

Memorandum 2018-6

**Nonprobate Transfers: Creditor Claims and Family Protections
(Request for Public Comment)**

In this study, the Commission¹ is considering the extent to which nonprobate transfers (“NPTs”) should be liable for a decedent’s debts and family protections. This study is based on a background report from the Commission’s former Executive Secretary Nathaniel Sterling entitled *Liability of Nonprobate Transfer for Creditor Claims and Family Protections* (“NPT Report”).²

BACKGROUND ON STUDY

One of the key concerns underlying this study is that the liability of a decedent’s assets depends on the particular form of transfer used to convey the asset. In particular, the means used to transfer a particular asset (e.g., will vs. NPT) can affect whether the asset is available to satisfy family protections or to pay the decedent’s or the estate’s creditors.

The NPT Report states “[t]he policy of the law to require payment of a decedent’s just debts and to protect a decedent’s surviving spouse and children in probate has been shredded by the ad hoc development of nonprobate transfer law.”³ The Report concludes that the law in California governing the liability of a nonprobate transfer for debts of a decedent “is sketchy, and what there is of it shows no coherent public policy but rather a pattern of haphazard development.”⁴

1. Any California Law Revision Commission document referred to in this memorandum can be obtained from the Commission. Recent materials can be downloaded from the Commission’s website (www.clrc.ca.gov). Other materials can be obtained by contacting the Commission’s staff, through the website or otherwise.

The Commission welcomes written comments at any time during its study process. Any comments received will be a part of the public record and may be considered at a public meeting. However, comments that are received less than five business days prior to a Commission meeting may be presented without staff analysis.

2. The NPT Report is available at <http://www.clrc.ca.gov/pub/BKST/BKST-L4100-NPT-Creditors.pdf>.

3. NPT Report, p. 151.

4. *Id.* at 10.

The NPT Report proposes a comprehensive treatment of NPT liability, but suggests that “[a]t a minimum the law should clearly state the substantive liability of a nonprobate transfer for the decedent’s debts and family protections.”⁵

Recently, this study has focused on evaluating the potential enactment of Section 102 of the Uniform Nonprobate Transfers on Death Act (“Uniform Act”)⁶ to govern NPT liability. This memorandum raises broader questions about NPT liability reform and seeks public comment on these issues.

STUDY FOCUS: NPT LIABILITY PRINCIPLE VS. NPT LIABILITY FRAMEWORK

Initially, this study was focused on a relatively simple reform — enact a general principle establishing the liability of NPTs for a decedent’s debts and family protections, without providing a procedural framework for the allocation and enforcement of that liability. By pursuing this simple reform first, the Commission could, with the commitment of a relatively modest amount of resources, determine the viability of reform in this area of the law. If the initial reform were enacted, the Commission could then commit the significant resources required to develop a comprehensive procedural framework.⁷

Even without such a framework, a statutory liability principle was expected to be an improvement over the status quo. Providing a clear liability rule “would save parties a trip to court to establish the rule. A clear rule will also facilitate out of court resolution of a liability dispute in the ordinary case.”⁸

At its June 2017 meeting, the Commission decided that this study should focus on Section 102 of the Uniform Act,⁹ which includes a procedural framework for imposing liability.

5. NPT Report, p. 153; see also generally *id.* at 151-160.

6. Section 102 of the Act is codified as Section 6-102 of the Uniform Probate Code. Throughout this memorandum, any quoted language is drawn from the Uniform Probate Code unless noted. The Uniform Probate Code and the Uniform Act are available at the following addresses, respectively: http://www.uniformlaws.org/shared/docs/probate%20code/UPC_Final_2017mar30.pdf; http://www.uniformlaws.org/shared/docs/nonprobate%20transfers%20on%20death/unpnda_final_with98amend.pdf.

7. See Memorandum 2012-45, p. 13.

8. NPT Report, p. 153.

9. Minutes (June 2017), p. 6. In addition, the Commission decided to consider whether reforms are needed to address any problems created by the decision in *Kircher v. Kircher*, 189 Cal. App. 4th 1105, 117 Cal. Rptr. 3d 254 (2010), *rev. denied* 2011 Cal. LEXIS 1437 (liability of joint tenancy property for the obligations of a deceased spouse).

Since June, this study has focused specifically on implementation issues for Section 102 in California (including the types of NPT assets that would be liable, types of claims allowed, and application of family protections). Thus, the study has been systematically examining the detailed questions that would need to be addressed to construct a comprehensive NPT liability framework.

Working through the implementation details makes sense, in terms of moving toward completion of a reform proposal. However, this detailed analysis does not invite reflection on the overall direction of the study. Before committing the considerable resources needed to fully flesh out a procedural framework, the staff thought it would be helpful to pause and consider the bigger picture. This memorandum is intended to facilitate such reflection and seek public input on the broader question of NPT liability reform.

Concerns about Liability Principle

Having done substantial work on this study, the staff is concerned that enacting a simple liability principle, without an implementing framework, could leave a great deal of uncertainty in practice. Such a principle, by itself, would not provide guidance on who should pay whom how much in a situation with multiple creditors and beneficiaries or what steps a creditor with a claim should take in seeking payment from beneficiaries. Over time, such issues might be addressed by the courts and the Legislature. However, in the near-term, there could be increased confusion and litigation, with inconsistent and potentially inequitable results.

Many NPT beneficiaries would not be equipped to evaluate the validity of a creditor claim and the extent of their obligation to pay, particularly as these issues would largely be addressed, if at all, in case law. When presented with a claim, an NPT beneficiary would be faced with the choice of whether to simply pay the requested amount or undertake the expense of hiring a lawyer to determine the obligation to pay (and then, perhaps, still have to pay the creditor). Where a beneficiary of limited means receives valuable tangible property (e.g., a piece of real property or a vehicle) by NPT, the beneficiary may have no choice but to part with the property, either turning the property over to the creditor or selling the property to pay legal costs to fight the creditor.

Without rules allocating liability (e.g., rules establishing pro rata liability or a right of contribution or reimbursement from other beneficiaries),¹⁰ a creditor could presumably collect the entire amount due from a single NPT beneficiary (assuming that the amount of the claim does not exceed the value of the NPT¹¹). This could lead to inequitable results, with the creditors seeking payment from beneficiaries who received high-value gifts or are most accessible.¹²

Some of these problems could be addressed by supplementing a liability principle with rules on, for instance, allocation of liability,¹³ but adding such rules would shift the reform closer toward the comprehensive framework approach.

Concerns about Procedural Framework

A consequence of the Commission's decision to examine the Uniform Act was that the study was no longer focused on a simple liability principle, but instead on the Uniform Act's NPT liability framework.

The Uniform Act largely relies on the probate process as the procedural framework for enforcing NPT liability.¹⁴ Although the choice¹⁵ of the probate process to administer NPT liability is not necessarily a problem, it does undermine the decedent's effort to avoid probate through the use of NPTs. In addition, shifting NPTs into a judicially-supervised administration process, like probate, would presumably place a new burden on already-strained court resources.

Since the Commission's decision to focus on the Uniform Act, it has become clear that, even with the Uniform Act's reliance on the probate process to enforce NPT liability, there are a number of implementation issues and details that the Commission will need to consider before a recommendation could be completed.

10. See generally, e.g., NPT Report, pp. 65-66, 92-93.

11. See *id.* at 104; see also UPC § 6-102(b). The Uniform Act limits the liability of an NPT recipient to "the value of nonprobate transfers received or controlled by that transferee." *Id.*

12. See NPT Report, pp. 92-93 ("In the ordinary case the ... creditor could be expected to seek recovery from the transfer most sufficient and most readily accessible with least effort.").

13. See *id.* at 115-125.

14. See UPC § 6-102 Comment 1.

15. The NPT Report discusses different options for enforcement of liability. See NPT Report, pp. 114-125. The NPT Report concludes that the "existing probate and trust claim procedures should be supplemented by a procedure dedicated to discharge of the decedent's debts where there is no probate or trust claim proceeding. ... The Washington statute and the California trust claim and estate tax proration procedures should serve as models." See *id.* at 125.

In short, the staff foresees that the resulting reform proposal will be a complicated one.

Thus, by moving away from the liability principle approach, the Commission could be sacrificing one of the primary benefits of pursuing a more limited initial reform. Focusing first on the liability principle was intended to give the Commission a better sense of the perceived policy merits and practicability of reform in this area, before the Commission devoted the significant resources required to develop a comprehensive liability framework.

CONCLUSION

Although the Commission has made some progress towards the development of a liability framework based on Section 102 of the Uniform Act, there is still a great deal of work to be done to achieve that result.

Before continuing that work, the staff believes it would be helpful to invite and consider stakeholder input on the general approach to be taken in this study. Specifically, it would be helpful to receive feedback from stakeholders on the policy merits and practicability of the following reform approaches:

- Develop a simple NPT liability principle, without implementing procedural rules.
- Develop a comprehensive NPT liability framework (e.g. Section 102 of the Uniform Act).
- Do not pursue a general reform on the issue of NPT liability.

If the Commission were to take the third approach — deciding against developing a broad rule on NPT liability — there would still be narrower issues that could be addressed in this study:

- Consider whether the law should be reformed to address concerns about the decision in *Kircher v. Kircher*.¹⁶
- Consider whether certain existing probate family protections should be extended to NPTs.

The staff could reach out to relevant stakeholder groups (e.g., creditors, the Trusts and Estates Section of the State Bar, the California Judges Association, and the Judicial Council) to request comment on the merits of the approaches noted

16. 189 Cal. App. 4th 1105, 117 Cal. Rptr. 3d 254 (2010), *rev. denied* 2011 Cal. LEXIS 1437.

above. In order to provide sufficient time for response, these issues could be scheduled for discussion at the Commission's April meeting.

Is that approach acceptable?

Respectfully submitted,

Kristin Burford
Staff Counsel