THE HOUSTON
lawyer
Volume 51 - Number 3
November/December 2013

The Houston Lawyer Celebrates 50 Years

MR. MICHAEL J. CENATIEMPO
CENATIEMPO & DITTA, L.L.P.
770 S POST OAK LN STE 500
HOUSTON TX 77056-1974

Top Ten Perils for Probate Executors and Administrators

By GUS G. TAMBORELLO

An executor or administrator of an estate assumes all duties of a fiduciary as a matter of law.[1] An independent executor has the same responsibilities and duties as does an administrator acting under the direction of the probate court.[2] The fiduciary duties of a personal representative of an estate are the same as the fiduciary duties of a trustee.[3] A fiduciary has a duty to protect the beneficiaries' interests by dealing in good faith and with integrity.[4] Therefore, a representative must be aware of the many pitfalls associated with serving in that capacity.

1. Failing to prepare or file an inventory and list of claims

A representative must prepare and file an inventory and list of claims within 90 days after the representative qualifies, unless the time period is extended by the court.[5] If there are no unpaid debts, except for secured debts, taxes and administration expenses, at the time the inventory is due, a representative may file an affidavit in lieu of the inventory but must nonetheless provide a complete inventory to the beneficiaries.[6]

The inventory must list all of the property that has come to the representative's "knowledge or possession," and shall include all real property in the State of Texas and all personal property of the estate wherever situated.[7] The list of claims must include a list of all claims due and owing to, not by, the estate.[8] The inventory must be verified by the personal representative as a true and complete statement of the property and claims of the estate that have come to his or her knowledge.[9]

One purpose of an inventory is to provide notice to beneficiaries and creditors of the estate of what the representative claims to be the estate assets and claims. A holder of a secured claim may want to know if there are sufficient liquid assets to pay his claim so that he will know whether to elect to have his claim treated as a matured secured claim or as preferred debt and lien.[10] Likewise, a holder of an unsecured claim may want to know if the estate has sufficient assets with which to pay his claim in light of the fact that his claim is the last in priority to be paid.[11] The beneficiaries want to know what assets the executor claims are in the estate.

A representative who fails to file an inventory may be removed.[12] In 2013, the Texas Legislature added a provision taking effect on January 1, 2014, which will also allow the court to fine the representative up to $1,000 for failure to timely file the inventory or an affidavit in lieu of it.[13]

2. Failing to prepare or file a correct inventory or properly value estate assets

In addition to listing assets and claims belonging to the estate, the inventory must include an appraisement of the fair market value of each asset or claim as of the date of death of the decedent, and state whether the property was the separate or community property of the decedent.[14] The court may appoint appraisers to assist the representative with the determination of fair market value.[15]

Any interested person may attack the inventory by showing that property contained in it does not belong to the estate, or that property belonging to the estate has not been included in it.[16] Any interested person may also challenge the inventory if it is believed to be unjust or erroneous.[17] A representative should carefully examine the decedent's papers and records to determine the nature and extent of the assets, and, if necessary, obtain an appraiser to assess the fair market value of the property. An appraisal is especially prudent if it appears the estate is going to be a taxable estate that must file an estate tax return. Valuation is also important because assets receive a change in tax basis upon death.[18]

A common point of contention is the representative's characterization of property as separate or community, particularly when the decedent has a surviving spouse and children from a prior marriage. The executor spouse may characterize an asset as community property when the children believe it was their parent's separate property. Likewise, the executor child may characterize an asset as separate property when the spouse believes it is community property.[19] If there is a challenge to the inventory on the basis of such a characterization, and if it is not cost-prohibitive, the representative may have to employ a forensic accountant to trace the origin of the property.

3. Prematurely distributing estate assets

Many beneficiaries mistakenly believe they are immediately entitled to their share of the estate upon the decedent's death. Although title "vests" in the beneficiaries or heirs upon the decedent's death, inheritance is subject to the estate's administration.[20] The representative has the right and duty to take possession of the estate's assets before they are distributed to the heirs,[21] and must address the decedent's debts and claims before making any distribution of the assets. Often, the heirs will converge upon the decedent's house shortly after the decedent's death and begin "dividing" the decedent's property, but the representative should avoid the temptation to appease the beneficiaries and keep possession of the property until the overall condition of the estate is better understood.

The representative must move cautiously before distributing the property. If there is a will, one or more of the beneficiaries may file a contest contending the will is invalid, and may offer for probate a previous will that leaves the property in a different manner than the "last" will. If the decedent dies without a will, the heirship proceeding may not be straightforward, and could present issues concerning common-law spouses and persons claiming to be a child of the decedent. The representative should keep in mind that a beneficiary cannot compel a distribution of estate assets until two years from the date the representative was appointed.[22]

4. Mishandling the decedent's debts

Most people die with some debt. There may be both secured creditors, such as mortgage companies, and unsecured creditors, such as credit card companies. A representative is required to give certain notices to creditors. Within one month of being appointed, a representative must publish in a newspaper a general notice to creditors.[23] Within two months after appointment, the representative must send actual notice to any secured creditor by certified mail.[24] If the representative fails to give the required notices, the representative and the surety on the representative's bond shall be liable for any damage for failure to give the required notice, unless it appears that the individual otherwise had notice.[25]

Many representatives believe that all debts must be paid, and some begin paying the decedent's bills right away. This is usually a bad decision because Texas law also allows for "permissive notice" to unsecured creditors.[26] The representative may send unsecured creditors a notice by certified mail notifying them that they must present their claims in a certain manner before the 121st day after the date of the receipt of the notice, and their failure to do so will result in their claims being barred, even when the general statute of limitations would not bar them.[27] The permissive notice process is a powerful tool for avoiding payment of some unsecured claims that is often overlooked by representatives. Keep in mind that the representative owes a fiduciary duty to the beneficiaries of the estate,[28] and holds the property in trust for the benefit of the title holders, rather than the creditors.[29]

5. Failing to acknowledge the rights of the surviving spouse or dependent children

The most common conflict in estates is between the decedent's surviving spouse and the decedent's children from a prior marriage. Often, those children will attempt to force the decedent's surviving spouse out of their parent's house. Nevertheless, the decedent's surviving spouse and minor children have a homestead right in the house regardless of the characterization of the property,[30] and the representative is required to set apart the homestead for the surviving spouse's benefit.[31] Furthermore, the homestead passes free of claims against the decedent's estate, except as provided by statute.[32]

If the decedent died without a will and the homestead was the decedent's separate property, the surviving spouse is entitled to a life estate in one-third of the property.[33] Therefore, although the children of the decedent may own the underlying interest in the property, their interest is subject to the surviving spouse's life estate. Although similar to a homestead right, the life estate is a separate legal interest that has a monetary value based upon the value of the property and the life expectancy of the surviving spouse.

6. Failing to give beneficiaries proper notice and failing to keep them informed

No later than the 60th day after the date of an order admitting a will to probate, the representative shall give notice to each beneficiary by certified mail that the will was probated and provide a copy of the will or a summary of the gifts to the beneficiary.[34] Failure to provide the notice can subject the representative to removal.[35]

Further, the fiduciary duties owed to the beneficiaries include disclosure of all material facts known to the representative that might affect the beneficiaries' rights.[36] This fiduciary relationship requires the representative to disclose fully and fairly to the beneficiaries matters pertinent to the estate.[37] If challenged, the representative has the ultimate burden of showing that he or she acted fairly and informed the beneficiaries of all material facts.[38]

After 15 months have passed from the issuance of letters, the beneficiaries may make a demand for a formal accounting by the independent executor.[39] If demand is made, the independent executor must provide a signed and sworn written statement of account within 60 days or his or her compliance can be compelled by the court.[40] Moreover, failure to file a required accounting may be a ground for removal.[41] A dependent administrator is required to file annual accountings and a final accounting without demand by the beneficiaries.[42]

7. Failing to collect or protect estate property

The representative shall take care of estate property just as a prudent person would treat his or her own property.[43] The representative must maintain any real property in good repair, unless directed not to do so by court order.[44] The representative shall take possession of the personal property and records of the estate.[45] The executor should sell any property that is liable to perish, waste or deteriorate in value, or that will be a disadvantage to the estate if kept.[46]

A representative must be diligent in collecting all claims and debts due the estate, and recovering property belonging to the estate, provided that there is a reasonable prospect of collecting such claims or of recovering such property.[47] If a representative willfully neglects to use such diligence, the representative and the surety on the bond may be liable for the value of the property that has been lost by the representative's neglect.[48]

A representative may be removed if proven to have been guilty of gross misconduct or mismanagement in the performance of his or her duties.[49] A representative may also be subject to a suit for breach of fiduciary duty.

8. Commingling estate funds with personal funds

A representative is prohibited from commingling estate funds with any personal funds or any other non-estate assets.[50] Although an estate in Texas is not a legal entity, it is considered to be a separate taxpayer by the Internal Revenue Service (IRS). Therefore, the representative should obtain a tax identification number (Form SS-4) for the estate. The representative must then place the funds in an estate bank account. If the executor was a joint account holder with the decedent prior to the decedent's death, the proceeds of the account belong to the estate unless the account was set up as *joint with right of survivorship or payable on death*.[51] Therefore, the joint account holder/executor should close the decedent's account and transfer it to an account under the estate's tax identification number.

A representative can be removed for misapplying estate property.[52] A representative may also be subject to a suit for breach of fiduciary duty for commingling funds.

9. Failing to pay taxes or file tax returns

The representative must file a final income tax return (Form 1040) on behalf of the decedent for the year of death and any returns not filed for preceding years.[53] Furthermore, because an estate is a separate taxable entity, the representative must file an estate income tax return (Form 1041) if the income exceeds $600.[54] Any accounting of a dependent administrator must contain verification that tax returns due during the accounting period have been filed and that all taxes due and owing have been paid.[55]

If the decedent's gross estate (which includes probate and non-probate assets) exceeds the amount of the applicable exclusion amount on the date of the decedent's death, the representative must file an estate tax return (Form 706) within nine months after that date, unless the time period is extended.[56] A willful failure to file the estate tax return or to pay the tax constitutes a misdemeanor and subjects the representative to a fine.[57] Further, the IRS will impose a penalty for failure to timely file the return or pay the tax.[58]

A claim of the United States Government must be paid before the decedent's other debts are paid.[59] A personal representative who does not give priority to the claims of the United States can be held personally liable.[60]

10. Receiving compensation when none is allowed or receiving too much

Most wills have a provision addressing executor compensation. The executor is bound by the compensation provision in the will.[61] If there is no will, or if the will does not address compensation, the representative's compensation is governed by statute.[62] The statute provides the representative shall be entitled to receive a commission of five per cent cash received and five per cent on sums paid out in cash on a finding that the representative has taken care of and managed the estate in compliance with the Texas Probate Code.[63] The court may modify the compensation amount if the statutory formula results in an amount which is "unreasonably low."[64] The court may deny a representative's commission if the representative has not taken care of the property prudently or has been removed.[65]

Conclusion

There is an aphorism which states, "no good deed goes unpunished." The job of a personal representative is fraught with many potential hazards. Therefore, the representative should take his or her job seriously and make every effort to fulfill his or her duties and treat the estate with utmost care.

Gus G. Tamborello specializes in probate law and is a frequent author and speaker on subjects relating to estates, trusts, and guardianships. He also serves as a mediator in probate cases and has taught as an adjunct professor at the University of Houston Law Center.

Endnotes

1. *Punts v. Wilson*, 137 S.W.3d 889, 892 (Tex. App.—Texarkana 2004, no pet.).
2. *Walling v. Hubbard*, 389 S.W.2d 581, 590 (Tex. Civ. App.—Houston 1965, writ dism'd w.o.j.).
3. *In re Roy*, 249 S.W.3d 592, 596 (Tex. App.—Waco 2008, pet. denied) (citing *Humane Society, Etc. v. Austin Nat'l Bank*, 531 S.W.2d 574, 577 (Tex. 1975)).
4. *Id.*
5. TEX. PROB. CODE ANN. § 250(a) (West 2013) [TEX. ESTATES CODE § 309.051(a)].
6. TEX. PROB. CODE ANN. § 250(c) (West 2013) [TEX. ESTATES CODE § 309.056(b)].
7. TEX. PROB. CODE ANN. § 250(a) (West 2013) [TEX. ESTATES CODE § 309.051(a)].
8. TEX. PROB. CODE ANN. § 251 (West 2013) [TEX. ESTATES CODE § 309.052].
9. TEX. PROB. CODE ANN. § 252 (West 2013) [TEX. ESTATES CODE § 309.053].
10. TEX. PROB. CODE ANN. § 146(b) (West 2013) [TEX. ESTATES CODE § 403.052]; TEX. PROB. CODE ANN. § 306(a) (West 2013) [TEX. ESTATES CODE § 355.151(a)].
11. TEX. PROB. CODE ANN. § 322 (West 2013) [TEX. ESTATES CODE § 355.102] (unsecured claims are Class 8 claims).
12. TEX. PROB. CODE ANN. § 149C(a)(1) (West 2013) [TEX. ESTATES CODE § 404.0035].
13. TEX. ESTATES CODE § 309.057.
14. TEX. PROB. CODE ANN. § 250(b) (West 2013) [TEX. ESTATES CODE § 309.051(a)(2), (b)].
15. TEX. PROB. CODE ANN. § 250(a) (West 2013) [TEX. ESTATES CODE § 309.051(b)(2)].
16. *Moore v. Wooten*, 280 S.W. 742, 746 (Tex. Comm'n App. 1926); TEX. PROB. CODE ANN. §257 (West 2013) [TEX. ESTATES CODE § 309.102].
17. TEX. PROB. CODE ANN. § 258 (West 2013) [Tex. Estates Code § 309.103].
18. 26 U.S.C. § 1014.
19. Property possessed by either spouse on dissolution of the marriage is presumed to be community property. TEX. FAM. CODE ANN. § 3.003(a) (West 2013). The presumption can be overcome only by clear and convincing evidence. TEX. FAM. CODE ANN. § 3.003(b) (West 2013).
20. TEX. PROB. CODE ANN. § 37 (West 2013) [TEX. ESTATES CODE §§ 101.001-101.003].
21. TEX. PROB. CODE ANN. § 232 (West 2013) [TEX. ESTATES CODE § 351.102 (the representative shall immediately take possession of the estate property)].
22. TEX. PROB. CODE ANN. § 149B (West 2013) [TEX. ESTATES CODE § 405.001].
23. TEX. PROB. CODE ANN. § 294(a) (West 2013) [TEX. ESTATES CODE § 308.051]; TEX. PROB. CODE ANN. § 146(a)(1) (West 2013) [TEX. ESTATES CODE § 403.051(a)(1)].
24. TEX. PROB. CODE ANN. § 295(a) (West 2013) [TEX. ESTATES CODE § 308.053]; TEX. PROB. CODE ANN. § 146(a)(1) (West 2013) [TEX. ESTATES CODE § 403.051(a)(1)].
25. TEX. PROB. CODE ANN. § 297 (West 2013) [TEX. ESTATES CODE § 308.056].
26. TEX. PROB. CODE ANN. § 294(d) (West 2013) [TEX. ESTATES CODE § 308.054(b)(1)]; TEX. PROB. CODE ANN. §146(a)(2) (West 2013) [TEX. ESTATES CODE § 403.051(a)(2)].
27. TEX. PROB. CODE ANN. § 146(b-4) (West 2013) [TEX. ESTATES CODE §§ 403.051, 403.056].
28. *Mohseni v. Hartman*, 363 S.W.3d 652, 657 (Tex. App.—Houston [1st Dist.] 2011, no pet.).
29. *Id.* at 658.
30. TEX. PROB. CODE ANN. § 271 (West 2013) [TEX. ESTATES CODE § 353.051].
31. TEX. PROB. CODE ANN. § 272 (West 2013) [TEX. ESTATES CODE § 353.052].
32. TEX. PROB. CODE ANN. § 270 (West 2013) [TEX. ESTATES CODE § 102.004].
33. TEX. PROB. CODE ANN. §38(b) (West 2013) [TEX. ESTATES CODE § 201.002].
34. TEX. PROB. CODE ANN. §128A (West 2013) [TEX. ESTATES CODE §§ 301.001-308.004].
35. TEX. PROB. CODE ANN. §149C(a)(4) (West 2013) [TEX. ESTATES CODE § 404.0035]; TEX. PROB. CODE ANN. §222(b)(7) (West 2013) [TEX. ESTATES CODE § 361.052].
36. *Montgomery v. Kennedy*, 669 S.W.2d 309, 313 (Tex. 1984).
37. *In re Roy*, 249 S.W.3d 592, 597 (Tex. App.—Waco, 2008, pet. denied).
38. *See Lesikar v. Rappeport*, 33 S.W.3d 282, 298 (Tex. App.—Texarkana 2000, no pet.).
39. TEX. PROB. CODE ANN. § 149A (West 2013) [TEX. ESTATES CODE § 404.001].
40. *Id.*
41. TEX. PROB. CODE ANN. § 149C(a)(3) (West 2013) [TEX. ESTATES CODE § 404.0035(b)].
42. TEX. PROB. CODE ANN. § 399 (West 2013) [TEX. ESTATES CODE §§ 359.001-359.005]; TEX. PROB. CODE ANN. § 405 (West 2013) [TEX. ESTATES CODE §§ 362.003-362.004].
43. TEX. PROB. CODE ANN. §230 (West 2013) [TEX. ESTATES CODE § 351.101].
44. *Id.*

45. TEX. PROB. CODE ANN. § 232 (West 2013) [TEX. ESTATES CODE § 351.102].
46. TEX. PROB. CODE ANN. § 333(a) (West 2013) [TEX. ESTATES CODE § 356.051].
47. TEX. PROB. CODE ANN. § 233(a) (West 2013) [TEX. ESTATES CODE § 351.151].
48. *Id.*
49. TEX. PROB. CODE ANN. § 222(b)(4) (West 2013) [TEX. ESTATES CODE § 361.052(4)]; TEX. PROB. CODE ANN. §149C(a)(5) (West 2013) [TEX. ESTATES CODE § 404.0035(b)(3)].
50. *See Punts*, 137 S.W.3d at 892.
51. TEX. PROB. CODE ANN. § 438B(c) (West 2013) [TEX. ESTATES CODE § 113.1541].
52. TEX. PROB. CODE ANN. § 222(b)(1) (West 2013) [TEX. ESTATES CODE § 361.052(1)]; TEX. PROB. CODE ANN. §149C(a)(2) (West 2013) [TEX. ESTATES CODE § 404.001(2)].
53. I.R.C. § 6012(b)(1).
54. I.R.C. § 6012(a).
55. TEX. PROB. CODE ANN. § 399 (West 2013) [TEX. ESTATES CODE §§ 359.001-359.005]; TEX. PROB. CODE ANN. § 405 (West 2013) [TEX. ESTATES CODE §§ 362.003-362.004].
56. I.R.C. § 6018(a)(1), (a)(2), & (b).
57. I.R.C. § 7203.
58. I.R.C. § 6651(a)(1).
59. I.R.C. § 3713(a).
60. I.R.C. § 3713(b).
61. *Stanley v. Henderson*, 139 Tex. 160, 164, 162 S.W.2d 95, 97 (Tex. Comm'n App. 1942); Allen v. Berrey, 645 S.W.2d 550, 553 (Tex. App.—San Antonio 1982, writ ref'd n.r.e.).
62. TEX. PROB. CODE ANN.. § 241 (West 2013) [TEX. ESTATES CODE §§ 352.002-352.004].
63. *Id.*
64. *Id.*
65. *Id.*