The Wise Inheritor: A Guide to Managing, Investing and Enjoying Your Inheritance

Ann Perry
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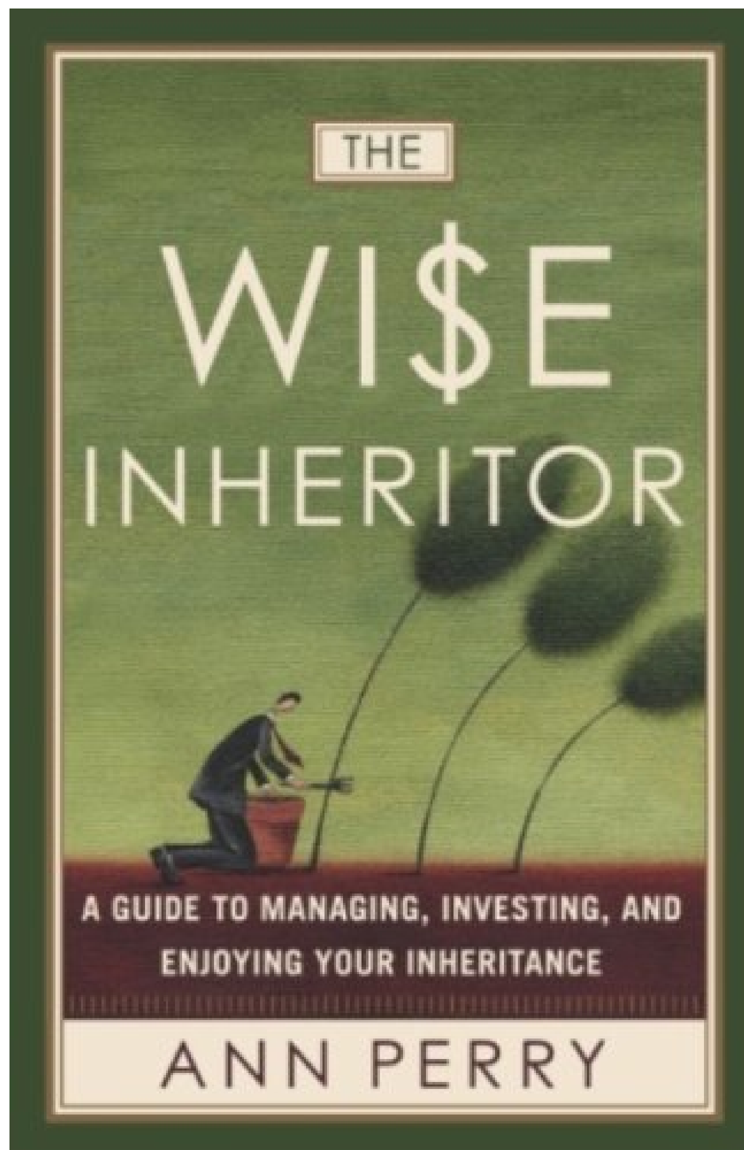

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The complete guide for managing the financial, legal, and emotional issues of inheritances large and small. A death in the family is never easy, but receiving an inheritance, whether expected or not, can leave heirs feeling overwhelmed and even guilty at this change in their fortunes. Ann Perryrsquo;s insightful examination of the challenges make managing a bequest a little easier. Combining her practical know-how as a personal finance writer, the expertise of financial advisors, attorneys, and psychologists, and the wisdom gained from her personal inheritance experience, Perry deftly deals with such touchy subjects as selling the family homestead, divvying up property in ldquo;blended families,rdquo; parceling out heirlooms, dividing a family business, and sharingmdash;or not sharingmdash;an inheritance with a spouse.With refreshing candor, Perry addresses the guilt, grief, and unrealistic fantasies that can keep heirs from making the most of their windfalls, and also explores the unique, even life-changing, opportunities that a bequest can present. An excellent tool for estate planning, as well, this is essential reading for those who are writing their wills as well as those who are remembered in one.From the Trade Paperback edition.

From the Inside FlapThe complete guide for managing the financial, legal, and emotional issues of inheritances large and small. A death in the family is never easy, but receiving an inheritance, whether expected or not, can leave heirs feeling overwhelmed and even guilty at this change in their fortunes. Ann Perry's insightful examination of the challenges make managing a bequest a little easier. Combining her practical know-how as a personal finance writer, the expertise of financial advisors, attorneys, and psychologists, and the wisdom gained from her personal inheritance experience, Perry deftly deals with such touchy subjects as selling the family homestead, divvying up property in "blended families," parceling out heirlooms, dividing a family business, and sharing--or not sharing--an inheritance with a spouse. With refreshing candor, Perry addresses the guilt, grief, and unrealistic fantasies that can keep heirs from making the most of their windfalls, and also explores the unique, even life-changing, opportunities that a bequest can present. An excellent tool for estate planning, as well, this is essential reading for those who are writing their wills as well as those who are remembered in one.About the AuthorAnn Perry writes a weekly personal financial column for the San Diego Union-Tribune that is syndicated by Copley News Service. She has also written an Internet shopping column for Knight-Ridder newspapers and contributed to many other financial publications.She lives in Encinitas, California, where she can be reached at www.moneyperry@aol.com. Her grandmother popularized the first widely marketed Go Fish card game, helping lay the foundation for Perryrsquo;s own inheritance.Excerpt. copy; Reprinted by permission. All rights reserved.Chapter 1The Great Wealth TransferMoney is always there, pockets change.--Gertrude SteinHow quickly the time went. We've gone from the Pepsi to the Probate Generation. Remember those television ads inviting us to join a carefree group of beautiful young people romping on the beach? Now we 76 million baby boomers are middle-aged and laden with responsibilities--jobs, mortgages, children, and aging parents. But we are still sought out by advertisers. They know we're coming into a lot of money, the largest transfer of wealth the world has ever seen.Our "great expectations" were first quantified by two Cornell University researchers in 1993. Robert Avery and Michael Rendall estimated that the baby boomers would receive at least $10.4 trillion in inheritances from their parents between 1990 and 2040. This would account for 115 million bequests, according to the study, starting with 900,000 in 1990, rising to 2.8 million in 2005, peaking at 3.4 million in 2015, and then dropping off gradually until 2040. The annual amount of the bequests would start at $40 billion the first year, grow to $217 billion in 2005 and peak at $336 billion in 2015, before winding down in the other direction.1As vast as these numbers are, they will likely turn out to be much larger. The prediction was made using 1989 dollars. Inflation, plus the tremendous run-up in the prices of homes and stocks in the 1990s, could double or even triple the size of the bequests.A more recent study released in 1999 from Boston College that covers a longer period, includes a larger population, and takes into account the prosperity surge of the 1990s, forecasts a transfer between 1998 and 2055 of at least $41 trillion and as much as $136 trillion. This study by John Havens and Paul Schervish also includes the wealth passed from the boomers to their children.2Any way you slice it, this intergenerational transfer of wealth is unprecedented. But what does it mean for our economy? And for the millions of inheritors?It's helpful to think of this movement of assets not like an avalanche of wealth, but more like the slow and inexorable movement of a glacier. In any given year, says Avery, the money left through inheritance nationwide is not enough to fundamentally alter the economy or impact a recession. But for an individual, an inheritance can be life changing. Avery estimates that an inheritance managed wisely can boost an individual's wealth by 25 percent or more."There are a lot of people in the world counting on this money," says Olivia Mellan, a Washington, D.C., psychologist who specializes in money issues. These people view inheritance as freeing or transforming. Prospective inheritors shouldn't put their lives on

hold while awaiting their bequests, however. While it's possible to make an educated guess about how much money an entire generation might bequeath, it is much more difficult to predict one family at a time. Members of the older generation, though they hold more than half the nation's wealth, are living longer and therefore spending more money than previous generations.As families are discovering, the cost of medical care during the last few months of a loved one's life can easily consume an inheritance of several hundred thousand dollars. One woman who helped care for her late father recalls, "We were running through his money like water. Six more months and he would have been bankrupt." Instead, she says, "There will be a nice hunk of money to invest in my son's college fund. I never really expected that."The Bequest BreakdownSome baby boomers will get their inheritance in dribs and drabs, or not at all. In fact, many Americans will be left out of this transfer. A full one-third of all assets bequeathed, or $3.5 trillion, will go to the ultrarich, the top 1 percent of the nation's families, according to Avery and Rendall. A second third is destined for the top 10 percent of affluent Americans, and the remaining third will be parceled out among the other 90 percent of the population. Those who do receive an inheritance will get $90,000 on average (in 1989 dollars).Clearly, the baby boomers are the beneficiaries of their parents' frugality. Reared in the Depression, tested by World War II, this "greatest generation" is also one of the greatest and most successful generation of savers. Even in their retirement years, many find it difficult to spend the money they have. "A lot of people who grew up in the Depression never planned to be wealthy and they don't think of what they have as wealth, even if it's $5 million," says Richard J. Muscio, a CPA and estate planner.Their children, however, grew up with a different attitude toward money, forged during the sixties and seventies, when inflation was often a formidable force. Borrowing, rather than saving, was the way to accumulate assets. Because of inflation, the money you borrowed would cost you less in real dollars in future years, so it made sense to leverage the purchase of a home or business. Baby boomers also got hooked on consumer credit, however. While their parents are inclined to live below their means, baby boomers have no compunction about living beyond it.So how will these new inheritors manage their windfalls? Economist Avery believes they will follow familiar patterns and simply consume them, rather than invest for the future. Although many heirs will be at least middle class if not affluent, they are not financially secure. As part of the "Sandwich Generation," balancing the needs of the generations before and after them, they face a financial triple-whammy, struggling to finance their children's education and to care for elderly parents while simultaneously trying to save for their own retirement. All too often, their own retirement savings are put off.The Insecure InheritorBut this is a risky approach, according to a 1997 research report by Phoenix Duff Phelps entitled "The American Dream Reconsidered: The Hopes, Fears and Dreams of the American Affluent in the 1990s." The report says that while the affluent (those with income greater than $100,000 and net worth of more than $660,000) are at the top of their professions, their future prospects are uncertain. "Their work environment is haunted by downsizing, reengineering and phase-outs." They lack the job and retirement security their parents enjoyed.3Many inheritors will be members of this growing affluent class, which has been called variously the upper middle class, the over-class, and the ultra middle class. But it would be wrong to think of them as heirs in the traditional sense, like a Rockefeller or a Kennedy. The affluent Americans interviewed for the report expected to receive on average an inheritance of $210,000, and one third of the group thought theirs would be less than $100,000."They are not the rich," states the Phoenix report. "The affluent depend on their jobs and careers to maintain their standard of living. Neither are the affluent the freewheelers and big spenders many think them to be; instead, they are hard-working families with traditional values." The message is clear: If they want to preserve their dreams for themselves and their children, they must continue to work hard--and to shepherd their inheritances wisely and well.For even if they manage to keep their trigenerational families afloat financially, boomers could face a demographic backwash set off by their sheer numbers. The 76 million Americans born between 1946 and 1964 have strained every system they've encountered: sending school enrollments soaring in the 1950s and 1960s and prompting new school construction, flooding the job market in the 1970s and slowing wage growth, buying homes in the 1970s and contributing to soaring real estate prices, and, most recently, purchasing stocks through 401(k)s, thereby fueling the great bull market of the late 1990s.So what happens when boomers go to cash out their investments to pay for their retirements? A study by Stanford University economist John Shoven and Wyatt Corp. economist Sylvester Schieber suggests that the massive sell-off of pension and retirement funds as baby boomers retire could depress investment values. "It doesn't seem too much of a stretch," says Shoven, "to think that something like the housing price run-up of the 1970s will be played out in reverse in the second and third decades of the twenty-first century, although this time the assets affected could be stocks, long-term bonds, houses and perhaps even gold."Of course, no one can predict what will happen that far in the future. The authors say it's possible that boomers could offload their stocks to investors from developing countries like China and India as they enter our financial markets. But Shoven and Schieber warn not to expect a bailout. Instead, they say, the Big Chill generation can best keep themselves warm in retirement by saving and saving still more, while continuing to work past age sixty-five.THE GREAT WEALTH transfer will accelerate the creation of a socioeconomic class I've dubbed the McMillionaires. During the 1990s, the number of households with net worth of more than $1 million more than doubled, from 2.6 million to more than 7 million, with the potential to grow to 20 million by 2010. The arrival of an inheritance of several hundred thousand dollars will help tip many affluent families over the $1 million net-worth mark.McMillionaires, so common there will seem to be one on every

corner, will by their very numbers devalue the idea of millionaire as economically independent. Indeed, this group will be prosperous but not truly wealthy, because they must work to maintain their lifestyles. And they will differ from "the millionaire next door" described in the best-selling book of the same name as an industrious male business owner and a stay-at-home wife who live below their means. The McMillies, by contrast, are dual-income hard-charging families living at or above their means, struggling to juggle their need to fund their retirement with the requirements of their children and aging parents.How will Americans spend their inheritances? This is hard to say. But a 1998 survey undertaken for the financial products firm Lutheran Brotherhood offers a guide. Asked how they would spend a sizable windfall, the most popular choices were either a home (31 percent of those surveyed) or an education (30 percent). Ten percent chose a vacation, 9 percent picked a car, and 3 percent elected to help children or family members. Only 2 percent would pay off debt and a mere 1 percent would invest it. "People don't seem to have lavish dreams about what they would do right away with a larger inheritance or lottery prize," concluded a Lutheran Brotherhood spokesman. "Instead, Americans would just want a home to live in and an education to secure their futures."4As they sell off their parents' homes and other assets, heirs will be left with cash to invest. It's likely that they will invest somewhat differently from their parents, due to the difference in age and generational temperament. For example, forty-five-year-old parents wanting to invest for their children's education will probably consider stock and bond mutual funds rather than the bank certificates of deposit on which so many seniors rely. The movement of funds from low-yielding deposits at bank institutions to higher-yielding investments in the general market is known as "disintermediation," a trend that investment management companies are awaiting with eagerness."A lot of the investment community is excited about this transfer of wealth," says Avery. That's because boomers are more likely than their parents to seek financial advice. So major institutions have surveyed these prospective inheritors, tailored ads to suit them, and offered to demystify the world of estates and planning. For example, Fidelity Investments, the nation's largest mutual fund company, created something it called Fidelity Legacy Services noting that "decisions customers make may affect more than one generation." Among the services the company offered were online educational materials and an estate planning calculator at its web site.Inheritance AmbivalenceAmericans have a love-hate relationship with inheritance. On the one hand, most of us would like to receive a bequest from our parents someday, just as property has been handed down from one generation to another for centuries. On the other hand, our nation is built upon the notion of individual opportunity, so that getting ahead, we like to believe, is based on merit and not on who your parents are and how much money they left you. Each year these two kinds of wealth seem to duke it out on the Forbes 400 list of wealthiest Americans. Vying for the top spot in recent years have been two self-made billionaires, Microsoft founder Bill Gates and renowned investor Warren Buffett. But at least seven of the top twenty spots are usually held down by heirs of those who created great fortunes, the Walton family of the Wal-Mart empire and the Mars family of the Mars candy dynasty.As poet Ogden Nash so deftly put it: "Some people's money is merited/And other people's is inherited."This ambivalence about inheritance runs through our history, starting with the founding fathers, according to Robert K. Miller, Jr., and Stephen J. McNamee, editors of the book Inheritance of Wealth in America. American leaders have long struggled to decide whether an inheritance is a natural right with which government shouldn't interfere or whether it should be subject to regulation, even to the point of reallocating the wealth of a person no longer living.Thomas Jefferson and other revolutionaries argued for redistribution, fearing that letting the dead control property was a danger to the new nation, which they reasoned, belonged to the living. It's not surprising that the founding fathers would have harsh views on inheritance, given that they had defeated a monarchy whose wealth and power were passed from generation to generation regardless of merit.A Taxing DebateEventually, inheritance rights in the new nation were subject to the power and taxation of government. But the merit versus inherit debate has never gone away. In the late 1800s, as the industrial revolution widened the gap between rich and poor, wealthy industrialist Andrew Carnegie joined with populists in an unsuccessful movement to curtail the power of rich family dynasties to pass wealth to future generations. A similar movement in 2001, led by billionaire investor Warren Buffett and the father of Bill Gates, tried unsuccessfully to preserve the estate tax as a means of encouraging meritocracy. Instead, Congress passed legislation that would phase out estate taxes in 2010 (only to have them reinstated in 2011 if no new legislation passes). See Chapter 13 for more on estate planning.Despite the philosophical debates about inheritance, federal estate taxes have been imposed over the years for strictly practical reasons--to raise cash for war efforts. They were first levied in 1797 in the undeclared naval war with France. The tax was repealed, then adopted, several times more to create a war chest. It was revived in 1916, during World War I, and has remained in effect ever since. It's probably no coincidence that in the decade before Congress agreed to reduce and eventually repeal the estate tax in 2010, the United States had not been involved in any long-term wars for twenty-five years--and that elected officials themselves stood to benefit from the great wealth transfer. If the war against terrorism proves both lengthy and costly, it is likely the estate tax will not be repealed after all.