Sudden impact: When a spouse unexpectedly dies

Do you know someone who suddenly became widowed when a beloved spouse unexpectedly passed away in the prime of life? You may have tried to console the widow or widower, but then resumed your normal daily activities. And the surviving spouse was left to pick up the pieces of his or her life, often, on their own.

But this isn't always "someone else's" problem. Don't think that it can't happen to you or a member of your immediate family. Would you be prepared to cope emotionally and financially? Could you afford to live the same lifestyle?

It's almost impossible to fully prepare beforehand for such a calamity, but it helps to keep your finances organized and communicate with your spouse about these matters. In addition, know that your trusted estate planning advisor can help you navigate through the minefield. You aren't alone, after all.

Key points to address

In the event a spouse passes away without warning, a surviving spouse will face several critical challenges, including some significant financial decisions. Of course, handling the funeral arrangements comes first.

The following are other key points that will need to be addressed:

Emotional responses. It's easy to say, and hard to do, but don't let your emotions rule your judgment. For instance, if you're tempted to immediately move out of your home, sell your spouse's business or invest a lump-sum life insurance payout, hold off. Take the time to sort out what will likely be best for you and your family in the long run.

Death certificates. One of the first things to do is visit the county clerk's offices to officially record the death. At this time, you can obtain death certificates which will be needed for dealings with financial institutions and others. The numbers will vary person-to-person, but you'll probably need at least a dozen.

Notifications. Along with the county offices, you must get the word out to other interested parties, including your spouse's employer; credit card companies; life insurance companies, retirement plan and IRA administrators; the Social Security Administration (SSA); the state motor vehicle agency; the state office for inheritance tax (when applicable); and your attorney and other professionals.

Social Security benefits. Obviously, if your spouse was receiving benefits, you should consult with the SSA as to the benefits available to a surviving spouse. Frequently, modifications are required if the survivor was the lower-earning spouse. Even if your spouse wasn't receiving benefits yet, you may be eligible for survivors' benefits, depending on your age and other factors.

Insurance. Don't assume that everything about your insurance plans will stay the same. Review your various insurance policies — such as life, health, disability income, auto and long-term care — to ensure that you'll have the optimal coverage going forward. Make whatever beneficiary changes are required.

Retirement plans and IRAs. Besides beneficiary designations comparable to insurance, you may face important decisions regarding employer retirement plans, like a 401(k) plan, and traditional and Roth IRAs. For example, if your spouse had a traditional IRA, you can complete a timely rollover to an IRA of your own without owing any tax. Conversely, you might opt for a lump-sum payout from a 401(k) or IRA should you need their funds.

Investments. Similarly, examine the investments that were owned solely by your spouse, as well as those you owned jointly. When you have time, sit down with your financial advisor to chart out a path for the future, focusing on changes in personal objectives, time horizon and risk assessments. Again, don't rush into any hasty decisions.

Other practical considerations

Is that the entire to-do list? Not by a long shot. For instance, other actions may be required if your spouse was the grantor or beneficiary of a trust or was a military veteran. Veterans are entitled special burial reimbursements. Also, you may have to address assets your spouse owned jointly with someone else, such as a sibling.

Once you're over the initial shock of the death, your overall focus should shift to organization and analysis. Account for all of your assets and figure out a long-term plan for paying regular monthly expenses and other obligations, such as college education for children. Finally, don't forget to factor in your needs in retirement.

SIDEBAR: What about tax filings?

Although federal estate tax returns are required only for the wealthiest individuals, you may choose to file a return to establish the value of inherited assets. Generally, the return is due within nine months of the date of the death. For example, if a spouse passed away on November 1, 2017, the return must be filed by July 1, 2018.

Also, you may face responsibilities for state estate taxes. Finally, you must file an income tax return on behalf of your spouse.

Keeping a vacation home "all in the family"

A vacation home typically is treasured by families and is often passed down from generation to generation. But there may be more to transferring the family vacation home than first meets the eye. If you plunge ahead without careful planning, it could disrupt harmony and lead to a "family feud." In some cases, relationships may even be severed forever.

Potential sources of conflict

Why would transferring a vacation home lead to conflict? The possible reasons are numerous and sundry and, of course, depend on whom you choose to name as your successors.

For starters, the home may elicit strong emotions, with precious memories for different family members. Due to this connection, someone who's logically excluded from ownership may still harbor resentment. Or, if the ownership is divided equally — say, one-third to each of three siblings — one party might feel they have a greater right to the property than the others.

In addition, adult children are often married with children of their own, which can complicates matters, especially if any of the siblings and the respective spouses don't get along. Existing sibling rivalries or other long-standing tensions may come into play.

Once ownership of the home is legally transferred to one or more of your kids, it can be subject to the claims of creditors. This may be troublesome when married adult children get divorced. It might even result in a situation where the divorced spouse of a sibling attempts to claim a portion of the home's ownership.

The costs of operating a vacation home can't be ignored either. Not even counting property taxes and mortgage interest (when applicable), some family members may be stretched thin by outlays for repairs, maintenance and insurance. If siblings have disparate incomes, arguments about what to spend money on can boil over.

Finally, assuming you divide ownership equally among adult children, your decision may not be embraced by everyone concerned. While some may want to keep the home, and preserve the traditions, others might want to sell it and use the proceeds for other purposes. Thus, the family is divided.

Communication is critical

Much of the potential discord can be avoided by talking things out before taking action. For example, you may learn that one child has no desire to continue using the home while another intends to keep it for themselves and their kids as long as they can. This might provide a practical solution that benefits everyone without causing financial hardships.

If possible, assemble all the children for a face-to-face get-together to hash out all the issues. Doing so may be more effective than making phone calls. Depending on the circumstances, spouses may — or may not — be invited. As a result of these talks, you might arrange a division of expenses or ownership that differs from the usual equal allocation.

In addition, you may discuss the possibility of renting the home to tenants, at least part of the time. This can be a lucrative source of income for your children while providing certain tax benefits. Conversely, if some members feel strongly about maintaining the home for personal use, this discussion could be tabled.

Other issues at stake

Before taking action, consider all the other legal and tax ramifications of transferring ownership of a vacation home. Although the most common method is to leave a home to children as tenants in common, this may not be the best approach if it causes discord. In that case, you may utilize a trust instead, thereby maximizing the available tax benefits under the prevailing laws. Contact your estate planning advisor for help addressing your vacation home in your estate plan.

Are your assets fully protected from creditors?

One of the primary objectives of estate planning is protecting your assets from unreasonable creditors' claims, frivolous lawsuits or financial predators. The reason being is you want to pass as much of your wealth to your family as possible.

Both offshore and domestic trusts can be highly effective vehicles for protecting wealth, but they can be complicated and expensive. The good news is there are basic, yet effective tools you can implement to protect your hard-earned wealth.

Basic asset protection strategies

Some of these strategies involve transferring assets to another person or entity, or changing the way property is titled.

Buying liability insurance. For many people, insurance is the first line of defense against liability claims that expose their assets to risk. It includes personal or homeowner's liability insurance, as well as professional liability insurance for doctors, lawyers and other professionals who are common targets for lawsuits.

Making lifetime gifts. The most effective asset protection strategy may also be the simplest: giving your assets away to your children or other loved ones. After all, a creditor can't come after assets you don't own. The disadvantage of this approach, of course, is that you must relinquish control over the assets. But if you're comfortable parting with assets during your lifetime, gifts are a great way to place them beyond the reach of your creditors.

Using tenancy by the entirety. Many states permit married couples to hold their home or other real estate as "tenants by the entirety." This form of ownership protects assets against claims by either spouse's separate creditors. So, for example, it can be effective when one spouse is exposed to professional liability risks. It doesn't, however, protect couples against claims by their joint creditors. Tenancy by the entirety, if available, is a good option for people who aren't comfortable transferring title to their spouses.

Including assets in retirement accounts. Qualified retirement plans — such as 401(k), 403(b), and 457 plans, as well as certain pension and profit-sharing plans — are excellent asset protection vehicles. IRAs offer more limited protection. Assets held in most qualified plans enjoy unlimited protection from creditors' claims — both in bankruptcy and outside of bankruptcy — under the Employee Retirement Income Security Act.

IRAs are exempt from creditors' claims in bankruptcy up to a specified threshold. This limit doesn't apply, however, to amounts rolled over from a qualified plan to an IRA or to future earnings on those amounts within the IRA.

Outside the bankruptcy context, the level of asset protection for IRAs varies depending on applicable state law.

Creating a family limited partnership (FLP) or family limited liability company (FLLC). Transferring assets to an FLP or FLLC can be an effective asset protection strategy, especially if you wish to retain control over a business or other assets. To take advantage of this strategy, you simply set up an FLP or FLLC, transfer assets to the entity, and either give or sell ownership interests to your children or other family members.

You can maintain control over the assets by retaining a small (for example, 1%) general partnership interest in an FLP or acting as manager of an FLLC. Limited partners in FLPs — as well as managers and members of FLLCs — aren't (except in very limited circumstances typically involving some personal wrongdoing) personally liable for the entity's debts. And their personal creditors cannot reach the entity's assets. Instead, these creditors are limited to obtaining rights to any distributions received by the limited partner or LLC member.

Beware of fraudulent transfer laws

Most states have fraudulent transfer laws, which prohibit you from transferring assets with the intent to hinder, delay or defraud any creditor, including a *probable* future creditor. Typically, these laws also prohibit "constructive fraud," which is when you transfer assets, without receiving reasonably equivalent value in exchange, and you're insolvent before or after the transfer.

To ensure that your asset protection efforts are successful, be sure that you're solvent before and after any transfer and that you transfer assets at a time when there are no actual or potential creditors' claims on the horizon.

First things first

Before considering your asset protection options, conduct a risk assessment to get a handle on your level of exposure. The results can help you determine which asset protection strategies to implement. Your advisor can help with the risk assessment.

You haven't transferred ownership of a life insurance policy to a trust

After recent tax legislation, including the Tax Cuts and Jobs Act (TCJA), very few tax shelters are left standing. One key exception is life insurance. If certain requirements are met, the buildup of value in a life insurance policy is exempt from current income tax, while proceeds payable upon death can avoid estate tax.

But there's a potential problem if you possess any "incidents of ownership" in the life insurance policy. In that case, the proceeds are included in your taxable estate. Yet there's a simple solution: transfer the policy to an irrevocable life insurance trust (ILIT).

Naturally, you forfeit the estate tax exemption if you own a policy outright, but the rule goes much further than that. Typically, it applies if you reserve certain policy rights, such as the right to change beneficiaries or borrow against the policy. Depending on the circumstances, if you retain incidents of ownership in a policy with a payoff in six figures, it could trigger estate tax when you die.

Fortunately, you can avoid this result by establishing an ILIT and transferring ownership of the policy, including all the other rights, to the trust. The transfer may be sheltered from gift tax by the $11.18 million gift and estate tax exemption under the TCJA. Designate someone you trust — such as a professional or family member — to act as the trustee. If you require additional life insurance coverage, arrange for the ILIT to acquire any new policies.

Remember that the life insurance trust must be “irrevocable” to qualify for the estate tax break. So you can’t change your mind once you make the commitment.