

## Finance for Lawyers: Eve Adamson Written Assignment

Eve Adamson (76) is an elderly widow, who is about to move into a retirement community/nursing home. Between social security payments and pension benefits, she expects to have more than adequate resources to support herself in her new situation. What she needs from you is assistance with her estate planning. She has two sons, Cain and Abel, between whom she would like to divide her financial assets equally. Eve has already made a preliminary division, which is described below. She would like your advice whether this division is fair.

### Background

Just a few months ago, Eve's accountant put together a balance sheet (reproduced below). Eve is comfortable with the valuations that appear on this balance sheet. Aside from financial assets (consisting of bank accounts and various investments with a current market value of \$600,000), the largest asset on Eve's balance sheet is her home, an old Victorian house with an estimated market value of \$350,000. Eve's only other significant asset is an art collection consisting of a dozen early American primitive paintings, which Eve and her deceased husband had purchased over the years largely as a result of her husband's interest in the subject. Eve's insurance company recently appraised the collection as having a current market value of \$300,000. Aside from a \$100,000 home mortgage loan, Eve has no significant liabilities.

Eve's Balance Sheet as of December 31, 2002

Assets		Liabilities and Net Worth	
Cash Reserves in Bank		Home Mortgage Loan	<u>\$ 100,000</u>
Accounts (market)	\$ 650,000	Total Liabilities	\$ 100,000
Art Collection (appraised)	\$ 300,000		
Value of House (est.)	<u>\$ 350,000</u>	Net Worth	\$ 1,200,000
Total Assets	\$1,300,000		

Cain is Eve's elder son. He dropped out of college a number of years ago, and works episodically as a musician and part-time handyman, living in a small apartment. Eve has always worried about his financial security and would like to do what she can to help him out as soon as possible. Recently he has expressed interest in moving to California to find full-time work as a musician.

Abel is Eve's younger son. He recently graduated from medical school and is developing a promising practice in podiatry. Abel has no major financial obligations, although he is emotionally attached to the family's home, in which he still lives, and also shares his father's passion for early American primitive art.

## Eve's Proposed Division of Assets

In light of the differing needs and interests of her sons, Eve is thinking of the following division of assets.

First, she would like to use \$100,000 of her cash reserves to pay off the balance due on the home mortgage loan. She would also like to give Cain an immediate gift of \$50,000 to help him move to California and get settled there. The remaining \$500,000 of cash reserves, she would like to keep as an emergency nest-egg, with the understanding that she would leave the balance in this account to Abel when she dies.

Second, her art collection, she would like to divide equally among her two sons immediately. Since Abel has a greater interest in the collection, she would let him pick his six favorite paintings, and then let Cain have the other six with the understanding that Cain will be free to keep or sell the pictures as he chooses.

Third, regarding the house, she would like to let Abel live in the house for the rest of her life. When she dies, she is planning to leave the house to Cain, with the understanding that Abel may want to buy the property from Cain at that time. She sees the bequest of the house as a means of ensuring that Cain will have a some financial security as he grows older.

Finally, in order to help Cain over the next few years, Eve is planning to give him annual gifts of her extra income. She is reasonably confident that she will be able to give \$10,000 a year for as long as she lives. In trying to figure out the value of these annual gifts, Eve has assumed that she will live for another ten years, which seemed like a reasonable estimate given her family health history and mortality rates for the general population.

Based on the foregoing assumptions, Eve has determined that this plan fairly divides her financial resources as follows:

<i>Item</i>	<i>Abel's Share</i>	<i>Cain's Share</i>
1a. The outstanding balance on their home equity loan will be repaid with \$100,000 of their cash reserves in bank accounts.	—	---
1b. Cain will receive an immediate cash payment of \$50,000 to help him move to California.		\$50,000
1c. On her death, the cash reserves in Eve's bank account will be left to Abel	\$500,000	—
2. Abel will pick his six favorite paintings from the collection and the remaining six will be assigned to Cain to sell or keep as he sees fit.	\$ 150,000	\$ 150,000
3. In order to provide Cain with longer-term financial security, Eve will leave him her house when she dies; in the meantime Abel will live in the house and have the option of purchasing the house from Cain at the time of Eve's death.	---	350,000
4. Annual support for Cain for ten years (\$10,000 a year).	—	\$100,000
Total	\$ 650,000	\$650,000

Please write a short memorandum analyzing this proposal from a financial perspective. Does it represent an even division of assets between Eve's two sons? What changes, if any, would you recommend?