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Importance of Proper Asset Ownership and Beneficiary Designations

By Richard M. Morgan & Loraine M. DiSalvo

This installment of the Passionate Estate Planner is a reminder that a well done estate plan includes not only properly prepared legal documents, but also the need to properly own your assets and have proper beneficiary designations.

It is of key importance that assets are owned and beneficiary designations are handled properly now and periodically reviewed thereafter in light of your changing circumstances and changes in the law. The failure to take these steps can lead to (1) the wrong party initially or ultimately receiving your assets after your death (such as a prior spouse, one of multiple children, or your step children over your natural children or worse), (2) the loss of various tax and asset protection benefits (by not being able to take advantage of the benefits from any trusts built into your estate planning documents), (3) the loss of income tax deferral benefits from an inappropriate beneficiary designation on your IRA and qualified plan accounts, and (4) the loss of assets to creditors over your intended beneficiaries where your economic circumstances have taken a turn for the worse.

Why discuss this ever present topic now? A “hot off the presses” Florida District Court of Appeals Court decision was a wake up call to those who do not think it really matters. In this case, <u>The Estate of Carlton W. Morey, Jr. v Everbank, et al.</u>, Case 1D11-1401 (FLA 1st DCA 2012), Mr. Morey had been a successful businessman and real estate investor with a multi-million dollar net worth when he did his estate planning. His intent was to have his wealth at his death pass to a trust for his daughter’s benefit. He did a good job in his planning and even purchased $250,000 in life insurance (“LI”) to help provide some needed liquidity (cash) upon his death since his wealth was fairly illiquid. As a Florida resident, he did what most people do in Florida, he used a Revocable Living Trust (“RLT”) as his primary estate planning vehicle, and he transferred most of his assets to the RLT while he was living to avoid Florida probate. He likewise designated his RLT as the beneficiary of his LI to provide the RLT Trustee with needed liquid funds. So far so good.

Well, guess what happened? The economy crashed and the value of his businesses and real estate investments plummeted. Under the very debtor friendly Florida state laws, life insurance proceeds are exempted from the claims of creditors *unless*, it was thought, you went out of your way to waive this exclusion by having the LI proceeds payable to your estate or directly to a creditor. Well, the Florida courts have now said that it is easy to waive this exclusion. While the LI proceeds would normally be exempt from the claims of creditors, the paying of those proceeds to the RLT in general, and not directly to the child or to the sub-trust for the child’s benefit, waived the exclusion because of the general standard language in the RLT to pay the due and owing debts of the estate. The effect of the Court’s ruling in this case was to provide that no assets passed to the trust for the child’s benefit since the estate/RLT had more debt than assets upon Mr. Morey’s death.

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Based on this Court case, what should Mr. Morey have done when his circumstances changed so significantly for the worse? One simple option would have been to change his beneficiary designation on the LI policy to the sub-trust for his daughter under the RLT. Later, if and when his circumstances significantly improved, he could have changed the beneficiary designation back to his RLT.

What does this Court's holding mean to everyone else, living in Florida or not? As to the designation of a beneficiary of a life insurance policy in GA, this case should be taken very seriously since GA also protects life insurance proceeds in a similar manner to Florida, at least outside bankruptcy. While it may make perfect sense to name your estate or RLT as the beneficiary of a life insurance policy that you do not want to be owned by an irrevocable life insurance trust ("ILIT" or "Family Gifting Trust") in order to have the proceeds available to provide needed liquidity and/or to otherwise fund your estate plan, this may not make so much sense if your financial circumstances change significantly for the worse. In other words, and not just as to insurance, you need to revisit your asset ownership decisions and beneficiary designations periodically to make sure they still make the most sense in your particular situation at the time. Your failure to do this could mean a significant difference to your loved ones after you are gone.

When deciding how to own your assets and as to the most appropriate beneficiary designation, you should consider the following factors:

1. Funding the plan set out in your estate planning documents;
2. Providing needed liquidity to enable the plan to be carried out more smoothly;
3. Tax benefits;
4. Asset protection benefits; and
5. Risk of a future divorce (separate vs. marital asset classification).

These decisions are not always easy to make since different factors may provide you with different answers, but the key is to consciously consider the factors and decide what is right for you in your given situation.

We at Morgan & DiSalvo have years of experience helping our clients evaluate these issues. To request further information or to schedule a meeting with us to review your current fiduciary choices and consider any necessary or desirable changes, we invite you to call (678) 720-0750 or email sollila@morgandisalvo.com.