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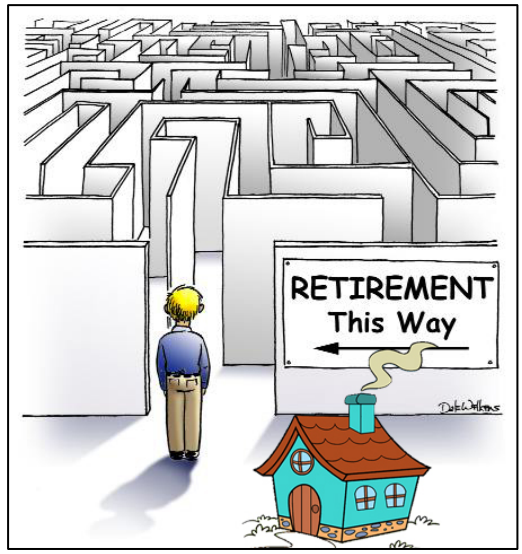
Preventing second home family feuds

Navigating the Retirement Maze



"Happiness is having a large, loving, caring, close-knit family in another city."

- *George Burns – American comedian, actor, writer (1896 - 1996)*

The vacation home is a cherished place where you can enjoy the fruits of your lifetime labors, and it can be the ideal venue for family gatherings. It is often a very special place to your children… until the second parent passes away and then the "family feud" begins. Keeping it versus selling it is often the first contentious issue that gets dealt with. If the choice is to keep it, then deciding who pays the ongoing expenses, establishing the rules for usage, and other split ownership issues can strain even the best of sibling relationships.

Yet it needn't be this way. With sufficient planning and preparation, your family vacation home can provide years of pleasure to your children without requiring legal intervention. There are measures you can take to ensure that your family's favorite gathering place continues to create fond memories long after you are gone.

Potential pitfalls of second homes

Owning a second home comes with a known set of problems. First and foremost, you're paying all the expenses – utilities, property taxes, maintenance, insurance, upkeep – on two homes rather than just one. As with many physical assets, it isn't just the upfront cost, it's the ongoing expenses that can most negatively impact your retirement income spending. Some of the added expenses might be tax deductible if you itemize, though there are caps on the amount that can be deducted for property taxes and mortgage interest.

You are managing two properties rather than one, which takes additional time and effort. Some of this can be outsourced to third parties at added expense, and condo associations handle this for you as part of the condo fee. You have also doubled your potential legal liabilities – twice as many places for potential accidents by third parties – though this can be addressed with insurance, again at added cost.

Still, the benefits of owning a vacation home are many if it is within your financial means and your willingness to manage two homes. One of them is seeing your children and grandchildren more often, if your vacation home is in a place where they are inclined to spend their vacation time. But as much as your children may enjoy gathering at the family vacation house with their siblings, the bliss may end when the second parent has passed away, and vacation home ownership and costs become contentious issues among family members.

Where sharing leads to problems

Once the ownership of a family vacation home has passed to siblings, the fantasy of owning a piece of paradise often succumbs to the reality of managing split ownership of an asset. Let's consider the situation of three siblings who have just inherited equal shares of their parents' lakefront cottage: John, a physician who is at a peak earning period of his career but has little free time; Susan, a teacher who has summers off but is barely able to make ends meet financially; and Bill, the slacker youngest child who never finished college, works sporadically, and leads a mostly carefree (and money-free) existence. John loves the family cottage and wants to keep it in the family but has limited time at present to make use of it. Susan and Bill have the time, but not the money to help pay for its upkeep. Plus, there is the crucial issue of liability that might not be obvious until it is too late. Suppose Bill decides to throw a weekend party at the cottage with his friends. One of his guests has too much to drink, and while returning home is involved in a car accident. Guess who the victim's lawyers are going to go after? All three siblings, particularly the one with the most money. The vacation dream house has just turned into a nightmare.

Trusts to the rescue

Owners of vacation houses have options available that can preempt post-mortem family mayhem, preserving both familial harmony as well as the prized asset. It comes down to three basic elements: protection, funding, and guidelines. The protection and funding can be accomplished by the creation of two trusts: one that holds the title of the vacation home, and another that provides the funding for its future expenses. The first trust acts as a liability shield to the assets of the siblings should there ever be a lawsuit involving the house. The children can be co-trustees of this trust, to jointly manage its maintenance and usage, but they do not have an ownership interest in the property while it is in the trust, which protects them from lawsuits involving the house. Similarly, the house is protected from creditors of children who could force the sale of the house if it were held outside of a trust.

The second trust holds second to die life insurance, the premiums for which are paid through annual gifts to that trust from the parents. Called an irrevocable life insurance trust (ILIT), it provides tax-free funding for the expenses of the house after the second parent has passed away. A third trust, a revocable or "living" trust in the name of the two parents, provides the mechanism for the creation of the trust that holds the title to the vacation home at the death of the second spouse, permitting the parents to maintain control of the house during their lives.

The guidelines for the use and upkeep of the house can be incorporated into the vacation home trust. These can include a procedure for determining who uses the house and when, a daily usage fee paid to the trust to partially cover ownership costs, and instructions for insurance, maintenance, and improvements, It can also include a process among the beneficiaries for modifying the rules, as well as for deciding when to eventually sell the house or for one beneficiary selling their interest in the house.

Before setting up trusts and rules for the future governance of a vacation home, check with the children to make sure that what you create is consistent with their longer term desires and financial means. Also consider the alternative of putting your vacation home into an LLC, which may be a better option for you and your family compared to a trust. LLCs confer some of the same benefits of trusts at a lower upfront legal cost, but there are significant differences between the two. Discuss this with an attorney before making a decision.

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