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Market View/Special Topics

Six Major Mistakes to Avoid After Receiving an Inheritance

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A substantial inheritance can have a life changing financial impact: if handled wisely, the elusive goals of financial security and a comfortable future retirement may become attainable. But sudden wealth can sometimes be overwhelming and, if not guarded carefully, can easily be eroded or destroyed. Avoiding the following common mistakes is key to your future financial wellbeing after receiving a substantial inheritance.

1) Making rapid decisions before developing a well thought-out plan.

Some inheritors react by splurging on themselves, their immediate family and sometimes on their friends. Buying new cars, taking an expensive vacation, buying a new house, even quitting a job may be the immediate reaction of some to a substantial inheritance. Others may make a series of isolated financial decisions without considering all of the possible implications. A well thought-out plan including the right legal, tax and investment advice can provide rewards in both the short term and long term. An effective plan might include paying off loans, creating a rainy day fund, funding retirement accounts, funding college saving plans, and creating or reviewing your estate plan.

2) Forgetting about future generations.

Families that successfully pass wealth down for multiple generations view their financial inheritance as a gift that should eventually be left to the next generation. Such inheritors focus less on the value of the assets received and more on a sustainable amount to draw from those assets. This approach is more likely to ensure the gift you receive will keep giving—to you as the power of compounding works its magic, and to the following generations.

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3) Broadcasting the good news far and wide.

Sharing the news of an inheritance may seem harmless but information in the wrong hands can be dangerous. Friends and acquaintances may suddenly look to you for financial help. Others may approach you with investment "opportunities." Some scam artists target recent inheritors. Maintaining the confidentiality of your personal finances is the best approach, both before and after an inheritance.

4) Ignoring the potential tax pitfalls of inherited IRA and retirement plan assets.

The Internal Revenue Service requires beneficiaries of inherited IRAs, 401(k) Plans, Profit Sharing Plans and other retirement plans to withdraw a portion of the assets each year. In most cases the rules apply to young and old beneficiaries alike. Withdrawing less than the required amount can result in substantial penalties.

5) Failing to consider the future costs associated with inherited real estate.

Inheriting a vacation home or other significant property may initially seem like a dream come true but failing to factor in the potentially high cost of real estate taxes, insurance and upkeep can sink your household budget. Valuable artwork and antiques can also have high insurance costs. Failing to plan for the on-going costs related to inherited property, or property bought with a cash inheritance, may significantly strain your budget.

6) Deciding to go it alone without finding the right advisors.

Thoughtfully handling a substantial inheritance typically involves the assistance of experienced experts. The right legal, tax and investment advice can help you establish and attain both short and long term goals. An estate planning attorney will create the right long-term estate plan. A qualified tax accountant will have various strategies to help minimize income taxes. The right investment professional will construct and maintain investment portfolios that match your particular risk profile and attempt to maximize risk-adjusted investment returns.

Individuals seldom receive more than one significant inheritance. A properly handled inheritance may help provide financial security to you and future generations that would otherwise be unattainable. Avoiding significant spending and planning mistakes by seeking the help of experienced professionals is key to maximizing the long term benefit of an inheritance.

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