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Recent Developments in Estate Planning for Arizona Residents

This article highlights recent legal developments regarding estate planning and asset protection for Arizona residents. I refer past clients of mine to this article to check for law changes that may affect their estate plan or legal documents. Updated from time to time as new developments occur, some topics remain in the article for several years so that everyone has a chance to read them.

1. Arizona Small Estate Affidavits

Summary: Arizona law permits higher value assets to avoid probate using affidavits.

In 2025, the Arizona legislature amended A.R.S. 14-3971, which increases the maximum value of real estate and personal property that may be transferred using a small estate affidavit after the death of the property owner. Effective June 30, 2025, an heir or successor to real property may take ownership by filing an Affidavit for Transfer of Title of Real Property with the local probate court; provided, however, the deceased owner's net equity does not exceed $300,000 (was $100,000). Also, effective June 30, 2025, an heir or successor to personal property (bank accounts, motor vehicles, non-retirement investments, etc.) may take ownership by presenting an Affidavit for Collection of All Personal Property to the relevant financial institution or government agency; provided, however, the combined value of such personal property does not exceed $200,000 (was $75,000). The effect of these changes is to reduce the specter of probate for most Arizona residents.

In summary:
For real property the maximum value increases from $100,000 to **$300,000**.
For personal property the maximum value increases from $75,000 to **$200,000.**

2. Arizona Visitation Law and Health Care Power of Attorney

Summary: Your health care power of attorney may permit your agent to restrict visitation.

In 2021, the Arizona legislature enacted A.R.S. 36-3211, which prescribes an assortment of rules and procedures regarding whether and how a health care agent may restrict the visitation of an incapacitated person. The law now requires a health care agent to "encourage and allow contact" between the principal (the incapacitated person) and other people who have a significant relationship to the principal. The health care agent may not restrict reasonable contact between the principal and any other person without prior court approval.

But there is an exception, and you will probably want to use it. You can include a provision in

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your Arizona health care power of attorney that specifically permits your agent to limit, restrict, or prohibit reasonable contact between you and any other person. This provision gives your health care agent the right to determine who is permitted to interact with you while you are incapacitated. Your agent will be able to restrict visitation by people who he or she believes might try to fraudulently persuade you to change your estate plan or others whose involvement in your life brings strife. For example, an ex-spouse or estranged child.

It is now common, and recommended, to include the following provision in an Arizona health care power of attorney: "I authorize my Health Care Agent to limit, restrict, or prohibit contact between me and any other person not named as an eligible Health Care Agent in this instrument." On the other hand, you might also view the issue another way. Perhaps you are concerned that your health care agent might unreasonably restrict visitation by your children from a prior relationship. In this case, you might choose to intentionally omit this provision in your health care power of attorney and rely upon the default law. Either way, it's an issue worth considering.

3. Arizona Homestead Exemption

<u>Summary</u>: The Arizona Homestead Exemption amount has increased to $425,200.

The Arizona homestead exemption amount increased from $250,000 to $400,000 in 2023 and will continue to increase with an annual inflation adjustment. The homestead exemption, which is automatic in Arizona, is intended to protect an Arizona resident's primary residence (“homestead”) from creditors. But the new law includes several intricacies that make it more complex than initially appears. For example, the new law requires any existing judgment liens (recorded in the same county) to be paid when the homeowner either sells or *refinances* the residence. The prior law stated that a homeowner with less equity than the exempt amount could still refinance a home loan without having to first pay off any existing judgment liens. The new law does the opposite – effectively preventing the homeowner from exercising a cash-out refinance.

The Arizona homestead exemption is also complicated by federal bankruptcy laws. If the home was acquired within 1,215 days (3 years, 4 months) of filing the bankruptcy case, the exemption amount is limited to $189,050 (subject to change). If this rule applies to you, be sure to investigate further with a bankruptcy attorney because there are some exceptions that may help.

4. SECURE Act Makes Major Changes to Retirement Accounts

Summary: 2019 tax law affects anyone with a retirement account naming a trust as beneficiary.

The SECURE Act, signed into law on December 20, 2019 (and supplemented with SECURE Act 2.0 in December 2022), is the most impactful legislation to affect estate planning in decades. Although the SECURE Act includes many positive changes in regard to tax-deferred retirement accounts, it no longer permits most non-spouse beneficiaries (e.g., children) to withdraw an inherited retirement account over the beneficiary’s life expectancy (aka “stretch IRA”). Instead, the default law now requires the entire account to be withdrawn and liquidated by the end of the 10th year after the death of the account owner (“10-year liquidation rule”). This change has major implications when considering whether to name an individual or trust as beneficiary of a retirement account.

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The 10-year liquidation rule results in the acceleration of income tax due, possibly causing a beneficiary to be bumped into a higher income tax bracket and receiving less money from an inherited retirement account than under the prior law. However, the SECURE Act does provide a few exceptions to the usual rule that are available to surviving spouses, beneficiaries less than 10 years younger than the account owner, children under age 21, and disabled individuals. But these exceptions only complicate the analysis because your estate planning objectives likely include more than just tax considerations. For example, you might be concerned with protecting a beneficiary's inheritance from future creditors and ex-spouses or preventing your spouse from disinheriting your children upon the spouse's remarriage. All these issues should be considered simultaneously when naming beneficiaries of a retirement account.

If your estate plan currently names a trust as the primary or secondary beneficiary of a retirement account (e.g., IRA, 401k, TSP), then you should reconsider whether this is still appropriate after the SECURE Act, and if yes, determine what type of trust to use. I have written an article, "Decision Tree for Naming Retirement Account Beneficiaries after the SECURE Act" which provides a structured analysis, i.e., a decision tree, for determining the answers to these questions. The article is available on the Articles Library page of my law firm website.

In some cases you may discover the reason you named a trust as beneficiary of a retirement account is no longer applicable, which permits you to name individuals as beneficiaries instead of a trust (although a trust restatement may still be appropriate in case circumstances change).

But in most cases the solution will be to integrate SECURE Act compliant provisions into your will or revocable living trust by restating it.

Arizona law provides a mechanism called a "decanting power" that gives your trustee a tool to fix the trust in the event you die before updating your estate plan. But relying on this mechanism invites an unnecessary hassle for your trustee. Doing nothing is a careless approach.

By integrating SECURE Act compliant provisions into your will or revocable living trust, you can ensure the trust qualifies as a *designated beneficiary*, which is necessary to use the most advantageous distribution rules under the SECURE Act.

5. Inheritance Protection Trusts

Summary: 2016 Arizona case exposes weakness in many inheritance protection trusts.

If your estate plan includes an inheritance protection trust for a child or other beneficiary, you may want to consider an amendment in response to a 2016 Arizona legal case.[1] The case involved an inheritance trust established for a child by his mother's will upon her death. The IRS filed a tax lien against the trust because the beneficiary owed substantial personal income taxes from prior years. The beneficiary argued that the inheritance was a "purely discretionary trust" and therefore

[1] Duckett v. Enomoto, U.S. District Court, D.Arizona; April 18, 2016.

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not a personal asset subject to the lien.[2] The judge ruled against the beneficiary based upon a careful review of the specific trust provision regarding distribution of income and principal.

The relevant provision stated, "The Trustee shall pay to [the beneficiary] so much or all of the net income and principal of the trust as in the sole discretion of the Trustee may be required for support in the beneficiary's accustomed manner of living, for medical, dental, hospital, and nursing expenses, or for reasonable expenses of education, including study at college and graduate levels."

The judge interpreted the phrase "shall pay" as a mandatory fiduciary duty owed to the beneficiary by the Trustee, although he also noted that specific calculations were left to the discretion of the Trustee. This approach is sometimes referred to as a "discretionary support" or "hybrid" trust. The combination of the Trustee's duty to make distributions ("Trustee shall pay to the beneficiary…") and the inclusion of guidelines regarding how to define support ("in the beneficiary's accustomed manner of living…") gives the beneficiary an underlying right to distributions from the trust – at least to the extent of the support guidelines. The judge applied this logic to permit the IRS to attach a lien to the beneficiary's interest in the trust.[3]

For maximum protection of inheritance you leave to others, it may be appropriate to amend your will or living trust to clarify your intent that a Trustee's power to make distributions is purely discretionary and not mandatory. Otherwise, a creditor could use the above-described case to establish a legal argument that diminishes, or worse, eliminates the protections you intended to create.

If your trust was drafted by a WealthCounsel attorney using its proprietary WealthDocx software[4], it probably does not include the type of extraneous wording ("in the beneficiary's accustomed standard of living") that contributed to the adverse ruling in this case. However, the software, by default, uses the phrase "shall pay" and that may be enough to give creditors a slight opening to argue that you intended to create a discretionary support trust. Thus, in response to this recent Arizona case, I recommend an amendment that does the following:

- Adds a sentence, "The discretion to make distributions includes the discretion to exhaust the principal or to make no distributions at all."
- Adds a sentence with conservative guidelines of this nature, "Accordingly, I request that my Trustee always consider the other known resources available to the beneficiary before making discretionary distributions."

I believe that these changes will eliminate any ambiguity about your intent and strengthen the protection an inheritance trust can provide.

6. Certification of Trust

Summary: Arizona amends law encouraging acceptance of a Certification of Trust.

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[2] A purely discretionary trust does not grant a property interest to the beneficiary because the Trustee is not legally obligated to make any distributions to the beneficiary. See A.R.S. 14-10504(E).

[3] Whether the IRS could immediately seize assets from the trust to pay the lien is a different matter and was not ruled upon in this case.

[4] Bouman Law Firm has used WealthDocx software exclusively since October 2006.

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In 2018, the Arizona legislature amended the law regarding Certification of Trusts (A.R.S. 14-11013, revision effective 8/3/2018). When a trustee provides a Certification of Trust to a financial institution, it may not require the trustee to provide copies of excerpts from the trust document that contain dispositive provisions (i.e., who gets what) or successor trustee names (i.e., who will manage the trust upon death of trustor) unless the financial institution also provides a verified statement that states a reasonable basis for the request.

A financial institution is now liable for damages, costs, expenses, and attorney fees if a court determines that it did not act in good faith or did not comply with the need for a verified statement in demanding a copy of the trust document.

In summary, the law change reinforces the legislature's intent to simplify the process of doing transactions with trusts. When buying or selling property using a trust, or opening or re-titling an account into a trust, a trustee needs only to provide a copy of the Certification of Trust and not the entire document. Financial institutions that still request a copy of the entire trust document are acting unreasonably and, in some cases, against the law.

7. Estate Tax

Summary: Federal estate tax exemption increases again.

For people who die in 2025, up to $13,990,000 may be transferred free of estate tax using the basic exclusion amount. The exclusion amount is unified with the gift tax because the exclusion amount is reduced by the total amount of taxable gifts made during the deceased person's lifetime. Thus, lifetime gifts of $1 million would reduce the basic exclusion amount to $12,990,000 million. The exclusion amount is adjusted annually for inflation.

The current law expires on December 31, 2025. If Congress fails to extend the current law, the applicable estate tax exemption would drop to approximately $8,000,000.

8. Testamentary Powers of Appointment

Summary: Increase in federal estate tax exemption affects testamentary powers of appointment.

If your estate plan includes an inheritance protection trust for a child or other beneficiary, the provision likely gives the beneficiary a testamentary power of appointment. This permits the beneficiary, effective upon the beneficiary's death, to redirect any remaining trust assets among individuals or charities of the beneficiary's choice. When avoiding estate tax is a major concern, it makes sense to define the power of appointment in a manner that restricts the beneficiary from using trust assets to pay off personal debts. This has the effect of allowing trust assets to pass to the successor beneficiaries free of estate tax, which is important for large estates. But the *limited* power of appointment also prevents the successor beneficiary from getting a step-up in income tax basis, which can increase capital gains tax upon sale of trust assets.

The current estate tax exemption, now dramatically higher than it was just a few years ago, eliminates the estate tax as a planning issue for all but the very wealthy. This means it makes more sense to refrain from using *limited* powers of appointment in inheritance trusts. Why? The reason

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is because the value of *potentially* avoiding estate tax is outweighed by the more likely benefit of reducing income tax. In summary, the better alternative for modest sized estates is to use a *general* power of appointment that excludes the limitation described above.

9. Planning for Digital Assets

Summary: Estate planning for digital assets is a trending area of law development.

In 2016, the Arizona Legislature enacted a law entitled, "Uniform Fiduciary Access to Digital Assets Act." The Act extends the rights a fiduciary (personal representative, trustee, agent) already possesses to manage tangible property to also include digital assets like computer files, access to Internet sites, and online digital media, but restricts a fiduciary's access to electronic communications unless the original user consented in a will, trust, power of attorney, or other record.

About the Author

Thomas J. Bouman provides legal counsel in the areas of estate planning, estate administration, and asset protection. He brings a highly systematic approach to the practice of law, which is critically important when wading through the complex, and often bizarre, legal requirements associated with estate and trust law. Mr. Bouman is the author of the Arizona Estate Administration Answer Book and a prominent member of WealthCounsel, the nation's premiere organization of estate planning attorneys.

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