

1990 S.C. Op. Atty. Gen. 169 (S.C.A.G.), 1990 S.C. Op. Atty. Gen. No. 90-58, 1990 WL 482445

Office of the Attorney General

State of South Carolina

Opinion No. 90-58

October 2, 1990

***1** The Honorable Gus H. Pearlman
Judge of Probate for Charleston County
Post Office Box 537
Charleston, South Carolina 29402

Dear Judge Pearlman:

You have requested the opinion of this Office as to whether the items set forth in Section 62-3-805(a)(1) and (2) and (3) have paramount priority for payment over the value of the security held by a secured creditor. You have asked that we consider Sections 62-3-805 and 62-3-809 of the South Carolina Code of Laws in responding to your question.

Section 62-3-805 of the Code establishes a classification scheme in the event that assets of an estate are insufficient to pay all claims in full. That section provides:

(a) If the applicable assets of the estate are insufficient to pay all claims in full, the personal representative shall make payment in the following order:

(1) Costs and expenses of administration, including attorney's fees, and reasonable funeral expenses;

(2) reasonable and necessary medical and hospital expenses of the last illness of the decedent, including compensation of persons attending him;

(3) debts and taxes with preference under federal law;

(4) debts and taxes with preference under other laws of this State, in the order of their priority;

(5) all other claims.

(b) Except as is provided under subsection (a)(4) above, no preference shall be given in the payment of any claim over any other claim of the same class, and a claim due and payable shall not be entitled to a preference over claims not due.

Payment of allowed secured claims is provided for in Section 62-3-809:

Payment of a secured claim is upon the basis of the amount allowed if the creditor surrenders his security; otherwise, payment is upon the basis of one of the following:

(1) if the creditor exhausts his security before receiving payment, upon the amount of the claim allowed less the fair market value of the security as agreed by the parties, or as determined by the court; or

(2) if the creditor does not have the right to exhaust his security or has not done so, upon the amount of the claim allowed less the value of the security determined by converting it into money according to the terms of the agreement pursuant to which the security was delivered to the creditor, or by the creditor and personal representative by agreement, arbitration, compromise, or litigation.

Payment of allowed secured claims will be made in full if the creditor surrenders the security. If the creditor does not surrender the security, payment to the creditor would be based as provided in the statute.

Your question is, effectively, whether the interest of a secured creditor would be satisfied prior to the claims of the first three classes specified in Section 62-3-805. The resolution of your question seems to involve a determination of what assets are "applicable" for purposes of Section 62-3-805.

In *Matter of Estate of Ycalick*, 69 Ill.App.3d 353, 387 N.E.2d 399 (1979), the court stated that a personal representative of the decedent stands in no better a position than the decedent as to one holding a lien on the decedent's property. Secured collateral in the possession of a personal representative is not, and does not become, a part of the assets of the estate until the creditor's lien upon it is discharged. The latter principle is repeated in *Matter of Estate of Philp*, 114 Ill.App.3d 107, 448 N.E.2d 535 (1983), which stated further that proceeds from the sale of secured collateral do not become assets of the estate until the lien of the secured creditor is discharged. These principles are also found in 31 Am.Jur.2d Executors and Administrators § 492.

*2 It also appears that a secured creditor has other remedies to enforce his lien, instead of merely relying on filing his claim with the personal representative of the estate. For example, Section 62-3-803 (the non-claim statute) provides in part (c):

(c) Nothing in this section affects or prevents:

(1) any proceeding to enforce any mortgage, pledge, lien, or other security interest upon property of the estate;

In addition, Section 62-3-104, which requires creditors of decedents to assert their claims against the personal representative, provides:

This section has no application to a proceeding by a secured creditor of the decedent to enforce his right to his security except as to any deficiency judgment which might be sought therein.

Moreover, Section 62-3-804 provides as to encumbered assets:

If any assets of the estate are encumbered by mortgage, pledge, lien, or other security interest, the personal representative may pay the encumbrance or any part thereof, renew, or extend any obligation secured by the encumbrance or convey or transfer the assets to the creditor in satisfaction of his lien, in whole or in part, whether or not the holder of the encumbrance has presented a claim, if it appears to be for the best interest of the estate.... See also Sections 62-3-804, 62-3-812, and 62-3-806 as to other relevant provisions of the Code; see also 31 Am.Jur.2d Executors and Administrators §§ 617, 645, 679, 705, and 712, among others, as to the rights of secured creditors to enforce their liens.

The State of Minnesota has adopted the Uniform Probate Code. In *In Re Estate of Larson*, 359 N.W.2d 281 (Minn.App.1984), the court, construing Minnesota's probate law, stated:

A secured creditor is treated differently than other creditors under the probate code. Minn.Stat. § 524.3-803(c) (1982), which governs limitations on presentation of claims, provides:

Nothing in this section affects or prevents:

(1) any proceeding to enforce any mortgage, pledge, or other lien upon property of the estate * * *.

Similarly, Minn.Stat. § 524.3-104 (1982), providing generally for claims against the estate, states:

This section has no application to a proceeding by a secured creditor of the decedent to enforce his right to his security except as to any deficiency judgment which might be sought therein.

The probate code permits the personal representative authority to pay a secured claim in three ways. The personal representative may pay the claim in whole or in part; renew or extend the secured obligation; or convey or transfer assets to the creditor in satisfaction of the lien, whether or not the holder has filed a claim. Minn.Stat. § 524.3–814 (1982).

For the secured creditor who seeks payment, the code provides three options. Minn.Stat. § 524.3–809. First, payment is to be made upon the basis of the amount allowed if the creditor surrenders his security. Second, if the creditor exhausts its security before receiving payment upon the amount owing, it may receive its credit less the fair value of the security. Finally, if the creditor does not have the right to exhaust its security, or has not done so, it may receive the amount of the claim allowed less the value of the security. Minn.Stat. § 524.3–809 provides options for the secured creditor, but does not interfere with the process set out in Minn.Stat. § 524.3–806....

*3 *Id.*, 359 N.W.2d at 285–286. The court noted that a creditor holding a security interest could, at his option after death of the decedent, enforce the security for payment or file a claim as a general creditor of the estate.

Summarizing all of the foregoing, it appears that, in the question you have raised, the assets encumbered by a security interest (mortgage, for example) would not become assets of the estate until the security interest has been satisfied. The holder of the security interest has options, other than filing as a creditor of the estate, to satisfy the security interest. Until such satisfaction, the assets would remain outside those assets considered “applicable assets of the estate” under Section 62–3–805. Thus, the holder of a security interest with respect to the assets in question would, in effect, have priority over, or at least be accorded more preferential treatment than, those persons or entities who would be paid pursuant to the classification scheme established in Section 62–3–805(a)(1), (2), and (3).

With kindest regards, I am
Sincerely,

Patricia D. Petway
Assistant Attorney General

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