Ancillary Methods of Probate Avoidance

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Regardless of the estate size, a Revocable Living Trust (RLT) addresses virtually every basic estate planning need in providing the privacy, convenience, practicality, safety, aggregation, and control that everyone wants. The cost savings and administrative efficiencies associated with a funded RLT are well established, undisputed facts – particularly in the matter of probate avoidance. And for the astute asset owner who wants to do it right, a living trust should always be the *foundational* estate planning tool <u>including</u> for those who may have already employed ancillary probate-avoidance methods such as "Payable on Death" (POD) and/or "Transfer on Death" (TOD) accounts.

Avoiding Probate is the Goal

Whether the probate-avoidance design is (i) a Joint Tenancy with Right of Survivorship (JTWROS) property deed or (ii) a POD/TOD account, there is only one reason for those structures to be utilized, and that is to avoid probate at the decease of the asset owner. Those methods do avoid probate, and that is good, but when closely examined, potential problems become apparent when such are used instead (or outside the aggregative features) of a Revocable Living Trust.

Problems with Non-Spousal JTWROS Ownership

With the exception of "tenants-by-the-entirety" structures between a (legally married) husband and wife, when anyone enters into a JTWROS type of ownership of an asset with another – whether an adult child, a sibling, a friend, or a business associate – they are subjecting themselves to the possibility of *total forfeiture* of that property. Regardless of the jurisdiction where the property is located, each respective tenant in a JTWROS ownership arrangement is deemed to own 100% of the property for creditor payment purposes. In other words, if a child whose name was on a JTWROS deed were to get sued (or involved in a divorce settlement), the parent could lose the entire property to satisfy the legal claim.

In addition, problems can arise if an unprepared JTWROS tenant were to become incapacitated prior to the time when the sale of the subject property became necessary since a sale would require the conveyance of both owners. In such case, the other (non-incapacitated) tenant would need to arrange for a court-appointed conservatorship over the incapacitated tenant in order to sell the property.

Ownership by JTWROS between non-spousal tenants is generally a bad idea. And that is especially so when considering such an arrangement is entirely unnecessary when a living trust works much better to provide the desired end result.

POD/TOD Plans Avoid Estate Settlement Problems. Right?

Ancillary POD & TOD arrangements are essentially the same in their primary functions (PODs are typically offered through banks and TODs through investment institutions), which is to avoid probate of the account upon the owner's decease. Such arrangements are easy and inexpensive to create. The account owner names a beneficiary(s) to take title of the account immediately upon his decease; probate of the account is avoided.

So, what could possibly go wrong?

First, it should be understood that financial institutions provide these services solely as a front-end incentive to draw (and keep) clientele. They are not helping to establish an effective personal estate plan in the client's best interests, nor can they. Moreover, those institutions offering such probate-avoidance "features" generally don't disclose to the account owner (unless by fine print) that with the POD/TOD arrangement(s) he could actually be creating a "new set of circumstances" that could make for an <u>undesirable</u> outcome – upon the account owner's decease – now after the POD/TOD account-transfer planning has been employed.

More Consideration is Often Necessary

In fact, the likelihood is that such type of minimally-contemplative "estate planning" will produce adverse circumstances for the executor/trustee who is settling the estate of the well-meaning, howbeit uninformed, account owner. In addition, POD/TOD account usage alone can create other undesirable outcomes such as unintentionally disinheriting grandchildren, payouts becoming vested at an inopportune time (e.g., during a divorce or bankruptcy proceeding, or under any other unforeseen, legal-liability condition that may garnish a beneficiary's receipts – *all of which a trust can prevent*).

POD Plans are Common (and Numerous)

Realize that Payable on Death (POD) structures are not exclusive to banks and the account services they offer. POD arrangements are actually very common and are a prominent feature of many other assets such as (i) life insurance policies, (ii) beneficiary deeds, (iii) certain life estate deeds, (iv) traditional & Roth IRAs, (v) defined contribution (401k) & defined benefit plans, (vi) tax sheltered 403[b] annuity plans, (vii) qualified & non-qualified annuities with remainderman interests, and the like.

All of these POD-featured accounts certainly avoid probate. But they often end up being conveyed **outside the control** of the account owner's core estate plan, which is potentially problematic and should be avoided. The wise and simple solution is to make all such accounts payable to a Revocable Living Trust.

Other Negatives of "Stand-Alone" POD/TOD Planning

When reference is made to a POD account as "standing-alone", that means that it will be conveyed/administered outside of the control otherwise imparted unto the account owner's executor/trustee. A stand-alone POD account cannot be administered by the account owner's executor since it avoids probate; only assets subject to probate are administered by an executor. And it cannot be administered by the account owner's trustee if the account owner does not have a trust, or the account is not payable to his trust. So why can this be a problem?

Federal Regulations can be a Factor

For starters, let's look as the federal estate tax recovery rules – as recorded in Internal Revenue Code (IRC) §2207 – concerning liability imposed upon a recipient of property who (as a classic example) would be a POD/TOD beneficiary(s) receiving a distribution from an account *outside* of a will or trust:

> *"Unless the decedent directs otherwise in his will, if any part of the gross estate on which the tax has been paid consists of the value of property included in the gross estate under section 2041, the* executor *shall be entitled to recover from the person receiving such property… such portion of the total tax paid as the value of such property bears to the taxable estate. If there is more than one such person, the* executor *shall be entitled to recover… in the same ratio."*

This IRC §2207 rule means that unless the decedent's will or trust expressly waived the "right to recover" from a POD/TOD beneficiary receiving an otherwise "tax free" distribution outside of the will or trust, he may find himself owing a significant sum of money back to the estate – some or all of which may have already been spent! That's because, in such case, the trustee/executor administering the decedent's estate would be legally obligated to obtain a "payback" from the POD/TOD beneficiary(s). Where a state and/or federal transfer tax has been imposed upon a decedent's estate, the consequence of such a condition could obviously turn into a significant problem including the requirement of imposing legal, court-ordered solutions.

The Convenience/Safety of Asset Aggregation is Forfeited

Then, there are the complications associated with the prorated equalization among all of the decedent's beneficiaries including those receiving POD/TOD type of distributions *outside* of the decedent's trust. That can turn what could have been an easy, aggregated settlement for the trustee into a chaotic and time-consuming experience, or worse.

Durable POAs are Often Restricted

With a POD or TOD account, a Financial Power of Attorney would be required to have another person handle the account. Financial institutions are often times reluctant to accept powers of attorney for their various "in house" and/or other technical reasons. On the other hand, a funded Revocable Living Trust (RLT) allows the asset owner to plan for incapacity, and if the grantor/creator of the RLT becomes incapacitated, the successor trustee can assume management of the account for the benefit of the creator.

There is One Way to do it Right

An RLT allows one to carefully and systematically plan for specific beneficial allocations, including for contingency distributions, and to make changes whenever necessary (which is particularly the case with "The eStatePlan" provided with the ITS platform). if the beneficiaries are minors, have special needs, have creditor issues, or have mental health or substance abuse issues, trusts can hold and manage assets to protect those assets for such beneficiary's uncontrolled and unrestricted use.

In addition, inheritances can be managed over years or decades with a trust, even to second and third generations (or more). That's not possible with the stand-alone use of traditional POD/TOD accounts.

The primary missing ingredients with POD/TOD planning is the lack of aggregation and control… otherwise available with a Revocable Living Trust. Here is the takeaway:

There is no substitute for a properly implemented, fully funded
REVOCABLE LIVING TRUST ESTATE PLAN