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Top Ten Estate Planning Myths and Mistakes

In our day-to-day interaction with clients, and most often during the workshops and seminars that we conduct, we frequently encounter persistent misconceptions about the entire estate planning process. Our “Top Ten” are listed below, along with brief commentary about each of them. They are not listed in order of priority or importance, as they all, in their own way, material in the estate planning process.

MYTH/MISTAKE #1:

ESTATE PLANNING IS NOT NECESSARY UNLESS YOU ARE OLD AND/OR RICH

A root cause of this myth may be the word “Estate” itself. The word conjures up images in our minds, much like a luxury car commercial. When I think of the word “Estate”, I see an expensive car rolling up a long driveway to a large mansion, with thoroughbred horses striding alongside in a pasture bordered by white fencing. The home has large columns supporting the entry, and out back are a tennis court and a pool the size of a small lake. Since I don’t actually have these, I must not have an “Estate”, and therefore I don’t need to engage in “Estate Planning”. The truth is, your age and the size or value of your estate is immaterial to the issue of whether or not you need to engage in estate planning. The real issue is one of choice and control, and who has it.

The fact is if you are 18 or older, you already have an estate plan. We all do. It was drafted on our behalf by the legislatures of the states in which we reside, and is governed by the state laws of intestacy. If you die “intestate”, meaning without a Will or a trust, these laws govern who will inherit your assets. If you have minor children, these laws also govern who will be chosen to be their guardian and the trustee of their inheritance until they reach the age of 18. It will also give your children complete and unfettered access to their inheritance upon reaching that age. Might it be harmful to an 18-year-old to have unrestricted access to any significant sum of money? As you might imagine, the state laws of intestacy might not arrive at the same choices that you would make. I think of the default plan drafted by the states as the “No Plan” plan.

Choosing to accept the “No Plan” plan, and yes, it is a choice, means that your family might also have to endure a lengthy, public and possibly expensive probate in order to administer the estate. Additionally, all of the proceedings and the choices made by the probate court will be public record, open for anyone to review who cares to.

Let's take the case of a young couple in their early thirties, with one or two young children, either living in a rental, or perhaps they have just purchased their first home and have only a small amount of equity in the home. Are they rich? No. Are they old? No. Do they need an estate plan? Unequivocally Yes.

As discussed above, without a formal estate plan, should both of them die while they are young, who will raise their children? Who will watch over their children's assets until they are adults? And most importantly, who makes those decisions – the young couple, or the state?

The question then becomes, do you want to accept the plan created for you by the state (The "No Plan" Plan), or take control and create your own plan, one that reflects your choices and your wishes? If your choice is the latter, then regardless of your net worth or age, estate planning in some context is appropriate for you. It may involve little more than drafting a Will to distribute your assets according to your wishes, and appointing a guardian in the Will for any minor children, along with Powers of Attorney for Health Care and Finance (two separate documents). For a more thorough discussion about Powers of Attorney, and their importance in even the most basic of estate plans, please link to the article on this site entitled "[Powers of Attorney: Critical Components of Your Estate Plan](#)". Creation of this most basic of estate plans is neither expensive nor time consuming. The most difficult part is actually making the decision to design your own plan, instead of settling for the "No Plan" plan. However, with the assistance of competent legal counsel, it is much easier than you think.

MYTH/MISTAKE #2: **IF I HAVE A WILL, MY FAMILY WILL AVOID PROBATE**

How this particular myth began is baffling. In short, using a Will as your primary estate planning document will not necessarily avoid probate, period. Whether or not you have a Will, your estate may be probated. Without a Will, your estate will still go through the probate process, but the state laws of intestacy, what I call the "No Plan" plan, are applied to determine the distribution of your assets. But first, let's discuss exactly what Probate is, and whether or not it should be avoided. Briefly, probate is a court supervised proceeding, whereby the validity of your Will is "proven" in court. If the Will is proven to be valid, then title on your assets, after payment of your debts and expenses, can be legally transferred to your heirs according to your wishes. Since this is a court supervised process, it is also a public process, meaning the full details of your Will are public and available to anyone wishing to view the court records. This includes the information about who your heirs are, where they live, and what they may or may not have received from your estate.

As if the public airing of your final wishes and disposition of your assets is not bad enough, going through probate is also often a lengthy process. Notices must be sent out to all parties in interest to your Will (anyone named in the document), usually to all family members, to your creditors, and public notices of your death must be posted. This is to notify and allow anyone who may have a claim against your estate the time to file that claim and have it included in the probate process. The time allotted for response to the notices is four months. Additionally, the court dockets are usually quite full, and as a result, in California, even the average uncontested probate can easily take over one year.

Last, but certainly not least, probate can be quite expensive. Statutory probate fees start at four percent of the first \$100,000 of the estate, three percent of the next \$100,000, two percent of the next \$800,000, one percent of the next \$9,000,000, and one-half percent of the next \$15,000,000. For

estates larger than \$25,000,000, the court will determine the fee for the amount that is greater than \$25,000,000. The value of your estate is not an arbitrary figure - a probate referee is appointed by the court and assigned to appraise the value of your assets. Thus, an estate with a gross value of \$1 million could incur statutory attorney fees as high as \$23,000. Both the attorney and the executor of your Will can charge these fees, so the expenses could actually be as high as \$46,000. Add in the court costs and the probate expenses might exceed \$50,000. Additionally, the probate fees are assessed on the gross value of your estate, not the net value. In other words, if your home is worth \$500,000, but you owe the bank \$250,000 on the mortgage, your probate fees are based on the \$500,000 value, not just on your \$250,000 of equity.

Further, for those individuals with property in more than one state, upon death there will not only be a probate process in the state of residence of the deceased, but also the need for what is known as an “ancillary probate” in each of the other states where property is owned. This may create the need to seek legal representation in those other states, and thus the estate will likely incur additional expenses as well.

Given this information, most people would choose to avoid probate if they could. Why would anyone voluntarily choose to allow their estate to be probated? There are other methods to use, such as using a living trust as your primary estate planning document instead of a Will, which can avoid most of the time, expense and publicity associated with the probating of a Will.

However, some of the advantages of probate are that a court and a judge oversee the process, and can settle disputes that arise between your beneficiaries, or between your beneficiaries and the executor. The executor must also provide an accounting of the estate to the court, and a report of their activities. The goal of having court oversight of the process is to keep all the proceedings above board and open for all interested parties to see. The disadvantage of probate is that it usually costs significantly more than the administration of an estate that is passing to your heirs through a living trust or other alternatives, and it usually takes significantly more time to probate an estate than to administer a trust. Additionally, most estates do not need the supervision of the probate court unless disputes arise.

In short, using a Will as your primary estate planning tool will not keep you, or rather your heirs, out of probate. It does mean however, that your probate will likely be more organized than it otherwise would have been had you died without a Will.

MYTH/MISTAKE #3: USING A LIVING TRUST AVOIDS ESTATE TAXES

This is a very common myth. I hear people say, “I don’t need a trust because my estate isn’t big enough to incur estate tax”. Let me be very clear: The fact is, a living trust cannot not help you avoid estate taxes any more than a Will can. However, both can include provisions for at least reducing, if not completely eliminating, the estate tax. If avoiding the estate tax was as simple as simply creating a trust and then placing all of your assets in it, wouldn’t everyone do it, or have already done it?

The primary purpose of a living trust, sometimes called a revocable living trust, is not to avoid estate taxes at your death, but to avoid probate when you die, and avoid the need for a conservatorship in the event of your incapacity. Loss of legal capacity can occur as the result of an accident or illness, and may only be temporary, or can be caused by something more permanent such

as Alzheimer's disease or dementia. Further, a living trust keeps your affairs private, and significantly reduces both the time and expense associated with administering your estate when compared to probating a Will. These are important issues regardless of the size of your estate.

A living trust can also be a "Will substitute", whereby your assets are still distributed to your heirs in the manner that you specify, but the distribution is done in private, not in public. Most estate planning more often revolves around family planning issues than it does around estate tax planning. In fact, many of our clients have estates that are under the thresholds where estate taxes would apply to them. They are much more concerned with an orderly transfer of assets to the next generation, and doing so in a way that does not fracture their family, than they are concerned about estate taxes. Just as a Will can, a living trust can have special provisions for the inheritance of a special needs beneficiary, an heir who is a spendthrift and can't manage money, or young beneficiaries who do yet not have the maturity to manage an inheritance wisely. You can even include provisions for the care and adoption of your pets if they survive you.

However, while a living trust can do much more as part of a comprehensive estate plan than a Will can, it is not a "stand alone" document. A "Pour Over" Will is usually still used in conjunction with the living trust, and "pours over" into the trust any assets that were inadvertently left out of the trust, or removed from the trust. The Will is also where you name a guardian for any minor children. Finally, and these are documents critical to all estate plans, Durable Powers of Attorney for Health Care and for Financial Management round out the suite of basic documents to avoid probate, manage your affairs, avoid a conservatorship in the event of incapacity and keep your estate distribution private.

In summary, a living trust is not a tool for avoiding estate taxes, and therefore something only the wealthy use. It is a tool for the management of your affairs while you are alive and the transfer of your assets to the next generation, regardless of your wealth, privately and cost-effectively. Personally, I like to think of a living trust as a "Loving Trust" – one final way to show your family how much you care for them.

MYTH/MISTAKE #4:
PUT YOUR ADULT CHILD ON TITLE TO YOUR HOME
TO AVOID PROBATE

This particular myth is a real "land mine" waiting for an unsuspecting person to step on. Some assets do pass by title, most notably real estate, and therefore escape the need for using a Will or trust to transfer to the surviving joint tenants, at least until the death of the last surviving tenant on the asset. This is also true of joint investment accounts and joint bank accounts. For example, a house titled as "*John Doe and Jane Doe, Husband and Wife, as Joint Tenants with Rights of Survivorship*" means that at the death of either John or Jane, the house will pass to the survivor of them, and no probate will be involved. But, at the death of the survivor of John or Jane, what then? The mistake is to think that if "a little joint tenancy" is good, more must be better, so let's add the kids to the title too. After all, your estate is going to them after you die anyway, right?

First, if you add a child as a joint tenant on your home, you have potentially made a taxable gift to that child. If gift tax is to be paid, it is the donor who pays it, not the recipient. However, you do have an exclusion from gift tax on the first of \$13,000 of gifts you make each year. Gifts above that annual amount are considered taxable gifts. Both husband and wife also have a lifetime exemption on the first \$1 million of taxable gifts made in excess of the annual exclusion, so if the estate is more

modest in size, then making a taxable gift might not be harmful when viewed just from the standpoint of gift taxes.

Okay, so we dodged that one – no gift tax issues. However, your child is now on title with you. This means that your home (or other joint account) is now exposed to what might go wrong in the life of that child. What happens to your home if your child declares bankruptcy, and is listed as an owner on your home? Maybe it's not a bankruptcy, but an auto accident where your child is "at fault", and the resulting settlement exceeds the liability limits of your child's auto insurance. Might your home or other assets potentially be at risk due to the joint tenancy title arrangement? A resounding YES.

I often hear that the parents have put one adult child, usually the "Responsible Child", on their home or investment account with them as a joint tenant, with the understanding that at the death of the parents, the child will distribute the property fairly and evenly among all of his or her siblings (Do I hear laughter?). Notwithstanding the liability issues discussed above, your child is under no legal obligation to make this distribution, and could simply keep the entire balance of the joint tenancy property. No one would ever do that, would they?

But, just for the sake of this discussion, let's say that your child does comply with your wishes, and actually distributes the property as you have directed. Remember those gift tax rules discussed above? Your child has now run afoul of them. Using a \$500,000 home as an example, with four children as beneficiaries, one of whom is the joint tenant, the value to be distributed to each child would be \$125,000 (\$500,000/4). The "responsible child" who is a joint tenant with you has just made taxable gifts to his or her siblings totaling \$375,000! If the \$13,000 annual exclusion per recipient is insufficient to cover the gifts, which is quite likely, the child has two choices: (1) Pay the gift tax, starting at 18% of the first \$10,000 and rising rapidly from there, or (2) claim the excess amount against his or her own lifetime \$1 million exemption. If the child chooses option number 2, this will avoid any current tax liability, but will also reduce the amount that your child can then pass without estate taxes to his or her heirs at death. This was probably not your intended outcome.

In conclusion, before you think of using Joint Tenancy as the "simple" or "easy" way to avoid the need for a formal estate plan, consider some of the issues just covered. Is that something you are willing to risk, just to avoid drafting or revising a Will or trust? This can turn out to be the classic case of being "*Penny Wise, Pound Foolish*".

MYTH/MISTAKE #5: **NOT FUNDING YOUR LIVING TRUST**

Having come to the conclusion that avoidance of probate and/or a conservatorship is a good goal, many people choose to use a revocable living trust instead of a Will as their primary estate planning document. Once the trust is executed, most feel they are finished with their planning. Not quite. Unfortunately, an all too common mistake is failing to then "fund" the trust. Funding a living trust simply means changing the title on the assets and accounts that you wish the trust to be able to control and placing them in the name of the trust. A living trust cannot control assets that it does not own, meaning assets that have not been "funded", or re-titled, into the trust. For example, changing title on the primary residence from "John and Mary Doe, Joint Tenants with Rights of Survivorship" to "John and Mary Doe, Trustees of the Doe Revocable Trust dated January 4, 2010" means that the trust is now "funded" with the primary residence. The same holds true for title on joint investment accounts, bank accounts and vacation properties.

Therefore, not properly re-titling assets and funding a living trust defeats the primary purposes of having a living trust: Avoidance of probate at the death of the grantor(s), and/or the need for a conservatorship upon the incapacity of the grantor(s). Not funding the trust will also mean that at the death of the grantor(s), there may still be a need for a probate process, if for no other reason than to transfer the assets into the trust post-mortem. Not funding the trust also means that in the event of the incapacity of the grantor, there will still be a need for a conservatorship of the estate, because once again, the trust cannot control what it does not own.

Related to the mistake of not funding the living trust at the beginning is the issue of making sure that the trust remains funded over time. For example, whenever you purchase or refinance a home, most banks will require the property to be in your own name, and not in the name of your trust, in order to complete the financing arrangements. Once the financing has been completed, title on the property can be transferred back to the trust, but very often the homeowner inadvertently forgets to take this final step. Thus, an asset that was once properly held in the trust is no longer in the trust, and therefore no longer under the control of the trust.

If you are not sure if your home or other real property is held in the name of your trust, simply examine your property tax bills. If the property is in the trust, the bill will usually be addressed to the trust or the trustees in the addressee section of the bill. For investment or bank accounts, a similar reference to the trust or trustees is usually found in the addressee section of the monthly or quarterly statements. If you are not sure, contact the county assessor's office where the real property is located, or the financial institutions holding the accounts.

It is the practice at this firm to make sure that all assets that should be titled in the name of the trust are transferred to the trust at the beginning of the estate planning process by having our clients provide us copies of property tax bills and account statements up front. This allows us to proactively prepare the proper transfer documents on a client's behalf and ensure that this mistake is avoided.

If you already have a living trust established but find that some or all your assets have not been placed in the name of your trust, don't panic – this is easy to correct. All of the counties, as well as your financial institutions are very familiar with the use of living trusts by individuals, and most already have simple documents that are used in transferring title to living trusts. These documents, plus a certification of your trust, provided by the attorney who prepared your trust, are usually all that is needed to complete the title transfer.

Simply put, there are three steps to ensure that a living trust does for you what you intended: First, create the trust; second, fund the trust; and finally, review the title on your assets periodically to verify that they are still in the trust.

MYTH/MISTAKE #6:
FAILURE TO COORDINATE INSURANCE, PENSIONS AND IRAs
WITH YOUR ESTATE PLAN

Life insurance proceeds, both from individually owned and group life insurance, as well as pension assets and individual retirement accounts (IRAs), pass to your heirs through a beneficiary designation, and therefore will usually avoid probate without the need of a living trust. Accordingly, it is not necessary to transfer the ownership of these assets to your living trust. This is also becoming

true of some investment and bank accounts, which may have the ability for you to designate a “Transfer-on-Death” (TOD) or “Pay-on-Death” (POD) beneficiary for the account.

However, it is important to review the beneficiary designations on these kinds of assets in order to ensure that they are coordinated with your overall estate plan. If, for example, you have named your estate as the beneficiary, assets which would have otherwise avoided probate will unfortunately be forced back into the probate process, subjecting them to unnecessary expenses and delays before distribution to your heirs. If the assets are IRAs or pensions, naming your estate as beneficiary can also have very unfortunate income tax consequences for the beneficiaries.

Further, your estate plan may provide that upon the death of the grantor(s), some or all of the assets to be distributed to children, grandchildren or other heirs, are to remain in trust for their benefit until they reach a certain age, say 30, 35 or 40, instead of being distributed outright, in order to allow time for the beneficiary to gain the maturity needed to manage an inheritance. While the assets are in trust, your trustee is usually instructed to use the income and principal of the trust for the health, education, maintenance and support needs of the beneficiaries, and the trust may also allow for distributions to them for the purchase of a home or the establishment of a business.

Perhaps you have a “special needs” beneficiary, and the receipt of funds from your estate would cause them to lose their eligibility for Supplemental Security Income (SSI), Medi-Cal, or other governmental programs where eligibility is resource-based. Your estate planning documents may provide for the special needs beneficiary through a special needs trust, used to provide for the ongoing needs of a disabled beneficiary while still maintaining eligibility for governmental assistance. For a more thorough discussion about planning for disabled or special needs beneficiaries, please link to the article on this site entitled [“Special Needs Planning”](#).

If your child or grandchild is named as a primary or secondary beneficiary of your life insurance, pension plan or IRA, or as the TOD/POD beneficiary of a bank account or investment account, the proceeds will be disbursed to them directly, provided they are age 18 or older, and the provisions of your trust will not apply or be able to control. This may be contrary to your wishes, and potentially detrimental to the financial well-being of your heirs, particularly those who may be special needs beneficiaries.

Another reason to review and coordinate the beneficiary designations on your accounts with your estate plan is to make sure there is adequate liquidity for the executor of your estate and/or the trustee of your trust. This person is usually charged with the obligation to pay your final expenses and debts, as well as any taxes and legal or accounting fees, before distribution can be made to your heirs. If there is insufficient cash within the trust or estate to accomplish this, the heirs who received outright distribution under an insurance, pension or investment beneficiary designation are under no obligation to return the funds to your estate.

Last, but unfortunately not least, dissolution of marriage is an all-too-common reality in this country. However, for whatever reason, this does not always prompt an individual to review the beneficiary designations on their life insurance and pension assets, and subject to any property agreements from the divorce decree, remove the former spouse as a beneficiary. It is not uncommon for us to discover that a former spouse is still named as a beneficiary on life insurance or pension assets many years after the divorce has been finalized, and often, many years into the second marriage! Recent court cases have also upheld the rights of a former spouse to claim life insurance

proceeds where the insured forgot to change the beneficiary in order to reflect his or her new circumstances. Just imagine what a nightmare it can become trying to unravel such a mess!

The simple way to avoid this common mistake is to conduct a regular review of the beneficiary designations on all of your life insurance, IRAs, pension and retirement accounts, and any investment accounts with TOD/POD provisions, and compare them with the design of your estate plan. If you are unable to locate a copy of your current beneficiary designations, there is no harm done in filing a new one just to make sure.

MYTH/MISTAKE #7:
HAVING A LIVING TRUST WILL COMPLICATE
MANAGEMENT OF YOUR AFFAIRS

When a revocable living trust is recommended as the preferred alternative to a Will for use as a client's primary estate planning document, the concern is sometimes voiced that, "Won't a trust make my life more complicated?" This question sometimes arises because of a concern that it will make preparation of income taxes more complicated. In other cases, it is because the additional paperwork needed to initially coordinate all of the assets with the trust – bank and investment accounts, pensions, life insurance and IRAs, and real property – can be intimidating.

Let's deal with the income tax issue first. A revocable living trust is not a separate taxable entity, and thus, does not require any additional income tax preparation. The tax ID number of the trust is usually the social security number of the grantor (creator) of the trust, and all income reported on assets placed in the trust is reported on that social security number. This is the same way the income was reported prior to the creation of the trust, so creating the trust has no additional impact on the record keeping needed to file an income tax return, or on the filing of the return itself.

As regards the title transfers needed to fund the trust, it is true that when a living trust is first established, there is a bit more legwork to do in order complete the estate plan. As discussed in the prior Myth/Mistake #5, on Funding the Trust, and Myth/Mistake #6, on Coordinating Beneficiary Designations on Insurance and Pension Assets, the plan is not completed until these items are also finished. This does require somewhat more work at the front end than a Will may require, but do not let this discourage you from pursuing this direction in your estate planning.

Once a revocable living trust is completed AND funded, it actually becomes easier to manage your affairs – not harder. Think of the trust as a collection point for all of the assets that remain in your estate after your death. Once you have either titled assets in the trust, or named the trust as the ultimate beneficiary of assets that pass by beneficiary designation, it is a simple matter to alter how your estate is distributed after your death. By making one change to the distribution provisions of the trust document, the change automatically extends into all of the assets that flow through the trust. No need to contact all of your life insurance carriers (group and personal), your pension and IRA administrators, your bank(s), the county or counties where you hold real property, or any of the investment firms you deal with. It is all handled by making a simple amendment to your trust, and voilá, you're done.

Making the trust the controlling instrument also ensures that your trustee will have the funds and assets needed to pay any debt, taxes, or other obligations of your estate prior to making distribution to your beneficiaries. Assets that pass directly to heirs through a beneficiary designation,

through a transfer-on-death or pay-on-death provision, or by title (joint-tenancy) are not available to your trustee, and could place a hardship on the estate and other beneficiaries, potentially undoing your intended distribution plans.

Yes, a revocable living trust does take a little more energy to finish than does a Will, but in the long run, the ease of administration of your affairs more than compensates for any perceived headaches at the beginning.

MYTH/MISTAKE #8: **YOU MUST LEAVE YOUR ASSETS TO YOUR CHILDREN**

I sometimes think that the perfect estate plan should be able to fit on a 3" x 5" card, and simply state, "I, John or Jane Doe, being of sound mind, spent it all while I was alive". You may laugh, but really, none of us are obligated to leave anything behind when we die. However, since most of us cannot time the hour of our passing, and do not want to risk running out of money while still alive, the odds are great that when we pass away there will still be assets remaining in our name. In the absence of a formal estate plan, the state will look to a spouse first, and children second. From this springs the notion that we must leave our worldly possessions to our children.

In many cases this is our desire, but in some circumstances, there may be reasons that someone chooses not to leave their estate to children or grandchildren. There is also nothing in the law that requires that anything be left to children or grandchildren. Sometimes the reasons people choose not to leave anything to their children, or perhaps just a specific child, are unfortunate, such as a family fractured by conflict, a child who is permanently incarcerated, or even a child who did not marry as the parents might have liked. In other cases, the children have all flown the nest and are doing quite well on their own, and do not need or want anything, other than personal mementos, from the estate.

As a reflection of your values, or perhaps as an expression of gratitude for the impact an organization has had on your life, you may want to choose a charity as the beneficiary for all or a portion of your estate. These could be your church or synagogue, a community foundation, your alma mater, a national charity like the Red Cross or the American Cancer Society, or any combination of these. This is a wonderful thing to do, and provides a living example to your children of what you valued in life. If they do not like it, there is also little they can do about it.

Whatever the reason for not leaving some or all of your estate to your children, you are not under any obligation to leave them anything. That being said, most of us do wish to leave most, if not all, of our estate to our children. However, the concern that we often hear voiced is that the children, particularly if they are minors or young adults and not financially mature, will squander their inheritance. This is a valid concern and one we are accustomed to handling.

Often we will draft a revocable living trust with provisions to hold the children's inheritances in trust until a certain age, such as 35. Until that time, the trustee is authorized to use as much of the net income and principal of the trust as the trustee deems necessary for the health, education, maintenance and support needs of the child. There can also be scheduled distributions at certain age, such as 1/3 at age 25, 1/2 at age 30, and the balance of the trust at age 35. I like to think of this as a personal "three strikes" rule.

We frequently draft these trusts to also allow the trustee the discretion to distribute a portion of the trust to the beneficiary for the down payment on a personal residence or the establishment of a business. Another favorite is to include a provision that after a certain age, such as 22 or 23, the trust will only distribute income for education and health needs, but no more support for lifestyle. Instead, upon reaching that age, the trust will provide a dollar-for-dollar earned-income match (up to a chosen limit) to the beneficiary. The objective is to encourage the beneficiary to find gainful employment, develop a work ethic, and become a contributing member of society. There is a strong incentive for the beneficiary to do this as well. Let's say the child enters the workforce and begins to earn \$35,000 per year. If the trust has this particular provision, it will match that \$35,000, or some portion of it, from the trust assets.

So, are you required to leave anything to your children? No. But if you do, and most of us do, perhaps what you really want to think about is how you can leave a legacy or more than just money to your children, but also a legacy that reflects your values, and instills those values into the next generation. This is a worthy goal, and something to consider.

MYTH/MISTAKE #9: **LIFE INSURANCE IS TAX-FREE TO MY BENEFICIARIES**

Life insurance can play a valuable role in estate planning, from providing cash to the trustee or executor to pay off debts and final expenses, or to produce income for a surviving spouse and children. Sometimes it is used to infuse cash into a business upon the untimely death of a key shareholder or partner, or in larger estates, to provide the liquidity needed settle up with Uncle Sam for any estate tax liability while avoiding the liquidation of estate assets.

However, when it comes to taxes, it is important to remember that in the estate planning arena, we are often talking about two different kinds of taxes: Income tax and Estate tax. Life insurance is almost always income-tax free. There are a few exceptions in business uses of life insurance where the death benefit might be income taxable, but for purposes of this discussion, we will assume that we are not looking that unusual situation. The key to remember is that while life insurance in most instances is income-tax free, it may still be taxed under the federal estate tax rules. A very brief review of the estate tax rules is in order.

The federal estate tax is a transfer tax, and is assessed on the assets you leave to the next generation. In 2009, we each had an exemption from that tax, which was \$3.5 million per person. Just for 2010, the federal estate tax has been repealed, unless Congress takes action to reform estate tax regulations later this year. Otherwise, in 2011 and beyond, the exemption from the federal estate tax will fall to only \$1 million per person. Some people joke that 2010 "is the year to die", but I would not make that one of your short-term goals! It is possible the \$3.5 million exemption will be reinstated and extended; however, nothing is final yet. In fact, the House of Representatives passed a bill in December of 2009 that would have extended the \$3.5 million exemption, but at this writing, the Senate has yet to act on it. The estate tax rates, whatever the exemption amount ultimately becomes, will range from 45% to 55%, of the amount on the estate in excess of the exemption.

Why is this important in a discussion about life insurance? Because the death benefit of all the life insurance that you own or control (such as group life insurance) is included in your taxable estate for purposes of calculating your taxable estate. For example, let's assume that in a worst case scenario, the exemption has fallen to \$1 million per person after 2010. With a properly constructed Will or trust, a

married couple can each make use of the exemption, thereby sheltering up to \$2 million of their assets from estate taxes. Let's further suppose that our hypothetical couple's financial statement shows that they have a net worth of \$1.5 million. No problem, right? But they also each own a \$750,000 life insurance policy naming the other as beneficiary, for a total of \$1.5 million of life insurance protection. When added to their net worth of \$1.5 million, that \$1.5 million of life insurance now takes their taxable estate to \$3 million! This exceeds their combined exemptions by \$1 million, and can result in federal estate tax liability of anywhere from \$450,000 to \$550,000, depending on where the tax rates ultimately settle.

The short answer then, is that life insurance proceeds are almost always income-tax free, but depending on the size of the estate, the death benefit may be taxed as part of the estate, the same as if it were a piece of real estate or an investment portfolio. There are ways to "have your cake and eat it too", and keep life insurance both income and estate tax free, but they are beyond the scope of this myth-busting article. To learn more about ways to ensure that your life insurance does not create additional estate tax liability, please see the article on this site entitled "Advanced Estate Planning"

MYTH/MISTAKE #10: **FAILING TO PERIODICALLY REVIEW YOUR ESTATE PLAN**

There is a tendency on the part of some people to think that once they have completed their estate planning documents, they can put them away in a safe place and not give them another thought – they are "done". This idea can be dangerous to your planning. It is true that age alone does not invalidate a Will or trust. They do not have an expiration date, like a carton of milk, and can't go "bad". However, failing to periodically review your estate planning documents can result in, at the least, some inconvenience for your heirs, and at the worst, a failure of the estate plan to accomplish your intended goals. Many things can impact on your planning and necessitate at least a review, and possibly some changes to your estate plan: Marriage, divorce, establishing or closing a business, or a change in your financial circumstance because of an inheritance, just to name a few.

We recommend that you review your Will and/or trust annually. This does not mean that you take it to your attorney and have it reviewed, but rather, take out the documents and simply read them yourself. First look at the order of succession for the trustees for your trust and the executors of your Will. Are the people you named in the documents still the ones you would choose today, and in the order you have specified, or might you need to make a change? Have you or any of them moved away, and acting in as your executor or trustee would now present a hardship to them or your other family members? If so, a tune-up is in order. You should also do this same review of the people listed as the successor agents in your powers of attorney and powers of attorney for health care.

The next step in your review is to look over the dispositive provisions of the Will and trust. This is where you have provided instructions and provisions for the distribution of your estate after you have passed away. Are these still in keeping with your wishes now, and with the current structure of your family? Perhaps one of your children is in an unstable marriage now, and you would like to protect their inheritance from being dissipated in a divorce, or another child is proving to be unable to manage money, and needs to have their inheritance metered out over a period of years instead of receiving it outright. Maybe you now have grandchildren that you did not have at the time you completed your Will or trust, and some of them are facing these same issues. Did you name a charity to receive a portion of your estate, and you would now prefer to increase or decrease that bequest, or change the charity?

These are all valid reasons to review your estate plan and if needed, make changes that reflect your current situation; otherwise your planning may fall short of the goal.

Thus far the reasons listed for reviewing your estate plan are personal (or internal) changes to your circumstances. There are also external events that can provide valid reasons to review your planning documents. For example, have you changed your state of residence, and although your family structure or situation may not have changed, are the laws of your new state of residence different than those in the state where your documents were originally drafted? Additionally, it seems as though tax laws are always changing, so it is important to determine if any of these changes have impacted on your estate distribution planning. The federal estate tax is currently in a state of flux, and may have a significant impact on the planning that many people have already done, depending on what action the Congress finally takes, if any, during 2010. At our firm, we stay abreast of changes in the external environment that impact on the planning of our clients, and alert them when anything significant happens that might necessitate a change to their plans.

This list of reasons to review your estate plan on a regular basis is by no means comprehensive. However, it should serve to demonstrate that estate planning is not a static process, but a flexible one that evolves as your life and the world around you changes. As much as we might all like to be “done for good” when we finish our estate planning documents, the reality is that, as with all things in life, change will occur, and it is therefore critically important to review your estate plan periodically in order to ensure that it will achieve your desired objectives. After all, your estate planning documents will speak for you when you are either incapacitated, or after your death, and you are no longer able to speak for yourself, so it is vital that they speak clearly and accurately.