## **Conclusion**

In summary, cohabitation agreements have the benefit of avoiding a legal vacuum and/or implied-in-fact and other equitable doctrines, guaranteeing the financially less secure party a fair settlement, limiting the exposure of the financially more secure party, compensating a party for time spent as a homemaker, disclosing expectations of the relationship (both financial and personal), clarifying rights and obligations of both parties, addressing issues at a time when the parties are loving, level-headed and favorably disposed toward one another (not when in the throes of a messy split), and avoiding litigation if the relationship terminates. Accordingly, as cohabitation continues to skyrocket, so will the demand for cohabitation agreements.

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## Endnotes:

<sup>1</sup> U.S. Census Bureau, “The 2011 Statistical Abstract: The National Data Book,” (Jan. 6, 2011), <http://www.census.gov/compendia/statab/>; see also Haya El Nasser & Paul Overberg, “Fewer Couples Embrace Marriage; More Living Together,” USA TODAY, May 26, 2011, at 1A.

<sup>2</sup> Lawyers.com, “New Legal Concerns for Cohabiting Couples,” (July 19, 2005), <http://research.lawyers.com/New-Legal-Concerns-for-Cohabiting-Couples.html> (survey commissioned by LexisNexis and Martindale-Hubbell).

<sup>3</sup> Galena K. Roahes, et al., “The Pre-Engagement Cohabitation Effect: A Replication and Extension of Previous Findings,” 23 JOURNAL OF FAMILY PSYCHOLOGY 1, 107-11 (2009).

<sup>4</sup> Linda Greider, “Unmarried Together,” AARP Bulletin (Oct. 8, 2004), <http://www-static-w2-md.aarp.org/family/love/articles/shacking.html>.

<sup>5</sup> Marriage Equality Act, A. 8354, 234th Legislature (2011); National Conference of State Legislatures, “Same-sex Marriage, Civil Unions and Domestic Partnerships,” (June 27, 2011), <http://www.ncsl.org/default.aspx?tabid=16430> (Connecticut, Iowa, Massachusetts, New Hampshire, New York, Vermont and the District of Columbia currently issue marriage licenses to same-sex couples).

<sup>6</sup> *Baron v. Suissa*, 74 A.D.3d 1108, 1109 (2d Dept. 2010).

<sup>7</sup> *Morone v. Morone*, 50 N.Y.2d 481, 484 (1980).

<sup>8</sup> *Moors v. Hall*, 143 A.D.2d 336, 337-38 (2d Dept. 1988).

<sup>9</sup> *Williams v. Lynch*, 245 A.D.2d 715, 715-16 (3d Dept. 1997).

<sup>10</sup> *Drost v. Hookey*, 881 N.Y.S.2d 839, 844 (Suffolk Co. Dist. Ct. 2009).

<sup>11</sup> *Morone*, 50 N.Y.2d at 486.

<sup>12</sup> *Soderholm v. Kosty*, 676 N.Y.S.2d 850, 852 (Chemung Co. Justice Ct. 1998); see also Elizabeth A. Pope, “Cohabitation: What to Do When Couples Cannot or Do Not Marry,” 20 DCBA BRIEF 22, 26 (2007).

<sup>13</sup> *Reid v. Calvin McLeary*, 271 A.D.2d 668, 669 (2d Dept. 2000); *Donnell v. Stogel*, 139 Misc. 2d 72 (Sup. Ct. Queens Co. 1988), rev’d on other grounds, 161 A.D.2d 93 (2d Dept. 1990).

<sup>14</sup> *Morone*, 50 N.Y.2d at 486.

<sup>15</sup> *In the Matter of David Duran*, 2011 WL 2624011, at \*1 (2d Dept. July 5, 2011).

<sup>16</sup> DRL §236B(3) (1980).

<sup>17</sup> *Werther v. Werther*, 2005 WL 2384722, at \*3 (Sup. Ct. Nassau Co. Sept. 2, 2005).

<sup>18</sup> I.R.C., 26 U.S.C.A. §2503 (1998).

<sup>19</sup> I.R.C., 26 U.S.C.A. §2503 (1998).

<sup>20</sup> I.R.C., 26 U.S.C.A. §105 (2010).

<sup>21</sup> I.R.C., 26 U.S.C.A. §§2503 & 61 (1997).

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<sup>22</sup> I.R.C., 26 U.S.C.A. §1001 (1993); I.R.C., 26 U.S.C.A. §2516 (1984).

<sup>23</sup> I.R.C., 26 U.S.C. §2001 (2010).

<sup>24</sup> Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, 124 Stat. 3296 (2010).

<sup>25</sup> N.Y. Tax Law §952 (2004); see also I.R.C., U.S.C.A. §2011 (2002).

<sup>26</sup> Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780 (2006).

<sup>27</sup> National Conference of State Legislatures, “Common-law Marriage,” (April 19, 2011), <http://www.ncsl.org/default.aspx?tabid=4265>.

<sup>28</sup> Id.

<sup>29</sup> *Baron v. Suissa*, 74 A.D.3d 1108, 1109 (2d Dept. 2010).

<sup>30</sup> Supra note 5.

<sup>31</sup> *In re Estate of H. v. Leiby*, 81 A.D.3d 566, 567 (1st Dept. 2011).

<sup>32</sup> Linda Lea Viken and Ken Altshuler, American Academy of Matrimonial Lawyers, “Prenups: Not just for married couples anymore,” (Feb. 14, 2011), <http://www.aaml.org/about-the-academy/press/aaml-in-the-news/pre-post-nuptial-agreements/prenups-not-just-married-couple>.

<sup>33</sup> Marriage Equality Act, supra note 5.

<sup>34</sup> Defense of Marriage Act, 1 U.S.C. §7 (2000).

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