

Questions families need to ask about inheritance

There are many difficult questions that must be addressed when developing an estate plan. Knowing what those questions are and identifying the issues is vital to producing an estate plan that meets your wishes and the needs of your family. This document is designed to help you identify the most important questions and offers ideas to help you answer them. (This information is based on a *Wall Street Journal* article titled, "Pass It On" which appeared in the March 25, 2002 issue.)

1. Should I talk with my children about their inheritance?

The answer is simply "yes." But many parents have legitimate reasons for not discussing inheritance with their families. An obvious concern is that if children learn of future gifts, they may become lazy or not meet prior educational or professional goals. On the other hand, discussing your plans allows you to observe their reactions. Whether they react positively or negatively, it's believed to be a better course of action because you'll have the chance to explain your decision. Otherwise, children's memory of you may be soured simply because they don't know why you did what you did.

Having said that, how do you raise the subject with your children? A popular method is to speak with each affected family member individually. Tell them that you're trying to decide what to do and ask them what they want and expect. Once all of this information is gathered, you'll be able to address any conflicts. Keep in mind, however, that this does not guarantee that all interested parties will agree with your final plan. It simply provides you with the information you need to minimize potential conflicts.

Whether or not you feel comfortable discussing your plans with your children, it's critical to manage their expectations and not mislead them. This can be done by stating your intentions clearly and by avoiding vague terms. Frequently, of course children can get upset over not getting more money from their inheritance. This is exacerbated when parents tell their children that they'll "be taken care of" when the parent(s) die and then receive much less than they expected. The parent may have honestly thought that the amount of money was substantial but the children's view of the amount could be very different. Family members can also become confused and upset when they receive more than they expected because they could have used the money earlier when they really needed it.

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2. If my parents don't discuss their inheritance plans with me, should I ask them what their plans are?

Yes. If your parents haven't discussed their inheritance plans with you, there's a chance that they haven't discussed them with anyone. Because your parents assets must be transferred

(either to you or somewhere else) once they die, you need to know what their intentions are. As their child, you may be responsible for managing this transfer so it's in your best interest to see that it goes smoothly. Another important reason to have this discussion is that the children won't be left to speculate on what their parents' intentions were. Without this knowledge, children often dispute what their parents would've wanted. This scenario typically leads to family disputes and sometimes to the destruction of sibling's relationships with one another.

So, how do you bring up the topic of inheritance with your parents without sounding greedy?

One idea is to tell them that you're working on your own estate plan and that quality of the plan depends on knowing as much as possible about your future financial position. Even if they turn your discussion offer down, it often leads to them discussing it amongst themselves and eventually to their lawyer. It's not imperative that you know what your parents' plan is. However, it *is* imperative that you know they have one.

3. Should each child receive an equal piece of the pie? What if I want to give more to one or even give nothing to one of them?

While it seems perfectly natural and fair to divide all the assets by the number of children in the family, there are good reasons for both a balanced and unbalanced distribution of your assets.

As parents you have inevitably done financial favors for some – or all – of your children. The cost of these favors – college tuition, car purchases, loans that haven't been repaid – are likely different. This may be a moot point to you but you can bet that your children are keeping score and have a good idea how much financial assistance you've given to which child or children. This is a good reason to consider adjusting the distribution for some children.

It's common for parents to leave less money to those children that are financially stable. While this may sound reasonable, it may leave the brain surgeon of the family feeling unloved and resenting his or her brothers and sisters. One solution is to divide a portion of the assets equally and put the remainder in a trust for emergency needs.

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Estate planning often gets sticky when a family business is involved and makes up the bulk of the estate and/or only one child works for the business. A common solution is for the parents to buy extra life insurance payable to the children outside of the business. Another option is for the child involved can buy out his siblings.

What if you have a child that hasn't been a part of the family for 20 years or has a drug problem? You may be tempted to write him/her completely out of your will but there are likely consequences to doing so. The child could make life miserable for his/her siblings by contesting the will or constantly asking them for money. A possible solution is to leave them enough money that they won't want to risk losing it. You can also add a clause in your will that states "If you contest this will, you lose your bequest."

4. Should I include my grandchildren in my inheritance plan?

This is fine as long as it's done correctly. As usual, there are a few pitfalls to avoid. First, your children may feel as though you are usurping their authority if, for example, you leave money to a grandchild if the money is available to him or her before finishing college. Doing so gives the grandchild financial freedom and the means to stray from the parents' original plan for their child's education. Additionally, a young child receiving an inheritance could end up confused because their goal goes from creating and building their life via education and employment to not screwing up what they've been given. The latter goal doesn't promote high self-esteem and could have disastrous consequences.

As usual, communication can help limit surprises. By talking to your children about what you'd like to give to *their* children you would be taking the steps necessary to keep your generosity from backfiring. A possible outcome could be that you place the grandchild's inheritance in a trust fund with his or her parents acting as trustees.

Lastly, consider at what age your grandchild will get control of the inheritance. Putting some restrictions on when your grandchild has access to the money – and what purposes the money can be used for – is a good way to avoid disaster.

5. What considerations are there for a "blended" family?

Unfortunately, in these situations, the worst solution is the most common: leave everything to the second spouse for use during his or her lifetime, with the remaining assets passing to the children when the spouse dies. This causes an instant conflict between the children and the surviving spouse because the spouse needs to invest the money to provide income while the children want the money invested for long-term growth. Not to mention that the spouse may decide to simply spend the entire pot and leave nothing to the children.

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One alternative is to give the children their inheritance while you're alive. Depending on the age of the children, it can be used to help pay for college, buy a house, or be put away for later use. Doing this tends to take a lot of pressure off of the parent.

For those that can't afford to give up assets now a good option is to establish an irrevocable life insurance trust with the children named as the beneficiaries. The trust would own the policy and when the parent dies, the benefits would go to the children – tax-free. With this arrangement, your children would receive their inheritance and you could leave the rest of your assets to your spouse.

If you and/or your spouse have children from more than one marriage, things get proportionately more complicated. A serious consideration is the age of the children. This is not so much a consideration when deciding how much to leave each child, but more for what vehicle is used to transfer the assets. For example, if the children range in age from three to 30, consider giving each child an equal share but also holding 25% in a trust. This will allow the younger children to have future expenses, such as weddings and college tuition, taken care of by the money in the trust. This is equitable because the older children likely would have had these things paid for by you.

6. Am I pulling the reins too tight?

Well, you can't plan for every possible contingency or problem and some people have legitimate concerns about trying to exercise too much control for too long from beyond the grave.

Rather than using a trust to try and prevent bad behavior, some estate planning advisors and their clients are using "incentive trusts" that are designed to encourage good behavior. For example, a family that is concerned about an heir inheriting a large sum and then not pursuing an education might provide a cash incentive for graduation from college or graduate school. Alternatively, some families have a concern that wealth can destroy a young person's willingness to work. To counter this, an incentive trust might provide income that matches a portion of the young person's compensation over a minimum threshold. The trust might provide a dollar for dollar match (up to some maximum) for every dollar of compensation over \$50,000 per year.

Others argue that family-incentive trusts can cause problems if they aren't designed properly. For example, a trust can be drawn with an incentive that is too narrow. Assume the trust provides a cash bonus if the beneficiary graduates from medical school. However, the beneficiary chooses to devote his/her life to social work and pursues a graduate degree in sociology. That beneficiary would not receive the bonus distribution, but is that really what

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the grantor of the trust wanted? Did they intend to provide an incentive to be a doctor or to pursue a career of service to humanity?

7. Should I give my heirs part of their inheritance before I die?

Many people used to give away large sums of money each year as a way to avoid paying estate taxes in the future. This year, however, is the first of several that will see the estate tax exemption increase. Whether or not this practice is still viable depends on a few variables.

The number one concern is that you aren't giving money away that you might need for yourself in the future. Nursing home expenses, among other things, will continue to increase – as will the likelihood that you could live well into your 90s.

If you decide that you can still afford to share, you may want to consider ways to give other than simply writing a check. Paying for family vacations, college tuition, medical bills, or down payments on a new home are all ways you could spend your money while creating a lasting memory or helping loved ones build their own families.

8. Who's going to manage all this when I'm gone?

The answer to this question depends on a few factors. If you have a will, you'll have to name an executor of your estate. If you have a trust, you'll have to name a trustee to manage it.

In both instances, you have several choices as to who serves as executor or trustee. You can name a lawyer, a trust officer, professional personal representative, or a family member. You also have the option of splitting duties and having, for example, a trust officer and a family member act as co-trustee for your trust. Likewise, you may name your lawyer and a family member as co-executors of your estate. Try to avoid naming one family member as "the boss." It is a quick way to generate conflict, in-fighting and jealousy among all the children. It is also a good idea to avoid naming someone who lives far away because they can slow down the settlement process.

You should also want to allow your family switch trustees. A bank where your trust officer works may be acquired, or your lawyer may retire. Building this flexibility into your estate plan could save your children a lot of frustration. If possible, it's a good idea to introduce the appropriate children to the professional you've named as co-executor or co-trustee. It will benefit everyone involved if the first time they sit down together is before they need to settle your estate. Also, if they don't get along, you can oversee the naming of a new executor or trustee.

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9. Should I leave something other than money?

While most inheritances involve monetary assets, some consist of family keepsakes such as photographs, paintings, collections, etc. The key to leaving items such as these is that they are organized in a way that they are useful to the recipient – especially if the recipient is a museum or library.

Another interesting tool for leaving non-monetary assets is the “ethical will.” While it’s no substitute for a legal will, it is used to document personal reflections and stories that can be passed along to heirs. This is a helpful compliment to a legal will because oftentimes legal wills fail to capture the essence of a person’s valuables – monetary or not. Ethical wills help to document what someone did, why they did it and why it was important.

10. Should I leave everything to my family?

If there’s a cause that’s near and dear to your heart, you may want to consider using a portion of your estate – regardless of size – to establish a family foundation to support that cause. For those with sizable estates, they are sometimes afraid that leaving a large inheritance to their children or grandchildren could undermine their will to work hard, go to school, and get a good job.

One set of grandparents decided to create a private charitable foundation with themselves and their children as trustees. They held annual meetings on July 4 that doubled as family reunions. Another set of grandparents created a family limited partnership that was funded with real estate and securities. They transferred their interest in the partnership to their adult children and used it as a learning tool with semiannual meetings to review its operations and tax strategies. Both of these scenarios illustrate how the grandparents used their estate to keep their harmonious family intact. Unfortunately, inheritances have the ability of turning strong family relationships and destroying them.