

MEMORANDUM

TO: Floyd M. Lewis, General Statutes Commission

FROM: James C. Hardin, III and Timothy W. Jones
NCBA Estate Planning and Fiduciary Law Section, Legislative Committee

DATE: May 17, 2015

RE: Uniform Probate Code Section 2-606 – Nonademption of Specific Devises

The Legislative Committee of the NCBA Estate Planning and Fiduciary Law Section formed a subcommittee to compare the current North Carolina law on nonademption of specific devises with the applicable section of the Uniform Probate Code. The general conclusion of the subcommittee is that although there is value to having laws that are consistent with the laws of other jurisdictions on the interpretation of wills, Section 2-606 of the UPC would add complexity to the administration of estates and would increase the likelihood of litigation.

Current North Carolina Law

North Carolina case law distinguishes between voluntary acts and involuntary acts in determining whether a specific devise in a will adeems. In general, the current North Carolina law can be summarized as follows:

1. If the property specifically devised in a will is not part of the testator's estate as a result of a **voluntary** act by the testator, the devise fails and the devisee receives nothing. The voluntary act is equivalent to a revocation of the devise.
2. If the property specifically devised in a will is not part of the testator's estate as a result of an **involuntary** act by the testator, the devisee is entitled to whatever replaced the property.

Common examples of involuntary acts include merger, theft, casualty and condemnation. See Huggard, J.P. *North Carolina Estate Settlement Practice Guide*, 2d ed. (2013), which includes an example that illustrates how North Carolina law applies to such involuntary acts:

Example: Frank's will made the following provisions:

- "... to St. Paul's Church, I give my 1,000 shares of XY stock."
- "... to the American Red Cross I leave my farm."
- "... to my sister I leave my yacht."

During the last year of Frank's life, he was very ill. Shortly before he died, Frank's XY Corporation was merged with ABC Corporation and all of Frank's XY stock was converted to ABC stock. About that same time, Frank's farm was taken by the state in a condemnation proceeding. The state sent a check for \$400,000 as condemnation proceeds to Frank. Finally, Frank's yacht was destroyed by fire. The insurance company sent a \$200,000 check to Frank for the yacht's loss . . . Under North Carolina law, the proceeds of the corporate merger, condemnation, or marine insurance policy that replace the original specific devisees would pass, by substitution, to the original specific devisees. [*Grant v. Banks*, 270 NC 473, 155 SE2d 87 (1967); *Reading v. Dixon*, 10 NC App 319, 178 SE2d 322 (1971)].

In addition, North Carolina law clarifies that the sale of property by an attorney-in-fact while the testator was incompetent is not ademption and the devisee is entitled to the remaining proceeds of the sale. *Creekmore v. Creekmore*, 126 NC App 252, 485 SE2d 68 (1997).

Uniform Probate Code Section 2-606

The UPC significantly increases the likelihood that a devisee will be entitled to receive something if the specifically-devised property is not part of the testator's estate. This increased likelihood is illustrated well in Example 1 and its Variation in the Comment to Section 2-606:

Example 1. G's will devised to X "my 1984 Ford." After she executed her will, she sold her 1984 Ford and bought a 1988 Buick; later, she sold the 1988 Buick and bought a 1993 Chrysler. She still owned the 1993 Chrysler when she died. Under subsection (a)(5), X takes the 1993 Chrysler.

Variation. If G had sold her 1984 Ford (or any of the replacement cars) and used the proceeds to buy shares in a mutual fund, which she owned at death, subsection (a)(5) does not give X the shares of the mutual fund. If G owned an automobile at death as a replacement for her 1984 Ford, however, X would be entitled to that automobile, even though it was bought with funds other than the proceeds of the sale of the 1984 Ford.

Current South Carolina Law

When South Carolina adopted the Uniform Probate Code ("UPC") in 1986, its General Assembly chose to omit sections (a)(5) and (a)(6). At the time, subsection (a)(6) assumed that the testator did not intend an ademption of the devise. After five of the first seven states to adopt the UPC omitted subsection (a)(6), the UPC Committee of the National Conference of Commissioners on Uniform State Laws ("NCCUSL") amended (a)(6) to switch the burden to the devisee to establish that an ademption was not intended. However, when the South Carolina General

Assembly amended S.C. Code Ann. Section 62-2-206 in 2013 in order to add provisions regarding an agent acting under a durable power of attorney, it again declined to adopt subsections (a)(5) or to even adopt the amended (a)(6).

South Carolina's partial adoption could lead to several undesirable outcomes. One troubling aspect of South Carolina's approach to ademption is how it treats condemnation awards under (a)(2), insurance proceeds under (a)(3), and sales proceeds under (a)(1). In each case, the devisee will receive only such proceeds that remain unpaid at the testator's death. This differs substantially from North Carolina common law, as described above, which differentiates between voluntary vs. involuntary transfers rather than whether the testator collected the proceeds prior to death.

For example, for property that is condemned, subsection (a)(2) would provide the devisee with the amount of the award that remains unpaid, but without subsection (a)(5), the devisee would arguably not receive the amount of the award that was paid to the testator before death and which was used to acquire replacement property.

In addition, the amount that the devisee would be entitled to could be dramatically different depending on whether the testator was incapacitated at the time of the conversion and protected by a conservator or if the award was paid to an agent acting within the authority of a durable power of attorney for an incapacitated principal. In such cases, pursuant to subsection (b), the specific devisee would have the right to a general pecuniary devise equal to the condemnation award, regardless of whether it is paid before or after the testator's death. By comparison, if the testator were not incapacitated, the devisee would only receive the amount of the award that remained unpaid at the testator's death.

Presumably, the additional benefit conferred by subsection (b) was based on the traditional principle that only a competent testator may change a will. If the testator was not incapacitated, and if the testator still desired the received awards to be distributed to the devisee, South Carolina law presumes that the testator would have either clearly specified the testator's intent in the language creating the specific bequest or would have later amended the testator's will to make such a provision with regard to the proceeds of the adeemed assets.

As a catch-all provision, subsection (a)(6) provides a devisee an opportunity to establish that ademption would be inconsistent with the testator's manifested plan of distribution, or that at the time the will was made, the testator did not intend ademption of the devise. Without subsection (a)(6), a devisee would have no ability, for example, to establish that the condemnation award amounts paid to the testator before his death were intended to be distributed to him. However, of course, this subsection would open the doors to litigation to determine the testator's intent, which South Carolina common law has decidedly veered away from.

The Comment to UPC Section 2-206 states that the majority common law rule of ademption by extinction followed the "identity" theory, where courts do not inquire into the testator's intent. The subsections (a)(5) and (a)(6) are meant to adopt the "intent" theory. Some view the intent theory as better because of the sometimes harsh results produced by the identity theory.

If the “intent” theory is implemented, the Personal Representative would be tasked with the responsibility of determining what might be considered “replacement property”. Under subsection (a)(5), the devisee would be entitled to any real property or tangible personal property owned by the testator at death which the testator acquired as a replacement for the specifically devised property. In practicality, commonly devised assets, which are frequently sold and replaced during lifetime, are arguably often relatively easy to identify. Such commonly devised assets may include automobiles, boats, and personal residences, which are often owned by the testator one-at-a-time. The identity of their replacement may be quite clear to the Personal Representative.

The general rule pertaining to ademption in South Carolina is, “[i]f the identical thing bequeathed is not in existence, or has been disposed of so that it does not form a part of the testator's estate, at the time of his death, the legacy is extinguished or adeemed, and the legatee's rights are gone.” *Gist v. Craig*, 142 S.C. 407, 451 (S.C. 1927). South Carolina has held that ademption “operates as a rule of law to void specific legacies, without regard to the subjective intent of the testator.” *Taylor v. Goddard*, 265 S.C. 327 (S.C. 1975). This is an example where South Carolina relies upon the “identity” theory, where courts do not inquire into the testator’s intent. South Carolina’s common law may have aided the General Assembly in its decision to omit subsections (a)(5) and (a)(6) from the South Carolina Uniform Probate Code.

Increased Complexity and Litigation

Under Example 1 or its Variation, the Executor would need to determine the facts surrounding the transactions detailed in order to determine what, if anything, the devisee is entitled to receive. Records of the transactions are not likely to have been kept for gifts of personal property, and the Executor may have no reliable way to determine what should be considered to be “replacement property” for the transferred property. If it is instead determined that subsection (a)(6) would apply, then the Executor would be obligated to determine the value of items that are no longer part of the estate and are no longer available to the Executor. The Executor may have no reliable basis for determining value.

Under the UPC, a devisee of a specific devise will be much more likely to expect something from the estate, and as a result, would be much more likely to initiate litigation. Even if the devisee does not actively pursue his/her rights under the UPC, an Executor would be well-advised to initiate a proceeding for a declaratory judgment to determine the rights of the devisee, in all cases where the specifically-devised property is not part of the testator’s estate.

Conclusion

North Carolina’s distinction between voluntary acts and involuntary acts avoids many of the harsh results that caused many states to move towards the principles set forth in Section 2-606 of the UPC. In North Carolina, there does not seem to be a great deal of uncertainty imposed upon Executors nor resulting litigation when specifically-devised property is not part of the testator’s estate.

If Section 2-606 is adopted, we recommend a full adoption rather than a partial adoption (as in South Carolina).

In deciding whether to adopt Section 2-606 at all, we recommend that value of the well-reasoned principles already contained in our North Carolina case law and the increased complexity and likelihood of litigation resulting from Section 2-606 be considered.