ESTATE PLANS

for When Your Kids Won't Do As Well As You

By Douglas G. Chalgian, CELA ©2014

By the time I meet with clients (usually in their 50s or 60s, if not older), they have a pretty good idea of how their children will make out: whether their marriages will be successful, whether they will have children, and what their prospects are for a sound financial future. All this is good to know when preparing an estate plan.

Lately I've been seeing a lot of clients who have done well financially themselves, but who can see that their children are never going to enjoy the same level of material success as they did. They love their children and grandchildren to death — but they worry about how they will fare financially in the future. Typically these clients have two main concerns:

- Providing a mechanism to assure that their children will have something to live on when those children are no longer able to work.
- Providing their grandchildren with the ability to get a college degree without being burdened with a large debt.

With respect to each of these concerns, there is more than one way to approach the issue, and there are special considerations with respect to each approach.

Providing Adult Children with a Replacement Retirement Plan

A couple realities of the new economy are: (1) People rarely stay with the same employer for an entire career, and (2) Employers don't provide lifetime pensions like they used to. In the "good old days," people worked 30 years in a job and retired with a pension that gave them an income for the rest of their life (along with health care coverage). Today, even if someone stays with the same employer for their entire career, very few jobs provide the same level of security.

Much more common today are the so-called "defined contribution" retirement plans, in which people put away some portion of their earnings while they are working, and those contributions go into the retirement fund tax-free. In most situations, the employee contributions are matched to some degree by the employer. This allows people to accumulate accounts that they can draw on in their retirement (at which time the withdrawals will be taxed as income), and to move from job to job and take their retirement accounts with them. However, outside of a small number of highly compensated occupations, the value of these defined contribution accounts will rarely ever grow to the point where they would match the value of a lifetime pension.

In addition, the cost of health care coverage is not met by these retirement plans, and fewer and fewer businesses offer continued health care coverage for retirees. Where they do, those plans almost always require contributions from the retiree. On top of that, the whole world of government health care benefits is changing, with the future of Medicare and Medicaid up in the air. When one considers that in the future there will only be more old people and fewer workers, with those workers earning less, reliance on government health care benefits is especially speculative.

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It is in this environment that my clients who have accumulated wealth appropriately worry about how their children will fare when they age.

One option we discuss is to leave funds in trust for children that can't be touched until those children reach retirement age themselves, and that then provides a stream of income to the child. The idea is that the children will have some income (hopefully Social Security benefits will still be around) and will have some money set aside in their own retirement plans that they can draw on, so that the money from the trust will simply supplement their income and/or pay for health care expenses. Parents who want to encourage their children to plan for retirement can even structure these trust provisions so that the children who save the most will get the most help. Alternately, parents can set it up so that all children are treated equally, or so that the children who have the least get the most.

Another option is to set aside a sum of money for children, but, rather than create a stream of income when they reach retirement age, give a trustee the authority to make distributions on an "as needed" basis. This approach provides flexibility to deal with the realities as they exist at the time, and avoids one troubling potential pitfall, which is that many government benefits are already "means tested"—that is, the more assets someone has, the less the government will pay for. It is possible (maybe probable) that means testing in government benefits will continue to expand. So it is possible that, in the future, providing a child with a predictable stream of income could result in them receiving fewer benefits from programs like Social Security and Medicare.

Another challenge in planning for your children's retirement is picking a trustee—the person or entity who would be in charge of the trust when the children reach the age that they can get distributions. The answer in most cases is appointing a "professional fiduciary" such as a bank. The downside is that those institutions are frequently bought and sold, and predicting which banks will be around in the future is difficult. In addition, banks charge fees on trust assets they hold and that fee will limit the rate at which the trust funds will grow.

Putting Grandkids Through College

Many clients consider a college education a minimum requirement for a "good life." They helped their children pay for college but they recognize that it may be difficult, if not impossible, for their children to provide the same level of support to the grandchildren. That, and the ever-increasing cost of higher education, makes it important for many people to set aside something in their own estate plans to encourage and support their grandchildren to obtain a college degree.

While there are many good plans created by the government to allow people to contribute money toward the college education of others, trusts are unique in that they can provide parameters about what the money can or can't be used for, what types of programs will be paid for, and even how well the student must do in order to obtain help. In addition, when someone dies, ownership of plans like 529 accounts must be passed to others who may or may not have the same objectives.

Trust agreements can again provide a flexible answer to college fund planning. As indicated above, grandparents who create college funds can specify all sorts of standards and requirements so that the money is used for educational expenses that the grandparents perceive as most beneficial. And again, picking a trustee becomes a critical issue, which is more true the more nuanced the terms of the trust.

Conclusion

Mature adults planning today face unique challenges in creating estate plans that are thoughtfully designed to help their children and grandchildren. Although there is nothing wrong with simply leaving money to children outright, in those families where the children are financially struggling, the result will predictably be that the money left will be dissipated on living expenses and debt. For people who have specific objectives, such as helping their children realize a dignified retirement, or making sure their grandchildren are able to get a quality college education without the burden of overwhelming debt, more thought is required, but well-conceived estate plans can provide an answer.

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