Trust bust: Steer clear of the 8 biggest estate-planning mistakes

By Barry Glassman CNBC Online Wednesday, 22 Oct 2014

Let's be honest: Thinking about the inevitable—death—is not very pleasant. Perhaps that's why so many people fail to plan for the time when their time will be up. Even clients who make the effort to plan their estates often neglect to follow through or update their plans as changes occur in their lives.

Over the years, we've seen estate plans fail to do what they were intended to do. For your estate plan to remain a valuable asset for you and your heirs, you would be wise to avoid these eight common mistakes.

1. Thinking your state will handle everything. You might think that having a trust, such as a revocable trust, is just for the rich or that if you have a will, you've covered your bases. Well, consider this: A will may indicate who gets what upon your death, but your estate may have to go through a very public probate process, and probate can be very expensive.

If you have a revocable trust, it eliminates the probate process for the assets titled in the name of the trust, and it ensures that your privacy and the privacy of your heirs are protected.

2. Thinking your work is done after creating a trust. Establishing a trust and signing the document is just the first step, but many people forget to fund their revocable trust. Remember, the trust does not exist unless it holds assets. When you establish a revocable trust, you need to retitle your accounts in the name of the trust. Your financial planner or brokerage firm will help you do this.

As an additional measure, we recommend clients have a "pour over" will. Upon the grantor's death, it will collect and transfer all additional assets—such as jewelery and cars—into the revocable trust so that they will be dispersed according to your instructions and avoid probate.

3. Setting it and forgetting it. This faulty thinking applies to many situations in financial planning. In this case, it means that clients all too often set up their estate-planning documents and then rarely look at them again.

Keep in mind that these documents might specify who will be guardian to your children should something happen to you. Those sober, married guardians you originally named years ago may now be divorced, active alcoholics. The point is that life changes. Your needs, as well as the number of children you have now, may be different.

In the last few years, the estate-tax exclusion bounced around. It was $2 million, and then, for a period of time, it didn't even exist before settling at $5.34 million per person. With so many changes, people needed to look at their estate documents to make sure their trust still worked within that current framework.

Now that the estate tax exclusion is more stable—gradually increasing each year—it may fall off your radar. So plan to review your trust documents every few years or whenever your life, or the estate tax law, changes.

Thinking all your assets will follow your will or trust. Retirement accounts and insurance policies are governed by the beneficiary form you filled out when you opened the account or bought the policy. These assets do not flow through your trust or your will.

Whomever you designated on that form you signed so long ago is who will get that money should you die. It's a good idea to look at those beneficiary forms and revise them, especially if you have gone through a divorce or had more children. It's the easiest thing you can do, and it costs you nothing.

5. Relying on the "DIY" trust. Paying a few thousand dollars for a good drafting of your estate plans will ultimately save you much more money in the end. It's like paying for a good accountant. They will most likely save you enough money to be more than worthwhile in the end. Not convinced? Refer to mistake number 1 above for the potential costs of probate.

6. Giving too much too soon. Many parents who establish trusts when their children are 5 or 6 years old assume that by the time those kids are young adults, they will will be responsible enough to handle their inheritances.

But as said children get closer to 21 or 25, parents often realize that they could be giving their kids too much too soon. But with many trusts, that's already too late to make any changes.

I recommend that parents consider delaying larger portions of their children's inheritance, giving them more when they are older and allowing the trustee to have more discretion in distributing their money should they need it sooner.

7. Not considering the needs of your children. We all know how different each of our children can be, and there may be times when it's appropriate to treat each of them differently when it comes to disbursing their inheritance.

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One example: If you have a special needs child, he or she may require more help for a longer period of time. In this case, it's especially important to consult an estate-planning attorney because the rules are tricky. Assets owned by a disabled child could count against his or her supplemental Social Security Income (SSI) and Medicaid benefits.

8. Choosing the wrong trustee. Choosing your brother or sister as the trustee of your trust may sound like a good idea, and he or she might technically be the best person for the job. But you may be putting them in the uncomfortable position of playing bad cop, rather than loving aunt or uncle, to a difficult niece or nephew.

In this case, you may want to consider hiring a corporate trustee. It's easier for an impartial third party to be the heavy when your heirs come asking for money. This comes at a cost, but it may be worth it in the interest of preserving the family peace.

Good estate planning is an essential component to any good financial plan. By working with a reputable estate-planning attorney and making time to review and discuss your estate plan on a regular basis, your estate will pass to your heirs—hopefully with less drama but certainly as you intended.