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Capital Advice

Capital Financial Advisors of New York, LLC

Famous People Who Failed to Properly Plan

It's almost impossible to overstate the importance of estate planning, regardless of the size of your estate or the stage of life you're in. A close second to the need to plan your estate is getting it done correctly, based on your individual circumstances.

You might think that those who are rich and famous would be way ahead of the curve when it comes to planning their estates properly, considering the resources and lawyers presumably available to them. Yet, there are plenty of celebrities and people of note who died with inadequate (or nonexistent) estate plans.

No estate plan

It's hard to imagine why some famous people left this world with no estate plan. A case in point involves former entertainer-turned-congressman Salvatore Phillip "Sonny" Bono. He died in a skiing accident in 1998, leaving no will or estate plan of any kind. His surviving wife had to petition the probate court to be appointed her deceased husband's administrator, seek court permission to continue various business ventures in which Sonny was involved, and settle multiple claims against the estate (including one from Sonny's more famous prior spouse, Cher). To make matters worse, a claim against the estate was brought by a purported extramarital child, which necessitated a DNA test from Sonny's body to determine whether he'd fathered the claimant (he did not).

Do-it-yourself disaster

We've all seen the ads for do-your-own legal documents, including wills and trusts. And the law does not require that you hire an attorney to prepare your will. But even the highest ranking jurist of his time should have relied on estate planning experts to prepare his estate plan. Instead, U.S. Supreme Court Chief Justice Warren E. Burger, who died in 1995, apparently typed his own will (consisting of only 176 words), which contained several typographical errors. More importantly, he neglected to address several issues that a well-drafted will would typically include. His family paid over $450,000 in taxes and had to seek the probate court's permission to complete administrative tasks like selling real estate.

The importance of updating your estate plan

Sure, formulating and executing an estate plan is important, but it shouldn't be an "out-of-sight, out-of-mind" endeavor. It's equally important to periodically review your documents to be sure they're up-to-date. The problems that can arise by failing to review and update your estate plan are evidenced by the estate of actor Heath Ledger. Although Ledger had prepared a will years before his death, there were several changes in his life that transpired after the will had been written, not the least of which was his relationship with actress Michelle Williams and the birth of their daughter, Matilda Rose. His will left everything to his parents and sister, and failed to provide for his "significant other" and their daughter. Apparently his family eventually agreed to provide for Matilda Rose, but not without some family disharmony.

Let someone know where the documents are kept

An updated estate plan only works if the people responsible for carrying out your wishes know where to find these important documents. Olympic medalist Florence Griffith Joyner died at the young age of 38, but her husband claimed he couldn't locate her will, leading to a dispute between Mr. Joyner and Flo Jo's mother, who claimed the right to live in the Joyner house for the rest of her life.

The will of baseball star Ted Williams instructed his executor to cremate his body and sprinkle the ashes at sea. However, one of William's daughters produced a note, allegedly signed by Ted and two of his children, agreeing that their bodies would be cryogenically stored. Before the will could be filed with the probate court, the body was taken to a cryogenic company, where its head was severed and placed in a container.

It's Time to Review Your Life Insurance Needs

Regularly reviewing your life insurance can help it keep pace with your changing needs, and your financial and family obligations.

Your life insurance needs may change without you even realizing it. You may have purchased life insurance years ago, and never gave it a second thought. Or, you may not have life insurance at all--and now you need it. When your life circumstances change, you have a fresh opportunity to make sure the people you love are protected.

You're tying the knot

When you were single, you may not have thought much about life insurance. But now that you're getting married, someone else may be depending on your income. If one of you should die, the other spouse may need to rely on life insurance benefits to meet expenses and pay off debts.

The amount of life insurance coverage you need depends on your income, your debts and assets, your financial goals, and other personal factors. Even if you have some low-cost life insurance through work, this may not be enough. To be adequately protected, you may each need to buy life insurance policies from a private insurer. The cost of an individual policy will be based on your age and health, the amount of coverage you buy, the type of policy (e.g., cash value or term insurance), and other variables.

You've become a parent

When you become a parent, it's time to take another look at your life insurance needs because your family's financial security is at stake. Married, single, and stay-at-home parents all need life insurance. Life insurance proceeds can help your family meet both their current expenses (such as a mortgage, child care, or car payments) and future expenses (such as a child's college education). Even if you already have life insurance, it's time to review your policy limits and beneficiary designations.

You're contemplating divorce

During a divorce, you'll have a number of pressing financial issues to address. Make sure that one of these is life insurance. You'll want to think about what protection you need, and what protection your children (if any) will need in the future. For example, if you'll be paying or receiving child support, you may want to use life insurance to ensure continuation of those payments. During a divorce, you may also need to negotiate ownership of life insurance policies. Life insurance ownership and obligations may be addressed in your divorce settlement, and state laws vary, so ask your attorney for advice and information. Finally, you'll want to evaluate your own life insurance needs to make sure your family is protected in the event of your death.

Your children have left the nest

If having children was the reason you originally purchased life insurance, you may feel that you no longer need coverage once your children are living on their own. But this isn't necessarily the case. Before making any decision, take a look at the types and amounts of life insurance you have to make sure your spouse is protected (if you're married). And keep in mind that life insurance can still be an important tool to help you transfer wealth to the next generation--your children and any future grandchildren.

You're ready to retire

As you prepare to leave the workforce, you should revisit your need for life insurance. You may find that you can do without life insurance now if you've paid off all of your debts and achieved financial security.

But if you're like some retirees, your financial picture may not be so rosy. You may still be saddled with mortgage payments, tuition bills, and other obligations. You may also need protection if you haven't accumulated sufficient assets to provide for your family. Or maybe you're looking for a way to pay your estate tax bill or leave something to your family members or to charity. You may need to keep some of your life insurance in force or even buy a different type of coverage.

Your health has changed

If your health declines, how will it affect your life insurance? A common worry is that if your health changes, your life insurance coverage will end if your insurer finds out. But if you've been paying your premiums, changes to your health will not matter. In fact, you should take a closer look at your life insurance policy to find out if it offers any accelerated (living) benefits that you can access in the event of a serious or long-term illness.

It's also possible that you'll be able to buy additional life insurance if you need it, especially if you purchase group insurance through your employer during an open enrollment period. Purchasing an individual policy may be possible, but more difficult and more expensive.

Of course, it's also possible that your health has changed for the better. For example, perhaps you've stopped smoking or lost a significant amount of weight. If so, you may want to request a reevaluation of your life insurance premium--ask your insurer for more information.

The goal of a stretch IRA is to make sure your beneficiary can take distributions over the maximum period the RMD rules allow.

Stretch IRAs

The term "stretch IRA" has become a popular way to refer to an IRA (either traditional or Roth) with provisions that make it easier to "stretch out" the time period that funds can stay in your IRA after your death, even over several generations. It's not a special IRA, and there's nothing dramatic about this "stretch" language. Any IRA can include stretch provisions, but not all do.

Why is "stretching" important?

Any earnings in an IRA grow tax deferred. Over time, this tax-deferred growth can help you accumulate significant retirement funds. If you're able to support yourself in retirement without the need to tap into your IRA, you may want to continue this tax-deferred growth for as long as possible. In fact, you may want your heirs to benefit--to the greatest extent possible--from this tax-deferred growth as well.

But funds can't stay in your IRA forever. Required minimum distribution (RMD) rules will apply after your death (for traditional IRAs, minimum distributions are also required during your lifetime after age 70½).

The goal of a stretch IRA is to make sure your beneficiary can take distributions over the maximum period the RMD rules allow. You'll want to check your IRA custodial or trust agreement carefully to make sure that it contains the following important stretch provisions.

Key stretch provision #1

The RMD rules let your beneficiary take distributions from an inherited IRA over a fixed period of time, based on your beneficiary's life expectancy. For example, if your beneficiary is age 20 in the year following your death, he or she can take payments over 63 additional years (special rules apply to spousal beneficiaries).

As you can see, this rule can keep your IRA funds growing tax deferred for a very long time. But even though the RMD rules allow your beneficiary to "stretch out" payments over his or her life expectancy, your particular IRA may not. For example, your IRA might require your beneficiary to take a lump-sum payment, or receive payments within 5 years after your death. If stretching payments out over time is important to you, make sure your IRA contract lets your beneficiary take payments over his or her life expectancy.

Key stretch provision #2

What happens if your beneficiary elects to take distributions over his or her life expectancy but dies a few years later, with funds still in the inherited IRA? This is where the IRA language becomes crucial.

If, as is commonly the case, the IRA language doesn't address what happens when your beneficiary dies, then the IRA balance is typically paid to your beneficiary's estate.

However, IRA providers are increasingly allowing an original beneficiary to name a successor beneficiary. In this case, when your original beneficiary dies, the successor beneficiary "steps into the shoes" of your original beneficiary and can continue to take RMDs over the original beneficiary's remaining distribution schedule.

When reviewing your IRA language, it's important to understand that a successor beneficiary is not the same as a contingent beneficiary. Most IRA providers allow you to name a contingent beneficiary. Your contingent beneficiary becomes entitled to your IRA proceeds only if your original beneficiary dies before you.

Stretch even further ...

If you name your spouse as beneficiary, your IRA can stretch even further. This is because your spouse can elect to treat your IRA as his or her own, or to transfer the IRA assets to his or her own IRA. Your spouse then becomes the owner of your IRA, rather than a beneficiary. As owner, your spouse won't have to start taking distributions from your traditional IRA until he or she reaches age 70½ (and no lifetime RMDs are required from your Roth IRA). Plus, your spouse can name a new beneficiary to continue receiving payments after he or she dies.

What if your IRA doesn't stretch?

If your IRA doesn't contain the appropriate stretch provisions, don't fret--you can always transfer your funds to an IRA that contains the desired language. In addition, upon your death, your beneficiary can transfer the IRA funds (in your name) directly to another IRA that has the appropriate stretch language.

A word of caution

While you might appreciate the value of tax-deferred growth, your beneficiary might prefer instant gratification. If so, there's little to prevent your beneficiary from simply taking a lump-sum distribution upon inheriting the IRA, rather than "stretching out" distributions over his or her life expectancy. It's possible, though, to name a trust as the beneficiary of your IRA to establish some control over how distributions will be taken after your death.

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What rate of return should I expect from stocks?

That depends on many factors, including your time frame and the types of stocks involved. Many retirement planning calculators project a portfolio's future value based on historical returns. However, past performance is no guarantee of future results, and you should take any such assumptions with a grain of salt.

You may have heard that stocks have historically averaged a 10% return. However, be careful about relying too much on that number. First, the figure on which that statement is based--9.8%--reflects the compounded annual total return of the S&P 500 between 1926 and 2012. Is your time frame likely to be that long? Second, equities' performance in recent years hasn't been as robust. The last time the S&P's compounded annual 10-year total return was 9.8% or more was 2004; from 1999 to 2008 it was negative for the first time in decades, and from 2003 to 2012, it was 7.1%.*

Third, that 7.1% was the index's nominal return; it doesn't take into account inflation or taxes. As of April, the annual inflation rate was a little over 1%, according to the Bureau of Labor Statistics. That would cut that 7.1% to just over 6%. And a 1% inflation rate is very low; over the last 20 years, it has averaged roughly 2.4% a year, which would mean an inflation-adjusted return under 5%. That's less than half the often-quoted 10% average, not including any taxes owed.

What would that mean to a hypothetical $100,000 portfolio? Even if you managed to achieve a 9.8% nominal return compounded annually for 10 years, adjusting it for 2.4% inflation would mean a projected balance of almost $255,000 would actually be worth roughly $200,000 before taxes. That's a pretty substantial gap.

Returns for stocks other than the large caps of the S&P 500 can be different. Still, when planning for income or long-term goals, focusing on real returns could help keep your expectations realistic.

*Calculations based on total returns compounded annually through December 2012 on the S&P 500 Index, which is an unmanaged market-cap weighted index composed of the common stocks of 500 leading companies in leading U.S. industries. It is not available for direct investment.

What is a disclaimer of property?

A disclaimer is an estate planning tool that allows you to redistribute transfers of property free from transfer taxes. A disclaimer is your refusal to accept a gift, bequest, or other form of property transfer. Once disclaimed, the property is then distributed to the next recipient. As a disclaimant, you are not regarded as having received the property, or having transferred the property. As a result, no gift, estate, or generation-skipping transfer tax is imposed on your disclaimer of the property.

After you receive a gift or bequest, you generally have up to nine months to decide whether to disclaim the property. (State law can provide a shorter period.) During that period, you may not accept any of the benefits of the property if you ultimately decide to disclaim the property. When you disclaim the property, you may not direct who is to receive the property. The property passes as if you never held an interest in it. For example, you disclaim property left to you by your spouse, and it then passes to your children under the terms of your spouse's will.

The disclaimer must generally be in writing and be signed, and specifically identify the interest in the property being disclaimed. State law may impose other requirements, such as that the disclaimer may need to be acknowledged, witnessed, or recorded.

What are some reasons for disclaiming property?

- You already have enough property.
- You can shift income-producing property to someone in a lower income tax bracket. (However, unearned income of a child subject to the kiddie tax may be taxed at your income tax rate. The kiddie tax rules apply to (1) those under age 18, (2) those age 18 whose earned income doesn't exceed one-half of their support, and (3) those ages 19 to 23 who are full-time students and whose earned income doesn't exceed one-half of their support.)
- Disclaiming the property, or an interest in the property, may enable the property to qualify for a marital or charitable deduction.
- Disclaimers can be used to make changes to an estate plan at a later time.