LIFE ESTATE WARNINGS

If you transfer property to your children, reserving the right to use the property until you die, you are known as the life tenant and your children are known as the remaindermen. The following are some possible adverse side effects from the transfer:

1. If you wish to sell or mortgage your property, it may be awkward because all of your children and their spouses, must sign the deed or mortgage.

2. If any of your children have a judgment or tax lien it may well attach to their remainder interest. This will usually mean that it must be satisfied before the property can be sold or mortgaged, resulting in a loss to your child. If a child later develops financial problems and files bankruptcy, he or she will lose their remainder interest.

3. If any of your children have marital problems, which end in divorce, their remainder interest may figure in your child's property settlement and may pose a problem.

4. In the event of a sale of the property before your death, if there is a tax gain, your children will have to pay ordinary income tax on a portion of the gain.

5. In the event of a sale of the property during your lifetime, your children will receive part of the sale proceeds and they will have no legal obligation to return any portion of it to you.

6. If you are receiving nursing care and the property is sold, it will be necessary to use a portion of the sale proceeds to pay for your nursing care expense. The percentage is determined by actuarial tables published by the Internal Revenue Service.

7. If any of your children die before you, it will be necessary to probate that child's estate. Usually a remainder interest owned by a deceased child will go to his or her spouse, if they are married. This will require some special effort to have the surviving spouse transfer the property to grandchildren.

8. The property will be included in your taxable estate for estate tax purposes.

9. In the event of a sale of just your life estate or a sale by just one of your remaindermen, you will run into the so-called 'term interest rule' which means that no income tax basis is allowed on the sale and the entire sale price is treated as a taxable gain.

10. If, at a later time, you want your children to give back their remainder interest, you will probably find that it will have a harmful effect on your children because the gift back to you will probably be regarded as a future interest and, therefore, part of their unified credit will be lost. This may have a harmful effect on your children's estate tax situation at the time of their death.

11. The 2003 and 2005 Minnesota Legislature enacted laws providing that the State can impose a lien for Medical Assistance furnished to the life tenant from and after August 1, 2003. The value of a continued life estate shall be "that portion of the interest in the real property subject to a life estate that is equal to the life estate percentage factor for the life estate as listed in the Life Estate Mortality Table of the health care program's manual for a person who was the age of the medical assistance recipient on the date of the person's death."

You should discuss the benefits and pitfalls that are inherent in the creation of life estates with an attorney. Should you wish to speak with us, we would be happy to discuss your particular situation and advise you on the best course of action.

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