

The Rules of Intestacy

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Danielle Friedman: Welcome to Trust US Estate Planning Wisdom, the podcast where we unravel the complexities of estates and trusts to empower you with the knowledge needed for effective estate planning.

Max McCauley: This podcast is hosted by Seasoned Estates and trust attorneys, Danielle Friedman, herb Feinberg, and Charles Max McCauley.

Herb Fineburg: This podcast is your guide to the intricate landscapes of estate planning, including wills, trusts, and probate.

Danielle Friedman: Thank you for joining us and we hope you find the discussion informative. But remember, when it comes to legal matters, always consult with a qualified attorney regarding your specific case.

Herb Fineburg: Welcome everyone to trust us. We're here this afternoon, Danielle Friedman. Max McCauley and myself, tur Feinberg, we wanted to talk to you today about the rules of intestacy. What is intestacy all about? Kandal.

Danielle Friedman: So intestacy generally means when somebody dies without a will, and depending on what state they were a resident of

Danielle Friedman: When they died, that state's law controls what happens to their property when they die.

Herb Fineburg: So I don't understand. So you're telling me that you're gonna have to trust the government to decide where your estate goes.

Danielle Friedman: That's exactly right. So if you die without a will, something has to happen to your property and the laws of each state dictate where that property goes.

Danielle Friedman: A lot of people make assumptions about what their state's law says as far as where their property's going to go, and you would be surprised to learn that oftentimes the law is not what you would assume it would be. For example, clients often come to me and say, well, I don't need a will. I'm married.

Danielle Friedman: Everything's just gonna pass to my surviving spouse. And while that may be true for assets that you own jointly with your spouse, because oftentimes when property is owned jointly, it passes to the surviving joint owner for any property that is in your own name. That doesn't pass by beneficiary designation because that's a whole other type of rule.

Danielle Friedman: Let's say you just have real estate in your own name. It's going to pass pursuant to your STAs intestacy statute When

you die, if you don't have a will.

Herb Fineburg: Well let, let me give you the standard situation. Client walks in, he's married, he has two kids, a 6-year-old, a 10-year-old, and his parents are still alive.

Herb Fineburg: What happens to his estate? 'cause it sounds like you're telling me, you're telling our audience that. His estate will not pass to his wife.

Danielle Friedman: So she's gonna get something. But

Herb Fineburg: she's not just Pennsylvania, you're talking

Danielle Friedman: about. Yeah. Yeah. So in Pennsylvania, which is primarily where I practice, I also, uh, practice in New Jersey.

Danielle Friedman: But we'll talk about Pennsylvania 'cause it is not the case that everything would pass to his wife. So if he is married and the children are also the children of his spouse. Then his wife is going to get the first \$30,000 of his estate, plus one half of the balance, and then the other half is going to pass to his kids.

Danielle Friedman: And his kids in the example you gave are minors and they can't inherit property. And so some clients will say, well, it's fine their, their mom will handle it for them, but that's not the case either. Their mom is not allowed to handle . The property that goes to the children, they have to go to court and get court appointed guardians.

Danielle Friedman: Uh, it's called Guardians of the Children's Estate, and that is the person who's able to legally take title to the property that they're going to inherit. So it creates this whole waterfall of issues and unintended consequences when you have someone who. Assumes that everything is gonna pass to their spouse or or another beneficiary under state law.

Danielle Friedman: When in reality, state law often defies logic and says something completely different.

Max McCauley: And I would like to add something that we said previously, and that is this outcome is different in every state by practice in Delaware. So you're going to get a different outcome, however slight that might be in every state.

Max McCauley: It's going to depend on what state you lived in when you died without a will. So

Herb Fineburg: in the example I gave, I had a married couple and I had two minor children, and, and you just explained the fact they're gonna

have to have guardians appointed that that's a very expensive process. It'd be a heck of a lot cheaper for the, uh, client to just set up a will.

Danielle Friedman: Sure, absolutely. And. On top of all of that, if something were to happen to the client and his wife at the same time, it's possible that then everything would pass to the kids and then their minors. And not only do you need to have guardians of their estate appointed, you would also have to have guardians of what the state calls their person appointed someone who's able to make legal decisions for them.

Danielle Friedman: And you have to go to court to do that. Normally parents in their wills will say who they want to serve as guardian. Here, it's a free for all. You know, it could be. Grandparents from one side of the family versus grandparents from the other side of the family, or any number of different individuals who wanna serve as the legal guardians of these minor children.

Danielle Friedman: So you avoid a lot of disputes and infighting and unnecessary court involvement when you have a will.

Herb Fineburg: So you're gonna have two sets of grandparents who wanna be the guardians of their grandchildren in that situation. But a client could have had a will and could have said who they prefer.

Danielle Friedman: Yes. And so no matter what, when you have guardians of minors appointed, you do have to go to court.

Danielle Friedman: But when you have parents stating what their preference is in their documents, the court gives great weight to the parents' preference, and unless there is some other overarching reason why those. Individuals that the parents named in their documents should not serve as guardian. The court is going to give deference to what the parents put in their wills.

Herb Fineburg: So let's use an example. Let's say there's an estate of \$5 million and it goes into, let's say 50% for each child, two and a half million dollars for each child into this guardian estate. How long does it stay in the guardianship estate for the children?

Danielle Friedman: Well, that's the other problem. It only stays in until the children reach the age of majority, which again, depending on the state you're in, sometimes it's age 18, sometimes it's age 21, but still relatively young.

Danielle Friedman: And then you have an 18-year-old or a 21-year-old having unfettered access to two and a half million dollars, which we all know is not gonna last very long in the hands of a teenager or a young adult. And. That again, could have been avoided if parents had a

will, had set up trusts for the kids that would have received that two and a half million dollars in trust for the benefit of their children.

Danielle Friedman: And someone with more financial responsibility could oversee that money for the benefit of the children rather than two and a half million passing outright to a child

Herb Fineburg: sounds like a series of complete disasters. We, we often hear about people, uh, who sit down and say to their brother or their sister, well, I want you to be the guardian of my children because I think you're best fit for that.

Herb Fineburg: Does that count?

Danielle Friedman: No, nothing that you say verbally unless you commit it in writing in some way, whether it's in a will or other document. That typically has to be witnessed and notarized your conversations with your. Preferred guardian are not gonna bear any weight in court because anybody could go and say, Hey, the decedent told me he wanted me to be guardian.

Danielle Friedman: And then another party could also say, no, no, no. He told me he wanted me to be guardian. And then you have this conflict that no court is going to give any weight to the other thing that arises. And Max, maybe you could enlighten us if you have a decedent who owned a business. Dies without a will, what happens to that business interest?

Max McCauley: Absolutely. So, uh, we have, uh, another example that we can provide and walk through and that is, uh, a pair of siblings that owned the business and the one brother had no will, and he assumes he married who wasn't married and didn't have any children. Wow. And he assumed that his brother would inherit his half of the business.

Max McCauley: Incorrectly assumed that his brother would inherit his half of the business, when in reality under Pennsylvania law it would've passed to his mother. He did not know that. Now, this is where it's important to have a lawyer involved because not only can we solve this problem with a will, it can also be solved with, uh, other legal corporate governance documents, such as a buy sell agreement or an operating agreement.

Max McCauley: Shareholders agreement, partnership agreement, and the like. But you do need the lawyers to work hand in hand with your estate plan, do not conflict, and that the outcome of the death is the deceased's preferred outcome. And in this case, it was for the brother to get the business and none the business, not his mother.

Max McCauley: He had no will and until he consulted with a lawyer and lawyer pointed out the several ways where this issue could be solved

in a very inexpensive fashion upfront as compared to what would happen if his half of the business had passed to his mother and then his brother was left with buying that business from his mother if he wanted it to continue.

Herb Fineburg: What happens if he either doesn't have a mother, doesn't have any living parents, or the parents say. They disclaim it. They say, I don't want it, but he's got three other siblings. So the two siblings are in the business and two siblings are not in the business. What happens to his 50% interest in the business with the, with the sibling?

Danielle Friedman: Well, I could say what would happen under Pennsylvania's intestacy law, which if you don't have children, you don't have a spouse, you're not survived by any parents, but you have a number of siblings. Whatever your interest is is going to go to those siblings Equally, it doesn't matter that some are involved in the business and some are not involved in the business.

Danielle Friedman: Let's say you have four brothers and sisters, all four of them are gonna share that interest and then you have to deal with the siblings that are involved in the business may be buying out the ones that are not involved in the business or getting into this negotiation between family members to try to resolve this issue.

Danielle Friedman: Where again, it could have been avoided with the governing documents that Max mentions or a will in the absence of those governing documents.

Herb Fineburg: Well, what happens, Danielle, if he dies in test state and there's a buy sell agreement with the sibling? How does the intestate laws interact with the buy sell agreement?

Danielle Friedman: So the buy sell agreement is gonna control because any contractual agreement that you've made during life, which is essentially what a buy sell agreement is, is going to control over the state's intestacy statute. So with respect to the business interest, not really anything else that the decedent owns.

Danielle Friedman: The buy sell agreement is going to control and the states intestacy statute would cover everything else like bank accounts and things of that nature. A contract is very convenient in this situation because you can carve out exactly what you want to happen to that property with your co-owners of the business.

Danielle Friedman: There are other types of assets. Contract would also control, for example, a beneficiary designation is a type of contract. So if someone has a retirement account or any other type of account that permits a beneficiary designation and they die without a will, but they have a designated beneficiary on certain accounts,

those designated beneficiaries are going to inherit that asset.

Danielle Friedman: It's just everything else. That is just in the deceased name that isn't controlled by a contract or beneficiary designation or by operation of law, let's say if there's joint ownership, everything else gets funneled into the intestate estate, and that's where the state's intestacy statute is going to control.

Danielle Friedman: The other interesting thing I've noticed in a multi-jurisdictional practice and in an area where we live, where we have clients who own property in New Jersey, in addition to Pennsylvania or another state in addition to Pennsylvania, is that you die in test state. You know, one state's intestacy law may control where the property is located versus.

Danielle Friedman: Where you lived when you died. So you could have a beach house in New Jersey that's controlled by New Jersey's Intestacy Law and the rest of your estate if you died. A Pennsylvania resident controlled by Pennsylvania's intestacy statute. So the unpredictability is massive, where you could have certainty and control if you have a proper estate plan.

Max McCauley: Jumping back to the buy sell agreement as well versus dying and tested. The buy sell agreement can dictate the payment price and the payment terms, whereas if you died without a will, the remaining business owners are left to negotiate the payment price in terms with the siblings that they're buying out, and so they might be faced with less favorable purchase price or a less favorable.

Max McCauley: Terms that might saddle the business with debt that it can't afford, ultimately leading its demise.

Herb Fineburg: So in your example, max, you're going to have two siblings who are in the business. When you have a business, one of the great benefits of having a business is to get a salary. So if one of the owners dies and the siblings who aren't in the business, they're not gonna receive a salary and they're gonna be pretty demanding and checking on all the things.

Herb Fineburg: The surviving sibling does, including his salary, his benefits, how's that going to work now,

Max McCauley: whether or not profits are being distributed quarterly or annually? Uh, are enough profits being distributed that cover the tax payments that are due on those profits? Sounds like a, a case for massive litigation usually involves very expensive litigation that might last for years and destroy the family relationships.

Herb Fineburg: So again, a will's a pretty cheap solution to all these problems.

Danielle Friedman: Absolutely. The, the other benefit of having a will and having a experienced attorney prepare your estate plan is that they can also review . Any buy, sell agreements, shareholders agreements, and the like that may exist so that there's no conflict between your estate plan and the governing documents of the business.

Danielle Friedman: Even though as we discussed the governing documents of the business control, we don't want the will to say something contrary to what the governing documents say, because if under the governing documents, the sibling is inheriting the business, but under the will. Everything is passing to a friend. We don't want a friend to say, well, I should get the business interest, even though they're wrong.

Danielle Friedman: Anybody can sue for anything, and you have this unnecessary conflict generated that, again, can be avoided if you have competent counsel who makes sure that everything is in order and everything is not conflicting with one another.

Max McCauley: Another added benefit of having a will in an estate plan, it enables your attorneys.

Max McCauley: And your tax preparer to engage in federal and state tax planning as well as debt tax planning in an effort to try to minimize the tax burden associated with your debt.

Danielle Friedman: That's a great point, max, because again, I'll bring it back to Pennsylvania. Pennsylvania is one of the few states in the country that has an inheritance tax.

Danielle Friedman: And in the example Herb you raised earlier, where you have someone dying who is married, who also has children, the way that their assets pass under Pennsylvania's intestacy laws will trigger inheritance tax. Whereas if they had a will leaving everything to their spouse, no tax is gonna be due. But because the person is leaving.

Danielle Friedman: Inadvertently by, by virtue of the intestacy statute assets to their children and to their spouse, anything passing to the children is going to trigger Pennsylvania's inheritance tax at a rate of 4.5%. If siblings are inheriting under intestacy statutes in Pennsylvania, the tax rate is 12%. So by not having a will, even if you have the best intentions, you are unfortunately

Danielle Friedman: Imposing inheritance taxes on your beneficiaries, and that's just at the state level. If you have assets passing to nons, spousal beneficiaries at the federal level, you're gonna have to use a portion of your federal estate tax exemption. If you have someone with an extremely large estate, that is gonna be subject to

federal estate taxes.

Danielle Friedman: You may be triggering federal estate taxes because you have assets passing to non-exempt beneficiaries, and that tax rate is 40%. So it's really important to have competent counsel, make sure that your estate plan mitigates death taxes as much as possible. So

Max McCauley: potentially up to 52% death tax, 12% Pennsylvanian, and 40% federal.

Danielle Friedman: Yeah, siblings are inheriting. Absolutely.

Max McCauley: And when are those taxes due?

Danielle Friedman: Generally within nine months of death. So. It triggers, in some cases what we call a fire sale, where if there's a business involved, you might need to sell the business in order to generate the cash needed to pay death taxes.

Herb Fineburg: So it sounds like anybody who's married better have a will or be in deep trouble with his family after he passes his legacy.

Danielle Friedman: I would say

Max McCauley: even if you're not married, have children.

Herb Fineburg: And the other one is, as Max is describing, is. Whether you're married or not married, this could end up in a huge disaster. Huge litigation expenses, and then on top of it, the icing on the cake is death taxes,

Max McCauley: unnecessary income and debt taxes. Yes.

Danielle Friedman: As I tell all my clients, everybody needs an estate plan.

Danielle Friedman: It doesn't matter truly how much property you have, because none of us want. The government making the decisions about where your property passes when you die, because oftentimes it is not where you would have selected your property to go when you die,

Max McCauley: and nobody wants to unnecessarily pay extra federal income tax, state income tax, or death tax.

Herb Fineburg: One of the things that I see people confused about is some people get a will and say, that's my estate plan. But I find that that's not necessarily an estate plan. It's just a stop gap document that doesn't take into account all the issues that we just discussed here.

Danielle Friedman: Yeah, if you have your will, which is very simple, you go online, you get a two page will that says, everything goes to my spouse, and if my spouse is not alive, everything goes to my kids. It's not an estate plan because you haven't taken into consideration how much your kids might get if they're going to be minors, when they inherit, whether you want your kids to inherit property outright or whether it should pass to them in trust and frankly.

Danielle Friedman: Same thing applies to your spouse. If you're a young person, and I'm, I'm just using young people as an example, but this could apply to anyone at any age, and you leave everything to your spouse and then your spouse gets remarried and in their will, they leave everything to their new spouse. Then they die.

Danielle Friedman: You know, nothing is really passing to your kids, which is probably where you really wanted your property to go. And all of that, as we discussed in other episodes, can be addressed. And those problems can be eliminated through the use of trusts in your estate plan. But in order to know to do that, we don't expect.

Danielle Friedman: Clients to know to do that. That's where an estate planning attorney comes in and provides those recommendations, and then the clients have an aha moment and say, yes, that's what I need. That's what I want.

Max McCauley: Go back to the, the siblings that own the business, hypothetically. If they had bought the business from their parents and they then own the business 50 50, the sibling without the will.

Max McCauley: And without a wife and without children, his parents would inherited his half. The remaining surviving business owner would then again have to buy the business, 50% of the business from his parents.

Danielle Friedman: Oh, what disaster that is

Max McCauley: by twice, in course of a few years, potentially.

Herb Fineburg: Well, we could find a large number of scenarios where people are just simply shocked about what's happened.

Herb Fineburg: You don't hear about it on the street because nobody talks about the problems they've had. In our business, we see all these things happen and play on every day, and we scratch our head as to why people don't plan, but would rather have their family go through the time and expense of dealing with their death.

Max McCauley: But in my experience and closely held family businesses like that, it usually leads to family disharmony among the beneficiaries when somebody dies without a will. Because then whether

it's the siblings, the children, the spouse. Uh, can't agree on who should get what and what amounts and what percentage,

Danielle Friedman: and sometimes that's the most valuable aspect to all of this.

Danielle Friedman: Not so much the, the business or the money that anyone's going to receive, but just family dynamics and the preservation of relationships. Again, having a will, having a proper estate plan, having trust in place. Preserve all of that. On top of, of course, giving you control and certainty about where your property goes.

Danielle Friedman: You're gonna be sure that your family isn't fighting over what happens when you die.

Max McCauley: I'll ask to you as well, but in my experience, when you die without a will, the legal fees expended as a result of that decision are usually a hundred or a thousand times the legal fees. Would've been spent preparing a simple will and estate plan.

Max McCauley: Is that your experience as well?

Danielle Friedman: It's oftentimes more expensive, no doubt, and not only more expensive, more time consuming things move slower through the courts. You have to have more court involvement. If you have someone dying without a will, it just becomes this costly slog that could have been avoided, and I understand.

Danielle Friedman: For some people thinking about their death and thinking about where their property's going to go isn't a conversation that they wanna have, but sometimes reality has to set in and you have to know that even if you avoid this conversation, state law is gonna kick in. So it's better to make those decisions on your own rather than

Max McCauley: trust the government to make the decision.

Danielle Friedman: Yeah, absolutely.

Herb Fineburg: Well, great. Very interesting, uh, topic for our listeners.

Danielle Friedman: Thanks guys.

Herb Fineburg: Thanks.