

THE PITFALLS OF DYING WITHOUT PROPER ESTATE PLANNING IN KENTUCKY: FIVE GOOD REASONS TO PREPARE A WILL



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Introduction

A will is a written document that directs the distribution of one's property after death. In fact, the Kentucky statute KRS 394.020 authorizes any person who is of sound mind and 18 years of age or over to use a will to dispose of his or her property upon death. Most Kentucky residents know of the purpose and function of a will. However, despite this common knowledge, many Kentuckians fail to prepare even a basic a will, even though they are uncertain of the consequences of dying without one. While there can be many good reasons a will may be necessary in a given case, the following are five good reasons for a Kentuckian to draft a will.

1. Designate Beneficiaries and the Manner in which They Are to Receive Your Property.

As noted above, a will allows one to designate the person or persons ("beneficiaries") who will receive his or her property upon death. However, if a person dies without a will, he is said to have died "intestate." The property of a person who dies intestate is distributed pursuant to rigid, complex formulas found in Chapters 391 and 392 of the Kentucky Revised Statutes. For example, an unmarried person's estate will pass to his or her surviving children and their descendants. If there are no descendants, the estate will pass to the decedent's parents, or if they

are deceased, the decedent's surviving brothers and sisters and their descendants and so forth. To further complicate the matter, if the decedent was married at the time of death, then the surviving spouse will be entitled to one-half of the decedent's property.

The intestate rules of distribution may be avoided through the use of a will. In Kentucky, a resident is generally free to provide for the distribution of his property to any person or persons.¹ In addition, there is no requirement that persons or the members of a particular class of beneficiaries be treated equally. For example, a person may choose to leave all of his property to one of his children and none to another of his children for any reason or no reason at all. A person is free to include or not include any person as a beneficiary of his estate.

In addition to freely choosing beneficiaries, a person is also entitled to choose the manner in which beneficiaries receive property. When gifts are made to a beneficiary by will, they are said to be "testamentary." A testamentary gift may be made "outright" or "in trust." If a gift of property is made outright, the beneficiary will have immediate rights to the property. Outright gifts may be used or spent by the beneficiary and will be subject to the claims of beneficiary's creditors.

Gifts of property which are made in trust are held by a third party (a "trustee") for the beneficiary until a later date. Gifts in trust

are recommended when a beneficiary is young or disabled. For example, Kentucky law provides that property left outright to a child may be used and spent by the child when the child reaches the age of majority (age 18). Therefore, parents of a young child are well advised to create a will that includes a trust that holds property until the child is older and more responsible. The terms of the trust may also permit the trustee to use the property for the child at any time for certain specified purposes, such as a child's college education and health care emergencies. A trust can also protect the property from the creditors of a beneficiary. This means that the property of the trust will be protected even if the beneficiary files for bankruptcy.

2. *Designate Your Executor.*

A person who signs a valid will in Kentucky may designate an "executor." The executor is a person named in a will who oversees the administration of an estate. Under Kentucky law, any Kentucky resident over the age of 18 years may serve as an executor. In addition, any nonresident who was related to the decedent by blood, adoption, or marriage may also serve as executor of an estate. State banks and trust companies incorporated under Kentucky law may also serve as executors as well as certain national banks.

Those persons who fail to have a will when they die leave it again to Kentucky statutory law to determine who is entitled to oversee the administration of the estate. Kentucky law gives priority to the decedent's surviving spouse, if any, and then to children and more remote relatives. However, if no relative applies for administration within 60 days, any person, even a creditor of the decedent, may apply to oversee the administration of the estate. Even when family members are available to serve, conflicts may arise if more than one family member seeks the appointment.

Consequently, a will serves the im-

portant function of designating one's executor. A court will give "particular preference" to a qualified executor nominated in a will to exclusion of all other petitioners. Specific designation of an executor allows one to choose a person in whom he or she has special trust and removes the chance of conflict between family members who might seek to oversee the administration of the estate. It is usually recommended that an alternate executor be named in the event the first nominee is unwilling or unable (by reason of death or incapacity) to serve.

3. *Designate Guardian for Minor Children.*

Persons with minor children (children under the age of 18) have an extra reason for having a will in Kentucky. KRS 387.040 states that the "last surviving parent of a minor may by will nominate a guardian...for the minor." This means that Kentucky courts will recognize and give effect to a parent's choice of guardian contained in a will. On the other hand, if the surviving parent dies without a will, the family court or other court will have to use the information presented and available to it in determining what to do with the children. A court will consider the evidence presented by family members and social agencies in determining with whom to place the custody of the children. Of course, if there are surviving family members of both parents, conflicts may arise. Therefore, it is wise to utilize statutory power to nominate the guardian of surviving children through the use of a will.

4. *Avoid Surety Expense.*

KRS 62.060 provides that every executor must enter into a covenant, or bond, with the Commonwealth of Kentucky, insuring that he or she will faithfully execute the duties of as executor. The bond is set in a penal sum, and if the bond is broken, the executor may be sued. KRS 395.130 further provides that the executor must provide a "surety" on the bond. The surety acts as the guarantor for the performance of the execu-

tor's duties in accordance with law. The expense of a corporate surety can be substantial because the surety is required to verify having a net worth of double the penal sum of the bond.

There is, however, an exception to the rule that an executor must procure a surety on his bond found in Kentucky statute. KRS 395.130 states that a court may excuse "the requirement of a surety...(if) by the terms of the will or trust, a surety is not required." Therefore, one may waive the surety requirement by stating that the executor be relieved of this obligation in the will. It generally makes good economic sense to avoid the expense of the surety, especially when the named executor is a close relative or another person in whom the decedent had great trust.

5. Address Federal Estate Tax Issues.

The federal estate tax is applied against the property of a decedent which is transferred upon death. Property of a decedent includes all property which the decedent owned or had the right to dispose of, including cash, land, retirement accounts, stocks, and life insurance proceeds. Fortunately, there is a rather large tax credit which permits a decedent to transfer the first \$1.5 million to his or her designated beneficiaries free and clear of the estate tax.² Of course, this means that the vast majority of persons dying in the United States do not have to worry about the estate tax.

However, for those persons who do own property in excess of that covered by the credit, the estate tax is a serious concern. Currently, for property in excess of \$1.5 million, the tax rate begins at 45% and increases to 48% for property over \$2 million.

A will is one planning document that may be utilized to make sure that married couples take full advantage of the estate tax credit. For example, married couples typically make the mistake of having simple

wills which leave all property outright to the surviving spouse. Simple wills cause all of the property owned by the married couple to wind up in the surviving spouse's estate. This is bad tax planning because the surviving spouse only gets the benefit of his or her tax credit. The surviving spouse is not permitted to use the decedent spouse's tax credit, even though none of it may have been used. This can result in a large estate tax being due on the death of the surviving spouse when the property is passed to the children or other heirs.

The estate tax laws, however, permit married persons to shelter the first spouse's property from the estate tax through the use of a trust and still allow the surviving spouse to have some control and benefit from the property. This sort of trust is generally referred to as a "credit shelter trust," and it may be created in a properly drafted will. A credit shelter trust generally provides that the surviving spouse receives all of the income produced by the property of the trust. The surviving spouse may also receive property of the trust for specified reasons, such as health, maintenance, and support. Perhaps best of all, all of the property held by the credit shelter trust may ultimately pass to the children of the decedent free of the estate tax because it is covered by the first spouse's tax credit. In addition, when the surviving spouse later dies, he or she may pass an additional amount of property free of the estate tax to the extent of the tax credit.

Conclusion

As one can see, there are a number of reasons wills are important planning documents for Kentucky families. This article, however, contains only a few of the reasons that wills may be necessary for estate planning. The circumstances of each individual or family situation are unique. In addition, there are other estate planning documents, such as revocable trusts and powers of attorney, that may be necessary for a complete

estate plan. Therefore, it is recommended that Kentucky residents contemplating estate planning meet with a competent lawyer for advice as to which documents may be appropriate to meet their particular goals.

1. There is one notable exception to this rule. Unless there is a prenuptial agreement in place whereby the spouses have waived their dower rights, a surviving spouse has a statutory right to a portion of the decedent's property regardless of whether the decedent had a will.
 2. The tax credit is scheduled to increase to cover \$2 million in 2006 and \$3.5 million in 2009. Under current law, the estate tax will be repealed in 2010, but reinstated in 2011 with a tax credit of only \$1 million.
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About Ted

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Ted's experience at **Denton & Keuler** spans a broad spectrum of business law and taxation, including purchases, mergers, acquisitions, and business planning. His skill has been invaluable to clients arranging multi-million dollar mergers as well as to those planning for closely held businesses. Ted also concentrates his practice in estate planning for clients with needs ranging from basic wills to more complex estate and gift tax planning.

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