

Does Your Estate Plan Account For Your Blended Family?

Estate planning for blended families -- where one or both spouses have children from previous marriages -- can be more complex than planning for “original” families. Your blended family must deal not only with the inevitability of death and taxes, but also with potential conflicts among your current spouse, ex-spouse, any children from your previous and your current marriages, and any stepchildren.

As a parent in a blended family, your challenge is to divide your assets among your heirs according to your wishes -- not according to the directives of a probate court -- while minimizing both estate tax and animosity among family members.

Asset Distribution Issues

If you die without a will or a living trust, a probate court will divide your assets among your current spouse and your biological and adopted children. In most states the division is 50/50, but in some your spouse’s share may be as high as 60%. The probate court splits your children’s portion equally among them, regardless of how many children are in your blended family. Issues regarding separate property that you brought into the marriage and community property can further complicate this division.

Your wishes will probably vary from this state-dictated distribution. For example:

You may want some children to inherit more than others.

If your new spouse has a substantial estate of his or her own, you may wish to leave more of your estate to your children from a previous marriage -- especially if they are minors.

If your new spouse doesn’t have substantial assets, you may wish to leave a portion of your estate to him or her.

If your children from a previous marriage are grown and successful and you have young children with your current spouse, you may wish to leave more to your current spouse. You may even consider disinheriting children from your previous marriage and leaving everything to your current spouse.

If your new spouse has children from a previous marriage, you may wish to leave them an inheritance too. (Unless you legally adopt your new spouse’s children, the probate court will not treat them as your children for estate-distribution purposes.)

Estate Tax Issues

The marital deduction is a useful estateplanning tool that allows any assets to pass estate tax free to your current spouse when you die. Everything that goes to your children on your death will be subject to estate tax (or at least use up some of your gift and estate tax exemption -- currently \$675,000).

Yet if you leave everything to your current spouse to maximize the benefits of the marital deduction, children from a previous marriage could end up with nothing. That is why you should consider a qualifying terminable interest property (QTIP) trust.

The QTIP trust allows you to provide your spouse with income from the trust for the remainder of his or her lifetime. Structure your will or living trust so that some portion or all of your assets pass into the QTIP trust. This trust can provide your spouse with as much or as little access to the trust principal as you choose. Then upon your spouse's death, your will or living trust can direct the remaining QTIP trust assets to pass to your children from a previous marriage. When your spouse dies, the entire value of the QTIP trust may be subject to estate tax.

Leave Explicit Instructions

Rather than leave your estate distribution decisions to a probate court, state explicitly in your will or living trust to whom you want to leave your probate assets. (Non-probate assets -- life insurance, joint tenancy property, and 401(k) plan and IRA benefits -- aren't included in your will or living trust because you have already designated beneficiaries for these assets.)

In addition, set up trusts to hold assets for your minor children and others to whom you don't want to leave a lump-sum inheritance. For example, you might not want your 22-year-old child to inherit \$1 million in one lump sum. You may prefer to have a third-party trustee administer and distribute the assets for that child's benefit until he or she reaches age 25 or 30.

Minimize Animosity

Your estate plan for your blended family should ensure an orderly, equitable and compassionate distribution of estate assets among your heirs with minimal animosity between them. The first step is to discuss your objectives with family members and professional advisers. The second step is creating an estate plan that addresses your concerns and accomplishes your goals.

The Ex-Factor

Dealing with an ex-spouse in your estate plan can be a delicate matter, especially if you've had children with him or her. Without smart estate planning, your ex-spouse could possibly control money you leave to your minor children because he or she would become their sole legal guardian after your death. If this is not desirable, set up a trust for the children's benefit and appoint a third-party trustee.

After your death, the trustee will distribute the trust funds to your ex-spouse (or directly to third parties for your children's benefit) according to your explicit instructions. The trustee has a legal obligation to make sure your ex-spouse uses any funds distributed to him or her only in your children's interest. Theoretically, if your ex-spouse misappropriates the trust funds, the trustee can ask a court to appoint a new guardian for your children, although that may not always be in your children's best interest.