The Weight of Your World

Understanding the New Reality of Your Retirement Future

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Educated Solutions

1405 Garden Street

San Luis Obispo, CA 93401

www.educatedsol.com

Ordering Information:

Quantity sales. Special discounts are available on quantity purchases by corporations, associations, and others. For details, contact the publisher at the address above.

Printed in the United States of America

"In God we trust, all others must pay cash."

"The only man who sticks closer to you in adversity than a friend is a creditor."

-Two American proverbs

I'd like to dedicate this book to my grandparents, my father's parents we affectionately called Nana and Nono, as well as my mother, Maureen, who have all passed from this life. These three people were paramount in shaping the person I am today.

-RM

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Introduction

The reason I got into the investment management business was because of my grandparents, whom I affectionately called Nana and Nono. I was very close to them. They both passed in the ’90s, and still today I consider both of them to be some of the best people I have ever known in my life. My Nono’s full name was Angelo Blasio Morelli. I named my firstborn Ronan Angelo Morelli in his honor. My father, who lives with us today after the sudden passing of my mother, was very close to them as well. My grandmother, Catherine Morelli, whom I affectionately called Nana, was one of the best cooks I have ever known still to this date. She didn't do much else but cook, pray, and sleep. I still find it interesting that she never drove a car. She was born in 1903 in Italy and immigrated to the United States in the early 1920s. Nono was born in 1897 and immigrated here around the same time as Nana, and they met soon after that.

We saw them often as they only lived about half an hour from our house. Generally, on Sundays, we would attend church and have a big meal. One weekend day in 1985, when I was 12 years old, we arrived at their house and something wasn't right. I noticed that my grandfather was sitting on the couch with a despondent expression on his face, and my grandmother was in the kitchen sitting at the kitchen table with her head in her hands. I knew that something was wrong. I immediately thought that maybe somebody had passed, or they had gotten some bad news from a relative, but no one had died. Instead, they had opened a piece of mail with bad news. This struck them as something they had never really understood could happen; they were simple and honest people. My grandfather was self-trained and had worked his whole life as a master electrician, and at this time, he was about 90 years old. They were very frugal as they both lived through the Great

Depression and saved their whole lives to amass about $100,000.

What I found out next made me very angry, even as a young boy. They were taken for about half of their life savings. Unfortunately, they hadn't asked for advice from my father or anybody else. As I said, they were simple people and had never really made any investments before in their lives. Initially, I remember my father shocked they would do this without asking him, until we learned who perpetrated this scam. We learned the investment my grandparents made was for building a market near their house. There wasn't a market, and most of the neighbors would often talk about this. The gentleman who scammed them was a neighbor who had recently sold his house right down the street. They were friends. He would always drop off what he told them was homemade jam. He did this to all the neighbors as a way to further get to know them and garner their trust.

This gentleman's scam was to move into a neighborhood for a year, befriend his neighbors, sell his house, move out, then go back after he had garnered a relationship and scam his old neighbors. They trusted him, so when he came to them with this idea about opening a market, giving him the $50,000, half their life savings, seems like a great idea. My grandparents and several of their neighbors invested and were also scammed. But this man had no intention of opening anything.

I still to this day remember my grandmother crying. I don't believe I had ever seen her cry before that day. Nono was a very happy and optimistic person and I remember this changed him for a while. He was depressed and unhappy, something that I had never experienced with them in my short life. Seeing him this way made a big impact on me because I was 12 years old. I vowed that day never to allow that to happen to anybody else if I had the chance. I didn't know what that meant at the time, but I knew I didn't want to

see that happen again. They got through it, but that was a defining moment in my life. My grandparents, who never hurt anyone, were the most loving people I knew. It was awful.

Fast-forward about 10 years to 1995 when I graduated college. At that time, I had the opportunity to start working in the investment business. I've always enjoyed numbers, but it was mainly the experience that my grandparents had that was my underlying motivation to work in the financial business.

There are a lot of scammers in the world today. One of the most popular and well-known scammers is Bernie Madoff. You might remember that he scammed some very influential and bright people out of about $50 billion dollars over several decades until he was finally caught. I tell people what I wish I could have told my grandparents: Be very cautious about giving money to someone unless they are affiliated with a big, well-known institution. In other words, if you're going to invest in the stock market, make sure the person helping you is affiliated with a well-known institution. Make sure your assets are kept in your name where the advisors' only powers are to manage the account, not have the power to access and move the funds without your express consent. Staying with large, well-known firm makes it almost impossible for anyone to scam you by stealing your money, because these big institutions have checks and balances and insurance. My grandparents gave their money to a neighbor who deposited it into his “business account,” which allowed no checks and balances and allowed him to abscond with the funds. When you work with a large company, it's virtually impossible for the money to be absconded. This horrible experience that my grandparents had was the catalyst that drove me to do what I'm doing today.

I was born in Southern California and grew up in Malibu. My parents moved there when it was nothing but a small beach horse town in the early ’70s. I remember there being a hitching rail at our local supermarket. For those who don’t know, a hitching rail is where you can tie up your horse. I attended Santa Monica High School and after graduation went on to graduate from the University of California Santa Barbara. In 1996, after college, I started working in the investment business as a stockbroker with Dean Witter, which was later bought by Morgan Stanley. I left after four years to pursue being an independent advisor as an RIA. I felt I could better serve my clients’ needs by being independent because being independent allowed me to choose the best investments for my clients. Working for a big company has its limitations. Big companies have a finite number of relationships with service providers. The problem arises when a product or service that's best suited for the client is not offered. When you're captive and work for a big company, you have no choice but to offer the products and services chosen by that company. The problem with this model again is the products and services offered are not governed by fiduciary-based regulation. Many times, the products are structured to benefit the firm first, not always the client. Being an independent RIA Fiduciary allows one to provide the best product based on the client's needs, not the needs of the firm.

My focus has primarily become the transition to retirement or the few years before retirement, preparing the client for nearly one-third of their life they might spend in retirement. We like to call these retirement years the go-go years, the slow-go years, and the no-go years.

I have helped hundreds of people retire with a focus on income planning, tax planning, Long-Term Care Health Care, and investment planning, to name a few. What I find most interesting is that most people I come across have never focused on the potential impact of tax rates and how

that will affect their retirement income. Today people are living a lot longer, when almost one-third of life for most people is spent in retirement. Tax rates are an important issue that must not be overlooked. In addition to taxes being a big issue, choosing the right money manager for your assets in the stock market could make a huge impact on your future nest egg.

I have also taken several courses in retirement planning distribution planning. I took a class in 2003 from Ed Slott, whom *The Wall Street Journal* describes as "the best source of IRA advice." I learned a lot from his class and began at that time to really understand what he called the ticking tax time bomb for retirees. That was almost 20 years ago, and things have only gotten worse, as I will explain in the following chapters.

I'm extremely confident this book will provide you with several facts and issues to focus on, many of which you're most likely not aware of!

Enjoy!

Chapter 1: A Wake-Up Call

"Our government has made a whole lot of promises that, in the long run, it cannot possibly keep without huge tax increases."

David Walker, Comptroller General of the United States, 1998-2008

"There is only one kind of shock worse than the totally unexpected: the expected for which one has refused to prepare."

Mary Renault, *The Charioteer*

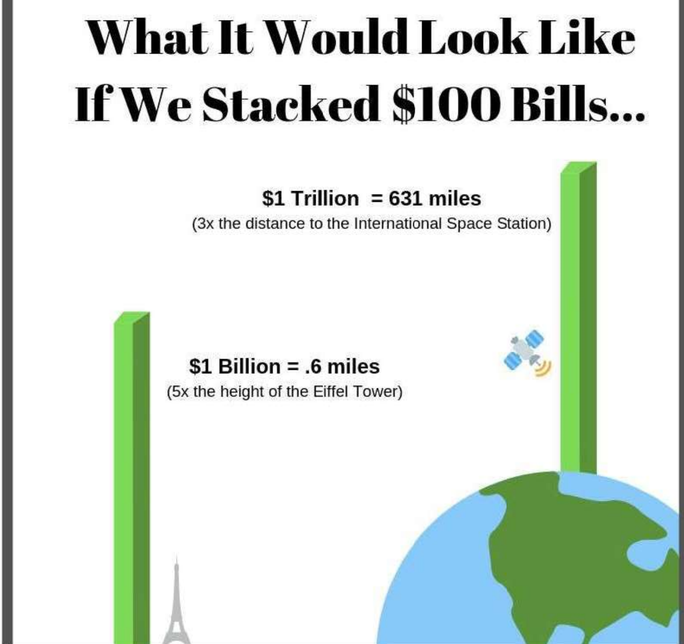
What does the US government pay for, what have they promised to pay for, and why does this matter to you?

Currently, the US government, proxy for the US taxpayer, owes $23.9 trillion dollars in unfunded obligations. An unfunded obligation is a promise to pay at a future date, but there are no savings set aside to make the payment. Remember the character "Wimpy" in the old *Popeye* cartoon? He popularized this concept with the phrase, "I'll gladly pay you Tuesday for a hamburger today." The US government, or rather, the US taxpayer is on the hook for trillions of hamburgers, and the question is, how are we going to pay for them?

These $23.9 trillion dollars in unfunded liabilities are more than the current national debt of $22 trillion. And did you know the national debt is growing at almost two million dollars per minute?[1]

If you've never visited the www.usdebtclock.org website, check it out—it's eye-opening and will give you an excellent

visual illustration of the ever-growing debt problem we're facing. If this debt is the responsibility of every American, even though many of us had nothing to do with the policies that created it, and nor did we enact the laws to allow it, we're still going to pay for it. How? Most likely in the form of much higher taxes.



Remember back in 2008 when we had the financial crises that were called a debt crisis? The national debt at that time was $10 trillion dollars, while today it's over $22 trillion dollars. So, if we had a debt crisis in 2008, what would you call the crisis that we're facing today? We were told back then that without a government bailout, which was simply adding more debt, the system would collapse. Adding more

debt to fix a debt problem is not a fix; it's more like kicking a can down the road, to be dealt with later.

If the current growing debt isn't bad enough, when we total all the financial promises the government has made, we're talking over $200 trillion dollars.[2]

What financial promises have they made? The four most expensive now are Social Security, Medicare, Medicaid, and interest on the debt. There are almost too many more to name, but here are a few others: defense spending, backstopping pensions, CDC, FBI, CIA, SEC, FAA, FEMA, Navy, Army, Air Force, Marines, IRS, NASA, immigration, and disaster relief, to name a few.

First, let's look at the problem with Social Security.

Social Security was started by President Franklin Roosevelt in 1935, during the Great Depression, as a way to make people feel better. At the time, millions of people were out of work, and there was an alarming concern for the elderly and retired Americans who had lost everything. Social Security was intended to be a social insurance program providing economic security to US citizens.[3]

The facts about Social Security should make you stop and think about how we're going to pay for it in the future and how that will likely affect you, even if you personally don't need Social Security. I believe that this issue alone, not to mention the dozens of others we'll discuss, will affect us all in the form of higher taxes. However today, in 2019, I believe taxes are a bargain, that's why I say they're on sale. Look at the graph below for an illustration of what I mean when I say taxes are on sale.

Taxes Are On Sale?

2017	2019
10% = $0 - $18,650	10% = $0 - $19,450
15% = $18,651- $75,900	12% = $19,451- $78,950
25% = $75,901 - $153,100	22% = $78,951- $168,400
28% = $153,101 - $233,350	24% = $168,401 - $321,450
33% = $233,351 -$416,700	32% = $321,451-$408,200
35% = $416,700 - $470,700	35% = $408,201- $612,350
39.6% = $470,700 and up	37% = $612,351 and up

As you can see, not only are the tax rates lower, but the amount one can earn is much larger in each bracket. As an example, look at the 2017 tax table married filing jointly, which we're told is coming back in 2026, best case. In 2017 you would pay 28% up to $233,000, then 33% up to $416,700. On the 2019 tax tables, you pay 24%, up to $321,450! So just in this example, you'd pay 9% more on almost $90,000 in income! If you're going to move money out of your tax-deferred bucket or only add money to your 401(k) up to the match, I think this would be the time to do so. We'll talk more about this later on in the book.

We already know that the Tax Cuts and Jobs Act of 2017 contains a sunset provision. This provision contains an expiration date of 2025 for the current tax code. It's likely taxes will precipitously rise at that point, if not before.[4]

My dad always said, "You can't get blood from a stone," while my mother always said, "You don't know what you don't know." Both comments apply here. Money doesn't grow on trees, and unless you're educated on the fiscal situation we face, you cannot prepare for what is to come.

Here are some eye-opening history and facts:

In 1935, Social Security was created by FDR after the Great Depression. It was created primarily to take care of older people who lost everything at the end of their life. When Social Security was established, 42 workers contributed to the Social Security system for every one worker that took out of the system. In 1935, you had to be 65 years old before you could draw from Social Security.

Now, get this.

In 1935, the average life expectancy was 61 years old, but when you factor out infant mortality, people lived, on average, to age 67.[5] In other words, if you survived infancy, on average, you'd live five years longer than the average life expectancy. This meant that the average person only drew on Social Security for two years before dying. So herein lies the problem.

Today, only three workers pay in for every one drawing Social Security. As the large and aging Baby Boomer working population shrinks, those same people will be taking from the system instead of contributing to it. As a result, the number of workers paying into the system per each one taking out will shrink from three workers to two. What's even

more staggering is that life expectancy today, when you factor out infant mortality, is 85 years old!

So, to recap, in 1935, the average person drew on Social Security for two years until death while 23 workers paid into the system. But today, if you start drawing at 65, on average, you'll likely live until age 85, which is 20 years or 10 times longer than we lived when Social Security was established!

It doesn't take a rocket scientist to realize that Social Security has big problems, and remember, that's only one government program out of many.

How many people actually need their Social Security to enjoy their current lifestyle?

Sixty-one percent of retired workers rely on Social Security as part of their monthly income, and 15 percent of Social Security recipients live below or just above the federal poverty level.[6] It's not like the US government can just stop paying Social Security benefits without having a massive starving and homeless population on their hands.

How is Social Security funded? First, by contributions from the working population, and then by the taxpayer.

In 2017, Social Security had $997 billion dollars in income and $952 billion in expenses. When income exceeds expenses, the Social Security trust fund is required to loan that money to the US Treasury. Now, get this: As of 2017, the US Treasury owes $2.9 trillion dollars to the Social Security fund. After the federal government pays back with interest all the money that is borrowed from Social Security, the program's current claim against the earnings of future generations is $32.4 trillion dollars. To offset the collapse of

Social Security, payroll taxes must be increased to 27 percent in 2034.[7]

Now, I don't want you to lose any sleep, but this is only Social Security we're talking about.

How about Medicare and Medicaid? Let's quickly define them.

Medicare is the federal health insurance program for:

- People who are 65 or older
- Certain younger people with disabilities
- People with End-Stage Renal Disease (permanent kidney failure requiring dialysis or a transplant, sometimes called ESRD) and ALS

Medicaid, on the other hand, provides health coverage to millions of Americans, including eligible low-income adults, children, pregnant women, elderly adults, and people with disabilities. Medicaid is administered by states, according to federal requirements. The program is funded jointly by states and the federal government.

How do we pay for these programs?

Mostly from taxes. Fifty-seven percent of Medicare is currently funded from premiums, and the rest comes from payroll taxes. Medicaid is paid out of the general fund, which is comprised of tax revenue.

The approximate cost of Medicare is $580 billion per year, while the estimated cost of Medicaid is $389 billion a year.[8]

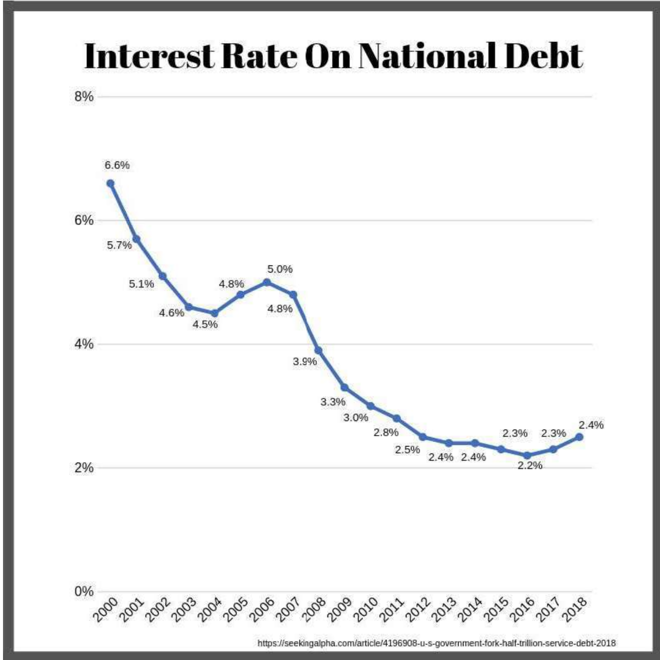
How about the national debt—how much does that cost? And who is the biggest owner of the national debt, by the way? Again, the US citizen is the largest owner of US debt, so since “We the People” own this debt, who do you think is

going to pay for it? The interest on the debt was $393 billion in 2018 and was also funded by tax revenue.[9]

To put it in perspective, income taxes bring in about $1.6 trillion per year, payroll taxes generates about $1.1 trillion per year, and corporate taxes add $205 billion per year.[10]

The problem is simple. We're just able to cover the cost today, but as the working Baby Boomer population ages and retires, then what? The income tax and payroll tax collected from these high-paying Boomer jobs will decrease precipitously. Couple that with these same people transitioning from givers to takers. The number of people utilizing Medicare, Medicaid, and Social Security skyrockets. Let's not forget that the interest on the national debt only goes up.

What if interest rates return to normal levels? The $325 billion interest paid today could balloon to $1 trillion per year quickly. Look at the chart below for a history of the interest on the National Debt since 2000. We head back to around 5% and our debt service will be one trillion per year.[11]



I wish these were the only fiscal problems facing us today, but they're not.

The insolvency of pensions is also a massive problem that is not as quantifiable as Medicare, Medicaid, and Social Security.

Most companies no longer offer pensions, and for a good reason. Imagine trying to estimate what a 60-year-old would receive when that person is still only 25 years old. You'd have to estimate the amount of contributions that would be contributed annually by a future workforce as well as what return the pension funds would earn. Many pensions assumed when rates on bonds were 10 percent that an 8 percent pension return would be a cinch, but then we had

"the lost decade" of 2000-2010, when interest rates cratered, and the major stock market indexes lost money over this 10-year period and averaged a zero percent yearly return instead of the expected 8 percent.

Predicting future values and income streams is no easy task. The Teamsters' pension, as an example, is one of the largest and oldest pensions in the United States. The Western Pennsylvania Teamsters and employers pension fund Board of Trustees announced that it filed for federal approval to cut benefits effective August 1st, 2019. As of last year, the Teamsters' pension fund had about $0.48 for every dollar in benefits it owes to its retirees and workers. This pension is projected to be insolvent by the early 2030s.[12]

What ripple effect is felt when more than one million people in the Teamsters Union lose their pension income? And this is only one pension; there are thousands of others in trouble as well.

This is the story of many pensions in the United States. This is one main reason many of them are failing, and why so few companies and organizations in the US still provide pensions to their members and employees. Pensions are another one of the government's unfunded liabilities. There's a US government agency called the PBGC, or the Pension Benefit Guaranty Corporation. This is a federal agency created by the Employee Retirement Income Security Act of 1974 to protect pension benefits in private-sector benefit plans—the kind that typically pays a set monthly amount at retirement.

If your plan is terminated because of insolvency and is unable to pay all benefits, PBGC's insurance program will pay you the benefit provided by your pension plan, up to the limit set by law. Most people receive the full benefit they earned before the plan terminated. These plans are insured even if your employer fails to pay the required premiums.

No politician gets elected by campaigning on raising taxes, even though we see this issue being raised during the primaries today more than ever before. We'll look at some of their suggestions below.

The fact is that when the have-nots finally outnumber the haves, the haves are going to have a big problem. Best-selling author Malcolm Gladwell would call this a "tipping point." The haves who didn't arrange their affairs properly and plan for this almost-certain outcome are going to suffer the most, and those with large tax-deferred retirement accounts are in for a rude awakening.

Before Ronald Reagan became the 40th president of the United States and before he was governor of California, he was an actor. In those days, movies were filmed in about 90 days, so actors could do as many as four movies per year, and Reagan was one of the most popular actors of his day. But he only did two movies per year. Why? Well, the federal tax rate for those making over $199,000 was 94 percent. He also lived in California, and his state tax at that level was 6 percent. If he made over $199,000, he didn't keep a dime, so two movies it was! Also, $199,000 was a hefty sum back then, but these were the tax rates![13]

In the following chapters, we'll share a bit more about the historical precedence illustrating higher taxes are not only likely but probable. More importantly, we'll share strategies and case studies of others who have prepared for this outcome.

Chapter 2: I Will Gladly Pay You Tuesday for a Hamburger Today

"Regardless of what politicians tell you, any additional accumulations of debt are, absent dramatic reductions in the size and role of government, basically deferred tax increases...Unless we begin to get our fiscal house in order, **there's simply no other way to handle our ever-mounting debt burdens except by doubling taxes over time.**"

David Walker, Comptroller General of the United States, 1998-2008

Have you heard of David Walker? He was the comptroller general, head of the Government Accountability Office, and was on the board of Social Security as well. In short, he was the CPA of the United States.

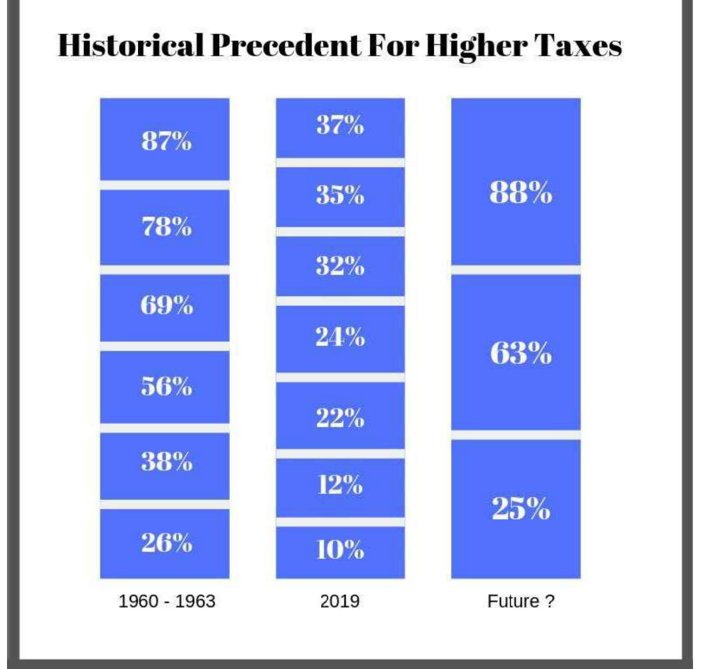
How many people know more about the fiscal state of our country than this man? Are you familiar with the function of the Government Accountability Office he ran? The Government Accountability Office is a legislative branch government agency that provides auditing, evaluation, and investigative services for the United States Congress. It is the supreme audit institution of the federal government of the United States.[4]

This supreme audit institution of the federal government is quoted as saying,

"If Social Security, Medicare and Medicaid **go unchanged**, *the rate for the lowest tax bracket* **would increase** *from 10% to 25%; the tax rate on incomes in the current 25% bracket*

would have to be increased to 63%; and the tax rate of the highest bracket would have to be raised from 35% to 88%."[2]

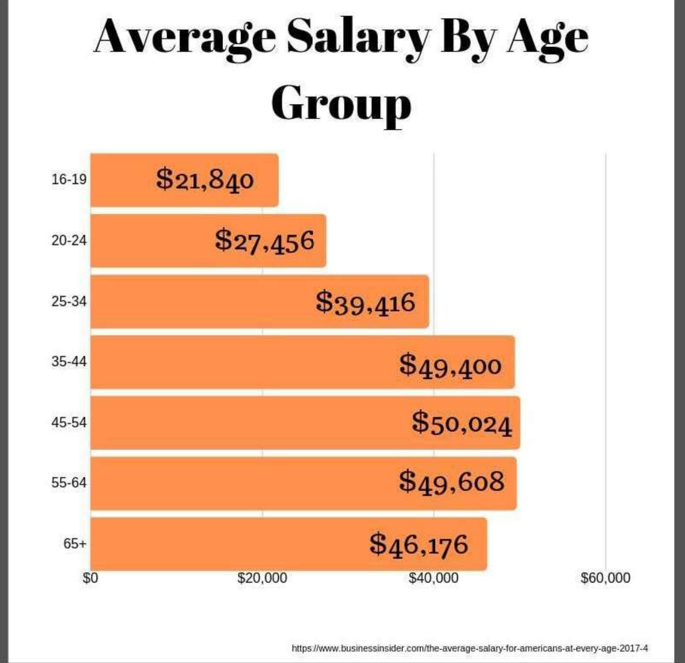
After initially reading this statement, I was personally shocked, but after reflecting on the actual tax rates earlier in American history, such as during Ronald Reagan's movie-making years, it wasn't so outrageous. Look at the tax rates from 1960-1963 and compare that with rates today, then compare this potential projected increase stated above.



Is it that inconceivable that taxes could rise precipitously after understanding the debt we have, the entitlements owed, the shrinking higher-paid Boomer working population

compared to Generation Y, and the ever-increasing Boomer population relying on Social Security, Medicare, and Medicaid?

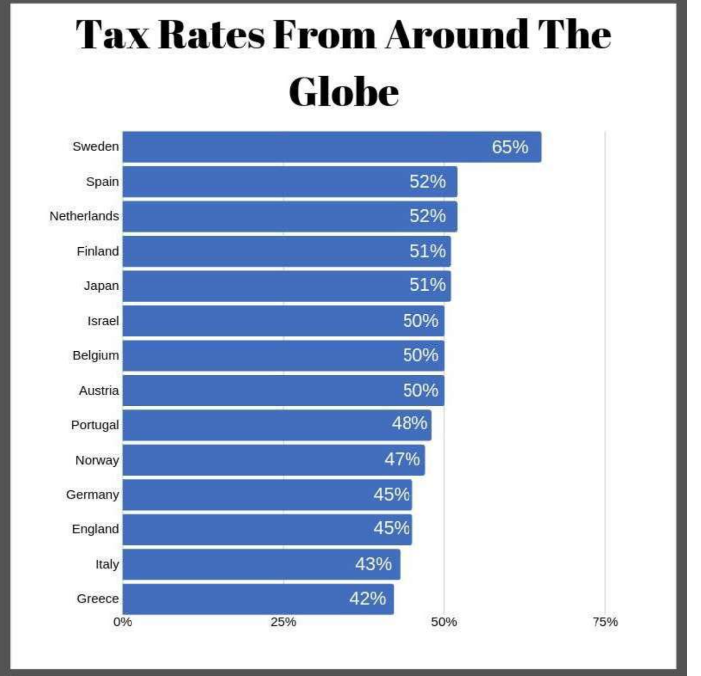
The Boomers were paid well and there were a lot of them, but now, as they retire, the following generations will need to support them. Take a look at this graph below. Anyone in the workforce 35 or younger makes quite a bit less than your average Boomer.



During the war years of the1940s, the top marginal rates exceeded 90%! Those rates lasted until the early '60s. During the 1970s, the top marginal rate was 70%. Compare

that with the top bracket of 37% today and it's pretty clear a rising tax environment is more than likely.

In the UK if you make over £50,000, you pay 40% in taxes at that income level!![3] Now let's look around the world at their highest marginal brackets. It's also important to note that many countries' tax brackets go much higher much faster.



As you can see, tax rates in Europe are all substantially higher than in the US.

No one can predict the future, but it just doesn't seem possible that tax rates can stay anywhere near the levels they are today.

Now let's look at some of the tax plans being suggested by candidates in the 2020 primaries. These candidates will most likely not be elected and will soon be old news but it's still interesting. The fact that candidates from one of the two major political parties in our country are all proposing large increases, not decreases, is telling.

The Democrat Tax Plans

According To Taxfoundation.org

Joe Biden	Elizabeth Warren	Bernie Sanders
• Increase capital gains tax to 39.6% • Increase taxes on middle class to 15%, 25%, and 28% • Reduce child tax credit from $2000 to $1000 • Families making $170,000 per year or more would receive no tax credit	• 7% tax on corporate profits, reducing investment incentives • New tax strategy reduces wages by 1.5% • Proposed tax plan would shrink the economy by almost 2%	• Increase payroll taxes by 6.2% • New tax strategy reduces after-tax income for all by 10.56% • Transaction tax on stocks and bonds up to 0.5% per trade • Tax plan to reduce GDP by up to 9.5%

I think the case has been made that preparing for higher taxes in the future by looking at strategies to ease your coming tax burden is the only prudent choice.

Where else will the money come from to pay for all these unfunded liabilities? The poor have nothing to tax, there aren't enough high-income earners to make a dent even if you tax them to the moon, so the middle class is going to be the one paying.

What other financial headwinds should we be aware of in our retirement years?

How about the cost of care if you're unable to care for yourself in your old age? The national average cost of long-term care is $6,844 to $7,698 per month, and 70% of retirees will need care at some time during their retirement. One spouse spending down all the family assets and leaving the living spouse almost destitute before the assets even have a chance to reach the next generation happens regularly. Many times, children are incapable of providing this level of care while others become resentful of taking care of an aging parent.[4]

Another issue that people face in retirement that goes hand in hand with health issues is not having a living trust in place or medical and financial powers of attorney completed. I've seen probate and medical power of attorneys ravage family finances. Probate occurs when your asset, such as your house, is not placed in the name of a trust. California, as an example, is a community property state, so if you die, your house goes to your wife, assuming it's jointly owned. If you don't have a spouse or they have passed away and your asset is in your name only and you pass, it will go to probate court, which takes time and money.

The only assets that are not probated are those that have beneficiary forms. The powers that be recognize beneficiary forms as legal documents like a trust. Annuities, life insurance, and all retirement accounts like 401(k)s and IRAs are not probated and do not need to be in the name of the trust. But every other asset does or it is subject to probate.

One of the toughest experiences I had concerned a woman named Patty who was very ill. She knew she had to get her affairs in order after speaking with me on the phone but was waiting to invite me over until she was well enough to get out of bed and sit in her living room. A few months passed and Patty wasn't getting better. Both of her daughters and their two children were living with her, and she supported the whole clan.

Before Patty got ill, she had worked in a hospital as an administrator. One would have thought that her seeing so many people come and go that she would have had her affairs in order before she passed on, but like many, she did not. This was more of a case of you don't know what you don't know. One afternoon I got a call from her daughter, who told me Mom was getting worse and couldn't speak to me on the phone. Her daughter asked me to come over. When I arrived, Patty was having what they said was a good day, but I was confident she wasn't going to last long. Once I started speaking to her, I was surprised to learn, among other things, that she didn't have any of her affairs in order, but mostly she had no living trust, and she owned her own home in her name only.

This was a problem because if she passed without her daughters on the title of the house or as joint owners, the house would most certainly go through probate. I immediately suggested we get an attorney over to the house. The next day one arrived and gathered the appropriate information to get the house prepared to pass to her daughters.