Memorandum 90-62

Subject: Study L-3041 - Procedure for Creditor to Reach Nonprobate Assets

After the death of the settlor, trust property of a living (revocable) trust is subject to the claims of the creditors of the decedent settlor's estate and to the expenses of administration of the estate "to the extent that the decedent settlor's estate is inadequate to satisfy those claims and expenses." Prob. Code § 18201. A similar rule applies to property subject to a general testamentary power of appointment or to a general power of appointment that was presently exercisable at the time of the donee's death. Civil Code § 1390.3. A gift made in view of death is subject to claims of creditors. Civil Code § 1153. No specific statutory provision prescribes the extent to which creditors of a deceased account owner can reach deposit accounts in financial institutions that have a POD beneficiary designation or other property of the decedent subject to a nonprobate transfer upon the decedent's death.

California statutes do not provide any procedure for enforcing creditor claims against nonprobate assets. It is unclear whether a creditor can enforce the liability under the Trust Law by bringing an action against the trustee directly. There is no specific procedure provided to cover the situation where there are several nonprobate assets and the probate estate is inadequate to pay the expenses of administration and the allowed claims of creditors.

In 1985, the staff prepared a memorandum on this matter. Memorandum 85-96. However, consideration of the matter was deferred because the Estate Planning, Trust and Probate Law Section reported that the Section was working on the development of legislation, and the Commission decided not to duplicate the efforts of the Section. At the March 1990 meeting, the Commission decided to give this matter a priority for Commission consideration.

A 1989 statute enacted in Missouri may provide a concept that would be useful to explore in drafting legislation to deal with this situation in California. The key provision of the Missouri statute is set out in Exhibit 1 (attached). Other related provisions are not set out in the exhibit. The Uniform Multiple-Persons Accounts Law (Uniform Probate Code §§ 6-201-6-227) provides substantially the same scheme for deposit accounts if the other assets of the estate are insufficient. See Exhibit 2 (attached). A number of states have adopted this provision, but the provision is not included in the California Multiple-Party Accounts Law.

As an examination of the Missouri statute will disclose, the statute permits enforcement only by the personal representative of the decedent's estate, permits the personal representative to enforce the liability only if the personal representative has received a written demand therefor from a creditor, and makes the recipient of the nonprobate transfer liable only for a prorata share. Any party to the proceeding may bring into the proceeding the beneficiaries of other nonprobate transfers of the decedent. The statute provides a two-year statute of limitations on enforcement of the liability running from the decedent's death. Only property that was subject to the satisfaction of the decedent's debts during the decedent's lifetime may be reached and some property (such as insurance death benefits) is excluded.

There are many policy issues presented by this legislation that will need to be identified and resolved if the Commission undertakes to draft legislation for California. However, the staff believes that these issues can be resolved and legislation can be drafted if that is the Commission's desire. However, before undertaking to draft the legislation, the staff needs the reaction of the Commission (and other interested persons) to the concept of the Missouri legislation. We are not concerned with the details of the Missouri statute; we are concerned only with whether the concept of the statute is one that the Commission believes merits further consideration as a possible approach to California legislation in this area. If the Commission wishes to give further consideration to this approach, the staff will prepare a memorandum for a future meeting identifying the policy issues that need to be resolved.

Respectfully submitted,

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Executive Secretary

MISSOURI STATUTE

§ 461.071. Rights of creditors

1. If a deceased owner's probate estate is not sufficient to pay claims, taxes and expenses of administration, including statutory allowances to the surviving spouse, minor children and dependent children, the beneficiaries that receive a nonprobate transfer of decedent's property under sections 461.003 to 461.081 and the persons who receive other property of the decedent by a transfer other than from the administration of the decedent's probate estate that was subject to satisfaction of the decedent's debts during the decedent's lifetime, shall be liable to account to the decedent's personal representative for a pro rata share of the value received or forgiven of property that the decedent owned beneficially immediately before death to the extent necessary to discharge the claims and charges remaining unpaid after application of the funds and property in the decedent's estate. This subsection shall not apply to a death benefit paid pursuant to a life or accidental death insurance policy, contract, trust, plan or law; and it does not apply to survivorship rights in property held as tenants by the entireties.

2. Only decedent's personal representative may enforce the obligation of decedent's beneficiaries under subsection 1 of this section by bringing an action for accounting, but no proceeding to assert this liability shall be commenced unless the personal representative has received a written demand therefor by a creditor, surviving spouse or one acting for a minor or dependent child of the deceased owner, and no proceeding shall be brought for accounting under this section more than two years following the decedent's death. Sums recovered by the personal representative shall be administered as part of the decedent's estate.

3. After an action for accounting has been commenced under this section, any party to the proceeding may join and bring into the action for accounting beneficiaries of other nonprobate transfers of the decedent, persons subject to a similar proceeding for multiple-party

accounts held in financial institutions, and persons who succeed to property not subject to probate administration that was subject to satisfaction of the decedent's debts during the decedent's lifetime, including decedent's interest in property distributed at decedent's death by a trustee of a revocable trust or a trust under which the decedent had a right to appoint trust principal to himself, the decedent's estate, the decedent's creditors or the creditors of decedent's estate, property held for decedent by a personal custodian, and property held as a joint tenant with rights of survivorship, but only to the extent of decedent's contribution to the value of the joint property.

4. This section shall not affect the right of any transferor to execute a direction of the decedent to make a payment or to make a nonprobate transfer on death of the decedent, or to make the transferor liable to the decedent's estate, unless before the payment or transfer, the transferor has been served with process in a proceeding brought by the decedent's personal representative and the transferor has had a reasonable time to act on it.

§ 6-215. Rights of Creditors and Others.

(a) If other assets of the estate are insufficient, a transfer resulting from a right of survivorship or POD designation under this part is not effective against the estate of a deceased party to the extent needed to pay claims against the estate and statutory allowances to the surviving spouse and children.

(b) A surviving party or beneficiary who receives payment from an account after death of a party is liable to account to the personal representative of the decedent for a proportionate share of the amount received to the extent necessary to discharge the claims and allowances described in subsection (a) remaining unpaid after application of the decedent's estate. A proceeding to assert the liability may not be commenced unless the personal representative has received a written demand by the surviving spouse, a creditor, a child, or a person acting for a child of the decedent. The proceeding must be commenced within one year after death of the decedent.

(c) A surviving party or beneficiary against whom a proceeding to account is brought may join as a party to the proceeding a surviving party or beneficiary of any other account of the decedent.

(d) Sums recovered by the personal representative must be administered as part of the decedent's estate. This section does not affect the protection from claims of the personal representative or estate of a deceased party provided in Section 6-226 for a financial institution that makes payment in accordance with the terms of the account.

COMMENT

The sections of this article authorize transfers on death that reduce the estate to which the surviving spouse, creditors, and minor children normally must look for protection against a decedent's gifts by will. Accordingly, this section provides a remedy to these classes of persons that assures them that multiple-person accounts cannot be used to reduce the essential protection they would be entitled to if such accounts were deemed to permit a special form of specific devise. This section provides a remedy for collection of amounts necessary to pay tax obligations incurred by the decedent during life, but not for death taxes. See Section 1-201(4) ("claims" defined). Apportionment and allocation of death taxes, and their collection, is governed by law other than this section.

Under this section a surviving spouse is automatically assured of some protection against a multiple-person account if the probate estate is insolvent; rights are limited, however, to sums needed for statutory allowances. The phrase "statutory allowances" includes the homestead allowance under Section 2-401, the family allowance under Section 2-403, and any allowance needed to make up the deficiency in exempt property under Section 2-402. In any case (including a solvent estate) the surviving spouse could proceed under Section 2-201 et seq. to claim an elective share in the account if the deposits by the decedent satisfy the requirements of Section 2-202 so that the account falls within the augmented net estate concept. In the latter situation the spouse is not proceeding as a creditor under this section.

Under subsection (b), a proceeding must be commenced within one year after the decedent's death. This limitation period corresponds to the long term self-executing statute of limitations applicable under the code to creditors' claims generally.