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BUSINESS TRANSACTIONS • TRUST AND ESTATE LAW

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Personal Representative Handbook

The purpose of this handbook is to assist you in carrying out your duties as the Personal Representative (or Executor) of an estate of an Arizona decedent. This handbook is updated from time to time; please contact us if you are not sure you have the latest version. Also, please remember that this handbook is a guide; it is not intended to answer every question that could come up in the administration of a trust, and it is not intended to give you legal advice.

INTRODUCTION

What Is a Personal Representative? In Arizona, a *personal representative* (known in many states as an *executor*) is the person or entity appointed by the Court to administer the estate and assets of someone who has died (a *decedent*). In other words, the personal representative has the responsibility to ensure that the decedent's affairs are taken care of after death, in accordance with the decedent's Last Will and Testament (*Will*), if one exists, or in accordance with state law if the decedent died without a Will.

Duties. The personal representative's essential duties are to:

- collect the assets of the decedent,
- pay any outstanding bills or creditors that need to be paid, and
- distribute the decedent's assets to whomever is supposed to receive them under the Will (or, if no Will exists, under state law).

While that may not sound overly complicated, there are many issues a personal representative must address once he or she is appointed by the Court.

Acting as a personal representative can be simple or complicated, depending largely on whether the Decedent's assets are fairly straightforward and simple, or the decedent owned complex assets at death, such as business interests or real estate in multiple states.

Who Will Serve? Who has the right to serve as personal representative will depend on whether the decedent left a Will. If the decedent died with a valid Will in place at the time of passing, the decedent is said to have died *testate*. In that case, whoever the decedent nominated to act as personal representative in the Will has the right to serve.

Bear in mind, though, that just because you may have been nominated to serve as personal representative in someone's Will does not mean you have a duty to accept that nomination. You can always decline, in which case any alternate candidate nominated in the Decedent's Will would then have the opportunity to serve as personal representative.

Conversely, if the Decedent died without a valid Will, the Decedent is said to have died *intestate*. In that case, state law (in Arizona, A.R.S. § 14-3203) controls who has the right to serve as personal representative. Roughly summarized, the people having the right to serve as personal representative under most intestate statutes are, first, the surviving spouse of the Decedent and, second, other persons who will inherit property of the Decedent under the intestate statutes.

Necessity of Probate. One of the first matters you must determine is whether a probate is needed.

If the value of all personal property held by the decedent at death, including cash in the bank and other accounts, vehicles, jewelry, etc., is valued at less than $75,000, and the net equity in real property owned by the decedent is valued at less than $100,000[1], then court involvement can be avoided entirely, and the estate can be administered quickly and inexpensively through a simple affidavit process.

If, however, the value of the estate exceeds the above figures, then a probate will be necessary in order to administer the decedent's affairs.

FIRST THINGS FIRST

As mentioned earlier, after the priority of appointment has been established, you need to decide whether you want to accept the role. Being nominated as personal representative in a Will is an honor; the nomination implies that the decedent held you in high regard.

At the same time, acting as personal representative involves considerable responsibility; if you make a mistake in handling the decedent's affairs, you can be held personally

[1] For this purpose, the "value" of the real estate is based on its assessed value for real property tax purposes, not its "fair market value," less any liens or encumbrances against the real property. For example, if the assessed value of a house for property tax purposes is $200,000 and the property has mortgages against it totaling $125,000, the "net equity" for purposes of whether a probate is required is $75,000 ⊚ or $25,000 under the $100,000 limit.

liable by the decedent's heirs[2] and creditors for any damages that your mistake causes. While most estates are not difficult to administer, if the assets owned by the decedent at death are especially complex, or the heirs or other parties involved do not get along well, acting as personal representative can be an onerous and thankless job. Before agreeing to serve, you should carefully consider the circumstances and whether you are up to the task.

You should also bear in mind that it is a rare estate that requires immediate action. While sometimes loved ones feel compelled to begin the probate process immediately, in most cases there is no need to rush. Family members should generally take whatever time they need to grieve the decedent's passing before turning to legal matters. After all, you have no duties to anyone (nor power to do anything with the decedent's assets) until you are officially appointed to the position by the Court.

OPENING THE PROBATE

If you decide to serve as personal representative, you need to be officially appointed to the position by the Court of the county in which the decedent resided at the time of death. That is accomplished by filing with the local Probate Court a pleading called an *Application for Informal Probate of Will and Appointment of Personal Representative*. Alternatively, in the case of an intestate decedent, the pleading is called an *Application for Informal Appointment of Personal Representative*. Both pleadings initiate what is called an "informal probate."

If certain heirs or creditors of the estate may become adversarial during the process, or there is a question as to whether a certain document is in fact the "last" Will of the decedent, you may instead apply for a "formal probate." This will also be true if the original of the decedent's Will cannot be located and you need to probate a copy of a Will.

The differences between an informal probate and a formal probate are fairly significant.

For example, an informal probate rarely requires a hearing prior to the appointment of the personal representative. In most informal probates, the Probate Registrar issues a *Letter of Personal Representative* immediately upon filing the appropriate paperwork and the original Will.

In a formal probate, a hearing will first have to be held with the Court to verify that the Will left by the decedent was in fact the decedent's Last Will and Testament or to verify that the decedent died without a valid Will in place.

Within 30 days after your appointment, you must (a) notify all heirs and devisees[3] of the decedent's estate that a probate has been opened and (b) provide such heirs and devisees with a copy of the Will in a "testate" probate. In an "intestate" proceeding there is no Will to provide a copy.

In a formal probate, the notice of appointment need not be given to anyone who was given notice of the initial application for formal probate, and who as a result has already been given an opportunity to object. In all other cases, the notice must also notify those heirs and devisees that they have a limited period of time to object to the appointment of the personal representative or to the admission of a particular Will as the decedent's valid Last Will and Testament.

GATHERING ASSETS

Initially, you (as the personal representative) must identify and collect the assets of the decedent's estate and protect those assets from harm. For example, you may need to secure the decedent's primary residence to protect it against vandalism or to prevent family members from removing items from the home.

Identifying the decedent's assets may not be an easy task, particularly if the decedent did not retain good records. You may also have to spend considerable time poring over the decedent's bank and other account statements to determine where the decedent's monies were kept. You will also need to inspect the contents of safe deposit boxes and locate life insurance policies and retirement plans. In many instances, copies of the decedent's income tax returns can be a good source of information to identify assets and accounts that the decedent owned.

You must be able to account for all of the decedent's assets as they existed on the date of the decedent's death. You must then be able to determine what the value of the decedent's estate was as of that date. For bank and investment accounts, determining value is easy. However, for many other kinds of assets, professional appraisals might need to be obtained. This course of action is essential not only when you cannot determine how much a particular asset is worth; it may be required if an estate tax return must be filed. For example, if the decedent's estate has a value greater than that which can pass free of estate taxes ($11.2 million for an individual in 2017), an estate tax return must be filed, accompanied by professional appraisals of assets.

In addition, regardless of whether an estate tax return is required, you must prepare and submit to heirs, within 90 days after your appointment, an inventory and appraisement of estate assets. The inventory and appraisement must identify each asset owned by the decedent and provide the fair

[2] An "heir" is a person legally entitled to the property or rank of another on that person's death.

[3] A "devisee" is a person who receives a gift of real property by a Will.

market value of each asset as of the date of the decedent's death. In some cases, it will be impossible for you to ascertain that fair market value without a professional appraisal. Real estate is one good example of when a professional appraisal may be needed, but other types of assets (e.g., art, jewelry, antiques, and stock in a closely held company) may be particularly hard to value without a professional appraisal or valuation.

After the inventory and appraisement are complete, you must mail copies to all parties interested in the estate, including heirs and others named in the Will, as well as any creditors who have filed claims against the estate (see "Notify Creditors" below). You must then file a pleading with the Court affirming that this requirement has been met.

Alternatively, you can file the inventory and appraisement itself with the Court and then mail a notice to all interested parties that you have done so.

The former option is almost always used because it preserves confidentiality, whereas the latter option makes the inventory and appraisement part of the public record.

Because not all of the decedent's assets will need to go through the probate process, it will be important for you to distinguish between probate and non-probate assets. Only those assets that at death were titled in the decedent's name alone, without a beneficiary designation, will need to go through probate. Most notably, this excludes from probate any assets:

- owned jointly by the decedent and another person;
- any assets held in a trust or held by an entity[4] in which the decedent had an ownership interest; or
- any asset that had a beneficiary designation.

The first two types of assets are controlled by the terms of the joint ownership, trust or entity to which they belong. The third type of assets, which can include life insurance policy benefits, IRAs and retirement plans; "pay on death" (POD) or "transfer on death" (TOD) bank and brokerage accounts; and even real estate for which a beneficiary deed has been recorded, are considered "non-probate transfers" and never enter into the probate process.

As mentioned above, after the extent and value of the decedent's assets at death are determined, you must secure valuable personal property, such as jewelry, artwork, guns, etc. If the decedent had a safe deposit box and you have access to it, you should inventory its contents and keep them in your custody. Especially important are any documents that may be helpful in administering the estate (e.g., the decedent's original Will or other estate planning documents).

Access can be tricky, as Arizona banks, after they are notified that the owner of a safety deposit box has passed away, are required to make an inventory of the box's contents, seal it, and send the inventory to the Arizona Department of Revenue for tax purposes.

Be aware, though, that you have no duty to inform the decedent's banks regarding the decedent's death – at least not right away.

The preliminary information-gathering phase is also a good time to collect important documents, such as bank statements, tax records, deeds to real property, titles to vehicles, etc.

Be certain to order, through the decedent's funeral home, plenty of certified copies of the death certificate, as many institutions will require the submission of a separate certified copy to verify the death.

Also, you will need to apply to the Internal Revenue Service for a taxpayer identification number (EIN) for the estate (this is a fairly simple step that can be completed online at www.irs.gov). As you gather the assets of the estate, and after you receive the EIN, you will then open an estate bank account into which you will deposit all cash proceeds.

NOTIFY CREDITORS

In addition to notifying the decedent's heirs and devisees that a probate estate has been opened, you must also notify all known and potential creditors of the estate that (a) the decedent has passed away, (b) a probate has been opened to settle debts of the decedent, and (c) you have been officially appointed to handle the decedent's affairs.

This notification is accomplished in two ways:

- written notice with the above information must be mailed to every known creditor of the decedent; and
- a similar notice must be published in a newspaper of general circulation in the county in which the decedent lived, to give notice to any potential or unknown creditors.

To submit claims against the estate, *known* creditors have the longer of (a) 60 days from receipt of the written notice or (b) four months after first publication. *Potential and unknown* creditors have four months from the date of first publication to submit their claims to the personal representative. After expiration of these time limits, any claims not timely

[4] The assets of the entity itself do not become part of the probate estate. Instead, the Decedent's ownership interest in the entity is personal property that would go through the probate process if titled in Decedent's name alone at death.

submitted to the personal representative are thereafter barred and can be safely ignored.

It is crucial that these notices be mailed and published as soon as possible after your appointment, so that the time period to submit claims against the estate can begin to run. Only after the period to submit claims has expired can you be certain of the full extent of the claims that may be made against the estate. If you distribute assets to heirs or devisees of the estate before all creditor claims have been paid, you will have a difficult time recovering those assets to pay creditors who later, but still timely, assert claims. In such a case, *you will have personal liability* to those unpaid creditors.

USING AN ATTORNEY

The process of notifying and dealing with creditors is one example of why relatively few probates can be successfully administered without some involvement from an experienced probate attorney. Even the simplest of estates can result in personal liability for the personal representative if the wrong creditor gets paid or a legitimate creditor gets paid too soon or too much. For instance, though the process outlined thus far may seem relatively simple, a layperson is unlikely to know that some life insurance proceeds and retirement assets are generally not subject to creditor claims but that other non-probate transfers are, and may need to be recovered by the estate in order to satisfy creditor claims. A false move here can subject you to significant personal liability.

Also, bear in mind that there is no requirement to consult with the attorney or law firm that prepared decedent's estate plan. Many lawyers can produce a simple Will, but only an experienced probate attorney can adequately advise you on the potential pitfalls of this process.

Never shrink from asking for legal or other advice. That advice may cost something in the short run, but the cost can be far less than it takes to fix a mistake later on. Remember, too, that the estate will pay the reasonable costs associated with your obtaining advice; conversely, you could end up paying out of your own pocket for your failure to secure advice when you needed it.

PAY VALID CREDITORS

If you receive creditor claims against the estate, one of your most important duties is to decide which, if any, of the claims are valid. You have 60 days from the receipt of a creditor claim to reject the claim as invalid; if you do not reject a claim within 60 days of receiving it, the claim is deemed to be valid. If a creditor's claim is rejected, that creditor then has 60 days from the date of rejection to file an adversarial proceeding with the probate court to prove that their claim is valid.

If the estate's assets are sufficient to satisfy all creditor claims in full, then all creditors get paid the full amount owed. If the assets of the estate are insufficient to pay all creditor claims in full, then each creditor gets paid according to the priority of claims described by state law, which in Arizona consists of:

1. costs and expenses of administration (including the personal representative's fees and legal expenses);
2. reasonable funeral expenses;
3. debts and taxes with preference under federal law;
4. reasonable and necessary medical and hospital expenses of the last illness of the decedent, including compensation of persons attending him or her;
5. debts and taxes with preference under Arizona law; and
6. all other claims.

Each of the estate's creditors is assigned to one of these categories and paid in the order listed above. As long as there are enough assets to satisfy all of the claims in a given tier, then the creditors within that tier are to be paid in full.

As soon as you reach a tier for which there are not sufficient assets to pay all creditors in full, then each creditor in that tier receives a pro-rated amount of their total claim based on whatever is left, and any creditors in lower tiers receive nothing. For example, if the estate assets are sufficient to pay in full only the costs and expenses of administration and reasonable funeral expenses, then no other creditors of the estate will receive payment.

Bear in mind, though, that the categories listed above are for "unsecured" claims. If a creditor such as a mortgage lender has a claim "secured" by the decedent's primary residence, then that creditor can foreclose on the residence if there is not enough in estate assets to pay that creditor in full.[5]

Because "costs and expenses of administration" have priority over all other claims, legal fees and the personal representative's fee (if you choose to take one) can almost always be paid immediately out of the estate, ahead of any other creditor.

Also note that taxes have always received relatively high priority and that *the IRS can pursue you personally* if you fail to

[5] As a practical matter, so long as the monthly mortgage payment continues to get paid, the mortgage lender will generally not foreclose on the house. Once the house is distributed to whoever is to receive it, the mortgage lender may press to have the house refinanced but will typically take no action so long as the monthly mortgage payment is made.

pay them. Consequently, you will need to file at least one, and maybe as many as three, of the following tax forms:

- Form 1040, Personal Income Tax Return, is for income earned by the decedent between January 1 and the date of death.
- Form 1041, Fiduciary Income Tax Return, must be filed if the estate's gross income from the date of the decedent's death through final distribution of estate assets exceeds $600. For example, if the estate holds investment accounts that generate even modest revenue, this form will likely be required. However, many simple estates will not hold such assets, gross income will not exceed $600, and no Fiduciary Income Tax Return will be required. If required, the Form 1041 will be filed using the estate's EIN, which you obtained to open up the estate's bank account.
- Form 706, Estate Tax Return, must be filed if the estate's gross value, plus any significant transfers made during the decedent's life, exceeds $11.2 million dollars (in 2018).

ADMINISTERING ESTATE ASSETS

As personal representative, you are duty-bound to deal with estate property as a "prudent person" would deal with the property of another. Note that this is a standard of *conduct* rather than of *performance*. Your actions (or times of inaction) will be judged against what a reasonable person would have done in the same circumstances, given the same limitations to which you were subject and armed with the same information that was at your disposal.

If you conduct yourself properly, you will not be faulted if something bad happens, such as a decline in the value of estate assets. Acting reasonably under the circumstances is your basic job description; if you do that, you generally need not worry about being judged in the light of hindsight.

Note that, if you have or claim to have special expertise in connection with any facet of estate administration, you will be duty-bound to exercise that expertise. Thus, the standard for judging your job performance will take into account your special abilities (whether actual or claimed).

As personal representative, you are serving for the benefit of someone other than yourself, and you must always act to further the interests of the estate's beneficiaries. You should not enter a transaction that gives you an opportunity to benefit yourself at all, much less at the expense of the estate. If any situation should arise in which there is a conflict between your personal interests and the interests of the estate, you must put the interests of the estate first.

For example, you should not sell estate property to yourself, because this creates the appearance that you may have taken advantage of the estate. In fact, such a transaction will be voidable by the heirs to the estate, unless they have previously consented to the transaction or prior court approval for the transaction was obtained.

Similarly, you should never loan estate funds to yourself or to family members. The rules set forth in this paragraph are strictly applied not only to transactions in which you deal directly with yourself, but also to transactions in which you deal with entities (such as partnerships or corporations) in which you are personally interested. These rules apply even though a particular transaction may be scrupulously fair, and even if it is advantageous to the estate.

SIGNING CONTRACTS AND OTHER DOCUMENTS

Your duties in administering the estate's assets will likely include executing contracts and other documents on behalf of the estate.

When acting in your official capacity as personal representative, you are generally shielded from personal liability for the estate's obligations, *provided* you observe certain important requirements, such as disclosing that, in signing a document on behalf of the estate:

- the *estate* is the party to the contract, not you individually (e.g., the contract names "the Estate of John Doe" as a party to the agreement), and
- it is clear that you are signing on behalf of the estate, not in your individual capacity (e.g., "*Your Signature,* Personal Representative").

Failure to do either can deprive you of the liability protection to which you are entitled and can result in your being held personally liable for claims made by the other party to the agreement.

DISTRIBUTE REMAINING ASSETS

After you pay all valid claims against the estate, you will then distribute the remaining assets according to the decedent's Will or, if the decedent died intestate, according to state law.

Before final distribution is made, you will need to account to the heirs and/or devisees for your administration of the estate. This accounting report must start with the initial inventory and appraisement of estate assets and then detail every bit of income to the estate, and every expense paid out of the estate, during your administration.

The heirs and devisees then have an opportunity to question or object to the accounting. As a result, it is critical that you keep very detailed records of all transactions occurring during your administration. If you intend to charge a fee for acting as personal representative, you must keep a detailed journal or log setting forth all of your time spent in administrative duties on behalf of the estate.

CLOSE THE PROBATE

After all of the estate's assets have been distributed to the heirs or devisees, your final task is to file a Closing Statement with the Court. The Closing Statement affirms that you have complied with all of your duties and that the estate's administration is complete.

In an *informal probate,* the probate will remain open and inactive for one year from the filing date of the Closing Statement. If no interested party decides to assert their rights to estate assets during that one-year period, you will be officially released from your duties by the Probate Registrar, and the probate matter will be officially closed.

In a *formal probate,* you must file a Petition with the Court for an order of complete settlement. If the Court determines that the estate has been fully administered and that proper accountings have been made of your administration, the Court will issue an order of settlement and discharge you from further responsibility.

CONCLUSION

Please keep in mind that the contents of this handbook are far from exhaustive. Rather, they are intended to alert you to your duties and to impress upon you the significance of your responsibilities.

To repeat an earlier suggestion, don't be overly cautious in seeking legal or other professional advice. That advice may cost something in the short run, but the cost can be far less than it takes to fix a mistake later on. The estate will pay the reasonable costs associated with your obtaining advice; conversely, you could end up paying out of your own pocket for your failure to secure advice when you needed it.