Five Costly Errors in Estate Planning

By Jerry Robinson, CFP®, AIF®, CFS®, ChFC®

1. The lack of a will and a funded living trust.

A Revocable Living Trust is created and becomes operative during your lifetime. This type of trust is flexible in that it can be changed any time prior to death. If drafted properly, the Living Trust can provide for you and your spouse in the event of incapacity. It should be noted that the living benefits of a properly drafted plan are wasted if the Living Trust is not funded. Most importantly, a Living Trust avoids the lack of privacy, and the expense and delays associated with the probate process.

A Will should be drafted primarily for the purpose of naming who will be the guardian(s) of your minor children in the event of the simultaneous death of you and your spouse. A Will should serve as a catch-all for the estate and set distribution provisions for all estate assets not previously titled in the Living Trust.

2. Not taking advantage of the single biggest tax break that Uncle Sam allows.

A married couple has the ability to pass $24,120,000 to the next generation free of any federal estate tax. If a properly drafted and funded revocable living trust has been utilized at the first death of a spouse, not only can $12,060,000 be exempted from your Federal Estate, but also, the growth of those assets shall be exempted from the surviving spouse's taxable estate.

For states such as Massachusetts that have their own separate estate tax, a properly drafted and funded Revocable Living Trust is necessary to help minimize the estate tax. For instance, in Massachusetts, a $1,000,000 exemption is available to every individual. In order to take advantage of this credit, you must leave $1,000,000 to someone other than your spouse, or in trust for the spouse's benefit. So, if you own jointly held property with your spouse, this property shall automatically pass to the surviving spouse at your death! This type of transfer would disqualify you from taking advantage of the credit. This is probably the most common method of not utilizing the exemption.

3. Insufficient liquidity to satisfy the estate settlement costs.

Often times, estates are comprised of large non-liquid assets, such as real estate holdings, farms, or closely held business interests. Upon the deaths of both spouses, a federal estate tax of 40% could be due.

A properly planned estate often has the foresight to provide for a liquidity shortfall by setting up a sinking fund in advance. Often, an Irrevocable Life Insurance Trust is included in a state of the art estate plan. The Irrevocable Life Insurance Trust proceeds are not part of your taxable estate since the trustee, not you, determines whether to purchase life insurance on you and/or your spouse. The advantages of an Irrevocable Life Insurance Trust can be great, such as the death proceeds becoming available when the liquidity is required (when the federal estate tax is due).

The combination of utilizing a joint survivorship policy and an irrevocable life insurance trust provides a cost efficient means of paying estate taxes. You should review with your CERTIFIED FINANCIAL PLANNER™ professional the other discounted methods of paying estate taxes.

4. The lack of a gifting strategy

Larger estates require an overall strategy to reduce the future growth of the estate value. This is most often accomplished through the use of the annual gifting program. A husband and wife may gift $16,000 each to anyone they wish. Thus, if the husband and wife have two children, they may gift $64,000 per year to their children alone. This is the most basic of gifting techniques; other more sophisticated techniques allow parents to give away their valuable homes or second homes at steep discounts, while allowing them to continue to live there. This type of strategy can provide a means of leveraging the gift.

5. The failure to provide a Durable Power of Attorney, Health Care Proxy and a Living Will.

Unfortunately, many clients neglect to tidy up the loose ends of their estate plan. Making your wishes known and providing the documentation to make sure your wishes are implemented is part of the estate planning process. Empowering others to make business and health decisions for you during incapacitation eliminates much agony and undue cost.

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