Presented:
16th Annual Estate Planning, Guardianship and Elder Law Conference

August 7-8, 2014
Galveston, TX

Nuts and Bolts: Planning for the Transfer Of Non-Probate Assets at Death

Arielle M. Prangner

Author contact information:
Arielle M. Prangner
Davis & Willms, PLLC
Houston, Texas 77027

arielle@daviswillms.com
281-786-4500

ARIELLE M. PRANGNER

Davis & Willms, PLLC

Board Certified - Estate Planning and Probate Law
Texas Board of Legal Specialization

3555 Timmons Lane, Suite 1250
Houston, Texas 77027

Phone (281) 786-4500
Fax (281) 742-2600
arielle@daviswillms.com

EDUCATION:

- J.D., University of Texas School of Law, 2008, with honors
- B.S., Special Education, Texas A&M University, 2005, *summa cum laude*

OTHER QUALIFICATIONS:

- Admitted to Practice: State Bar of Texas; United States Tax Court
- Board Certified, Estate Planning and Probate Law, Texas Board of Legal Specialization

PROFESSIONAL ACTIVITIES:

- Real Estate, Probate and Trust Law Section, State Bar of Texas
- Tax Section, State Bar of Texas
- Probate, Trusts and Estates Section, Houston Bar Association
- Houston Estate and Financial Forum
- Houston Estate Planner's Association

SPEECHES AND PUBLICATIONS:

- Speaker: *The Brave New World of Estate Planning*, Houston CPA Society 2014 Spring Accounting Expo, 2014
- Speaker: *Where to Begin? – An Overview of Trusts* and *Business Structure Choice and Conversion*, National Business Institute, Estate Planning from A to Z, 2013
- Co-Author/Speaker: *An Overview of the Probate Process*, National Business Institute, The Probate Process from Start to Finish, 2010, 2013
- Speaker: *Estate Planning Basics*, Houston Bar Association, 2013
- Co-Author/Panelist: *Irrevocable Life Insurance Trusts*, Texas Bar Association, Intermediate Estate Planning and Probate Course, 2012
- Author/Speaker: *Where to Begin? An Overview of Trusts*, National Business Institute, Trusts 101, 2011
- Author/Speaker: *Life Insurance Trusts,* National Business Institute, Trusts 101, 2011
- Panelist: *Twilight Planning: Using Advanced Techniques to Plan for Incapacity*, Houston Bar Association's Probate, Trust and Estate Section, 2011
- Author/Speaker: *Life Insurance Trusts*, Texas Bankers Association, Texas Trust Administration Forum, 2010 and 2011
- Author/Panelist: *Taking Stock- A Guide to Probate and Guardianship Inventories*, South Texas College of Law Wills & Probate Institute, 2009

NUTS AND BOLTS: PLANNING FOR THE TRANSFER OF NON-PROBATE ASSETS AT DEATH

NUTS AND BOLTS: PLANNING FOR THE TRANSFER OF NON-PROBATE ASSETS AT DEATH

I. INTRODUCTION

When crafting a comprehensive estate plan for clients, planning for and coordination of non-probate assets is an imperative part of the process. Most clients' estates include non-probate assets; and more and more, the proportion of these non-probate assets in relation to the overall value of the client's estate is quite significant. It is not uncommon for life insurance and retirement plans alone to make up the majority of the value of a client's gross estate. Accordingly, attorneys must advise clients to incorporate these assets into the estate plan, and not just as an afterthought.

Obviously, the attorney must ascertain the client's personal goals with respect to the overall estate plan in order to make a determination regarding the ultimate disposition of the client's non-probate assets. The attorney must then identify and analyze each non-probate asset and educate the client regarding how each asset should be distributed at the client's death. The paperwork involved in directing the disposition of non-probate assets can sometimes be daunting. The forms required are as varied as the financial institutions, life insurance companies, plan administrators, and plan custodians involved.

This outline is not intended to address every issue associated with the coordination of non-probate assets with the rest of the estate plan. In particular, the nuances of the income tax and distribution considerations involved in the disposition of retirement plans are not addressed. Additionally, structuring assets to pass outside of probate through trust planning, including revocable trust planning, is not covered.[1] Rather, the goals of this outline are to highlight issues that may influence the suggested disposition of non-probate assets, to assist in the identification of non-probate assets that may not be easily recognizable, and to provide guidance about how to manage some of the paperwork involved.

II. CONSIDERATIONS INFLUENCING THE BEST DISPOSITION OF NON-PROBATE ASSETS

The attorney must take the time to listen to the goals and concerns of each client and use the information gathered during these discussions to shape the plan for disposition of non-probate assets in a way that accomplishes the client's objectives and coordinates with the overall estate plan. Although the general considerations of our clients are usually similar, each client's personality and situation is unique and clients will inevitably place different emphasis on each of the considerations. In addition to the critical goal of providing for a particular person or class of persons, clients' goals may include tax savings, creditor protection, and probate avoidance. It is important to evaluate each of these goals when advising a client.

Most of our clients can identify exactly who they would like to receive their property at their death. While the client's ultimate goal may sound simple (e.g., "I want to take care of my spouse for her lifetime, and then I want my kids to be provided for."), consideration must be given to a host of factors in order to determine how that simple sounding objective can best be accomplished.

A. <u>Minor Children</u>. If minor children are involved in the estate plan, it is important to ensure that property will not pass to those children outright. In Texas, children under the age of 18 are minors and deemed to be under a legal incapacity.[2] Accordingly, if a minor child inherits property outright, a court will have to prescribe a management vehicle for the property, which may range from appointing a guardian of the child's estate, to ordering that the funds be held in the court's registry, to creating a management trust for the property. To avoid a costly and time consuming legal proceeding to determine how to collect and hold funds for a minor, the client may elect to employ trust planning in his or her Will. Non-probate assets, therefore, should be structured to avoid passing to minor children outright.

B. <u>Beneficiaries with Special Needs.</u> If the client wishes to benefit a person who may be accepting or eligible to accept governmental benefits, consideration needs to be given to whether the assistance received by the beneficiary has an effect on qualification. If so, receipt of inherited assets by the beneficiary (whether outright or in trust) may disqualify him or her from acceptance of those benefits. Careful consideration and planning is required if a client knows or anticipates that one of his or her intended beneficiaries may qualify for governmental benefits. A supplemental needs trust (sometimes also called a special needs trust) may need to be created to hold funds for a beneficiary receiving governmental assistance that will allow the beneficiary

[1] For an excellent discussion of revocable trusts and multi-party accounts in estate planning, see Davis and Willms, *Planning for No Probate: Special Issues with Revocable Trusts and Nonprobate Assets,* Hidalgo County Bar Association 2013 Probate, Trust & Guardianship Law Course.

[2] TEX. ESTS. CODE § 22.016.

to continue to qualify for the assistance. If such a trust is necessary, leaving non-probate assets outright to the beneficiary may thwart the purposes of the trust and may disqualify the beneficiary from receipt of governmental assistance.

C. Providing for Surviving Spouse and Children in Succession. If a client's goal is to provide for his or her spouse for the surviving spouse's lifetime and then provide for the client's children, leaving assets outright to a spouse may not accomplish these purposes. If a spouse receives property outright, whether through a bequest in the client's Will or through designation of the spouse as beneficiary of a non-probate asset, there is no guarantee that at the surviving spouse's later death he or she will leave that asset to the first spouse's children. This tends to be a more pressing concern when working with married couples who have children from prior relationships. Many couples employ trust planning to achieve ultimate disposition to a second generation at the death of the second spouse. Non-probate assets should be evaluated to determine if they should pass to the trustee of such a trust.[3]

D. Payment of Debts, Expenses, and Taxes. Some clients have earmarked certain assets for particular beneficiaries (e.g., a life insurance policy for Child A and the family business for Child B). Likewise, some clients, intending to provide equally for two parties, leave all of the probate estate to one beneficiary and leave a non-probate asset of equivalent value to another beneficiary. In these types of situations, the client must be made aware of disparities that may arise between the beneficiaries as a result of the necessary payment of debts, expenses, and taxes.

For example, if a client has a probate estate of approximately $3,000,000 which he leaves to Child A, and a life insurance policy with a death benefit of equivalent value of which Child B is the named beneficiary, Child B could end up being much better off. This is because the estate's creditors will first look to the probate assets for satisfaction of their debts. Additionally, although proper drafting can be done, it is common for a Will's apportionment clause to direct that all administration expenses and taxes be paid from the client's residuary estate. In that case, Child A's portion would be greatly depleted while Child B's portion would be left untouched. Even if Child B would like to do the right thing and pay for half of any debts, expenses, and administration expenses, there may be gift tax consequences to Child B.

Accordingly, if a client expresses a desire to provide for beneficiaries in such a manner, these issues should be discussed and the apportionment clauses in the client's Will should be scrutinized and modified if necessary to accomplish the client's objectives.

E. Tax Savings. I've yet to encounter a client whose goals do not include saving tax. The considerations involved in tax savings, whether in relation to estate tax or income tax, are complicated. Nonetheless, the client should be made aware of tax issues involved in the disposition of non-probate assets.

1. Estate Tax. If traditional tax planning is employed in the client's Will, it may be important for non-probate assets to be available to fund the tax-planned trusts created in the Will. Otherwise, these trusts can end up being unfunded or underfunded. The relatively new availability of "portability" of a deceased spouse's unused federal estate tax exemption amount may negate or minimize the underfunding problem in some circumstances. However, to take advantage of portability, a federal estate tax return must be filed for the deceased spouse within 9 months of his or her date of death (or within 15 months with a timely filed extension request).[4] For married clients who may have estate tax exposure, it is important to discuss the various methods of estate tax planning and coordinate non-probate assets accordingly.

2. Income Tax. Clients should be made aware of income tax implications of naming beneficiaries on certain non-probate assets. If the non-probate asset involved is a "qualified" retirement plan (IRA, 401(k), pension, thrift, profit-sharing, KEOGH, etc.) or tax-deferred annuity, the best income tax result (i.e., longest deferral period) is generally achieved only if the beneficiary meets the requirements to be treated as a "designated beneficiary" under the Internal Revenue Code and Treasury Regulations.[5]

If a client has charitable inclinations, naming a charity as a beneficiary of such qualified retirement plan may be the most tax efficient way to accomplish charitable goals. Although a charity cannot be a "designated beneficiary," when benefits are distributed to a charity, the charity will receive the benefits free of income tax, as opposed to individuals or trusts who would have to

[3] Of course, if the spouse is named as the trustee and distributes or ends up needing all of the assets in the trust, the assets won't be available to pass to children or other descendants at the spouse's later death.

[4] I.R.C. § 2010(c)(5).

[5] I.R.C. § 401(a)(9).

pay income tax on the distributions received from such retirement plans.[6]

While a complete discussion of the nuances involved in such a determination are outside the scope of this article, income tax implications should be considered when planning for these qualified non-probate assets.[7]

F. Creditor Protection. If a client has concerns about the creditors of a beneficiary or his or her own creditors, the rules relating to creditor exposure should be carefully considered when directing the disposition of non-probate assets.

1. Creditors of the Beneficiary. A client may have specific reasons for seeking creditor protection for a beneficiary. For example, the client's spouse may work in a high risk profession (e.g., the medical field), or a client's child may be bad at managing money. However, many clients just like the idea that their beneficiaries' inheritance may be protected from general creditors and potential claims in a divorce. To this end, a client may desire that any inheritance (including non-probate assets not otherwise protected from creditors as discussed below) pass to the trustee of a testamentary spendthrift trust for the benefit of the beneficiary rather than to the beneficiary outright.

2. Creditors of the Decedent. Additionally, the client may be concerned about his or her own creditors. At the client's death, his or her personal creditors will become creditors of the client's estate. Most assets that are administered as part of the estate will be exposed to claims of creditors of the estate. Accordingly, the knee-jerk reaction may be to structure assets so that they are non-probate assets and avoid naming the "Estate" as the beneficiary of non-probate assets that require a beneficiary designation. However, those actions may not be necessary or may not have the desired effect of creditor protection.

3. Creditor Exposure and Protection for Some Non-Probate Assets. The discussion below highlights a few notable creditor issues for select non-probate assets.

a. Life Insurance and Annuities. Estate planners used to caution against naming the client's "Estate" as a beneficiary on a life insurance or annuity contract. The Texas Insurance Code provides that benefits under life insurance and certain annuity contracts are exempt from garnishment, attachment, execution, or other seizure by creditors.[8] For many years, it was believed that if an estate was the recipient beneficiary, these protections did not apply. Texas Insurance Code Section 1104.023 makes it clear that that if a trustee of an inter vivos or testamentary trust is named as the beneficiary of a life insurance policy, the policy proceeds received by the trustee are not subject to the debts of the insured; however, the statutory language regarding estates as beneficiaries was not as clear. As of September 1, 2013, though, Section 1108.052 of the Texas Insurance Code was amended to provide that the creditor exemptions apply regardless of whether the insured's estate is the beneficiary.

b. Retirement Plans. Texas Property Code Section 42.0021 provides that a person's right to the assets held in or to receive payments under certain retirement plans is exempt from attachment, execution, and seizure for the satisfaction of debts to the extent the retirement plan or account is exempt from federal income tax, or to the extent federal income tax on the person's interest is deferred until actual payment of benefits to the person pursuant to certain provisions of the Internal Revenue Code. These plans and accounts include stock bonus, pension, annuity, deferred compensation, profit-sharing, or similar plans, including a retirement plan for self-employed individuals, or a simplified employee pension plan, an individual retirement account or individual retirement annuity, including an inherited individual retirement account, individual retirement annuity, Roth IRA, or inherited Roth IRA, or a health savings account (collectively herein referred to as "retirement plans"), and under any annuity or similar contract purchased with assets distributed from that type of retirement plan or account. This statute was amended effective September 1, 2013 to explicitly include Roth IRAs and inherited Roth IRAs. The statute makes clear that the interest of a person in a retirement plan because of the death of another person is exempt to the same extent that the decedent's interest was exempt on the date of the decedent's death.[9] However, there is no such creditor protection afforded to an estate, so naming the client's "Estate" as the beneficiary of a retirement plan will subject those assets to claims of creditors of the estate.

c. Accounts with Survivorship Features. On the other hand, some assets that pass outside of the

[6] *See* I.R.C. §§ 691(a), 501(a).

[7] For a thorough discussion of these issues, see Akinc, *Quick and Dirty Guide to Retirement Benefits*, UT Law CLE 16th Annual Estate Planning, Guardianship, and Elder Law Conference (2014), and Reis, *Leaving an IRA to a Trust, id*.

[8] TEX. INS. CODE §§ 1108.001, 1108.051.

[9] TEX. PROP. CODE § 42.0021. It should be noted that the United States Supreme Court recently held that if a client is in federal bankruptcy and chooses federal exemptions, inherited IRAs are not exempt from bankruptcy creditors. *Clark v. Rameker*, U.S. __ (2014).

probate estate may still be subject to claims of creditors of the decedent. For example, just because an account passes outside of the decedent's probate estate pursuant to a right of survivorship (as discussed further below), the account may still be subject to the debts of a deceased account holder. Section 113.252 of the Texas Estates Code provides that a multiple-party account remains subject to the debts of a deceased account holder for debts, taxes, and expenses of administration, and statutory allowances, if other assets of the estate are insufficient. Any party receiving payment as a result of surviving must account to the personal representative for amounts necessary to discharge these claims and expenses, but such party is not liable for more than he or she received.[10] After a claim is asserted, the personal representative of the estate has two years to file suit to recover the property.[11]

G. Probate Avoidance. Many clients enter an estate planning attorney's office with preconceived notions about the horrors of probate. Some have had a conversation with a banker about how much easier things are when assets pass pursuant to a right of survivorship and insist that as many assets as possible be structured as non-probate assets. Other times clients come to our office insisting that they need revocable trust planning to avoid probate altogether because their cousin's wife had such a terrible experience with her mother's probate in California. Fortunately, with proper estate planning in place, the probate procedure in Texas is relatively straightforward, and many clients come to their senses after a discussion about what is involved in Texas probate. In some circumstances, of course, it may be appropriate to advise clients to engage in revocable trust planning, such as when a client would like management assistance with his or her assets or wants to keep any informaiton regarding their estate plan out of public record. In those situations, each non-probate asset should be structured to coordinate with the revocable trust planning.

There are reasons other than probate hysteria to arrange for certain assets to bypass probate, of course, and these should be considered. Often a client wants a household account to pass to his or her spouse at his or her death to avoid the possibility that the spouse will not have to wait for the probate process to have access to necessary funds for living expenses. Sometimes clients desire for there to be a fund immediately available for funeral expenses. Some clients may own real property in another state with a cumbersome probate process and want to avoid the need for an ancillary probate in that state. These concerns should be explored when discussing the disposition of non-probate assets.

III. SPECIAL CONSIDERATIONS FOR A CLIENT WHO IS OR HAS BEEN MARRIED

A. Marriage. When representing clients who are married, consideration must be given to community property laws and the rights of spouses to non-probate assets, subject to any federal law preemptions.

1. Spouse's Community Property Interest. In Texas, if a client is married, the non-probate assets in his or her name are often community property (because they are acquired during the couple's marriage while residing in Texas). Even though a non-probate asset may be community property, only the owner of a life insurance policy (usually the insured) or the participant in the retirement plan has the right to designate the beneficiary.[12] If the non-insured or non-participant spouse is not named as the beneficiary, the community property interest of the non-insured or non-participant spouse must be taken into account in beneficiary designation planning. If the asset is payable to the surviving spouse, these issues become less important. Furthermore, provisions in the deceased spouse's Will providing for the non-pro rata division of community property assets can mitigate these issues.

2. Spouse's Rights in Plans Governed by Federal Law. In the case of certain qualified retirement plans and life insurance policies, federal law, specifically, the Retirement Equity Act of 1984 ("REA"), requires that plans provide that the participant's spouse receive a mandatory death benefit upon the death of the participant or a joint and survivor annuity upon the retirement of the participant.[13] With regard to assets held in most employer-sponsored retirment plans, a non-participant spouse must give his or her consent to the beneficiary designation if the participant names someone other than the non-participant spouse as the beneficiary.[14] If a non-participant spouse desires to give his or her consent regarding such a designation, the consent must take the form proscribed by statute. Several cases have held

[10] TEX ESTS. CODE § 113.252.

[11] *Id*.

[12] *See* TEX. FAM. CODE § 3.102, TEX. INS. CODE § 1113.001. But see discussion regarding assets governed by federal statues, immediately below.

[13] 29 U.S.C. § 1055(a). It should be noted that a retirement plan governed by federal law may provide that benefits will not be payable to the surviving spouse unless the participant and such spouse had been married throughout the 1-year period ending on the earlier of the participant's annuity starting date or the date of the participant's death. *Id.* § 1055(b)(4).

[14] *Id.* § 1055(c).

that these REA granted rights are not waived as a result of general waiver provisions in a premarital or antenuptial agreement.[15]

Therefore, if the estate plan includes a desire to direct non-probate assets to anyone other than the client's spouse, it is prudent to determine whether the asset is subject to federal law that would prevent such a designation without the spouse's consent and plan accordingly. Keep in mind that one spouse giving up rights to property that he or she would otherwise have raises issues regarding joint representation that are beyond the scope of this article.

B. <u>Divorce</u>. In the event that a client has been divorced or has had a marriage annulled, the divorce decree and all beneficiary designations for non-probate assets should be reviewed.[16]

1. <u>"Divorce Revokes" Statutes.</u> If a client has designated his or her spouse as a beneficiary of a life insurance policy or retirement plan and fails to update the beneficiary designation after divorce, whether as a result of forgetfulness, procrastination, or untimely death, Texas law may provide some protection. Texas Family Code Sections 9.301 and 9.302 provide that if a decree of divorce or annulment is rendered after a person has designated his or her spouse as a beneficiary under a life insurance policy, individual retirement account, employee stock option plan, stock option, or other form of savings, bonus, profit-sharing, or other employer plan or financial plan of an employee or a participant which was in force at the time of the divorce or annulment, a provision in favor of the former spouse is not effective unless (1) the divorce decree designates the former spouse as the beneficiary; (2) the person redisignates the former spouse as the beneficiary after the divorce; or (3) the former spouse is designated to receive the proceeds in trust for, on behalf of, or for the benefit of a child or a dependent of either the person or the former spouse. If either of those sections acts to revoke a designation of the former spouse as a beneficiary, the proceeds or benefits are payable to the named contingent beneficiary, or, if there is no named contingent beneficiary, to the estate of the deceased spouse.[17]

However, clients should be advised to not blindly rely on these "divorce revokes" statutes, especially in relation to non-probate assets governed by federal law. The United States Supreme Court (the "Court") has held that when a "divorce revokes" statute acts to change the disposition of an asset governed by federal law, the statute is preempted.

In *Egelhoff v. Egelhoff*, a life insurance policy and pension planed governed by ERISA named Mr. Egelhoff's former spouse as beneficiary.[18] His children from a prior marriage contended that the state of Washington's "divorce revokes" statute acted to revoke the designation in favor of the former spouse. However, the Court held that because the statue attempted to include ERISA plans, it was expressly preempted by ERISA's preemption provision. ERISA states that it "shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan" covered by ERISA.[19] ERISA contains no "divorce revokes" language. Accordingly, the Court held that benefits were properly payable to the former spouse pursuant to the beneficiary designation.

Further, a cause of action may not be available against a former spouse who receives the proceeds of an asset governed by federal law as the result of the failure of a "divorce revokes" provision. In *Hillman v. Maretta*, a life insurance policy governed by the Federal Employee's Group Life Insurance Act of 1954 ("FEGLIA") was at issue.[20] The parties in that case agreed that the portion of a Virginia statute revoking the designation of the former spouse as beneficiary was preempted by FEGLIA. At issue, however, was another provision of the statute, which created a cause of action rendering a former spouse liable to the person who would have received the asset if the "divorce revokes" provision was not preempted. The Court held that the provision in the statute creating a cause of action against the former spouse was likewise preempted.

Accordingly, if a client has been divorced, he or she should be advised to review any beneficiary

[15] *See, e.g., Manning v. Hayes*, 212 F.3d. 866 (5th Cir. 2000), cert. denied, 121 S.Ct. 1401 (2001) (language in a premarital agreement not sufficiently explicit to constitute waiver); *Hurwitz v. Sher*, 789 F. Supp. 134 (S.D.N.Y 1992), aff'd by 982 F.2d. 778 (2nd Cir. 1992), cert denied 508 U. S. 912 (1995) (spouse had not waived rights to plan benefits because consent in proper form was signed before marriage and only a spouse can waive rights; antenuptial agreement after marriage did not meet requirements of statute for waiver); *Zinn v. Donaldson Co., Inc.*, 799 F.Supp. 69 (D. Minn. 1992) (language in antenuptial agreement not specific enough to constitute waiver).

[16] A client who is separated or in the process of obtaining a divorce may desire to make changes as well. As noted above, federal law may prevent changes without consent until the divorce decree is final.

[17] TEX. FAM. CODE §§ 9.301(b), 9.032(b).

[18] *Egelhoff v. Egelhoff*, 121 S.Ct. 1322 (2001).

[19] 29 U.S.C. § 1144(a).

[20] *Hillman v. Maretta*, 133 S.Ct. 1943 (2013).

designations immediately and update them as necessary.

2. Proper Form of Waiver by Spouse. In addition to being wary of "divorce revokes" statutes, one cannot always rely on the language in a decree or agreement of divorce in connection with a former spouse's rights in an asset governed by federal law.

In *Kennedy v. Plan Administrator for DuPont Savings & Investment Plan*, at Mr. Kennedy's death, his ERISA-governed savings and investment plan ("SIP") named his former spouse as the beneficiary.[21] The Court ruled that benefits should be paid to the former spouse even though the decedent had subsequently been married to another woman and the divorce decree between the former spouse and the decedent explicitly provided that the former spouse was divested of all of her rights in the SIP. The Court ruled that the waiver by the former spouse in the divorce decree was not effective because it was not in the form specifically required by the plan documents (a Qualified Domestic Relations Order, or "QDRO"). Accordingly, the benefits were properly payable to the former spouse.

In a situation such as this, presumably there would be some cause of action against the former spouse in the context of contract law. However, with regard to any non-probate asset that may be governed by federal law, the best practice would be to ensure that the instructions in the plan documents (often requiring a QDRO) are strictly followed with respect to divesting the former spouse of his or her interest in the asset.

3. Divorce Decree or Agreement Requiring Beneficiary Designation. If a client has been divorced, the divorce decree or agreement may require that the client designate his or her former spouse as the beneficiary of a non-probate asset such as a life insurance policy. Such a provision is relatively common when there are minor children involved and the client has a child support obligation to the former spouse. An attorney must be careful not to advise the client to change the disposition of an asset that may be subject to such restrictions. Therefore, it is advisable to review any documents related to the divorce that establish an ongoing obligation to the spouse.

After each of the foregoing considerations have been discussed and evaluated, the attorney can make a recommendation regarding whether each non-probate asset should be structured so that it passes to the client's estate to be distributed in accordance with his or her Will, outright to an individual or charity, or to a trustee of a trust (testamentary or otherwise).

IV. IDENTIFYING AND COORDINATING NON-PROBATE ASSETS

Before non-probate assets can be coordinated with the estate plan, they must be identified. Generally, non-probate assets are those which, at the owner's death, pass via a statutory or contractual beneficiary designation rather than pursuant to the owner's Will or under the laws of intestate succession. When most people think about non-probate assets, the assets that immediately come to mind are life insurance policies and retirement accounts. Those are the easy non-probate assets to point out to clients, because clients generally remember that some kind of beneficiary designation was required in relation to those assets. (Of course, they may not know where the beneficiary designation forms are and may only be "pretty sure" who they named as beneficiary.)

In reality, however, the universe of non-probate assets is much broader. In some circumstances, clients may not realize that their joint brokerage account held as joint tenants with rights of survivorship (or other non-probate asset) will not pass pursuant to the terms of his or her Will. It is the attorney's job to educate the client regarding how each asset will be distributed at the client's death and provide appropriate guidance.

In my experience, the most commonly unrecognized non-probate assets are multi-party accounts that are structured to pass pursuant to survivorship designations at the client's death.

A. Multi-Party Accounts.[22] Chapter 113 of the Texas Estates Code governs multiple-party accounts, which include joint accounts, pay on death (or "P.O.D.") accounts, trust accounts, and convenience accounts. Section 113.001 defines an "account" as a contract of deposit of funds between a depositor and a financial institution, and includes a checking or savings account, CD, and "other like arrangement." Chapter 113 addresses many issues associated with multiple-party accounts, including rights of survivorship, ownership during life, and ownership at death. There are special rules that govern accounts consisting of community property,

[21] *Kennedy v. Plan Adm'r for DuPont Sav. & Inv. Plan,* 129 S.Ct. 865 (2009).

[22] Portions of this section of the outline have been adapted with permission from Davis and Willms, *Planning for No Probate: Special Issues with Revocable Trusts and Nonprobate Assets*, Hidalgo County Bar Association 2013 Probate, Trust & Guardianship Law Course. Special thanks to Mickey Davis and Melissa Willms for all of their guidance and assistance in the preparation of this entire outline.

however. Ownership of community property during life is governed by relevant provisions of the Texas Family Code. Rules for how community property accounts pass with rights of survivorship can be found in Chapter 112 of the Texas Estates Code and are discussed separately below.

Please note that as used in this outline, the term "multi-party accounts" includes any accounts that involve more than one party, including joint accounts, P.O.D. or transfer on death ("T.O.D") accounts, trust accounts, and convenience accounts.

1. Accounts with Survivorship Features. In Texas, we start with the presumption that if two or more people own an asset, no survivorship right exists and they own the property as tenants in common. There must be some writing that affirmatively establishes a survivorship right among the parties.[23] If a writing exists, Chapter 113 and Subchapter B of Chapter 111 of the Texas Estates Code control, or, with regard to community property, Chapter 112 of the Texas Estates Code controls. The requirements of these sections are discussed below. The term "accounts with survivorship features" as used in this outline include not only accounts that pass pursuant to rights of survivorship, but also as a result of P.O.D. or T.O.D. designations.

a. Ownership during Life (Other than Accounts of Community Property). During the lifetimes of the joint owners, joint accounts belong to the joint owners in proportion to the sums deposited by each of them.[24]

In contrast, a pay on death (or "P.O.D.") account belongs to the original account holder or holders during his or her life or their lives, and only passes to the P.O.D. beneficiary at the death of the account holder(s).[25]

Likewise, a trust account for which no actual trust exists (e.g., an account simply styled "John Doe, Trustee for Jane Doe," commonly referred to as a "Totten trust" or "poor man's trust") belongs beneficially to the trustee and only passes to the trust beneficiary at the death of the account holder.[26] If more than one trustee is named, the beneficial rights between them are governed by the rules applicable to joint accounts.[27] A trust account in this context is not to be confused with an irrevocable or revocable trust established pursuant to a trust agreement that is separate from a deposit agreement.

Clients should be cautioned: with a multi-party account (other than a convenience account as discussed below), any party to the account may pledge the account for his or her debts.[28] The only protection is that the financial institution must provide other joint tenants (but not P.O.D. payees, beneficiaries, or convenience signers) with written notice of any pledge of the account within 30 days after the security interest is perfected.[29]

Also with multi-party accounts other than convenience accounts, funds may be withdrawn by any party in excess of his or her net contributions.[30] However, the party who makes withdrawals in excess of his or her net contributions may be liable for civil conversion or be criminally convicted of theft.[31]

b. Ownership after Death. Without any survivorship features on a joint account, when one party to a joint account dies, the decedent's interest in the account does not belong to the other party, but rather passes as part of the decedent's probate estate.

Texas Estates Code Sections 113.151 through 113.158 and 113.052 provide the requirements for establishing a right of survivorship in accounts other than community property accounts. For a joint tenancy account, Section 113.151(a) provides that there must be a written agreement between the parties, signed by the party that dies. In 2009, in *Holmes v. Beatty*, the Texas Supreme Court held that simply titling the account as joint tenants created a right of survivorship.[32] Texas Probate Code Section 439(a) (now Texas Estates Code Section 113.151(c)) was amended in 2011 to overturn this decision and to make it clear that merely titling an account as a joint account is not enough to create a right of survivorship between the joint owners. That Section provides explicit language that if included in an agreement will absolutely establish a survivorship right:

> On the death of one party to a joint account, all sums in the account on the

[23] TEX. ESTS. CODE § 101.002.

[24] *Id.* § 113.102.

[25] *Id.* § 113.103.

[26] *Id.* § 113.104.

[27] *Id.*

[28] *Id.* § 113.251(a).

[29] *Id.* § 113.251(c).

[30] *See id.* § 113.003 (For purposes of establishing net contributions, financial institutions are not required to inquire regarding the source of funds received or amounts withdrawn from a multiple-party account).

[31] *See Hicks v. Texas*, 419 S.W.3d 555 (Tex. App.—Amarillo 2013, pet. ref'd).

[32] *Holmes v. Beatty*, 290 S.W.2d 852 (Tex. 2009).

> death vest in and belong to the surviving party as his or her separate property.[33]

Substantially similar language will also act to create a right of survivorship.[34]

For a P.O.D. account, the agreement must be signed by the original payee(s), and upon the death of all original payees, the remaining funds belong to the then surviving P.O.D. payee(s).[35]

Likewise, for a trust account, the agreement must be signed by the trustee(s), and upon the death of all trustees, the then remaining funds belong to the surviving named beneficiaries. If more than one trustee is named, during the lifetimes of the trustees, the rights between the trustees are determined as for joint tenants.[36] Although no explicit provision states what happens when one trustee dies, in conformity with these provisions, the Texas Supreme Court has held that the funds did not pass to a surviving trustee who did not make any contributions to the account and the funds did not pass to the beneficiaries since a trustee was still surviving, but instead the account passed to the deceased trustee's estate.[37]

c. <u>Uniform Account Form.</u> The Texas Estates Code provides a uniform account form to conclusively establish the type of account indicated (other than community property accounts), whether it be with or without right of survivorship, and the form allows one or more convenience signers to be added to each type of account.[38] Unfortunately, despite the many safe harbors provided by Texas law, experience shows that many financial institutions do not use the specific language provided in Section 113.151 for creating rights of survivorship or the form of account agreement provided in Section 113.052.

d. <u>Community Property with Rights of Survivorship.</u> If spouses own community property with rights of survivorship in favor of the surviving spouse, Sections 112.001 through 112.253 of the Texas Estates Code control those accounts. Spouses may agree at any time that their community property will be subject to a right of survivorship in favor of the surviving spouse, as long as the agreement is in writing, <u>signed by both spouses</u>, and contains language creating the survivorship.[39] Note the distinction here from other multi-party accounts in that both spouse must sign the agreement. Section 452 of the Texas Probate Code (now Section 112.052(d) of the Texas Estates Code) was also amended in 2011 to overturn the *Holmes v. Beatty* decision discussed above so that a designation of joint tenacy is not enough to create a right of survivorship in community property.[40] Any one of four phrases will conclusively create a right of survivorship between spouses in community property:

(1) "with right of survivorship,"

(2) "will become the property of the survivor,"

(3) "will vest in and belong to the surviving spouse," or

(4) "shall pass to the surviving spouse."[41]

In addition, any agreement that "otherwise meets the requirements of this part" will create a right of survivorship.[42]

The creation of a right of survivorship does not affect the management rights of the property between the spouses.[43] Therefore, sole or joint management community property will remain so regardless of a right of survivorship.

2. <u>Default Estate Planning by Financial Institutions.</u> For estate planners, multi-party accounts with survivorship features can be frustrating. For people of modest means, who have no estate tax or other trust planning in their Wills, or for clients whose estate plan leaves all of their assets outright to adult beneficiaries, accounts with survivorship features may be fine. Many people have household checking accounts or other accounts with relatively small balances that are intended to pass outright to the surviving account holder. Survivorship features on these accounts generally do not cause a problem, so long as the account holder understands that the account will pass outright to the survivor, and not under the account holder's Will.

In a typical estate plan when trust planning or multiple beneficiaries are involved, however, it is generally best if accounts are held in a form without survivorship features. Otherwise, trusts can end up being unfunded or underfunded or the property may pass to one

[33] TEX. ESTS. CODE § 113.151(b).

[34] *Id.*

[35] *Id.* § 113.152.

[36] *Id.* § 113.153.

[37] *Stegal v. Oadra*, 868 S.W.2d 290 (Tex. 1993).

[38] TEX. ESTS. CODE § 113.052.

[39] *Id.* §§ 112.051, 112.052.

[40] *Id.* § 112.052(d).

[41] *Id.* § 112.052(b).

[42] *Id.* § 112.052(c).

[43] *Id.* § 112.151.

beneficiary when the decedent intended to benefit more than one beneficiary. Who hasn't heard clients say that if they name Child A as the beneficiary of an account, Child A will just take care of everything and will make sure and share the account with the rest of his or her siblings?

Unfortunately, many advisers at banks and other financial institutions furnish these accounts with survivorship features thinking that they are convenient for their clients without recognizing that such designations can thwart an otherwise sound estate plan. After death, it may not be possible to remedy these accounts, even by disclaimer, as discussed further below. Even with disclaimer as an option, the added expense and hassle may frustrate clients. Since most clients are naïve regarding these issues, it is important to advise them how to correctly title their accounts.

3. Changing Multi-Party Accounts to Remove Survivorship Features. Many clients are unaware of their account designations, and the account designations should be reviewed during the estate planning process. Bank or brokerage statements may indicate survivorship language on their account statements. Joint accounts often list two names, followed by the designation "JTWROS," "Jt. w/ Surv.," or with some other indication of survivorship. The account may also list one name, followed by the designation "P.O.D.," "T.O.D.," or with some other indication of survivorship. However, not all accounts with survivorship features are so clearly labeled. Survivorship is governed by the account agreement or signature cards that were signed when the account was opened (or when someone's name was added to the account). The terms of the account agreement or signature card, and not the names listed on the account statement, establish survivorship.

If necessary as part of the estate plan, the financial institution should be contacted to eliminate any survivorship designation.

Some financial institutions have proven uncooperative in altering these designations, based apparently on the well known legal maxim "that's the way we always do it. There's no reason for it, it's just our policy." Section 113.157 of the Texas Estates Code, however, allows any party to a survivorship account to alter its effect by written order received by the financial institution. The order must be signed by a party, received by the financial institution during the party's lifetime, and not countermanded by another written order of the same party during the party's lifetime.[44] With regard to a survivorship account between spouses of community property, a written agreement that does not provide another method of revocation must be signed by both spouses or one spouse must sign the agreement and deliver it to the other spouse.[45] Accordingly, if a written order to a financial institution is made with respect to such an account, both spouses should sign the document.

An example of a letter to a financial institution ordering that an account not include any right of survivorship is attached as "Exhibit A." Presumably, sending the letter by certified mail, return receipt requested, would satisfy any burden of proof with respect to this receipt requirement. The return receipt and copy of the letter should be retained by the client with his or her other estate planning documents.

Most account agreements contain a provision regarding governing law or choice of law. Texas law may prohibit a bank from enforcing the laws of another state if the branch or a separate office of the bank that accepts the agreement is located in Texas.[46] However, if an account agreement directs that the laws of a state other than Texas control, the client may find it difficult or impossible to remove survivorship provisions from multi-party accounts. This is especially true with the proliferation of online banking.

For example, in its deposit agreement effective as of December 7, 2013, Ally Bank, a popular online bank, provides that "all joint accounts are titled as joint tenants with right of survivorship."[47] The agreement further provides that all of Ally Bank's actions relating to the account "will be governed by the laws and regulations of the United States and, to the extent not preempted, the laws and regulations of the State of Utah."[48] Accordingly, a written order to Ally Bank pursuant to Texas Estates Code Section 113.157 may not be effective to remove a right of survivorship provision. Anecdotally, I have also been told that GE Capital Bank account agreements have similar provisions with regard to joint accounts.

If a client has contacted a financial institution to eliminate a right of survivorship designation and has not been successful, the account agreement should be obtained and reviewed. An account agreement such as the one at Ally Bank may necessitate moving funds on deposit from the financial institution or changing the

[44] *Id.* § 113.157.

[45] *Id.* § 112.054.

[46] *See* TEX. BUS. & COM. CODE § 4.102(c).

[47] Ally Bank Deposit Agreement and Disclosures (2014); www.ally.com/resources/pdf/bank/ally-bank-deposit-agreement-2013-12-07.pdf.

[48] *Id*.

account to name only one account holder. Of course, clients attracted to a specific financial institution due to their interest rates or convenience may resist such a change. It is important for attorneys to advise clients of the impact of these issues on their estate plans.

4. Alternative to Accounts with Survivorship Features. If a client would like one or more friends or family members named on his or her account for purposes of convenience, or in the event of the client's disability, the best alternative may be to establish the account as a "convenience" account. A convenience account allows an account holder to name someone to sign on the account but gives no right of ownership or right of survivorship to the convenience signer.[49] In addition to not establishing a right of survivorship with the convenience signer, and in contrast to other multi-party accounts, the convenience signer may not pledge the account for his or her debts.[50] When the owner dies, his or her interest in the account passes under his or her Will or pursuant to the laws of intestate succession. If properly styled as a convenience account, an account does not give rise to the problems associated with accounts with survivorship features. Unfortunately, not every financial institutuion provides this option.

B. Securities and Contracts Other than Deposits of Funds. Section 111.052 of the Texas Estates Code covers a myriad of contracts, including insurance policies, employment contracts, promissory notes, retirement accounts, securities, and accounts with financial institutions. That Section states that if any of these contracts are at issue, the Texas Estates Code will not invalidate any provision in a written agreement related to these contracts that makes the account nontestamentary because of a right of survivorship, forgiveness of debt, or beneficiary designation.[51] In other words, the contract rather than the statutes control.[52]

Assets that are transferred pursuant to beneficiary designations include, but are not limited to: life insurance policies on the client's life, qualified or non-qualified retirement plans and Individual Retirement Accounts (IRAs), including rollover IRAs, in which the client is the participant, tax deferred annuities in which the client is the annuitant or owner, and immediate annuities in the client's name. Throughout this discussion, the term "sponsoring company" refers to the insurance company in the case of an insurance policy or annuity on the client's life, the administrator of the retirement plan in which the client participates, the custodian or trustee of the client's IRA or IRA rollover, or any other institution responsible for the administration of a non-probate asset requiring a beneficiary designation.

The beneficiary designation form, when properly completed and returned to the sponsoring company, is simply a contract between the client and the sponsoring company in which the sponsoring company agrees to pay the benefits to the named beneficiary at the time of the client's death. Because payment of these benefits is based upon contract law, all of the requirements imposed by the sponsoring company must usually be met in order for the contract to be honored. For example, the sponsoring company will frequently require that the beneficiary designation be made on the company's own form and delivered to the company on a timely basis.

Accordingly, for every asset that passes pursuant to a beneficiary designation, a change of beneficiary form should be obtained from the sponsoring company.

1. Absence of Beneficiary Designation. If the client fails to complete a beneficiary designation form, distribution of the asset at the client's death will be subject to the fine print in the sponsoring company's contract with the client. The contracts of sponsoring companies vary greatly, and accordingly, disposition of non-probate assets in the absence of a beneficiary designation vary as well. In many cases, the client's estate becomes the default recipient of property if no beneficiary has been named. In other cases, the client's spouse or children may be the default recipients, which may not align with the client's wishes, especiall when minor children are involved.

2. Naming Contingent Beneficiaries. Note that, in many cases it should be recommended that the client name both a primary and a contingent (secondary) beneficiary of each non-probate asset for which a beneficiary designation is required. This is because (i) something could happen to both the client and the named primary beneficiary, in which case the contingent beneficiary will become the primary

[49] TEX. ESTS. CODE §§ 113.105, 113.106, 113.154.

[50] *Id.* § 113.251(b).

[51] *Id.* § 111.052.

[52] Financial institutions are defined in Texas Estates Code Section 113.001 to include brokerage firms. This creates some murkiness and begs questions as to whether the earlier mentioned provisions of the Texas Estates Code apply to these types of accounts when securities rather that cash are held in the accounts and what provisions apply when both cash and securities are held in these accounts. Unfortunately, no clear answers exist. For an excellent discussion of the issues and case law that has seemingly ignored the distinction, see Karisch, *Multi-Party Accounts and Other Non-Probate Assets in Texas* (2011).

beneficiary, or (ii) if the primary beneficiary survives the client, naming a contingent beneficiary will give the primary beneficiary additional options through disclaimer.

It is not typically necessary to name a contingent beneficiary if the primary beneficiary is the Trustee under the client's Will or revocable trust. However, if the sponsoring company insists on a contingent beneficiary, in most circumstances it may be acceptable to name the client's "Estate" as the contingent beneficiary.

3. Problems that Sometimes Arise when Trusts are named as Beneficiaries. In many situations, the client's estate tax, creditor protection, and distribution goals will best be accomplished by naming the trustee of a trust as the beneficiary of a non-probate asset. In discussions with clients, attorneys often refer to "naming a trust" as the beneficiary as a form of shorthand. However, trusts are not legal entities that can hold title. Accordingly, the trustee of the trust should be named on each beneficiary designation form. Often, the trusts into which these assets are passing are testamentary trusts, and the proper beneficiary designation is **"The Trustee(s) named in the Will of [Name of Client]"** or **"The Trustee named in the [Revocable Trust],"** as applicable. However, when clients attempt to submit beneficiary designation forms with this language, they sometimes run into trouble. Some of the commonly encountered problems and possible solutions are listed below.

a. The sponsoring company wants the Trustee's name listed. Some sponsoring companies do not like a generic designation of the Trustee named in the client's Will or revocable trust. Rather, they insist on having the actual name of the Trustee listed. While the client's estate planning documents will likely name a primary Trustee and provide for alternate Trustees who will serve in the event that the primary Trustee fails or ceases to serve, until the time of the client's death, there is no way to know who, in fact, will be serving as the Trustee. Although you could try to explain this to the employee of the sponsoring company who is making the request, in our experience, bureaucrats are often very inflexible. As an alternative to the generic designation recommended to the client whose estate planning is through a Will, the client may designate his or her primary Trustee by name, as the Trustee in his or her Will, followed by "(or his/her successor)." For example, John Doe has named Jane Doe as the primary Trustee in his Will. Therefore, he would word his beneficiary designation as follows: "Jane Doe, Trustee under the Will of John Doe (or her successor)."

b. The sponsoring company wants the date of the Will listed. Some sponsoring companies want the date the client's Will was signed included in the beneficiary designation. If required, it is generally not a problem to include the date of the Will. However, clients should be advised that the beneficiary designation should be updated each time a new Will or other estate planning document impacting the non-probate asset is signed.

c. The sponsoring company insists on a time limit for probating the Will. Some sponsoring companies want to add a provision to a Trustee beneficiary designation stating that the benefits will only be paid to the Trustee under the Will if the Will is probated within a certain number of months. Generally, this is fine. Of course, the client's family or other people involved in the client's estate plan will need to be sure that the Will is actually probated within the specified time period.

d. The sponsoring company asks for additional beneficiary information. Some sponsoring companies also want additional information regarding the named beneficiary, such as current address, relationship, social security number, date of birth, etc. If the client is naming his or her spouse or any other individual as a beneficiary, the requested information should be included. However, if the client is naming the Trustee in his or her Will as a beneficiary, this information is mostly inapplicable. This may be indicated on the form by entering "N/A" where appropriate.

e. The beneficiary designation form is not consistent with the attorney's instructions. Most beneficiary designation forms are structured so that the words "Primary Beneficiary" appear first, followed by a space to provide the appropriate name(s). These forms then have a second section entitled either "Contingent Beneficiary" or "Secondary Beneficiary," followed by a space to list the name(s). It is possible, however, to encounter a form that is not set up in this manner (such as a form containing preprinted beneficiary designation options with boxes that must be checked). If there is an option to choose "other," that should be done with an indication to see an attachment on which primary and contingent beneficiaries can be named as recommended by the attorney. If the client is unable to determine how to complete a form, however, the client should reach out to the attorney for assistance. An attorney's participation in completing the paperwork to coordinate non-probate assets is discussed below.

4. Delivering Beneficiary Designations. Once a beneficiary designation form has been completed, the

completed form must be returned to the sponsoring company according to its instructions.

a. Online Submission. Many sponsoring companies now allow beneficiary designation forms to be submitted online. If a form is returned to a sponsoring company in this manner, a copy of the confirmation page or page indicating the revised beneficiary designations should be printed and retained by the client with his or her other estate planning documents. If the form is submitted via email, the email should request written confirmation of receipt.

b. Submission Via Fax or Mail. If a beneficiary designation form is submitted via mail, it should be sent by certified or registered mail with a return receipt requested. An example of a letter transmitting a beneficiary designation to a sponsoring company is attached hereto as "Exhibit B." The return receipt and copy of the letter transmitting the completed beneficiary designation should be retained by the client with his or her other estate planning documents. If a beneficiary designation form is sent via fax, a copy of the fax transmission sheet should be retained in the same manner. In our experience, if proof is given to a sponsoring company that it received the beneficiary designation form, the beneficiary designation form will be honored.

5. Following Up. A transmission to a sponsoring company of a completed beneficiary designation form (whether by email, fax, or mail) should always request written confirmation from the sponsoring company that a change has been made. Once written confirmation is received from the sponsoring company, it should be retained with the client's other estate planning documents.

If confirmation that the change has been made is not received within a reasonable period of time (e.g., two weeks), the client should follow up to ensure that the change has been made. Often, beneficiary designations can be viewed online. However, if the beneficiary designation is not available online, the sponsoring company should be contacted to inquire whether the change has been made and to ask for written documentation regarding the same.

C. Real Property Held with Survivorship Features. In Texas, it is uncommon for real property to be held with survivorship features. However, in many other states, it is customary for joint owners to hold real property in a way that creates some right of survivorship between them. If the client owns real property in a state other than Texas or in any other foreign jurisdiction, it is prudent to request a copy of the deed to the property so that a determination can be made regarding whether the property is held with rights of survivorship.

1. Tenancy by the Entirety. Although it is not a form of ownership recognized in Texas, real property in many states may be held as a tenancy by the entirety.[53] Tenancy by the entirety is a type of shared ownership of property available only to married couples. Generally, a husband and wife (or same-sex spouses in states where same-sex marriage is recognized) who own property as tenants by the entirety each own an undivided interest in the property, each have full rights to occupy and use the property, and each have a right of survivorship in the property, so that upon the death of one of the spouses, the survivor is entitled to the decedent's share.

2. Evaluating and Removing Real Property Survivorship Features. Several considerations must be made when advising clients regarding real property held in tenancy by the entirety or with other survivorship features. For clients with estate tax or other trust planning in their Wills or revocable trusts, the inclination may be to change how the property is held so that no survivorship feature exists. However,

[53] States that recognize tenancy by the entirety include Alaska (ALASKA STAT. § 34.15.140), Arkansas (*See Ford v. Felts*, 624 S.W.2d 449 (Ark. Ct. App. 1991)), Delaware (*See Citizens Sav. Bank, Inc. v. Astrin*, 61 A.2d 419 (Del. Super. Ct. 1948)), Florida (FLA. STAT. § 655.79), Hawaii (HAW. REV. STAT. § 509-2), Illinois (ILL. COMP. STAT. 65/22), Indiana (IND. CODE ANN. § 32-17-3-1), Kentucky (KY. REV. STAT. ANN. § 381.050), Maryland (MD. REAL PROP. CODE ANN. § 4-108); Massachusetts (MASS. ANN. LAWS ch. 209 § 1); Michigan (*See Butler v. Butler*, 332 N.W.2d 488 (Mich. Ct. App. 1983)), Mississippi (MISS. CODE ANN. § 89-1-7), Missouri (MO. REV. STAT. § 442.025); New Jersey (N.J. STAT. ANN § 46:3-17.4), New York (NY CLS REAL PROP. §240-b), North Carolina (N.C. GEN. STAT. § 39-13.3), Ohio (OHIO REV. CODE ANN. § 5302.21, *See Cent. Benefits Mut. Ins. Co. v. Ris Adam'Rs Agency*, 637 N.E.2d 291 (Ohio 1994)), Oklahoma (OKLA. STAT. tit. 60 § 74), Oregon (OR. REV. STAT § 91.020) Pennsylvania (69 PA. STAT. ANN. § 541), Rhode Island (*See Bloomfield v. Brown*, 25 A.2d 354 (R.I. 1942)), Tennessee (TENN. CODE ANN. § 66-1-109), Vermont (VT. STAT. ANN. tit. 15 § 67), Virginia (*See Rogers v. Rogers*, 512 S.E.2d 821 (Va. 1999)), Wyoming (WYO. STAT. ANN. § 34-1-140), and the District of Columbia (*See Travis v. Benson*, 360 A.2d 506 (D.C. 1976)).

tax advantages and trust protections must be weighed against the benefits of holding real property in a manner that provides a survivorship feature. If ownership of the real property would require a costly and cumbersome probate procedure in the state where the property is located, the client's interests may best be served by maintaining the survivorship feature to avoid probate. Additionally, under a tenancy by the entirety, it is typical that creditors of an individual spouse may not attach and sell the interest of a debtor spouse: only creditors of the couple may attach and sell the interest in the property owned by tenancy by the entirety. If the client has concerns about creditors, it may be prudent for the real property to be maintained in tenancy by the entirety.

If it is ultimately determined that changing the way that real property is held in order to eliminate survivorship features is the best course of action, generally a filing must be made in the real property records where the property is located to reflect the change. The requirements of such a filing in the jurisdiction where the property is located should be researched, and a deed or other document should be prepared and filed accordingly. If local counsel does not prepare the document, local counsel should at least review the document before it is filed.

V. THE ATTORNEY'S ROLE

So what is the role of an attorney preparing a client's estate plan in all of this? How far must the attorney go to ensure that non-probate assets are properly coordinated with the estate plan? Certainly an attorney should ask about the client's non-probate assets and educate and advise clients regarding the disposition of non-probate assets. However, the extent of the attorney's actual participation in the activities required to coordinate non-probate assets should be determined by the individual attorney and his or her client and should be addressed in the engagement agreement between them.

A. Gathering Information. Before the initial meeting, if feasible, or during the initial meeting, the attorney should gather as much information as possible regarding the client's assets in order to identify each non-probate asset. A helpful way to request this information is to ask that a client complete a data-gathering form. The data-gathering form can request personal information about the client, the client's family, and others who may be involved in the client's estate plan, and any other information that will help the attorney to better understand the client's goals regarding disposition of his or her estate. The data-gathering form should also request information about the client's assets which will assist the attorney in identifying any non-probate assets. An example of the portion of a data-gathering form relating to the client's assets is attached hereto as "Exhibit C."

To avoid overwhelming clients with requests for information, the sample excerpt is not designed to gather all of the information that the attorney will need to evaluate and coordinate each non-probate asset. Rather, the sample form requests just enough information to alert the attorney that a certain type of non-probate asset exists (e.g., the client owns life insurance on his or her life). During the initial meeting, the attorney can gather additional information about each non-probate asset that will be required when advising clients about coordinating those assets with the overall estate plan (e.g., How many life insurance policies are there, and in what amounts? Are the policies term or whole life policies? Are they provided by the client's employer, which may rise to federal law issues? Who are the named beneficiaries of each policy?).

In addition to requesting information about the client's assets, a data-gathering form should inquire about circumstances which may influence the way non-probate assets are handled. For example, if the client has been divorced, a divorce decree or agreement incident to divorce may subject the client to an ongoing obligation to a former spouse, or may direct that the client hold life insurance naming the former spouse as a beneficiary. A client may be subject to a buy-sell agreement that requires the ownership of life insurance. It is important to identify each source of such an obligation and review the document imposing the obligation.

B. Educating the Client about Non-Probate Assets. Even if a client has completed a beneficiary designation form with regard to a non-probate asset, he or she may not understand that signing a Will or revocable trust does not direct the disposition of all of his or her assets.

The attorney must take the time to educate the client regarding what assets in his or her estate are non-probate assets, the considerations that are involved in directing the disposition of those assets, and the practical steps for coordinating non-probate assets with the overall estate plan.

C. Participation in Coordination of Non-Probate Assets. The engagement agreement between the attorney and client should make clear whether the active coordination of non-probate assets (such as completing beneficiary designation forms) is included in the engagement, or whether it will be undertaken by the attorney only at the explicit request of the client.

Our firm's typical engagement agreement states that we will assist the client with the preparation of beneficiary designation forms for their non-probate assets only to the extent that they request us to do so. If the fee quoted for preparing estate planning is a "fixed fee," the agreement explicitly states that the fixed fee will not cover drafting or reviewing actual beneficiary designations, but that if such a service is requested, additional fees will be charged based on our standard hourly fees.

If the attorney is engaged to complete or review beneficiary designation forms and otherwise actively coordinate non-probate assets, the attorney should communicate with the client regarding the extent of his or her participation. For example, the attorney should either commit to following up with each sponsoring company to ensure that beneficiary designations have been changed as requested, or should advise the client that the client will be responsible for doing so.

If a client has a relationship with a financial advisor or financial planner, it is often helpful to take a team approach to coordination of non-probate assets. Often, the financial advisor will have direct access to financial institutions and will be familiar with the forms and paperwork required. If the client consents, the attorney should communicate with the financial advisor so that he or she can take an active role.

D. Providing Clients with Tools to Coordinate Non-Probate Assets. Regardless of whether or not a client requests that the attorney assist with the active coordination of non-pronate assets, the attorney should provide clients the necessary tools to coordinate non-probate assets on their own. After clients leave our offices, their assets seldom remain static. For example, a client may acquire new life insurance polices, roll over an employer-sponsored retirement plan to an IRA, or inherit an IRA. In those situations, it is helpful for clients to have a clear set of instructions regarding how to handle the paperwork involved in coordinating non-probate assets with their estate plan.

During the initial meeting and when drafts of estate planning documents are sent to our clients, we advise them that they should begin gathering beneficiary designation forms and checking accounts for survivorship designations. When clients come to our office to sign their estate planning documents, if appropriate, we provide them with a memorandum regarding the coordination of non-probate assets with their estate plan. The memorandum contains some of the information set out in this outline, including what constitutes a non-probate asset, steps to follow, sample language to be used on beneficiary designation forms, and tips for troubleshooting issues that sometime arise in connection with changing the beneficiary designations. If necessary, included with the memorandum is a chart specific to the client showing recommended beneficiary designations. Examples of charts that may be provided to clients who are married and who have employed "disclaimer bypass" trusts or typical tax planned trusts in their Wills are attached as "Exhibit D" and "Exhibit E," respectively. Charts such as these should not be generic, but rather should be tailored to meet each client's needs.

Providing these written recommendations and instructions to the client is a best practice for an estate planning attorney. Although preparation of the written material and tailoring the material for each client takes time, it provides untold additional value, and our clients are always extremely appreciative of the effort.

VI. POST-MORTEM REMEDIES IF NON-PROBATE ASSETS ARE NOT CORRECTLY COORDINATED

Hopefully, at a person's death, all of his or her non-probate assets will have been perfectly coordinated with his or her overall estate plan. However, many times, this will not be the case. If at a person's death, his or her non-probate assets have not been correctly coordinated with the estate plan, there are a few post-mortem actions that can be taken to remedy the situation.

A. Scrutinize Account Agreements. If a multi-party account is at issue, the account agreement or signature card governing the account should be scrutinized. As mentioned above, although the Texas Estates Code provides a uniform account form, experience shows that many financial institutions do not use the specific language provided. As a result, the language on the account agreement or signature card may be insufficient to create a right of survivorship, especially in light of the relatively recent changes to the statutes as a result of the decision in *Holmes v. Beatty*.

If that is the case, the decedent's portion of the account may pass as part of the decedent's probate estate. The personal representative may contact the financial institution to collect the assets and explain to the proper representative of the financial institution (generally in the legal department) that the account agreement or signature card does not create a right of survivorship. I have had several experiences with smaller, local banks in which the banks have conceded that the language on their form was not sufficient to create a right of survivorship under Texas law and have acknowledged the estate's ownership. However, some financial institutions are not as easy to reason with. In those circumstances, if the other party to the account understands the law and receives the decedent's portion of the account from the financial institution, upon receipt, that party may deliver the funds or assets to the personal representative of the estate as the proper owner.

B. Consider Disclaimers. If a person is the proper recipient of a non-probate asset (as a result of a right of survivorship, beneficiary designation, or otherwise), he or she may have an option to disclaim (i.e., renounce) his or her right to receive the property or any portion of the property.

If an asset or any portion of an asset is disclaimed, it will pass as if the disclaiming party predeceased the decedent.[54] Accordingly, before disclaimer is recommended, a determination should be made regarding what would happen and who would receive the disclaimed asset as a result of the disclaimer. Successive disclaimers might need to be made by multiple parties if necessary to obtain the desired disposition of the property.[55]

A disclaimer is a complete renunciation of property and to be valid in Texas must be made in accordance with Chapter 122 of the Texas Estates Code. For the disclaimer to be a qualified disclaimer pursuant to federal law, the disclaimer must also be made in accordance with Section 2518 of the Internal Revenue Code. Although currently, the requirements under Texas Estates Code Chapter 122 and Internal Revenue Code Section 2518 are similar, there are some differences, so each should be reviewed at the time of disclaimer to ensure full compliance with both.

Chapter 122 of the Texas Estates Code requires the following for a disclaimer to be effective.

1. The disclaimer must be in writing and notarized.[56]

2. It must include a statement regarding whether the disclaimant is a "child support obligor," even if the disclaimant has no minor children.[57] This is a new requirement, effective as of January 1, 2014, so any forms used in connection with the disclaimer should be scrutinized to ensure that they include this statement.

3. It must be filed not later than 9 months after the decedent's date of death[58] in the decedent's probate proceeding,[59] except in some cases it must be filed with the county clerk's office in the county of the decedent's residence[60]or filed with the county clerk of the county in which real property owned by a non-resident decedent is located.[61]

4. In addition to the filing requirement, it must be delivered in person to, or mailed by registered or certified mail to and received by, the legal representative of the transferor of the interest or the holder of legal title to the property within 9 months of the decedent's death.[62]

5. The disclaimant must not have "previously accepted the property by taking possession or exercising dominion and control of the property as a beneficiary."[63]

For a disclaimer to be qualified under Section 2518 of the Internal Revenue Code, the following requirements must be met.

1. The disclaimer must be in writing.[64]

2. It must be received by the transferor of the interest, his legal representative, or the holder of the legal title to the property to which the interest relates not later than 9 months after the day on which the transfer creating the interest is made.[65] If the disclaimant is receiving non-probate property as a result of a person's death, the date of the transfer creating the interest is generally the decedent's date of death.

3. The disclaimant must not have previously accepted the interest or any of the benefits of the property.[66]

---

[54] TEX. ESTS. CODE § 102.101.

[55] *See id.* § 122.103.

[56] *Id.* § 122.051(a).

[57] *Id.* § 122.051(b).

[58] *Id.* § 122.055(a). There are some exceptions to the 9-month rule in the case of a future interest or if the disclaimant is a charity. *Id.* § 122.055(b-c).

[59] *Id.* §122.052.

[60] *Id.* §122.053.

[61] *Id.* § 122.054.

[62] *Id.* §122.056(a)(1). Again there are exceptions to this rule in the case of a future interest or if the disclaimant is a charity. *Id.* 122.056(a)(2), (c).

[63] *Id.* §122.104.

[64] I.R.C. § 2518(b)(1).

[65] *Id.* § 2518(b)(2). If the person receiving the interest is under the age of 21 at the decedent's death, the disclaimer must be made within 9 months of the day on which such person attains age 21.

[66] *Id.* § 2518(b)(3).

4. The disclaimed property must generally pass in a manner that the disclaiming party will not benefit from the property.[67] An important exception to this rule, however, permits the surviving spouse to disclaim property and still retain benefits from a trust into which the property may pass.[68]

5. The disclaimed property must pass without direction or control of the disclaiming party.[69] This requirement may prevent a disclaimant from serving as a trustee of any trust into which the assets are disclaimed, unless the trustee's powers are appropriately restricted. If the trust contains unduly broad powers, other family members or a professional trustee may serve as trustee.[70] This restriction also prevents a trust beneficiary from retaining a power of appointment over the trust property.

C. Equalization by Beneficiaries. A recipient of a non-probate asset may be altruistic enough to voluntarily distribute the proceeds of the asset among others if he or she believes that was the decedent's intent. Similarly, if there are debts, expenses, or taxes payable by the estate, the recipient may desire to pay his or her "share." While the recipient's goodwill may be utilized to effectuate the decedent's intent, people who desire to take such equalizing actions should be aware of gift tax consequences that may arise as a result.

If any amount is given outright to another person, it will be a gift from the original recipient for federal gift tax purposes.[71] If debts, expenses, or taxes are paid by the original recipient that he or she is not obligated to pay, the amount paid will be deemed to be a gift to the people from whose share the amounts should have been paid.

The federal transfer tax system imposes a tax on the right to transfer assets by gift.[72] Annual gifts of up to $14,000 per donee can be made without any gift tax consequences and without the necessity to file a federal gift tax return.[73] This $14,000-per-donee amount is referred to as the "annual exclusion." However, if the amount given to any one donee is in excess of the annual exclusion, the donor will be required to file a federal gift tax return and the amounts given in excess of the annual exclusion will reduce the person's lifetime gift tax exemption ($5,340,000 for 2014), or, if the lifetime Gift Tax exemption has been used, the amounts will be subject to Gift Tax with a top marginal rate of 40%.

VII. CONCLUSION

The best result can be achieved for our clients when clients coordinate their non-probate assets with their overall estate plan. An attorney advising clients in this area should be knowledgeable about the myriad of issues and considerations associated with non-probate assets and should be able to identify clients' non-probate assets and educate clients regarding those assets.

Additionally, the attorney should put into place purposeful policies and practices in order to facilitate the collection of information about clients' non-probate assets, to set clear guidelines regarding responsibilities for coordination of non-probate assets, and to ensure best practices in the practical actions involved in coordination of the non-probate assets if they are engaged to do so.

If non-probate assets are not properly coordinated, there are some post-mortem actions that can be taken in an attempt to align the non-probate assets with the overall estate plan. However, these post-death fixes are not always available, and the best result will be achieved if the disposition of non-probate assets is carefully considered and coordinated in connection with the estate plan at the outset.

[67] *See id.* § 2518(b)(4).

[68] *See id.*, Treas. Reg. §§ 25.2518-2(e)(5) Examples (4)-(6).

[69] I.R.C. § 2518(b)(4).

[70] *See* Treas. Reg. §§ 25.2518-2(e)(2), (e)(5) Examples (4)-(6).

[71] Note that the use of a disclaimer to equalize is not considered a gift by the disclaimant.

[72] I.R.C. § 2501(a)(1).

[73] *Id.* § 2503(b). While the Internal Revenue Code states that the annual exclusion is $10,000 per donor per donee per year, the Taxpayer Relief Act of 1997 provides for an inflation adjustment of this amount beginning in 1999, with the adjustment rounded to the next lowest $1,000.