The DAILY PLAN-IT™

Volume 21, Issue 4

What happens to a client's debt upon death?

Most of your clients will die with at least some debt to their names. The average total balance of debt for U.S. consumers in 2016 was $61,554, according to credit bureau *Experian*.

But what happens to a client's debt when he dies?

Debt incurred by your client basically belongs to him or to his estate. When a client dies with enough assets to cover his debts, then his creditors will be paid, and his beneficiaries will receive what's left over.

When there isn't enough in the estate to satisfy a deceased client's debts, then his creditors may get some, but not all, of what they're owed. Family members generally don't become legally responsible for a deceased loved one's debt, but many worry they might.

Complicating Factors

There can be complex factors, though, depending on the type of debt your client incurred, where your client lives, and the value of his estate.

- Federal student loan debt is eligible for cancellation upon death, but private student loan companies typically won't offer the same benefit and may go after a deceased borrower's estate for repayment.
- Some states have homestead exemptions for a surviving spouse and lineal descendants. Absent a homestead exemption it may become necessary to liquidate the homestead to satisfy debts and claims of the estate.
- Debts incurred by your client with co-signers or co-applicants can also result in those debts falling back onto someone else's lap.
- If your client is married and lives in a community property state, then he might be responsible for debt his spouse incurred during the marriage, even if it was only in the spouse's name.

How to Protect Beneficiaries

Here's the core message we share with clients: Estate planning is not just about you or what you want to have happen when you die - it's also about protecting those you leave behind.

Advisors should encourage their clients to meet with an experienced estate planning attorney to, at the very least, prepare a will, medical powers of attorney, financial powers of attorney, and an advanced medical directive (living will). In many cases, we also recommend that a revocable trust be created to receive the estate's assets in order to add further protections.

Of course, life insurance is a great way to provide additional money in a client's estate to pay off debts. We encourage all clients to consider getting life insurance to ensure everything - including all of their debts - will be covered upon death.

But there's a lot more that your clients can do to reduce the debt they leave behind when they pass away. They can live below their means and minimize any new debts they take on. They can also keep their fingers on the pulse of their financial health by regularly checking their credit history.

How much debt a client has isn't usually the first thing he wants to discuss with an advisor, but it is one of the most important issues that he should be asked about. We are happy to help guide these conversations with you to develop a planning strategy for your clients.

We hope this information is useful to you and helps your clients and their families. If you have a specific case or a question, please don't hesitate to call our office.