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Common Estate Planning Mistakes

By James C. Mulder

This article will cover mistakes people make in estate planning. Here are seven common estate planning mistakes.

Mistake 1: Not having a will or living trust. A last will and testament or funded revocable living trust is a set of instructions. Just as important, it empowers certain people to carry out designated tasks: the executor or trustee. It has been reported that 70% of American adults do not have an estate plan, i.e. a will or living trust.

In Texas a simple will can make it easier for the executor to wind up the affairs of a decedent because certain probate court filings (especially those which give probate a bad name) are streamlined, provided the will has the language required by Texas law in the document. Thus, an executor with proper language in a will can conduct what we Texans call an “independent administration” with very few filings made with the Probate Court after the will is probated. Of course, a properly funded revocable living trust will avoid even this.

Mistake 2: Assuming you don’t need an estate plan. Your economic affairs can be much more complicated than you think — even after your death. Coordinating them with your will or living trust and other legal documents is the process of estate planning. Your real estate, financial assets, life insurance, retirement accounts and tangible personal property all need to be addressed. Some assets, like real and personal property, almost always pass through your will or are transferred to your living trust. Some assets like life insurance, annuities and retirement benefits and IRAs require beneficiary designations to coordinate with your estate plan.

Mistake 3: Not understanding the estate tax system. Each person has a lifetime credit against estate and gift taxes. In 2011 this exemption is \$1,000,000, assuming the law doesn’t change. If a family’s wealth (including 401k’s, IRA’s and life insurance) is somewhat larger than \$1 million, then some estate tax planning may be appropriate because when the estate tax hits, it’s big. The initial estate tax rate for 2011 is 37%.

Mistake 4: Ignoring the issues present in a blended family. The term “blended family” has been coined to describe the family unit where the husband and wife have children who might be from as many as three marriages: his previous marriage, her previous marriage and their marriage. If the will of the first spouse to die leaves everything to the surviving spouse, then there is a strong possibility of children from an earlier marriage being disinherited. The surviving spouse can

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re-marry and have a new spouse and even more children who replace the step-children as the object of his or her affection and beneficence. One of the benefits of a revocable living trust is that it almost automatically avoids this potentiality.

Mistake 5: Jointly titling all or most financial assets. Joint financial assets almost always have a right of survivorship that transfers ownership at death to the joint owner because it is governed by the account agreement with the financial institution, and they almost universally provide for rights of survivorship as the default arrangement.

This bypasses the will. Since most estate planning attorneys plan their client's estates with a will because Texas probate is relatively inexpensive compared to most other states, survivorship accounts trump the will and will interfere with the estate plan embodied in the will and/or revocable trust. This is especially so when the assets are jointly owned with adult beneficiaries.

Again, a revocable living trust will avoid this if it is properly funded, because a trust can not have a survivorship account by default.

Mistake 6: Naming minor children as life insurance beneficiaries. This is a subtle mistake. A natural reaction when completing insurance forms is to equate who you want to benefit with who should be beneficiaries. Thus, children are often named as secondary beneficiaries, to receive the death benefit if the spouse (as primary beneficiary) is not surviving. If the children are minors at that death, the insurance company cannot pay the policy proceeds to them because they are too young to own life insurance proceeds. By law the company must instead pay to a guardian appointed by order of the probate court. Unlike probate, a Texas guardianship is a very expensive process and usually turns the assets over to the beneficiaries at age 18.

Mistake 7: Failing to update your estate plan. Marriage and birth or adoption of a child are events that may render an estate plan lacking, unless the event is specifically anticipated in the document. A person's financial situation changes over the years. Who to use for certain roles can change. I tell people that getting five to ten years use out of their wills should be considered normal. Asking for more could mean trouble. A periodic review allows one to conduct a reality check, with adjustments to account for changes in the law or situation.

Finally, having no written estate plan leaves you with the standard estate plan written by the Texas legislature. Trust me. You probably won't like it.

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