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Back to the Basics: How Do Assets Pass at the Death of the Owner?

By Richard M. Morgan & Loraine M. DiSalvo

Have you heard of a situation where a deceased person's former spouse ended up receiving his life insurance or retirement savings, instead of the person's new spouse or children? Have you heard of a situation where the deceased person wanted to have assets held in trust for her minor children after her death, under her Will, but instead most of the assets ended up passing directly to the children, so that a conservator had to be appointed for them and they received direct access to the assets at 18? Have you heard of a situation where the deceased person wanted to have some of his cash and investments go to his adult children at his death, but instead the decedent's surviving second wife ended up with all the assets? Unfortunately, these situations, and many other, similar, situations, do occur. In many, many of those cases, the unintended result happens because the deceased person made a Will, but then forgot to also update beneficiary designations and ensure that assets were titled correctly.

In order to ensure that your estate planning intent is carried out at your death, it is critical to understand exactly how your assets will pass at your death. It is important to have a Will, at a minimum. However, a Will, by itself, is not enough for most people. Beneficiary designations effectively override a Will; so, if the beneficiary designation and the provisions of the Will conflict, the beneficiary designation will control, not the Will. In addition, if assets are owned jointly subject to a right of survivorship, the right of survivorship will also effectively override the Will and control the disposition of those assets. Therefore, if you care what happens at your death, and you want to be able to control who will benefit from your assets, how and when the beneficiaries will receive the benefits, and whether assets pass to intended beneficiaries outright or in trusts, you must understand exactly how the assets you own will pass at your death, and you must ensure that your beneficiary designations and asset titles are properly structured to coordinate with the desired plan.

Assets pass in the following ways at the death of the owner:

1. **<u>Beneficiary Designations.</u>** Assets that are subject to a beneficiary designation are controlled by a contract between the owner and a third party who has some form of control over the assets, and pass under the rules of contract law. Assets subject to a beneficiary designation will always pass directly to the designated beneficiary or beneficiaries at the death of the owner. The owner's Will or other estate planning documents will not control these assets unless the owner's estate or a trust created by the owner is the designated beneficiary **(Please note: designating the owner's estate may or may not be a good idea, depending on the asset involved and other factors. Do not rely on this article alone to determine a proper beneficiary designation.)** Some assets always pass by beneficiary designation: these include life insurance policy proceeds, annuities, Individual Retirement Accounts (IRAs), Qualified Employee Benefit Plan accounts (QPs) such as 401(k) accounts, and other

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types of deferred compensation. Other assets do not always pass by beneficiary designation but can be made to do so: these include regular, non-IRA bank or brokerage accounts, which can be made subject to a payable on death ("POD") designation, and securities, which can be held under a transfer on death ("TOD") designation. In general, the applicable contract will set out any limitations on who can be named as the beneficiary, as well as spelling out what happens if no beneficiary is named or a named beneficiary does not survive the asset owner. In many cases, there are few or no limitations on who can be named as a beneficiary in the applicable contract. However, the most common exception applies to retirement plans and other forms of deferred compensation that are subject to a federal law often referred to as "ERISA": the account owner must designate his or her spouse as the sole beneficiary of these assets unless the spouse properly waives this requirement in writing. Assets subject to ERISA include QPs such as 401(k) plans, among many other employer-sponsored benefits programs. IRA accounts are not normally subject to ERISA. However, if an IRA account holds assets that were received from a QP that was rolled over by the owner, that IRA can become subject to ERISA and its spousal consent rule. For example, if Jane leaves her employer and decides to roll her existing 401(k) account balance rolled over into an IRA, the new rollover IRA is still subject to ERISA, just like the 401(k) was.

The contract that applies to an asset subject to a beneficiary designation will also normally state the requirements that must be met in order to successfully change the beneficiary designation. The owner must generally strictly comply with the stated requirements. Common mistakes include filling out a form and then failing to submit it at all, failing to properly submit the form, failing to sign a form when required, failing to complete the form, and failing to submit the entire form. If a beneficiary designation change is not made correctly, then the previous beneficiary designation will normally stay in effect unless and until all of the necessary steps to change the designation have been completed and the proper documents have been received by the proper department.

2. <u>Joint Ownership with Rights of Survivorship</u>. Under Georgia law, there are two forms of joint ownership: joint tenants with rights of survivorship (JTWROS) and tenants in common (T in C). In some other states, including Florida, married couples also have access to a third form of joint ownership, which is called tenancy by the entirety (T by E). Assets owned by multiple parties as JTWROS and assets owned by a married couple as T by E are subject to rights of survivorship. This means that, by operation of law, the interest held by a deceased owner automatically transfers to the surviving owner(s) outright at the deceased owner's death. Assets owned jointly as T in C are not subject to rights of survivorship, and nothing transfers automatically at an owner's death. Instead, the surviving owners each keep their original interests, and the deceased owner's share passes to his or her estate.

In Georgia, financial accounts like bank checking or savings accounts, CDs, and taxable (non-IRA) brokerage accounts are automatically held as JTWROS by joint owners unless the owners take specific steps to have the account held as T in C. However, Georgia law provides that other assets,

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including homes and other real property interests, are treated exactly the opposite: these non-financial account assets which are owned by more than one person are presumed to be held as T in C unless the deed or other asset title document specifically states that the joint owners hold the asset as JTWROS. A statement showing that an asset is held as JTWROS usually needs to include the words "as joint tenants," "with rights of survivorship," or some very similar language, and the deed or other asset title document must be clear in stating that rights of survivorship are intended to exist.

We **do not** recommend that Georgia residents hold financial accounts jointly unless they are certain that they want the surviving owner or owners to automatically receive all of the assets in the account at the first owner's death. We also **do not** recommend that people hold financial accounts as T in C in Georgia, due to the manner in which Georgia law determines how the assets in a financial account are actually owned. Many people assume that assets held in a financial account are owned equally by each account owner. This is not true in Georgia: instead, if one owner contributed assets to the account, those assets, plus a proportionate share of income and gains or losses on the account, still belong to the contributing owner. An account owner does not acquire an interest in assets contributed by the other owner unless and until the non-contributing owner withdraws those assets from the account with the express or implicit consent of the contributing owner. And, when an account owner dies, if that owner's estate planning provides that his or her share of assets is to pass to someone other than the surviving owner (including into a trust for the surviving owner's benefit), it becomes necessary to trace the source of the assets held in a T in C account to determine the share of the account that actually belongs to the deceased owner.

3. <u>**Trust Terms**</u>. If you created a trust and transferred assets to it during your life and assets remain in that trust at your death, then the trust's terms will control what happens to those assets after your death. This is what happens if a person uses a Revocable Living Trust ("RLT") as his or her primary estate planning document and funds it partially or fully during his or her lifetime. It is also what happens if the person has transferred assets to various types of irrevocable trusts during his or her lifetime. Irrevocable trusts funded during the creator's lifetime are typically used to gain some sort of benefit; these benefits can include sheltering the assets from estate tax at the creator's death, protecting the assets from the beneficiaries' problems, or allowing either the beneficiary or the creator to qualify for a needs-tested benefit such as Medicaid or VA benefits.

4. <u>**Your Will Controls the Rest of your Assets.**</u> When you die, any assets you own that are not controlled by a beneficiary designation, a right of survivorship, or a trust will become part of your probate estate. The assets in your probate estate are the assets that will be controlled by your Will. Whether you realize it or not, you always effectively have a Will. The Will can either be one that was properly executed by you, created based on your situation and your wishes, preferably with the help of an experienced estate planning attorney, or it can be the one provided by state law for those who die without their own customized Wills.

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The Will provided for you by state law is set out in the intestacy laws (often referred to as laws of descent and distribution) of the state where you have your primary residence (your state of domicile). In addition, if you own real estate in other states, the intestacy laws of those states, not the law of your state of domicile, will apply to that real estate. State intestacy laws can differ significantly, which means that a person who dies without a customized Will and holds real estate in more than one state can have some assets passing one way, and other assets passing a different way.

If you spend the time and money needed to create your own well drafted Will, your loved ones will usually be better off than if you rely on the state law Will. In your own Will, you can decide who will take care of your minor children, if you have any; who is to benefit from your assets and how; if and to what extent costs, taxes and hassles are minimized; and who will be in charge of carrying out your wishes. Having a well-drafted Will in place can also help reduce the risk of any post death disputes. **If you rely on state law**, your loved ones will have to deal with more hassles and expenses after your death. It can also increase the risk of a post death dispute, and make any such dispute much more difficult and expensive to handle. For many, however, the most critical difference between what your state law Will provides and what you might really want to see happen is who benefits from your assets and how the benefits are provided.

As discussed above, your state law Will is really the distribution plan set out in the state's laws of intestacy. These laws differ from state to state. However, in general, these laws deem certain persons to be your heirs (your closest living relatives as determined under state law rules of kinship), and then they set out how your assets are distributed among your heirs. Let's examine how these laws work in Georgia. First, remember that assets in a deceased person's probate estate are first used to pay items such as a year's support claim (discussed below), estate administration expenses, final medical expenses, debts, and taxes, before any assets will be distributed to heirs or beneficiaries. After all of these items have been paid from a intestate estate (one where there is no valid Will in place), the remaining probate assets will be distributed to the person's heirs.

If the person is married and all of his children survive him, the person's heirs will be his spouse and children. The spouse and the children will each receive an equal share of the remaining assets, except where there are more than 2 children. If there is a spouse and more than 2 children, then the spouse gets 1/3, and the children divide the other 2/3 equally between them. If there is no spouse, the children divide the entire remaining probate estate. It gets more complicated if there is a child who died before the deceased person did: in that case, the child's share will pass to that child's own children, if there are any (the deceased person's grandchildren by the deceased child). If a grandchild also died before the deceased person but has one or more of her own children, that grandchild's share goes to her children, and so on. If the deceased person is survived by a spouse but has no children, grandchildren, or other descendants, however, then the spouse is the only heir, and will receive the entire remaining probate estate. **Please note:** only children who are either biological or adopted children will count in determining someone's descendants under the intestacy rules; people

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who are only related to the decedent through marriage, such as stepchildren, and who have not been adopted by the decedent or one of his descendants are not counted as his descendants for this purpose.

If a Georgia resident dies without a Will and has no surviving spouse or descendant (no children, grandchildren, etc.), things get even more complicated. The person's parents will be his heirs, if either or both parents survive him. If neither parent survives, then the person's siblings (brothers and sisters) will be his heirs. Siblings are counted as siblings without regard to whether they are related to the decedent through one parent or both parents; in other words, your half-sister or half-brother is treated the same as your full sister or brother. This feature of intestacy law, when it came up recently in Minnesota following the unexpected death of famed singer, Prince, appeared to surprise many commentators, who seemed to have originally assumed that his only full-blooded sister would be his only heir. Instead, both his full-blooded sister and his numerous half-siblings will be his heirs, assuming that no higher-priority relatives turn up (such as the man who is currently claiming to be Prince's out-of-wedlock son). If a sibling also died before the deceased person, then that sibling's share will be distributed to his or her children (the decedent's nieces and nephews by that sibling), with any deceased child's share going to his or her own children, if any, and so on, just as described above with regard to shares for a deceased child in the preceding paragraph.

If there are no parents, siblings, nieces, nephews, or descendants of nieces and nephews, however, the next relatives in line to be heirs are the deceased person's grandparents, all four of them, if any or all of them are living. If there is no living grandparent, then the aunts and uncles will be the potential heirs. As with siblings, a deceased aunt or uncle's share goes to that person's own descendants, if any (the decedent's cousins).

If for some reason none of the relatives described above is living, then you begin a search for even more remote relatives. There is a complicated set of rules in place to help the administrator of the estate determine who would be the closest living relative. In many cases, these would likely be people who the decedent doesn't even know, and may not have even heard of.

If no living relative can be found at all, then the decedent's remaining probate assets go to the state, to be added to the state's own funds. This is called escheating to the state.

Any person who receives assets as the heir to the estate where there was no Will receives his or her share outright. If an heir is under age 18, then a formal, court-supervised custodianship, with all of its related expenses, hassles, and restriction, will have to be set up for that person's share, and the heir will then receive full control at age 18. This can be a terrible result, and it is one that can easily be avoided by using a properly-drafted Will that places any assets that would go to a younger or immature beneficiary, or to an incapacitated beneficiary, in an appropriate trust, instead of having those assets pass outright to a beneficiary regardless of his or her age or capabilities.

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Important note for parents of minor children: in addition to controlling the distribution of your probate assets, a properly-drafted, customized Will that you have prepared can control who ends up raising your children if you aren't able to do so. For parents of minor children, the scariest aspect of dying without a valid Will and relying on state law may be that the Probate Court or some state agency will be the one determining where their children will live and who will take care of them. If you have a customized Will in place, you can designate the people who you want to serve as guardians and conservators, if needed, for your children. This stated preference is not absolutely binding on the probate court, but it is given very significant weight and will generally result in the appointment of the chosen parties.

5. State Law Sometimes Limits Your Ability to Control How Your Assets Pass at Death: Year's Support and Forced or Elective Shares. We have already mentioned federal law restrictions on what you can do with your assets at your death, such as the ERISA rules. Most states' laws also contain some provisions designed to protect a decedent's surviving spouse and minor children, and these laws often apply even where the deceased person has a properly-drafted, valid Will in place. In Georgia, this protection takes the form of laws that give a surviving spouse and any surviving minor child (one who is under 18) the right to an award of assets from the probate estate in the amount needed to support them for one year after the decedent's death. This is referred to as a "year's support." Although the heirs or beneficiaries of an estate normally come behind funeral expenses, debts, taxes, and administrative expenses in Georgia, the assets awarded as part of a year's support claim are protected, and most creditors cannot attach those assets. (**Please note:** a year's support claim will not be able to protect against a secured debt like a mortgage or a car loan, and it may not defeat a claim for federal taxes owed; however, it does protect against most other claims.) In Georgia, a Will can force the surviving spouse to choose between receiving the benefits provided for the spouse under the Will and the year's support; however, it is not clear whether you can force this choice on surviving minor children. But if there is no Will, the only potential challenge that can be brought against a person who is entitled to make a claim for year's support is for another heir, another beneficiary, or another interested party, such as a creditor, to try to argue that the amount being requested is too large, and that the court should award a smaller amount. If no such challenge is made to a year's support petition, then the probate court is required to approve the request as made.

Most other states provide that the spouse, and, sometimes, the children, are entitled to a specific minimum share of the estate. These shares are often referred to as forced or elective shares (forced, because in many cases you cannot fully eliminate that right through your estate planning, and elective, because the spouse or child holding the right can elect to take it in spite of the provisions made for that person in the estate plan). The share for a spouse is often in the range of 30% or 1/3 of the estate. The estate to which the forced share applies is defined differently in different states:

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some look only at the probate estate, others look to the probate estate and other assets, such as assets held in a trust created by the deceased person during his or her lifetime, assets passing under a beneficiary designation, and assets passing by a right of survivorship. However, in most states, a forced share is considered to be a beneficiary interest, not a support interest, and, therefore, is only paid after all higher-priority items have been fully paid from the estate.

While year's support and forced shares are rights held by certain persons under state law, in many cases it is possible to limit or eliminate the potential that these rights will be exercised. When putting together an estate plan, one of the many important issues to consider is the extent to which it may be desirable to take those steps, to help ensure that the plan will actually work as intended.

We hope that this newsletter has helped explain the many possible ways that your assets can pass at your death. When you are armed with this knowledge about how assets pass at your death, you are better able to control what actually happens.

While we hope this information has been helpful, putting together an estate plan and ensuring that all of the assets pass as intended can be incredibly complex, and having the help and advice of an experienced professional can be invaluable. If you have questions about whether your assets will all pass as intended and would like to review your existing estate plan or develop a new one, we are here to help. Contact our paralegal, Karrah Hammock, at either (678) 720-0750 or info@morgandisalvo.com to schedule an estate planning consultation.