LEE KIEFER & PARK
TRUST AND ESTATE ATTORNEYS

Preparing the Inventory and Accounting

1. **Introduction:** This memo addresses the preparation of an Inventory and Accounting for those who have been officially appointed by the Court as a fiduciary with the responsibility to manage an "estate,"[1] such as an executor, an administrator, or a trustee of a trust. The Inventory and Account should present financial information in a format which is understandable and meaningful to the interested parties. The information should clearly show what came into the estate, what went out, and what is left at the end of the accounting period.

    a. **Asset Administration:** Generally, your tasks are to:

        i. Collect all assets[2] belonging to the estate;
        ii. Manage and invest assets;
        iii. Pay debts and taxes; and
        iv. Distribute the remaining assets to the person(s) entitled thereto.

    b. **Marshalling Assets:** "Marshalling assets" is the process of taking control/possession of the assets of the estate. This will include registering assets, such as financial accounts, real estate, vehicles, etc., in your name as personal representative or trustee. The estate assets should always be kept separate from your personal assets, and should never be used for your own purpose.

    c. **Inventory Generally:** The Inventory is a list of all the assets that belong to the estate.

    d. **Account Generally:** In the first account, you will start with the Inventory amount, add receipts (including gains on sales), and subtract disbursements (including losses on sales) to show what is left ("assets on hand"). After the first account, you are generally required to file an annual account, using the prior year's ending value as the starting point for the new account. This can usually be done on a fiscal year beginning with the first day of the month of your appointment.

[1] The "estate" consists of all assets subject to the proceeding. Generally, this includes assets held in the name of the trustee (for trusts), the decedent (for probates) or the ward (for guardianships).

[2] the words "property" and "assets" are used interchangeably. Real property outside of Nevada is not subject to the jurisdiction of the Nevada courts, and local legal counsel should be retained where such real property is located.

e. **Engaging a CPA**: Except for the simplest of estates, it is strongly recommended that you engage a certified public accountant to keep track of the Inventory, receipts, and disbursements, and to prepare all required tax returns. You will normally be required by law to prepare and file a fiduciary income tax return (IRS Form 1041) for an estate or trust, as well as a federal estate tax return (IRS Form 706) for probate estates that have a gross value exceeding the "applicable exclusion" for estate tax purposes.[3] Engaging a CPA will ensure that the fiduciary accounting and tax returns are properly coordinated. Under normal circumstances, the fees charged by the CPA are paid for from the funds of the estate or trust, and you will not be personally liable for such fees.

2. **INVENTORY:** The Inventory is a list of all the assets that belong to the estate. You should identify, describe, and value each asset. Often, the Inventory will contain schedules, with each type of asset reported on a different schedule. The Inventory becomes the "starting point" for the first accounting.

   a. **Categories:** An Inventory will often be categorized by the type of assets included in the estate. At a minimum, the assets can be separated between real property and personal property. Often, an estate with significant assets is broken into more categories, each listing the assets of that category on a separate exhibit. Some of these categories include tangible personal property, business interests, promissory notes/receivables, and securities.

      i. **Real Property:** You should review how real property is titled to confirm it belongs to the estate. Real property can be owned solely, as a joint tenant, as a tenant in common, or as community property. You should determine whether the estate has an ownership interest in the real property, and what percentage the ownership is. Only the portion that is owned by the estate is appropriate to record on the Inventory.

      ii. **Personal Property:** Personal property encompasses all other assets that are not classified as real property. Personal property can include tangible assets like vehicles, precious metal, and collectibles, as well as intangible assets such as bank accounts, business interests, and receivables.

      iii. **Household items:** Miscellaneous household items and personal effects that have relatively little value are typically not listed out individually on the Inventory. These items are best handled by grouping them together as one line-item and estimating a value for all items combined.

[3] Internal Revenue Code § 2010(c) provides for an "applicable exclusion" for estate tax purposes, which is the cumulative amount that can pass free of estate tax.

1. Items that are specifically listed in a will or trust should be listed separately and not grouped in this catch-all category.

2. Items that are part of a collection (stamps, coins, or other collectibles) should be listed and valued as a collection and not individually.

b. **Identifying Assets:** The assets on an Inventory should be clearly identified and described in reasonable detail. All items should be valued as of the decedent's date of death (not the date the assets are appraised or the date the inventory is prepared).

i. **Value:** The assets are to be valued at their fair market value. Fair market value is the price at which the property would be sold between a willing buyer and a willing seller, both having reasonable knowledge of the relevant facts.

1. The value of some assets can be determined very easily. Bank accounts, publicly-traded securities, and vehicles that are listed in a valuation book can often be listed without a formal appraisal. Real estate, valuable jewelry, and other special collections should be appraised by an independent appraiser. Business interests can be valued by a certified public account or other business valuation expert.

2. Whether the value on the Inventory is listed as the gross value, or is reduced by liens or encumbrances and is listed as the net value will depend on the relevant local rules.

3. When possible, you should not round off numbers, and should instead use exact dollar and cents.

4. Any reasonable expenses incurred in determining the values to place on estate assets, such as appraisals, are allowable as an administrative cost of the estate.

ii. **Descriptions:** The full description of each asset should be provided so as to identify the asset with reasonable certainty. The description should also indicate whether the estate only owns a portion of the asset.

1. Simply listing an asset as "checking account" or "home" is not acceptable.

    a. Financial accounts should list the name of the financial institution, the account type, and the account number.

    b. Real property should list the address, full legal description, and the assessor's parcel number.

    c. Vehicles should include the make, model, year, and VIN.

    d. Stocks and mutual funds should include company name, number of shares, and price per share.

    e. Bonds and promissory notes should include the issuer's name, face amount, interest rate, and maturity date.

2. As a general rule, the description should include enough detail that would be sufficient in order to transfer title.

3. At times there may be assets that have no recognizable market value, these may be valued at $1.00 or an estimated value until better information is obtained.

iii. **Amended Inventory:** Occasionally, you may discover additional assets after the Inventory has already been filed. In this case, you can prepare an Amended Inventory or a Supplemental Inventory. Additionally, if there were errors in the description or valuation of an asset, an Amended Inventory can be used to correct these errors.

3. **RECORD KEEPING:** You are not expected to be an accountant, but you should keep meaningful records of all transactions. While keeping a balanced checkbook is necessary, it is often not enough. You should keep track of all transactions in a ledger.

    a. **<u>Income and Principal</u>:**

        i. The initial "principal" is made up of the assets shown on the Inventory. If additional assets are discovered, these are "principal" items which need to be reflected on a supplemental or amended Inventory.

        ii. "Income" refers to revenues generated from the assets of the estate (the principal), and includes interest, dividends, rent, royalties, gains from the sale of estate assets, etc. Some payments may include income and principal, such as a mortgage payment which represents both interest and principal.

1. Example 1: if you sell an asset, the cash received is not a new asset, but simply a conversion of one asset (car) to another (cash). Your records would show a "disbursement" of the car and a "receipt" of the cash. If the car is sold for a price different than the value shown on the Inventory, the difference would be a gain or loss and categorized as income.

2. Example 2: if you receive a payment on a promissory note or other debt that was shown on the Inventory as an asset, the interest amount is "income" and the amount paid down on the loan is "principal." The present value of the note is reduced by the amount of principal that is now represented by the cash payment.

b. **Journal Entries:** You must keep an exact record of all receipts and disbursements in and out of the estate. Your records should reflect whether each transaction represents principal or income.

i. As receipts and disbursements are made, you should clearly indicate the source of each receipt, the recipient of each disbursement, and the nature of each transaction. If you have diversified assets, you may wish to keep a separate ledger for each asset.

ii. We strongly recommend that you use a "double entry" bookkeeping system so that each entry reflects a "credit" to one account and a "debit" to another. For example, a payment of a medical bill is a debit to the "Checking" account and a credit to the "Creditors' Claims" account. A receipt of an account receivable may be a debit to the "Checking" account, and a credit to "Accounts Receivable."

c. **Account Generally:** In the first accounting, you will start with the Inventory amounts, add receipts (including gains on sales), and subtract disbursements (including losses on sales) to show what is left ("assets on hand"). After the first account, you are generally required to file an annual accounting, using the prior year's ending value as the starting point for the new accounting. This can usually be done on a fiscal year beginning with the first day of the month of your appointment.

i. **Final Account:** When the estate is ready to be closed, you will need to prepare a final account, which may be in conjunction with a petition for permission to make a final distribution of the estate. For some estates, the first account can also be the final account.

4. **Account:** You must file an account with the court by the statutory deadline. This is often an annual account, but may differ by jurisdiction depending on the local rules. The first account may be due within a few months of starting the probate or taking over as trustee.

   a. **Content of Account:** The account should state the period covered and contain a Summary of the Account that is supported by detailed schedules. The account will usually show the following information:

      i. Property on hand at the beginning of the accounting period,
      ii. Income receipts,
      iii. Gains on sales,
      iv. Net income from a trade or business,
      v. Disbursements,
      vi. Losses on sales,
      vii. Net losses from a trade or business,
      viii. Distributions to beneficiaries, and
      ix. Property on hand at the end of the accounting period.

   b. **Summary of Account:** The Summary of Account is a recap of the total charges to and credits from the estate. Each category will be supported by an attached schedule with details for each transaction. The "Total Charges" represent the total amount for which you are responsible, and the "Total Credits" represent the amount actually accounted for. Of course, the amount for which you are responsible and the amount for which you can account should be identical. The Summary of Account could look something like this:

CHARGES	
Description	***Amount***
Inventory	$304,851.49
Income Receipts	$9,183.06
Gains on Sales	$2,232.32
TOTAL CHARGES	$316,266.87
CREDITS	

1707 Village Center Circle, Suite 150, Las Vegas, NV 89134
Tel: 702.333.1711 | Fax: 702.333.1712
lkpfirm.com

Description	*Amount*
Disbursements	$23,432.43
Losses on Sales	$1,900.00
Distributions	$15,000.00
Assets on Hand	$275,934.44
TOTAL CREDITS	$316,266.87

c. **Schedule of Receipts and Disbursements:** The two primary schedules that should be attached to the Summary of Account are the Schedule of Income Receipts and the Schedule of Disbursements.

i. The Schedule of Income Receipts should show the following:

1. The amount
2. The date
3. The source, including details to identify the income source (such as account numbers)
4. Description (e.g. interest income, dividend)

ii. The Schedule of Disbursements should show the following:

1. The amount
2. The date
3. The payee
4. The purpose (e.g. insurance, tax, filing fees, etc.)

a. If the expense is unusual or appears questionable, you should provide additional information in a note attached to the Schedule.

iii. You can list the receipts and disbursements chronologically or by category.

iv. If there are repetitive transactions, such as monthly interest income from one particular account, you can list the total as one line-item. However, you must keep a backup schedule detailing the transactions in that group and attach that backup schedule to the Account.

d. **Other Schedules:**

i. **Schedule of Gains and Losses:** gain or loss is the difference between the gross sales price and the value of the asset as shown on the Inventory.

1. Sale of estate assets should be listed on a schedule for Gains on Sales if the asset was sold for more than the value shown on the Inventory.

2. Sale of estate assets should be listed on a schedule for Losses on Sales, if the asset was sold for less than the value shown on the Inventory.

3. The schedule should list both the gross sales price and the value as shown on the Inventory, and show the calculations to reach the net gain or loss.

4. The details of the sale should also be provided, including: the date of sale, the purchaser, and the description of property sold.

5. If an asset was sold that had no gain or loss, you still need to report the transaction, and show the gain as $0.

ii. **Schedule of Distributions:** all cash or property that has been distributed to an heir or beneficiary of the estate should be listed.

1. The schedule should include the date and value of the asset distributed at the value shown on the Inventory.

2. A Receipt of Distribution should be signed by the person receiving the property and filed with the court as proof that the property was in fact distributed and received by the person entitled to it.

iii. **Schedule of Property on Hand:** this schedule contains a detailed list of all the current assets on hand at the end of the accounting period. This is essentially an updated inventory as of the end of the accounting period. You will usually not be required to update valuations or appraisals.

5. **Subsequent Accounts And Distributions:** You will be required to file periodic accounts, usually annually, but this will depend on your local rules. At the end of each period, you will prepare a similar account until the estate is ready to be terminated.

a. **Number the Account:** Each account should be numbered (First, Second, Third, etc.). The final account should be numbered and titled "Final" (i.e. Third and Final).

b. **Final Account**: A probate proceeding is terminated when creditors have been paid and the estate is ready for final distribution. A trust proceeding is terminated when the trust instrument calls for final distribution of the remaining assets. The final account is like any annual account, but it also includes a Schedule of Proposed Distribution of the estate. Once the final account and proposed distribution is approved, the estate is ready to be distributed and terminated.

c. **Schedule of Proposed Distribution:** this Schedule contains a list of all the assets of the estate and the name of the beneficiary that will receive each asset. The Schedule should list a value for each asset, as of the date of distribution.

   i. The ultimate goal is to get the assets distributed into the hands of those entitled to them. It is common for a will or trust to be divided into shares for various beneficiaries or groups of beneficiaries. The trustee should strictly comply with the dispositive provisions of the governing instrument.

   ii. When there is no will or trust, then the intestate succession laws of the probate state will govern how the estate is to be distributed. The personal representative is obligated to make distributions in accordance with that statute.

d. **Receipts of Distribution:** A Receipt should be provided to the distributee for each distribution that is made. These Receipts should be signed, returned, and filed with the court (if applicable).

e. **Discharge:** For a probate, after all the Receipts are filed, the court will issue a "Final Discharge" Order which releases you from any further responsibility for the estate. At that point, the legal proceeding is completed.

6. Who is Entitled to an Account

a. The beneficiaries entitled to an account include "current beneficiaries" and "remainder beneficiaries."

   i. Current beneficiaries are all persons to whom the trustee is currently permitted or required to make distributions from the trust.

ii. Remainder beneficiaries are future beneficiaries who will be permitted to receive distributions upon the occurrence of an event, such as the death of the current beneficiaries.

iii. Accounts in a probate will be filed with the court, and interested parties to the estate proceeding should receive a copy.

b. The following individuals are NOT entitled to request a trustee's account:

i. A "remote beneficiary," which is a person who may become a current beneficiary upon the death of two or more persons, or upon the occurrence of some other event that cannot possibly occur during the beneficiary's lifetime.

ii. The beneficiary of a revocable trust (other than the person holding the power to revoke).

iii. A beneficiary who, under the terms of the trust instrument, is not entitled to a trustee's account.

NOTE: This memo provides general information only and does not contain legal, accounting, or tax advice. For brevity, this memo is oversimplified and should not be relied on for any particular situation.

1707 Village Center Circle, Suite 150, Las Vegas, NV 89134
Tel: 702.333.1711 | Fax: 702.333.1712
lkpfirm.com