

## **POST-MORTEM DEBT COLLECTION**

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**Disclaimer:** These materials are not intended to be comprehensive. Many portions only lightly touch the surface. Also, not all of the issues are updated at the same time, so some parts may be less current than others. Before using any authorities or comments contained in these materials, the attorney should research these issues independently rather than rely on these materials.

1. **Assets in the Probate Estate**

**Decedent's probate estate**

- Assets held in decedent's name alone
- Properties held with others as tenants in common

**Assets outside of decedent's probate estate**

- Assets held in decedent's revocable trust [part of decedent's taxable estate; available to creditors]
- Properties held with others in joint tenancy [Not available to creditors]
- Community property with right of survivorship [not part of decedent's probate estate but available to creditors]
- Pay on death accounts [not available to creditors]
- Retirement accounts governed by federal law [go to the designated beneficiaries, not available to creditors]

2. **Case Study No. 1 ("Plain Vanilla") – Probate Estate, No Trust (Rare these days)**

Client owes his lawyer borrows \$50K, fails to pay the outstanding balance, and dies. He is survived by one sister. He had one bank account with a \$70K balance, but there are multiple creditors. Debtor's sister files a probate petition and gives notice to creditors

3. **Estates Smaller Than the Total Liabilities**

Debtor owes his lawyer	\$50,000
Other creditors are owed	\$30,000
Total assets in Debtor's name	-\$70,000
Total debts owed (multiple creditors)	<u>\$80,000</u>
	(\$10,000)

4. **Creditor's and Other Creditors' Pro Rata Share:**

$$\$50K:\$30K = 63\%:37\%$$



Creditor's pro rata share from net proceeds = 63% of the net proceeds  
\$70K less the personal representative's fee and the probate attorney's fees  
if all creditors have *same priority\** and if the personal representative approved all *creditor's claims\** (To be explained later)  
Wait! There is a long and winding road before creditor is paid

## 5. **Statute of Limitations – Minefield For Creditors!**

- Underlying civil statute of limitations: e.g. oral contract, written contract, personal injury, property damage
- California example:
  - Breach of written contract – 4 years
  - Property damage – 3 years
  - Personal injury – 2 years
  - Breach of oral contract – 2 years
  - Caregivers wage and hour claims – 3-4 years

## 6. **Creditor's Claims Against Decedent's Estate**

Two most important things to remember

- Creditor's claim: An action may **not** be commenced unless a claim is filed and rejected (Cal. Prob. Code §9351)
- Statute of limitations for claims against decedent's estate – In CA, 1 year (Code Civ. Proc. §366.2)

## 7. **Creditor's Claim Procedures – 3 Steps**

- Step 1 in probate court – File a creditor's claim with probate court – either approved or rejected
- Step 2 in civil court – File a civil action against the estate (or an appropriate petition in probate court)
- Step 3 in probate court – Wait for the distribution of \$\$
- *Practice tip:* File a request for special notice to monitor the probate matter

## 8. **Decedent's Representative Following Appointment.**

### **Step 1: Notice of Petition to Administer Estate**

- Estate's notice requirement: The personal representative must publish a "Notice of Petition to Administer Estate"
- Serve the Notice of Administration of the Estate to *all known and reasonably ascertainable creditors by mail*
- Time period for notice: Must be given within *the later of*
  - 4 months after the date the letters are first issued to the personal representative;
  - 30 days after the personal representative first has knowledge
- Contents of the Notice of Administration of Estate of XXX, Decedent (Probate Code §9052)
- Creditor's claim

A creditor shall file a claim before expiration of the later of:

- 4 months after the date letters are first issued to a general personal representative
- 60 days after the date notice of administration is mailed or personally delivered to the creditor
- Again – Don't forget the 1 year SOL!
- As well as the SOL for the underlying claim

## 9. **Contents of Creditor's Claim**

- Generally tort or contract claims
- When in doubt, file a timely claim
- Check local judicial council form
- Exemplar California form – See Appendix DE-172 form
- General requirements: demand for payment + documentary support (including declarations, business records, etc.)
- Be mindful of the **Business Record Exception** to the Hearsay Rule under Evidence Code § 1271
  - (a) The writing was made in the regular course of business;
  - (b) made at or near the time of the act, condition, or event;
  - (c) the custodian or other qualified witness testifies to its identity and the mode of its preparation; and
  - (d) the source of info and method and time of preparation were such as to indicate its trustworthiness.
- Representative may request additional supporting proof
- Claim based on written instrument – the original or a copy of the promissory note or written instrument must be attached to the claim
- Secured obligation – no need to attach the document. It is sufficient to describe the mortgage, deed of trust or lien and the recording reference for such
- Notice of debt instead? Insufficient. A valid statutory claim must demand payment from the estate

Even serving the personal representative with summons and complaint does not satisfy the claim-filing rules. **MUST DEMAND PAYMENT!**

- Secured lender's non-judicial foreclosure – no creditor's claim required if creditor does not seek recovery beyond the security property
- Public entities' claims – outside the general procedures of §9100

## 10. **Personal Representative's Response to the Claim**

- Once the claim is presented, personal representative can:
  - Accept the claim;
  - Reject the claim – creditor must commence a legal action within 90 days in California
  - Do nothing – deemed rejected

11. **What If No Probate Petition Filed By the Decedent's Family Members? – Very Common When the Family Members Are Aware of the Decedent's Debts**
- Creditor has to file a probate petition to open the debtor's probate estate
  - Letters of testamentary issued
  - File the creditor's claim before the 1-year SOL
  - *Practice tip:* Often, after having done nothing, the decedent's family steps up and files a competing probate petition once a creditor files a probate petition. If you know of the decedent's family's existence, contact them and encourage them to file the petition so you won't waste your money. Family members have priority over creditors. See priority below
12. **Priority of Right To Appointment – Check the Local Statute! Court Must Stick To the Statutory Priority**
- The following is priority in California:
    - Surviving spouse or domestic partner
    - Children
    - Grandchildren
    - Other issue
    - Parents
    - Brothers and sisters
    - Brothers' and sisters' issue (e.g., nieces and nephews of decedent)
    - Grandparents
    - Grandparents' issue (e.g., uncles, aunts)
    - Predeceased spouse's or domestic partner's children (i.e., step-children)
    - Predeceased spouse's or domestic partner's other issue
    - Other "next of kin"
    - Predeceased spouse's or domestic partner's parents (e.g., decedent's mother-in-law)
    - Predeceased spouse's or domestic partner's parents' issue (e.g., your mother-in-law's children)
    - Decedent's conservator or guardian of the estate acting in that capacity at that time, provided he or she has filed a first account and is not acting in the same capacity for any other person
    - Public administrator, i.e., a county officer
    - *Creditors.* Appointment of creditors is *disfavored*. The court may deny the creditor's appointment and appoint any qualified person who claims appointment.
    - Any other person
13. **Effect of Personal Representative's Failure To Act On Claim** – if no action is taken **within 30 days**, at creditor's option, it can be deemed equivalent to giving a notice of rejection on the 30<sup>th</sup> day, and file a civil action
- **Within 90 days** from the 30<sup>th</sup> day, or
  - Within the SOL, but not more than **a year** from the date of death

14. *Practice tip: start* the probate petition and claim procedures well before the 1-year anniversary from the date of death so that the claim can be filed within 1 year from debtor's death

15. **Tolling of Statute of Limitations**

- The filing of a creditor's claim or a petition to file a late claim [e.g., Cal. Prob. Code §9352] – tolls the SOL
- The allowance or approval of a claim in whole or in part [during the administration of the estate as to the part allowed or approved]

16. **Filing of Late Claim**

The creditor fails to timely file a claim when:

- Within 4 months after the Letters are first issued or
- Within 60 days after the date Notice of Administration is mailed

Creditor can seek the court's permission to file a late claim, if

- The personal representative failed to send proper and timely notice of administration of the estate to the creditor, and the petition is filed within 60 days after the creditor has actual knowledge of the administration
- The creditor had no knowledge of the facts reasonably giving rise to the existence of the claim more than 30 days prior to the time for filing a claim under the claim period statute (e.g., Cal. Prob. Code §9100), and the petition is filed within 60 days after the creditor has actual knowledge of both of the following:
  - the existence of the facts reasonably giving rise to the existence of the claim
  - the administration of the estate

17. **Step 2: After the Claim Is Rejected**

File a legal action against the representative of the estate – obtain a judgment – judgment is treated like other *approved* claims

18. **Step 3: Back to Probate Court**

- Judgments and approved claims – wait until the personal representative's petition for final distribution is filed and approved – \$\$ FINALLY!
- Either pro rata share to the creditors if assets are less than the liabilities
- If sufficient assets to cover all creditor's claims, after expenses and claims are paid, heirs receive their shares

19. **Order of Priority for Payment** [e.g., Cal. Prob. Code §11420(a)]

- (1) Administration expenses
- (2) Secured obligations and liens, including a judgment lien, *in the order of their priority*. If the proceeds are insufficient, the unsatisfied part of the secured obligation (deficiency) – classified with general debts

- (3) Funeral expenses  
*[federal tax claims took preference over last illness expenses]*
- (4) Last illness expenses
- (5) Family allowance
- (6) Wage claims (up to \$2,000 for each employee of the decedent for work done within 90 days before the date of death)
- (7) General debts, including judgments not secured by a lien and all other debts not included in a prior class

Payments within classes of debts – pro rata payments if estate insolvent

No preference within each class of debts

**20. Action Covered By Insurance**

- It's covered, no need to join as a party the personal representative or successor-in-interest [Cal. Prob. Code §550]
- A judgement with the policy limits may be enforced against the insurer without first filing a claim, unless the insurer seeks reimbursement [Cal. Prob. Code §9390]

**21. Lienholders**

- Secured lender, or judgment creditor, with a lien against the property that is subject to the lien.
- Not required to file a claim so long as the lienholder waives all other recourse against the decedent's estate's other properties (e.g., Cal. Prob. Code §9391).

**22. Case Study No. 2 – Debtor’s Assets Held In Trust**

Facts: Debtor dies with or without a will, but he had a living trust and his assets belong in the Don Debtor Living Trust. None of the family members filed a Probate Petition. The heirs/successor trustees filed an Affidavit of Death.

- Title-holder? Assets in his trust → to his successor trustee who can sell or transfer the property.
- Creditor's claims statutes against the decedent's trust – e.g., California Probate Code section 19000 et seq. gives the decedent's trustee to option to the decedent's trust to handle the creditor's claims.
- What if the successor trustees do nothing? Unclear. Some authorities indicate that the creditor may simply sue the trustee if there is no probate administration and the trust claims procedure is not initiated.
- § 850 petition - alternatively, a creditor of the deceased settlor or a person who claims that the trustee is in possession of real or personal property belonging to the claimant may file a petition under Prob. Code § 850(a)(3)(A) or (3)(C).
- Recommended course of action: Most practitioners file a creditor's claim before the 1-year SOL expires.

### 23. **Creditor's Recourse Against Decedent's Trust Assets**

- Property that was placed by Decedent in a revocable inter vivos trust (living trust) is "subject to" to the claims of creditors of Decedent's probate estate *to the extent* the probate estate is inadequate to satisfy those claims and expenses.
- In California, Prob. Code §18200 – Creditor's rights against revocable trust during settlor's lifetime (but subject to all exemptions, §18201).
- In California, Prob. Code §19001 – available to satisfy creditors' claims.

### 24. **Debtor's Living Trust Assets**

- Dobler I (*Dobler v. Arluk Med. Ctr. Industrial Group, Inc.* (2001) 89 Cal.App.4th 530) – A Medi-Cal case. No need to file a separate creditor's claim against the trustee
- Dobler II (*Arluk Med. Ctr. Industrial Group, Inc. v. Dobler* (2004) 116 Cal.App.4th 1324, 1335) – Personal representative has no duty to preserve the trust assets for creditors
- Warning: Do not blow the SOL while negotiating with the successor trustee! If the Trustee plays hard ball, go ahead and file a probate petition so that you would have a court case number and file a creditor's claim.

### 25. **Case No. 3 – Action To Recover From Community Property**

- **Facts:** Debtor and his wife owned a house as **community property with Right of Survivorship**, resulting in Widow's becoming 100% owner upon the debtor husband's death. Debtor has no other asset.
- Real property in Wife's name – Available to creditors.
- **Side bar: Procedural difference when Debtor spouse is alive.**
- *11601 Wilshire Associates v. Grebow* (1998) 64 Cal.App.4<sup>th</sup> 453, 455-458 [In Landlord's action against H based on his personal guaranty of lease, no C/A could be stated against W solely to establish parties' community estate liability where W neither signed the guaranty nor used the office space.
- Family Code section 916(a)(2): former community estate property received by the nondebtor spouse at division is liable **only if** the nondebtor spouse is assigned the debt in division." *In re Marriage of Braendle* (1996) 46 Cal.App.4<sup>th</sup> 1037, 1042.

### 26. **Various Assets of Debtor and His or Her Souses**

- Debtor's **separate property** liable to creditors.
- Spouse's **separate property not** liable to creditors.
- *Exception:* Spouse may be liable for necessities of life of the debtor.
- **Joint tenancy** property generally not liable – a device most commonly used by debtors for asset protection, especially when the debtor is older. Most commonly used asset protection device.
- cf. *Belshe v. Hope* (1995) 33 Cal.App.4th 161, holding joint tenancy liable for Medi-Cal recovery
- **Community Property Generally Liable** – Community property is liable for the debtors of either spouse incurred BEFORE or DURING marriage with



exceptions. (E.g., Cal. Family Code §910.) **After death, the community property of the debtor and the surviving spouse is also liable for the debts of each.** (*Dawes v. Rich* (1997) 60 Cal.App.4<sup>th</sup> 24, holding that the community property share of a decedent spouse was held liable for the debts of surviving spouse.)

- Joint tenancy with Right of Survivorship – No authority on point, but should be treated like community property and liable for the debts of either spouse.

## 27. **Case No. 4. Post-Mortem SPOUSAL Property Disputes [aka Post-Mortem Divorce]**

**Facts:** W2 brings a creditor's claim against H's estate to recover the expenses H incurred to pay for non-community obligations, e.g., rehab and college education for the children from W1 a long time ago.

- **Fam. Code §751(b).** This confidential relationship imposes a duty of the *highest good faith and fair dealing* on each spouse, and neither shall take any unfair advantage of the other (*Lintz v. Lintz* (2014) 222 Cal.App.4<sup>th</sup> 1346, 1353-1354).
- **Family Code §1101. Breach of Fiduciary Duty**
  - (d)(1) Except as provided in paragraph (2), any action under subdivision (a) shall be commenced within three years of the date a *petitioning* spouse had actual knowledge that the transaction or event for which the remedy is being sought occurred.
  - (2) An action may be commenced under this section ***upon the death of a spouse*** or in conjunction with an action for legal separation, dissolution of marriage, or nullity *without regard to the time limitations set forth in paragraph (1)*.
  - *Latches defense.*
  - Not subject to the 120-day SOL; but subject to the *latches* defense (Fam. Code §1101(d)(2); *Patrick v. Alacer Corp.* (1011) 201 Cal.App.4<sup>th</sup> 1326, 1337, the Emergen-C case.)
- Remedies
  - Set-aside suit against transferee – a common law action against the transferee (e.g., *Shelly Sterling vs. Donald Sterling's girlfriend*).
  - Action against the deceased spouse's estate
    - a. Section 13650 set-aside petition;
    - b. A separate civil action against the estate; or
    - c. Once probate proceedings have been commenced for the decedent's estate, the surviving spouse may file a Section 850(a)(2) petition.

## 28. **Uniform Voidable Transactions Act**

- Formerly known as the fraudulent conveyance act
- Actual Intent to Hinder-Delay-Defraud Creditors (Civ. Code §3439.04(a)(1).)
- Factors to Consider Determining Actual Intent to Hinder-Delay-Defraud:
  - (a) Whether the [transfer/obligation] was to a/an \_\_\_\_\_;
  - (b) Whether [Third Party Debtors] retained possession or control of the property after it was transferred;
  - (c) Whether the [transfer/obligation] was disclosed or concealed;
  - (d) Whether before the [transfer was made/obligation was made] [Third Party Debtors] had been sued or threatened with suit;
  - (e) Whether the transfer was of substantially all of [Third Party Debtors]'s assets;
  - (f) Whether [Third Party Debtors] fled;
  - (g) Whether [Third Party Debtors] removed or concealed assets;
  - (h) Whether the value received by [Third Party Debtors] was not reasonably equivalent to the value of the [asset transferred/amount of the obligation incurred];
  - (i) Whether [Third Party Debtors] [was/were] insolvent or became insolvent shortly after the [transfer was made/obligation was made];
  - (j) Whether the transfer occurred shortly before or shortly after a substantial debt was incurred;
  - (k) Whether [Third Party Debtors] transferred the essential assets of the business to a lienholder who transferred the assets to an insider of [Names of Defendants]; and
- Constructive Fraudulent Transfer – No Reasonable Equivalent Value (Civ. Code §3439.04(a)(2).)
- Constructive Fraudulent Transfer (Insolvency) (Civ. Code §3439.05.)
- Affirmative Defenses – Good faith, Statute of Limitations (Civ. Code §§3439.08(a), (f)(1); 3439.09(a), (b).)

## 29. **Enforcement of Judgments**

- Generally Enforcement of Judgment Law “EJL” – CCP §680.010, et seq.
- Beneficiary’s interest in trust subject to Code of Civil Procedure section 709.010.
- Enforcement of Money Judgment – only upon petition under §709.010 by a judgment creditor to a court having jurisdiction over administration of the trust (§17000, et seq.)
- §15300 Restraint on Transfer of **Income**  
  
“Except as provided in Sections 15304 to 15307, inclusive, if the trust instrument provides that a beneficiary's interest in income is not subject to voluntary or involuntary transfer, the beneficiary's interest in income under the trust may not be transferred and is not subject to enforcement of a money judgment until paid to the beneficiary.”
- §15301 Restraint on Transfer of **Principal**:

“(a) Except as provided in subdivision (b) and in Sections 15304 to 15307, inclusive, if the trust instrument provides that a beneficiary's interest in principal is not subject to voluntary or involuntary transfer, the beneficiary's interest in principal may not be transferred and is not subject to enforcement of a money judgment **until paid to the beneficiary**.

(b) After an amount of principal has become **due and payable** to the beneficiary under the trust instrument, **upon petition to the court under Section 709.010** of the Code of Civil Procedure by a judgment creditor, the court may make an order directing the trustee to satisfy the money judgment out of that principal amount. The court in its discretion may issue an order directing the trustee to satisfy all or part of the judgment out of that principal amount.”

- *Carmack v. Reynolds* (2017) 2 Cal.5<sup>th</sup> 844; *Frealy v. Reynolds* (9<sup>th</sup> Cir. 2017) 867 F3d 1119.
- §15304 – Where settlor is beneficiary, no spendthrift protection.