

What to Know After the *Spears* Case Ruling; No Not That One



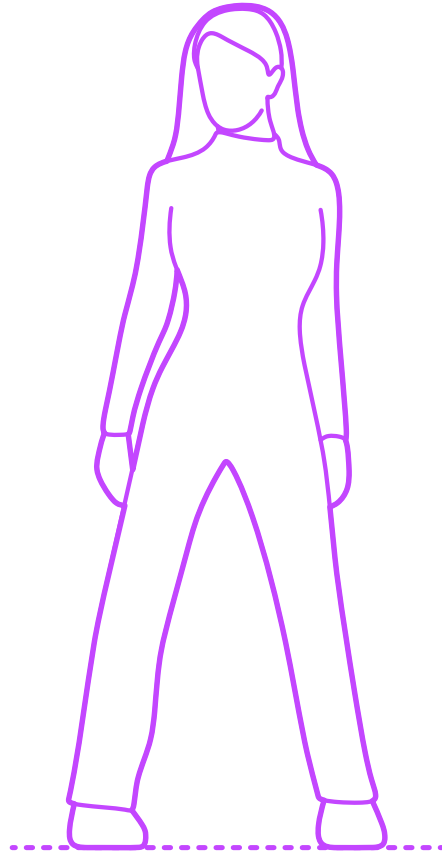
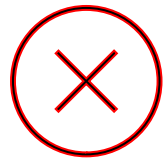
***Spears v. Spears* (2023) 97 Cal.App.5th 1294**

The California Court of Appeal's recent decision in *Spears v. Spears* created a statewide cascade of consternation and confusion about the ruling and its effect upon both trust law and judgment enforcement.

SFVBA
Probate & Estate Planning Section
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**This is NOT the topic
of discussion today!**



Today's topic is the law of probate and trusts interacting with debt collection and judgment enforcement principles.



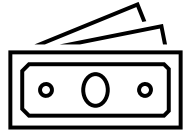


THE BASIC RULES

**Death Alone Does Not Render a Debt Uncollectable,
But it Does Make the Process More Complex**

- Dead people cannot be sued, and they do not pay off their debts.
- But not all hope is lost because their assets remain behind to be applied towards satisfaction of their debts.
- So, death alone does not render a debt uncollectable, but it does make the process more complex.





THE BASIC RULES

- ❖ Debt which has been reduced to a money judgment does NOT elude these complexities.
- ❖ Although California has a comprehensive statutory scheme for the enforcement of judgments enacted at the Enforcement of Judgments Law, Title 9 of the Code of Civil Procedure (see Code of Civ. Proc. §§680.010 et seq.), *a money judgment may NOT be enforced using those procedures after the death of the judgment debtor.*

NOTE: There are some exceptions to the restriction against using the provisions of the Enforcement of Judgments Law after death—which is beyond the scope of this presentation.

THE BASIC RULES

The California Court of Appeal's recent decision in *Spears v. Spears* created a statewide cascade of consternation and confusion about the ruling and its effect upon this field...



So, let's get into this...

THE BASIC RULES

- ❖ Instead, after death, a creditor's collection efforts, *whether or not the creditor has previously obtained a money judgment*, **are governed by the Probate Code.**

Code of Civ. Proc. §686.020

- ❖ Judgment creditors do **not** have priority over those without a judgment; all must submit claims if required by the Probate Code.

See Prob. Code §§9300 & 19300

NOTE: Non-money judgments may still be enforced, subject to several important restrictions. See Prob. Code §§9302 & 19302.

THE BASIC RULES

Property of a Decedent

- ❖ Assets of a decedent are *generally available* to satisfy the claims of a decedent's creditor.
- ❖ Property of a decedent passes upon death to the person devised in the decedent's last will or, in the absence of such a devise, to the decedent's heirs as prescribed in the laws governing intestate succession. *However, that property is subject to administration as well as the rights of beneficiaries, creditors, and other persons as provided by law.*

See Prob. Code §§7000-7001

THE BASIC RULES

Property of a Decedent (Trust Assets)

Assets held in trust present several challenges. However, they can be available to satisfy the claims of a decedent settlor's creditors *depending upon the existence of a power to **revoke***.



THE BASIC RULES

Property of a Decedent (Irrevocable Trust)

- ❖ **If the settlor did NOT retain the power to revoke** the trust either in whole or in part (i.e., property over which the settlor did not had power of revocation at the time of death), *the trust assets are **generally not** subject to the claims of a deceased settlor's creditors.*
- ❖ Instead, creditors may seek to exercise any rights available under the Enforcement of Judgments Law, Title 9 of the Code of Civil Procedure (see Code of Civ. Proc. §§680.010 et seq.), the law of fraudulent transfers, and other applicable laws to under the transfer and seek the return of the property contributed to an irrevocable trust, or, alternatively, its value in money damages and other permissible relief.

THE BASIC RULES



Property of a Decedent (*Revocable Trust*)

- ❖ Property over which the settlor had power of revocation at the time of death is **subject to creditors' claims “to the extent that the deceased settlor’s probate estate is *inadequate* to satisfy those claims and expenses.”** See Prob. Code §§19000 et seq. and 19001(a).

More on this later...

- ❖ Distinguished from irrevocable trusts: although assets in a revocable trust are transferred without probate to a trustee and therefore are *not* in the deceased settlor's name as of decedent’s death, the trust estate is subject to the settlor’s creditors without any need for showing fraudulent intent or other means to undo the non-probate transfer.



THE BASIC RULES

The ONE (1) YEAR Rule (Code of Civ. Proc. §366.2)

In addition to needing to know what assets are in dispute, we also need to contemplate the statute of limitations. Virtually any action or claim based upon the liability of a decedent must be made by a creditor within one (1) calendar year of death.

CODE OF CIV. PROC. §366.2

(a) If a person against whom an action may be brought **on a liability of the person**, whether arising in contract, tort, or otherwise, and whether accrued or not accrued, dies before the expiration of the applicable limitations period, and the cause of action survives, **an action may be commenced *within one year after the date of death***, and the limitations period that would have been applicable does not apply.

THE BASIC RULES

(con't) **CODE OF CIV. PROC. §366.2**

(b) The limitations period provided in this section for commencement of an action **shall not be tolled or extended for any reason except** as provided in any of the following, where applicable:

(1) Sections 12, 12a, and 12b of this code. [**HOLIDAYS**]

(2) Part 4 (commencing with Section 9000) of Division 7 of the Probate Code (creditor claims in administration of estates of decedents). [**CREDITOR CLAIM FILED IN A *PROBATE DECEDENT'S ESTATE PROCEEDING***]

(3) Part 8 (commencing with Section 19000) of Division 9 of the Probate Code (payment of claims, debts, and expenses from revocable trust of deceased settlor). [**CREDITOR CLAIM FILED IN THE *OPTIONAL TRUST CLAIMS NOTIFICATION PROCEDURE***]

(4) Former Part 3 (commencing with Section 21300) of Division 11 of the Probate Code (no contest clauses), as that part read prior to its repeal by Chapter 174 of the Statutes of 2008.



THE BASIC RULES

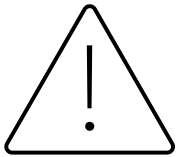
OFFICIAL COMMENTS to Code of Civ. Proc. §366.2:

This section applies a 1 year statute of limitations on all actions against a decedent on which the statute of limitations otherwise applicable has not run at the time of death. This 1 year limitations period applies regardless of whether the statute otherwise applicable would have expired before or after the 1 year period.

....

This section is concerned only with the time within which an action on a liability of the decedent may be brought, not with the proper parties in such a case. See Code of Civ. Proc. §377.40 (assertion of cause of action against decedent). **The 1 year limitation of Section 366.2 applies in any action on a liability of the decedent, whether against a personal representative** under Probate Code §§9350 9354 or against another person, such as a **distributee** under Probate Code §9392, a **person who takes the decedent's property** and is liable for the decedent's debts under Probate Code §§13109 (affidavit procedure for collection or transfer of personal property), 13156 (court order determining succession to real property), 13204 (affidavit procedure for real property of small value), or 13554 (passage of property to surviving spouse without administration), **or a trustee.**

THE BASIC RULES



- So the one (1) year rule of Code of Civ. Proc. §366.2 applies to virtually any action or claim based upon the liability of a decedent, **regardless of *against whom* or *against what* that liability may be asserted.**
- But the one (1) year rule does **not** apply to claims that do **not** assert an action on liability of the decedent.

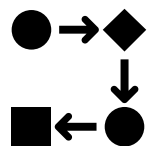
THE BASIC RULES

Depending upon the actual claim asserted, actions regarding title, ownership, or possession of items of property raised pursuant to the provisions of **Prob. Code §850** might not be subject to the one (1) year restriction of Code of Civ. Proc. §366.2 because such claims are not asserting an action on liability of the decedent. ***But not always!*** Consider the following:

- Prob. Code §850(a)(3)(A) – “Where the trustee is in possession of, or holds title to, real or personal property, and the property, or some interest, is claimed to belong to another”
- Prob. Code §850(a)(3)(C) – “Where the property of the trust is claimed to be subject to a creditor of the settlor of the trust”
- Prob. Code §856 – “If the court is satisfied that a conveyance, transfer, or other order should be made, the court shall make an order authorizing and directing the personal representative or other fiduciary, or the person having title to or possession of the property, to execute a conveyance or transfer to the person entitled thereto, or granting other appropriate relief.”

More on this later...

Creditor Claims



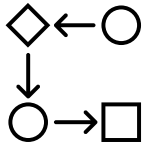
Probate - Decedent's Estates

- As provided in Prob. Code §§9000 et seq., a probate estate is opened and a personal representative is appointed to give notice to creditors and to provide a forum for the receipt of verified, substantiated creditor's claims.
- If a probate case is opened, then the creditor must file a claim. Prob. Code §§9000 et seq., 9002(a) & 9150.
- Assuming full compliance with the requirements for the giving of notice and publication, all claims not properly and timely filed before expiration of certain “**quick**” deadlines, and served on the personal representative, are barred. Prob. Code §9002(b).

Creditor Claims

- The personal representative may allow or reject the creditor's claim, in whole or in part. The creditor of a rejected claim has another “**quick**” deadline in which to initiate litigation to prove and liquidate any rejected claim. Prob. Code §9353.
- Thereafter, all allowed claims and judgments on rejected claims are payable in the course of the estate administration and are not enforceable against property in the trust estate pursuant to the Enforcement of Judgments Law. See Prob. Code §9300.
- If the estate is insufficient to satisfy all creditors (i.e., insolvency), the creditor priority provisions become applicable. See Prob. Code §11420.

Creditor Claims



Trust(s) – *Optional* Trust Claims Proceeding

- As provided in Prob. Code §§19000 et seq., a court proceeding is initiated by the trustee by the filing of a proposed notice to creditors. The trustee then provides notice to creditors of that proceeding, which provides a forum for the receipt of verified, substantiated creditor’s claims.
- It is ***optional*** to do so.
- But if a proceeding is elected and the notification given, then the creditor must file a claim. Prob. Code §§19000 et seq., 19004(a) & 9150.
- Assuming full compliance with the requirements for the giving of notice and publication, all claims not properly and timely filed before expiration of certain “**quick**” deadlines, and served on the trustee, are barred. Prob. Code §§19004(b).

Creditor Claims

- The trustee may allow or reject the creditor's claim, in whole or in part. The creditor of a rejected claim has another “**quick**” deadline in which to initiate litigation to prove and liquidate any rejected claim. Prob. Code §19255.
- Thereafter, all allowed claims and judgments on rejected claims are payable in the course of the trust administration and are not enforceable against property in the trust estate pursuant to the Enforcement of Judgments Law. See Prob. Code §19300.
- If the trust is insufficient to satisfy all creditors (i.e., insolvency), the same creditor priority provisions applicable in probate apply to the trust. Prob. Code §§19001(b) & 19027(b). See Prob. Code §11420



It's Getting Complex...

What if nothing is done when someone dies?????

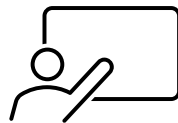
- The standard of practice is:
 - 1) The creditor seeks to *open* a probate proceeding *before* the one (1) year expires;
 - 2) Goal of the probate to is to have *someone appointed* as personal representative (for example, a special administrator, etc.) to receive creditor claims;
 - 3) The creditor then *files* a claim and serves the appointed personal representative; and
 - 4) If no action is taken to allow or reject the claim, then Creditor then deems the claim rejected and thereafter commences litigation against the personal representative either with or without waiting for completion of the decedent's probate proceeding.
- If there are assets held in a decedent's revocable trust, then the litigation would be commenced against the successor trustee of the trust too.

It's Getting Complex...

That's great for probate estate assets. But what about the decedent's assets held in a revocable trust? There is a statute that says...

PROB. CODE §19008

If there is **no proceeding to administer** the probate estate of the deceased settlor, **and** if the trustee **does not file a proposed notice to creditors** pursuant to Section 19003 and does not publish notice to creditors pursuant to Chapter 3 (commencing with Section 19040), **then the liability of the trust to any creditor of the deceased settlor shall be as otherwise provided by law.**



It's Getting Complex...

Inadequacy: Decedent's Liability and the Relationship Between Trust and Probate Assets

- ❖ As we saw earlier, California law declares that property over which the settlor had power of revocation at the time of death is subject to creditors' claims after death, **but only to the extent the settlor's estate is “inadequate.”** See Prob. Code §§19000 et seq. and 19001(a).
- ❖ The conventional wisdom is that the trust estate is *secondarily* liable; that is, only to the extent the settlor's estate is “inadequate” per Prob. Code §19001(a).

But how does a creditor establish “inadequate”?

It's Getting Complex...

Conventional wisdom BEFORE the *Spears v. Spears* case...

Genuine uncertainty existed when **no probate estate** is opened for a deceased settlor, and the trustee of the deceased settlor's revocable trust **does not** elect the optional trust claims notification procedure...what did one do?

- How did one establish “inadequacy”?
- Did a court have to decide this?
- Should a probate be opened to provide a forum to determine this?



It's Getting Complex...

In this author's opinion, prior to *Spears v. Spears*...

- It appeared that neither the existence of a probate proceeding nor its conclusion without distribution would be a formal prerequisite to asserting or establishing trust liability as per Prob. Code §§19001(a) and 19008.
- Why? Because Prob. Code §19008 states that if there is no proceeding to administer the estate and the trustee does not invoke the trust claim procedure, “then the liability of the trust to any creditor of the deceased settlor shall be as otherwise provided by law.”

For example, a creditor could file a lawsuit to collect the decedent's liabilities as against any successor in interest under Code of Civ. Proc. §§377 et seq., such as distributees of a trust as permitted by Prob. Code §19400, etc. Of course, the one (1) year rule of Code of Civ. Proc. §366.2 still applies. Prob. Code §§19400 & 19402. See Dobler v. Arluk Medical Center Industrial Group, Inc. (2001) 89 Cal.App.4th 530 (when there is no proceeding to administer a decedent's estate, creditors may pursue claims against the decedent by taking action against the decedent's distributees).

Spears v. Spears (2023)

The California Court of Appeal's recent decision in *Spears v. Spears* (2023) 97 Cal.App.5th 1294 created a statewide cascade of consternation and confusion about the ruling and its effect upon both trust law and judgment enforcement.

It is contended by many commentators that the *Spears v. Spears* opinion stands for this proposition:

Where no probate estate is opened for a deceased settlor, and the trustee of the deceased settlor's revocable trust does not elect the optional trust claims notification procedure, then a creditor may file suit against the trustee to recover on a settlor's debt from the trust estate without first having to proceed against the settlor's probate estate.

Let's just see...

Spears v. Spears (2023)

The Facts

- Brian's father James created a revocable trust in 2018 and funded it with separate property.
- James subsequently died in 2020 while he was still married to his spouse Therese.
- Brian alleged that the trustee, his stepmother Therese, owed him a total of \$40,000 based on two (2) alleged agreements arising from oral promises made by decedent James and surviving spouse/trustee Therese.
 - The first was an alleged breach of James' and Therese's oral promises to pay him a portion of the payments subsequently received from the State of California for the care of Therese's granddaughter (\$30,000).
 - The second was an alleged breach of James' and Therese's oral promises to pay him the balance due for their purchase from him of a modular home (\$10,000).
- Brian alleged that both debts were community property and should be included in the debts of his father James' separate property trust.

Spears v. Spears (2023)

Claims and Proceedings

- *What about claims? None...*
 - **No** probate proceeding was opened for James.
 - Moreover, Therese, as the successor trustee of James's separate property trust, **did not** elect to use the optional trust claims notification procedure.
- *Instead:*
 - Brian filed a petition **within one (1) year** of his father James' death with the trial court seeking to remove Therese as trustee of Jame's separate property revocable trust, compelling her to render an accounting, and to be added as a creditor of that trust.

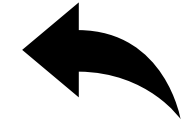
Spears v. Spears (2023)

Law and Motion

- The trial court sustained Therese's demurrer, with leave to amend.
- Brian then filed a document entitled "creditor's claim" in the same case, asserting the same two (2) alleged breaches of oral agreement previously alleged.
- Therese again objected by demurrer to Brian's creditor's claim document on the basis that he needed to file his claim against the decedent's estate, not the trust, and that his claims were barred by the statute of limitations. Brian responded with a mishmash of legal arguments, but did raise the issue of his theory of recovery being predicated on Prob. Code §850.
- The trial court dismissed the matter with prejudice after Brian declined to file an amended petition.

Spears v. Spears (2023)

Appeal



- The appellate court **reversed** the trial court's dismissal with prejudice.
- The filing of Brian's creditor's claim document constituted an amended pleading (effective retroactive to the date of the filing of the original pleading) as it reasserted his claim to be named as a creditor of the trust.
 - The appellate court found that one (1) of Brian's two (2) claims asserted in that creditor's claim document (*the balance due in connection with the sale of a modular home*) was barred by the applicable statute of limitations for breach of an oral agreement (2 years from date of breach).
 - However, the remaining claim (*the balance due for subsequent State of California payments*) was still viable in the face of a demurrer (accepting all factual allegations as true) and therefore the trial court's dismissal of the action without evidentiary determination of the date of breach was reversible error.

Spears v. Spears (2023)



IMPORTANT:

The appellate court noted that Brian asserted that **any probate estate** for his father James would be “**insolvent**” ***because all assets had been transferred to the separate property trust prior to death***, thereby establishing “inadequacy” pursuant to Prob. Code §19001(a) and permitting liability to be asserted against trust assets pursuant to Prob. Code §19008.

Based thereon, the appellate court reasoned that Brian **was not** required to bring an action under Prob. Code §850 against decedent James’ estate, and instead could bring his claim against Therese as trustee of James’ trust to recover from the trust estate **directly**, because no probate existed AND the trustee did not elect the optional trust claims notification procedure.

Spears v. Spears (2023)



But there are some issues and problems:

FIRST - some or all of Brain's remaining claim not barred by the statute of limitations could be considered an installment claim, arising in whole or in part ***after*** James' death. That is an obligation of Therese, individually or as trustee of James' trust—**not the assertion of liability of the decedent.**

If so, then there is no new law developed by the *Spears v. Spears* opinion since “inadequacy” is not a necessary element for a creditor of a trust to establish as a predicate of suing the trustee of that trust on an obligation owed by the trustee of that trust.

Perhaps the ruling is entirely *dicta*...?

Spears v. Spears (2023)

SECOND - there was **no** probate estate; **no** assets subject to administration in a decedent's estate proceeding. The appellate court considered Brian's assertion that the probate estate was "insolvent" to be sufficient to comply with the "inadequacy" requirement in Prob. Code §19001(a) to effectuate Prob. Code §19008's trust liability. **But...**

If a probate had been opened; ***or***

If Therese as trustee of decedent James' revocable separate property trust had elected to use the optional trust claims notification proceeding;

then Brian's claim would be barred for lack of compliance with the creditor claim requirements.

Spears v. Spears (2023)

THIRD - there is **only** a claim against Therese to consider, nothing else.

Here no creditor claim was filed to toll the one (1) year limitations period of Code of Civ. Proc. §366.2 and therefore Brian's action against Therese was his only viable pathway to collect on any alleged liabilities owed by his deceased father James.

That could be **risky and limiting** if Therese were to be bankrupt or otherwise judgment proof—Brian lost his ability as a matter of law to pursue **anyone else or anything else** because he did not open a probate and file a creditor claim to toll the one (1) year limitations period of Code of Civ. Proc. §366.2 and preserve his rights and options.

Spears v. Spears (2023)

UNKNOWN:

- *The appellate court spent time distinguishing prior case precedent (the Dobler case) because it assumed that it was impossible to get a judgment against an estate (that is, a personal representative) if no probate is opened for the creditor to do so. But creditors have standing to open their own probate case if no one else does...does this assumption make sense?*
- *The appellate court accepted the filing of a petition under Prob. Code §850 to be an action initiated prior to the expiration of the one (1) year limitation period of Code of Civ. Proc. §366.2(a), ignoring the explicit restriction of Code of Civ. Proc. §366.2(b) which restricts the tolling of the limitations period for “any reason” except for legal holidays and compliance with creditor claim requirements—the statutory language then suggesting that the mere filing of an action alone without a creditor claim may be insufficient.*
- *Should a claim asserted pursuant to Prob. Code §850(a)(3)(C) be considered to be an action on the “liability of the decedent” within the meaning of Code of Civ. Proc. §366.2—even though other subsections of Section 850 may concern merely title, possession, and ownership only?*

Spears v. Spears (2023)

In this author's opinion, the *Spears v. Spears* opinion stands for this revised and corrected proposition:

! ● Where no probate estate is opened for a deceased settlor and it can be demonstrated conclusively that any non-trust (probate) assets are "inadequate," and, further, the trustee of the deceased settlor's revocable trust does not elect the optional trust claims notification procedure, then a creditor may file suit an action pursuant to Prob. Code §850(a)(3)(A) and/or (C) against the trustee to recover on a settlor's debt from the trust estate without first having to proceed against the settlor's probate estate, but that it may not be the creditor's best practice to do so.



Best Practices

***Spears v. Spears* (2023) 97 Cal.App.5th 1294**

When faced with the *Spears v. Spears* situation, it remains a best practice for all creditors to continue ***to open a probate for the purposes of filing a creditor claim*** to ensure that there is a judicial proceeding to establish that the non-trust assets are “inadequate” and, further, to ensure compliance with creditor claim requirements and the tolling of the one (1) year limitations period of Code of Civ. Proc. §366.2 should liability need to be asserted against any other assets or responsible persons in addition to the assets held by the trustee of the decedent’s revocable trust.



What to Know After the *Spears* Case Ruling; No Not That One

***Spears v. Spears* (2023) 97 Cal.App.5th 1294**

THANK YOU!

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