

## Memorandum 90-83

Subject: Study L-1025 - Remedies of Creditor Where Personal Representative Fails to Give Notice (Comments on Tentative Recommendation)

The Commission's tentative recommendation relating to the remedies of a creditor where the personal representative fails to give notice of probate was distributed for comment in May. The tentative recommendation supplements the existing remedies available to a creditor who is forced to petition for a late claim in probate because of the personal representative's failure timely to notify the creditor of the probate:

(1) The filing of a late claim petition by the creditor would toll the statute of limitations on the creditor's claim.

(2) Preliminary distributees would be required to restore property to the estate to the extent necessary to satisfy the late claim.

(3) A personal representative whose failure to notify the creditor is wrongful would be personally liable to the extent preliminary distributions are not recoverable and have caused the estate to be insolvent.

Three of the letters we received approved the tentative recommendation without further comment. These were from Margaret R. Roisman of Oakland, Wilbur L. Coats of Poway, and Henry Angerbauer of Concord. The letters are not reproduced here.

An additional letter of general approval was received from Roger V. Marshall of Chico (Exhibit 7), who comments:

We agree with this recommendation as a preliminary distribution is usually completed because of a matter of convenience to the beneficiary and should not be used as a device to defeat creditors who have failed to receive notice because of the bad faith of the personal representative. Therefore, we support this change in law.

The remaining letters contain comments questioning specific aspects of the tentative recommendation. The comments are analyzed in

the attached draft of the tentative recommendation in Notes following the provisions to which they relate. The draft has been revised by the staff to reflect the enactment of SB 1855 (1990 Cal. Stats. ch. 140), which provides a one-year limitation period from the date of death for all creditor claims.

Our objective here is to review the comments to see whether any changes should be made in the recommendation before printing it and submitting it to the Legislature.

Respectfully submitted,

Nathaniel Sterling  
Assistant Executive Secretary

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CA LAW REV. COMMISSION

MAY 22 1990

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May 21, 1990

California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
Palo Alto, California 94303-4739

Re: Tentative Recommendation  
relating to Remedies of  
Creditor Where Personal  
Representative Fails to  
Give Notice.

Gentlemen:

These proposals will make fully effective for practical purposes a one-year statute of limitations for filing claims, the one-year period running from the date of the first issuance of letters to a general personal representative. If these proposals are adopted, preliminary distributions of cash legacies will be impractical until the one-year period has elapsed. Nevertheless, in view of the constitutional requirements, I must approve the proposal.

Very truly yours,



John G. Lyons

JGL:car

Law Office

**Irving Kellogg****MAY 29 1990****R E C E I V E D**

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May 24, 1990

California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
Palo Alto, Calif. 94303-4739

Re: Proposed Amendments to PC Section 9053 and Section 9103


Attention: John DeMouly

Dear John:

The only question I have with respect to those sections is clarification about the term, bad faith. I believe the statute should give some examples of bad faith so that attorneys would have guidance in advising a personal representative just what conduct would fall under the bad faith umbrella. Otherwise, the term, bad faith, standing alone, leaves too many subjective opinions available for conflict.

If statutory drafting precludes giving examples, then legislative history or comment should include examples of bad faith behavior within the context of creditors' claims and executor responsibility. If the Code is left with just the term, bad faith, it invites lawsuits to get the Courts to determine what is bad faith in this context. In my opinion, the Code Section should give guidance rather than turning the guidance over to a judge whose idea of bad faith within a fact situation would cause confusion and perhaps ambiguities.

Sincerely yours,



Irving Kellogg

Edward M. Phelps  
Deborah Ballins Schwarz  
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JUN 04 1990

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May 31, 1990

California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
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Re: Tentative Recommendation Relating to  
Remedies of Creditor Where Personal  
Representative Fails to Give Notice

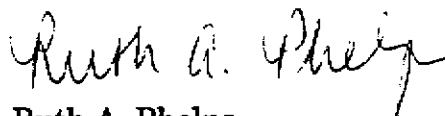
Dear Sirs/Madam:

I have read the Tentative Recommendation Relating to Remedies of Creditor Where Personal Representative Fails to Give Notice. I have a question on it. The proposed Section 9103(c) (2) provides that the creditor cannot file a late claim 1 year after the time letters are first issued to a general personal representative. However, Section 9053(b) (3) requires that the creditor have filed a petition in the court regarding liability of the personal representative within 16 months after letters were first issued. Does this mean that the creditor has to file the late claim within 1 year of the date letter is issued, and then has an additional 4 months to file this petition to determine the liability of the personal representative? I had to read these 2 sections at least 5 times each before I finally resolved the 2 time differences.

I agree with this proposed legislation, because I think failure to pay creditors is a problem. The problem with Section 9053 will be to prove that the failure was in bad faith. If a creditor inadvertently gets overlooked, which may happen since under 9103(b), this doesn't apply to creditors who are conducting a trade, business or profession, then the personal representative should not be personally liable. This still leaves a problem area if there aren't sufficient assets in the estate to pay the claim.

You are moving in the right direction. Good luck.

Very truly yours,



Ruth A. Phelps  
PHELPS, SCHWARZ & PHELPS

RAP:svt

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June 1, 1990

CA LAW REV. COMM'N

JUN 04 1990

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California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
Palo Alto, California 94303-4739

Re: Comments on Tentative Recommendations

Gentlemen:

I am responding to five tentative recommendations issued by your organization pertaining to modifications of the Probate Code.

1. Contingent, Disputed or Not Due Debts:

Your proposal of April 1990 is excellent and I believe should be submitted as proposed. My only question relates to the use of the term "interested person." As you note in your comment, the term "interested person" is already defined in Section 48 of the Probate Code. Would it be redundant to expressly reference the definition of Section 48, which includes a creditor and would permit a creditor to petition the court. This would be appropriate if the executor failed to do so.

2. Creditor Remedies:

The recommendation relating to a personal representative who deals in bad faith makes no attempt to define the scope of bad faith. Perhaps it is your desire that this be left to a court to determine, but it seems appropriate that some definition be included when the purpose of this proposal is to expand the remedies of creditors for that specific purpose. Since bad faith may be very subjective, it might assist to provide specific examples which would be considered bad faith and for which the burden of proof might be imposed upon the personal representative. Such instances might include the intentional disregard of known or readily available evidence of the debt.

3. Alternate Beneficiaries for Unclaimed Distribution:

This is an excellent proposal.

4. Elimination of Seven-Year Limit for Durable Powers of Attorney:

I heartily concur. I have never understood why a limitation should be imposed; furthermore, if it is to be limited, I do not understand why it should differ from the limitation upon the directive to physicians. I concur with your proposal that the limitation be eliminated completely.

5. Litigation Involving Decedents:

Your proposal regarding litigation involving decedents is excellent. The ability to continue these actions without commencing a probate and appointing a personal representative is most practical. I have not had an opportunity to fully evaluate this proposal, but I support its intent and purpose. I will leave to those with greater litigation experience the full analysis of your proposal.

Very truly yours,



Paul H. Roskoph

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PHR248/1637:2

JUN 06 1990

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DAVID W. KNAPP, SR.  
DAVID W. KNAPP, JR.

June 5, 1990

California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
Palo Alto, CA 94303-4739

Re: REMEDIES OF CREDITOR WHERE PERSONAL REPRESENTATIVE FAILS TO GIVE NOTICE

I must stress my objections to this continual attempt by the Commission to further "protect" the phantom creditors. The present law, I feel, is adequate and to now put an additional burden both on the personal representative and the heirs (any sensible representative will now request the courts to increase the monies reserved from distribution just to protect from some spurious creditor who was asleep at the switch).

Such a creditor can file suit and cause the representative personal expenses long after distribution and only a court will determine if it was "bad faith"...."negligence" or simple an over-zealous creditor.

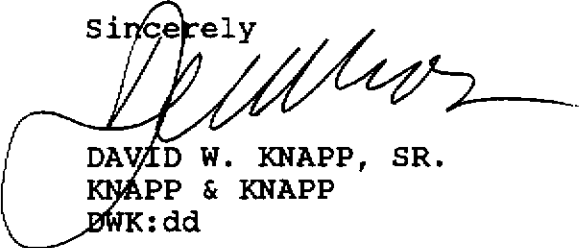
What is the Commissions interpretation of "bad faith"? Is it what we, as lawyers interpret it to be, i. e. actual or constructive fraud....or, could it be, as the layman feels, gross negligence and must this be determined in trial?

I feel you are placing too high a burden on the personal representative and leaving him or her open to continued lawsuits to be defended without estate funds!

I have practiced law for 37 years and was a Clerk of the Superior Court for seven years prior thereto and have NEVER ENCOUNTERED OR HEARD OF SUCH A "BAD FAITH" situation, hence can it really be a current problem?

You are to be congratulated on the fine work you have done in the revision attempts however the "poor creditor" protection has reached its ceiling.

Sincerely

  
DAVID W. KNAPP, SR.  
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DWK:dd



JUN 08 1990

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June 4, 1990

California Law Revision Commission  
1100 Middlefield Road, Suite D-2  
Palo Alto, California 94303-4739

Re: Tentative Recommendations

Gentlemen:

I support the following recommendations relating to:  
debts that are contingent, disputed or not due; alternate  
beneficiaries for unclaimed distribution; and elimination of  
seven-year limit for durable power of attorney for health care.

With respect to remedies of creditor where personal  
representative fails to give notice, I am concerned about what  
types of actions or failure to act would constitute bad faith  
on the part of the personal representative. For example,  
when is failure to give notice to a known creditor bad faith as  
opposed to excusable neglect?

Very truly yours,

*Patricia H. Jenkins*  
PATRICIA H. JENKINS  
Attorney at Law

PHJ:cb

JUN 14 1990

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June 11, 1990

California Law Revision Commission  
4000 Middlefield Road, Suite D-2  
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**RE: Comments to Tentative Recommendation**

To Whom It May Concern:

1. Probate Law and Procedure - Debts that are Contingent, Disputed, or Not Due.

We feel that this tentative recommendation is advisable as it provides flexibility to facilitate distribution and closing of an estate and, at the same time, provide for protection to the creditors and the estate's beneficiaries. Keeping an estate open until all issues involving debts are resolved or satisfied is not acceptable.

2. Elimination of Seven-Year Limit for Durable Powers of Attorney for Health Care.

While we do agree that a Durable Power of Attorney For Health Care should be reviewed on an established time basis, we also understand and agree with the statement that our clients are not efficient in reviewing and possibly renewing this statement every seven years. It has been our experience that even if reminded and encouraged to update their estate planning, clients often procrastinate. Also, quite often, we are unable to locate a client who has moved. Therefore, providing assurance that the Durable Power of Attorney For Health Care is in existence when it is necessary is more important than forcing an analysis and review by terminating the document if it is not actively renewed.

3. Alternate Beneficiaries for Unclaimed Distribution.

We agree that most testators would prefer to have unclaimed property go to an alternate taker rather escheat to the State.

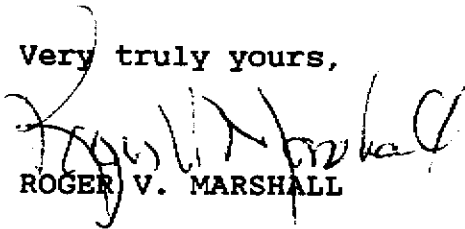
California Law Revision Commission  
June 11, 1990  
Page Two

Therefore, we agree with this recommendation. We do agree that the three year period for the primary distributee to claim his or her share is too short. We would be more agreeable to a five year time period.

4. Remedies of Creditor Where Personal Representative Fails to Give Notice.

We agree with this recommendation as a preliminary distribution is usually completed because of a matter of convenience to the beneficiary and should not be used as a device to defeat creditors who have failed to receive notice because of the bad faith of the personal representative. Therefore, we support this change in law.

Very truly yours,



Handwritten signature of Roger V. Marshall in cursive script.

ROGER V. MARSHALL

RVM/kc

CA LAW REV. COMM'N

JUN 18 1990

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FRANK M. SWIRLES  
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June 15, 1990

California Law Revision Commission  
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Re: Tentative Recommendations on:

Remedies of Creditor where personal representative  
fails to give notice

and

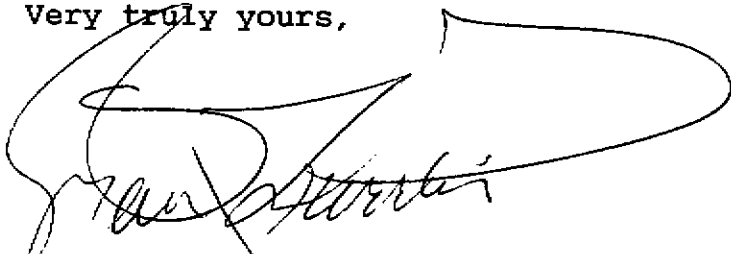
Alternate beneficiaries for unclaimed distribution

Gentlemen:

Re the remedy of creditor matter, what is the reason for your proposed 9103(2)(b)? Why does it not apply to an open debt of the decedent as well as to an action or a proceeding? Also, why do you rule out trade debts which arise out of the creditor's conduct of a trade, business, or profession? Business people are often the prey of frauds. They should be protected.

Re the alternate beneficiaries, the 3 year period is sufficient. But, during the possible 5 year gap, what becomes of the property? Is it just in limbo? Does the personal representative hold it? Is he liable for it? Who pays the insurance on it?

Very truly yours,



Frank M. Swirles

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ns71  
Rev. 07/02/90

Tentative Recommendation  
relating to  
REMEDIES OF CREDITOR WHERE PERSONAL REPRESENTATIVE  
FAILS TO GIVE NOTICE

If a personal representative in bad faith fails to notify a known creditor of the estate proceeding, the creditor has no remedy against the personal representative so long as the estate is open, but is relegated to a late claim. It is only where the creditor becomes aware of the administration after the estate is closed that the creditor may have a remedy against the personal representative.<sup>1</sup>

Even though the estate is open, the personal representative may have depleted the estate by preliminary distributions, with the result that the late claim is not a remedy for the omitted creditor. The late claim statute does not provide that preliminary distributions are subject to late claims in probate; property distributed before a late claim is filed is not subject to the claim.<sup>2</sup>

The statute should not immunize preliminary distributions from late claims. A preliminary distribution is intended as a convenience to potential distributees, not as a device to defeat the just claims of creditors. Distributees should take with the understanding that until there is an order for final distribution they may be liable to make restitution of the property or its value if required for estate administration. This is the implication of the preliminary distribution statute itself, which provides that the court may require a bond conditioned on "payment of the distributee's proper share of the

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1. Prob. Code § 9053.

2. Prob. Code § 9103(d). In addition, the filing of a late claim does not toll the statute of limitations applicable to the claim, with the result that the late claim remedy of an unnotified creditor may be illusory in some cases. Probate Code Section 9352 should be amended to provide that filing a petition for a late claim tolls the statute of limitations applicable to the claim.

debts of the estate, not exceeding the amount distributed".<sup>3</sup> Where a preliminary distributee is unable to make restitution because the distributee is insolvent, the creditor should have an alternative remedy against the personal representative who acted in bad faith.

PROPOSED LEGISLATION

Probate Code § 9053 (amended). Immunity of personal representative

SEC. . Section 9053 of the Probate Code is amended to read:

9053. (a) If the personal representative believes that notice to a particular creditor is or may be required by this chapter and gives notice based on that belief, the personal representative is not liable to any person for giving the notice, whether or not required by this chapter.

(b) If the personal representative fails to give notice required by this chapter, the personal representative is not liable to any person for the failure, unless a creditor establishes all of the following:

(1) The failure was in bad faith.

(2) Neither the creditor nor the attorney representing the creditor in the matter had actual knowledge of the administration of the estate before ~~the court made an order for final distribution~~ expiration of the time for filing a claim, and payment would have been made on the creditor's claim in the course of administration if the claim had been properly filed.

(3) Within 16 months after letters were first issued to a general personal representative, the creditor did both of the following:

(A) Filed a petition requesting that the court in which the estate was administered make an order determining the liability of the personal representative under this subdivision.

(B) At least 30 days before the hearing on the petition, caused notice of the hearing and a copy of the petition to be served on the

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3. Prob. Code § 11622(c).

personal representative in the manner provided in Chapter 4 (commencing with Section 413.10) of Title 5 of Part 2 of the Code of Civil Procedure.

(c) Nothing in this section affects the liability of the estate, if any, for the claim of a creditor, and the personal representative is not liable for the claim to the extent it is paid out of the estate or could be paid out of the estate pursuant to Section 9103.

(d) Nothing in this chapter imposes a duty on the personal representative to make a search for creditors of the decedent.

Comment. Section 9053 is amended to extend liability to a bad faith personal representative in a case where the estate is open but the debt cannot be satisfied out of the estate due to preliminary distributions that cannot be recovered under Section 9103 (late claims).

Note. Every comment we received addressed to this section was concerned with the "bad faith" requirement of subdivision (b)(1), even though this is existing law and is unaffected by the present recommendation.

Ruth A. Phelps of Pasadena (Exhibit 3) was concerned that the requirement that the creditor show the personal representative acted in bad faith is too restrictive, since this will be the only remedy available to a business creditor, who is precluded by statute from filing a late claim. The staff notes that this defect was corrected by SB 1855, which makes the late claim procedure available to any omitted creditor, business or otherwise.

A number of commentators point out that the meaning of "bad faith" is unclear and could encourage litigation. They worry about the standard being subject to the personal whim of different judges, and suggest that examples of bad faith would be useful. See letters of Irving Kellogg of Beverly Hills (Exhibit 2), Paul H. Roskoph of Palo Alto (Exhibit 4), David W. Knapp, Sr., of San Jose (Exhibit 5), and Patricia H. Jenkins of Los Angeles County Counsel (Exhibit 6).

The Commission considered this matter last year when the bad faith standard was enacted and made a conscious decision to adopt the bad faith standard without attempting to refine it. It is a familiar concept in the law, and the courts can develop its application to particular situations. The Comment to the enactment of the bad faith standard last year states the intent of the statute to protect the personal representative from liability for a failure to give notice to a creditor "unless the creditor establishes that the failure was in bad faith and satisfies the other requirements of the subdivision. As provided in subdivision (c), the remedy, if any, of a creditor who suffers loss as a result of a good-faith or inadvertent failure to give notice is against the estate and not against the personal representative."

Also relevant is the Comment to Section 9050 which defines when a personal representative has "knowledge" of a creditor for purposes of determining whether there is a duty to give notice:

*The personal representative is protected by statute from a failure to give notice unless the failure is in bad faith. See Section 9053(b). However, the personal representative may not willfully ignore information that would likely impart knowledge of a creditor. For example, the personal representative may not refuse to inspect a file of the decedent marked "unpaid bills" of which the personal representative is aware. Inferences and presumptions may be available to demonstrate the personal representative's knowledge.*

Probate Code § 9103 (amended). Late claims

SEC. . Section 9103 of the Probate Code is amended to read:

9103. (a) Upon petition by a creditor and notice of hearing given as provided in Section 1220, the court may allow a claim to be filed after expiration of the time for filing a claim if the creditor establishes that either of the following conditions is satisfied:

(1) Neither the creditor nor the attorney representing the creditor in the matter had actual knowledge of the administration of the estate more than 15 days before expiration of the time provided in Section 9100, and the creditor's petition was filed within 30 days after either the creditor or the creditor's attorney had actual knowledge of the administration whichever occurred first.

(2) Neither the creditor nor the attorney representing the creditor in the matter had knowledge of the existence of the claim more than 15 days before expiration of the time provided in Section 9100, and the creditor's petition was filed within 30 days after either the creditor or the creditor's attorney had knowledge of the existence of the claim whichever occurred first.

(b) The court shall not allow a claim to be filed under this section after the earlier of the following times:

(1) The time the court makes an order for final distribution of the estate.

(2) One year after the time letters are first issued to a general personal representative. Nothing in this paragraph authorizes allowance or approval of a claim barred by, or extends the time provided in, Section 353 of the Code of Civil Procedure.

(c) The court may condition the claim on terms that are just and equitable, and may require the appointment or reappointment of a personal representative if necessary. The court may deny the



creditor's petition if a ~~preliminary distribution to beneficiaries~~ or a payment to general creditors has been made and it appears that the filing or establishment of the claim would cause or tend to cause unequal treatment among ~~beneficiaries~~ or creditors.

(d) Regardless of whether the claim is later established in whole or in part, ~~property distributed under court order and~~ payments otherwise properly made before a claim is filed under this section are not subject to the claim. Except to the extent provided in Section 9392 and subject to Section 9053, the personal representative, distributee, or payee is not liable on account of the prior ~~distribution or~~ payment. Nothing in this subdivision limits the liability of a person who receives a preliminary distribution of property to restore to the estate an amount sufficient for payment of the distributee's proper share of the claim, not exceeding the amount distributed.

Comment. Subdivisions (c) and (d) of Section 9103 are amended so that they do not immunize a distribution made under an order for preliminary distribution from subsequent liability for a late claim. Only a distribution made under an order for final distribution is entitled to the immunity provided in subdivision (b). Cf. Section 11622(c) (bond for preliminary distribution).

Note. John G. Lyons of San Francisco (Exhibit 1) remarks that he supports this provision in view of constitutional requirements even though he is concerned that it will make preliminary distributions of cash legacies impractical until one year has elapsed from the date of issuance of letters. The staff notes that SB 1855 cuts down potential distributee liability to one year after the date of death. Moreover, the personal representative should not be concerned about making distribution so long as the personal representative acts in good faith, since Section 9053 immunizes the personal representative except for bad faith distributions. Of course, commentators on Section 9053 are concerned that the lack of definition of "bad faith" will make a personal representative unwilling to act for fear of lawsuits.

Ruth A. Phelps of Pasadena (Exhibit 3) was confused that the section cuts off late claim applications one year after issuance of letters, whereas Section 9053 makes the personal representative liable to a creditor if proceedings are initiated within 16 months after issuance of letters. Does this mean the creditor has an additional 4 months after the end of the late claim period in which to seek personal representative liability? The answer is yes. The statute allows the creditor additional time to seek personal representative liability because the intent is to provide a remedy for the creditor only in those cases where due to the personal representative's bad faith the estate is no longer available to satisfy the claim; this will not be known until after the opportunity for late claim treatment has expired.

Frank M. Swirles of Rancho Santa Fe (Exhibit 8) wonders why business creditors are precluded from making late claims. As the staff noted above, this defect was corrected by SB 1855, which makes the late claim procedure available to any omitted creditor, business or otherwise.

Probate Code § 9352 (amended). Tolling statute of limitations

9352. (a) The filing of a claim or a petition under Section 9103 to file a claim tolls the statute of limitations otherwise applicable to the claim until allowance, approval, or rejection.

(b) The allowance or approval of a claim in whole or in part further tolls the statute of limitations during the administration of the estate as to the part allowed or approved.

Comment. Subdivision (a) of Section 9352 is amended to provide that filing a petition for a late claim tolls the statute of limitations applicable to the claim.