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LIQUIDITY AS AN ESTATE PLANNING ISSUE

Most of us need a certain amount of money to pay our everyday bills. People who are in the workforce usually rely on their paychecks, and try to keep a little extra on hand for emergencies. Financial professionals refer to the “extra” amounts on hand, such as savings or investments that can readily be turned into cash as “liquid” investments. Retirees generally rely on their investments to earn interest and dividends for their income, and also have assets that they might liquidate in an emergency.

But what happens when you die? Does the need for liquid assets remain? It certainly does.

For those of us that are married, liquidity is needed for our surviving spouse. Liquidity might also be necessary for others that rely on you for support – such as children, grandchildren or in some cases, one’s parents.

Perhaps you own a family business that might find itself in a cash crunch if you should become incapacitated or die. The business may need liquidity to keep employees around and not look for other employment, or to pay for a replacement key employee.

Liquidity is necessary for those that are highly leveraged and have large loans, such as mortgages, car payments, or other investment loans. In these instances it is very important to have liquid assets available to keep up with the obligations under the notes, so loved ones aren’t burdened with major decisions as to what assets might need to be sold to keep the notes afloat.

If you have an estate that is taxable, hopefully you have enough liquid assets to pay any estate or inheritance taxes that might be due.

If you have a large retirement account, your estate may also need liquidity so that the retirement account balances don’t have to be withdrawn earlier than what otherwise may be necessary.

If retirement account amounts are necessary to pay funeral expenses or estate taxes, for example, extra amounts have to be withdrawn just to cover the income taxes imposed on the retirement account withdrawal. It can become a vicious circle.

Investors in real estate should beware of liquidity problems. I once had a client who was heavily invested in real estate. When he died, the estate was forced to sell many parcels just to pay estate taxes and other administrative expenses. Problem was, real estate takes a while to market, contract and close. You don’t want your loved ones to be in a position where they have to “fire sale” assets in these situations.

One answer to liquidity problems is to purchase a life insurance policy within an irrevocable life insurance trust. The life insurance trust beneficiaries should mirror those in your other documents, so that the money paid on the insurance claim can be used for those taxes and expenses that would normally have to be borne by the estate and its beneficiaries.

I don’t have the space in this column to review other solutions available for those that feel they may have a liquidity problem. This is an issue that is not often addressed. If you believe that you might have a liquidity issue in your estate, ask your attorney and financial advisor what steps are right for you.

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