

Ten Worst Estate Planning Mistakes

Estate planning, the process by which we create a plan to efficiently and cost effectively manage our property and assets during our lives and distribute them after our death, is a topic that most people would prefer to avoid. Although we all occasionally joke about the inevitability of death and taxes, these are not issues that we take lightly. Indeed, because estate planning forces us to face issues that are disagreeable, all too often, individuals and families postpone decision-making and sometimes completely neglect these important considerations. Planning, to the extent that it is undertaken, occurs under less than ideal circumstances and without the assistance of trained and experienced professionals. The following is a list of common mistakes and unfortunate misconceptions.

1. Failing to plan – People commonly believe that, having failed to draft a will or create a formal estate plan, they have no plan in effect. This is not the case. If you die without declaring your intentions, state law dictates how your assets will be distributed at your death, and it may not do so in accordance with your wishes. Moreover, the administration of an estate, the process by which the court supervises the payment of debts and distribution of the assets where one dies without a will, can be lengthy and quite costly.

Even more important than the costs and time considerations facing your beneficiaries after your death is the fact that, without any advance planning, no power of attorney, no health care proxy and no living will (all parts of an effective estate plan) will have been established. As a result, even during your lifetime your hard earned assets may not be properly protected if you get sick, and your family may not be able to carry out your health care decisions for you. In the event that you become mentally disabled the court will appoint someone to take control of your assets and your personal affairs. Apart from the expense associated with guardianship proceedings, as they are called, this process can be time consuming, impersonal and often humiliating.

2. Relying on “family loyalty” – Regardless of what state statutes direct, some people believe that their loved ones understand and will carry out their wishes during their lifetime and divide their assets accordingly after their death. Even if you have the model family, and have explained your expectations and desires to them, your goals may not be effectuated unless proper planning has been done. In order to empower an “agent” to make health care decisions on your behalf a health care proxy must be completed and properly witnessed. Without a power of attorney, your family may not be able to pay your debts and otherwise manage your assets. Additionally, in all too many cases, the absence of clear written directives creates the environment for family dissension. Family members may disagree as to what it is that you would want or

need. These disagreements can result in friction and the disruption of family harmony at a time when it may be most needed.

3. Utilizing joint accounts to effectuate your estate plan – Holding assets in joint accounts with a spouse or loved one may not be an effective estate plan for numerous reasons. For instance, although a joint bank account in the name of a parent and child may effectively transfer the sum deposited by the parent to the child upon the parent's death, in the interim, the funds in that account are subject to the debts and liabilities of the child. If the child is sued and has insufficient sums from which to pay an adverse judgment, the account can be attached, depleting funds which were to have been available, during the lifetime of the parent, for the parent's maintenance and support. If the child divorces, that account may fall subject to litigation tactics. Additionally, if only one child is named on the account, he or she may be unable or unwilling to fully effectuate the parent's wish to divide the funds in the account equitably with the other children without incurring tax consequences. This could lead to inequitable distribution.

As far as the government is concerned, the funds held in a joint account are your funds. They are part of your estate for estate tax purposes and are considered yours as far as Medicaid eligibility is concerned unless it can be established that the assets were deposited by the other joint tenant on the account.

When joint accounts and joint ownership of property as between spouses are utilized in place of proper estate planning, at the death of the first spouse the jointly owned accounts and property pass directly to the surviving spouse. While this may seem expedient in that it avoids probate at the death of the first spouse,¹ depending on the size of the estate, it results in a significantly greater tax liability at the death of the second spouse because no advantage was taken of the unified credit to which the first spouse to die was entitled.

4. Failing to allocate assets between Husband and Wife when using the Credit Shelter Trust. Not infrequently, and more typically when assistance in estate planning is sought from a lawyer or other than a trained professional whose practice is not devoted to estate planning, an effort will be made to take advantage of the unified credit by creating a Credit Shelter or ByPass Trust. The creation of such a trust merely establishes the framework for estate planning. It is not until the assets are actually allocated between the couple enabling the trust to be funded that this valuable tool can function as intended.

5. Failing to provide sufficient liquidity to pay estate taxes subjects the family home or other real property and non liquid assets to sale under less than ideal circumstances. Estate taxes are due and payable nine months after the date of death.

¹ It also avoids estate tax liability at the death of the first spouse as the government permits married couples who are citizens to transfer an unlimited amount of money and property from one to the other free of estate or gift tax. This "unlimited marital deduction" is deceiving in that, upon the death of the second spouse, estate tax is calculated upon the entire estate of the second spouse which has been enriched by the transfer of assets from the first spouse to die.

Typically, a probate proceeding is not even commenced until several weeks or months after the death of a loved one. By the time the court has authorized an executor to begin liquidating the assets, there isn't sufficient time to conclude an "arms length" transaction for the sale of the property. The phrase "estate sale" customarily means that the property has been reduced or discounted for quick sale.

6. Gifting the wrong assets. Although gifting is an important estate planning tool, having utility for both reducing estate tax liability and protecting assets from the costs of long term care, appreciated assets can create gifting problems. During your life, if you sell an appreciated asset you pay a capital gains income tax on the entire profit. If you give the asset away during your lifetime, the recipient pays the tax calculated upon your cost. If, however, you give that same asset away after you die, through a will or trust, the recipient receives it at a higher cost basis equal to the fair market value as of the date of your death, a "step up" in basis. It is, for this reason, important to understand the interplay between income, gift and estate taxation and to consider the entire financial and practical picture when gifting.

7. Creating a will instead of a trust – A will merely disposes of your assets after your death. A trust can be crafted to afford you the opportunity to manage your assets while you are alive and able and, while a will makes no provision if you become incapacitated, a trust usually directs who is to manage and how the property is to be managed. Probate, the process by which a court approves a will and supervises the distribution of the assets, is both time consuming and costly, however assets distributed through a trust are not subject to probate. Additionally, probate documents filed in court are a matter of public record whereas the disposition of the assets of a trust are entirely private.

8. Not creating a trust where real property is owned outside the state or where there is property in numerous jurisdictions – Ordinarily, a will is probated in the state in which the decedent resided or was domiciled. The exception is for real estate, which is subject to probate in the state in which it is located. Thus, ownership of property in more than one jurisdiction will subject your estate to probate fees in each state in which your property is located.

9. Failing to properly exercise all IRA elections can result in a 100% distribution of the funds in the account upon your death, subjecting the fund to both estate and income tax which together can total as much as 80%. Similarly, under most plans, where the primary beneficiary predeceases and no contingent beneficiary is named, the estate becomes the beneficiary and a 100% distribution results.

10. Believing that no plan is necessary – Even if you presently have very few or no assets, having a current and viable estate plan is very important. One client's mother was the unfortunate victim of a car accident. At the time of her death she had been separated from her husband for many years. As her children were grown and

independent and she was living on little more than social security, no formal estate planning had been done. Because she died without a will, the Surrogate's Court appointed an administrator to commence a wrongful death action on her behalf and, when a sizable settlement was achieved, her estranged husband was entitled, by state law, to a one-third share despite the fact she would undoubtedly have wanted the entire amount to be divided between her children. Additionally, significant estate taxes, totaling almost 50% of the settlement sum, were unavoidable. Proper planning would have alleviated these problems.

In sum, not only should advance planning be undertaken, it should be done with the help of an experienced professional. One further word of advice, **DON'T PROCRASTINATE**. We never know until its too late!

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