



Dean, Mead & Bovay
901 NW 57th Street
Gainesville, FL 32605

352-331-9092
352-331-6895 Fax
www.deanmead.com

Orlando
Fort Pierce
Viera
Gainesville

JACK BOVAY
SHAREHOLDER
352-331-9092
jbovay@deanmead.com

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JUST SAY NO; WHAT HAPPENS WHEN THE TRUSTEE REFUSES TO COVER THE PR'S NOTICE OF INSUFFICIENCY?

By: Jack Bovay, Esq.

Introduction:

The use of a revocable trust to avoid probate is a standard estate planning technique. What happens when the decedent died with no probate estate, but did have assets held in a revocable trust and debts owed to creditors? We know that the PR can seek contribution of assets from the revocable trust to cover the claims of creditors. But, what is the process if the trustee refuses to cover the insufficiency?

Discussion:

Section 736.1014(1) Fla. Stat (2007), makes it clear that a creditor can not proceed directly against a revocable trust when seeking to establish the "individual liability" of the decedent^{1[1]}. See also Ziino v. Baker, No. 5:07CV217 OC10GRJ, 2007 WL 2433902, at *2 (M.D. Fla. Aug. 22, 2007). (Section 736.1014(2), on the other hand, does allow a cause of action against the trustee not based on individual liability of the settlor.)

^{1[1]} Section 736.1014(1) Fla. Stat. (2007), provides "After the death of a settlor, no creditor of the settlor may bring, maintain, or continue any direct action against a trust described in s. 733.707(3), the trustee of the trust, or any beneficiary of the trust that is dependent on the individual liability of the settlor. Such claims and causes of action against the settlor shall be presented and enforced against the settlor's estate as provided in part VII of chapter 733, and the personal representative of the settlor's estate may obtain payment from the trustee of a trust described in s. 733.707(3) as provided in ss. 733.607(2), 733.707(3), and 736.05053."

Because of the possible damage this prohibition could cause to creditors of a decedent, the Florida Legislature has provided that the creditor is to bring a claim in the probate court. If successful, and if the assets of the probate estate are insufficient to cover the claim, then the estate can recover from the trust^{2[2]}.

What happens if the Trustee of the decedent's revocable trust refuses or declines or claims it is not able to cover the insufficiency? For example, perhaps the only asset of the revocable trust is a limited partnership interest and the partnership agreement requires the consent of all the partners before the interest can be transferred and the trustee claims she is unable to obtain such consent.

Assume the PR has not objected to the claim of the creditor, the PR has provided the notice of insufficiency to the trustee, and the trustee says..." I understand, but I simply do not have authority to transfer the limited partnership units to the PR."

The Florida Statutes do not address the issue. There are four Florida DCA cases somewhat on point. This article explores existing law and proposes a legislative fix.

It would seem that the PR could sue the Trustee to force the payment. But, the PR has no assets with which to fund the litigation. Some might suggest that the creditor ask the probate court to appoint an Administrator Ad Litem to pursue the trustee. But, again, how will such litigation be funded? Wouldn't a better solution be for the creditor to sue the Trustee directly? If the PR has not objected to the claim, isn't that enough to then support the creditor's cause of action against the Trustee? And, at that point, isn't the cause of action simply a collection action, and out of 736.1014(1) because it is no longer contingent on establishing the individual liability of the decedent?

The Fourth DCA explored the intersection of a decedent's individual liability and a revocable trust in Tobin v Damian, 723 So. 2d 396, 397 (Fla. 4th DCA 1999). The court held that the then existing version of 733.707(3), Florida Statutes, did not in and of itself create a cause of action. Id. That version of the statute used the term "enforceable claim." (The current version of the statute uses the term "obligation"). Id. The court held that an "enforceable claim" is a timely filed claim against the estate where no objection has been made by the personal representative or a timely filed claim against the estate where a timely objection has been made and a subsequent judgment has been entered in favor of the claimant or stipulation for payment has been reached. Id. The court held that the appellant did "not yet have an enforceable claim against the Trust." Implicit in the phrase "not yet" is that the appellant could have proceeded directly against the trustee if it had held an "enforceable claim." What form does such an enforceable claim or obligation take? What did the Tobin court mean by

^{2[2]} Section 733.607(2) Fla. Stat. (2010), provides "If, after providing for statutory entitlements and all devises other than residuary devises, the assets of the decedent's estate are insufficient to pay the expenses of the administration and obligations of the decedent's estate, the personal representative is entitled to payment from the trustee of a trust described in s. 733.707(3), in the amount the personal representative certifies in writing to be required to satisfy the insufficiency, subject to the exclusions and preferences under s. 736.05053. The provisions of s. 733.805 shall apply in determining the amount of any payment required by this section." Section 733.707(3) Fla. Stat. (2010), provides "Any portion of a trust with respect to which a decedent who is the grantor has at the decedent's death a right of revocation, as defined in paragraph (e), either alone or in conjunction with any other person, is liable for the expenses of the administration and obligations of the decedent's estate to the extent the decedent's estate is insufficient to pay them as provided in ss. 733.607(2) and 736.05053."

"judgment" or "stipulation for payment"? The author's position is that if a PR has not objected to the claim, then it should be enforceable directly by the creditor and that the Florida Statutes should be amended to make that clear.

In Read, the creditor attempted to proceed directly against a revocable trust on the grounds that no probate estate had been opened. Estate of Read v. A.D.K. Properties, 766 So. 2d 393, 394 (Fla. 2d DCA 2000). The Second DCA cited Tobin for support that an enforceable claim must be established against the estate and reminded the creditor that it could open a probate estate itself. 766 So. 2d at 394 (citing Tobin v Damian, 723 So. 2d at 397).

In Shuck and Becklund, the Second DCA reinforced the concept that a creditor must first have an enforceable claim before proceeding against a revocable trust. Becklund v. Fleming, 869 So. 2d 1, 4 (Fla. 2d DCA 2003); Shuck v. Bank of America, N.A., 862 So. 2d 20, 22-23 (Fla. 2d DCA 2003).

Those two cases were decided in the Fall of 2003. In a footnote in each case, the Second DCA raised doubts about whether a creditor can proceed directly against the Trustee, even with an enforceable claim, because of then applicable 737.3061 prohibition (now 736.1014) against litigation based on "individual liability" of the settlor. The court did not express an opinion, as the issue was not before the court in either case. The author thinks the footnotes miss the point...if the PR has not objected to the claim, the creditor by definition should have an enforceable claim and the cause of action is no longer dependent on "individual liability"; it is now just a collection matter and the creditor is allowed to proceed against the Trustee under 736.1014(2).

Conclusion:

The author suggests that a legislative fix would be quite simple. Section 733.707(3) could be amended to make it clear that (i) a claim that is not objected to becomes an "obligation" as that term is used in that section and (ii) either the PR (insolvent and thus, unlikely) or the creditor (who has the economic motivation) then has a collection cause of action against the trustee under the "obligation," as opposed to an action based on individual liability. This will eliminate confusion and even litigation (as the author has experienced) over who is the correct party to sue the Trustee.

About the Author:



Mr. Bovay is the Managing Shareholder of the Gainesville office. He is Board Certified in both Tax Law and Wills, Trusts and Estates Law. His practice involves estate planning and asset protection for high net worth individuals and families, business succession planning and fiduciary litigation. Mr. Bovay holds an LL.M. in Taxation and is also a Florida licensed CPA. He may be reached at jbovay@deanmead.com.