Chapter 1

The Concepts and Fundamentals of Estate Planning

Chapter Objectives

On completion of this chapter you should have a basic knowledge on:

- The Purpose and Importance of Estate Planning
- The Major Steps in the Estate Planning Process
- The Legal Rules and Principles Applicable in the Estate Planning Process
- The Principal Tools and Legal Instruments Use in Estate Planning
- The Overview of the Estate Administration Process in Malaysia

Chapter 1

The Concepts and Fundamentals of Estate Planning

Introduction

Anyone who earns an income or has financial assets and has dependents must seriously consider getting professional advice on estate planning. It is one of the key components of financial planning and is a process which has the objective of making the most suitable arrangements in order that an individual's assets may be passed on to dependents or beneficiaries in the most efficient, convenient and cost effective manner. Estate Planning may be defined as the process of making appropriate arrangements for the protection, preservation and provision of a person's assets for the benefit of dependents and other beneficiaries. This includes minimising estate administration costs, transfer fees and legal expenses, settlement of debts, provisions for the maintenance of dependents, avoiding disputes amongst beneficiaries as well as management of the assets of the deceased, if necessary. The word "estate" itself refers generally to an individual's assets when he has passed away.

The Human Factor in Estate Planning

Undoubtedly, making the "appropriate" arrangements for the dealing of one's assets if he were to pass away, is a morbid thought. No one likes to think of his own death, more so to make preparations for it. We are often reluctant to deal with the reality, though we know that death is inevitable and may even be sudden. There is always the feeling that we can make the necessary arrangements "later". Hence, the age old weakness of procrastination which affects almost all of us. Having accepted this common feature of most human beings, it should not be an excuse for us to shy away from the realities of life and the certainty of death. All of us have heard or have had personal experience of family members and dependents of persons who have passed away and the difficulties and frustrations they have faced in dealing with the assets and debts of a deceased person. Estate administration thus refers to the various procedures involved in dealing with the assets and other relevant matters of a deceased person. If we understand the challenges and difficulties the beneficiaries of a deceased are confronted with in the estate administration process, then we will naturally appreciate the importance of estate planning.

The Estate Planning Process

As in the other aspects of financial planning, estate planning also involves several stages and for the purposes of this course it is divided into, and commonly referred to as the “6 step process” which is as follows:

1. Establish the client’s objectives/goals.
2. Information or data gathering
3. Analyse and evaluate the client’s current financial situation.
4. Formulate practical strategies by selecting proper estate planning tools.
5. Develop an estate plan.
6. Implement and, where necessary, update the estate plan.

I) Objectives and Goals – The First Step

The objectives and goals of an individual in the estate planning process are very dependent on one’s personal value system. Generally, one would like to make all the necessary arrangements to provide maintenance and maximize the value of assets for the benefit of dependents as well as to minimize disputes, misunderstanding and inconveniences to family members. Of course, we also realize that, if all the proper arrangements are in place, unnecessary expenses and legal costs would also be kept to a minimum.

With this in mind, the following are some of the more common goals, most individuals would desire in the estate planning process:

a) Provide funds for funeral and testamentary expenses, and settlement of outstanding debts or loans.

b) Provide income to maintain a required standard of living to dependents and beneficiaries.

c) Establish adequate funds for children’s education needs

d) Create trusts, where necessary, authorising the management of assets for the benefit of beneficiaries and dependants.

e) Making arrangements to deal with one’s business interests such as those in partnerships and limited companies.

f) Provisions for charity or any other specific or peculiar wishes of the individual.

II) Information or Data Gathering - The Second Step

This is a basic requisite as in all other aspects of financial planning. All relevant information or the individual's assets, income, liabilities, outstanding debts and business interests must be made available before advice can be given to a client.

Most planners would use a standard "fact finding" questionnaire to obtain all that information. The extent of ownership interest and any limitations or constrains that may exist in dealing with any of the assets must also be identified. For example, if the client owns a piece of land, we need to be aware if it is "charged" to a financial institution as collateral for a loan or has any other restrictions with regards to the disposal of the land.

III) Analyse and Evaluate – The Third Step

The purpose of this step is to identify the strengths and weaknesses of the individual's position in relation to his goals and aspirations. A client may have substantial assets which leads him to believe that his estate planning goals may be achieved but he may have overlooked the fact that he may also be highly geared or have significant liabilities which will reduce his net worth at the time of death. These and similar issues need to be highlighted to the individual. Furthermore "ownership rights" may range from outright ownership to merely having a legal interest as a trustee. The limits of an individual's beneficial rights and interest in assets will have to be identified (see ownership rights below). This will determine how the assets may be dealt with and the most suitable estate planning tools to be used.

IV) Formulate Practical Strategies – The Fourth Step

This is the stage when the various strategies in dealing with the different types of assets are formulated. Wills, trust, assignments, buy-sell agreements for business interest and powers of attorney are some of the more common estate planning tools or legal instruments that are to be advised. This is done, taking into consideration the need to make provisions to settle liabilities and debts and preserve the various assets in accordance with the specific needs of the client. As a further example, nominations of insurance policies or EPF funds must be looked into and the effects of this must be considered in giving such moneys to the intended beneficiaries.

V) Developing an Estate Plan – The Fifth Step

Having completed all the above steps, the financial planner is now equipped to present an estate plan or "estate planning brief" to the client.

The brief should include the following:

i) the clients goals and objectives

ii) the financial details as to the assets, income and liabilities

iii) the various recommendations and the relevant estate planning tools respectively for the various assets. The rationale and explanation of the recommendations should also be stated.

iv) a recommended time schedule for the execution of the proposed plan.

v) the remuneration to the financial planner that is agreed upon.

vi) the clients authorisation to proceed with the recommendations made.

vii) a letter of discharge for the financial planner, to be signed by the client, if he has a differing view or rejects parts of the brief presented to him.

VI) Implementation and Update – The Sixth Step

This is the final stage when the client has consented to the implementation of part or all of the recommendations in the estate planning brief. Priorities must be identified as to the urgency and importance of the various aspects of the implementation. For example, upon the awareness of a mortgage reducing term assurance for protection against a loan, most clients may want to proceed with the purchase of an insurance policy for these purposes as soon as possible.

The professionals in the various fields such as lawyers, tax consultants, trustees and insurance advisers have to be engaged to execute specific areas of the implementation of the plan. Thereafter, there is a need to keep the client continually updated if there are specific concerns or issues that may arise, or if there are changes in the law introduced during this process of implementation. Finally, and if appropriate, family members or dependents may have to be kept informed of all or part of that which is implemented, with the consent of the client.

Ownership Rights

In analysing and evaluating the assets of an individual, we must first understand the concept of “ownership rights”, as there are different types of rights and each has its own mode of “transfer process” and subject to their respective legal processes.

The various forms of ownerships are as follows:

i) Outright ownership refers to an ownership which is free from encumbrances or restrictions;

ii) Life interest denotes an interest that a beneficiary possesses, enjoys, and has the benefit of whatever income that may be derived from such possession absolutely, until the demise of the beneficiary;

iii) Term interest is similar to that of a life interest, except that there is a limited term imposed on the benefits derived as decided by the legal or equitable owners.

iv) Future interest ownership is where there are no immediate rights to own, possess, use, and enjoy the property until the owner's death or the occurrence of a certain event or a specific appointed date, e.g. inheritance under a Will.

v) Business Interest in sole proprietorships and partnerships is where upon the death of the business owners, the business may have to be discontinued unless proper legal arrangements have been made.

vi) Joint Tenancy ownership occurs in circumstances where two or more persons may own an asset jointly and upon the demise of any one of the owners, his interest will automatically be transferred to the surviving owners based on the survivorship principle. This principle does not apply to immovable assets in Malaysia.

vii) Tenancy In Common occurs in circumstances where two or more individuals may own a particular asset and upon the demise of any one of the individuals, his interest shall form part of his personal estate.

In the Malaysian context and for estate administration purposes, it must be noted that all assets are classified into either movable or immovable assets. Immovable assets include land, residential homes, buildings, apartments and others which are basically "assets fixed to the land". All other form of assets are moveable and include:

i) monetary or liquid assets, such as moneys in various types of bank accounts,

ii) business assets, including interest in sole proprietorships, partnerships and shares in companies and goodwill of businesses,

iii) vehicles, jewellery and related items, antiques, paintings and other collectors items,

iv) intellectual property rights, such as trademarks and patents.

It must be further highlighted that there are several legislations, regulations and legal principles involved in dealing with the various types of assets in an individual's estate. A list of the main legislations is found in Appendix 1 at the end of this chapter.

Estate Administration

Estate administration is a process which should be conceptually seen as consisting of two major steps:

i) The first-step is to place the estate in the hands of one or more individuals, or an organisation who is authorised to "take charge" of the assets.

ii) The second-step is the “distribution” of the assets according to the relevant laws applicable.

At this point, we must be aware of two of the important basic principles that apply in the estate administration process. Firstly, the general principle of law that, liabilities of the estate and creditors must be paid first, before the assets of the estate are distributed or transferred to the beneficiaries. We shall see examples of this throughout this course when dealing with the various types of assets.

Secondly, is the implication of our laws on the estates of muslims in Malaysia. The legal process in this country is that the first-step stated above i.e. when “someone” is authorised to “take-charge” of the asserts, applies to both non-muslims and muslims. It is the second step, i.e when the distribution of assets are dealt with, that the principles applicable to muslims are different to that of others. For example, and as we shall see later, the Distribution Act 1958 (Amended 1997) does not apply to muslims who are governed by the Hukum Faraid principles.

Types of “Transfer”

There are broadly three types or modes of transfer “mechanisms”, by which the various assets of an individual are dealt with upon his death and this is with reference to the first-step in the estate administration process as stated above. They are:

i) Transfer in testacy or intestacy

ii) Transfer by statutory law provisions

iii) Transfer by contract (or contractual arrangements)

i) Transfer in Testacy or Intestacy

Testacy (or testate) refers to a situation where a person passes away leaving behind a valid Will. One of the main purposes of a Will is that one or more persons may be appointed as executors(s). An executor’s general responsibility is to take charge of the estate and eventually distribute the assets according to the instructions in the Will. More details of Wills will be discussed in the next chapter.

When a person passes away without a Will, he is said to have passed away intestate or the situation is said to be an intestacy. In such circumstances, one or more persons may apply to the High Court to take charge of the estate as administrator (s). Upon being confirmed as an administrator, his duties and responsibilities are similar to that of an executor but the assets would have to be eventually distributed according to the relevant laws applicable, such as, for example the Distribution Act 1958 (as amended 1997). Again, details will be discussed in the next chapter.

We can, as a general statement, say that in most cases when a person passes away, his estate is administered depending whether it is a testacy or intestacy. The personal representative, a term which refers to either an executor or administrator, is the person who takes charge of the estate.

ii) Transfer by Statutory Law Provisions

The moneys of a person in his Employee Provident Fund (EPF) will be paid to a named nominee upon his death. According to provisions in the EPF Act 1991, if a contributor has appointed a nominee and subsequently passes away any time thereafter, EPF will make payments directly to the nominee upon proof of death. The general rules are as follows:

i) if the contributor was a non-muslim, there is no obligation for the nominee to distribute the moneys to any other persons.

ii) if the contributor was a muslim, then the nominee has a duty to distribute the policy moneys accordingly to Islamic law principles.

Death claim proceeds of life and personal accident insurance policies are also to be paid directly to named nominees, if one or more of them are so named in the policy. This is specified in paragraph 4 of Schedule 10 (Section 130) of Financial Services Act 2013. Although details of such claim proceeds will be discussed at a later chapter, the following general principles are stated here for an initial understanding.

a) A policy of a non-muslim who has appointed his spouse, child or parent (only valid where there is no spouse or child living at the time of such a nomination) shall create a trust. The effect of this trust is that the moneys received by these nominees are intended to be for their personal benefit (i.e. they receive it beneficially). Furthermore, in these circumstances, even creditors do not take priority on such policy moneys. This is a unique privilege given to these immediate family members and is provided for in paragraph 5 of Schedule 10 (Section 130) of Financial Services Act 2013.

b) If the policy owner is a non-muslim and appoints as nominees individuals who are other than spouse, children or parents (the naming of parents being such that the policy owner was single and having no children at the time of nomination) such nominees will receive these moneys as an executor and have the responsibility to distribute the moneys accordingly. This means that if it is a case of testacy, the nominees (e.g. brothers or sisters) have to distribute the moneys in accordance to instructions in the will; and if the policy owner dies intestate, the moneys have to be distributed in accordance to the Distribution Act 1958 (1997) or Intestate Succession Ordinance (1960) (Sabah). This principle is embodied in Section 167(1) of the Act.

c) If the policy owner is a muslim, the role of the nominee is that of an executor and therefore he has a responsibility to deal with the policy moneys in accordance with Islamic law principles, as specified in Section 167(2) of the Act

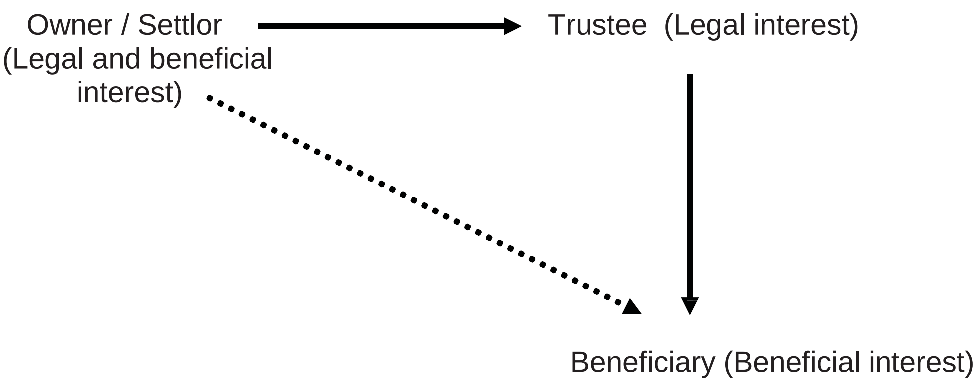
Thus, as we have seen above, the "nomination system" as provided in the EPF Act 1991 and the Financial Services Act 2013 places these moneys outside the general estate and therefore not subject to the various legal processes and rules that are applicable to testate and intestate estates.

iii) Transfer by Contract

Certain assets may be subject to "contractual terms" which place them completely or partially outside the general probate and administration process. The following that are briefly mentioned here (they will be discussed in detail in the later chapters), are the most common of these legal instruments which may be used as estate planning tools.

a) Trusts

A trust is an arrangement whereby the owner (settlor) of a particular asset transfers the legal rights to another person (trustee) to hold or manage it for the benefit of others (beneficiaries). To explain further, the typical arrangement of a trust is illustrated by the diagram below.



There are various types of trusts created for many specific purposes. For estate planning purposes the following serves as an example on how a trust arrangement maybe a great advantage.

An individual who has RM 2 million in cash may appoint a trust corporation as a trustee to manage the funds and also as to the manner it should be disbursed to him during his life time and to his family upon his death. All the terms and conditions of these arrangements are specified in a trust deed which is effectively an agreement between the settlor and the trustee. Upon the death of the settlor, the trustee can proceed to deal with the funds as specified in the terms of the trust deed. The trustee need not wait for a Grant of Probate or Letters of Administration to be obtained before executing the terms of the trust.

b) Powers of Attorney

A power of attorney (POA) is an instrument that allows the owner of an asset to appoint another (the attorney or donee) to deal with it as his “agent”. Such delegated authority, can be continued even after the death of the owner, if the POA is one that satisfies certain legal requirements. (Details will be discussed in Chapter 5).

c) Assignments of Insurance Polices

Assignments of insurance policies are also contractual arrangements, entered into by policyowners with the objective of transferring the ownership or the benefits to others who are called assignees.

d) Joint Accounts – Bank and Unit Trusts

Joint account holders of bank accounts and unit trust investors who purchase them as “joint owners” may also have certain rights to deal with these type of assets upon the death of one of the “owners”. Usually, in the application forms of such joint accounts in banks, there are terms and conditions which are stated that permits a surviving account holder to deal with the moneys upon the death of another of the account holders.

e) Buy-Sell Agreements among Business Owners

Business owners, especially partners or shareholders may enter into “Buy-Sell Agreements” among themselves to dispose off their interest in the business upon their death. Such arrangements allow the surviving business owners or appointed trustees to deal with the interest of the deceased, subject to various terms and conditions which have been agreed upon earlier (See Chapter 8 for further details).

Conclusion

As we have seen in this introductory chapter of estate planning, that it is a fascinating process that encompasses a wide area of knowledge to be acquired by the financial planner. Although the details of the various legal principals and issues will not be within the scope of this course, the planner must have a grasp of the overview of the processes so as to be of service to his clients accordingly. As was stated earlier, the estate planning process may be a delicate and sensitive subject when discussing with clients, but which is nevertheless necessary for almost anyone who owns any form of assets. Great care must be taken, when dealing with and advising clients and we must always take into consideration their personal and financial circumstances.

Appendix 1

IMPORTANT LEGISLATIONS IN ESTATE PLANNING

1) Probate & Administration Act 1959 - empowers the High Court to give personal representatives the Grant of Representations (i.e Probate or Letter of Administration) - governs the powers, rights, duties & obligations of personal representatives (executors or administrators)

   Rules of the High Court - procedural details to obtain grant of representations.

2) Will Act 1959 - contains formalities required in a Will - applies to non-muslims only.

3) Distribution Act 1958 (amended 1997) - applies to intestate distribution of non-muslims only.

4) Small Estates Distribution Act 1955 - intestate distribution - wholly or partly immovable estates - applies to both muslims & non-muslims.

5) Public Trust Corporation Act 1995 - intestate distribution - applies to wholly moveable estates only of muslims & non-muslims.

6) Trustee Act 1959 - Administrative and dispositive powers of trustees - duties & liabilities - where powers of Trustee are not specified in the trust deed, provisions may be specified in the Act.

7) Power of Attorney Act 1949.

8) Inheritance (Family Provision) Act 1971 - testate / intestate - dependents (4 categories) only - may apply to the Court for an increase in their share of the estate.

9) Muslim Wills (Selangor) Enactment 1999 - provisions relating to Wills of muslims in Selangor.

Appendix II

SPECIMEN CLIENT CONFIDENTIAL FACT-FIND

Part One: Personal Details

Name 1:		Name 2: (spouse)
Address	____________________	____________________
	____________________	____________________
D.O.B.	____________________	____________________
Place of Birth	____________________	____________________
Domicile /	____________________	____________________
Residence	____________________	____________________
	____________________	____________________
	____________________	____________________
	____________________	____________________
	____________________	____________________
	____________________	____________________
Tel	____________________	____________________
H/P	____________________	____________________

Marital Status ☐ Single ☐ Married

☐ Widow

State of Health ____________________ ____________________

Section Two: Family Details

Name	D.O.B.	Relationship	Health	Occupation

Other Immediate Family Members

Name	D.O.B.	Relationship	Health	Occupation

Section Three: Employment / Business Details

	Client 1	Client 2
Occupation / Business Name	______________________	______________________
Employer	______________________	______________________

For Business

Sole Proprietor ☐ Partnership ☐ Shares in Sdn Bhd ☐

	Yes	No
Any buy-sell contracts	☐	☐
Any agreement to sell your business in the Will	☐	☐

Number of partners ____________

	Yes	No
1) Any partnership agreements	☐	☐
2) Any existing agreements	☐	☐

Note: ____

Part Two: Financial Details

Section Four: Assets

Paper Assets

1) Bank Accounts
   a) Saving Account ______________________________

   b) Current Account ______________________________

   c) Joint Account ______________________________

   d) Fixed Deposit ______________________________

   e) Safe Deposit Account ______________________________

2) EPF / Private Pension / Gratuity ______________________________

3) Unit Trust / Mutual Funds ______________________________

4) Securities / Bonds / Futures ______________________________

5) Insurance
   a) Group Insurance ______________________________
   b) Personal Life / Investment-Linked Insurance ______________________________

   c) Personal Accident ______________________________

6) Club Memberships ______________________________

7) Nomination Interest ______________________________

Note: ____

Immovable Assets

1) Homes

____

____

____

2) Apartments

____

____

____

3) Condominium

____

____

____

4) Land

____

____

____

5) Others (please specify)

____

____

____

Note: ____

Movable Assets

1) Cars ____

____

____

2) Motorcycle ____

____

____

3) Others: ______________________________(please specify)

____

____

Note: ____

Business Assets

Sole Proprietorships -
________________________________ Partnerships -
________________________________ Private Limited
Company Shares ________________________________
Public Listed Company Shares ________________________________

Note: ____

Other Assets (Please specify)

____

____

____

____

____

____

____

Section Five: Liabilities

	Lender	Type	Amount Outstanding	Cost
1) Mortage				
2) Personal Loan				
3) Commercial Loan				
4) Others:				

Note: ____

Section Six: Objectives/Goals

List in order of priority of your estate planning objectives

1)

2)

3)

4)

5)

6)

Develop your client's objectives into Goals

1)

2)

3)

Part Three

Section Seven: Estate Planning Documents/Location

	Date of Writing	Located
1) Will	______________	______________
2) Trusts	______________	______________

Nomination From

	Yes	No	Don't Know
3) EPF Nomination	☐	☐	☐
4) Life insurance policy	☐	☐	☐
5) Power of Attorney	☐	☐	☐

Note: ____

Section Eight: Financial Advisors

1) Lawyer: ____

____

2) Accountant: ____

____

3) Stockbroker: ____

____

4) Insurance advisor (Financial Planner): ______________________

____

5) Investment Advisor: ____________________________________

____

Note: ____

____

____

Appendix III

Yearly review checklist

The following is an annual review checklist for keeping the estate plan updated. A positive response to any of these questions may indicate a need to revise the estate plan.

Check the following statements and tick where applicable.

a) Last Will and Testament	
( ) I would like to make a specific bequest to an individual not currently included in my last will and testament.	( ) An intended heir mentioned in my last will and testament has died within the past year.
( ) I would like to delete a specific bequest to an individual currently included in my last will and testament.	( ) I would like to change the amount of one or more of the bequests I have made under my last will and testament.
b) Change of Residence	
( ) I have changed residence during the past year.	( ) I have increased the amount of my mortgage during the past year.
( ) I have bought an overseas residential property during the past year.	
c) Wealth Holdings	
( ) The value of my home has increased over the past year.	( ) Either my spouse, or I have received an inheritance during the past year.
( ) The value of my home has decreased over the past year.	( ) Either my spouse, or I have received a legal settlement during the past year.
( ) The value of my overall estate has increased more than 10% during the past year.	

d) Family Status	
( ) A member of our family has married during the past year.	( ) A child (grandchild) has been born into our family during the past year.
( ) A member of our family has separated or divorced since our last review.	( ) A child (grandchild) has been adopted into our family during the past year.
( ) A member of our family died since our last review.	
e) Health Status of Own-self and Family Members	
( ) My health has substantially deteriorated during the past year.	( ) The health of one of my parents (spouse's parents) has substantially deteriorated during the past year.
( ) The health of my spouse has substantially deteriorated during the past year.	( ) A dependant has been seriously injured or handicapped since our last review.
( ) The health of one of my children has substantially deteriorated during the past year.	
f) Employment and Business Interests	
( ) My employment situation has significantly changed during the past year.	( ) I have entered into a buy-sell agreement during the past year.
( ) I have established a new business during the past year.	( ) The retirement program offered at my place of employment has been changed since our last review.
g) Life Insurance and Annuities	
( ) My group insurance benefits have been changed during the past year.	( ) I feel I need additional insurance
( ) I would like to change the nominee designation on an existing life insurance policy.	( ) I would like to learn more about the new types of life insurance policies being offered and how they might fit into my plans.
( ) I would like to transfer the ownership of a life insurance policy.	( ) I would like to change the nominee designation on an existing annuity.

h) Retirement	
( ) I would like to start my own individualized private retirement program.	( ) My spouse and I have some new goals for our retirement.
( ) My spouse and I are concerned about the rate of inflation and the impact on our current retirement program.	
i) Illness Care	
( ) I am uncertain about whether the benefits I will get from my current medical plans are sufficient to meet the increasing costs of illnesses.	( ) I am concerned about the cost of long term care if I should become ill during my retirement years.
j) Charitable Gifts	
( ) I would like to set up a gift-giving program to a charity.	( ) I would like to name a charitable beneficiary in my last will and testament.
k) Family Gifts	
( ) I would like to establish a gift-giving program for my adult children (grandchildren).	
l) Gifts for Minors	
( ) I would like to make annual tax free gifts to a minor child or grandchildren.	( ) I would like to name (or change) a trustee.
( ) I would like to establish a substantial fund for a child or grandchildren who are a minor.	( ) I would like to name (or change) the executor of my last will and testament.
( ) I would like to name (or change) a guardian to act on behalf of my children (grandchildren).	
m) Any other reasons	
( ) I would like to review my estate plan for the following reasons: ____________________ ____________________ ____________________	

Name : ______________________________

Address : ______________________________

____

____

E-mail Account : ______________________________

Telephone (House) : ______________ Fax No : ______________

Telephone (Business) : ______________ Fax No : ______________