

Title: 7 Estate Planning Mistakes to Avoid

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I have a \$5 bill waiting in my office for the first prospective client who walks into my office and says, “My situation is complex. How much do you charge for a **complex** will?”

My prediction is that the \$5 bill will remain in my office for a long, long time.

If you’re one of those people who thinks they need a **simple** will, don’t be alarmed. I’m not here to tell you that you “simple” is bad. In fact, I’m a strong believer in keeping things simple whenever possible. However, estate planning is full of traps a simple will may not avoid. The problem is compounded because a mistake you make today may not become known until after you are incapacitated or dead. By then it is too late to fix most estate planning mistakes. Your error may have serious consequences. For example, you may:

- * Unnecessarily disrupt the lives of your loved ones by forcing them to deal with complex and mundane estate administration tasks that could have been avoided.
- * Require your loved ones to make end-of-life treatment decisions on your behalf without any guidance or legal support from you.
- * Restrict your heirs from taking advantage of important tax savings techniques.
- * Spoil a child’s life by letting them inherit - and spend - too much too soon.
- * Disqualify a disabled loved one from government benefits.
- * Start a family disagreement that breaks down family relations for years to come.

My desire is to educate you about several common mistakes that I find and help you avoid them. Fortunately, the solution to avoiding each mistake is manageable. Although the solution may not be as simple as you hoped, there is no reason why you cannot avoid these mistakes. This is not rocket science, nor is an advanced law degree required. Let’s begin by reviewing the way you hold title to your residence.

MISTAKE #1: Falling Victim to a Joint Asset Trap

Joint tenancy is a method of owning an asset, and is usually used for real estate or other property. When one owner dies, the other automatically assumes ownership of the asset, despite what the deceased owner declared in his or her will. Joint tenancy avoids probate at the first death, but requires a probate when the last owner dies. Joint tenancy ownership also opens the door for each owner to lose the asset if another owner is sued for any reason. If you choose to add a child or friend as a joint tenant of a property you already own, the portion of ownership given to that person is considered an irrevocable gift which cannot be reversed.

The simple alternative for many is the revocable living trust. However, the trust is not appropriate for everyone. For example, a person owning a house and few other assets might accomplish the same estate planning goals by signing a beneficiary deed and a durable power of attorney. For those married couples who choose not to establish a trust, I recommend they own their home as community property with right of survivorship. This ensures a full step-up in tax basis at the first spouse's death, potentially saving capital gains taxes when the house is eventually sold.

Elderly persons should avoid naming a child as joint tenant of their property. In addition to losing a full step-up in basis at death and creating the possibility that Mom or Dad may be forced to sell the house in order to satisfy judgments against Child (by lawsuit, divorce or the IRS). Also, the change of ownership is an irrevocable gift requiring a gift tax return that eliminates flexibility that may be needed later. From a practical standpoint, the most important disadvantage occurs when Mom or Dad has multiple children. If one child is named as joint owner with Mom or Dad, the other children rely entirely on the goodwill of their sibling to share the value of the asset at Mom or Dad's death. Therefore, I would only suggest joint ownership if the value is relatively small and all of Mom or Dad's children have been informed of and agree to the arrangement. Certainly if you fail to gain approval of your arrangement by each child, you should anticipate a major family argument after your death.

It is important to remember that any asset held with a right of survivorship means that provisions in a will or trust regarding that asset are rendered meaningless. The asset will automatically go to the surviving owner. This might conflict with any intentions you may have had to place the asset into a trust for your spouse or children.

I also want to emphasize that married couples who hold property with a right of survivorship avoid probate on that asset at the first spouse's death, but not at the second spouse's death. If you're serious about avoiding probate at your deaths, don't use a right of survivorship in your estate plan.

MISTAKE #2: Beneficiary Designation Mishaps

The most important component of many estate plans is the beneficiary designation. For example, if you have a net worth of \$300,000, plus a term life insurance policy with a \$500,000 death benefit, then the life insurance beneficiary designation may transfer more assets than your will. Thus, the policy's beneficiary designation becomes a very important part of your estate plan.

Life insurance policies, qualified retirement plans, IRAs and annuities all have beneficiary designations. If you fail to keep them updated, or fail to ensure they are consistent with your will or trust, then they are likely to disrupt your estate planning goals.

Common mistakes with beneficiary designations include:

1. Failure to Name a Beneficiary or Contingent Beneficiary. If you fail to name a beneficiary, or fail to name a contingent beneficiary and your primary beneficiary predeceases you, the life insurance policy or retirement account will be subject to probate. After the probate is complete, the balance will be distributed according to state law, which may conflict with your intended plan.

2. Wrong or Outdated Beneficiary Designation. For most people, life will change significantly over the course of a few years. For example, imagine what your life was like 5 years ago...and where you think you'll be in the next 5 years. Has anything changed? As these changes take place in your family and your financial situation, it is important that you regularly examine your beneficiary designations to be sure that they are consistent with your wishes. I have seen many clients who named a parent or sibling as beneficiary prior to getting married, but forgot to update the designation after the wedding.

3. Lack of Coordination With Will and Trust. For example, assume you carefully drafted your revocable trust agreement to provide support trusts for your children upon your death. Each child would receive the trust principal in stages over several years in order to help them adjust to increased wealth and money management responsibilities. Unfortunately, one of your beneficiary designations said that your children inherit a large sum immediately upon your death. This would conflict with your desire to funnel all inheritance into the support trusts.

4. Using Transfer-on-Death Forms When Inappropriate. Bank accounts often allow the owner to add a Transfer-on-Death or Payable-on-Death designation to the account. This is an easy way to make sure the money ends up where you want it to be. Although this feature can be very useful, it is best to avoid using it for more than 1 or 2 accounts. If you don't limit their use, the typical result is an unequal allocation of assets to your heirs.

5. Unintended Tax Consequences. In most cases, it is undesirable to make a trust the beneficiary of a retirement plan. A trust beneficiary may lose valuable income tax deferral opportunities. Typically, it is best to name your beneficiaries individually, provided, they are not minors or disabled. This permits a surviving spouse to roll over the account into his or her own name. If there is no surviving spouse, the named beneficiary can take distributions over his or her life expectancy, which maximizes the income tax deferral. The money can grow tax-free for a longer period of time.

6. Triggering a Conservatorship. If a minor child receives a substantial amount of money through a beneficiary designation, a court-supervised conservatorship account will need to be established so that an adult can manage the funds until the child turns 18. A desirable alternative is to hold the funds in trust until the child turns a certain age and make this trust the beneficiary of your life insurance or retirement account. This can be done as part of your will or your trust.

7. Disqualifying a Disabled Heir from Government Benefits. If a beneficiary is someone who receives government benefits, such as disability or long term care payments, the funds they inherit from your estate may disqualify them for the benefits they receive. Instead, you can direct the funds to a special needs trust that provides supplementary care without disqualifying them from government benefits.

MISTAKE #3: Failure to Properly Fund your Revocable Living Trust

If you established a revocable living trust as the centerpiece of your estate plan, then it is very important that all of your assets that would otherwise be subject to probate are retitled in the name of your trust. Failure to do so will likely trigger probate proceedings upon your death. A revocable trust avoids probate only on assets titled in the name of your trust. Many people forget to retitle newly acquired assets when the memory of establishing the trust fades away. Others simply procrastinate so long that important assets are never transferred to the trust.

Some tips on transferring property into trust:

1. Real estate. Have an attorney draft and record a new deed in the county where property is located.
2. Timeshares. Most timeshares should be transferred to trust with a new deed.
3. Bank and brokerage accounts. Change ownership with custodian of account; usually requires filling out forms.
4. Stocks and bonds. Change ownership of account, if any, or of each and every stock. US Treasury and savings bonds can be retitled using forms on the Internet.
5. LLC, Partnership and Corporate Business Interests. Contact managing partner or owner; usually requires a simple assignment.

6. Tangible personal property. Use simple assignment, although this is not necessary for average size estates.

Don't forget that many assets are not transferred to the trust. For example:

1. IRAs, 401(k), 403(b), etc. These assets are paid directly to the named beneficiaries. If your trust includes trust provisions for your children, ask your attorney about how to name the trust as beneficiary.

2. Life Insurance. It is not necessary to have the trust own the policy. However, you can name the trust as the beneficiary of the policy.

3. Vehicles. It is usually easier to transfer these assets at death without having a trust involved.

For those with estate tax concerns, remember that the tax savings techniques require the trust to be fully funded and beneficiary designations to be coordinated with the plan. If you have a taxable estate (\$1.5 million or higher) and the majority of your estate consists of retirement assets (401k, IRA, etc.), see your attorney about the best way to draft your beneficiary designations.

MISTAKE #4 Neglecting to Plan for Incapacity

Estate planning is not strictly about death. It is equally important to properly plan for incapacity. You've probably heard the saying that you're more likely to become disabled this year than die. The saying is true. With today's advanced medical technology and miracle drugs, physicians are better able to prolong your life. However, these advances sometime make it more likely that you will survive an accident with a disabling condition. You need to have a plan in the event you become mentally incapacitated.

Incapacity planning is an integral part of any estate plan. Each one of us may suddenly become incapacitated temporarily (e.g., due to travel, accident or illness), and we are also subject to the effects of Alzheimer's Disease, dementia and other conditions common with elderly persons.

The mistake many people make is failing to consider what would happen in the event they were to become incapacitated. Who would pay your bills? Who would manage your rental properties? Who would determine how to invest your savings?

If you do nothing and become unable to manage your personal or business affairs, it may become necessary for a court to appoint one or more people to act for you. People appointed in this manner are referred to as conservators. If a court proceeding is needed, then you may not have the ability to choose the person who will act for you. Setting up a conservatorship is complicated, usually requires an attorney, and costs money. For

example, there will be a court hearing to determine who the conservator will be. At the court hearing, both the prospective conservator and the incapacitated person (you) are required to have separate attorneys. This is both awkward and expensive. In addition, the conservator will have to file regular reports with the court. Even if you are married, your spouse may have to set up a conservatorship to manage your separate assets on your behalf.

The simple solution is to sign a “durable” power of attorney, naming someone you trust as holder of the power. The power is “durable” because it is drafted to remain effective during your incapacity. The power is general in its application, empowering your agent to act on your behalf in a variety of situations. For example, the general power of attorney allows your agent to sell your house or car, pay your bills, purchase real property, buy or sell stocks, open or close bank accounts, and sign your tax return. Often your agent must present the actual document to invoke the power.

You should also have a valid health care power of attorney. This power is similar to the general power except this deals specifically with delegating the power to make medical decisions. A health care power of attorney is the appointment of a person to make medical decisions in the event you are unable to express your preferences. Most commonly, this situation occurs either because you are unconscious or because your mental state is such that you do not have the legal capacity to make your own decisions. Medical professionals make the initial determination as to whether you have the capacity to make your own medical treatment decisions. The health care power of attorney also allows you to state your preferences regarding organ and tissue donation upon your death.

We also find that people with these documents in place also make important mistakes. For example, some people use forms that are not valid under their state laws. That is why we suggest hiring an attorney to draft and supervise the signing of your documents. This will ensure that your documents are consistent with those that have already been tested in your area. The nightmare to avoid is having your agent attempt to use your power of attorney, only to find out it is rejected because it was not done correctly. Another mistake is including a gifting provision in your general power. This power is not appropriate for most people, unless carefully limited to the amount qualifying under the gift tax annual exclusion. Otherwise, the power to gift can be abused without your ability to do anything about it. Another compromise is to provide that your agent may continue your existing gifting plan. For example, if you give \$500 per month to your local church, the power of attorney could say that such gifts shall continue if funds are available.

The revocable living trust is a preferred method of dealing with financial incapacity issues. If you should become incapacitated, your successor trustee takes over management of the trust assets without any court involvement. This method is superior to the general power of attorney because the process of establishing the trust validates the existence of the trust. You will know right away whether your trust will provide incapacity planning as to its assets, rather than hoping a power of attorney will be valid during a later emergency.

Another important mistake is failing to give your successor trustee or agent the proper permission to obtain private medical information about you. Under the HIPAA Privacy Act regulations, health care providers face severe fines and penalties if they release private medical information about you without permission. Thus, your documents should include the appropriate language to grant this permission.

MISTAKE #5 Failure to Communicate

In estate planning, communication is vital. You must let your attorney know as much as possible about your financial and family situations. Your attorney needs to know about that life insurance policy you still have from years ago, the child you haven't heard from in 35 years, or the disability of a grandchild. Failing to disclose information leads to avoidable mistakes. The life insurance policy might trigger an estate tax. The child you intended to disinherit might start a probate court battle to get a share of your estate. The disabled grandchild might lose government benefits because of an improperly structured inheritance.

We recommend letting your loved ones know about the structure and intent of your estate plan. If you prefer that your organs be donated after death, then make them aware of it. If you distribute inheritance unequally, explain why to your children. If you established irrevocable trusts for your children, let them know the benefits of your decision now. A good estate plan facilitates transfer of assets upon death. The best way to minimize the value of a good estate plan is to keep it secret.

Another common mistake is hiding your documents where they cannot be found in an emergency. Don't leave your original documents in a safe deposit box that would be off-limits to your heirs. Let your family know where your important documents are and stay organized.

MISTAKE #6 Giving a Child "Too Much, Too Soon"

Warren Buffet, one of the world's richest men, is famous for his quote in Fortune magazine in 1986 saying that he was leaving the bulk of his fortune to charity because one should leave "enough money to your kids so they can do anything, but not enough so they can do nothing."

Certainly it is admirable to provide an inheritance to your heirs. King Solomon wrote, "A good man leaves an inheritance for his children's children, but a sinner's wealth is stored up for the righteous." However, Solomon also warned, "An inheritance quickly gained at the beginning will not be blessed at the end."

The sad stories are abundant. You might even know someone who inherited a large sum, but was unprepared to manage the sudden wealth. Estate planners often see

the results of giving a large inheritance outright. Many fall victim to greed, bad investments, and spending impulses. Others lose interest in their schooling or career and live an unproductive life of luxury.

Consider the average American couple with \$200,000 in net assets. Each spouse has a \$250,000 term life insurance policy. Although they probably don't think of themselves as rich, their children stand to inherit \$700,000 if Mom and Dad passed away. If the children are ages 18 and 21, do you think they are ready to inherit \$350,000? What if they are 28 and 30? Even a child with excellent money management skills may fall to the temptations inherent with receipt of a large inheritance.

You need to consider whether you have any heirs that would stand to inherit a large sum under your estate plan. Would that inheritance help or hurt them? Might they drop out of school or a productive career? Instead of making gifts outright, consider the possibility of putting their inheritance into trust. The opportunities are endless. For example, you might have the trust funds distributed in stages so that the child has a chance to adjust. Or you might tailor distributions to the child's productivity (e.g. matching distributions with earned income, with an adjustment for those who choose low income careers).

MISTAKE #7 Putting a "Bulls-eye" on your Assets

What if you were driving in your neighborhood and accidentally collided with a young child on a bicycle? What if your business start-up venture failed and you couldn't pay back the loans you personally guaranteed? What if your dog contracted rabies without your knowledge and bit your neighbor's 2 year old child? Any of these events is likely to trigger a lawsuit against you. Your insurance policies provide a first line of defense, but your policy limits may not cover the entire claim. If your insurance doesn't cover the event, you will have to pay for your own legal defense and pay for any judgment against you. The size of your emergency fund may be woefully inadequate in comparison to the size of most personal injury lawsuits and business loan defaults.

Our law firm incorporates asset protection planning into each client's financial and estate plan. Asset protection planning involves the use of lawful methods to manage legal risk. It involves arranging financial affairs in a way that minimizes the exposure of assets to the claims of future creditors. It is not meant to replace the need for insurance, nor intended to illegally avoid paying debts. Asset protection techniques vary from automatic statutory exemptions to highly complex international strategies with multiple entities involved. Our goal is to create a unique plan for each client, which provides a sufficient level of protection without adding so much as to remove the flexibility and control that we all desire over our personal and business assets.