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Summary of Estate Planning Concepts in Tennessee

1. **LAST WILL AND TESTAMENT:** If you do not have a will, your assets will be divided according to state law. Having a will allows you to select your personal representative and divide your estate according to your preferences.

   In Tennessee, you cannot disinherit your spouse or attempt to disinherit your spouse by not having a will and having property titled only in your name. The spouse is entitled to a marital share which is a child's share or equal to 1/3rd. The spouse may file for an elective share which is up to 40% based on length of marriage. A valid pre-nuptial agreement is an exception.

   If you are dealing with a blended family, a trust may be more suitable to avoid assets being re-titled and not benefiting your children. Never leave distribution of your estate to the discretion of the personal representative by making that person the sole beneficiary. Legally, the asset now belongs to him or her. Wills must be witnessed by two individuals not inheriting from the will and notarized.

   a) **HANDWRITTEN WILLS:** In Tennessee, a handwritten will is valid if all the material parts of the will are in the person's handwriting and signed by him or her. If the will is not notarized and witnessed by two people, the handwriting of the will must be proven by two witnesses in order to submit the document to the probate court.

   b) **CHANGES TO WILLS:** If you are married and have children from a previous marriage or relationship, and your will benefits your spouse, please keep in mind that if you designated your spouse as the beneficiary, he or she is not obligated legally to preserve assets for your children. If this is a concern, please consider a trust.

   c) **REVOCATION OF WILLS:** You may revoke your will by destroying it or simply making a new one. To avoid confusion and litigation, the old will should be physically destroyed once the new will is executed.

   d) **REVIEW:** Review your will annually to determine if changes in your life and those of your beneficiaries affect the content. Make certain that those named as executors, guardians, trustees are available and in good health. Marriage, divorce and other material changes in your life and those of your beneficiaries may call for a review of your will.

e) **PROBATE:** Probate is the legal process of administering the estate. Simply having a will does not avoid the probate process. If you own property in other states, an ancillary probate will also be opened in each state. Consider a trust as an alternative. Title the properties to the trust.

2. **SURVIVORSHIP OPTIONS:** Your bank accounts including savings, checking, CDs, retirement account, etc. will pass outside of probate if you have a joint account holder or a "Pay on Death" (POD) option or "Transfer on Death" (TOD).

   Please note if you have a joint account holder, the individual becomes owner of the account regardless of your oral conversations or intentions with that person.

   Real estate held as joint tenants with right of survivorship, tenants by the entirety (married people) as well as remainder interests of life estates pass outside of probate.

3. **TRUSTS:** To avoid the probate process, consider placing your property in either a Revocable Living Trust or an Irrevocable Trust. On your death, the trust would be administered without having court intervention thus protecting your privacy.

4. **REVOCABLE LIVING TRUSTS**: An RLT is an estate planning tool that allows you (as "Trustor" or "Grantor") to transfer ownership of certain assets to the Trust, continue to enjoy and benefit from those assets, express your wishes for how those assets will eventually be distributed to beneficiaries, and bypass the standard probate process.

   You can serve as the Trustee of your own RLT and appoint successor Trustees who will take over if you are unable or unwilling to look after it yourself. An RLT is "revocable" or changeable if you later want to make revisions to the Trust document.

   An RLT does *not* reduce income or estate taxes. In fact, any income earned by the Trust will, for tax purposes, pass through to you and be reported on your own personal tax return.

   a) **Advantages of a Revocable Trust**: Bypass probate. If you have a large estate and/or own real property in other states, having eligible assets owned by the RLT may eventually save your estate money by avoiding multiple probate cases. Further, your RLT document is private and not subject to the same public records requirement that your will would be in the probate process.

   b) **Funding**: Typically the kinds of assets that would be transferred to an RLT (called "funding" the Trust) could include: cash accounts (checking, savings, money market), non-retirement investment accounts, your residence, certain tangible personal property, your ownership of a business interest, etc. You generally would not transfer your car into the RLT (well, maybe a vintage collector's car). You also do not transfer ownership of retirement plans (such as IRAs, Roth IRAs), since they technically have a separate custodian and, in the event of your death, the assets will pass according to your specific beneficiary designations.

   c) **Disadvantages of a Revocable Trust:** No asset protection.

5. **IRREVOCABLE TRUSTS**: Irrevocable trusts are often used as an estate planning tool to preserve assets for beneficiaries such as a family farm. The irrevocable trust is a wise choice for those who own an asset not encumbered with debt. If the trust earns income, the trust would have a tax identification number. There are several types of irrevocable trusts and the taxation will vary. Please consult your certified public accountant or financial planner for tax guidance.

   a) **Advantages of an Irrevocable Trust:**

      i. **Probate Avoidance:** As with a revocable trust, probate is avoided.

      ii. **Creditor Protection:** Because the grantor no longer controls the assets held in the irrevocable trust, creditors cannot reach it.

      iii. **Medicaid:** As long as you don't need long-term care within 5 years of the transfer, the property does not count against you for purposes of qualifying for assistance.

      iv. **Capital Gains Benefits of the Trust:** The estate inclusion also provides a significant tax benefit known as a step-up in basis for capital gains tax purposes. If a parent transfers an asset that has increased in value, the parent's cost basis carries over to the child. That means, when the asset is eventually sold, the child will be assumed to have taken the asset at the same price as the parents and required to pay capitals gains taxes on the full increase in value.

      The step-up in basis means the asset is valued as of the date of the parent's death, not at the time of purchase. For example, if the parents put their home into an irrevocable trust with a fair market value of $500,000, the children's cost basis will also be $500,000. Therefore, if the children sold the home soon after their parents' deaths, there would be little or no capital gains to be taxed. As far as the children are concerned, this is a much more desirable outcome. This benefit is not available to individuals who transfer assets outright to their children as gifts.

      v. The irrevocable trust is the only type of trust that allows parents to transfer assets in a manner that will provide protection from their creditors, including the costs of long-term care, and their children's creditors (including ex-spouses) while allowing the parents to benefit from the assets comprising the trust during their lives.

   b) **Disadvantages of an Irrevocable Trust?**

      i. **Loss of control:** You lose control over any asset you place in an irrevocable trust.

      ii. **The 5 Year Rule:** If you gift assets to an irrevocable trust and need Medicaid within 5 years because your assets have dropped below the Medicaid asset limit ($2,000 in most states), you have to re-pay all transfers to the trust over the last 5 years – dollar for dollar – by paying for nursing home costs privately. Once you have "paid back" all of your gifted assets from the last 5 years, you become eligible for Medicaid.

      iii. **Cost:** In addition to the initial fee to set up the trust, there may be an ongoing fee owed to the trustee for managing the assets. There may also be accounting costs associated with tax returns, etc.

c) **Difference Between Revocable Trust and Irrevocable Trust:**

   i. **An Irrevocable Trust is IRREVOCABLE:** A revocable trust can be revoked, changed, amended, or altered during the grantor's lifetime. An irrevocable trust can never be revoked, changed, altered, or amended (except by court order).

   ii. **Gift taxes:** Transfer of assets to a revocable trust are not subject to gift taxes. A transfer to an irrevocable trust over a certain threshold may be subject to gift tax.

   iii. **Creditor protection:** Assets in a revocable trust are not protected from creditors. Assets held in an irrevocable trust are protected from creditors (unless it was a fraudulent transfer).

   iv. **Estate taxes:** Assets held in a revocable trust are included in the grantor's taxable estate (however, the grantor can reduce or eliminate the estate tax by using bypass trust planning). Assets held in an irrevocable trust are not included in the grantor's taxable estate (passing to the grantor's designated beneficiaries free of estate tax).

   v. **Tax filings:** A revocable trust does not require a separate tax identification number or tax return. The grantor of a revocable trust simply treats all of the assets of the trust as his or her own income for tax purposes. An irrevocable trust requires a separate tax identification number and may require an income tax return.

6. **LIFE ESTATE DEED**: This estate planning tool allows you to convey your property to your beneficiaries (remainderman) but retain a lifetime right to use and occupy the property. You pay the taxes, insurance, and maintenance. Upon your death, full ownership transfers to the individual who has the remainder interest. The real estate is not subject to probate.

   Creating a life estate requires executing a deed that transfers ownership of the property to the grantee yet gives the owners the legal right to live on the property as long as either of them lives. This approach can ultimately protect homeowners from having the property taken to pay for long-term care but can also create huge unnecessary problems.

   a) **Financial Problems of Children:** If the children experience financial difficulty during the life of the parents (bankruptcy, divorce, other), creditors may be able to put a lien on the residence. They could not force a foreclosure on the lien while the parents were alive, but the existence of the lien would still cause problems for the children when the property transfers to them following the death of both parents.

   b) **Life Estate Creates Conflicts of Interest:** A life estate also means that the parents cannot sell the home without the consent of all children that hold the remainder interest. A child that wants to keep the home in the family can stop the parents from selling.

   c) **Life Estate Creates Capital Gains Issues:** If the parents sell after transferring the property to their children, the children would be assessed a capital gains tax. If the parents transfer the property to their children, retaining a life estate, and later decide to sell, all of the individuals are considered owners. This can result in an unjust outcome. Transferring the property to the

children and retaining a life estate may not benefit the children. It may also cause strife if the children refuse to sell because of the potential tax liability. Remember that the parents cannot sell without the children's agreement.

7. **ADD CHILD(REN)'S NAME TO REAL ESTATE DEED:**
You might ask, "Why not add my child(ren)'s name to the deed now and save money on a trust?" Here are some considerations:

   a) **Gift Tax:** If you give your child something of value that exceeds $15,000 during the course of the year, you have made a taxable gift. This includes adding your child's name to your deed - if your child does not pay you anything to be added to the deed, then you have made a taxable gift. As a result, you will need to file a federal gift tax return on IRS Form 709 in order to report the taxable gift to the IRS.

   b) **Title Complications:** Once you add your child's name to the deed for your home, you cannot sell it, refinance the mortgage or take out a new mortgage without your child's consent. Also, your child could sell his or her interest in the property to a third party without your consent.

   c) **Creditor and Divorce Issues:** If your child ends up with a tax lien, creditor problems or in divorce court, then the government, creditor or ex-spouse may place a lien on your property and attempt to force a sale.

   d) **Delay in Medicaid Eligibility:** By adding your child's name to the deed for your home, you have made a taxable gift for gift tax purposes, and you have also made a transfer that will delay your eligibility for Medicaid if you apply for assistance within five years after making the gift.

   e) **Income Tax Problems Due to No Step Up in Basis:** When you die, and your children inherit your home through probate, a revocable living trust, or irrevocable trust, then your children will receive a step up in the income tax basis of the home. This, in turn, will minimize capital gains taxes on the sale of the home after your death. On the other hand, when you add your child's name to the deed for your home during your lifetime, then the home will not receive a step-up in basis after your death.

8. **LIFE INSURANCE:** Life insurance proceeds pass outside of probate. Please update the beneficiaries and contingent beneficiaries. The individual named receives the proceeds. Do not rely on oral conversations or intentions. If you intend this insurance to benefit a minor, then you must set this up in trust. If you intend this insurance to benefit a group of people, please specify their names. Do not rely on oral agreements with life insurance proceeds designated for your beneficiaries. Unless payable to the Estate, the individual named is the legal beneficiary. Consider making the proceeds payable to the Trustee of a Special Needs Trust to avoid disrupting government benefits of your loved one or the risk of a Medicaid take back.

9. **HEALTH CARE POWER OF ATTORNEY:** The health care power of attorney allows you to designate someone to be your representative, or agent, in the event you are unable to make or communicate decisions about all aspects of your health care. Without this document, you cannot make decisions for your spouse who may be suffering with dementia.

10. **GENERAL DURABLE POWER OF ATTORNEY:** This document allows you to designate an agent and authorize broad powers such as handling tax matters, insurance, bank accounts, and other financial matters. Authority may include gifting property, funding a trust and other important aspects of managing assets. If a power of attorney is not created during competency, this may result in a conservatorship which involves court intervention, more expensive legal fees and a loss of privacy.

11. **LIVING WILL:** The living will is an advance directive authorizing a natural death in the event the individual is in a permanent vegetative state with no chance of survival. This document may not be necessary if you have a health care power of attorney.

12. **ADVANCE CARE PLAN:** The state of Tennessee provides a free form at https://www.tn.gov/content/dam/tn/health/documents/Advance_Directive_for_Health_Care.pdf

13. **BURIAL / FUNERAL:** If you wish to pre-pay your funeral expenses, please purchase an irrevocable trust through the funeral home. Any unused portion will be refunded to your estate or holder.

14. **DIFFERENCE BETWEEN MEDICARE AND MEDICAID:** Medicare does not pay for long-term care in full. It will pay for 90 days of hospitalization, with a specific cost for the first 60 days, followed by a significantly higher copay responsibility for the next 30 days. For a shorter hospitalization stay lasting three days, Medicare will only pay for a maximum of 100 days of rehab or nursing home care, *only* after the patient has been admitted to a hospital for two nights.

    If you qualify, Medicaid will pay your entire nursing home bill. If you use Medicaid, your assets are subject to being recovered by the State after you die.

15. **HOW MEDICAID WORKS:**
    - **a)** It is wise to think of Medicaid as an interest free loan. If Medicaid pays for your long-term care, they want re-payment after your death.
    - **b)** The home is an exempt asset to qualify for Medicaid; however, recovery of benefits paid out is only made by a claim against the probate estate. Avoid having an estate that must be probated.
    - **c)** The institutionalized spouse may quit claim his/her interest in the home to the community spouse within one year. A valid Power of Attorney must be in place if the institutionalized spouse is incompetent. This means get your POA well in advance of incompetency if possible.
    - **d)** An exception to a Medicaid recovery is a disabled child or blind child living in the home. Another exception is a sibling living in the home continuously for 1-year that prevented you from requiring long-term care. Another exception is a child living in your home continuously for 2-years that prevented you from requiring long-term care.
    - **e)** If you give your home away, remember the 5-year look back period. Your benefits may be penalized and your care will become private pay for a certain time period. Also, keep in mind your children lose the step up basis regarding capital gains. Your asset may be at the risk of your children's creditors. Give serious thought to a trust.

f) There is no Medicaid take back with a Testamentary Special Needs Trust. This is a Special Needs Trust built inside of the will.

i. If your loved one has been in the nursing home for several years, you may consider selling the home and paying for the care as private pay. If your loved one dies and he or she is not on Medicaid, there is no recovery.

ii. If your loved one does not own a home but instead has considerable monetary assets, consider buying a home. It must serve as their "homestead."

iii. There are numerous options to consider. Please make an appointment for a detailed discussion.

According to Krause Financial (2018), the average cost of nursing home care per month is $6,110.00.

16. INTERNET DOCUMENTS: We have dealt with cases where an individual tried to save money and went online to write his trust. The trust failed. It was never funded with the real estate, bank accounts or life insurance despite listing such property on its schedule of assets. Consult an attorney who focuses on this area of law and you will no doubt save money in the future.

At our office, Olivia Wann feels that it is her job to educate you on the choices you have on your estate plan.

Your first consult is at no charge. Please contact (931) 232-4529.

Recap:

	Avoids Probate	**Designates Personal Representative & Guardian**	**Allows Step Up Basis re: Capital Gains**	**Provides Asset Protection**	**Notes**
Will	No	Yes	Yes	No	
Revocable Living Trust	Yes	Yes	Yes	No	
Irrevocable Trust	Yes	Yes	Yes	Yes	
Life Estate Deed	Yes on realty	N/A	Yes	No	