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Who Needs an Estate Plan Anyway? (Part 2)

When people discover I am an estate planning attorney, our conversation often takes the following turn:

> "So you're an estate planner. Let me ask you: do I really need an estate plan? I've heard the government only taxes the ultra-wealthy. And I've been told that if I die without having done anything, my stuff goes to my spouse, which is what I want. And if I do need some kind of basic plan, can't I do it myself?"

I reply that most adults would be well advised to do some estate planning, especially those individuals who fall within one or more of the following categories:

- Married Persons
- Persons in Committed, Non-Marital Relationships
- Persons Who Are Divorced
- Persons with Children
- Individuals with Significant Wealth

In the article referenced below, the second of a two-part series, I provide case studies to cover scenarios in the last two categories and discuss how a well-crafted estate plan would result in a better outcome.

People With Children. Having children is often a triggering event prompting people to do estate planning. Young parents are usually quite concerned about who will act as the guardian of minor children in the event both parents are gone, and devote a great deal of time selecting guardians. Unfortunately, young parents are usually less motivated to plan thoughtfully for the potential transfer of property to their children in the same circumstance. Most young parents do not perceive themselves as having yet accumulated enough wealth to worry about this issue. This perception is a potential trap.

Rhonda and Don. Consider the story of Rhonda and Don who have been married for three years and have just had a baby boy named Tommy. Rhonda has decided to stay at home with Tommy while Don works. Don wisely buys $2,000,000 of term life insurance so that Rhonda will not have to go back to work in the unlikely event he dies. In the beneficiary designation, Don designates first Rhonda and second any children he has as beneficiaries. Don and Rhonda also execute "simple will" forms that they find on the internet, which provide that the surviving spouse inherits all of the deceased spouse's property, or if there is no surviving spouse, any children inherit. Don and Rhonda designate appropriate guardians for Tommy and any other children they may have in the simple wills. The simple wills additionally contain some "boilerplate" which provides that if any of Rhonda and Don's children are minors, then any property passing to them is subject to a custodianship until age 25. This makes sense to Rhonda and Don. Rhonda and Don mistakenly think that this directive will apply to all of their property if they are both gone.

Don and Rhonda are killed five years later in an accident, leaving Tommy behind. The beneficiary designation naming Tommy (now 5) as contingent beneficiary controls the disposition of the proceeds from Don's life insurance, not Rhonda and Don's wills. This is bad news because as Tommy is only 5, the $2,000,000 of life insurance will be subject to a guardianship procedure under California law, which at the end of the day will only keep the money out of Tommy's hands until he turns 18.

When Tommy turns 18, there is $1,900,000 left in the guardianship account. Tommy elects to forgo college and takes off on a two year trip around the world during which he squanders the entire amount.

A Better Outcome. If Don and Rhonda had consulted with counsel, the attorney would have taken steps to ensure that the ultimate distribution of life insurance proceeds was controlled by an appropriately drafted estate plan. That being the case, the money probably would not have been distributed outright to Tommy, even at age 25. Instead, the insurance proceeds would have been subject to some form of trust for Tommy's benefit until he reached an age of maturity. This mode of distribution would have increased the chances that Tommy would have completed his college education and become responsible and self-sufficient prior to inheriting the insurance proceeds outright.

A Note For People With "Special Needs" Children. People who have a child with special needs should be especially diligent about estate planning. Improper planning or failure to plan can result in the disqualification of the child from receiving critical government benefits (e.g., Supplemental Security Income and Medi-Cal). The better alternative is a carefully drafted "special needs trust" that provides for the child without disqualifying him or her from receiving government entitlements. A special needs trust is also a far better solution than leaving everything to non-special needs children with the informal and unrealistic understanding that they will "take care" of their special needs sibling.

Persons With Significant Assets. I run into many people who own significant assets but whose net worth is below the amount of the current estate tax exemption ($5,000,000 for 2012). Because they do not appear to have a "tax problem," they wrongly assume that they don't need an estate plan.

Sally and Adam. Sally and Adam are a case in point. Sally and Adam have been married for years and have accumulated $4,000,000 of community property (well below the current $10,000,000 estate tax exemption amount available to married couples). Sally and Adam have two adult children. Sally and Adam have "sweetheart wills" that they signed 20 years ago which provide that the surviving spouse inherits everything outright.

Upon Sally's death, her entire $2,000,000 estate passes to Adam outright in accordance with her will.

A year later Adam marries a younger woman, who as it happens has few financial resources of her own. When Adam dies four years later, he leaves everything outright to his young wife, having been alienated from his children who never approved of the new spouse.

The children are angry that their parents' estate passes to the new wife and sue, claiming that Adam was mentally incapacitated at the time he signed his will and that his surviving spouse is a "financial predator." Rancorous litigation ensues. A settlement is reached some months later in which none of the parties take any satisfaction.

A Better Alternative. If Sally had done proper estate planning, she would have considered leaving her property in trust for Adam's benefit in a way that would have taken care of his needs while ensuring that their children were not "swindled out of their inheritance." Adam meanwhile could have established a trust for the lifetime benefit of his new wife (that also would have made provision for Adam's children upon the new wife's death) which may have helped avert litigation.

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