

Wealth Planning Insights

Estate planning for young families**2**

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Disclosures**8**

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Estate planning for young families

There are as many follies of youth as there are youth to carry them out. In estate planning, these follies often take the form of excuses for the failure to understand the importance of estate planning:

- *“I am too young to plan now.”(Translation: “I have a long life ahead of me. I’ll do it later when I am older.”)*
- *“I’ll get to it, but right now I’m too busy.”(Translation: “Get off my back. It’s just not a priority for me now.”)*
- *“I’m healthy. Nothing’s going to happen to me.” (Translation: “I am invincible.”)*

Add minor children to the mix and these excuses remain, albeit with a pang of guilt arising from the haunting knowledge that it probably is something a responsible parent should do.

“Failing to plan is planning to fail.”

The adage is true: the risk can be tragic yet the unintended results may be entirely avoidable. The foundation of a solid estate plan is a solid financial plan. For young families, the two are intricately intertwined because they both address the same core issue: uncertainty for the future. Combined, they represent a solid wealth management plan.

Knowing what you have

Before any estate plan can be prepared, an accurate understanding of your income, expenses, assets and liabilities is essential. Its expression is in the form of a simple budget with balance sheet. A comprehensive financial plan takes that further by presenting the budget and balance sheet in a financial context with your goals, risk tolerance, savings plan and investment strategy. An effective estate plan nestles the financial plan in a life context. When executed properly, it all works together in harmony.

Determining your responsibilities

Whom you need to protect may seem simple at first: spouse and children. A careful reflection might give rise to the inclusion of others to the nuclear family mix, such as parents, siblings, in-laws, business partners, employees and charities. Furthermore, a look to the legal nature of members of the modern family may reveal different legal relationships that may require different planning strategies. Consider these questions:

- Is your “life partner” your spouse, your domestic partner or your “happy attachment?”
- Are the children yours (natural born/adopted/present marriage/previous marriage/no marriage) or your spouse’s children (previous marriage/no marriage) whom you have not adopted?

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Protecting your surviving spouse

Spouses may see each other as equal partners to the marriage, yet the elements that make up that “equality” may be very different from one spouse to the other. Reflect on the following questions:

- What assets and/or liabilities did each spouse bring to the marriage? Did one spouse previously inherit property? Did the other spouse carry large student loans?

- Are both spouses employed outside the home? Are their incomes similar or significantly different? Is one spouse employed inside the home as a homemaker/caretaker of children or others? Does one spouse earn income from employment? Does the other spouse earn appreciation from volunteer work?
- What unpaid work does each spouse do to maintain the family and the home? Could one spouse do the other spouse's domestic work or would the domestic work be required to be hired out?

An understanding of these answers will aid in determining the degree of support needed for the surviving spouse.

Minor children

If there is one strong motivating concern, it must surely be the care of minor children in the event of the death of both parents. The Last Will and Testament appoints the guardian(s) of minor children. Failing to effectively determine the guardian for minor children leaves the decision in the hands of the probate court. It doesn't stretch the imagination to think that the court appointed guardian may not be the guardian that the parent would have chosen.

These questions may be useful in helping parents decide upon the best guardians for their minor children:

- Is this the right person to raise your children? Does this person have the right personality, temperament and patience to parent your children in the manner you would? Will your family values (religious, moral, ethical) be given to your children by this guardian?
- How will your children fit in with the guardian's family?
- Will the guardian foster your children's relationships with your extended family, such as grandparents, aunts and uncles, cousins?

As you think about potential the guardian's parenting and social skills think also about the guardian's ability to manage the finances and assets you leave for your children.

- Can the guardian be trusted to manage the assets of your children prudently?
- Does the guardian have the financial management and investment skills necessary to make proper decisions in managing the assets?

An honest appraisal of the guardian's business acumen may indicate the need for a professional investment manager and/or a corporate fiduciary trustee.

Another important factor involves the expense of raising your children. Direct expenses, such as food, clothing and education, are relatively easy to estimate. Indirect expenses, such as vacations, hobbies and other "quality of life" expenses are not. Capital expenditures and personal time are even more difficult to estimate:

- Will the guardian need to adapt his or her home to accommodate your children? Are there enough bathrooms and bedrooms? Is there enough communal living space? Would an entirely new home need to be bought or built?
- Would a guardian need to reduce or eliminate employment outside the home to create the time needed to raise your children?

It is likely that additional resources may be required to accommodate the raising of your children beyond customary daily expenses.

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Finally, ask yourself this “bottom line” question:

- Can the guardian balance the interests of his or her family and mine so as to provide all with a feeling of belonging in the new combined family?

You see? It’s not always about the money.

Adult children and other special considerations

Children are not necessarily clustered within a narrow age band, especially in second marriage situations. For those with young and adult children, there may be circumstances where a parent may wish to make special provisions for the adult children almost as though they were still minors.

The first category involves “troubled” adult children, examples of which include alcoholism and substance abuse, spendthrift issues, behavior challenges, and incarceration. These and other similar situations require sensitive understanding and technical planning so that the beneficiary’s life is enriched and their troubles not enabled.

The second category involves “special needs” children who have challenges or disabilities that inhibit their independence and ability to care for themselves. In this situation, careful consideration should be given to planning techniques which will preserve benefits available under government or other programs. Special needs planning may provide additional “quality of life” resources for the beneficiary, such as for the purchase of specialized equipment and specialized training. Capital expenses such as adapting the home may also be appropriate.

The third category may be labeled “the trust fund brat.” Estate planning here may be seen more as avoiding the creation of a future problem rather than addressing a present problem. For examples, peruse the tabloids in any supermarket checkout line.

Life and disability insurance planning for young families

For many people, life insurance is an integral component of any well organized and executed estate plan. Although there are many reasons for life insurance, the three common reasons for including it in a comprehensive estate plan are:

- Estate solvency—where liabilities are greater than assets, or where liabilities are significant in an illiquid estate, life insurance may be used to pay off debt.
- Income replacement—where premature death results in the loss of the income of an employed spouse, life insurance may be used to provide a replacement of the accumulated lost income.
- Wealth preservation—where an estate is subject to unavoidable income or estate taxes, life insurance may be used to reduce estate shrinkage due to taxes.

In determining the amount of insurance needed to supplement existing assets available to the surviving spouse, consideration should be given to the following questions:

- What was the earned income of the deceased spouse? What does the surviving spouse need for support pre-retirement? Post-retirement? What support is needed for dependent children? For other dependents?
- Will hired help be needed to replace the domestic services of a deceased employed spouse and/or a stay-at-home parent?

A comprehensive financial plan will help determine the appropriate amount and corresponding cost of insurance within your resources—insurance that is neither too much, too little nor too expensive.

The support needs of dependent children may vary considerably depending on whether a guardian is necessary. Ask yourself:

- How much will it cost to provide my children with the basics (food, clothing, shelter)? What additional expenses will contribute to my children’s quality of life?
- How much will it cost to educate my children? Primary school? Secondary school? College or trade school?
- Will I need to provide additional support to the guardian of my children?

Insurance planning should also consider the timing of the needs in determining the type of insurance to maintain.

- What is needed if one spouse dies prematurely? (Single life insurance) If both die prematurely? (Survivorship insurance)
- When are certain expenses likely to occur? Lapse? For example, term insurance may be appropriate for education expenses until the youngest child attains age 26, whereas permanent insurance may be appropriate for the lifetime support of the surviving spouse.

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An individual is also more likely to become disabled by accident or illness than die prematurely. Disability may affect the disabled spouse’s ability to earn a living and may add incremental expenses to the family budget. Disability insurance to replace a portion of lost income should be considered. It is often available through an employer’s benefit package. If not, private disability insurance may be available.

Basic estate planning documents

Regardless of your income or the size of your estate, the following documents comprise a basic estate plan:

1. Last Will and Testament
2. Revocable Living Trust*
3. Medical Power of Attorney
4. Financial Power of Attorney
5. HIPAA Authorization
6. Advanced Directive/Living Will

*The Revocable Living Trust may be deemed optional for individuals with small estates, but it is a basic document for those with large estate assets or those with smaller estate assets and large life insurance.

Basic estate planning decisions

The adage “you get what you pay for” is as true in estate planning as it is in many other areas. Avoid the temptation to either do it on the cheap or do it on your own. Instead, engage an attorney who specializes in estate planning. The ever evolving nature of estate planning indicates that it should be a prominent focus of your attorney’s practice, not something that is just occasionally dabbled with.

Next, assemble your estate team. This will consist of:

- Executor/Administrator/Personal Representative
- Trustee and Successor Trustee
- Holder of Financial Power of Attorney

The best estate plans are often those which accomplish an individual's wishes in a tax-efficient manner.

At minimum, you should review your estate plan every five years or sooner.

- Holder of Medical Directives
- Guardian of Minor Children

If you are considering naming family or friends for one or more of these roles ask them if they would take on the responsibility, determine who would best fit which role, and inform them that you have appointed them to a specific role in your estate plan. No one likes surprises.

Finally, decide on the distribution of your estate among your surviving spouse, children, others and charities. Often, the best decisions are made when you discuss options, opportunities and obstacles with your estate planning attorney and financial advisor.

The tax wrapper

The best estate plans are often those which accomplish an individual's wishes in a tax-efficient manner. Certainly, an understanding of the taxes involved and their application to your situation are important to helping you decide on what you want to accomplish, but tax minimization considerations alone rarely result in an estate plan that does what you want it to do for your beneficiaries. A competent estate planner will help you decide what is most important for you to accomplish in your estate plan and provide you with an estate planning recommendation in an efficient tax wrapper.

Implementing the plan

The estate planning process is not complete once your documents are signed and the ink has dried. The final step involves implementing the plan. That includes retitling assets, changing beneficiary designations on retirement accounts and existing life insurance policies, and purchasing any insurance recommended in your estate. Most estate planning attorneys will provide their clients with instructions on implementing your estate plan. Your UBS Financial Advisor can help you retitle your accounts already at UBS, consolidate other assets in accordance with your estate plan, and provide you with the necessary disability and life insurance coverage you need.

One more thing

Your documents are signed. Your assets are retitled. Your beneficiary designations have been changed. Your insurance is in place. Your estate plan is complete.

Now what? Are you through forever and a day?

No.

What always remains is the ongoing review of your estate plan. At minimum, you should review your estate plan every five years or sooner, especially if any one or more of the following circumstances occur:

- Any significant change to your personal family situation, including births, adoptions, deaths, divorces, remarriages, illnesses and disabilities.
- Any significant change to your financial situation, including increases or decreases in employment, income, expenses, cash flow, inheritances, assets and liabilities.

- Any significant change to the timing of an anticipated financial or personal event.
- Any change of domicile to another state or country, especially if it involves a move that involves a new state with or without community property laws.

If you are unsure whether a change is significant enough to merit a modification to your estate plan, make sure you mention it to your UBS Financial Advisor, either during a formal review of your financial plan or during any conversation on a routine matter.

– *David R. Mietty, Wealth Planning Strategist*

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