
THE UNCERTAIN DURATION OF THE POST-MORTEM RIGHTS OF CREDITORS OF A REVOCABLE TRUST SETTLOR

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Enactment of the Maryland Trust Act¹ (the “MTA”) resolves a number of long-standing questions about creditors’ rights to reach the property of self-settled trusts during the life and after the death of the settlor². As of January 1, 2015, new section 14.5-508 (a) expressly provides that

The following rules apply, whether or not the terms of a trust contain a spendthrift provision:

(1) During the lifetime of the settlor, the property of a revocable trust³ is subject to claims of the creditors of the settlor;

(2) With respect to an irrevocable trust, a creditor or assignee of the settlor may reach only the lesser of:

- (i) The claim of the creditor or assignee; and
- (ii) The maximum amount that can be distributed to or for the benefit of the settlor;

(3) If a trust has more than one settlor, the amount the creditor or assignee of a particular settlor may reach may not exceed the interest of the settlor in the portion of the trust attributable to the contribution of that settlor;

(4) After the death of a settlor, and subject to the right of the settlor to direct the source from which liabilities will be paid, the property of a trust that was revocable at the death of the settlor is subject to claims of the creditors of the settlor.

Maryland law has long favored the policy that “[w]henver property is subject to alienation by the owner, it is subject to his debts.”⁴ In particular, a debtor may not place his assets beyond the reach of his creditors by using a trust. Under Maryland common law, during a settlor’s life, his creditors can recover against the assets of both his revocable trust⁵ and his self-settled irrevocable trust, to the extent that the trustee can access the assets for the settlor’s benefit.⁶ Under the now-codified provisions of MTA section 14.5-508(a)(1) and (2), whether or not the trust contains a discretionary provision, a support provision, or a spendthrift provision with regard to distributions to the settlor, a creditor of the settlor may reach all of the property of a revocable trust and the maximum amount that an irrevocable trust trustee could distribute to the settlor-beneficiary. Even if the trustee of a revocable trust has discretion whether or not to distribute the entire income and principal to the settlor, the effect of this subsection is to place the settlor’s creditors in the same position as if the trust had not been created.

MTA section 14.5-508(a)(5) additionally recognizes that a revocable trust is usually employed as a will substitute. As

such, and as in the case of a decedent’s estate, the assets of a formerly revocable trust continue to be subject to the settlor’s lifetime debts after his death.⁷

This new legislation, however, fails to delineate the period following the settlor’s death in which creditors may exercise these rights to reach trust property. This unresolved question is not inconsequential. Absent a clear statement of when creditors can no longer reach trust property, prudent trustees of formerly revocable trusts must either (i) refrain from making post-mortem⁸ distributions until certain that there are no further forthcoming section 14.5-508(a)(5) creditors’ claims or (ii) make distributions that are encumbered with burdensome guarantees of repayment in the event a section 14.5-508(a)(5) creditor’s claim surfaces.

This article reviews the current Maryland law that addresses this situation⁹ and concludes with a plea that the Legislature consider this issue to provide needed certainty and relief.

How long does a formerly revocable trust remain subject to the claims of the settlor’s creditors?

Absent a statutory provision to the contrary¹⁰, section 5-101 of the Maryland Code’s Courts and Judicial Proceedings Article provides a general three-year statute of limitations for all civil claims. In practice, Maryland courts construe this three-year limitations provision strictly and frown upon implied and equitable exceptions.¹¹ Additionally, Maryland provides an extended 12-year statute of limitations for a number of specialty claims that might impact the liability of a decedent settlor: “(1) [p]romissory note[s] or other instrument[s] under seal; (2) [b]ond[s] except a public officer’s bond[s]; (3) [j]udgment[s]; (4) [r]ecognizance[s]; (5) [c]ontract[s] under seal; or (6) [a]ny other specialty.”¹² Moreover, at a debtor’s death, MD. CODE ANN. ESTATES AND TRUSTS ART. § 8-102(b) extends these section 5 101 and section 5-102 limitations periods for any claim that would terminate during the 6-month period after the decedent’s death until the end of that period. Note that section 8-102(b) extends these periods regardless of who the potential defendant parties might be.

Importantly, however, while section 8-102(b) extends the statute of limitations for any claim expiring during the 6 month post-death period, MD. CODE ANN. ESTATES

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AND TRUSTS ART. § 8-103(a) (“Section 8-103(a)”) bars most unrepresented claims against a decedent’s estate as follows:

(a) Except as otherwise expressly provided by statute with respect to claims of the United States and the State, all **claims against an estate of a decedent**, whether due or to become due, absolute or contingent, liquidated or unliquidated, founded on contract, tort, or other legal basis, are forever barred **against the estate, the personal representative, and the heirs and legatees** [emphasis supplied], unless presented within the earlier of the following dates:

- (1) 6 months after the date of the decedent’s death; or
- (2) 2 months after the personal representative mails or otherwise delivers to the creditor a copy of a notice in the form required by § 7-103 of this article or other written notice, notifying the creditor that his claim will be barred unless he presents the claim within 2 months from the mailing or other delivery of the notice.

Some practitioners argue that Section 8-103(a) applies to claims against formerly revocable trust property by the creditors of the deceased settlor. In this regard, however, note that the express language of Section 8-103(a) bars only untimely “claims against an estate of a decedent.” The Estates and Trusts Article does not include a specific definition for the word, “estate”, but MD. CODE ANN. ESTATES AND TRUSTS ART. § 1-301(a) provides that it is “[a]ll property of a decedent” that is “subject to the estates of decedents law.” MD. CODE ANN. ESTATES AND TRUSTS ART. § 1-101(r) further provides that, as used “[i]n the estates of decedents law, . . . ‘[p]roperty’ refers to (1) all real and personal property of a decedent and (2) any right or interest therein **which does not pass, at the time of the decedent’s death, to another person by the terms of the instrument under which it is held** [emphasis supplied], or by operation of law.” Property held in trust that passes by the terms of a trust instrument obviously falls outside this definition of what comprises the “property” to which the estates of decedents law applies.¹³ As such, “claims of the creditors of the settlor” against “the property of a trust that was revocable at the death of the settlor” covered by MTA section 14.5-508(a)(5) would seem to be very different from “claims against an estate of a decedent” under Section 8-103(a) because of these mutually exclusive types of property.

In addition, while explicitly barring claims against the estate, the personal representative, and the heirs and legatees, this Section 8-103(a) statutory exception fails to refer explicitly

to creditor claims against a decedent’s trustee or trust assets. By the express terms of Section 8-103(a), the only claims barred are those against the decedent’s estate, personal representative, and heirs and legatees. Because Maryland strictly construes its statute of limitations and Section 8-103(a) does not expressly include creditor claims against trustees or trust property in its reach, Section 8-103(a) likely does not bar claims by a settlor’s creditors against the trustee or trust assets. Thus, a lifetime creditor of a settlor under MTA section 14.5-508(a)(5) likely has up to three years (or up to twelve years if the creditor has a claim on a specialty) from the date his cause of action accrued to file a claim against the trust assets, regardless of when the settlor dies.

The history of Section 8-103(a) also lends credence to the applicability of the general statute of limitations to claims against formerly revocable trust property and trustees. Prior to 1969, strict construction of the statutory predecessors of Section 8-103(a) barred untimely suits only against a decedent’s executor/administrator and failed to prevent creditors from pursuing stale claims against the decedent’s heirs and legatees. The statutory bar was limited to the parties explicitly referenced in the statute.¹⁴ Thus, although a claim was extinguished as to the decedent’s estate and executor/administrator, it remained viable as to other interested persons. In the case of a formerly revocable trust, the trust and the trustee could be sued because they are not in the Section 8-103(a) list of barred defendants.

As a result, the post-mortem administration of formerly revocable trusts is likely to be extended and/or made much more complicated.

A Legislative Solution

It doesn’t make sense that the personal representative of an estate can make a final distribution of a decedent’s property after six months while his trustee counterpart must wait up to 12 years. Absent relief from this situation, every prudent trustee of a formerly revocable trust will be tempted to delay making significant distributions from the trust until he is certain there are no lurking potential creditors of the settlor. Alternatively, the prudent trustee may make distributions from the trust estate before the end of the limitations period only after first receiving enforceable indemnification for future creditors’ claims from all trust distributees. In this case, the trustee will insist that these indemnifications be on a joint and several basis to avoid situations where beneficiaries dissipate their benefits before the claims are received. An extremely prudent trustee may even require that such indemnification agreements be collateralized. In

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these situations, if distributions are made prior to the end of the applicable limitations period, beneficiaries will be saddled with uncertainty as to the possibility that they might be required to remit benefits back to the trustee for the payment of claims in potentially disproportionate amounts.

To avoid this result, the MSBA's Estate and Trust Law Section originally recommended to the Legislature that the MTA include a second clause of section 14.5-508(a)(5) that addressed this issue: "If a claim is or would be barred against the probate estate of the settlor under section 8-103 of this article, that claim is barred against the trustee and the property of the revocable trust." This recommendation was based on the recommended text of Section 505(a)(3) of the National Conference of Commissioners on Uniform State Laws' Uniform Trust Code (the "Uniform Trust Code"):

After the death of a settlor, and subject to the settlor's right to direct the source from which liabilities will be paid, the property of a trust that was revocable at the settlor's death is subject to claims of the settlor's creditors, costs of administration of the settlor's estate, the expenses of the settlor's funeral and disposal of remains, and [statutory allowances] to a surviving spouse and children to the extent the settlor's probate estate is inadequate to satisfy those claims, costs, expenses, and [allowances].

Given the procedure already present in Title 8 of the Maryland Code's Estates and Trusts Article and a desire to avoid duplication of this procedure, the Section Council felt it was better to use this Title 8 procedure for the MTA's nonclaim statute as to claims by creditors of the revocable trust settlor after his death. However, in its wisdom (or uncertainty as to how this would work), the Legislature elected to omit this recommended provision.

The authors suggest that the General Assembly should reexamine this issue.

Adoption of a nonclaim statute for a period less than the three- (or 12-) year general statute of limitations would be highly desirable for several reasons. First, we need certainty in an area that affects a large number of Maryland citizens. By omitting the Estates and Trust Law Section's original proposal, the Legislature left a gaping hole in the law that is extremely difficult to fill given the limited precedents currently available in Maryland.

Second, and more importantly, if revocable trusts are legitimately used as will substitutes to dispose of assets upon death¹⁵, having a period for claims against formerly revocable trust property that is substantially longer than the

period for claims against a probate estate is incongruous. Because the disposition of property by revocable trust is functionally equivalent to disposition by will, the rules affecting the timing of post-mortem dispositions ought to be the same¹⁶ or at least similar. In both situations, there should be a policy favoring the prompt administration of a decedent's assets in accordance with his wishes. However, like probate assets, we recognize that the assets disposable under revocable trusts should be subject to the settlor's lifetime debts for some reasonable period. The authors suggest that by enacting the current Section 8-103(a), the Legislature has already decided that this period should be no more than six months after a decedent's death. Adopting legislation to include language such as that originally proposed by the Section Council would provide a congruous result for both revocable trust and probate assets. This six-month window would provide a rational, finite period for settlement of a decedent settlor's affairs in an equitable manner, as compared to the current, uncertain state of the law where it is possible that some creditors may be able to assert claims against trust assets nearly 12 years after the decedent's death. The Section Council's proposal both allows creditors to assert their claim and requires that they do so in an expedient manner, ensuring that trust assets will transfer to beneficiaries unencumbered by still viable, but unknown claims.

Finally, Title 8 of the Estates and Trusts Article (of which Section 8-103(a) is a part) already provides a comprehensive, fair, and expeditious procedure for creditors to advance their claims. It merely requires that they be reasonably diligent in determining whether their debtor remains alive. If no estate is opened for the debtor (such as when the debtor wishes to settle his affairs by a revocable trust), section 8-104(c) already provides two mechanisms by which a creditor can perfect his claim within the required period: (1) by filing it with the register of wills in the county in which the decedent debtor was domiciled; or (2) by filing an action against the trustee of the formerly revocable trust. If the Legislature believes that creditors of a settlor should be given notice that the deceased settlor left a formerly revocable trust, it should not be difficult for a trustee to send such notice to the creditors when the trustee of the formerly revocable trust gives notice to qualified beneficiaries as required under MTA section 14.5-813(b)(2). To encourage the notice, the abbreviated period for presenting claims could be conditioned on the trustee's provision of this notice to creditors in a timely manner.

By failing to include the language originally suggested by

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the Section Council or as otherwise recommended in Section 505 of the Uniform Trust Code, Maryland is one of the few trust code states where potential claims by post-mortem creditors of revocable trust settlors will lead to extended and complicated administration after the decedent settlor's death. By following the modern trend and addressing this problem, Maryland would provide a concrete status for both creditors and beneficiaries of deceased revocable trust settlors that is fair and equitable to all parties involved.

Endnotes

¹ MD. CODE ANN. ESTATES AND TRUSTS ART. Title 14.5 was enacted by 2014 Laws of Maryland Chapter 585 signed by Gov. O'Malley on May 15, 2014.

² In this article, the term, "Settlor" has the same definition as used in MTA section 14.5-103(t) which defines " 'Settlor [to mean] a person, including a testator, that creates or contributes property to a trust.' " If more than one person "creates or contributes property to a trust . . . each such person is a settlor of the portion of the trust property attributable to the contribution of that person except to the extent another person has the power to revoke or withdraw that portion."

³ Per MTA section 14.5-103(s), " 'Revocable', as applied to a trust, means revocable by the settlor without the consent of the trustee or a person holding an adverse interest."

⁴ *Baker v. Keiser*, 23 A. 735 (Md. 1892).

⁵ *Brent v. State Cent. Collection Unit*, 311 Md. 626, 537 A.2d 227, 229 (Md. 1988) ("[I]t is contrary to sound public policy to permit a person to have the absolute and *uncontrolled* ownership of property for his own purposes, and to be able at the same time to keep it from his creditors.") (quoting *Ullman v. Cameron*, 186 N.Y. 339, 346, 78 N.E. 1074 (N.Y. 1906)); see, e.g., *In re Robbins*, 826 F.2d 293, 294 (4th Cir. 1987)(applying Maryland law) and RESTATEMENT (SECOND) OF TRUSTS § 156(1).

⁶ *Brent*, 537 A.2d at 229, n. 1 (citing RESTATEMENT (SECOND) ON TRUSTS § 156 and cmt. m (1959))

⁷ Note, however, that as long as creditors' rights are not impaired, the decedent settlor is free to shift liability from the probate estate to the revocable trust and to direct the source from which liabilities will be paid. See MTA § 14.5-508(a)(5).

⁸ As used in this article, "post-mortem" refers to the period following the death of the settlor of what, prior to his death, was a revocable trust.

⁹ This article presupposes that the revocable trust assets in question were not funded to the settlor's trust illegally or as a result of a fraudulent conveyance.

¹⁰ MD. CODE ANN., CTS. & JUD. PROC. § 5-101 (LexisNexis 2014).

¹¹ See, e.g., *Walko Corp. v. Burger Chef Systems, Inc.*, 281 Md. 207, 378 A.2d 1100 (Md. 1977); *McMahan v. Dorchester Fertilizer Co.*, 184 Md. 155, 40 A.2d 313 (Md. 1944); *Decker v. Fink*, 47 Md. App. 202, 422 A.2d 389 (Ct. Sp. App. 1980).

¹² MD. CODE ANN., CTS. & JUD. PROC. § 5-102(a) (LexisNexis 2014).

¹³ ALLAN J. GIBBER, GIBBER ON ESTATE ADMINISTRATION § 2.5(e) (5th ed. 2013 supp.).

¹⁴ See *Zollickoffer v. Seth*, 44 Md. 359 (1876) where the Court of Appeals observed that former Article 93, section 109 exonerated only the executor or administrator, not the estate, and allowed recovery against a legatee; cf. *Campbell v. Welsh*, 54 Md. App. 614, 460 A.2d 76 (Ct. Sp. App. 1982) (reciting the legislative history of Section 8-103(a)).

¹⁵ See UNIFORM TRUST CODE § 505(a)(3), cmt. (2005).

¹⁶ See *id.*, at § 112, cmt.

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