Study L-3032.1 January 23, 2019

Memorandum 2019-4

Revocable Transfer on Death Deed: Follow-Up Study — Trust as Beneficiary

In 2006, the Commission[1] recommended that California authorize the use of a revocable transfer on death deed ("RTODD") to transfer real property on death, outside of probate.[2]

In 2015, Assembly Bill 139 (Gatto) was enacted to implement the Commission's recommendation (with some significant changes).[3] Among other things, the Legislature added a "sunset" provision, which will repeal the RTODD statute on January 1, 2021 (unless the sunset is extended or repealed before it operates).[4] In addition, the law requires the Commission to conduct a follow-up study of the efficacy of the RTODD statute, and make recommendations for the improvement or repeal of that law.[5]

In 2016, the Legislature elaborated on the specific issues that the Commission should address in its follow-up study, requiring that the study address:

> Whether it is feasible and appropriate to expand the revocable transfer on death deed to include the following:
> (A) The transfer of stock cooperatives or other common interest developments.
> (B) Transfers to a trust or other legal entity.[6]

After some initial consideration of those questions,[7] the Commission requested further public comment on those issues.[8] The comment it received was

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1. Any California Law Revision Commission document referred to in this memorandum can be obtained from the Commission. Recent materials can be downloaded from the Commission's website (www.clrc.ca.gov). Other materials can be obtained by contacting the Commission's staff, through the website or otherwise.

The Commission welcomes written comments at any time during its study process. Any comments received will be a part of the public record and may be considered at a public meeting. However, comments that are received less than five business days prior to a Commission meeting may be presented without staff analysis.

2. *Revocable Transfer on Death (TOD) Deed*, 36 Cal. L. Revision Comm'n Reports 103 (2006).
3. AB 139 (Gatto), 2015 Cal. Stat. ch. 293; Prob. Code §§ 5600-5696.
4. Prob. Code § 5600(c).
5. 2015 Cal. Stat. ch. 293, § 21.
6. 2016 Cal. Stat. ch. 179.
7. See Memorandum 2018-33.
8. See Memorandum 2018-44.

considered in Memorandum 2018-58 and its First and Second Supplements. The Commission made a number of provisional decisions based on that input, but "postponed making a decision on whether an RTODD should be able to transfer property to a trust."[9]

This memorandum revisits the postponed question about trusts as beneficiaries of an RTODD. The public comments that bear on that question have been attached to this memorandum for convenience of reference. They are included in the Exhibit as follows:

Exhibit p.

- Mark S. Poochigian, Trusts and Estates Section Executive Committee, State Bar of California (6/1/2017) 1
- Angela Petrusha, Eureka (6/20/18) 11
- Craig Page, California Land Title Association (8/16/18) 14
- Mason L. Brawley, Trusts and Estates Section Executive Committee, California Lawyers Association (11/20/2018) 20
- Nina Whitehurst, Montague (12/4/18) 24
- Nina Whitehurst, Montague (12/17/18) 26

The letters from the Trusts and Estates Section Executive Committee ("TEXCOM") and the California Land Title Association ("CLTA") address a number of issues besides naming a trust as beneficiary. The trust-related parts of those letters can be found at Exhibit pages 3-4, 16-17, and 21-22. The letters from Ms. Petrusha and Ms. Whitehurst are entirely relevant to the trust issue.

Note: In conducting this study, the Commission will examine a number of specific ways in which the law might be improved. The fact that the Commission is considering those specific issues does not mean that the Commission has reached a decision on the general question of whether the RTODD statute should be repealed or continue in effect. It has not done so.

SUPPORT FOR ALLOWING TRUSTS TO BE NAMED AS BENEFICIARIES

Ms. Petrusha and Ms. Whitehurst, both estate planning attorneys, write in support of allowing the RTODD to be used to transfer property to a trust.

Ms. Petrusha notes that she had a client who wished to use an RTODD to transfer property to a trust. She explains why a person might wish to take that approach, rather than simply transferring title to the trust during life:

9. Minutes (Dec. 2018), pp. 7-8.

> Some have questioned the necessity of naming a trust as beneficiary of an RTODD rather than transferring the subject property to a revocable living trust, which would also avoid probate. While this may be the solution in most cases, sometimes this is not a viable option. For example, consider the homeowner who does not wish to incur the expense of creating a trust for herself, but wishes to name a supplemental needs trust (or "Special Needs Trust") as beneficiary of her home. A Special Needs Trust is typically created for the benefit of a person with a disability who would encounter negative consequences if he or she received property or money outright. The homeowner has a modest estate that would not otherwise require a formal probate. In keeping with the intent of AB 139, shouldn't this homeowner be allowed a straightforward, inexpensive, non-probate option for transferring this asset upon death?[10]

Ms. Whitehurst offers a different scenario in which it would make sense to use an RTODD to transfer title to a trust on death, rather than transferring title during life:

> Too many times I have seen individuals place their home into their revocable living trust only to be forced by a refinance lender to deed it back out again. (Many lenders think they cannot lend to a “trust”. They are mistaken in that regard, but that is not the issue before us. The fact is it happens, a lot.) Then the borrower forgets to deed the property back into his or her or their trust after the refinance transaction is concluded. The results are time-consuming and expensive probate, frustration of the intended plan of distribution, and money wasted on estate planning that was not put to use because the main asset wasn’t in the trust at death.
>
> Although keeping the home in the trust at all times is the ideal, and second best is remembering to deed it back after every refinance, I would like to be able to recommend to clients that if they think there are one or more home loan refinancings in their future, they might want to just name their revocable living trust as the death beneficiary pursuant to a RTODD.[11]

She adds:

> It would be nice if homeowners in California could retain title in their individual names during lifetime to facilitate residential acquisitions and refinancings but be able to sleep at night knowing that when they pass their trust will be funded with said real estate and not get tied up in lengthy, expensive and public probate proceedings.[12]

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10. See Exhibit p. 12.
11. *Id.* at 24.
12. *Id.* at 27.

The Commission has not received any comment suggesting that it would be inappropriate, *as a policy matter*, to allow a trust to be named as beneficiary of an RTODD. The same result (post-death transfer of property to a trust) is routinely achieved with a will (although that would generally require probate administration).

Ms. Petrusha and Ms. Whitehurst offer concrete examples of situations where naming a trust as beneficiary of an RTODD would be beneficial.

Concerns About Allowing Trusts to be Named as Beneficiaries

Both TEXCOM and CLTA maintain that the law should not permit an RTODD to be used to transfer property to a trust.

TEXCOM believes that allowing a trust to be named as beneficiary of an RTODD would lead to confusion and error:

> In TEXCOM's view, allowing for transferors to name trusts and legal entities as beneficiaries of RTODDs invites confusion and errors by unknowing transferors; thus, the better rule would be to provide that only individuals may be named as beneficiaries in RTODDs.[13]

CLTA is concerned that allowing a trust to be named as beneficiary of an RTODD could create opportunity for fraud:

> *Trustee of a trust:* Testamentary trusts are governed through probate courts. Allowing a trustee of a trust to be named a beneficiary only allows opportunity for fraud under the pretense of formality and creates a potential conflict with well-established existing law.
>
> …
>
> [W]e have serious reservations over the expansion of RTODDs to include legal entities as beneficiaries, and strongly believe that – were such an expansion to take place – the trustee of a trust continue to be excluded.[14]

The risks of confusion and fraud are discussed separately below.

Before beginning that discussion, it is worth considering a general point made by Ms. Whitehurst:

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13. See Exhibit p. 4. See also Exhibit p. 21 ("TEXCOM believes that the option of naming a trust as beneficiary invites confusion and has urged the Commission to foreclose the possibility of naming a trust as the beneficiary of an RTODD. ").

14. See Exhibit p. 16.

> At some point, there has to be a limit to how far the state should go in protecting people from their poor choices. Don't be so protective of the least common denominator that you eliminate huge benefits for the vast majority of candidates for this type of planning.[15]

It is worth noting that California does not prohibit people drafting their own wills, despite the likelihood that some self-help drafters will make mistakes that could defeat their intentions (including the possibility that execution errors could invalidate the entire instrument). Nor does California preclude self-drafted trusts or grant deeds.

Confusion

TEXCOM has not provided a specific explanation of why allowing a transferor to name a trust as beneficiary of an RTODD would increase the risk of confusion and error. **The staff invites further explanation on that point.**

The staff does see one potential source of confusion — ambiguity as to the identity of a trust that is named as a beneficiary.

When naming a natural person as beneficiary of an RTODD, the mandatory statutory form requires that the transferor provide "the FULL NAME(S) of the person(s) who will receive the property on your death (DO NOT use general terms like "my children") and state the RELATIONSHIP that each named person has to you (spouse, son, daughter, friend, etc.)."[16] That requirement should provide enough information to correctly identify a natural person who is named as a beneficiary.

But how would one identify a trust with enough specificity to avoid any uncertainty as to the identity of the trust? A good starting point would be to require that the trust be named, using the name that was given to the trust in the trust document itself.

The staff sees two potential complications with that approach. First, there does not seem to be any legal requirement that a trust be given a name. So it is theoretically possible that a trust could be unnamed. However, every sample trust that the staff found online or in legal practice treatises called for the trust to be named.[17] It seems likely that the naming of trusts is a routine practice, even

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15. *Id.* at 25.
16. Prob. Code § 5642(a).
17. See, e.g., M. Stern, Drafting California Revocable Trusts, Appendices A-D, at 757, 799, 832, 858 (Cal. Cont. Ed. Bar 4th Ed.); <https://www.nolo.com/legal-encyclopedia/sample-shared-living-trust.html>; <https://eforms.com/living-trust/ca/california-revocable-living-trust-

for laypeople using forms. So it is not clear that this would be more than a theoretical problem.

Second, the name of a trust may not be sufficiently distinct to differentiate it from other trusts. For example, there are probably thousands of trusts named "the Jones Family Trust" in California. How would it be possible to know with certainty which "Jones Family Trust" has been named as beneficiary of an RTODD?

In many situations, common sense would make the answer obvious. But that degree of certainty is not sufficient for the operation of an RTODD. Because it operates without court involvement, the RTODD statute depends on title records and title insurance as away of effectuating the transfer of title. The effect and validity of an RTODD must be determinable from title records, without the need for any inquiry outside of those records. If the record contains any material ambiguity, title insurers will be reluctant to insure that the beneficiary has good title. That would make it difficult or impossible for the beneficiary to sell or encumber the transferred property. The beneficiary would probably need to go to court to establish clear title.

The staff sees two ways to minimize or eliminate any uncertainty as to the identity of a trust that is named as the beneficiary of an RTODD.

The first possibility would be to require that the date of execution of the trust also be provided, along with the name of the trust (e.g., "Jones Family Trust, executed on January 1, 2020"). The biggest downside of that approach would be the risk of a technical error. If a transferor provides the wrong date, the error could raise doubts about the validity of the RTODD and its intended effect.

A second possibility would be to require that a copy of the trust document be recorded along with the RTODD. This approach should eliminate any uncertainty as to the identity of the trust that is being named as beneficiary. Again, the biggest downside would be the risk of a technical error. If a transferor does not realize that the trust must be recorded, and fails to do so, the RTODD could wind up in the courts and could be invalidated. Trust documents can be lengthy and it is possible that a transferor could accidently omit a page or not realize that the notary's acknowledgement should be included (if that were a requirement).

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form/>; <https://freedownloads.net/living-trust/ca-trusts/california-revocable-living-trust-form/>.

Those kinds of practical problems could probably be worked out. If the Commission would like to pursue either or both options (i.e., require that the RTODD specify the date of execution of a trust named as beneficiary and/or require recordation of the trust document), the staff will bring the issue back in a future memorandum, with a fuller analysis and range of options. **If the Commission decides to take that approach, the staff would welcome suggestions from stakeholders on how to unambiguously identify a trust, an issue that must come up regularly in estate planning.**

Fraud

CLTA expresses concern about fraud, but does not provide specific detail about how naming a trust as beneficiary of an RTODD would create any additional or special risk of fraud.

One possible explanation might be found by looking closely at the language that CLTA used in its letter. CLTA writes (with bold added for emphasis):

> ***Trustee** of a trust:* Testamentary trusts are governed through probate courts. Allowing a **trustee** of a trust to be named a beneficiary only allows opportunity for fraud under the pretense of formality and creates a potential conflict with well-established existing law.
>
> …
>
> [W]e have serious reservations over the expansion of RTODDs to include legal entities as beneficiaries, and strongly believe that – were such an expansion to take place – the **trustee** of a trust continue to be excluded.[18]

CLTA consistently refers to the naming of a "trustee of a trust" as the beneficiary of an RTODD. That is reasonable. Under the existing Uniform Testamentary Additions to Trusts Act, a "pour-over" will may devise property to "the trustee of a trust."[19] Property devised in that way "becomes a part of the trust to which it is given" on the testator's death.[20] So, it appears to be an established practice to name the trustee of a trust as devisee, when devising property to a trust.

This suggests that some transferors would do the same with an RTODD, naming the trustee of a trust as beneficiary when intending to transfer property to the trust as an entity.

18. See Exhibit p. 16.
19. Prob. Code § 6300(a).
20. Prob. Code § 6300(b).

That approach could perhaps create an opening for fraud when the transferor is a layperson. If a transferor wishes to name a trust as beneficiary, the trustee of that trust could perhaps trick the transferor into naming the trustee as an individual, rather than in the trustee's capacity as trustee. The result could be an unintended gift to the trustee personally.

That strikes the staff as a very indirect way to perpetrate fraud. It would also require an unusual set of circumstances — the bad actor would need to be the trustee of a trust that the transferor wishes to name as beneficiary. As the staff has noted before, there are much more direct and immediately effective ways to commit elder financial abuse.

That said, if the staff is understanding CLTA's concern correctly, it might be possible to address the problem by expressly precluding (and warning against) naming a trustee as beneficiary, rather than naming the trust itself.

If the staff is not understanding the issue, we would appreciate getting a fuller explanation from CLTA of their concern.

CONCLUSION

As discussed above, there seem to be good reasons to allow the use of an RTODD to transfer property to a trust. For example:

- An RTODD could be used to provide a revocable way to transfer real property to an irrevocable trust (such as a special needs trust), on the transferor's death. This would give the transferor the greatest degree of control of the property during the transferor's life, while also allowing the at-death transfer to occur without probate administration.
- An RTODD could be used to avoid the problem that Ms. Whitehurst describes: A person sets up a revocable living trust and transfers real property to the trust. Later, when refinancing the property, the lender requires that the property be deeded back out of the trust. The owner then forgets to reconvey the property back to the trust, after the loan is approved. An RTODD could be used as a back-stop in that situation, insuring that real property will be transferred to a trust on the transferor's death, in the event that the property was inadvertently left out of the trust during life.

However, there are practical problems that could arise if the law were to permit a trust to be named as beneficiary of an RTODD:

- It is theoretically possible that a trust could be unnamed, which might make it difficult to clearly designate the trust as beneficiary of an RTODD.
- The trust could have a relatively common name, which might undermine certainty as to which of the trusts that share the name is being designated as beneficiary of an RTODD.
- If a transferor names the trustee of a trust, rather than the trust itself, there could be uncertainty about whether the transferor intended a gift to the trustee as an individual, or to the trustee as an agent of the trust. That could create scope for fraud or error.

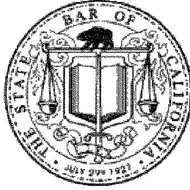
With all of the above in mind, the Commission needs to decide whether the law should permit a trust to be named as a beneficiary of an RTODD. If so, the Commission should also consider whether to pursue any of the following measures to reduce the risks of confusion, error, and fraud:

- Require that a trust be named, using the name that it was given in the trust documents.
- Preclude naming a trustee (as opposed to a trust) as beneficiary.
- Require that the date of execution of a trust be included when naming a trust as beneficiary of an RTODD.
- Require that part or all of the trust document be recorded along with an RTODD, when naming a trust as beneficiary.

How would the Commission like to proceed?

Respectfully submitted,

Brian Hebert
Executive Director



TRUSTS & ESTATES SECTION

THE STATE BAR OF CALIFORNIA

June 1, 2017

VIA E-MAIL AND U.S. MAIL

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Re: Comments from TEXCOM
Study L-3032.1 (Revocable Transfer on Death Deed: Follow-Up Study)

Dear Mr. Hebert:

Thank you for soliciting comments from the Executive Committee of the Trusts and Estates Section of the State Bar of California ("TEXCOM") regarding California's revocable transfer on death deed ("RTODD") law enacted in Assembly Bill 139 of 2015 (Stats. 2015, ch. 293). TEXCOM appreciates the Commission's interest in TEXCOM's views regarding the RTODD law. As you know, attorneys appointed to TEXCOM have technical expertise in the area of trusts and estates law, including planning, administration and litigation regarding nonprobate transfers such as those made by RTODDs.

As we have discussed, TEXCOM expects to relate to the Commission information regarding experiences relating to RTODDs at some point in the next 18 months. The RTODD law still being quite new, TEXCOM anticipates surveying its members once some additional time has passed in order to attempt to obtain information regarding California trusts and estates attorneys' practical experiences with RTODDs that may, in turn, be reported to the Commission. Pending completion of that survey, and as we have discussed, this letter will contain TEXCOM's comments regarding the RTODD law itself.

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General Comment

As you know, TEXCOM has continuing concerns regarding the law providing for statutory RTODDs. TEXCOM agrees in principle with the goal of providing a mechanism by which persons could pass on their real property at death without the need for expensive estate planning during lifetime or a court-supervised probate administration after death. However, TEXCOM believes that RTODDs, as enacted in Statutes of 2015, chapter 293, (i) potentially facilitate the victimization of vulnerable persons by fraud, abuse and undue influence, (ii) will lead to costly litigation regarding the validity and effectiveness of RTODDs, (iii) will lead to undesirable consequences for recipients of property received by RTODD, including the possibility of liability to creditors and the decedent's estate, and (iv) make the property that is subject of the RTODD less marketable, leading to frustration on the part of the recipients of the property, and the need to clear title through the legal process.

TEXCOM believes the RTODD law is fundamentally flawed in a way that TEXCOM fears is not capable of being remedied. Although the statute is well-intentioned—providing owners of certain real property a means of passing that property to chosen beneficiaries at death without the need to incur the expense of engaging competent legal counsel or other professional advisors—the practical pitfalls destroy its effectiveness. The most common drafter of a RTODD will be the property owner himself/herself, usually drafting a deed for the very first time. Costly mistakes—some affecting the very validity of the RTODD—are inevitable. Knowledgeable attorneys will generally not recommend RTODDs because they have more appropriate tools at their disposal.

For these reasons, and some others discussed in this letter, TEXCOM believes that consideration should be given to repealing the RTODD law or allowing it to be automatically repealed effective on January 1, 2021, pursuant to the sunset provision in California Probate Code section 5600, subdivision (c).[1] However, TEXCOM acknowledges that the Commission is supportive of RTODDs, having recommended in *Revocable Transfer on Death (TOD) Deed*, 36 Cal. L. Revision Comm'n Reports 103 (2006) (the "2006 Recommendation") that RTODDs be adopted in California. So, to the extent that the Commission concludes that RTODDs should remain authorized by California statutory law, this letter will provide TEXCOM's observations regarding deficiencies in the law that should be reconsidered.

[1] Unless otherwise indicated, all further statutory references are to the California Probate Code.

<u>Areas of Specific Concern</u>

Following is discussion regarding specific areas of concern that TEXCOM has identified regarding the RTODD law enacted in Statutes of 2015, chapter 293:

1. <u>Definition of "real property."</u> The definition of "real property" contained in Probate Code section 5610 (which limits the types of real property that are eligible to be transferred by RTODD) includes:

> *(a) Real property improved with not less than one nor more than four residential dwelling units. [and]*
>
> ...
>
> *(c) a single tract of agricultural real estate consisting of 40 acres or less that is improved with a single-family residence.*

Thus, it appears from section 5610, subdivision (c), that agricultural property of more than 40 acres was intended to be excluded from the definition of "real property." However, as long as agricultural real property (of potentially unlimited size) is improved with not less than one nor more than four residential dwelling units, such real property would come within the definition of "real property" under subdivision (a).

2. <u>Time for Determining Qualification Under Definition of Real Property</u>. Section 5614 provides that a "[r]evocable transfer on death deed" means an instrument created pursuant to this part that . . . makes a donative transfer of real property to any beneficiary." As discussed above, section 5610 limits the type of real property that may be the subject of a RTODD to the types of real property described in that section. However, the statutes are ambiguous regarding when the real property must come within the statutory definition of "real property." In other words, must the real property be "real property," as defined, at the time that the RTODD is executed? Or, at the time that the RTODD operates because of the transferor's death? Suppose that a parcel of real property was improved with a residence at the time a transferor signs a RTODD with respect to the property; however, before the transferor dies, the residence is demolished such that the property is unimproved at the time of the transferor's death. Such property would have come within the definition of "real property" at the time that the RTODD was executed, but would not come within the definition of "real property" at the time that the RTODD operates because of the transferor's death. The intention in this regard should be clarified.

3. <u>Eligible Beneficiaries</u>. TEXCOM is aware that Statutes of 2016, chapter 179, section 1, amends Section 21 of Chapter 293 of the Statutes of 2015 (the section requiring the Commission to study the effect of California's RTODD) to require that the Commission address, "[w]hether it is feasible and appropriate to expand the revocable transfer on death deed to include . . . [t]ransfers to a trust or other legal entity." However, TEXCOM notes that trusts and legal entities are already authorized to be named as beneficiaries of RTODDs, without any expansion of the enacted statutes required. Pursuant to section 5608, the beneficiary of a RTODD

may be any "person." And, in turn, section 56 defines "person" to include, "an individual, corporation, government or governmental subdivision or agency, business trust, estate, trust, partnership, limited liability company, association, or other entity." Thus, regardless of whether such was intended by the Legislature, trusts and legal entities are already eligible to be named as beneficiaries in RTODDs. In TEXCOM's view, allowing for transferors to name trusts and legal entities as beneficiaries of RTODDs invites confusion and errors by unknowing transferors; thus, the better rule would be to provide that only individuals may be named as beneficiaries in RTODDs.

4. Manner of Execution. Section 5624 provides as follows: "A revocable transfer on death deed is not effective unless the transferor signs and dates the deed and acknowledges the deed before a notary public." This section is ambiguous with respect to what is actually required of the transferor in at least two respects:

a. It appears that section 5624 requires that the transferor must personally date the deed such that a RTODD containing a typewritten date of execution likely would not satisfy the execution requirement contained in section 5624. This should be clarified if it was contrary to the intended requirement.

b. Section 5624 could be read to require that the transferor sign and date the deed before a notary public. Generally, a document need not be signed in the presence of the notary public; all that is required in order to obtain a notary public's acknowledgment is that the signer personally appear before the notary public, and acknowledge having executed the document (including, for example, having executed the document outside of the presence of the notary public). (Civil Code § 1189.) The intention in this regard should be clarified.

5. Timing of revocation of RTODD. The statutes are unclear regarding whether a revocation of a RTODD must be recorded prior to the transferor's death. On the one hand, section 5632 requires that an instrument revoking a RTODD "shall be executed and recorded before the transferor's death" However, on the other hand, section 5628, subdivision (a), specifically authorizes revocation of a RTODD by a second, subsequent RTODD, and under the general rule of section 5626, subdivision (a), relative to the time to record a RTODD, the second RTODD would be valid if recorded within 60 days of execution, even if after the transferor's death. This matter should be clarified. The Commission should consider whether any instrument that would have the effect of revoking a RTODD should be required to be recorded prior to the transferor's death. In TEXCOM's view, requiring that a revocation of a RTODD be recorded prior to the transferor's death imposes a risk that transferors' desires to revoke RTODDs may be frustrated when, for example, recordation of a RTODD before the transferor's death is impractical (e.g., where the transferor signs the revocation of a RTODD far away from the relevant county recorder's office), or impossible (e.g., where the transferor signs the revocation of a RTODD during a weekend when the revocation cannot be recorded until the next business day). Sections 5632 and 5628 should be harmonized to provide that any instrument revoking a RTODD shall effect a revocation if the instrument is recorded within 60 days of execution, even if the recordation occurs after the transferor's death.

6. Attorneys-in-fact. The RTODD law is silent regarding whether an attorney-in-fact may execute or revoke a TOD deed. This should be clarified. The Commission's 2006 Recommendation observed that California law (section 4264) allows an attorney-in-fact named in a power of attorney to create, modify, or revoke the principal's trust, make or revoke a gift of the principal's property, create or change survivorship interests in the principal's property, and designate or change a beneficiary to receive property on the principal's death, provided that the principal expressly authorizes the act in the power of attorney. The Commission further observed that this rule would appear to cover revocation of a revocable TOD deed as well, but recommended that the power of attorney law should be revised to make the coverage explicit. TEXCOM agrees that the power of attorney law should be revised to allow for attorneys-in-fact to make or revoke RTODDs, provided that the principal expressly authorizes the act in the power of attorney.

7. Conflicting dispositive instruments. Section 5660 relating to conflicting dispositive instruments is confusing and ambiguous. The meaning of an "instrument [that] makes a revocable disposition of the property" is unclear and should be clarified.

8. Joint tenancy and other rights of survivorship. Section 5664 provides that, if at the time of the transferor's death, title to the property described in the RTODD is held in joint tenancy or as community property with right of survivorship, the revocable transfer on death deed is void, and the transferor's interest in the property is governed by the right of survivorship and not by the revocable transfer on death deed. This is contrary to the 2006 Recommendation, which proposed a rule whereby the death of the transferor severs the joint tenancy as to the interest of the transferor, and the interest of the transferor passes pursuant to the RTODD. The Commission's recommendation in this regard seems superior and more consistent with the likely intentions of makers of RTODDs. Section 5664 should be revised accordingly.

9. Creditors' rights in property subject to RTODD. The provisions dealing with the liability to creditors and to the transferor's estate of a beneficiary of a RTODD are highly problematic and should be reconsidered. Among the problems with the RTODD law in this regard are the following:

a. Misapplication of provisions from Sections 13200-13210 (Affidavit Procedure for Real Property of Small Value). With respect to the rights of creditors in RTODD property following the death of the transferor, the law follows the existing California model applicable to a successor who takes property of a decedent without probate under the affidavit procedure for real property of small value contained in sections 13200-13210. That model has some major deficiencies when applied to RTODD property. To the extent the Commission feels that continuing to model the provisions dealing with creditors' rights after the procedure applicable to a successor who takes property without probate under the affidavit procedure for real property of small value contained in sections 13200-13210, some problems with the existing statutes that should be considered by the Commission are discussed below.

i. The affidavit procedure for real property of small value only applies where the gross value of all real property in the decedent's estate located in California does not exceed $50,000. Needless to say, the property that can be the subject of a RTODD can be much more valuable. So, while the beneficiary's liability to creditors or to the transferor's estate are somewhat modest in the context of the affidavit procedure for real property worth no more than $50,000, the stakes—along with the burdens placed on recipients of RTODD property—are increased dramatically where more valuable properties are involved as will be the case with RTODDs. For example, the possibility of accrual of interest at 10% per year may be of little concern to a recipient of property worth only $50,000 who chooses to use the affidavit procedure of section 13200 (the risk being only $5,000 per year), but when the similar provisions of section 5676 are applied to a RTODD beneficiary who would receive a property worth, say, $1 million, that beneficiary risks accrual of interest at the rate of $100,000 per year.

ii. The affidavit procedure for real property of small value is only an optional procedure that the beneficiary may choose to employ or not employ. If the beneficiary desires to avoid the risks associated with that procedure, the beneficiary may simply commence probate proceedings, in which the liability of the estate to creditors (and, by extension, the extent to which the beneficiary will bear such liability) will be settled without the beneficiary being exposed to personal liability. This is not the case with respect to RTODDs, which imposes upon the beneficiary the specter of liability for restitution of the property to the decedent's estate, liability for net income received on the property, plus prejudgment interest at the rate of 10% per year (see item #9.a.iii. immediately below).

iii. The beneficiary's liability to creditors includes interest at the legal rate (currently 10% per year pursuant to Code of Civil Procedure section 685.010). This seems harsh, as this is the rate typically applicable to post-judgment interest, where the debtor has been adjudged to have incurred some type of liability for a wrongful act. With RTODDs, the beneficiary may have done nothing wrong at all; his/her only misfortune was having been the beneficiary under a RTODD as opposed to a will, revocable trust or joint tenancy.

b. Liability where beneficiary has made a significant improvement.

i. The provisions of section 5676 dealing with the beneficiary's liability to the transferor's estate where the beneficiary has made a "significant improvement" to the property (§5676) can be quite punitive, and should be reconsidered. Take, for example, a transferor's child who receives property under a RTODD unaware that the transferor had some unpaid unsecured debts. If that child makes a "significant improvement" to the property, then the child is exposed to the fair market value of the property at the time of the improvement, less liens and encumbrances on the property at that time, plus

interest on the net amount at the rate payable on a money judgment, because the personal representative has the option to decline to accept the improved property, and instead demand that amount under section 5676, subdivision (b). This could result in substantial hardship on RTODD beneficiaries who improve property received. The logic of this is unclear and should be reconsidered.

ii. A beneficiary who has made a significant improvement of RTODD property after receiving it and is required to restore the fair market value of the property, plus net income, plus interest, is seemingly not entitled to credit for payments made by the beneficiary toward encumbrances that existed before the transferor's death, an important and inequitable omission in section 5676, subdivision (b). This should be corrected to give RTODD beneficiaries credit for payments made by the beneficiary toward encumbrances that existed before the transferor's death.

iii. Although section 5676, subdivision (b)(1) provides that (under certain circumstances) where a beneficiary restores the property to the estate of the transferor after having made a significant improvement to the property, the estate shall reimburse the beneficiary for the amount by which the improvement increases the fair market value of the property restored, the statutes do not provide any clear guidance regarding how a beneficiary is reimbursed for the value of property attributable to improvements made. Third parties should not unfairly benefit from a beneficiary's devotion of personal resources to improving the property. Thus, any reimbursement due to a beneficiary for improvements made to property that passed by RTODD should enjoy the highest priority, akin to that of a secured creditor.

c. <u>Credit for payment of pre-death encumbrances</u>. A beneficiary required to restore property to the transferor's estate is seemingly not entitled to credit for payments made by the beneficiary toward encumbrances that existed before the transferor's death, an important and inequitable omission in section 5676, subdivision (a)(1). This should be corrected.

d. <u>Payment by beneficiary of post-death encumbrances</u>. Pursuant to section 5676, subdivision (a)(2), if a beneficiary encumbers property after the death of the transferor, and then disposes of the property before restitution is requested to be made, the beneficiary may be made to restore to the decedent's estate the fair market value at the date of disposition less liens existing at that time, plus net income received by the beneficiary, plus interest. This approach assumes that the liens existing at the time of disposition already encumbered the property when the beneficiary received it, and does require the beneficiary to repay the decedent's estate the proceeds of any loan that the beneficiary may have obtained secured by the property after the transferor's death. This appears to be an oversight and should be corrected.

e. Casualty insurance proceeds not contemplated. The provisions dealing with the beneficiary's liability to the transferor's estate do not require the beneficiary to restore to the transferor's estate the proceeds, if any, of any casualty insurance claims. This should be reconsidered, lest a devastating fire on property received by a RTODD beneficiary result in a windfall to that beneficiary.

f. Ambiguity of the phrase "net income". The measure of a RTODD beneficiary's liability to creditors includes "the net income the beneficiary received from the property." The statute would benefit from a definition of "net income." While one might expect that "net income" would include a reduction for maintenance expenses actually incurred, seemingly less clear are issues of reasonable repairs, depreciation, income tax liability on rental income, the value of the beneficiary's personal labor that created the income received, etc.

g. Priority for reimbursement of payments to creditors made by the beneficiary. Where a beneficiary is required to restore property or an amount to the estate of a deceased transferor, that liability is reduced by any property or amount paid by the beneficiary to a creditor of the deceased transferor directly. However, there is no guidance regarding how the beneficiary is to be reimbursed for those payments. Any reimbursement due to a beneficiary for amounts paid directly to creditors should enjoy the highest priority, akin to that of a secured creditor.

h. Reimbursement for certain necessary payments. Where a beneficiary is required to restore property to the estate of a deceased transferor, the law should provide for the beneficiary to be reimbursed for certain payments that benefitted the property, such as property taxes and insurance premiums. Without provisions requiring those reimbursements, the transferor's estate will unduly benefit from the beneficiary's expenditure of resources on these necessary expenses.

10. No requirement that restitution be required in order to satisfy creditors. The personal representative of a decedent's estate may require a beneficiary who received property pursuant to a RTODD to restore that property to the estate, even if there is adequate property already subject to probate administration to provide for the payment of creditors claims. The Commission should consider whether this should be the case. That is, should property that passed by RTODD be exposed to restoration to the deceased transferor's estate even if that property is not required to pay creditors claims? We suggest no.

11. Liability of beneficiaries of different properties. The RTODD law provides no guidance regarding the priority or apportionment of debts among beneficiaries of different properties that pass by RTODD. This should be addressed. Also, where a decedent executes RTODDs for more than one property, the law allows the personal representative to demand that one beneficiary restore the property to the decedent's estate, while leaving other RTODD beneficiaries undisturbed. This should be addressed.

12. Marketability issues and clouds on title. The new RTODD law creates several challenges in terms of the marketability of real property that should be considered further, some of which are discussed below.

a. Pursuant to section 5694, subdivision (a), if a successful contest of a RTODD was filed and a *lis pendens* recorded within 120 days of the transferor's death, the court must order the RTODD void and transfer the property to the person entitled to it. So, any property held pursuant to a RTODD deed will effectively be unmarketable by the beneficiary for the 120-day period after the transferor's death, because no title company will insure title during that period. This should be considered further.

b. Related to the issue raised in item #2 above, will title insurance companies determine whether real property held pursuant to a TOD deed was of a type that may be passed by RTODD because it comes within the definition of "real property" contained in section 5610? Or, will title insurers simply insist upon an exception to title insurance coverage, adversely affecting the marketability of the property? This should be considered further.

13. Survival of encumbrances. Pursuant to section 5652, subdivision (b), property is transferred by RTODD, "subject to any limitation on the transferor's interest that is of record at the transferor's death, including, but not limited to, a lien, encumbrance, easement, lease, or other instrument affecting the transferor's interest, whether recorded before or after recordation of the revocable transfer on death deed." Section 5652 seems to create a special rule for encumbrances on property held pursuant to a RTODD, to the effect that the property passes free and clear of any unrecorded liens, encumbrances, leases, etc., at the transferor's death. This is contrary to the general rule relating to real property liens and encumbrances, and could have significant effects. Suppose an owner of real property held pursuant to a RTODD enters into an agreement to sell the property, but dies during the escrow period. Were the property not held pursuant to a RTODD, the decedent's successor would be required to perform under the contract made by the decedent. However, section 5652 seems to allow for the beneficiary under a RTODD to disavow without any consequence any unrecorded agreements made with respect to the property by the transferor while living. This should be addressed.

14. Effect of sunset provision. The second sentence of Section 5600, subdivision (c), attempts to preserve the validity and effect of RTODDs executed before January 1, 2021, and the ability of transferors to revoke such RTODDs, in the event that the RTODD law is automatically repealed. However, that sentence itself would be repealed by the sunset

provision contained in the first sentence of section 5600, subdivision (c). The principle that the validity of existing RTODDs (and the ability of transferors to revoke existing RTODDs) would survive repeal of the RTODD law does not seem to have been enacted by the Legislature in a provision that would survive the automatic repeal. This should be considered.

Thank you for your consideration of TEXCOM's comments in this regard. If you have any questions, or if I may provide any additional information regarding TEXCOM's perspective on these matters, I invite you to contact me anytime by e-mail at mpoochigian@bakermanock.com, or by telephone at (559)432-5400.

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Respectfully submitted,

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PETRUSHA LAW
Estate Planning & Administration

July 20, 2018

Via email to:bhebert@clrc.ca.gov
and U.S. Mail

Mr. Brian Hebert, Executive Director
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c/o UC Davis School of Law
400 Mark Hall Drive
Davis, CA 95616

Re: Study L-2032 (Revocable Transfer on Death Deed: Follow-Up Study)
Trusts as beneficiaries

Dear Mr. Hebert:

Thank you for the opportunity to address the California Law Review Commission regarding California's revocable transfer on death deed ("RTODD") law enacted in Assembly Bill 139 of 2015 (Stats. 2015, Ch. 293). I am a California-licensed attorney practicing exclusively in the area of trusts and estate law, including planning and administration regarding non-probate transfers such as those made by RTODDs. My specific concern deals with whether trusts or other legal entities may be named as a beneficiary of an RTODD under the current law.

Last year, prior to preparing an RTODD for my client who wished to name a trust as beneficiary, I reviewed California Probate Code 5600-5696, including Section 5608 which defines beneficiary as a "person" named as the transferee in an RTODD. I also reviewed the attached educational material published by the Continuing Education of the Bar (CEB) in California Probate Workflow Manual Revised (rev ed Cal CEB) Section 4.12C. Therein, CEB states that the beneficiary of an RTODD may be any "person" as defined in Probate Code Section 56, which includes "an individual, corporation, government or governmental subdivision or agency, business trust, estate, trust, partnership, limited liability company, association, or other entity." In an effort to avoid any potential future title issues, I also contacted my local title insurance company to discuss the naming of the trust on the RTODD. Its senior title officer acknowledged that from the title company's perspective, trusts and other legal entities are eligible beneficiaries of an RTODD because they qualify under the definition of "person."

Thereafter, my client's RTODD was properly executed and recorded. Several weeks later the county assessor's office contacted me to advise that the RTODD is invalid because a trust cannot be named as beneficiary, per the State Board of Equalization's interpretation of the current law. The assessor notified my client that although the document was recorded, it will have no effect upon her death because it is invalid. Thereafter I did some additional research, including a review of comments by the Senate Judiciary Committee asking for further study of this issue, and a letter from the Executive Committee of the Trusts and Estates Section of the State Bar of California ("TEXCOM") to the Commission dated June 1, 2017, addressing several RTODD issues including this one.

TEXCOM's letter points out that under the current law, trusts "... are already authorized to be named as beneficiaries of RTODDs." Although its recommendation is to *change* the law to provide that only individuals may be named beneficiaries, the fact remains that the law already allows any "person" under Probate Code Sec. 56 to be named on an RTODD.

Considering the fact that both CEB and TEXCOM have interpreted the current law to allow this practice, I am certain other California attorneys have recorded RTODDs naming trusts, charitable organizations, or other legal entities as beneficiaries. Surely many laypersons using the statutory forms continue to do so as well. Some transferors may have already died or become incompetent to sign additional legal documents. Narrowing the scope of this law now, more than 2 ½ years after its effective date, should be done with the following in mind:

There is great concern that if these already-recorded RTODDs are later declared invalid, there will be unintended results upon the death of the transferor, when it will be too late to take any alternative action. These results will likely lead to costly litigation for estates which have little resources (other than the subject property) and cannot afford the legal costs. Therefore the testamentary intent of the transferors will be undermined, and this law will have failed them.

Some have questioned the necessity of naming a trust as beneficiary of an RTODD rather than transferring the subject property to a revocable living trust, which would also avoid probate. While this may be the solution in most cases, sometimes this is not a viable option. For example, consider the homeowner who does not wish to incur the expense of creating a trust for herself, but wishes to name a supplemental needs trust (or "Special Needs Trust") as beneficiary of her home. A Special Needs Trust is typically created for the benefit of a person with a disability who would encounter negative consequences if he or she received property or money outright. The homeowner has a modest estate that would not otherwise require a formal probate. In keeping with the intent of AB 139, shouldn't this homeowner be allowed a straightforward, inexpensive, non-probate option for transferring this asset upon death?

Thank you for your consideration of my comments. If you have any questions, or if I may provide further information, please do not hesitate to contact me by telephone at (707) 798-6030 or by email to angela@petrushalaw.com.

Respectfully submitted,

Angela Petrusha
Attorney at Law
State Bar of CA License No. 297287

AMP:ah
Enclosure

§4.12C 1. Execution of a Transfer on Death Deed

An effective revocable TOD deed must meet the following requirements:

- The transferor must have capacity to contract (Prob C §5620);
- The beneficiary must be identified by name in the revocable TOD deed (Prob C §5622);
- The revocable TOD deed must be signed and dated and acknowledged by the transferor before a notary public (Prob C §5624); and
- The revocable TOD deed must be recorded on or before 60 days after the date it was executed (Prob C §5626(a)).

A revocable TOD deed need not be delivered to, or accepted by, the beneficiary during the transferor's lifetime to be effective. Prob C §5626(b), (c). A TOD deed beneficiary may be any "person" as defined in Prob C §56, which includes individuals, governmental entities, trusts, estates, corporations, partnerships, limited liability corporations, and other entities. Beneficiaries must be named individually and the transferor should include the beneficiary's relationship to him or her (*i.e.,* my wife, my son, my friend). General terms to describe beneficiaries, such as "my children" or other class of persons, are not permitted. Prob C §5642(b).

NOTE► Because contingent beneficiaries may not be named on a revocable TOD deed, it has the disadvantage that a named beneficiary may die at a time when the transferor no longer has contractual capacity to name a new beneficiary. See Prob C §1872(a). All beneficiaries of a revocable TOD deed take the property in equal shares on the death of the transferor. Prob C §565(a)(3). Therefore, a revocable TOD deed should not be used if a transferor wants to transfer real property disproportionately to the beneficiaries.

August 16, 2018

Mr. Brian Hebert
California Law Revision Commission
c/o UC Davis School of Law
400 Mrak Hall Drive
Davis, CA 95616

RE: Comments from CLTA on CLRC Study L-3032.1 Memorandum 2018-33
(Revocable Transfer on Death Deed: Follow-Up Study, Aug. 6, 2018)

Dear Mr. Hebert:

Thank you for soliciting comments from the California Land Title Association ("CLTA") regarding specific provisions of the revocable transfer on death deed ("RTODD") law enacted by Assembly Bill 139 of 2015 (Stats. 2015, Ch. 293). CLTA's industry members have substantial experience in dealing with matters of trusts and estates as they relate to real property and are well-positioned to provide a "real-world" perspective on non-probate transfers such as those attempted through the use of RTODDs.

We remain concerned about the negative impact of RTODDs on consumers:

As you know, CLTA has long viewed the implementation of RTODDs in California with concern given that there is not always a simple fix for the transfer of real property. We appreciate and understand the goal of wanting to provide individuals a less expensive and (theoretically) less complicated mechanism by which they can transfer their real property at death. However, we maintain that RTODDs, as enacted, continue to pose risks for transferors and beneficiaries, as they could:

a) potentially encourage the exploitation of at-risk individuals through fraud and abuse;
b) result in unmarketable title and curative work to remove the clouds on title of real property attempted to be transferred via RTODD;
c) trigger lengthy litigation required to determine the validity of RTODDs, often in a probate court arena that ironically was supposed to be avoided through the use of RTODDs, and;
d) confer an unexpected and unwelcome liability, through a debt owed to creditors and/or the decedent's estate, on beneficiaries of property conveyed by RTODD.

In response to a request from the CLRC for title insurance industry feedback, we are respectfully providing comments on several specific issues relating to RTODDs but want to make clear that we remain skeptical about their long-term use in California.

We believe this is especially true when consumers –without benefit of counsel—fill out and execute a RTODD without fully understanding the unintended consequences these “simple” forms can sometimes create to the detriment of the intended beneficiaries and surviving family members.

Residential Property Limitation:

In a recent memo[1], CLRC staff examined at length the effect of the “residential property limitation” on the applicability of RTODDs. Within the scope of this evaluation, CLRC staff explored several issues, a number of which we have enumerated and responded to as follows.

1. *Standardizing the Terminology of Probate Code Section 5610*

   In an examination of Probate Code Section 5610, CLRC staff identified that, as currently enacted, the terms within the Section are not entirely “based on facts that can be determined from the record”, and that this negatively affects a title insurer’s ability to “assess the validity of an RTODD solely from the information that is in official public records.”[2]

   We agree with the CLRC staff’s assessment and recommendation that the terminology of Probate Code Section 5610 should be standardized to be based on facts determinable from a search of public records.

2. *Expanding RTODDs to Provide for Transfer of All Types of Common Interest Developments (“CIDs”)*

   As identified by CLRC staff, the language in Probate Code Section 5610(b) expressly provides for a single type of CID – condominiums – within the definition of “real property”, “impliedly [precluding] the use of an RTODD to transfer other types of CID property.”[3] In addition, the statutory RTODD Frequently Asked Questions (“FAQ”), in an enumeration of the only types of property that can be transferred via RTODD, the only type of CID listed is a “condominium unit”,[4] supporting the intent of the statute.

   Though CLRC staff opine that there is “no good justification for the condominium limitation”,[5] we respectfully disagree, and believe that the limitation should remain in place.

   Other types of CIDs, such as cooperatives, can have restrictions on property ownership and a co-op could argue with a straight face that the transfer of a non-condominium CID via RTODD is void because of restrictions on transfers. Such a situation would prove much more problematic than conveyance via will or trust, wherein if a co-op board were to disapprove the beneficiary the estate or trustee would simply sell the property.

   Thus, CLTA believes that amending the law to allow the use of RTODDs to transfer other types of CIDs is a bad idea.

[1] CLRC Memorandum 2018-33

[2] *Id.* at 4.

[3] *Id.* at 5.

[4] Prob. Code § 5642(b).

[5] CLRC Memorandum 2018-33, p. 5.

3. *Timing Clarifications*

In addition, CLRC staff also explored the question of when it is best to evaluate the validity of an RTODD – whether at the time of execution or operation of the RTODD. We agree with CLRC staff's assertion that RTODDs should be evaluated for meeting the standard of "real property" under the law at the time of execution of the RTODD.[6]

4. *Elimination of Residential Property Limitation*

Lastly, CLRC staff recommend that the residential property limitation on RTODDs be eliminated, asserting that the restriction "might have made sense as a way to narrow the scope of a pilot project", and inviting policy arguments to the contrary.[7]

We respectfully disagree with CLRC staff's provisional recommendation. In many cases, the value of commercial properties is much higher than residential properties and the sophistication of the parties usually translates into the parties using traditional estate planning documents with the advice of counsel, as well as being subject to more rigorous regulations and statutory requirements.

Thus, assuming that the RTODDs are flawed at a more fundamental level, it makes no sense to the title industry that the method of transfer be expanded for use by individuals who are already using traditional methods of conveying real property. Expanding the use of RTODDs to higher value properties only compounds the existing potential for fraud and abuse, litigation, and loss of title marketability, but in this case the dollar amounts will be substantially larger.

In short, if the RTODDs are already problematic for "simpler" and less costly transfers, where is the logic in expanding the use of RTODDs in higher cost –and more complicated—transactions?

For these reasons, we assert that RTODDs should remain limited to residential properties.

Natural Person Limitation:

In its August 6th memo, CLRC staff also requested comments on whether the law "should permit a legal entity to be named as a beneficiary of an RTODD" and "whether there are any…problems that would result from allowing that practice."[8] In consideration of this question, we have identified several issues that could arise from reforming the law so as to allow legal entities to be named as beneficiaries of RTODDs.

- *Trustee of a trust:* Testamentary trusts are governed through probate courts. Allowing a trustee of a trust to be named a beneficiary only allows opportunity for fraud under the pretense of formality and creates a potential conflict with well-established existing law.

[6] *Id.* at 9.
[7] *Ibid.*
[8] *Id.* at 15.

- *Corporations:* There are multiple problems that would need to be considered in the context of allowing a corporation to be named as a beneficiary to an RTODD. Such problems include a limited liability corporation or other corporation being granted property that had not been addressed or approved in operating agreements, minutes, etc., or legal issues with the property that could be inherited such as abatement items, environmental concerns, etc.
- *Governmental entities:* Current law requires a declaration from governmental entities consenting to conveyance as a beneficiary; however, RTODDs do not need to be consented to by, or delivered to, the beneficiary to operate.
- *Other issues in general:* In addition, other considerations with respect to legal entities include the constitution of a legal entity changing over time in the context of the transferor's original intent, or the conveyed property transferring despite a legal entity's established vetting process that would have otherwise rejected the transfer.

For these reasons, we have serious reservations over the expansion of RTODDs to include legal entities as beneficiaries, and strongly believe that – were such an expansion to take place– the trustee of a trust continue to be excluded.

As stated earlier, if the RTODDs are already problematic when used on "simpler" and lower-dollar real estate transfers, where is the logic in expanding the use of RTODDs to these new applications that have higher risk and statutory requirements that conflict with the recommended changes to the law?

Return of Property Transferred by RTODD for Creditor's Claims:

Lastly, CLRC staff requested comment on possible reforms to Probate Code Section 5676, including whether the property restitution remedy should be eliminated, thereby making the beneficiary's liability for decedent debts personal only.[9]

Specifically, CLRC staff examined two potential avenues for reform, including:

1. *Clarifying How Enforcement of Section 5676 Affects Purchasers or Encumbrancers*
2. *Revising Section 5676 to Only Impose Personal Liability on a Beneficiary*

While we view the first of the two proposals as a potential improvement over current law, we remain unconvinced that either option would be a "silver bullet" in addressing all potential liability for bona fide purchasers that we insure.

State law already gives bona fide purchaser and bona fide encumbrancer protections if past the 120 days. However, the statute doesn't, nor do we think it should, get rid of the application of general fraud or forgery law – which has a longer statute of limitation of three years.

If an estate goes through probate or is administered by a trust, then the administrator or trustee has a duty to pay the estate's liabilities before distributing to beneficiaries. The inherent problem with RTODDs is that the property

[9] *Id.* at pp. 15-23.

transfers to the beneficiary ***prior*** to any confirmation that the estate liabilities have been paid. This presents a problem when the beneficiary doesn't have the property anymore or has used up all the equity before a probate court has determined liability. In those instances, it is entirely possible that holding the beneficiary personally liable will not amount to anything for the creditors, likely resulting in them arguing that the RTODD is void.

The benefit of RTODDs does not outweigh general fraud or forgery law, and it is all the more critical that the RTODD statutes ***not*** get rid of the application of general fraud and forgery law because RTODDs are, by their nature, prone to fraud and forgery. As such we can't envision a way to draft legislation that reduces the risk associated with the three-year enforcement period without beneficiaries being able to show the estate liabilities are zero or have been paid in full.

Not all transactions are of equal risk:

It is important that an evaluation of RTODDs take into consideration that ***the feasibility of the RTODD as a conveyancing instrument will vary from transaction to transaction***. For example, the following factors can greatly increase the risk associated with a RTODD:

- How close to the transferor's death was the RTODD recorded?
- What is the relationship of the beneficiary to the transferor? Was the transferor elderly and the beneficiary a caregiver?
- If surviving siblings in a family are specifically excluded from the RTODD, can interested parties truly rely on the RTODD as being dispositive of the grantor's wishes?
- Were multiple RTODDs recorded over a period of time on the affected real property? Do the multiple RTODDs indicate potential claims against the real property?
- Is there a surviving spouse living on the property and excluded as a beneficiary by the RTODD, potentially triggering community property concerns?

These are just a few quick examples that easily come to mind. In some cases, the potential claims to the real property will be nonexistent or easy to ascertain and the RTODD may be the appropriate instrument for conveyance. In other situations, the RTODD is a recipe for disaster and costly litigation.

We suggest that RTODDs also be evaluated based on their risk to good faith purchasers/consumers who are NOT covered by title policies:

In most cases, good faith purchasers/consumers will often enlist a title company to insure them and to conduct a title search as part of the underwriting process. In addition, a lender will often be providing a purchase money mortgage and also will be insured by a title company.

However, in some situations consumers will decide to purchase real property with cash from their savings and forgo purchasing a title policy to save money. In these instances, no independent title or escrow company expert will be conducting a title search or considering the potential risks associated with a RTODD. In interfamilial transfers or transfers between friends, such a situation is not all that unusual, despite the inherent risk.

In these situations, if an RTODD ends up being faulty or fraudulent and the consumer is insured by a title company, the insured's security interest in the real property will be protected under the terms of the policy. However, if no title policy exists, the defective or fraudulent RTODD could mean a total loss for the innocent good faith purchaser/consumer who unfortunately relied upon the RTODD as being a valid instrument of conveyance without risk.

While we realize there is "a provision that expressly protects a good faith purchaser of property transferred by an RTODD"[10] in existing law, realistically this means the good faith purchaser must still hire – out-of-pocket – an attorney to assert this claim.

Elimination of the 2021 sunset provision is premature:

The reason that CLTA and other stakeholders requested a sunset date in the original RTODD legislation is to allow for all affected industries, estate planners, attorneys and consumer advocates to evaluate the value of the RTODDs and to create a track record associated with their use. Given that we are seeing some problems with RTODDs as stated above, we believe the wiser course of action is to leave the sunset provision in place as we monitor the use of RTODDs over the next two years. If the consensus of all affected parties at the end of that time is that the value of RTODDs exceeds the risk associated with their use, then the sunset provision in law could be more reasonably removed from the statute.

Conclusion:

CLTA agrees in principle with the CLRC's goal of a simplified estate planning process. However, despite efforts at reform, we continue to view the RTODD as a well-intended tool that nevertheless exposes transferors and beneficiaries to many unintended – and undesirable – consequences. Given that many individuals who utilize an RTODD are unlikely to be, or even assisted by, a capable estate attorney, we think it likely that an elevated risk of error is inherent to the process, notwithstanding the already discussed potential for fraud and abuse. Therefore, we continue to assert that individuals would be better served by seeking the services of the state's many qualified estate attorneys whom understand the other, better options for estate planning.

Thank you for your consideration of CLTA's comment on this matter. If you have any questions, please feel free to contact me via e-mail at cp@clta.org or phone at (916) 444-2647.

Respectfully,

Craig C. Page
Executive Vice President
and Counsel

[10] *Id.* at 17.

TRUSTS AND ESTATES SECTION
CAlawyers.org/Trusts

November 20, 2018

<u>**VIA E-MAIL AND U.S. MAIL**</u>
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Re: Memorandum 2018-44
Study L-3032.1 - Revocable Transfer on Death Deed: Follow-Up Study (Public Inquiry)

Dear Commissioners:

This letter contains comments regarding the recordation of a revocable transfer on death deed ("RTODD") on behalf of the Executive Committee of the Trusts and Estates Section of the California Lawyers Association ("TEXCOM"). Specifically, the comments in this letter are in response to Memorandum 2018-44 in which the California Law Review Commission solicited public comment regarding eight specific issues relating to RTODDs. Each of those issues is listed below, followed by TEXCOM's comments.

1. **Are there practical or legal reasons why it would be problematic to allow the use of an RTODD to transfer the ownership of a share in a stock cooperative?**

   In a stock cooperative, the real property is owned by a corporation. Individuals own shares of the corporation which provides the right to lease and occupy a unit. (Civil Code section 4190).

   Since a corporation (not the individual shareholders) owns the real property, it would not be possible for the individuals to effectuate a transfer of the property by a deed, including an RTODD. Any transfer by a shareholder would be a transfer of shares of the corporation, not the real property.

2. **Are there practical or legal reasons why it would be problematic to allow the use of an RTODD to transfer an ownership interest in a community apartment project?**

In a community apartment project, the members own the entire development jointly and each has the right to lease and occupy a unit. (Civil Code section 4105)

Since the individual owners of the community apartment project collectively own the land (each will typically own a percentage ownership interest in the entire development), their interests in the land could be transferred by a deed, such as a RTODD. However, it is likely that the community apartment project would have restrictions on transfers and/or require approval before allowing an ownership transfer. It may also have restrictions or require approval regarding the occupancy of a unit. If so, the attempted transfer via the RTODD could be void or ultimately not approved.

These issues would also exist for a transfer by trust or probate, so they are not necessarily specific to an RTODD.

3. **Are there practical or legal reasons why it would be problematic to allow the use of an RTODD to transfer an ownership interest in a planned development?**

In a planned development, members own a separate lot or parcel with an interest in a common area that is either owned by an association or the members jointly. (Civil Code section 4175)

A planned development may have restrictions on transfers and require approval of new owners. Accordingly, an attempted transfer via an RTODD would raise issues similar to those described above relating to an interest in a community apartment project.

4. **Are there practical or legal reasons why it would be problematic to allow the use of an RTODD to transfer property in an age-restricted community?**

Using an RTODD to transfer property in an age-restricted community may create an issue if the beneficiary would not qualify for occupancy due to their age. This issue would also exist for a transfer by trust or probate, so it is not necessarily specific to an RTODD.

5. **In general, are there practical or legal reasons why it would be problematic to name a trust as beneficiary of an RTODD?**

TEXCOM believes that the option of naming a trust as beneficiary invites confusion and has urged the Commission to foreclose the possibility of naming a trust as the beneficiary of an RTODD. (see the letter to the Commission from Mark Poochigian, Esq. dated June 1, 2017)

6. **Are there practical or legal reasons why it would be problematic to name a *specific type* of trust as beneficiary of an RTODD?**

   It is not clear what the Commission is referring to by a "specific type" of trust, which makes this question too vague to answer.

7. **Are there practical or legal reasons why it would be problematic to name a public entity as beneficiary of an RTODD?**

   California Government Code section 27281 prohibits the recordation of any deed conveying an interest in real estate to a political corporation or governmental agency for public purposes without the consent of the grantee evidenced by its certificate or resolution of acceptance attached to or printed on the deed. This would create an issue in the context of RTODD deeds since it appears that the deed could not be recorded without the consent of the public entity.

8. **Are there practical or legal reasons why it would be problematic to name a nonprofit corporation as a beneficiary of an RTODD?**

   Yes, use of an RTODD may be problematic when a nonprofit corporation is the beneficiary designated to receive the property on the death of its current owner.

   A nonprofit corporation may not be able to accept real property due to legal constraints (e.g., the lack of corporate authority to accept or own real property). Furthermore, the charity may have dissolved, changed its name or merged with another entity when the grantor of the RTODD dies, which could make it very difficult or impossible to identify the beneficiary or may result in the transfer failing. These issues would also exist for a transfer by trust or probate, so it is not necessarily specific to an RTODD, but the RTODD is intended to be self-executing, which is significantly different than passage by trust or will, in which a trustee or executor is present to assure that title to the property passes to a new owner and that the new owner is the intended recipient.

   Furthermore, when a charitable gift is made in a will or trust and the charitable organization no longer exists, the property may be distributed to a successor organization. If entity has dissolved, a court may salvage the gift by invoking the doctrine of *cy pres* and order that the property be distributed to another charitable organization.

/////

Thank you for your continued consideration of TEXCOM's comments regarding RTODDs. If you have any questions, or if I may provide any clarity regarding the comments described above, please do not hesitate to contact me.

Respectfully submitted,

Mason L. Brawley
Trusts and Estates Section Executive Committee
California Lawyers Association

cc: Saul D. Bercovitch (via email to saul.bercovitch@calawyers.org)
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EMAIL FROM NINA WHITEHURST (DECEMBER 4, 2018)

Re Memorandum 2018-59
Revocable Transfer on Death Deed: Follow-Up Study

Dear Commissioners:

You have requested comments on whether the law governing Revocable Transfer on Death Deeds (RTODD) should allow the designation of a trust as the death beneficiary, and you also questioned whether there would be any purpose in allowing designation of revocable living trusts. My answers are yes and yes, respectively.

The classic goals of a revocable living trust include, among others, (1) provide for distribution of assets upon death, (2) avoid probate, and (3) provide for administration of assets during lifetime while the grantor is incapacitated. The use of a RTODD that names a revocable living trust as the death beneficiary would accomplish goals (1) and (2) but not goal (3), so why would I advocate that it be allowed even though it is less than ideal?

Too many times I have seen individuals place their home into their revocable living trust only to be forced by a refinance lender to deed it back out again. (Many lenders think they cannot lend to a "trust". They are mistaken in that regard, but that is not the issue before us. The fact is it happens, a lot.) Then the borrower forgets to deed the property back into his or her or their trust after the refinance transaction is concluded. The results are time-consuming and expensive probate, frustration of the intended plan of distribution, and money wasted on estate planning that was not put to use because the main asset wasn't in the trust at death.

Although keeping the home in the trust at all times is the ideal, and second best is remembering to deed it back after every refinance, I would like to be able to recommend to clients that if they think there are one or more home loan refinancings in their future, they might want to just name their revocable living trust as the death beneficiary pursuant to a RTODD. For disability planning they could use a durable power of attorney (DPOA). Just for your information, the DPOA method is less than ideal because third parties (incorrectly) tend to only honor them only for a year or so after execution and then start to consider them stale, and they are not well suited to planning for succession of the agent/attorney-in-fact.

Regarding the question about whether a distinction should be made among types of trusts as death beneficiaries, I can think of no reason whatsoever to distinguish among them. All trusts should be eligible – grantor, non-grantor, revocable, irrevocable, special needs, charitable, you name it. If the trust could be an eligible beneficiary of a will, the trust should be an eligible beneficiary of a RTODD, the purpose of which is to avoid having to use a will as the transfer device because, as we all know, "Where there's a will, there's probate."

Yes, there are some types of trusts that would be poor choices for a death beneficiary of a home. It would be highly unusual to transfer a home at death to a standalone retirement trust or an irrevocable life insurance trust, as a couple of examples, because such special purpose trusts are not designed to hold real estate, but if that were to happen, it would "work", just in a less than ideal way. Besides, it is a very unusual individual that would pay an attorney to prepare such a specialized trust and then run off on his or her own and designate the trust as a death beneficiary in a RTODD without the advice of the estate planning attorney that created the trust.

It would be very difficult, in any event, to line out via legislation which trusts would be poor choices and which trusts would be good choices. If you did decide to go down that road, will you do the same for wills, making some trusts ineligible will beneficiaries as to homes? At some point, there has to be a limit to how far the state should go in protecting people from their poor choices. Don't be so protective of the least common denominator that you eliminate huge benefits for the vast majority of candidates for this type of planning.

As an aside, I have heard (though not personally experienced) that some (again, poorly informed) lenders are considering RTODDs to be clouds on the title and are demanding that they be revoked before the lender will lend against the security of the home. This is nonsense, of course, for reasons that I need not explain to this audience, but if there is anything you can do in the legislation to alleviate this problem, that would be greatly appreciated. The existence of a RTODD should not be any more of a cloud on title than a will would be, the only difference being that the former is on the record and the latter is not.

Thank you for your time and consideration.

Nina

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EMAIL FROM NINA WHITEHURST
(DECEMBER 17, 2018)

Re Memorandum 2018-59, Supp. 2

Ladies and Gentlemen:

I differ with the California Land Title Association with regard to whether a RTODD should be allowed to transfer real property to a trust. Of course it should! CLTA's reasoning is that it is "too late" to effect a transfer at death because the transferor has died. If that reasoning is correct, then there are a whole lot of death transfers taking place every day that are in grave jeopardy.

The adjective that describes transfers taking place at death is "testamentary" and, it should be noted, devices for effecting testamentary transfers abound and have proven to be quite workable, efficient, effective, and not hampered by the fact that the transfer trigger is death. Indeed, transfer at death is the whole point of a testamentary transfer.

The best example is the good old fashioned last will and testament, pursuant to which the testator states his intentions as to who should own his properties, real and personal, when he dies, reserving the right to revoke or modify the will at any time during lifetime (provided he still has testamentary capacity and certain statutory formalities have been satisfied). Wills have been effective at accomplishing transfers after the testator has died for centuries.

And, it is extremely common for wills to transfer properties to all kinds of trusts, including both trusts that are in effect prior to death and trusts that were not in effect prior to death but that spring into existence at death. The classic example of the former is every estate planner's bread-and-butter "pour-over will" that transfers the probate estate to the testator's pre-existing revocable living trust. The classic example of the latter is the will that leaves assets to one or more testamentary trusts created and governed by the terms of the will.

I submit that a RTODD ought to be able to transfer to either a pre-existing trust or to a trust created by will, but I will also concede that the latter would not seem to make a whole lot of sense when the testator could accomplish the same thing within the four corners of the will given that he has already chosen to go down that path. Still, he might reason that it is easier to revoke and replace a RTODD than it is to amend a will (requiring the cooperation of not one but two witnesses and all that) and should be able to choose that option.

More modern examples of testamentary transfers include death beneficiary designations on bank, brokerage, retirement and numerous other financial accounts as well as, of course, life insurance policies. None of these techniques are questioned because the account or policy owner is not alive when the transfer takes place.

The California Department of Motor Vehicles permits and honors transfer on death designations on motor vehicle titles, which designations are revocable and, if you don't mind me mentioning this again, but it bears repeating, take effect when the motor vehicle owner is no longer alive.

Then there are the techniques that currently exist and are specific to real estate and real estate titling, referring of course to joint tenancy with right of survivorship and community property with right of survivorship, which feature a sort of partial revocability (not revocable as to the share given up presently but revocable as to the retained interest, though I admit there are some conflicts between the Family Code and the Civil Code on this that you all might want to address).

And surely you are already aware of the old California case law that supports the enforceability of non-statutory transfer on death deeds.

Although transferring real estate to a revocable living trust during lifetime is considered ideal, there are circumstances that would cause the settlor of a revocable living trust to want to delay transferring real estate to a trust until death. I referred in my last comment to the problem of lenders refusing to lend against collateral owned in trust. This seems to be more of a problem with residential lenders than with commercial and agricultural lenders, and for no good reason, but it does not seem to be a problem that is going away any time soon. It would be nice if homeowners in California could retain title in their individual names during lifetime to facilitate residential acquisitions and refinancings but be able to sleep at night knowing that when they pass their trust will be funded with said real estate and not get tied up in lengthy, expensive and public probate proceedings.

Thank you for your consideration.

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