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4 Costly Estate-Planning Blunders

Think your documents are bulletproof? Check again to avoid these common mistakes

by: G.M. Filisko | from: AARP | January 4, 2011

Why work hard to build wealth only to have your wishes thwarted or your family left with much less than you anticipated? From wills to trusts and beyond, protect your loved ones by avoiding these four costly but common estate-planning mistakes.

1. Forgoing an expert's review. There's nothing wrong with saving a few bucks by drafting your own estate-planning documents. You can find templates for basic wills and such online or in bookstores. Just be sure to invest in a review of the final documents by an expert to be sure everything is in order.

Estate-Planning Basics

- 10 things to know about wills. **Read**
- Understanding living trusts. **Read**
- More on estate planning. **Go**

"Ninety percent of the online estate-planning documents I see don't do what the people think they're going to do," says Leanna Hamill, an estate planner and elder law attorney in Hingham, Mass. "I've seen people use online documents, documents out of estate-planning books or documents borrowed from friends. But they screw up their estate plan because they don't understand the legal and technical aspects of the documents."

Common mistakes Hamill has seen? One client signed a deed transferring his house to a trust but hadn't properly created the trust. Thus, the deed had no effect. Another client's confusion over the term "beneficiary" resulted in the immediate transfer of all his property to his children and required him to pay them an annual income, leaving his wife in the cold.

2. Failing to tie your business to your estate plan. If you own a business, include it in your estate plan. "Parents sometimes don't want to talk to their kids about it and just leave the business to the kids," says Steve Ciepiela, president and owner of Charles Stephen & Co., a financial planning firm in Albuquerque, N.M. "That's a huge mistake."

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A typical conundrum is how to provide equally for children who work in the family business and those who don't. Ciepiela had hounded a couple with five children to do estate planning that covered their business. But they stuck with simple wills and died within five months of each other. At a family meeting after the parents' deaths, three children not working in the business wanted to know how much income they'd begin getting from the business. The two brothers who worked in the business contended they had to sell it to pay estate taxes.

The business was shut down and sold at a huge discount. The two brothers opened a new, but less successful, business, recalls Ciepiela. All of that could have been avoided if the parents had bought life insurance to cover estate taxes or equalize the distribution to children who didn't work in the business.

Considering a lump-sum payout? Think again. >>

3. Leaving lump sums. If you have money to leave behind, be sure it makes a difference in your family members' lives by leaving it in a trust, rather than cash. Donald A. DeLong, an estate, business and tax-planning lawyer in Southfield, Mich., witnessed one case in which a father left $250,000 to his heroin-addicted son, who was penniless six months later.

"He did his own will," says DeLong. "He knew the problems his son had with drugs because his son lived with him. I think he just wasn't aware he had other options. A trust was probably his best option, because it's the best way to protect people from themselves."

With a trust, you transfer property to a trustee, who is bound by a trust agreement. The trust agreement stipulates how you want the property distributed. So rather than giving property outright to a beneficiary, the trustee holds your property and doles it out per your instructions. It's an added layer of protection.

The most common types of trusts — revocable living trusts and irrevocable trusts — can contain so-called spendthrift provisions. "A spendthrift provision prevents the beneficiary from getting advances against or trying to get a loan using his interest in the trust as collateral," says DeLong. "It also leaves the beneficiary's creditors in the cold because the beneficiary has no control over or access to the trust funds in the trust."

4. Neglecting to update your estate plan. Each time the law or your family changes, revisit your estate plan. The all-time record for an out-of-date estate plan may go to a couple who not long ago came to Everett Sussman, an estate-planning attorney in Stratford, Conn. "They said they'd done their wills when their kids were young — that was in September 1957," says Sussman. "Legally, those documents were valid, but they'd have been worth nothing at all. The couple no longer needed guardians for their children, who now have adult children of their own. Their assets were wildly different, and the executor they'd chosen had died many years earlier."

Changes can also require alterations in not-so-old estate plans. Sussman is in the process of "fixing" the estate of a woman who split her assets between her daughter and granddaughter. But when she died, her daughter was again pregnant. "The grandmother didn't update her will when she found out her daughter was going to have a second child because she probably thought her attorney drafted it properly to accommodate for later-born children," says Sussman. "I was brought in to overturn the estate so half would be split among the grandchildren. Had there been feuding children, we never would have accomplished this because the will was valid on its face."