



What happens to your debts when you die?

It's a simple fact that death doesn't extinguish a deceased person's debts. Creditors that are owed money by the deceased can still pursue repayment from the deceased's Estate. However, there are some rules that apply to the order in which the deceased's assets can be used to pay debts and other limitations that exclude the use of certain asset types for debt repayment purposes.

Executor's Obligation to Pay Deceased's Debts

An Executor of a deceased person's Estate has many responsibilities and one of the most significant is ensure that the deceased's debts are paid from the Estate assets, if there are sufficient assets to do so, before the assets are distributed to the beneficiaries named in the deceased's Will. Under the NSW *Probate and Administration Act 1898* (the Act), an Executor is authorised to collect the deceased's assets and use them to satisfy the deceased's debts and the failure to do so can expose the Executor to a personal liability to any unpaid creditors.

Insolvent Estates

If there are not enough assets in the Estate to meet all the deceased's debts, the Estate is classed as "insolvent" and the Executor may need to contact creditors to let them know that the debts cannot be repaid, and to ask for the debts to be 'written off'. However, creditors are not required to write off debts and if the debts to a creditor amount to \$5,000 or more, the creditor may apply to court to have a bankruptcy trustee appointed to the Estate. The Executor is also entitled to apply to have a bankruptcy trustee appointed if they believe there are insufficient assets in the Estate to pay all of the deceased's debts.

Are Secured and Unsecured Debts treated differently?

A secured debt is a debt that is fixed to one or more of the deceased's assets, such as a home loan that is secured against the deceased's home by a mortgage, while an unsecured debt is not attached to any asset, for instance a credit card debt. Secured debts will generally be paid by the Executor before unsecured debts as the reality is that if a secured debt such as a home loan is not paid, the mortgagee holding the mortgage would exercise their right to sell the property to recover the debt owed to them.

If a beneficiary has been bequeathed an asset that was used to secure a debt, the beneficiary is actually only being given the equity the deceased held in that asset. Accordingly, if the beneficiary wants to retain the asset then, subject to any contrary intention expressed in the Will which specifies that the debt should be paid from the deceased's other assets, the beneficiary must take on the burden of the debt attached to the asset by either repaying or refinancing the secured debt before the asset is transferred to them.



In respect to unsecured debts, an Executor must use the deceased's assets in accordance with the order prescribed by the Act when paying these debts. The Act also expressly provides that all unsecured debts have equal standing and accordingly no unsecured debt can be paid in priority to any other unsecured debt.

Can any Debts be passed on to Beneficiaries?

Beneficiaries of a deceased are only held responsible for paying off the deceased's debts if:

1. the debt was jointly incurred by the deceased and the beneficiary (i.e. beneficiary was a co-borrower meaning that the deceased and the co-borrower were both liable for the whole of the debt); or
2. the debt was secured against an asset owned by the beneficiary; or
3. the beneficiary personally guaranteed an unsecured debt of the deceased.

Accordingly, if the deceased's assets are insufficient to pay out the deceased's debts, beneficiaries will not be held liable for satisfying the debts of a deceased, including taxes, a HECS/HELP debt, credit card debts or home loans, unless one of the above situations applies.

In what Order are Assets used to Pay Debts?

The Executor when paying the deceased's debts must pay the debts in the following priority:

- Secured debts from the assets securing them;
- Funeral expenses;
- Testamentary and administration expenses (e.g. legal costs in obtaining Probate); then
- Unsecured debts.

The Act stipulates the order in which assets should be applied to pay debts where the Estate is solvent. If the Will contains specific gifts of money amounts to beneficiaries, the Executor must first set aside that money in a fund from the other assets in the Estate that have not been left to a beneficiary. Once this is done the order of application of assets to pay debts is:

1. Assets undisposed of by the Will such as lapsed or void gifts;
2. Assets not specifically disposed of by the Will but included (either by a specific or general description) in a residuary gift;
3. Assets specifically appropriated for the payment of debts;
4. Assets charged with, or disposed of by the Will (either by a specific or general description) subject to a charge for the payment of debts;
5. The fund, if any, retained to meet monetary gifts; and
6. Assets specifically disposed of by the Will, proportionably among them according to their value.



What Assets Can't be Used to Discharge Debts?

Assets that are owned by the deceased as joint tenant with another person, such as bank accounts, shares and real estate will not form part of their Estate and will pass "by way of survivorship" to the surviving joint tenant/s. Accordingly, as the deceased's interest in these assets do not form part of the deceased's Estate they are not available to the Executor to discharge the deceased's debts.

If the deceased has Life Insurance or is a member of a Superannuation Fund, and has nominated a beneficiary to their Life Insurer or Superannuation Fund to receive the benefits of these assets on their death, then these benefits will be paid directly to the nominated beneficiary. They also do not form part of the deceased's Estate and as such are not available to pay the deceased's debts.

If no person has been nominated as the beneficiary of the deceased's Life Insurance or Superannuation benefits, the Life Insurer or Superannuation Fund may pay the deceased's benefits to their Estate. If they do so the benefits can be used by the Executor to pay for the deceased's funeral and for testamentary and administration expenses of the Estate but cannot be used to pay any other of the deceased's debts unless the deceased's Will contains a provision which specifically allows the benefits to be used for this purpose.

If you've been appointed as an Executor of a Will and want to know more about how to deal with paying the deceased's debts or otherwise require assistance to obtain a Grant of Probate and administer the Estate please contact [Lisa Delalis](mailto:lisa.delalis@batemanbattersby.com.au) or [John Bateman](mailto:john.bateman@batemanbattersby.com.au) at our office 02 4731 5899 or email willsestates@batemanbattersby.com.au.