

Guideposts in Addressing Claims in a Potentially Insolvent Estate

By Frank T. Santoro

When addressing claims in a potentially insolvent estate, it is important to remember that the fiduciary owes a duty to beneficiaries and creditors alike, and that the successful administration of such an estate will require a thorough understanding of SCPA Article 18.

Marshaling the assets of the estate, paying administration expenses, paying the obligations of the decedent, and paying taxes are fundamental duties of a fiduciary. An executor is obligated to determine the nature and extent of the assets of the estate and to determine whether estate assets are sufficient to satisfy administration expenses and claims against the estate. Where the assets of the estate are illiquid, the fiduciary must carefully address the estate's cash requirements and liquidate assets in a prudent manner as required to pay debts, administration expenses, and taxes. Where an illiquid estate is insolvent, creditors may be keenly interested in determinations made by the fiduciary in liquidating assets.

Addressing whether to allow a claim or defend a claim requires a good faith approach that objectively weighs the validity of the claim. A fiduciary has a duty to contest all claims except valid, legal obligations, but shouldn't improperly resist a valid claim. An executor's duty in addressing claims has been described by the Nassau County Surrogate's Court as follows:

Among the duties of an executor is an important one of ascertaining what debts there are. It needs emphasis that a representative of an estate is the fiduciary of its creditors as well as legatees and distributees. As this court has on occasion remarked: A fiduciary must be just (in paying legitimate debts) before being generous (to beneficiaries). There is no room in fiduciary administration for the representative who seeks to wear down creditors to a point where they will take less than they are legally entitled to. In substance, a fiduciary is not obligated to defend against a valid claim nor is it his duty to compel a creditor to accept less than he is legally due. It is only those claims which are of doubtful legality that a representative has a duty to defend against. Finally there is a duty placed upon this court to control the conduct of fiduciaries, discourage vexatious liti-

gation and protect the estate from unnecessary costs and expenses attending the assertion and settlement of claims.¹

When analyzing a claim in good faith, all procedural and substantive defenses must be considered. In this regard, it is important to note that the presentation of a notice of claim stops a statute of limitations from running under SCPA § 1808.² The question of when the cause of action accrues depends on the nature of the underlying claim and when the underlying claim arose.

Where the act which gives rise to the cause of action against the estate happens after the death of the person who would be liable, the cause of action cannot accrue until the appointment of a legal representative of the estate. This is because a cause of action cannot exist unless there is a person in being against whom an action can be brought. Where a cause of action against a decedent already exists at the time of the decedent's death, CPLR § 210(b) tolls the statute of limitations the moment the decedent dies, and the statute resumes running automatically eighteen months thereafter. The effect of the statute is to add eighteen months to the applicable statute of limitations.³

Where a claim is allowed, SCPA § 1807 provides that any party adversely affected by the allowance of a claim may object to the allowance of the claim in a judicial accounting proceeding. If the court disallows the claim and the claim has already been paid, the court may order the claimant to refund the estate or surcharge the fiduciary.⁴ Where a claim is rejected, it will be adjudicated in a proceeding to determine the validity of a claim under SCPA § 1809, in an accounting proceeding, or in another court of competent jurisdiction.⁵

Pursuant to SCPA § 1813, a fiduciary may seek the court's advance approval of a proposed settlement of a claim on notice to all parties affected by the settlement. The inquiry on a fiduciary's application seeking court approval of a compromise is whether the proposed settlement is in the estate's best interest. Whether a proposed settlement is in the best interests of an estate involves a consideration of numerous factors, including "the relative merit of the parties' positions (as qualified by the knowledge that litigation is never risk-free) and the value of achieving peace for the combatants sooner rather than later."⁶

Critically, potentially insolvent estates that contain illiquid assets may be administered for a longer period of time than other, relatively uncomplicated estates.

Years can pass in the mire of exhaustive litigation of claims and in marketing and selling assets such as closely held businesses. The time horizon for winding up an estate is an important factor that must be weighed in the exercise of prudent administration,⁷ but that time horizon may not be predictable with a potentially insolvent or illiquid estate. It is difficult to predict just how swiftly a litigated matter will be adjudicated or resolved. Where an estate remains open for an extended period, determinations made in the estate administration will be scrutinized by all those interested. The frustration engendered by the passage of years from the death of a loved one (or unloved one) and payment of a legacy or claim can result in enhanced scrutiny.

In a potentially insolvent estate, the fiduciary cannot make the mistake of making distributions or paying allowed claims where there may be insufficient assets to pay all claims and potential claims—in the case of insolvency, the priority scheme of SCPA § 1811 controls. At the same time, the fiduciary must be mindful of potential interest accruing on allowed claims and legacies and should not unduly delay distributions and satisfaction of valid debts.⁸ The fiduciary must also be mindful of the statutory order of abatement of estate assets (or the order determined by the will) in satisfying debts and administration expenses.⁹ As always, the fiduciary must be careful to avoid self-dealing—Article 18 specifically addresses claims by fiduciaries against estates.¹⁰

Endnotes

1. *Estate of Hollinger*, 93 Misc. 2d 926, 403 N.Y.S.2d 857 (Sur. Ct., Nassau Co. 1978) (citations omitted); see also *Estate of Smith*, 5 Misc. 3d 1015A, 798 N.Y.S.2d 707 (Sur. Ct., Nassau Co. 2004).
2. SCPA § 1808(6); *Matter of Feinberg*, 18 N.Y.2d 499, 277 N.Y.S.2d 249 (1966).
3. See 2B Carmody-Wait 2d §§ 13:377, 13:378.
4. See *Matter of Witherill*, 8 Misc. 3d 1012(A), 2005 NY Slip Op. 51062(U) (Sur. Ct., Madison Co.).
5. The claim may be adjudicated in the estate accounting proceeding, in a proceeding pursuant to SCPA § 1809, or in another court of competent jurisdiction. However, if the claimant wishes to have the claim adjudicated in another forum, this must be done within 60 days of the rejection of the claim or the Surrogate's Court becomes the only venue where the matter can be adjudicated under SCPA § 1810.
6. See *Matter of Lazarus*, N.Y.L.J. March 19, 1998, p. 29, col. 3 (Sur. Ct., N.Y. Co.); *Matter of Rappaport*, 102 Misc. 2d 910, 424 N.Y.S.2d 675 (Sur. Ct., Nassau Co. 1980); *Estate of Shubert*, 110 Misc. 2d 635, 442 N.Y.S.2d 703 (Sur. Ct., N.Y. Co. 1981).
7. *Matter of Kopec*, 25 Misc. 3d 901, 885 N.Y.S.2d 401 (Sur. Ct., Monroe Co. 2009); see also *Estate of Buck*, 184 Misc. 2d 294 (Sur. Ct., Westchester Co. 1944) wherein the court stated that "a distinction must also be made between the duties of an executor or administrator and those of a trustee. An executor or administrator is under a duty to distribute the assets of the estate or their proceeds after the payment of debts, taxes and funeral and administration expenses. However, it is not entirely correct to say that during the period reasonably required for administration an executor, as such, has no authority to make investments."
8. SCPA § 2102(7); EPTL § 11-1.5 (d), (e); see *Estate of White*, N.Y.L.J., Dec. 28, 2004, p. 2, col. 3 (Sur. Ct., Richmond Co.); see also *Matter of Kasenetz*, 196 Misc. 2d 318, 765 N.Y.S.2d 216 (Sur. Ct., Nassau Co. 2003) addressing interest payable on elective share.
9. EPTL § 13-1.3.
10. SCPA § 1805 requires that a fiduciary with a claim against the estate seek approval to pay himself.

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