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Estate Planning for People Who Don't Need Estate Planning

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Many people with relatively small estates, when asked whether they have a will, typically reply, "Oh, I really don't need a will. I just don't have enough property." Unfortunately, these may be the very people who most need a will, since without a will, their beneficiaries may have to suffer the consequences of expensive court proceedings to get possession of the small amount of assets remaining after death. In addition, most people do not realize that "estate planning" involves much more than just having a properly drafted will, even for a small estate.

Do I need a will?

Yes! Even though it is possible to structure the ownership of your assets in such a way to avoid the need for any of these assets to pass "under your will," this method is almost always more cumbersome and expensive than a will. Many people do this in order to try to avoid probate because of the perception that probate is an expensive procedure. In Texas, because of our "independent administration" statutes, probate can be relatively inexpensive if the will is properly drafted (and the attorney handling the estate knows what he or she is doing). No matter how diligent you are in structuring the ownership of your assets to make sure that they pass to your loved ones at your death, almost everyone owns some asset (a car, household goods, or a rent deposit, for example) that does not automatically pass to their loved ones at death. **In Texas, a will is the simplest and easiest form of accomplishing the goal of making sure that your property passes to the right people upon your death.**

Who will get my property if I don't have a will?

In the absence of a will or other arrangements governing how your property will pass at death, your property passes under the "intestacy" statutes. (Those "other arrangements" are discussed below.) A person is said to die "intestate" if he or she dies without a will. The rules governing community property remained unchanged in Texas for well over 100 years. Any community property (almost all property acquired by spouses during marriage) was divided in half. The surviving spouse kept his or her half, while the deceased spouse's half passed to his or her children. Many people assumed [**incorrectly!**] that the survivor would get all of the community property. However, until 1993, this wasn't the case if the deceased spouse had any descendants (children, grandchildren, etc.). Then, effective September 1, 1993, the intestacy

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statutes were changed so that all of the community property will pass to the surviving spouse as long as all of the deceased spouse's children are also the children of the surviving spouse. If the deceased spouse has any children who are not the survivor's children, then the old rules apply, and the deceased spouse's half passes to his or her children.

Separate property passes by intestacy under a different set of rules. Separate property consists of any property owned by a person before they were married, and any property that they were given or inherited after marriage (plus the **appreciation** on the separate property). If you are married and have descendants, one-third of your real estate (which includes mineral interests) will pass to your spouse "for life," and the other two-thirds will pass to your descendants. Your spouse will be entitled to the income generated by the portion of the real estate passing to him or her, but the principal will eventually pass to your descendants upon your spouse's death. All of the rest of your property, such as personal effects, bank accounts, stocks, bonds, etc. ("personal property"), passes one-third to your spouse and two-thirds to your descendants.

If you are married but have no descendants, then half of your separate real estate passes to your spouse, while the other half passes to your parents, siblings, or their descendants. All of your separate personal property passes to your spouse.

If you are not married, all of your property passes to your descendants, if any. If you have no descendants, your property passes to your parents, siblings, or their descendants.

One "exception" to these rules applies to your homestead. Unless properly waived, your spouse has the right to use and occupy your homestead as his or her home for the rest of her life, regardless of whether the homestead was community property or your separate property, or who inherits the property. Similar rules apply to limited amounts of exempt personal property.

Isn't probate expensive?

It can be but doesn't have to be. Probate is the process by which an executor or administrator of your estate gathers all of the probate assets, pays all of the debts and expenses that need to be paid, including taxes, if any, and then distributes the property to the persons entitled under your will or the intestacy statutes. With rare exceptions, there are two types of probate in Texas: dependent and independent. In a dependent administration, the executor or administrator, after filing an inventory listing the assets of the estate, must ask for court permission to make sales, compromise claims, or to take most other actions. Usually, the executor or administrator must file a "bond" with the probate court. A bond is an insurance policy that guarantees the executor will be honest and do a good job. The cost of the policy is paid out of your estate. In addition, the executor or administrator must file annual accounts with the court, reporting all receipts and all expenses. This type of administration involves the extensive use of an attorney, and therefore can be quite costly.

Most of the administrations in Texas, however, are "independent." In 1843, while Texas was still an independent nation, our legislature authorized for the first time in America the settlement of a decedent's estate with virtually no court supervision. When an "independent" executor or administrator is appointed, once the inventory is filed, the executor or administrator can take virtually all steps necessary to gather the assets, pay debts and expenses, and distribute them to the beneficiaries without further court involvement. Usually, bond is waived. The attorney's role is reduced drastically, resulting in a much lower cost.

What are "probate" assets?

Probate assets, simply put, consist of all of the assets that you own which either pass under your will, if you have one, or pass under the intestacy statutes, if you don't have a will. They are also the assets which may be subject to control or supervision of the probate court and your executor or administrator. This includes all of your property which does not pass by the "other arrangements" mentioned above. These other arrangements include a living trust, which is a trust you create during your lifetime which holds assets for your benefit and provides for the disposition of the property in the trust upon your death; bank accounts and other property held with another person as joint tenants "with right of survivorship;" and insurance proceeds or retirement plan benefits payable to another person directly by virtue of a beneficiary designation. Note that some assets, such as retirement plan benefits and insurance proceeds, are almost never "probate" assets because they almost always pass under their beneficiary designations directly to some other individual, while bank accounts and real estate may or may not be owned as joint tenants with right of survivorship, and therefore can be either probate or nonprobate assets, depending on how they are held. It is very important to coordinate the disposition of any nonprobate assets with the disposition of assets contained in your will.

Okay, so I need a will. Can I write it myself?

Yes and no. There is certainly no legal requirement that a will be drafted by an attorney. In fact, it does not even have to be witnessed. Texas law allows anyone to execute a "holographic" will. This is a will that is written entirely in your own handwriting and signed by you. Unfortunately, while a holographic will may be valid to dispose of your property, the money saved by avoiding a lawyer today is usually far less than the extra cost of dealing with the problems associated with most holographic wills, such as property that is not disposed of by the will, the failure to provide for independent administration, or an unfair disposition of your property because you failed to anticipate an unusual order of deaths in your family. In other words, "pay now or pay later."

What should my will contain?

There are a number of provisions a will should contain in order to make sure your property ultimately gets to your loved ones at the least cost. Your will should state the county and state of your **residence**. The will should appoint one or more **executors** (with alternates). The executor can be an individual or a bank with trust powers, but need not live in Texas. In order to avoid added expense, you should provide that your executors be "**independent** executors" and **waive bond**. Independent administration eliminates most of the expenses normally associated with probate. A bond is usually unnecessary if you appoint someone you trust.

Many wills begin with **directions that the executor pay all debts, taxes and expenses**. These directions are not necessary, since the executor is under a statutory duty to pay these items even in the absence of any directions in the will. However, if your will makes any specific gifts to particular beneficiaries which you wish them to receive without having to bear the burden of taxes and expenses, your will should say so.

For most people, the most important provisions of their wills deal with **who gets the property**. You need to consider whether to leave all of your property to your spouse, or whether to make some provisions for children or other loved ones. A well drafted will should also contain provisions dealing with the **possibility that your loved ones may not die in the normal order**. You may not get around to executing another will after one of your loved ones dies, so the will should take this possibility into account. After you have

made any special gifts that you may wish to make, your will should contain **a "residuary clause,"** which disposes of anything else you may own (whether or not you know you own it). Special **provisions for minor or incapacitated beneficiaries** are discussed below. The will may name **guardians for your minor children**, although that can be done in a separate instrument. Your will should give the executor all necessary **powers to settle your estate and divide up your assets** among the beneficiaries. Your will must be **signed and dated by you** ("the testator"). In addition, the will should be **signed by two witnesses** older than the age of fourteen who are not beneficiaries named in the will (unless the will is "holographic"). Most Texas wills also have a provision called a **"self-proving affidavit"** which makes it much easier (and less expensive) to probate the will following your death.

What about the kids?

There are two different questions which you should consider, and the answers to those two questions may not be the same. First, you need to decide who will take care of your children if you die before they become adults. The person who gets custody of your children is called a "guardian of the person." You can name a guardian either in your will or in a separate document. You can name two people to serve as guardian for your children, but only if they are married to each other. Again, you should designate alternate guardians in case the people you choose first either cannot or will not act as guardians. Also, you should appoint someone you trust, and waive any bond requirement.

If you fail to name a guardian for your minor children, then their closest ancestor (your parents, for example) is entitled to be appointed. If there is more than one ancestor in the same generation, they are equally entitled, and it is up to the probate court to determine whose appointment would be in the child's best interest. If there are no grandparents (or great-grandparents), then the "nearest of kin" is appointed guardian. This would usually be an uncle or aunt, but could be a sibling if you had an adult child.

The second question you should address is who will take care of any property passing to your children. As minors, the children do not have the legal right to take possession of any property passing to them. If you do not make any other provisions in your will, then someone will be appointed by the court as "guardian of the estate." This type of guardianship (as opposed to a guardianship of the person) can be very expensive. The guardian of the estate must seek court permission for virtually any action, and must file an "account" annually, listing every receipt, every expense, and the property remaining on hand. Because all of these documents that are filed with the court are prepared by lawyers, the cost of a guardianship can be extremely high. You can **and should** avoid a guardianship of the estate for your children by providing in your will that any property passing to your children will pass instead to a trust for their benefit if they are under the age of eighteen years (you can set a higher age if you wish). The property that would otherwise pass to a minor child will instead pass to one or more trustees whom you select who will then invest the property for the benefit of the child and distribute money to the person having custody of the child as necessary for their health, support and education. The trustee is not subject to court supervision, and therefore the expenses associated with property held in trust are minimal.

The guardian of the person is in charge of raising your children, while the trustee is in charge of managing and spending the property passing to your children wisely. It may be that one person (or one couple) will not be the best person to fill both rolls. Therefore, you may decide to name one

person or couple as guardian of the person, and name someone else as trustee.

Your will can also contain a trust similar to the one described above for minor children that would automatically hold any property passing to an incapacitated beneficiary until the beneficiary regained capacity. Again, the benefit of this trust is the avoidance of the high cost usually associated with a guardianship of the estate.

What if I get divorced?

If you are divorced after executing your will, Texas law provides that any provision in your will giving your ex-spouse property or naming the ex-spouse as a fiduciary (executor, trustee, or guardian) is "null and void and of no effect." The same is usually the case with respect to life insurance made payable to the ex-spouse. However, reviewing the provisions of your will and the beneficiary designations for your life insurance and retirement plans should always be done during or immediately following a divorce.

What should I do with life insurance proceeds or retirement plan benefits?

Normally, you would name your spouse as the primary beneficiary of insurance proceeds and retirement benefits upon your death by executing a beneficiary designation provided by the insurance company or the retirement plan administrator. You also need to name a "contingent" beneficiary. This is the person who will receive the proceeds in the event your primary beneficiary dies before you do. Most people name their children. This may not be best. If your children are minors, then the proceeds or benefits will have to be paid to a guardian of the estate which, as noted above, generates substantial costs. This will be the case even if your will provides for trusts for your children because the beneficiary designations override the provisions of your will. In addition, the beneficiary designation may not make clear what happens to the share of a deceased child (for example, whether it passes to that child's children, or to your other children). You can, however, coordinate these beneficiary designations with the provisions of your will. Your will should contain a provision placing any of these proceeds which are made payable to the trustees named in your will into trusts for your children or their descendants. By naming the trustees in your will as contingent beneficiaries, the proceeds will pass directly to the trusts for your children. One benefit of this arrangement is that your children get the benefit of the proceeds as if they had passed to them under the will, but the proceeds are not subject to your creditors' claims. This can be a problem, however, if you are relying upon these proceeds to pay debts, funeral or other administrative expenses after your death. The best solution is to discuss these questions with an estate planning attorney when your will is drafted.

What is a "Living Trust?"

Living trusts have received a great deal of publicity in the past few years in the national press. Basically, when you create a living trust, you create a trust for your own benefit which you may revoke at any time. All of the property that you convey to the trust will be managed by the trustee of the trust. Usually, you name yourself as the initial trustee. The trust document will contain provisions directing the trustee to distribute whatever amounts you need to live on, while investing the remaining assets of the trust prudently. If you should become incapacitated, then the trust provides for the appointment of a successor trustee to come in and manage the assets for you. Upon your death, the assets pass directly to the beneficiaries named in the trust document, "avoiding probate."

While living trusts can be beneficial in certain circumstances (especially for individuals in states other than Texas where probate procedures are more burdensome

and costly), a few misconceptions should be corrected. First, a living trust for a Texas resident will not save a penny in estate or inheritance taxes over a well-drafted, tax-planned will. Second, the cost savings of a living trust versus a will which utilizes an independent administration are minimal. While the trust document itself may cost about the same as a will, in order for the trust to "avoid probate," your assets must be transferred to the trust before your death. This often may involve paying a lawyer an additional amount to prepare deeds to transfer real property or other transfer documents to transfer other property. Third, you should still have a will. There are invariably some assets that are not transferred to the living trust, and therefore, at the very least, you should have a will giving all of those assets to the living trust upon your death. In fact, placing your homestead into a living trust may impair the homestead exemption to which you are entitled for creditor protection purposes. Finally, a living trust itself does nothing to protect the assets in the trust from your creditors.

Because Texas probate is relatively simple and inexpensive (if you utilize independent administration), we normally do not recommend living trusts for Texas residents. However, if you own real estate in another state, or you think it would be prudent to set up a mechanism to allow someone else to come in and manage your assets for you (if you become incapacitated and can't manage them yourself), then a living trust may be appropriate. With respect to management of your assets by another, however, see the discussion below relating to powers of attorney.

If I have a will and I have reviewed all of the other arrangements disposing of my property, have I finished planning my estate?

Not quite. All of those documents may take care of what happens to your property (and how it happens) after your death. However, you also need to consider what will happen to you and your property during your lifetime if for any reason you become incapacitated.

A "**Durable Power of Attorney**" for financial purposes allows you to name another person, usually your spouse or children, as your agent or "attorney-in-fact." The agent is given broad powers to manage your assets on your behalf. This way, if something should happen to you, it will be unnecessary to go to court to have a guardian appointed in order to give someone else authority to manage your assets for you. Remember, guardianships can be very expensive because they require a great deal of involvement on the part of attorneys and the probate court. The term "durable" merely means that the power of attorney will not terminate if you should become incapacitated. That is important, because usually you don't want the power of attorney to be used **until** you become incapacitated. Since September 1, 1993, you can even provide that the power of attorney does not become effective until you become incapacitated.

If you become incapacitated, a guardianship should normally be avoided, if at all possible. However, if for some reason a guardianship is required, then Texas law also allows you to designate in advance the person you would like to act as your guardian, or to designate any person you would not wish to be your guardian.

Texas law also allows you to execute two documents that relate to you, not to your assets. One is called the "**Medical Power of Attorney**." This document allows you to name someone else who knows your intentions who can make medical decisions for you consistent with your own values and beliefs. The person you designate may only exercise decision-making authority for you if your attending physician certifies in writing that you lack the capacity to make the health care decision for yourself.

A similar, but different, document is a "**Directive to Physicians and Family or Surrogates**," also known as a "living will." A living will is limited in scope since it only addresses withholding and withdrawing medical treatment while you suffer from a terminal medical condition. Copies of both of these documents are usually available for free or at a nominal cost from your local hospital, long-term care facility, physician, attorney, and other state health associations such as the Texas Medical Association, Texas Hospital Association, Texas Health Care Association, and the Texas Association of Homes for the Aging.

Many people often place funeral and burial instructions in their will. This is inappropriate, since it is possible that your family members may not read your will until after the funeral and burial have taken place. There is no formal written document needed to express these desires. You should let your family members know if you have any specific desires, or consider taking care of the funeral and burial arrangements in advance.

Finally, many people wish to allow their bodies to be used to sustain others' lives after their own deaths through organ donation. Many of you may have seen these forms when your driver's license was renewed. Various organ procurement organizations can provide you with the forms necessary to make these wishes known.

What about taxes?

The vast majority of Americans will pay no inheritance or estate taxes. If the value of your entire estate (including life insurance proceeds and retirement plan benefits) is less than the "tax-free amount," after deducting debts and expenses, then there should be no federal estate taxes. (There have been no Texas inheritance taxes since the end of 2004.) As a result of 2010 and 2012 tax changes, the tax-free amount increased to $5 million per person, indexed for inflation following 2011, with a 40% tax rate for taxable estates in excess of the tax-free amount. (The 2017 tax-free amount is $5.49 million.)

Remember that if a couple's estate consists of community property, then only the deceased spouse's half is considered in determining whether he or she is under these limits. In addition, a dollar-for-dollar deduction is allowed for all property given outright to the survivor. Therefore, a will (and other arrangements) leaving all of your property to your spouse should guarantee that no taxes will be due upon your death, no matter how large your estate. However, if your combined estates exceed the tax-free amount, or may exceed that amount upon the death of the survivor, you should see an attorney who is familiar with tax-saving provisions in order to save estate taxes that might otherwise be due upon the survivor's death.

Generally, assets received by the beneficiaries of your estate are not taxable as income to them. Income taxes will have to be paid on any income earned by those assets following your death, and retirement plan benefits will also constitute taxable income to the recipients (although surviving spouses may roll these benefits over into an IRA and defer income taxation). Also, the assets passing to your beneficiaries receive a new "basis" for determining capital gains equal to their value on the date of your death. This means that even if you purchased an asset at a very low price, if your children sell that asset following your death, they will only have to pay capital gains taxes on the appreciation of that asset between the date of your death and the date they sell the asset.

Significant lifetime gifts may be subject to taxes. If you have a large estate, you cannot escape the effects of potential estate taxes just by giving all of your assets away during your lifetime. "Taxable" gifts count against the lifetime tax-free amount, and if you exceed that aggregate amount

of gifts during your lifetime, you will owe gift taxes. Even if you don't exceed that amount during your lifetime, any taxable gifts will reduce the tax-free amount available to apply to estate taxes at your death.

Currently, you may give cash or other property to any number of people you desire, and the gifts will **not** be considered taxable gifts so long as the total value of the property given to any one person during a calendar year does not exceed $14,000, and the gift is of a "present interest." This $14,000 limit is called the "annual exclusion" and may be used each year. A present interest means that the gifts are given outright to the donee or to special qualifying trusts for the donee's benefit. In addition, any amounts paid on behalf of another (i) as tuition to certain educational organizations or (ii) as a payment for medical care to any person who provides that medical care will not be considered as taxable gifts or count against the annual exclusion limit. The annual exclusion has been indexed for inflation since 1998, moving up in minimum $1,000 increments. It reached its current value of $14,000 in 2014, and likely won't increase until at least 2018.

What if I want more information?

An excellent source of further information is a book entitled **"How to Live — and Die — With Texas Probate,"** edited by Charles A. Saunders in association with the State Bar of Texas (7th ed. 1995). While the estate tax amounts figures in this edition are a bit out-of-date, the basic description of Texas law remains accurate. The Seventh Edition may be found in many local bookstores or websites such as amazon.com and barnesandnoble.com for around $13.00. (An updated Eighth Edition is still several years away.)

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