

OPTIONS FOR CREDITORS IN INDEPENDENT ADMINISTRATIONS

Most articles written about “probate” and “creditors” are designed to advise the Executor.¹ The purpose of this article takes a different approach in an attempt to guide a creditor who is faced with the death of its debtor.

The claims process is a difficult and confusing part of probate practice. Part of the minefield for a creditor is a result of how the Estates Code² is written and organized.

There is a very detailed claims process for dependent administrations, but many of those statutes do not apply to an Executor in an independent administration. Therefore, a creditor dealing with an Independent Executor must follow a different process than if the administration were dependent.

Most Code subheadings are generic and appear to cover claims in both independent and dependent administrations. There are few sections which apply specifically to independent administrations. In general, Subtitle I of the Code³ deals with independent administration. Chapter 403 of Subtitle I deals with exemptions, allowances and claims. However, the Code also specifically states that, except as otherwise provided, the procedural provisions governing creditor claims in supervised administrations do not apply to independent administrations.⁴

A. Defining “Claims”

“Claims” are defined to include “(1) liabilities of a decedent that survive the decedent’s death, including taxes, regardless of whether the liabilities arise in contract or tort or otherwise; (2) funeral expenses; (3) the expense of a tombstone; (4) expenses of administration; (5) estate and inheritance taxes; and (6) debts due such estates.”⁵

As this definition shows, a claim is a debt that the decedent owed before death or which accrued after death. Both types of debts are handled the same way.

Every part of the definition of “claims” describes a claim for money. The extension “for money” is added to the term “claim” to make a single phrase in numerous statutes.⁶ There is no guidance in the Code if the “claim” is not one that involves money.

B. Initiating a Claim

How a claim must be pursued depends on whether the claim is liquidated or unliquidated, secured or unsecured, or for money or something else. Even if a creditor is in the midst of a collection action, or has perhaps obtained a judgment prior to the death of the decedent, the creditor must “start over” pursuing the claim after the Decedent dies.⁷

Following the death of a debtor, collection efforts cannot commence until a personal representative is appointed for the estate. The initial focus of the creditor should be to monitor the

filings in courts which handle probate matters in the county of death. If the decedent's family does not start the probate proceeding in a timely fashion, the creditor can also start the process.

An application to probate a Will, or to appoint an administrator when there is no Will, may be filed by certain persons, including an "interested person."⁸ A creditor is an "interested person."⁹

If the family fails or refuses to commence a probate action in a timely manner, a creditor can be the applicant in a request to create a temporary administration. The applicable statute dealing with temporary administrations uses the term "person"¹⁰ when stating who can commence such a proceeding. The term "person" is defined differently than the term "interested person."¹¹ However, the Supreme Court has made it clear that a creditor can seek a temporary administration in order to have a representative appointed to accept service of process.¹²

Once the administrator¹³ is appointed, the creditor can start efforts to collect the debt.

C. Sending Notices after Appointment of Executor

Once an Executor is appointed, two notices are required to be sent, and a third notice MAY be sent. The steps the creditor must take depend on which, if any, of the notices have been published/sent/received.

1. A general notice to creditors must be published within one month of the issuance of letters testamentary. The notice must be in a newspaper "of general circulation in the county in which the letters were issued."¹⁴

2. If there were secured debts at the date of death, within two months after receiving letters, the Executor must send notice by certified or registered mail, return-receipt requested, to each secured creditor.¹⁵

3. If there are unsecured creditors, the Executor may send a separate notice to them ("permissive notice").¹⁶

D. Filing the Claim and/or Suit

With the exception of those receiving permissive notice, a creditor dealing with an independent administration is not required to file a claim. Instead, the creditor may simply file suit against the Executor, and such a suit will toll the statute of limitations.¹⁷ If a suit is filed, the Executor is allowed to ignore the suit until six months after Letters were granted.¹⁸

A claim to be filed by a creditor must meet certain requirements specified in the Code, exactly like the document that must be filed by a creditor in a dependent administration.¹⁹ A claim which does not comply is not a proper claim, does not toll any applicable statute of limitations, and requires no further action by the Executor.

If an unsecured creditor is responding to newspaper notice, a claim is not required to be filed, and suit can be filed against the Executor or the heirs/beneficiaries if the estate has already been distributed.²⁰ Since there is some uncertainty as to what limitations periods may

apply after the death of a debtor,²¹ the only safe harbor for a creditor is to file suit and thus eliminate any concern about limitations.²²

E. Selecting Lien Classification Preference

Secured creditors must be careful to notify the administrator of any preference regarding the classification of their lien. There are two choices: “preferred debt and lien” and “matured secured claim.”²³ A secured creditor who elects “matured secured” continues to have its lien, but the creditor’s rights are subordinated to payment from the property to creditors with higher priority.²⁴

The secured creditor who elects “preferred debt and lien” will ultimately receive the collateral to which the lien is attached to either sell or retain, but the creditor cannot seek any additional recovery of cash or other property from the estate if the sale of the collateral yields less than the amount owed on the debt.²⁵

The default classification is “preferred debt and lien.” Within the later of 6 months from the date on which letters were issued or 4 months after receiving written notice from the Executor, the creditor must notify the administrator if the claim is to be classified as a “matured secured” claim.²⁶

If the collateral is real estate, and if the creditor elects “matured secured” claim, the creditor must both file a claim and record a notice of the creditor’s claim and of the “matured secured” election in the deed records of the county where the land is located.²⁷ If the secured creditor fails to get a “matured secured” election to the administrator within the required time, or if the secured creditor fails to make all of the proper filings and recordings, the claim will default to “preferred debt and lien.”²⁸

While the Code provides clear guidance as to what must be included in a claim,²⁹ there is no guidance as to what must be recorded in the deed records by a creditor with a security interest in real estate which is electing “matured secured” status.³⁰

F. Delivering the Notice to the Executor

As stated above, an Executor is required to send notices to secured creditors³¹ and may send notices to unsecured creditors.³² After the receipt of such notices, the creditor must send a notice back to the Executor. The creditor must be extremely careful to deliver its notice in one of the three ways allowed by the Code.³³ If the creditor fails to strictly comply, the implication is that the notice is invalid and the claim is no longer a debt against the estate.³⁴

G. Responding to Creditor Claims

Because an Executor acts without court supervision, the Creditor who files a valid claim can expect no response at all. While the Executor must classify all claims,³⁵ the Executor is not required to communicate the decision to the Creditor.

The purpose of the classification task is to make certain that the administrator pays claims in the order of priority if there are insufficient assets to pay all claims in full. If the estate's assets are insufficient to pay all of the classified debts, then the administrator pays the claims in the order of priority of the classification.³⁶

H. Pursuing Other Remedies

A secured creditor that has elected “preferred debt and lien” status can exercise any judicial or nonjudicial collection rights, including foreclosure and execution, but a nonjudicial foreclosure sale cannot be conducted until at least six months after Letters are granted.³⁷

On the other hand, a secured creditor that has selected “matured secured” status is not entitled to exercise any remedies in a manner that prevents the payment of the higher priority claims and allowances.³⁸ A “matured secured” creditor is also prohibited from exercising “any contractual collection rights, including the power to foreclose, without either the prior written approval” of the Executor or the court.³⁹

I. Conclusion

Representing creditors in probate actions can be perilous. Deciding whether and how to pursue a claim requires the creditor to follow closely the provisions of the Estates Code. Failure to do so could result in the loss of the claim and the underlying debt.

¹ “Executor” designates an Independent Executor throughout this article.

² References to the Estates Code are abbreviated to “Code” unless otherwise indicated.

³ Code §§401.001-405.012.

⁴ Code §403.058.

⁵ Code §22.005.

⁶ Code §§355.061, 355.008(1) and 403.052.

⁷ *Mackey v. Lucey Products Corp.*, 150 Tex 188, 190-91, 239 S.W.2d 607, 608 (1951) (a creditor who obtains a judgment prior to the decedent's death may not attempt to collect the judgment except through the probate court).

⁸ Code §§256.051, 301.051.

⁹ Code §22.018.

¹⁰ Code §452.002.

¹¹ Compare Code §§22.018 and 22.027.

¹² *Nelson v. Neal*, 787 S.W.2d 343 (Tex. 1990).

¹³ The term “independent executor” means the personal representative of an estate and includes an independent administrator. Code § 22.017.

¹⁴ Code §§308.051 and 403.051(a)(1).

¹⁵ Code §§308.053(a)-(c) and 403.051(a)(1).

¹⁶ Code §§308.054 and 403.051(a)(2).

¹⁷ Code §§403.059 and 355.008.

¹⁸ Code §403.059.

¹⁹ Code §§403.056, 403.052, 403.055 and 355.004.

²⁰ Code §§403.059 and 354.058.

²¹ Code §355.008; TEX. CIV. PRAC. & REM. CODE §16.062.

²² Code §403.057.

²³ Code §403.052.

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- ²⁴ Code §§403.053(a) and 403.055.
²⁵ *Wyatt v. Morse*, 102 S.W.2d 396 (Tex. 1937).
²⁶ Code §403.052.
²⁷ Code §403.052.
²⁸ Code §403.052.
²⁹ Code §355.004.
³⁰ Code §403.052.
³¹ Code §308.053.
³² Code §308.054.
³³ Code §403.056(a).
³⁴ Code §403.056(a) (1)-(3).
³⁵ Code §§403.051(a)(3) and 355.102.
³⁶ Code §403.051(a)(3).
³⁷ Code §403.054.
³⁸ Code §403.053(a)(1).
³⁹ Code §403.053(a)(2).