Study L-4100 April 5, 2018

Memorandum 2018-15

Nonprobate Transfers: Creditor Claims and Family Protections (Direction of Study)

In this study, the Commission[1] has been considering the extent to which nonprobate transfers ("NPTs") should be liable for a decedent's debts and family protections. The 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]

Memorandum 2018-6 raised questions about the general direction of this study and recommended that the Commission solicit public comment on how to proceed. The Commission has received a letter from the Executive Committee of the Trusts and Estates Section of the California Lawyers Association ("TEXCOM"), which is attached as an Exhibit.

This memorandum provides a brief overview of the general issues in this study and presents the letter from TEXCOM. These materials are intended as a prompt for discussion of the general policy direction of this study.

BACKGROUND

Historically, a decedent's property was generally distributed pursuant to a will or rules of intestate succession, through a court-supervised probate proceeding.[3] In probate, the decedent's property is gathered, used to pay debts

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. See NPT Report, p. 7.

and satisfy any "family protections,"[4] and the remainder is then distributed to devisees and heirs clear of any claims.[5]

In the 1960s, the inter vivos or living trust became popular as a means of avoiding the cost and delay of probate. Trusts are now "the standard method of passing property at death."[6]

In more recent years, the Probate Code has been amended to authorize other types of NPTs, like pay-on-death bank accounts and transfer-on-death registration of securities and vehicles.

Some forms of NPT may be liable for a decedent's debts. For example, if a decedent's probate estate is inadequate, the decedent's trust can be liable to the decedent's creditors.[7] The recently authorized revocable transfer on death deed is expressly liable.[8]

For other types of NPTs, the statutory law governing the specific NPT does not provide for creditor liability.[9] However, it is possible that a creditor could try to impose liability on an NPT asset under more general laws (e.g., the law on voidable transactions[10]).

It is not clear that any form of NPT is liable for family protections.[11]

The NPT Report indicates that the piecemeal development of NPT laws has resulted in liability rules that are "unclear, inconsistent, and haphazard."[12]

The rationale for the different liability treatment of probate property versus nonprobate property is not obvious. This is particularly true in situations where the asset transferred via NPT would be subject to liability were it instead transferred by will or trust.

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4. See, e.g., Prob. Code §§ 6500-6501 (temporary possession of dwelling), 6510-6511 (exempt property set-aside), 6520-6528 (probate homestead), 6540-6545 (family allowance), 6600-6615 (small estate set-aside).
5. NPT Report, p. 7; Prob. Code §§ 9000-9399, 11400-11467.
6. See NPT Report, p. 8.
7. See Prob. Code § 19001.
8. See Prob. Code §§ 5670-5676.
9. NPT Report, p. 19.
10. See Civ. Code § 3439.
11. See CEB, California Estate Planning, § 6.5 (2017) (one potential disadvantage of a revocable trust is "[f]amily members will not have the benefit of the family protection provisions of [Probate Code] §§ 6500-6545, including the right to a probate homestead under [Probate Code] § 6520."); but see NPT Report, p. 140 (Under abatement rules in the Probate Code, "[a]n argument can be made that [an NPT] may already be subject to family protection statutes in many circumstances."); Prob. Code § 21401.
12. See NPT Report, p. 9.

The NPT Report concludes with a proposal to reform the law to comprehensively address and rationalize the liability rules for NPTs.[13] Such a reform could clarify how to satisfy a decedent's debts and family protections taking into account *all* of the decedent's assets, regardless of how those assets are transferred at death (e.g., will, trust, pay-on-death designation). Presumably, this rule would offer clarity to creditors, family members and the recipients of the decedent's property as to which assets should be used to satisfy a particular claim. It would also eliminate any inequities that might arise through the use of NPTs that are not liable for the payment of debts.

STUDY APPROACH

Memorandum 2018-6 discussed the evolution of this study's focus as it has proceeded.[14] That history is briefly summarized below.

Initial Focus: Stand-Alone Liability Principle

The Commission's study of this topic was initially focused on a relatively simple reform — enactment of a statutory principle of liability, without any implementing rules or procedures. This narrow focus was intended to allow the Commission, with a relatively modest commitment of resources, to gauge the appetite for reform in this area.

It was thought that enactment of a liability principle by itself would be an improvement on existing law,[15] because it would eliminate the need for litigation on the basic question of liability. The Commission recognized that this approach would leave a number of important questions unanswered.[16] For example, if NPTs are liable for a decedent's creditors, how should that liability be allocated between different NPT beneficiaries? Should liability be limited to a pro rata share? What is the procedure for enforcing this liability?

If the liability principle were enacted, the Commission could then decide whether to conduct a follow-up study to address the unanswered questions.

13. See NPT Report, p. 151; see also *id*. at 151-160.
14. See generally Memorandum 2018-6, pp. 2-5.
15. NPT Report, p. 153.
16. See generally Memorandum 2018-6, pp. 3-4.

New Study Focus: Comprehensive Liability Framework

At its June 2017 meeting, the Commission turned away from developing a statutory liability principle. Instead, the Commission decided to investigate the possibility of a reform based on Section 102 of the Uniform Nonprobate Transfers on Death Act ("Uniform Act").[17] That provision makes NPTs potentially liable for a decedent's debts.[18] It also provides a comprehensive process for implementing that liability: In simplified terms, NPT assets needed to pay creditors are pulled into a probate.[19]

Since that change in direction, staff memoranda have focused on systematically working through specific implementation questions.[20] The end goal would be the development of a comprehensive liability framework based on Uniform Act Section 102 (with changes appropriate to implementation in California).

One major drawback of a comprehensive procedural approach to NPT liability is that it would likely reinstate, to some extent, the costs and delays of the probate process, which the decedent had presumably sought to avoid for assets transferred by NPT. This could be seen as a significant change to existing estate planning policy.

REQUEST FOR COMMENT

At its February 2018 meeting, the Commission directed the staff to reach out to stakeholders, seeking public comment on the policy merits and practicability of the following reform approaches:

(a) Develop a simple NPT liability principle, without implementing procedural rules.
(b) Develop a comprehensive NPT liability framework (e.g., Section 102 of the Uniform Act).
(c) Do not pursue a general reform on the issue of NPT liability, but, perhaps address narrower issues on this topic including:

17. Section 102 of the Act is codified as Section 6-102 of the Uniform Probate Code. 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/unptda_final_with98amend.pdf.
18. See Uniform Act § 102(b), (c).
19. See Uniform Act § 102(b).
20. See generally Memorandum 2017-36; Memorandum 2017-46.

(1) Consider whether the law should be reformed to address concerns about the decision in *Kircher v. Kircher*.[21]

(2) Consider whether certain existing probate family protections should be extended to NPTs.[22]

The staff reached out to potentially interested organizations, seeking public comment on these issues. The organizations contacted by the staff represent practitioners, the courts and judges, public guardians, creditors, financial institutions, seniors, and low-income persons.

In response to that request, the Commission received comment from TEXCOM. The staff greatly appreciates their input. If the Commission receives comment from other groups before the meeting, such comment will also be presented for consideration. Stakeholders are also encouraged to attend the meeting and testify orally.

TEXCOM recommends against the Commission pursuing any general reform on the issue of NPT liability (i.e., developing either a liability principle or a comprehensive liability framework).[23]

TEXCOM does not believe that there is a significant problem under existing law.[24] They note that the assets that would be governed by the reform "for which there is no current NPT liability is greatly limited."[25] Recall that assets that pass by living trust are potentially liable to a decedent's creditors.[26]

TEXCOM considers existing law on NPT liability to be adequate.[27]

Overall, TEXCOM's comments seem to indicate that the benefits of an NPT liability reform would be outweighed by the costs and burdens that the liability rule would impose in practice.[28] TEXCOM points out that the process of collecting NPT assets for allocation of creditor claim liability "will require an inordinate amount of effort relative to the claimed advantage of pro rata liability."[29]

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21. 189 Cal. App. 4th 1105, 117 Cal. Rptr. 3d 254 (2010), *rev. denied* 2011 Cal. LEXIS 1437.
22. See Minutes (Feb. 2018), p. 5; Memorandum 2018-6, pp. 5-6.
23. Exhibit p. 9.
24. Exhibit pp. 7-8.
25. Exhibit p. 7.
26. See Prob. Code § 19001; see also Exhibit p. 7.
27. Exhibit p. 8.
28. See generally Exhibit pp. 7, 8.
29. Exhibit p. 8.

TEXCOM also notes that a general NPT liability reform would "undermine[] the decedent's effort to avoid probate through the use of NPTs."[30]

Instead, TEXCOM recommends that the Commission consider the more targeted reforms suggested in option (c) set out above:

(1) Consider whether the law should be reformed to address concerns about the decision in *Kircher v. Kircher*.[31]

(2) Consider whether certain existing probate family protections should be extended to NPTs.[32]

CONCLUSION

The Commission needs to decide how to proceed in this study. It could decide to continue with the focus that the study currently has (or return to working on a stand-alone liability principle). Or it could set those more general goals aside and work on narrower reforms, as TEXCOM recommends.

How would the Commission like to proceed?

Respectfully submitted,

Kristin Burford
Staff Counsel

30. Exhibit p. 8.
31. 189 Cal. App. 4th 1105, 117 Cal. Rptr. 3d 254 (2010), *rev. denied* 2011 Cal. LEXIS 1437.
32. Exhibit p. 9.

Memo To: California Law Revision Commission

From: The Executive Committee of the Trusts and Estates Section of the California Lawyers Association (TEXCOM).

RE: Non-Probate Transfer and Family Protection Study

Response to Request for Comment

The CLRC has requested comment from stakeholders on the following NPT reform approaches:

1) Develop a simple NPT liability principle, without implementing procedural rules.
2) Develop a comprehensive NPT liability framework based upon Section 102 of the Uniform Probate Act ("UPA").
3) Do not pursue a general reform on the issue of NPT liability.

Further comment is requested as to whether narrower issues of NPT be addressed in the study including but not limited to:

A) Should the law be reformed to address concerns regarding the decision in *Kircher v. Kircher* (2010) 189 Cal. App. 4th 1105.
B) Should existing probate family protections be extended to NPTs.

Summary of NPT and Related Issues.[1]

Generally, a NPT is any transfer of property that is owned or controlled by the decedent after the decedent's death without probate administration. NPT's include:

1) Transfers of property to beneficiaries under the terms of the decedent's revocable trust.
2) Transfers of the decedent's property according to a beneficiary designation made by the decedent (e.g., pay-on-death bank account or vehicle registered in transfer on death form).
3) Receipt of property to which a beneficiary is entitled by reason of the decedent's death (e.g., life insurance or survivors' benefits).
4) Transfers of property without probate administration under statutorily defined procedures (e.g., affidavit procedures for personal or real property of small value).
5) Transfers of property based on the joint character of ownership (e.g., joint tenancy or community property). (CLRC MEMO 2017-7)

The Sterling Report opines that the ad hoc development of NPT law has not adequately incorporated the public policies requiring payment of a decedent's just debts and protection of a

[1] It should be noted that much of the summary is derived from Sterling Report and Staff Memoranda. Some citations have been omitted since the citation is referenced in the Sterling Report and Staff Memoranda. Mr. Sterling and CLRC staff are to be commended for their work.

decedent's dependents. As discussed more fully herein, TEXCOM believes this overstates the problem. Further, creditors are in a position during decedent's lifetime to protect themselves and should bear any burden claimed to result from the current system.

The public policies requiring the payment of a decedent's debts and the protection of a decedent's dependents have traditionally been imposed through the probate process (CLRC Memo 2017-7, Page 4) The probate system establishes a policy based order of abatement to satisfy claims, and a hierarchy of priorities in case the decedent's estate is insolvent (CLRC Memo 2017-7, Page 5). The probate system provides for the decedent's dependents in the form of temporary possession of the family dwelling and exempt property, a probate homestead, a family allowance, and a small estate set-aside.

The Probate Code also provides an optional creditor claims procedure for a NPT via trusts and establishes the liability of trust property for a decedent's debts when the probate estate is inadequate (Prob. Code section 19000-19403). However, it is possible that a decedent could dispose of all property outside of probate, without use of a trust such as TOD deed, joint tenancy and other NPT vehicles. If these NPT vehicles are utilized, whether the individual non-probate transfers are liable for the decedent's debts or family protections may appear inconsistent with public policy or create the appearance of an inequitable result.

Certain types of NPTs are generally liable for a decedent's debts under California law. Such liable NPTs include statutory liability. The Probate Code provides several statutory methods for persons to claim a decedent's property without probate, typically limited to small estates or property of small value. These methods include:

1) Vehicle or Vessel Claimed with an Affidavit for Transfer Without Probate.
2) Small Estate Set-Aside.
3) Summary Disposition of Small Estates.
4) Affidavit Procedure for Collection or Transfer of Personal Property.
5) Court Order Determining Succession to Property.
6) Affidavit Procedure for Real Property of Small Value.
7) Passage of Property to Surviving Spouse without Administration.

The recipients of the forgoing property are liable for the decedent's debts, but liability is limited to the value of property received.

Additional NPTs are liable. In 2015, the Legislature enacted the Commission's recommendation on revocable transfer on death deeds (hereafter, "RTODD"). The RTODD law imposes liability on the beneficiary receiving property under an RTODD. The law limits the liability to the fair market value of the property and any income received from the property.

California's laws on community property specify that "each spouse's interest in community property is liable for the debts of either spouse." This liability survives the death of a spouse. The Sterling Report notes that "[t]ransfer of the decedent's community property interest by means of a nonprobate transfer does not appear to change these rules." It is not clear, however, whether these liability rules govern community property in joint tenancy form or community property with right of survivorship. These forms of ownership may instead be governed by the rule of nonliability applicable to joint tenancy property.

Property in a revocable trust is liable for a decedent's debts under California law, but only when the probate estate is inadequate. The Sterling Report states that the basic liability rule – the decedent's trust estate is liable only to the extent the probate estate is inadequate – embodies two significant public policies: (1) The trust estate is subject to the decedent's creditors – fraudulent intent is irrelevant. (2) The trust estate is only secondarily liable – it is a protected form of nonprobate transfer (Sterling Report 44-49). The Sterling Report indicates that the statutory trust law would benefit from clarifying how this liability can be enforced in practice (Sterling Report, 49-53).

California law also provides that a creditor of a decedent "may reach property over which the decedent held a general power of appointment if the decedent's estate is inadequate to cover claims of creditors and expenses of probate." However, if the estate is inadequate, the liability is allocated proportionally between this property and the other estate property. Once it is determined that the estate is inadequate, the property is liable 'to the same extent' as it would be if it were owned by the decedent (Sterling Report, page 32).

Certain types of NPT's are typically not liable for a decedent's debts. These include:

1) Joint Tenancy
2) Social Security
3) United States Savings Bonds

Other types of NPT's are unclear in establishing or precluding liability for a decedent's debts. Such nonprobate transfers include:

1) Multiple Party Accounts.
2) Transfer on Death (hereafter, "TOD") Security Registration
3) Public Retirement Benefits
4) Worker's Compensation Benefits
5) Life Insurance.
6) Private Retirement Benefits.
7) Payment to Beneficiary for Partnership Interest

The Sterling Report discussed a claim that the transfer was a fraud against creditors, under the Uniform Fraudulent Transfers Act, as the "classic approach for a creditor to reach property that passes outside the probate estate." (Sterling Report, Page 22-29). However, in 2015, California enacted the Uniform Voidable Transactions Act. The Uniform Voidable Transactions Act effectively deems three types of personal transactions as voidable: (1) Transfers made or obligations incurred with actual intent to hinder, delay, or defraud any creditor of the debtor. (2)

Transfers made or obligations incurred without receiving reasonably equivalent value if the debtor intended to incur, or believed or reasonably should have believed that the debtor would incur, debts beyond the debtor's ability to pay as they became due. (3) Transfers made or obligations incurred without receiving a reasonably equivalent value in exchange and the debtor was insolvent or became insolvent as a result of the transfer or obligation. Such transactions are only voidable as to creditors at the time of the transfer was made or obligation was incurred.

The application of these principles to NPT is not entirely clear. The Sterling Report suggests that clarification of the interrelationship between NPT liability and voidable transactions law would be beneficial. Probate Code section 9653 authorizes the personal representative to recover property transferred by voidable transaction where the probate estate is inadequate to pay the creditors. A creditor also has Probate Code section 850 as an available remedy to pursue in a case of voidable transactions.

TEXCOM suggests that the forgoing provides the creditor with a mechanism to obtain a remedy to pursue NPT assets in cases of alleged abuse of the current creditor claim system by a decedent. The result is that the claimed inequity of inability to collect a just debt is reduced or eliminated.

Law in Other Jurisdictions

There are several examples of laws in other jurisdictions that impose liability on NPTs. The Sterling Report discusses four[2] such laws: (1) Federal Estate Tax (2) Missouri Statute (3) Washington Statute (4) Uniform Law

The Sterling Report analyzes Uniform Probate Act Section 102 in detail. Key provisions include the following:

1) Provides for the liability of a NPT for the decedent's debts and family protections, to the extent that the decedent's probate estate is insufficient.
2) The liability of an individual NPT is limited to the value of the property.
3) Establishes a default order of abatement for NPT- once the probate estate is exhausted, debts are first paid from the trust, then from other NPT property, absent other direction from the decedent.
4) Certain types of property are not covered by Section 102 including property over which the decedent held a general power of appointment; real property transferred by right of survivorship under joint tenancy; property in a joint ownership form that, prior to the death of the decedent, was owned by the decedent's co-tenant
5) Property that would be exempt from a creditor's claim under the state's enforcement of money judgments law.

[2] Since the CLRC is focused on UPA section 102, the other approaches are not discussed. The alternate approaches are summarized in the Sterling Report and Staff Memoranda.

The Sterling Report identifies several issues that need to be addressed concerning the issue of liability of NPT's for a decedent's debts. (Sterling Report, 71-78). These issues include:

1) Providing a definition of NPT.
2) Reevaluating the nonliability of joint tenancy property.
3) Determining the priority, if any, of NPTs (i.e., are such assets only liable to the extent that the probate estate is insolvent?).
4) Clarifying whether and how the general probate abatement scheme applies to NPTs.
5) Reconciling the exemptions from money judgments with the family protection provisions in the Probate Code.
6) Clarifying how exemptions work for property transferred by NPTs.
7) Assessing whether and how to prioritize among creditors who seek to hold NPTs liable for debts.
8) Developing a scheme for enforcement of liability against and collection of NPTs.

Family Protections

Certain family protections in the Probate Code are designed to limit the financial hardships and difficulties faced by the surviving spouse and dependent children temporarily, in the immediate aftermath of the decedent's death. For instance, the Probate Code provides for the surviving spouse and children to retain possession of certain property and receive an allowance during the course of probate administration. The probate code authorizes the probate court to set aside certain property for the surviving spouse and children. Depending on the character of the property, the set-aside property may be either permanently or temporarily relieved from liability for the decedent's debts.

If reform is pursued, TEXCOM suggests that family protections should be extended to NPTs.

Exclusions from any Liability Rule:

(1) Federal liability rules that preempt contrary state regulation.
(2) Medi-Cal estate recovery rules

Public Policy Argument in Support of Reform

As a general matter, absent some overriding policy issue, it is unclear why the decedent's property that is transferred by nonprobate means at death should not also be liable for a decedent's debts. The Sterling Report states, "[t]he policy, if any, that supports immunization of nonprobate property from a decedent's creditors and dependents is not obvious." More specifically, allowing a decedent to immunize certain property from creditor claims simply by using a different instrument to transfer the asset (e.g., a bank account passing to a beneficiary designated in a will versus a bank account passing to a beneficiary on a pay-on death designation) seems to favor form over substance. As a general matter, the law does not permit a person to transfer away assets to avoid those assets being available to satisfy creditors. To the extent that the decedent has prior obligations that have not been satisfied, the decedent's creditors seem to have a greater claim to the decedent's assets than an NPT beneficiary. (CLRC MEMO 2017-23, page 6)

CLRC Decisions on NPT to Date

The commission in the context of looking at implementing UPA section 102, has decided that the following should be subject to the liability rule: Personal property joint tenancies; multiparty accounts; TOD securities; property over which decedent holds power of appointment if power created by person other than decedent; and life insurance and death benefits to the extent decedent could have obtained funds prior to death.

The commission decided that the following should not be subject to the liability rule: Real property joint tenancies; retirement accounts subject to beneficiary designation.

At the September 2017 meeting, the commission voted to make several family protections applicable to NPTs.

Staff Concerns Related to Liability Principle

CLRC staff is concerned that enacting a simple liability principle, without implementing a framework, could leave a great deal of uncertainty in practice. Lack of guidance on allocation (who should pay whom how much in a situation with multiple creditors and beneficiaries) or procedures to enforce a creditor's claim. This could result in increased confusion and litigation, with inconsistent and potentially inequitable results. (Staff Memo 2018-6, pages 3).

TEXCOM agrees with this assessment.

CLRC staff is concerned that 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. (Staff Memo 2018-6, page 3).

TEXCOM agrees with this assessment.

CLRC staff is concerned that without rules allocating liability (e.g., rules establishing pro rata liability or a right of contribution or reimbursement from other beneficiaries), 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 NPT). This could lead to inequitable results, with the creditors seeking payment from beneficiaries who received high-value gifts or are most accessible. Some of these problems could be addressed by supplementing a liability principle with rules for instance, on allocation of liability, but adding such rules would shift the reform closer toward the comprehensive framework approach. (Staff Memo 2018-6, page 4).

TEXCOM agrees with the assessment and considers pro rata allocation practically unworkable.

Staff Concerns Related to 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 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. Although the choice 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. By shifting NPTs into a judicially-supervised administration process, like probate, this 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. (Staff Memo 2018-6, page 4).

TEXCOM agrees with the assessment.

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. (Staff Memo 2018-6, page 5).

TEXCOM agrees with the assessment.

TEXCOM Comments

The Current System Works.

The most common NPT is a trust for which the Probate Code provides established procedures for creditors to satisfy claims, although probate assets must first be exhausted. (Prob. Code 19000 et seq.). Since the CLRC has decided to exempt joint tenancy real property from the NPT Rule, the need for reform and impact of changes appears exaggerated since the assets subject to the rule for which there is no current NPT liability is greatly limited.

The current system for creditors to satisfy a claim from the assets of a decedent is analogous to the abatement rules set forth in Probate Code section 21402. Probate Code abatement provides that if there are creditors claims requiring payment from the estate of a decedent or a trust, the residuary gift bears the burden of paying those claims, then general gifts to nonrelatives, then general gifts to relatives, then specific gifts to nonrelatives, and finally specific gifts to the transferor's relatives. The existing law relative to NPT liability provides that the probate estate abates first, then the trust, then other NPT. TEXCOM considers this current system adequate.

<u>A Myriad of Administrative Problems and Burdens are Created</u>

NPT reform is likely to create numerous issues to consider and resolve including, but not limited to: allocation; claims filing time limits; notification procedures (do beneficiaries of NPT have duty to inform, do the institutions?); how does personal representative discover the existence of an NPT (ie. joint tenant account, life insurance) and what is their duty in this regard; mandatory (probate) or optional (trusts) procedures; and others.

The issue of allocation exemplifies the severity of the burdens. Since the perceived goal is equity, allocation is considered to be pro rata such as the Washington model. A pro rata liability rule would require implementation of procedures and rules in *all* solvent estates with *any* creditor's claims. Take the example of a typical estate with assets of $1,000,000 consisting of the following:

1. Furniture, furnishings and personal effects and cash in the decedent's probate estate worth $10,000 (1% of total estate value);
2. House and securities in the revocable trust worth $950,000 (95% of total estate value); and
3. Transfer on death bank account worth $40,000 (4% of total estate value).

Further assume that the only creditor claim is for medical bills totaling $2,000. If the law requires allocation among all recipients, then (1) the recipient of the probate estate must pay 1% of the debt ($20), (2) the trust beneficiaries must pay 95% of the debt ($1,9000), and (3) the recipient of the TOD bank account must pay 4% of the debt ($80). The allocation and collection will require an inordinate amount of effort relative to the claimed advantage of pro rata liability. Add additional small gifts of personal property (ie. typical personal property schedule) or a list of charity beneficiaries which is not uncommon in practice, and the burden is increased. Current law is adequate, as it would require payment of the medical bills from the $10,000 probate estate, almost without additional administrative burden or expense.

<u>General NPT liability reform defeats the purpose of probate avoidance vehicles</u>

TEXCOM agrees with the staff concerns that since the Uniform Act relies on the probate process as the procedural framework for enforcing NPT liability, it undermines the decedent's effort to avoid probate through the use of NPTs. By shifting NPTs into a judicially-supervised administration process, additional administrative burden and expense is created diminishing available resources to satisfy claims and make intended distributions. Additionally, as observed by the CLRC staff, this would presumably place a new burden on already-strained court resources.

TEXCOM RECOMMENDATIONS

1) TEXCOM recommends that the CLRC does not "Develop a simple NPT liability principle, without implementing procedural rules."
2) TEXCOM recommends that the CLRC does not "Develop a comprehensive NPT liability framework based upon Section 102 of the Uniform Probate Act ("UPA").
3) TEXCOM recommends that the CLRC does "not pursue a general reform on the issue of NPT liability".

   A) TEXCOM recommends that the CLRC consider reform to address concerns regarding the decision in *Kircher v. Kircher* (2010) 189 Cal. App. 4th 1105

   B) TEXCOM recommends that existing probate family protections be extended to NPTs if reform is pursued.

Submitted by David G. Knitter, April 2, 2018

TEXCOM, Chair CLRC Subcommittee