Frequently Asked Questions About Estate Planning

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What is Estate Planning?

Estate planning consists of the arrangements (plans) each of us makes, either intentionally or by doing nothing, in anticipation of our incapacity or death, for handling our estate (property) in the event of our incapacity and for disposing of our estate at our death. Estate planning frequently includes making a power of attorney, making a will, and/or creating a trust. Estate planning also includes a review of the manner in which we own our property (whether in our individual name or in joint ownership with someone else) and the beneficiary designations that we make to dispose of certain property (such as life insurance, IRAs, and retirement plan benefits). A well-coordinated estate plan will address such issues as minimization of income and death taxes (if any), the possibility of our temporary or permanent incapacity prior to our death, the disposition of our property at our death, and the management of property, where appropriate, for members of our family who may not be able to manage well for themselves. Estate planning also includes the consideration of provisions for church and charity.

What Is A Will?

A will is a legal instrument made for the primary purpose of transferring the ownership of property at death. Other reasons for making a will include the naming of a guardian for minor children and the naming of an individual, bank, or trust company (frequently referred to as the "personal representative," "executor," or "executrix") to supervise the estate settlement process. An individual who leaves a will is considered to have died "testate," whereas, one who dies without a will is considered to have died "intestate."

Who Can Make A Will?

In Indiana, an individual must be of sound mind and at least 18 years of age (or a member of the Armed Forces of the United States) in order to make a valid will. In Indiana, to be valid, a will must be in writing and must be witnessed by two disinterested individuals in the exact manner specified by law. Indiana does not recognize unwitnessed wills.

What Does A Will Do?

The function of a will is to transfer the ownership of specified property to the recipient(s) named in the will by the maker. In order to be controlled by the maker's will, the property must be owned by the maker in his or her own name at the time of death. Such property is sometimes referred to as probate property. A will cannot serve to transfer property owned by the maker as to which he or she is permitted to and has named a beneficiary. For example, if the maker owns a policy of insurance on his or her life or is a participant in a retirement benefit plan (401(k) or IRA), the maker probably will have signed a beneficiary designation form. That designation form, instead of the maker's will, will control the disposition of the life insurance, 401(k), or IRA benefit payable by reason of the maker's death.

The transfer of property, such as bank accounts, automobiles, and real estate, owned jointly by the maker with his or her spouse or another individual, with the right of survivorship, also is not controlled by the maker's will, so long as the spouse or other joint owner survives the maker. Rather, the jointly owned property will pass automatically at the first death to the surviving joint owner. Thus, with married couples, a will is not needed at the first death if all of the couple's property is owned by them jointly or is controlled by beneficiary designation. However, it is best for both of the spouses to have a will, just in case the first of them to die happens to own property in his or her own name at the time of death that is not controlled by beneficiary designation. Also, which spouse will survive always is a matter of speculation and, in any event, the surviving spouse may not have the time, ability, opportunity, or motivation to make a will following the first death.

What Should Be In A Will?

A will should state clearly that the instrument is the maker's will and that it is his or her intent to revoke all prior wills. It also should identify the maker and the members of his or her immediate family.

Under current Indiana law, if the maker and his or her spouse are both deceased, and the maker's family includes one or more minor children, the minor children of the couple are entitled to share in a collective $25,000 survivor's allowance which is paid before any other gifts are paid. This can prove to be especially problematic where a couple may have one or more children over the age of 18 and one or more under the age of 18. If the will is silent, the minor child or minor children would receive an additional $25,000. As most couples want their children to be treated equally, specific reference that the survivor's allowance is not to apply insures the maker's wishes are carried out.

Typically, the maker then will list any desired specific bequests of cash or other property (such as to an individual or a church or other charitable organization). Generally, with respect to household goods, furnishings, motor vehicles, tools, sporting goods, personal effects, and like items, it is best to dispose of them in the aggregate or by broad categories, rather than to incorporate long lists of specific items. Frequently, when long lists of specific items are incorporated into a will, some of the items either cannot be found following the maker's death or cannot be identified from the descriptions used in the will – or the named beneficiaries do not want the items specified for them.

After any desired specific gifts have been listed, a will should then indicate what is to be done with the balance of the maker's probate estate (frequently referred to as his or her residuary estate). In doing this, the maker should indicate a preferred plan of disposition and a contingent plan, just in case it is not possible to carry out the preferred plan. Family members and others do not always die in the order expected by the maker. This is an especially important consideration for couples who have young children, and in other situations where a common disaster affecting all of the members of the immediate family is possible.

Indiana law has been revised to give legal effect to a memorandum or list prepared by the maker after a will is signed if the intent to make a memorandum or list is mentioned in the will and the memorandum or list describes the items and beneficiaries with reasonable certainty and is signed by the maker. This list is limited to items of tangible personal property and cannot be used to dispose of anything other than items of tangible personal property. No such memorandum or list will be legally effective to make cash / monetary gifts, gifts of other items of intangible personal property (such as certificates of deposit, brokerage accounts, stocks, and bonds), or gifts of real estate. Because the possibility of unintended results from lack of coordination between the provisions of any such memorandum or list and other provisions of the maker's will is relatively high, we strongly advise you against the preparation of any such memorandum or list in the absence of competent legal advice.

A will also should specify how any death taxes and other expenses are to be paid – that is, whether they are to be paid generally out of the residuary estate before it is divided and distributed in the manner specified, or whether each (or certain) beneficiaries are to pay their own taxes and expenses out of the property received by them. Finally, a will should name the individual(s) and/or bank or trust company that the maker wants to act as the guardian of the maker's minor children, if any, and, whether the same or different, as the personal representative of the maker's estate.

What If There Is No Will?

If an individual (frequently called a "decedent") who is domiciled in Indiana at the time of his or her death does not leave a will, his or her property will be disposed of under the terms of the will substitute made by the Indiana legislature for all such individuals who fail to make a valid will. However, in many cases, the will substitute made by the legislature is not what the decedent would have wanted. To illustrate, in the case of a first-time married individual with children, the law provides that if that individual dies without a will, his or her surviving spouse will receive only one-half of his or her net probate estate, in addition to a $25,000 survivor's allowance. The other half will pass to the decedent's children, equally, regardless of their ages. Most married couples, whose only children are the ones from their marriage to each other, would prefer that all of their probate property pass to their spouse at the first death, and then to the children of their marriage at the second death. In order to assure this result, each spouse needs to have and maintain a will that indicates that preference.

The will substitute made by the legislature also is contrary to what most childless first-time married couples would want. The law currently provides that at the death of the first spouse, in addition to the $25,000 survivor's allowance, the surviving spouse is entitled to only three-fourths of the deceased spouse's net probate estate, if a parent of the deceased spouse is then living. The other one-fourth goes to the deceased spouse's parent(s).

The will substitute made by the legislature may be difficult to administer in the case of a second marriage. With a second marriage where the couple has no children of that marriage, at the death of the first spouse, after the $25,000 survivor's allowance, the surviving spouse is entitled to one-half of the deceased spouse's personal property (including household goods, furniture, etc., and bank accounts, stocks, bonds, etc), the same as with a first marriage, but only an amount equal to 25% of the fair market value of the real estate owned by the deceased spouse. The decedent's real estate may be difficult to value and the surviving spouse's entitlement to 25% of its fair market value may result in a forced sale of some or all of the decedent's real estate.

It should be noted, however, that the will substitute made by the legislature typically is of limited application in a second marriage context if the couple had a prenuptial agreement. It also should be noted, with second marriages where both of the spouses have children from a prior marriage, that placing title to property in joint ownership frequently is unwise, as there is a great likelihood that all of the joint property will end up in the hands of the surviving spouse's family (to the exclusion of the family of the first of the spouses to die).

A will is, therefore, a practical necessity if an individual's wishes are not the same as those expressed by the will substitute made by the legislature. A married individual, for one reason or another, depending upon whether it is the individual's first or a subsequent marriage, may wish to leave all of his or her net probate estate to his or her spouse (instead of partly to his or her children). An individual with children may wish to benefit one child over another. A childless unmarried individual may wish to leave property directly to nephews and nieces (for example), rather than to parents or siblings (as the legislature's will substitute provides). An individual also may wish to leave property to a church or other charitable organization. In all of those cases (and many others), for wishes that are not that uncommon, a will is needed.

What Is Probate?

In its simplest form, probate is the system or process by which the title to property owned by an individual at the time of his or her death is transferred to the beneficiaries of his or her probate estate. The probate system empowers the personal representative to transfer the ownership of that property from the decedent to the next owner. Without the probate system, banks and other institutions (for example) would not know who they could recognize safely as the new owner of the decedent's property (accounts, certificates of deposit, etc.).

The probate system was simplified greatly in Indiana with the advent of unsupervised administrations. Prior to unsupervised administrations, personal representatives were required to seek court approval for virtually all actions that they desired to take on behalf of an estate. The result was a more complicated, longer, and more costly settlement of a decedent's affairs. With an unsupervised administration, the court's involvement is essentially limited to the formal appointing of the personal representative. The balance of the settlement process is then left largely to the personal representative. This, of course, does not mean that the personal representative may proceed without scrutiny. At the end of the settlement process, the personal representative must provide all of the affected beneficiaries with a written accounting of his or her actions during the course of the administration. Further, anyone who believes that the personal representative acted improperly in any regard is afforded a period of three months, following conclusion of the administration, in which to file with the court an objection to the personal representative's accounting and discharge. If no objection is filed, the personal representative is discharged automatically from all further responsibilities and liabilities.

An unsupervised estate administration can be requested by an individual in his or her will. If not so requested, an unsupervised administration is still possible, if all of the beneficiaries sign a consent to an unsupervised administration.

As a practical matter, this can prove to be difficult in estates with more than a few beneficiaries.

Under current Indiana law, the probate process lasts for a minimum of three months. This allows creditors and others an opportunity to file claims against the decedent's estate. (This also establishes a deadline for the filing of claims.) In the unlikely event a federal estate tax return is required, the probate process can endure for more than one year before written approval of the return has been received from the Internal Revenue Service. Keep in mind, however, that most of this time is spent waiting for approval of the death tax return. Attorney fees and other expenses usually will not increase during the waiting period. In many cases, it also is possible to make a substantial partial distribution of the estate while waiting for approval of the estate tax return.

What About Death Taxes?

When it comes to death taxes, for estates of individuals dying after December 31, 2012, the only potential tax is the federal estate tax, and most estates are not subject to federal estate tax. Federal estate tax is a tax on the value of the property (estate) owned by the decedent at the time of his or her death. At the time of this publication, estates of up to $5.49 million for a single person and almost $11 million in the case of married couples are usually exempt from federal estate tax in 2017. In order for a married couple to receive the full benefit of the nearly $11 million exemption, the surviving spouse needs to arrange for a federal estate tax return to be filed for the deceased spouse—even if a return is not otherwise required. However, assets that are jointly owned need only be described on the federal estate tax return; there is no requirement to value jointly owned assets.

Indiana previously had its own unique system of inheritance tax. While originally slated for a gradual repeal over a period of several years, in 2013, the Indiana legislature voted to repeal the inheritance tax immediately for estates of individuals dying after January 1, 2013.

What Does An Estate Plan Look Like?

For the majority of individuals, an estate plan will take the form of a basic will that leaves everything to the individual's spouse, if surviving; otherwise, to his or her children (with, perhaps, a bequest of some measure to church or charity). In some cases, one or more trusts may be added to the estate plan, either within the will or separate from the will. Peace of mind may factor in the inclusion of trusts in a will. The ability of children or other beneficiaries to handle an inheritance may be a significant concern. For example, an individual may be concerned that if his or her children receive an inheritance at too young an age it may rob them of ambition or they may not have the maturity to handle their inheritance responsibly. Those concerns may be addressed through inclusion of a trust in the estate plan. Under Indiana law, in the absence of contrary provisions, all property inherited directly by a minor is turned over to the child at 18 years of age.

Trusts can also play a role when it comes to retirement accounts. One of the benefits of inherited retirement accounts is the ability to stretch distributions over the life expectancy of the retirement account beneficiary. Provided that the beneficiary only withdraws the required minimum amount, the retirement account can continue to grow virtually tax free, thereby providing a significant benefit for the beneficiary. In spite of this potential, if the beneficiary is named directly as a beneficiary of the retirement account, there is nothing to prevent that beneficiary from pulling out more than is required or even liquidating the entire account immediately. By designating a retirement trust as a beneficiary of a retirement account rather than the individual directly, you can insure that a beneficiary receives the benefit of the stretch technique. Planning of this nature is especially important for clients with large retirement account balances.

Additionally, a trust can be particularly useful in second marriage situations where an individual may wish to provide some lifetime benefit for a surviving spouse while insuring that some portion of the estate will pass to his or her children.

What Is A Trust?

Perhaps the most frequently discussed estate planning device today is the "revocable living trust." Such trusts are so popular that they are even being sold door to door as substitutes for wills. However, such trusts are not new at all, rarely are an effective complete substitute for a will, and have been available estate planning tools for hundreds of years. Their current popularity is due to actual and perceived abuses and deficiencies in the probate system in some areas of the country – and the representation of many trust promoters that having a revocable living trust will somehow make the trust customer's estate immune from those abuses and deficiencies. However, as frequently is the case, as one problem is addressed, another problem arises – and we now are seeing frequent abuses by some promoters of revocable living trusts.

In its most basic form, a trust is a legal device (declaration of trust or trust agreement) created in writing by an owner of property (frequently called the "settlor") by which the owner transfers the ownership of some or all of his or her property to himself, herself, or another individual or corporation (called a "trustee") who holds the title to and manages that property for the settlor in accordance with the provisions of the trust instrument. A revocable living trust will accomplish probate avoidance, with respect to property that is owned by the trust at the time of the settlor's death, because that property was not owned by the settlor at the time of his or her death; rather, that property was owned by the settlor's trust, which did not die. Consequently, there is no need for a process (probate) to handle the transfer of title to that property from the settlor to the next owner.

Trusts take two forms – living trusts and testamentary trusts. A living trust is a trust established during lifetime. Typically, the settlor acts as his or her own trustee until such time as he or she is unable to, or no longer desires to, act as trustee. The settlor transfers the ownership of some or all of his or her property to the trust, which is how probate is avoided over that property. Living trusts are the type of trust that is advocated by most trust promoters. A testamentary trust is a trust that is established by the provisions of a will and becomes effective at the maker's death. In essence, such a trust is a beneficiary like any other beneficiary named in the will. By its very nature, a testamentary trust will not avoid probate, but, nevertheless, may be very appropriate and useful in a variety of circumstances.

For total probate avoidance through the use of a revocable living trust, the key is in making certain that the settlor owns nothing in his or her own name at the time of death that is not disposed of by contract (the trust instrument, joint tenancy, or beneficiary designation). This includes property that the settlor owns at the time he or she establishes the trust, as well as property that he or she acquires after the trust is established. For many individuals, it is not very practical to transfer the ownership of all of their property to a trust and to continue to do so with respect to all property acquired over the remainder of their lives. Many individuals who attempt to avoid probate through the use of a revocable living trust fail to accomplish that objective – meaning, that at the time of death, for one reason or another, some of their property remains in their own name and is not owned by their trust or disposed of by contract – hence, the need to resort to the probate system to administer that property (in addition to the need to administer the trust).

It is commonly contended by revocable living trust promoters that the probate system carries with it a great deal of expense that is eliminated automatically by having a revocable living trust. The fact is, however, that there often are expenses associated with such a trust that are of the same or greater magnitude than typical probate expenses. Additionally, if the services of a professional trustee (i.e., a bank or trust company) are utilized, there will be trustee fees to pay. Although the use of a willing family member as the trustee can reduce or eliminate the fee that would be charged by a professional trustee, the job of trustee is one that carries with it all sorts of significant responsibilities and potential liabilities, which accounts for the size of the fees that professional trustees usually charge. Even in cases where settlement expenses are reduced (by having a properly funded trust), the cost of establishing the trust likely was significantly greater than the cost of a typical will. Many a revocable living trust customer is finding the required ongoing recordkeeping to be very confusing and frustrating, particularly when serving as his or her own trustee.

An additional consideration with the estate planning and settlement processes is that the expenses associated with probate can be lowered significantly with an unsupervised administration and a carefully selected lawyer to assist with the planning and settlement processes. Look for a lawyer whose fee is determined on a time and effort basis, rather than one who charges a flat percentage of the value of the estate.

All of this is not to say that revocable living trusts are a bad thing, as trusts are the most flexible and useful tool in the lawyer's workshop. Revocable living trusts offer a degree of privacy because the trust document which discloses the identity of the recipient of the trust does not become a public record. Revocable trusts can also be helpful in the context of property management for those who need help in managing their property. Finally, trusts are extremely useful for clients who own real estate outside the State of Indiana. By transferring ownership of non-Indiana real estate to a revocable trust, you can avoid probate in the other jurisdiction which can be more expensive and complicated than probate in Indiana.

Unfortunately, many individuals do not realize that qualified estate planning lawyers recommend and prepare trust agreements for their clients just as often as wills. If contemplating a revocable living trust, speak with a valued advisor like a family lawyer or accountant, rather than a stranger of unknown competence and reputation who will receive very private information, but who is not under the same obligation as is a lawyer or accountant to keep it private – and who is not likely to be available or capable of helping in the event that problems arise later on. Above all, use common sense. In many cases, a qualified family lawyer will help establish and fund a revocable living trust, if that is what is wanted and appropriate, for a lesser fee than the typical trust promoter will charge – and the family lawyer usually will be readily accessible if problems arise.

Where Should A Will Be Kept?

Obviously, a will is an important instrument and should be kept in a secure location. A desk drawer is not a good place, as it could end up in the wrong hands or get lost among other papers. A personal safe also is not a good idea, as the maker of the will may be the only one who knows the combination. Perhaps the worst place to keep a will is in an individually held safe deposit box. While this may seem to defy logic, because the will is secure, the reason is relatively simple. At the death of the depositor, the safe deposit box and its contents belong to the depositor's estate and the only person who can access the box is the depositor's named personal representative, following appointment by a court – but without the will to present to the court, it may not be possible to get the personal representative appointed. Banks are becoming less and less willing to bend the rules in these situations and allow access to a safe deposit box without the prior appointment of a personal representative.

The best place to keep a will is with the lawyer who prepared it, if he or she has the capability for secure and fireproof storage. The maker can then simply let his or her loved ones know who has the will and never worry about it again. Note, too, that leaving a will with the lawyer eliminates the ability of a disgruntled would-be beneficiary to find and destroy the will.

How Often Should A Will Be Updated?

Once a properly prepared will is in place, the maker will have a flexible document that can withstand certain changes, like the death of a spouse or child. However, as circumstances and wishes change, as inevitably they will, the maker should update his or her will. Generally, it is a good idea to review a will every three to five years. For example, after having made a will, the maker may decide over a period of time to change the beneficiaries of his or her estate, or the manner in which the beneficiaries share in the estate. A will also should be reviewed as milestones, such as marriage, remarriage, or the birth of a child, are reached – or as the maker's financial position changes or the tax laws change. These considerations apply equally to trusts. Whether incorporated in a will or a trust instrument (or both), estate plans need to be kept up to date. Many individuals have died with a will and/or a trust whose provisions were totally out of date with their wishes. Unfortunately, the provisions of the decedent's will and/or trust instrument will control the disposition of his or her property, even if not in accord with his or her known wishes at the time of death.

<u>General (Business) Power of Attorney</u>. Everyone over the age of 50 years should strongly consider giving someone else written authorization to act for him or her, either now or in the event that he or she becomes incompetent. A properly prepared and executed general (business) power of attorney empowers an individual designated by the maker (called the attorney-in-fact) to act for the maker with respect to the acquisition, management, and disposition of his or her property. In light of today's medical advances, each of us is statistically likely to face a period of incompetency prior to death. A power of attorney should be durable – meaning that it will remain valid, notwithstanding the lapse of time or the incompetency of the maker. General powers of attorney (and health care powers of attorney) are prepared by qualified estate planning lawyers with the same frequency as are wills and trust instruments.

If eligibility for Medicaid benefits may someday be a concern, it is essential for the power of attorney to specifically authorize the attorney-in-fact to make gifts, without limit, to the maker's spouse, children (including the attorney-in-fact), and their spouses. Sometimes, a properly prepared power of attorney is more useful and necessary than a will.

<u>Health Care Power of Attorney (Appointment of Health Care Representative)</u>. Separate from a general power of attorney, a health care power of attorney designates an individual specified by the maker (called the health care representative) to make health care decisions for the maker in the event that he or she is unable to make those decisions. This instrument is especially useful for second marriages, where there are several children; for single individuals without children; and where a parent would like to avoid potential conflict among his or her children. A health care power of attorney should be distinguished from a living will which, though more commonly recognized, accomplishes far less. A living will is only effective after a physician certifies in writing that death is likely to occur within a short period of time. Physicians do not like to do this. A living will may provide some psychological benefit (i.e., we are doing what Dad wanted), but has little legal benefit, as it does not authorize anyone to make health care decisions for the maker. Family members will likely receive far greater benefit from a health care power of attorney and careful choice of a health care representative who is authorized to make life and death decisions for the maker. Keep in mind that, contrary to an attorney-in-fact under a general power of attorney, a health care representative cannot make health care decisions for the maker unless and until the maker's attending physician has certified that the maker is not capable of making his or her own health care decisions.

Prenuptial Agreement. While many people think of a prenuptial agreement in the context of a divorce, it is perhaps even more valuable in the case of a death—especially in the case of a second marriage. As indicated above, when a couple marries, they are each entitled to a portion of the survivor's estate. With a prenuptial agreement entered into prior to marriage, each party may agree to give up some or all of the rights that are otherwise provided to them by law. This is especially important if the marrying parties have children from a prior marriage to whom they would like to leave some portion or all of their estate. In order to be enforceable, each party must disclose what they own as a part of the prenuptial agreement.

Limited Liability Company (LLC). Although they are popular tools in the corporate world, limited liability companies (LLC's) can also play an important role for estate planning purposes. To illustrate, if a client owns a significant amount of farm ground, they might want to consider creating an LLC that includes their children and then transferring an interest in their farm ground to the LLC. In addition to liability protection, an LLC can provide a management structure for the next generation which spells out issues, such as what happens if one of the LLC members dies or wishes to sell their interest. It can also help to shield the real estate from the creditors of a child.

Transfer on Death/Pay on Death. Much like an individual can designate a beneficiary on a life insurance policy or retirement account, it is also possible to designate a beneficiary on a bank account or even your house or other real estate. In the case of the bank account, this is done simply by completing paperwork at the bank where accounts are held. One should take care, however, by reading the designation form to make certain that one's wishes are carried out in the event of the death of a named beneficiary. In the case of a house or other real estate, one can have his or her attorney prepare a Transfer on Death Deed which will have the effect of the real estate passing automatically to the designated beneficiaries at the client's death. It should be noted that, in signing a TOD deed, all of the designated beneficiaries are owners of the property, which means they must all be in agreement as to what should happen with the real estate. There is no one individual who is in charge. However, for families that get along well, this can be a very valuable tool.

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