StudyL-3032 April 21, 2006

First Supplement to Memorandum 2006-16

Beneficiary Deeds (Discussion of Issues)

This memorandum supplements Memorandum 2006-16 (available from the Commission, www.clrc.ca.gov) with additional material relating to the TOD deed. Attached are the following communications we have received in connection with this study since Memorandum 2006-16 was released.

Introduction

Craig Page, writing on behalf of the California Land Title Association (CLTA), notes that the Commission's charge from the Legislature is an objective study to determine whether legislation establishing a beneficiary deed should be enacted in California. He stresses that the study is to determine if a TOD deed is necessary and in the best interests of California's real property consumers, lenders, title companies, and other interested parties.

CLTA is concerned that Memorandum 2006-16 focuses on specific drafting issues rather than the overarching question, giving the impression that the Commission has already reached a conclusion on the matter. CLTA believes the Commission must first determine whether existing devices are adequate, before proceeding to develop TOD deed legislation. "It should not be presumed that such a deed is necessary or that the CLRC charge is to create such a statute absent a strong finding that such a device is essential to real property consumers." Exhibit p. 5. CLTA is concerned that creating actual statutory language at this time creates an impression that the language will be offered to the Legislature irrespective of whether or not the TOD deed is necessary. Moreover, the staff's attention to statutory detail "signals to CLTA that the TOD

deed has already been embraced by the Commission itself without a thorough analysis or study of existing law already having been conducted to determine if such a new conveyancing document is actually necessary." Exhibit p. 6. CLTA believes the Commission needs to take a step back and first analyze whether traditional conveyancing methods are adequate before focusing on drafting details of the TOD deed.

CLTA is correct that the ultimate charge of the Legislature to the Commission is to determine whether TOD deed legislation should be enacted in California. The staff believes CLTA is also correct that a person viewing Memorandum 2006-16 in isolation might conclude that the Commission has approved the concept of the TOD deed in principle, and is just ironing out the details. We will make sure that any future public document concerning this study precisely indicates the status of the study.

In fact, the Commission has not reached any tentative conclusions on the need for the TOD deed. The Commission is following the procedure laid out by the staff and adopted by the Commission at its first consideration of this subject:

> **Method of Proceeding**
>
> AB 12 requires two decisions by the Commission — (1) whether a beneficiary deed should be authorized in California, and (2) if so, the content of proposed legislation to authorize it.
>
> The staff does not believe the first decision can be made in isolation. We need to look at problems that would be involved in implementing a beneficiary deed and how those problems would be handled legislatively. After we have gone through the process of developing a satisfactory statute, we can then step back and take a look at whether the whole thing makes sense.
>
> The staff would pursue a three-pronged approach. We would:
>
> (1) Evaluate existing devices in California for transferring real property on death, and compare them with the advantages and disadvantages of the beneficiary deed. This will require standard staff legal work.
>
> (2) Evaluate experience in other jurisdictions that authorize a beneficiary deed. This will involve reviewing the legal literature of the other jurisdictions, including cases under the beneficiary deed statute. It will also involve making an effort to get feedback from title insurers, attorneys, consumer groups, and others in those jurisdictions. This is something we are not adept at doing, but we will look for help on this from California interest groups.
>
> (3) Address and resolve issues that have been raised concerning the beneficiary deed. To a significant extent, this will involve a comparison of the statutes of other jurisdictions to see how this has been handled. If it has not been handled, we will need to develop our own solutions. It is not necessarily an answer to say that if it

> has not been a problem there, it won't be a problem here. California has more people, property values are higher, and litigation may be a first resort for dispute resolution.
>
> When we have completed this work we will be in a position to make an informed decision on the merits of the beneficiary deed.

Memorandum 2005-46 (11/3/05), at p. 8 (available from the Commission, www.clrc.ca.gov).

We have not overlooked existing devices. Memorandum 2006-5 (available from the Commission, www.clrc.ca.gov), considered by the Commission at its February meeting, spends 16 pages analyzing the advantages and disadvantages of existing California donative transfer techniques for real property, including:

- Lifetime Deed
- Will or Intestate Succession (including small estate procedures)
- Intervivos Trust
- Joint Tenancy
- Community Property
- Intervivos Transfer with Reserved Life Estate
- Revocable Deed
- Conveyance Pursuant to Nonprobate Transfer

However, we cannot rationally compare those devices with the TOD deed until we know exactly what the TOD deed does and what its legal consequences are. We cannot simply take an existing TOD statute, say Arizona's, and base our analysis on that. If there is a known defect in the Arizona statute that cannot be cured, that is a problem with the TOD deed concept. But if the defect can be cured by appropriate statutory language, the defect should not be considered a problem with the TOD deed concept. In the staff's opinion, the process we are currently engaged in is essential to a full deliberative process and a sound decision.

We could consider the incidents of the TOD deed without preparing draft language, as CLTA suggests. However, the staff believes that actual statutory language is preferable for two reasons:

(1) It will provide interested persons who wish to review and comment on this matter a precise indication of the nature of the TOD deed being considered for adoption in California. As we are often reminded in the legislative process, the devil is in the details.

(2) The Legislature's charge directs the Commission, if it recommends adoption of the TOD deed, to recommend the content of the proposed statute. With a legislative deadline of January 1, 2007, we

> must be in a position to finalize proposed legislation quickly if our ultimate recommendation is that TOD deed legislation should be adopted.

The bottom line is that the staff thinks the way we are proceeding is sound, but we must be attentive to the concerns expressed by CLTA.

The staff believes that the role of the title industry is critical in this study. Regardless of the Commission's ultimate decision on the matter, a TOD deed cannot succeed unless title insurers are satisfied that they can safely insure title based on the deed.

We address the other concerns raised in the CLTA letter at appropriate points in this memorandum.

Terminology

In Memorandum 2006-16 the staff recommends that "transfer on death deed" (TOD deed) terminology should be used rather than "beneficiary deed" terminology. The Executive Committee of the State Bar Trusts & Estates Section (ExComm) comes to the same conclusion. Exhibit p. 2.

Capacity to Make Deed

In Memorandum 2006-16 the staff recommends that the requisite capacity for execution of a TOD deed should be testamentary capacity. The State Bar Committee has analyzed the matter and recommends a dual standard. To the extent the TOD deed affects a present interest in property, a contractual standard should apply (under the Due Process in Competence Act); to the extent property is transferred at death under the TOD deed, a testamentary standard should apply.

ExComm is concerned about joint tenancy. Suppose either or both of two joint tenants executes and records a TOD deed of that joint tenant's 50% interest in the property. Under the scheme proposed in Memorandum 2006-16, that act would have the effect of severing the joint tenancy. A joint tenant might have testamentary capacity sufficient to understand that the joint tenant's 50% share of the property will pass to the named TOD beneficiary. But is that capacity sufficient for the joint tenant also to understand that, by so doing, the joint tenant is giving up the possibility of taking the other joint tenant's 50% share by right of survivorship?

"ExComm concluded that to the extent the recordation of a beneficiary deed affects a present interest, DPCDA should apply. Conversely, if a present interest

is not involved so that the beneficiary deed has no effect other than a transfer at death, ExComm believes the testamentary standard should apply." Exhibit p. 2. The Due Process in Competence Act employs a contractual capacity standard, that the person understand and appreciate "the significant risks, benefits, and reasonable alternatives" involved in a decision. Prob. Code § 812(c).

That is an interesting point. Suppose a person who has testamentary, but not contractual, capacity makes two TOD deeds on the same day — one deed for property held as a tenant in common and the other for property held as a joint tenant. Should the law recognize the one deed but invalidate the other? While the staff thinks ExComm is perhaps correct in theory, we would be concerned about spinning this out too finely and complexifying the law for everyone that will have to deal with the practicalities of a TOD deed.

Note also that the problem raised by ExComm disappears if we change the structure of the TOD deed law slightly so that either (1) we do not require the TOD deed to be recorded during lifetime (in which case there is no lifetime severance and no loss of survivorship right) or (2) we require the TOD deed to be recorded during lifetime but limit its severing effect so that severance does not occur on recordation but only when the TOD deed becomes operative by virtue of the transferor's death. (See "Effect of TOD Deed on Joint Tenancy" below).

In any event, testamentary capacity requires a person to understand the nature and situation of the property the person is giving away. Prob. Code § 6100.5. At least an argument can be made that a person who severs a joint tenancy is merely giving away property — in this case the right to receive property by survivorship — and therefore testamentary capacity is the appropriate standard.

Recordation

We have adopted the policy that a TOD deed must be recorded before the transferor's death in order to be effective. The State Bar Committee is concerned about what happens if the recorder's office does not record the deed immediately and the transferor dies after submission of the deed to the recorder's office but before recordation.

In Memorandum 2006-16 the staff suggests that the Commission consider adopting the rule that applies to severance of a joint tenancy. Under the law of joint tenancy, a deed or other instrument severing a joint tenancy in real property must be recorded before the severing joint tenant's death in order to be effective.

Civ. Code § 683.2(c)(1). But an exception is made for a deathbed severance executed within three days before death — the severance is effective if recorded within seven days after death. Civ. Code § 683.2(c)(2). Such a provision would have the effect of making a TOD deed unmarketable for a week after the transferor's death, but that is perhaps not an undue burden on successors to the property and may help effectuate the decedent's intent.

Battle of Recorded Deeds

The California Land Title Association is concerned that if an owner records multiple TOD deeds, the law will undermine the basic real property recording concept of "first in time, first in right". Since the last recorded TOD deed would have priority over earlier recorded deeds, that would cause numerous problems, turning the rule on its head and essentially creating a "last in time, first in right" regime.

CLTA offers as an example a transferor who executes two different TOD deeds for the property, years apart. Even though the transferor records the last executed deed, a disappointed beneficiary could at the last minute find and record the earlier deed, thereby frustrating the transferor's intent. For these reasons, CLTA believes that the TOD deed process could create a negative precedent for constructive notice in California and result in a transferor's intent being undermined.

The problem alluded to by CLTA is what we have been calling the "battle of recorded deeds" in our memoranda on this subject. Arizona law does in fact provide that "If an owner executes and records more than one beneficiary deed concerning the same real property, the last beneficiary deed that is recorded before the owner's death is the effective beneficiary deed." Ariz. Rev. Stat. § 33-405(G). However most jurisdictions with TOD deed legislation provide that it is the last executed deed, not the last recorded, that controls.

The Commission has approved the policy argued for by CLTA — that the last recorded deed should not prevail. Rather it should be the last *executed* deed. See the staff draft in Memorandum 2006-16:

> **Effect of multiple deeds**
>
> If a transfer on death deed is recorded for the same property for which another transfer on death deed is recorded, the later executed of the deeds is the operative instrument.
>
> **Comment.** This section gives effect to the last executed of recorded TOD deeds. A TOD deed is executed by signing, dating,

> and acknowledging before a notary public. See Section [to be provided] (execution of TOD deed). For purposes of this section execution is complete when the transferor acknowledges the deed before a notary public, not when the deed is signed and dated.

Effect of TOD Deed on Joint Tenancy

In Memorandum 2006-16, we propose that execution and recordation of a TOD deed by a joint tenant severs the joint tenancy and results in the property passing to the TOD transferor's beneficiary rather than to the surviving joint tenant. If the transferor revokes the TOD deed before death, the joint tenancy is not revived, but the property passes to the transferor's heirs by will or intestate succession.

The California Land Title Association is concerned that this rule could have a negative effect for many transferors who did not intend the TOD deed to have that result. What will real property owners and transferors know about the TOD deed if it is introduced in California? An uninformed user of the TOD deed could end up with an unintended result. "The advent of the TOD deed, used improperly, could have a very negative effect on an option that has worked rather well over the years and is very simple to understand." Exhibit p. 9.

It would certainly be possible to provide that the TOD deed does not sever a joint tenancy, but instead passes the entire property to the TOD beneficiary only after the death of the last joint tenant. And in fact most jurisdictions follow that rule. But that could also result either in (1) hamstringing the survivor's ability to deal with the property in the interim or (2) frustrating the TOD transferor's intent if the survivor decides to sell or encumber the property. The staff believes the better rule is that a TOD deed should sever a joint tenancy.

However, it does not necessarily follow that severance should occur on recordation of the TOD deed. We could provide, for example, that recordation does not sever the TOD deed; severance only occurs at the transferor's death. Under that scheme, neither the recordation nor the revocation of a TOD deed would affect the joint tenancy. Whether the TOD deed prevails, or the joint tenancy prevails, would be determined on the basis of the instruments of record at the death of the first to die of the joint tenants.

Such a rule would perhaps be more consistent with the concept that a TOD deed has *no effect* during the lifetime of the TOD transferor. It would also obviate the concern of the State Bar Committee about capacity of a transferor to sever a joint tenancy.

On the other hand, such a rule would unbalance the current balance found in the law governing joint tenancy. Under current law, either joint tenant has the opportunity to receive the entire property, depending on which dies last. But allowing for a TOD deed override without severance of the joint tenancy would preserve the TOD *transferor's* right to take all the property by survivorship, but eliminate the *other* joint tenant's opportunity to take all of the property by survivorship. It would convert what is currently a two-way street into a one-way street.

The staff believes fairness demands severance, but we do not feel strongly about it. We simply raise the issue here for further Commission consideration.

CLTA's underlying concern about this, and other aspects of the TOD deed, appears generally to be more a problem with uninformed use of the TOD deed than with the substantive rules. **It might be desirable to add to any statutory form that is developed a simple statement about the effect of a TOD deed on the transferor's estate plan.**

Multiple Owners

The discussion of joint tenancy severance, immediately above, is symptomatic of the complications that multiple ownership causes for the TOD deed concept. If co-owners jointly execute a TOD deed, what happens during the interim between the deaths of the co-owners, until the property finally passes to the TOD beneficiary? May the surviving co-owner revoke or change the beneficiary designation (thereby frustrating the intent of the first to die)? If the survivor may not revoke the TOD deed or change beneficiaries, can the survivor encumber the property and give the loan proceeds to a different beneficiary? What about waste — must the survivor maintain the property for the TOD beneficiary?

The staff takes the position in Memorandum 2006-16 that the death of the first co-owner should pass that co-owner's interest to the TOD beneficiary (consistent with our position on joint tenancy severance). That would enable the surviving co-owner to deal with that co-owner's interest freely. It would also result in the surviving co-owner and the TOD beneficiary being tenants in common of the property, with the possible complications that would entail.

The State Bar Committee thinks the statute should provide a means for spouses to convey their property jointly, whether held as community property or joint tenancy, effective on the death of the second spouse to die. "Most spouses likely would assume that upon the death of the first spouse to die, the property

would pass to the surviving spouse and upon the subsequent death of the surviving spouse to the beneficiary named on the beneficiary deed." Exhibit p. 2.

The staff is sympathetic to that position. We acknowledge in Memorandum 2006-16 that the concept of a co-owner's interest passing immediately to the beneficiary on that co-owner's death would make the TOD deed a less attractive estate planning device for some owners (particularly spouses) than it would otherwise be. The staff's position, however, is that on balance it is better to keep things simple and avoid the problems of "limbo" ownership between the deaths of the two spouses. Co-owners who want the property to pass first to the survivor and then to a beneficiary should employ some other estate planning device.

If the Commission prefers to develop a system whereby property passes first to the surviving spouse and then to the TOD beneficiary, that would certainly be appropriate. In fact, there are plenty of models available, since a number of states that have enacted TOD deed legislation have taken that approach. The key question is whether the survivor should have the right to revoke the TOD deed. The states that have addressed the issue provide, understandably, that the survivor may revoke the TOD deed. That would be essential to avoid the types of problems foreseen by the staff.

A typical provision in another state is not limited to spousal co-ownership and provides, in effect:

> **Joint tenancy and community property**
>
> A transfer on death deed of joint tenancy property or community property with right of survivorship may provide that the deed does not take effect until the death of the last surviving owner. The deed has the following effect:
>
> (a) The deed transfers the property to the named beneficiary effective on the death of the last surviving owner, unless the deed was executed by fewer than all of the owners. If the deed was executed by fewer than all of the owners, the deed transfers the property to the named beneficiary only if the deed was executed by the last surviving owner.
>
> (b) The deed may be revoked only if the revocation is joined in by all of the then surviving owners who executed the deed.

Note that under this type of provision, if one of two joint tenants (or spouses of community property with right of survivorship) executes a TOD deed, the deed is ineffective to transfer that person's interest to that person's chosen TOD beneficiary unless that person survives the nonparticipating owner, in which

case the whole property and not just that person's interest passes. But such a person could ensure that the person's interest passes to the person's chosen beneficiary, without taking a chance on survival, by the simple device of first severing the joint tenancy or the CPWROS, and then executing a TOD deed. That is why the Commission previously concluded that two instruments should not be required where one will suffice, and the TOD deed should have the effect of directly severing a joint tenancy.

If the Commission were to take the route suggested by ExComm, we would probably want to consider expanding the provision to cover tenancy in common property and also regular (non-CPWROS) community property, to enable co-owners to pass property first to the survivor of them and then to the jointly designated TOD beneficiary.

Subsequent Incapacity of Owner

The State Bar Committee would have the statute identify the parties who may revoke the TOD deed, i.e., the transferor or the transferor's conservator.

The staff agrees that the statute should be clear on this point. We have proposed language in Memorandum 2006-16 to the effect that the "transferor or the transferor's agent or other fiduciary" may convey, assign, contract, encumber, or otherwise deal with the property (to the extent the action is within the scope of the agent's or fiduciary's authority) as if no transfer on death deed were executed or recorded. Our proposed comment refers expressly to a conservator. We would also add a cross-reference to substituted judgment principles under the Probate Code.

Survival

The State Bar Committee would have the statute determine how restrictions or conditions can be placed on a beneficiary.

In Memorandum 2006-16 we express our concern about a condition other than survival. Imposition of a non-record condition will make property that passes by TOD deed unmarketable, absent a court determination that the condition has been satisfied. A court proceeding would defeat a major purpose of using a TOD deed.

The California Land Title Association is also concerned that ambiguities will require title companies to require a TOD beneficiary who wishes to transfer property to get further "off record" documentation before title insurance will be offered. In some cases the documentation may be difficult to obtain and a quiet

title action will be necessary. "If a quiet title action is required, this can run into the tens of thousands of dollars for heirs that would have been much better off if the transferor had undertaken estate planning steps on the front end of the process." Exhibit p. 10.

Nonetheless, the staff thinks TOD transferors will not refrain from putting conditions and restrictions in TOD deeds. But the staff's position is that should not be encouraged.

If the Commission agrees with ExComm that something should be said about conditions, we would be minimalist about it. For example:

> **Interest transferred by TOD deed**
>
> A transfer on death deed of real property transfers the transferor's interest in the property to the beneficiary subject to any condition or restriction in the deed and 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, regardless of whether the instrument is recorded before or after recordation of the transfer on death deed.

Priorities As Between Creditors of Transferor and Creditors of Beneficiary

Commissioner Regalia raises two issues concerning the interaction between existing statutes that protect the rights of creditors of a beneficiary and the proposed TOD deed law protecting creditors of the transferor. These are basically priorities issues.

After-Acquired Title

The first issue relates to application of the after-acquired title doctrine. Under this doctrine, if a person that does not have title to property makes an encumbrance or transfer in anticipation of acquiring title, the encumbrance or transfer affects the property by operation of law when title is acquired. See, e.g., Civ. Code §§ 2390 (mortgage), 1106 (transfer). That situation could occur where the beneficiary of a decedent has an expectancy of receiving property and desires to convert the expectancy to cash. Cf. Civ. Code § 2883 (agreement by beneficiary of probate estate to create a lien on estate property creates no lien until distribution of property; any expectancy of lien is extinguished by sale of the property in probate).

Under these general principles, the lien would attach, or the property would be transferred, as of the date the beneficiary succeeds to the property. But would

that affect the rights of the transferor's creditors, particularly creditors whose secured or unsecured right arose *after* the beneficiary mortgaged or transferred the expectancy?

The after acquired title doctrine ought not to affect rights of the transferor's creditors. The beneficiary may mortgage or transfer only what the beneficiary ultimately receives from the transferor, subject to all the transferor's encumbrances and liabilities. If the beneficiary were permitted to create a priority in the beneficiary's own creditors, to the detriment of the transferor's creditors, that would negate the fundamental TOD deed principle that the transferor retains full ownership rights, and the beneficiary acquires no interest, until the transferor's death.

The question is, do we need to specifically address this issue by statute, or are general principles adequate to cover the point? Relevant language proposed in Memorandum 2006-16 would provide:

> **Effect of TOD deed on rights during lifetime of transferor**
>
> Neither execution nor recordation of a transfer on death deed of real property:
>
> (a) Affects the ownership rights of the transferor during the transferor's life, and the transferor may convey, assign, contract, encumber, or otherwise deal with the property, and the property is subject to process of the transferor's creditors, as if no transfer on death deed were executed or recorded.
>
> (b) Creates any legal or equitable right in the beneficiary, and the property is not subject to process of the beneficiary's creditors, during the transferor's life.
>
> (c) Results in a transfer or conveyance of any right, title, or interest in the property before the transferor's death.
>
> **Interest transferred by TOD deed**
>
> A transfer on death deed of real property transfers the transferor's interest in the property to the beneficiary 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, regardless of whether the instrument is recorded before or after recordation of the transfer on death deed, and the holder of rights under the instrument may enforce those rights against the property notwithstanding its transfer to the beneficiary by the transfer on death deed.

It appears to the staff that these provisions are adequate to address the after-acquired title issue, at least with respect to a secured creditor of the transferor. **It**

is probably sufficient to augment the Comments to these provisions with an explanation of how they interact with the after-acquired title doctrine.

Whether the general provisions are adequate to address the rights of an unsecured creditor of the transferor is less clear. The answer depends ultimately on the Commission's position on the rights of an unsecured creditor. If the Commission adopts the staff's recommendation in Memorandum 2006-16, an unsecured creditor will have no rights against TOD property, only a right of recovery against the beneficiary. In that circumstance there will be no after-acquired title issue. But if the Commission takes the position that an unsecured creditor of the transferor has rights against TOD property itself, then we may need to clarify the priorities by statute.

Purchase Money Encumbrance

The second issue relates to a transaction made by the beneficiary after the decedent's death. If the beneficiary sells the property, and the sale is financed by a purchase money mortgage or deed of trust, the secured creditor may be entitled to a special statutory priority. See Civ. Code § 2898 (purchase money encumbrance "has priority over all other liens created against the purchaser, subject to the operation of the recording laws").

This provision is not inconsistent with the Commission's general approach to give primacy to the recorded instrument. See the draft of "Interest transferred by TOD deed" set out immediately above. **We could add language to the comment** to that provision, cross-referencing Section 2898, if we wanted to make clear that the transferor's recorded encumbrance has priority over a purchase money encumbrance derived from the beneficiary.

General Provision on Priorities

Rather than addressing the specific issues of the after-acquired title and the purchase money encumbrance, we may want to address priorities among creditors globally. There are undoubtedly other priority issues that could surface, given the right combination of facts. Commissioner Regalia suggests that, "Perhaps these problems can be solved simply by a statutory recitation that nothing in the recommended new law replaces or supercedes priorities among creditors which are otherwise applicable, perhaps with specific references to the above statutes?"

That approach has obvious attractions, although we wonder whether we can say anything that has enough content to be meaningful, without at the same time

causing unintended consequences. Here is a stab at some general statutory language:

> **Priorities among creditors**
>
> Notwithstanding any other statute governing priorities among creditors, the following priorities apply with respect to real property transferred by TOD deed:
>
> (a) A creditor of the transferor whose right is evidenced by an encumbrance or lien of record at the time of the transferor's death has priority over a creditor of the beneficiary, regardless of whether the beneficiary's obligation was created before or after the transferor's death and regardless of whether it is secured or unsecured, voluntary or involuntary, recorded or unrecorded.
>
> (b) A creditor of the transferor whose right is not evidenced by an encumbrance or lien of record at the time of the transferor's death [to be determined, based on Commission's decision as to how unrecorded debts of transferor, whether secured or unsecured, are to be treated].
>
> **Comment**. Subdivision (a) of this section makes clear that a creditor of the transferor has priority over a creditor of the beneficiary, at least to the extent the transferor's creditor has a lien or encumbrance of record at the time of the transferor's death. Thus the doctrine of after-acquired title (Civ. Code §§ 1106, 2930) does not create a priority in the beneficiary's creditors, even if the right of the transferor's creditor was created after the interest of the beneficiary's creditor. Likewise, the priority given by statute to a purchase money encumbrance by the beneficiary's transferee does not override the general priority of an encumbrance of record by a creditor of the transferor. See Civ. Code § 2898 (priority of purchase money encumbrance, subject to operation of recording laws).

Liability of TOD Beneficiary for Transferor's Debts

The staff recommends in Memorandum 2006-16 that the beneficiary of a TOD deed should be liable for the transferor's unsecured debts to the extent of the value of the TOD property received:

> **Liability of beneficiary of TOD deed for creditor claims**
>
> (a) The beneficiary of a transfer on death deed is liable to the transferor's estate for an allowed or approved claim against the estate to the extent provided in this section.
>
> (b) A beneficiary's liability under this section may not exceed the value of the real property received under the transfer on death deed. A beneficiary may satisfy in full the liability under this section by transferring the property to the transferor's estate, together with rents and profits received on the property and free of encumbrances imposed since receipt of the property.

(c) A beneficiary is liable under this section only if the claim remains unsatisfied after exhaustion of all of the following property:

(1) Property in the transferor's estate.

(2) Property of a trust serving as the principal nonprobate instrument in the transferor's estate plan as shown by its designation as devisee of the transferor's residuary estate or by other facts or circumstances, to the extent of the value of the property received or controlled by the trustee.

(d) On due notice to the beneficiary of a transfer on death deed, the liability imposed by this section is enforceable in a proceeding in this state, whether or not the beneficiary is located in the state.

(e) A proceeding under this section shall be commenced within one year after the transferor's death.

Commissioner Regalia has noted an ambiguity in this provision. Is the beneficiary liable to the transferor's estate for the full value of the property received, even if the beneficiary has obligations that attach to the property immediately on receipt? Typical examples would be a pre-existing judgment lien or tax lien against the beneficiary that operates under after-acquired title principles.

The staff agrees with Commissioner Regalia that the unreduced value of the property should be the measure of the TOD beneficiary's liability. Otherwise the beneficiary would in effect be able to thwart the transferor's creditors by subjecting the property to the beneficiary's own pre-existing creditors to the detriment of the transferor's creditors.

The staff thinks the proposed draft set out above is adequate to achieve that result. **It may be useful to point out its operation in the Comment.**

The staff would give the same treatment to a related ambiguity. When the proposed statute limits the TOD beneficiary's liability to "the value of the real property received under the transfer on death deed", the intention is to refer to the net value of the interest received (as reduced by any liens or encumbrances on it). **That could be pointed out in the Comment.**

Alternatively, we could spell that out in detail. We note that the analogous Probate Code small estate procedure, allowing a beneficiary to take real property of small value by affidavit, addresses the matter expressly. (Selected provisions of the small estate procedure are set out in Memorandum 2006-16.) The small estate statute describes the method of valuing property taken by affidavit, for the purpose of determining the beneficiary's liability to the decedent's estate. Liability is typically limited to "the fair market value of the property, determined

as of the time of the disposition of the property, less the amount of any liens and encumbrances on the property at the time." See Prob. Code §§ 13204-13207.

In fact, one possibility the staff raises in Memorandum 2006-16 is to incorporate by reference the small estate affidavit procedure in the TOD deed statute, thereby avoiding the need to reinvent the procedure here. **We would be interested in comments of practitioners as to the efficacy of the existing small estate procedure and how adaptable it would be for TOD deed purposes.**

Retroactivity

We have become aware that instruments purporting to be "beneficiary deeds" exist and have been recorded in California, perhaps using a form deed from another jurisdiction. How should the TOD deed law deal with a preexisting instrument that purports to make a nonprobate transfer of real property effective on the death of the transferor?

If the instrument conforms to the requirements of the TOD deed law, the instrument should be recognized as a TOD deed executed under the law. That would have the effect of applying all the provisions of the TOD deed law to the instrument, including revocability, creditor rights, and the like. The staff has no problem with that approach, since (1) it would clarify the rules applicable to the instrument, and (2) it would not frustrate the transferor's expectations since there would have been no relevant law in effect at the time of execution of the instrument on which the transferor could base any expectations.

That approach would also be consistent with the general approach of the Probate Code generally to make a revision of the law applicable retroactively, to the extent practicable. See Prob. Code § 3 (new law applies to all matters governed by it regardless of whether an event occurred or circumstance existed before, on, or after operative date of new law).

But the staff would not invalidate an instrument that does not comply with the TOD deed law. After all, it may still be a valid transfer on death under Probate Code Section 5000:

> A provision for a nonprobate transfer on death in an insurance policy, contract of employment, bond, mortgage, promissory note, certificated or uncertificated security, account agreement, custodial agreement, deposit agreement, compensation plan, pension plan, individual retirement plan, employee benefit plan, trust, *conveyance, deed of gift,* marital property agreement, or *other written instrument of a similar nature* is not invalid because the instrument does not

> comply with the requirements for execution of a will, and this code does not invalidate the instrument.

Prob. Code § 5000(a) (emphasis added). Such an instrument would be governed by the applicable law in effect at the time, whatever that might be. See Prob. Code § 3(g) (if new law does not apply to a matter that occurred before the operative date, old law continues to govern the matter notwithstanding amendment or repeal by new law).

We have addressed the nonconforming instrument to some extent in Memorandum 2006-16:

> **Effect on other forms of transfer**
>
> (a) This part does not preclude use of any other method of conveying property that is permitted by law and that has the effect of postponing enjoyment of an interest in real property until the death of the owner.
>
> (b) This part does not invalidate any deed otherwise effective by law to convey title to the interests and estates provided in the deed that is not recorded until after the death of the owner.

We would supplement it with a transitional provision along the following lines:

> **Transitional provision**
>
> (a) This part applies to a transfer on death deed of a transferor who dies on or after January 1, 2008, whether the deed was executed before, on, or after January 1, 2008.
>
> (b) Nothing in this part invalidates an otherwise valid transfer under Section [to be provided].
>
> **Comment**. This section implements the general rule that a new provision of the Probate Code applies retroactively. Section 3. However, this part does not interfere with rights of a decedent's successors acquired by reason of the decedent's death before the operative date of this part. An instrument of a decedent that dies before the operative of this part, or an instrument of a decedent that dies after the operative date of this part but that was not executed in compliance with this part, is governed by other law. See Sections 3(g) (application of old law), [to be provided] (effect on other forms of transfer).

Evaluation of TOD Deed

Adequacy of Other Instruments

The California Land Title Association raises the question whether existing conveyancing instruments are inadequate, necessitating the TOD deed. Perhaps better educational opportunities for seniors and unsophisticated consumers on

how best to achieve their goals would be more effective that creating a new form of title. "[E]xisting laws — with enhanced educational opportunities for seniors and other parties — might be a less hazardous path to take than creating what might be viewed in hindsight as 'drive through deeds' that harm those we seek to protect: seniors and unsophisticated real property owners." Exhibit p. 7.

The staff agrees that the Commission should take these considerations into account when it gets to the point of making a policy determination whether or not to recommend enactment of a TOD deed law in California.

Experience in Other Jurisdictions

Arizona. The California Land Title Association has forwarded us information concerning the operation of the Arizona beneficiary deed statute, enacted in 2001. See Exhibit pp. 11-15. The Land Title Association of Arizona notes the following issues that have arisen in Arizona (most of which were fixed in 2002 or are addressed by pending legislation):

- Beneficiaries unaware that they need to record a death certificate.
- The consequences if the beneficiary predeceases the transferor.
- The effect of a conveyance or encumbrance by the transferor after recordation of a beneficiary deed.
- Whether notice of the beneficiary deed must be given to the beneficiary.
- The effect of a beneficiary deed on property held in joint tenancy.
- How to designate successor beneficiaries.
- The effect of a deed to a class, such as heirs, rather than to a named beneficiary.
- Whether a transfer to a beneficiary who is married requires any special community property waiver.
- Can the beneficiary be an entity?
- How do multiple grantees hold title if the transferor fails to specify?

The staff believes Memorandum 2006-16 adequately addresses all of these issues. (With the exception of the community property issue, which is governed by general law. Property acquired by a married person by gift, bequest, devise, or descent is separate property. Fam. Code § 770. Arguably this language would be construed to cover acquisition by TOD deed.) The Land Title Association of Arizona's legislative committee chair observes, "Bottom line — with the 2002

revisions, I think the beneficiary deed is working pretty well — at least, we haven't seen significant issues, other than the one LTAA is trying to fix this session. I think the bill is pretty comprehensive." Exhibit p. 13.

CLTA also forwards us an article by Ciupak and Forest, *Beneficiary Deeds: Potential & Problems*, Arizona Journal of Real Estate & Business p. 37 (Oct. 2001). This article, written by two attorneys when the Arizona legislation was first enacted, notes a number of potential problems (all of which are addressed in Memorandum 2006-16), and indicates that, "Because of these and other potential complications, various title companies have stated that they will refuse to issue Beneficiary Deeds and that they will require owners to revoke Beneficiary Deeds before selling or refinancing the property." Exhibit p. 15. (These concerns have now been resolved, according to the Land Title Association of Arizona.) The authors conclude:

> In short, Beneficiary Deeds are ideal for small estates wishing to avoid probate and associated costs, such as a single parent with a modest estate leaving the property to children at death. The Beneficiary Deed does not provide for posthumous control of the property, as would a trust, but does transfer ownership at death in an uncomplicated manner. There may be a relatively small niche best suited for the Beneficiary Deed, but it appears the Beneficiary Deed can be an effective, inexpensive estate planning tool when used correctly.

Exhibit p. 15. It is the last caveat that concerns CLTA — "when used correctly".

Colorado. We have spoken with personnel from the Colorado Bankers Association who worked with the Colorado Bar Association to address concerns of financial institutions with the 2004 Colorado beneficiary deed legislation. The issues were worked out satisfactorily, and the statute appears to be operating smoothly, although there is not yet much experience under it.

Support for TOD Deed Concept

Sarah Shena, an attorney with the Kings/Tulare Area Agency on Aging, gives a number of reasons for adoption of the TOD deed concept. She indicates some of the inadequacies of existing transfer devices:

> Over my 20 years in practice I have often seen expensive living trusts, bought from trust mills by senior clients. Some of the trusts were useless, and all of them cost the senior too much of his/her very limited resources. These elders simply wanted to pass their homes to their children outside of probate. If revocable transfer-on-death deeds had been available, all of those clients could have used

> that much simpler method, and would not have been such easy prey for the trust salespeople.
>
> As time has shown, often these predators offer trusts only to obtain financial information later used to pressure the seniors to buy products or services that are entirely inappropriate under the circumstances.
>
> Even the seniors who deal with reputable attorneys are using significant amounts of their limited incomes paying for living trusts that wouldn't be necessary if California allowed beneficiary deeds.

Exhibit pp. 3-4.

Ms. Shena also notes that she is the only attorney in her agency, which offers free services to 65,000 elderly. She argues that real property should be able to pass free of probate in most instances. "Probate is a highly complicated and expensive process that can take years; the court supervision it involves is unnecessary in nearly all of the cases I see. My office cannot handle probate cases because of the time involved. A beneficiary deed would help simplify and expedite the transfer of homeowners' property without forcing hairs to endure the costly and time-consuming probate process." Exhibit p. 4.

The communications attached at Exhibit pages 16-18 also urge the Commission to recommend adoption of TOD deed legislation.

Concern About the TOD Deed Concept

The California Land Title Association cautions that the TOD deed could lend itself to use by a real property owner without adequate counseling by an attorney or estate planner. No one wants to burden a real property transfer with unnecessary costs. While the TOD deed may be a way to cheaply and quickly transfer property, it may not be the safest or most reliable method of accurately ensuring the transferor's wishes are carried out as the transferor intended. "If a transferor saves $1,000 up front to convey his or her real property but another $10,000 is spent in attorney's fees after his or her death determining what was actually intended by the transferor, what has really been accomplished with the creation of a TOD deed process?"

CLTA also notes that historically, "fast and easy" conveyancing documents (such as a quit claim deed) are often the instrument of choice of con artists who prey on seniors and unsophisticated consumers. Because the quit claim deed is easy to use, cheap to record, and doesn't require the use of an attorney, it makes it easy for fraud to be perpetrated. CLTA expresses the concern that the TOD deed — because of the ease and simplicity of use associated with it — may lend

itself to similar abuse. The ease and simplicity of use, without benefit of legal or financial advice, "simply shifts much of the work in estate planning from the front end — where it belongs — to the back end of the process, long after the transferor is dead and his or her intent difficult to sort out."

CLTA strongly urges the Commission to request feedback from district attorneys, law enforcement officers, and other related groups on what they think about the use of the TOD deed in California and what the potential for misuse would be. The staff thinks this is a good idea, and we will seek their comments on any proposal the Commission may develop. Also, experience in other jurisdictions that have enacted TOD deed legislation may be instructive on this point.

Legislative Activity

In Memorandum 2006-16 the staff flags pending legislation — AB 2267 (Huff) — and suggests that the Commission monitor its progress. As introduced, the bill would have increased the value of real property that may be taken under the statutory affidavit procedure from $20,000 to $40,000. See Prob. Code § 13200. Because of the low values involved, that procedure is not currently a realistic alternative to the TOD deed.

The bill was amended on March 29 to increase the value of real property that may be taken under the statutory affidavit procedure to $100,000. If enacted, that could diminish the utility of an instrument such as a TOD deed in some instances.

Respectfully submitted,

Nathaniel Sterling
Executive Secretary

TRUSTS & ESTATES SECTION

THE STATE BAR OF CALIFORNIA

TO: Nathaniel Sterling, CLRC Staff (By E-Mail and Regular Mail)

FROM: Charlotte K. Ito
Steefel Levitt & Weiss
One Embarcadero Center, 30th Floor
San Francisco, CA 94111
Phone: (415) 403-3285
Fax: (415) 788-2019
E-Mail:cito@steefel.com

Date: April 5, 2006

Re: Beneficiary Deeds

ISSUE:

What is the requisite level of capacity for the execution of a beneficiary deed?

SECTION POSITION:

Two standards of capacity should apply. (1) To the extent a present interest in property is affected, DPCDA (the Due Process in Competence Act, Probate Code Sections 810-813) should apply. (2) To the extent the transfer occurs at death, the testamentary standard under Section 6100.5 should apply.

EXECUTIVE COMMITTEE VOTE:

13 votes in favor of 2 standards; 6 votes in opposition; 1 abstention. The 6 votes in opposition believed that only 1 standard, the testamentary standard, should apply.

ANALYSIS:

A beneficiary deed affects a present interest in property when its recordation causes a severance, i.e., if a joint tenancy with right of survivorship interest or community property with right of survivorship interest were to be severed. For example, assume that A and B are joint tenants in property with rights of survivorship. A executes a beneficiary deed in favor of C in the event of A's death. B executes a beneficiary deed in favor of D, in the event of B's death. The joint tenancy is severed, and C and D each would hold 50% of the property upon the respective deaths of A and B, assuming there is no revocation.

ExComm was concerned whether each party would understand that he or she is giving up his or her survivorship right in the property. In the example above, by executing a beneficiary deed and thus

severing the joint tenancy, A gives up A's survivorship rights to B's interest, and B gives up B's survivorship rights to A's interest. ExComm concluded that to the extent the recordation of a beneficiary deed affects a present interest, DPCDA should apply. Conversely, if a present interest is not involved so that the beneficiary deed has no effect other than a transfer at death, ExComm believes the testamentary standard should apply.

ADDITIONAL COMMENTS:

- Adopt different nomenclature, i.e., a "Transfer on Death (TOD) Deed" or "Revocable Grant Deed". The term "Beneficiary Deed" implies that standards used for beneficiary designations apply.

- Address what happens if the Recorder's Office does not record the beneficiary deed immediately and the grantor dies after submission to the Recorder's Office but before recordation.

- Provide a means for spouses to convey the property jointly, whether held in joint tenancy with right of survivorship, community property with right of survivorship or community property without right of survivorship, upon the second spouse to die. Most spouses likely would assume that upon the death of the first spouse to die, the property would pass to the surviving spouse and upon the subsequent death of the surviving spouse to the beneficiary named on the beneficiary deed.

- Determine how restrictions or conditions can be placed on a grantee.

- Identify the parties who may revoke the beneficiary deed, i.e., the grantor or the grantor's conservator.

cc: By E-Mail:
Tracy M. Potts, Chair, State Bar Trusts & Estates Executive Committee
John A. Hartog, Vice-Chair, State Bar Trusts & Estates Executive Committee
Christopher M. Moore, Co-Chair, CLRC Subcommittee of the State Bar Trusts & Estates Executive Committee
James B. MacDonald, Vice Chair, Estate Planning Subcommittee of the State Bar Trusts & Estates Executive Committee

KINGS/TULARE AREA AGENCY ON AGING
3500 W. Mineral King, Suite A., Visalia, CA 93291
(559) 730-2553, (800) 321-2462, FAX (559) 737-4220
John M. Davis, Director

April 6, 2006

California Law Revision Commission
4000 Middlefield Road, Rm. D-1
Palo Alto, CA 94303-4739

Re: Support for Transfer-on-Death Beneficiary Deeds

To Whom It May Concern:

I request the Commission to recommend that the legislature adopt a statutory scheme establishing beneficiary deeds. This legislation would help avoid some of the most prevalent elder financial abuse (trust mills). In addition, it would help countless seniors and other low-income California residents to leave their modest estates (often consisting only of a home) to their heirs without the expense of probate.

As the only attorney at the Kings/Tulare Area Agency on Aging, and with no staff, I offer free services to 65,000 elderly here in Tulare and Kings Counties. On the best of days it is a daunting task, and there are many other lawyers throughout California who serve seniors as I do, with too little or no staff.

Helping Elders Avoid Exposure to Fraud & Financial Abuse: Over my 20 years in practice I have often seen expensive living trusts, bought from trust mills by senior clients. Some of the trusts were useless, and all of them cost the senior too much of his/her very limited resources. These elders simply wanted to pass their homes to their children outside of probate. If revocable transfer-on-death deeds had been available, all of those clients could have used that much simpler method, and would not have been such easy prey for the trust salespeople.

As time has shown, often these predators offer trusts only to obtain financial information later used to pressure the seniors to buy products or services that are entirely inappropriate under the circumstances.

Even the seniors who deal with reputable attorneys are using significant amounts of their limited incomes paying for living trusts that wouldn't be

necessary if California allowed beneficiary deeds. (Of course, the lawyers who prepare the trusts will argue to try to protect their income. I was a private attorney for most of my career, and I believe their concerns can all be satisfied. See the April 2005 position paper by David Mandel of Senior Legal Hotline, and any subsequent materials from him.)

Avoiding Probate Expense: Real property should be able to pass free of probate in most instances. Probate is a highly complicated and expensive process that can take years; the court supervision it involves is unnecessary in nearly all of the cases I see. My office cannot handle probate cases because of the time involved. A beneficiary deed would help simplify and expedite the transfer of homeowners' property without forcing heirs to endure the costly and time-consuming probate process.

A revocable transfer-on-death deed would be especially helpful to California's seniors, who are often house rich and cash poor. Enabling them to transfer real property in a deed without the time and expense of creating a trust, or using some other non-revocable instrument, will provide them greater flexibility and control over their property.

Again, I ask that the Commission recommend that the Legislature enact law creating beneficiary deeds. This law will help cash poor elderly avoid fraud and financial abuse, hand down their property to their families, and help their families avoid the expense and complication of probate.

Very truly yours,

Sarah Shena
Attorney at Law

Cc: Assemblymember Chuck De Vore

CLTA California Land Title Association
SINCE 1907

April 19, 2006

Nat Sterling
California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

RE: Beneficiary Deed/Transfer on Death Deed Study by the CLRC

Dear Nat:

First of all, thank you very much for requesting comment from the California Land Title Association which represents the title insurance industry in California.

The Statutory Charge of the CLRC is to Analyze if the Beneficiary Deed/Transfer on Death Deed is a Necessary Device in California:

In preparation for a CLTA response, we first revisited the legislation, AB 12, to refresh our memories regarding what is, and is not, the charge of the CLRC's study in regards to the transfer on death deed (TOD deed) study.

We would like to bring attention to an important reference in the bill found in Section 1 (a) which reads as follows:

> "The ***objective of the study*** shall be to determine ***whether legislation establishing beneficiary deeds should be enacted*** in California." [Emphasis added]

We are citing this reference in the bill to stress that the charge of the CLRC study is to determine if a TOD statute is necessary and in the best interests of California's real property consumers, lenders, title companies, and other interested parties.

It should not be presumed that such a deed is necessary or that the CLRC charge is to create such a statute absent a strong finding that such a device is essential to real property consumers. Given that these devices may have a profound effect –much of it potentially negative—should all give us all pause as we contemplate such a dramatic change to real property law in California.

Creating Actual Bill Language at this Time Creates an Impression that Statutory Language Will be Offered to the Legislature Irrespective of Whether or Not the TOD Deed is Necessary:

As CLTA staff read the March 29th document generated by the CLRC staff (Entitled "Beneficiary Deeds (Discussion of Issues)," we assumed that most of the CLRC staff efforts have been in the creation of proposed statutory language and very little time appears to have been spent

analyzing whether ***existing*** transfer and conveyancing documents or other means of easily conveying real property, such as a trust, fail to serve real property consumers.

In fact, it would appear that much of the CLRC time and effort has been spent in drafting of actual TOD language rather than reviewing the existing law relative to abbreviated transfer options.

As participants to the early deliberations of AB 12 (and the subsequent committee analyses on the bill as it progressed through the legislative process), we can testify that the TOD deed analysis was steered by CLTA and others to the CLRC in order for a deliberative and well respected body—such as the CLRC—to actually review the existing state of the law in this area and to make an unbiased determination what changes, if any, should take place in California law relative to the TOD deed.

Given that much of the recent CLRC paper seems to be spent actually drafting new proposed statutory language and an analysis of that language, we believe that the CLRC efforts are putting the proverbial cart before the horse.

While we understand the desire to have some language in front of the CLRC to discuss potential issues and to drive the debate, we have serious concerns about the CLRC staff drafting and "improving" language at this time. This effort signals to the CLTA that the TOD deed has already been embraced by the Commission itself without a thorough analysis or study of existing law having been conducted to determine if such a new conveyancing document is actually necessary.

From the perspective of CLTA, we believe it behooves the CLRC to step back from this process and revisit the charge of AB 12: to study whether or not a TOD deed is a good idea. In other words, refocus the debate not on "how best can we develop a TOD deed," but rather, "should develop a TOD deed at all."

In order to do that, the CLRC would first need to analyze traditional methods of conveying real property: Grant deeds, quit claim deeds, trusts, etc., to determine how those methods, documents and processes are working and what problems have arisen for senior citizens and others looking for a process that is as simplified and cost effect as possible.

Are Existing Conveying Documents a Problem if Educational Opportunities are Provided?:

CLTA posits this question: "Are existing conveyancing documents and processes inadequate or are unsophisticated transferors simply not getting all the information they need to easily, cheaply, and safely convey their real property to others and avoid probate?"

Assuming that the common goal of all interested parties is to make sure real property consumers can easily, quickly, and cheaply convey real property to others, is it absolutely necessary for us to change the existing laws on the books to accomplish this goal? Perhaps all of us should be considering whether or not our efforts would be better spent on urging the Legislature to create better educational opportunities and outreach to seniors and unsophisticated real property consumers on how best to safely and accurately convey their real property according to their wishes by using existing resources and better understood conveyancing documents to achieve these goals..

Let us all tread lightly as we explore all of the positive and negative implications of a TOD deed in California and whether or not existing laws –with enhanced educational opportunities for seniors and other parties—might be a less hazardous path to take then creating what might be viewed in hindsight as "drive through deeds" that harm those we seek to protect: seniors and unsophisticated real property owners.

The Simplicity of the TOD Deed is Both a Blessing and a Curse:

To proponents of the TOD deed, the beauty of the TOD is that it is simple and (arguably) does not require the use of an attorney or estate planner. To opponents, the risk of such a device is that it is simple and does not require the use of an attorney or estate planner. Thus, whether or not the quickness and brevity of this conveying device is a blessing or a curse depends on your perspective.

While there are some arguments in favor of providing a "fast and easy" way for some consumers to easily, quickly and cheaply convey real property to another party without the oversight and counseling of an attorney and estate planner, CLTA would caution that the loss of this oversight will in many cases result in disaster that might have been avoided had and estate planner or attorney reviewed the documents and counseled the consumer PRIOR to their use of this document.

Nobody, including CLTA or the title industry, wants to burden real property consumers with any additional costs in order for them to convey real property to another person. However, many times a more thoughtful and contemplative approach will save a consumer from negative consequences they would never had considered in a more abbreviated and expedited approach.

Thus, "fast and easy" is often not a good way to address the transfer of a consumer's most valuable asset: their real property While the TOD deed may be a way to cheaply and quickly transfer property, but it may not be the safest or most reliable method of accurately ensuring the transferor's wishes are carried out as he or she intended.

If a transferor saves $1,000 up front to convey his or her real property but another $10,000 is spent in attorney's fees after his or her death determining what was actually intended by the transferor, what has really been accomplished with the creation of a TOD deed process?

The CLRC Would be Wise to Seek Feedback from District Attorneys and Others Who Combat Real Property Fraud in California:

In numerous discussions over the years with the California District Attorneys Association, law enforcement officers and those who combat elder abuse, existing "fast and easy" conveying documents –such as quit claim deeds—are often the instrument of choice among con artists who prey on senior citizens and unsophisticated real property consumers. Because the quit claim deed is easy to use, cheap to record, and doesn't require the use of an attorney, it makes it very easy for fraud to be perpetrated against consumers.

CLTA strongly urges the CLRC to request feedback from district attorneys, law enforcement officers, and other related groups on what they think about the use of TODs in California and the potential for misuse would be.

Like quit claim deeds, TOD deeds will often be filled out and recorded without the benefit of an independent third party overseeing the execution and recording of these documents. Certainly, quit claim deeds are essential tools for title companies and others to accomplish certain goals, but the brevity and ease of using such documents lends itself to abuse in the wrong hands and the targets of such abuse will often be senior citizens and unsophisticated real property owners.

While we see that the CLRC is examining important issues such as "capacity" and other pitfalls associated with the TOD deed, we would argue that all of those discussions highlight that the so-called "ease" and "simplicity" attributed to the TOD deed by it's proponents simply shifts much of the work in estate planning from the front end—where it belongs—to the back end of the process, long after the transferor is dead and his or her intent difficult to sort out.

What is accomplished if attorneys, courts, and interested parties are spending tens of thousands of dollars to unwind and interpret exactly what the transferor intended, just so he or she can avoid establishing a trust or seeking legal and financial advice?

The TOD Process Ironically Turns the "First in Time, First in Right" Recording Rules on Their Head and Undermines "Constructive Notice":

Under California law, the well established "first in time, first in right" rule urges all parties with a vested interest in real property in question to record documents establishing this interest *as soon as possible*.

In other words, if you want to protect your rights as a lienholder, lender, real property owner, etc., you are urged to record the document establishing this right and security interest as soon as possible to ensure no intervening liens, encumbrances, or other interests will trump your right by having an earlier priority established by the earlier recordation date. This ***constructive notice provided through the recording process is essential*** to put the world on notice that the real property interests exist.

Since the last recorded TOD deed would have "priority" over earlier recorded documents, arguably, the TOD deed process contemplated by the CLRC would create a perverse ***incentive for a party with a TOD deed to record their interest last***, especially if there are multiple, conflicting TOD deeds or other deeds that exist. Having multiple TOD deeds would hardly be a unique situation given the past scenarios the title industry has witnessed when family members fight over real property left behind and multiple promises were made to different relatives and heirs over the years.

While the CLRC staff suggests recordation should take place before the transferor dies, this requirement could easily be addressed by the beneficiary by racing to the recorder's office ***right before the transferor dies*** without any appreciable constructive notice being provided to interested parties. This lack of constructive notice will result in innocent buyers, lenders, creditors, title companies and others being harmed by what they assume is title free and clear of any previously recorded interests.

Thus, the rule that the last recorded TOD deed wins, is really a "last in time, first in right" rule that runs completely contrary to well established recording laws in California and establishes a potentially negative precedent for recorded documents that will undermine the certainty of existing recording rules.

Problems surrounding this proposed new "last in time, first in right" rule are exemplified by the following fact pattern: Transferor A has filled out and recorded two separate TOD deeds, each conveying her fee simple interest to two different people. While the *last recorded* TOD deed would "trump" the other TOD deed simply *because it was recorded last,* it is clear from its face that it was actually filled out two years earlier, but for whatever reason, it was only recorded recently just before the Transferor died. From this example, clearly the transferor intended to have the last created TOD deed dictate the transfer, but the recording date would be controlling, completely undermining her intent.

Thus, the proposed "last in time, first in right" rule would create a very perverse outcome in this situation.

Because of these reasons, CLTA believes that the TOD deed process –and the new recording rules-- could create a very negative precedent for constructive notice in California and result in a transferor's intent being undermined.

Furthermore, as real property owners get older and older, it often becomes more difficult to keep track of previous legal steps that have been taken over the years. People simply forget what they, or other owners of the real property, have done. Requiring transfer documents to be recorded ASAP to create a discoverable chain of events is another reason to leave the existing "first in time, first in right" process alone.

TODs Severing Joint Tenancy May Have Disastrous Effect:

Proposing that the TOD, recorded after the creation of a joint tenancy, would sever a joint tenancy may have negative effects for many transferors who did not intend to have the TOD accomplish that goal.

The question before the CLRC is this: "What will real property owners and transferors know about the TOD document if it is introduced in California?"

Unfortunately, in many instances the transferor may know very little about the effect of the TOD document. This will be especially true if the consumer/transferor has never discussed what the recordation of a TOD will do with an attorney or estate planner.

Ironically, the joint tenancy with right of survivorship vesting has traditionally been a default option for many couples seeking to avoid probate and have the real property immediately vest in the surviving spouse or partner. The advent of the TOD, used improperly, could have a very negative effect on an option that has worked rather well over the years and is very simple to understand.

The Uncertainty of What a Transferor Intended May Force Many Title Companies to Get Further Documentation as to Intent:

Reliance by title companies on the official recorded chain of title on real property affords some protection from liability and the ability to more quickly help in the transfer of real property and the issuance of title insurance to protect lenders and consumers. However, given that title companies are providing insurance and have different underwriting guidelines, it is possible that the ambiguities surrounding the TOD deed process—as evidenced in other states—will require title companies to require sellers (now the owners of the real property transferred by the transferor under a TOD deed) to get further "off record" documentation before title insurance will be offered. In some cases, this kind of documentation will be difficult or impossible to obtain and may require a quite title action to clear the title on the real property.

If a quiet title action is required, this can run into the tens of thousands of dollars for heirs that would have been much better off if the transferor had undertaken estate planning steps on the front end of the process.

Other comments from other states have been included in the CLTA response:

Attached are comments from other states in which title companies are dealing with the TOD deeds.

Many of the issues, confusion, and potential problems have been highlighted in the CLRC report. For instance, (1) Multiple TOD deeds with conflicting provisions; (2) Beneficiaries who believe they have a vested interest before the transferor dies; and (3) Transferors who are using the TOD deeds without fully understanding the implications of executing and recording such a document.

Respectfully,

Craig C. Page
Vice President
and Legislative Counsel

Arizona has had a beneficiary deed statute since 2001. It was amended in 2002 and an additional amendment has been proposed to the Arizona legislature this session by the Land Title Association of Arizona, of which I am legislative committee chair. By separate Smartfax, I will be sending you (1)the statute, which contains the original version and the current one, so you can compare the changes, (2) the legislative summaries regarding the changes and (3)various news articles that were published when the statute was first implemented. These should give you a flavor for the bill and some of the issues that have arisen.

There are only two other issues of which I'm aware. First, beneficiaries who take title via a deed think the deed vests in them automatically without the need to record a death certificate. While the statute does not specifically require a death certificate, it does, of course, require that the grantor be dead and the only way of record to demonstrate that is to have the death certificate recorded. Thus, it becomes a title company requirement.

Second, an issue arises when the beneficiary pre-deceases the grantor. At least one company has faced the issue of determining whether the deed fails or whether the property passes to the heirs of the deceased beneficiary. This is the issue LTAA is attempting to remedy this session. Our (hopefully) easy fix is to add a box to the statutory form of deed whereby the grantor can check off whether he wants the deed to "___become null and void; or ___become part of the estate of the grantee beneficiary" if the beneficiary pre-deceases him/her. Interestingly, the Probate Section of the State Bar was aware of this issue when it drafted the initial statute and chose not to address it on the assumption that lawyers drafting these deeds for their clients would address the issue. There are two flaws with that assumption: (1) lawyers aren't doing it

and (2) the deed is available at stationary stores, so many times lawyers aren't involved in preparing the deeds.

Most issues with the deed occurred prior to the 2002 amendments. They involved (1)what happened if the grantor conveyed or encumbered the property after recording a beneficiary deed, (2)did the grantor have to get the consent of, or otherwise notify, a beneficiary of the deed, especially if it conveyed to the beneficiaries as joint tenants, (3)what happened when the property was held by the grantor(s) in joint tenancy and (4) how to designate successor beneficiaries.

The biggest issue for title companies was the conveyance/encumbrance issue. Prior to the 2002 amendments, companies were requiring that any beneficiary deed of record be revoked prior to selling or encumbering property. This is because no one was sure what effect the deed had on the title. The 2002 amendment cured this problem by providing that the beneficiary deed was subject to "all conveyances, assignments, contracts, mortgages, deeds of trust, liens, security pledges and other encumbrances made by the owner or to which the owner was subject during the owner's lifetime." Thus, the owner could continue to deal with the property as if the deed did not exist and, when the grantor died and the beneficiary came into title, he took with all voluntary/involuntary encumbrances against the property up to that time. The amendment also effectively provided for an automatic revokation of the deed in the event the property was sold. As a result, I believe most title companies are no longer calling for revokations or showing the deed as a Schedule B exception in these situations. (See ARS 33-405.A.)

Consent was another issue because often the grantor would convey to spouses as joint tenants. This was an issue because Arizona is a community property state and the question was whether you needed the consent of the spouses prior to the grant. Attorneys were vehemently against providing notice on the grounds that it would be like providing heirs a copy of a will or beneficiaries a copy of a trust prior to the owner's death. Granted, the deed needed to be recorded, so there was a possibility that individuals could discover the deed anyway, but ultimately the attorneys won out and a provision was included indicating that the beneficiary did not need to be notified of the deed. To address the joint tenancy issue, since a grantor cannot eliminate a community property right of a spouse simply by so stating in a deed, I believe most title companies require the spouses to sign an acceptance of the joint tenancy at the time they attempt to deal with the property following the death of the grantor. (See ARS 33-405.I.)

Successor beneficiaries were permitted under the original law. The problem was that there was nothing in the statute requiring the grantor to specify under what conditions the successor was to come into title. ARS 33-405.C addressed that concern, requiring the grantor to state the conditions on which title in the successor would vest.

As for grantors holding as joint tenants, several statutory changes were made to clarify the conditions under which one grantor could convey by beneficiary deed and the situations under which such a deed, executed by one or more joint tenants, would become effective or could be revoked.

One issue that does occasionally crop up now is when grantors or attorneys drafting the deed do not specifically name the beneficiary but, instead, use terminology like "the heirs of" the grantor. In this case, probate may still be necessary to verify who the heirs are. This may also be a problem with the statutory "fix" noted above since, if the grantor checks the box indicating that the property passes to "the estate" of the beneficiary, some form of "heir" verification may still be necessary.

One other related change in Arizona law. Upon a conveyance of property, an Affidavit of Value must be recorded unless certain exemptions apply. When the beneficiary deed statute was passed, an exemption was added to this statute for such deeds.

Other questions I've had come up and my general responses (whether indicative of the LTAA or not, I can't say):

1. Is a disclaimer deed needed for property conveyed to one spouse? In Arizona, property is considered community property unless it is conveyed "by gift, devise or descent." Since the beneficiary deed is intended to be a death transfer in lieu of probate, I believe it would fall within the statutory exception and no disclaimer deed should be needed for the beneficiary to convey or encumber the property.

2. Can the beneficiary be an entity? The statute doesn't limit the deed to individuals and, since a grantor could, by will, leave property to an entity like a non-profit corporation, I believe a corporation could be a beneficiary.

3. How do multiple grantees hold title if the grantor fails to specify? Probably as tenants in common, just like any other deed that fails to specify the manner of holding title.

You will see that our statute addresses the manner of revokations, designation of multiple beneficiaries, transfers to a trust, effect of multiple deeds on the same property and effect of a will. It also provides very simple statutory forms for the deed and for revokations.

Bottom line - with the 2002 revisions, I think the beneficiary deed is working pretty well - at least, we haven't seen significant issues, other than the one LTAA is trying to fix this session. I think the bill is pretty comprehensive.

If you have any questions after reviewing this e-mail and the materials I'm e-mailing by separate "cover," please do not hesitate to call me.

BENEFICIARY DEEDS: POTENTIAL & PROBLEMS

By Susan M. Ciupak, Esq. and Joshua Forest, J.D. of Fennemore Craig, P.C.

As of August 9, 2001, those wishing to pass real state upon their deaths have a new option, the eneficiary Deed. Through House Bill 2280, found rospectively in Arizona Revised Statutes § 33-405, the egislature has provided a means for conveying an nterest in real property effective only upon the death of ne grantor. Without giving up any present possessory r ownership rights (such as with property held in joint enancy with right of survivorship (JTWRS) or community property with right of survivorship (CPWRS)), rantors can now make valid, revocable, testamentary ransfers of property using the Beneficiary Deed. The grantor may convey a Beneficiary Deed to any lawful enancy, entity, or trust (including revocable trusts). The grantor may also transfer the property to be held as enants in common, community property, or any other enancy. Such designation, however, is not binding on he grantees and may be changed at will after the death of the grantor. The Beneficiary Deed was also added as an additional exemption under A.R.S. § 11-1134, and hus an Affidvait of Value is not needed to record the Beneficiary Deed.

The grantor may convey a Beneficiary Deed even if he grantor holds less than complete ownership, or holds the property in JTWRS or as CPWRS with others. In the survivorship situation, the Beneficiary Deed will not take effect until the death of the last surviving owner. Further, in order for the transfer to be valid, all of the owners under the JTWRS or CPWRS must grant the Beneficiary Deed, or the grantor of the Beneficiary Deed must survive the other co-owners. Apparently, the grant of a Beneficiary Deed by a JTWRS or CPWRS property owner is to be treated as a provisional conveyance to take effect upon the grantor's death in the event that the grantor is the surviving co-owner. Unlike other conveyances, it appears that the legislature did not intend for the grant of a Beneficiary Deed to destroy the existence of a JTWRS or CPWRS.

Essentially, there are only two requirements for conveying a Beneficiary Deed. First, the deed must be recorded and executed according to the laws of the official county recorders office. Second, the deed must specifically state that it is not to take effect until the death of the owner. The Beneficiary Deed may also be revoked at any time, so long as the revocation is recorded. Any co-owner may revoke a Beneficiary Deed, however, all co-owners must revoke, if more than one has granted the Beneficiary Deed, to completely revoke all of the grantee's contingent interest. According to House Bill 2280, if multiple Beneficiary Deeds are granted, the last to be recorded controls. All Beneficiary Deeds and revocations must be recorded before the death of the last surviving grantor in order to be valid.

The Beneficiary Deed is not without its pitfalls or perils. Some of the anticipated problems that have been raised by title companies and real estate attorneys are:

- It may not be clear to title researchers and others viewing the records that the interest does not exist until the grantor's death.
- A Beneficiary Deed grantee may be mistaken as a remainderman.
- Revocation by only one co-owner may leave uncertain the extent of the revocation.
- Revocation by a non-granting co-owner may cloud the grantee's interest.
- Subsequent addition of a party as owner (for example, a second marriage) after granting of Beneficiary Deed, may call into question the grantee's rights.
- There is no requirement of filing the death certificate or otherwise proving the death of the grantor.
- A potential conveyance of a Beneficiary Deed to unborn grantees brings into question the validity of the transfer, who holds the property in the interim and the potential application of the Rule Against Perpetuities.
- There is potential uncertainty pertaining to whether the conveyance of Beneficiary Deed transforms a joint tenancy with right of survivorship into a tenancy in common.
- There is potential confusion concerning the delay or failure to record, and subsequent grants of Beneficiary Deeds.

EX 14

- There is potential litigation concerning the subsequent recording of a prior grant of Beneficiary Deed, as the legislation provides that the last recorded grant prevails.
- Whether a foreclosing party must give notice of foreclosure to a grantee beneficiary.

Because of these and other potential complications, various title companies have stated that they will refuse to issue Beneficiary Deeds and that they will require owners to revoke Beneficiary Deeds before selling or refinancing the property.

So who is best suited to use a Beneficiary Deed? The Beneficiary Deed is most effective when there is only one owner of the property or all owners agree on who should be designated as beneficiary. If the grantors should wish to change the grantee, they should revoke any prior Beneficiary Deeds. Additionally, the deed is best used when the grantor does not anticipate refinancing or further mortgaging the real property. In short, Beneficiary Deeds are ideal for smaller estates wishing to avoid probate and associated costs, such as a single parent with a modest estate leaving the property to children at death. The Beneficiary Deed does not provide for posthumous control of the property, as would a trust, but does transfer ownership at death in an uncomplicated manner. There may be a relatively small niche best suited for the Beneficiary Deed, but it appears the Beneficiary Deed can be an effective, inexpensive estate planning tool when used correctly. ▲

March 28, 2006

California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

I would like to notify the Commission that I want California to have a law that would allow the homeowner to transfer the home at the time of death in a Revocable Transfer-on-Death Beneficiary Deed. This would help homeowners who cannot afford a trust, or who do not want a trust, and who want to protect their loved ones from the expenses of Probate. It would prevent elder abuse. It would help the Beneficiaries avoid expensive Capital Gains Taxes. We must work to defeat the actions of AB 12 opponents.

Thank you for your consideration.

Maria D. Faur

Maria D. Faur
200-B Avenida Majorca
Laguna Woods, CA 92637

REVOCABLE TRANSFER-ON-DEATH BENEFICIARY DEED

This Petition will be mailed to the CALIFORNIA LAW REVISION COMMISSION, 4000 Midlefield Road, Room D-1, Palo Alto, CA 94303-4739.

Signers of this Petition request that the Commission recommend to the California Legislature the enactment of a new law that would allow Californians to transfer real estate to a benficiary on the death of the property owner without probate. Several states have such a non-probate real estate transfer law.

This REVOCABLE TRANSFER-ON-DEATH BENEFICIARY DEED would allow the homeowner to avoid the expenses of Probate, a Trust, and Capital Gains Taxes.

The first name is to be used as an example.

NAME:	ADDRESS
1. Mary Pat Toups: Mary Pat Toups	3467B-Bahia Blanca West Laguna Woods, CA, 92637
2. Ronald C. Hightower: RONALD C. HIGHTOWER	3700-A Via Buena Vista Laguna Woods Beach, CA 92637
3. A. George Parker: A. GEORGE PARKER	5308 CANTANTE LAGUNA WOODS CA 92637
4. Barbara Halbin: Barbara Halbin	632 Via Sevilla, Laguna Woods CA 92637
5. Neil W. Benner: Neil W. Benner	2051-D Via Mariposa E Laguna Woods, Ca. 92637
6. Suzanna Muccia: SUZANNA MUCCIA	[illegible] Laguna Woods Ca.
7. Frances J. Thomas Trust: Frances J. Thomas Trust — Thomas Fry	3266 B San Amadeo Laguna Woods CA 92637
8. Janice D. Kerr: Janice D. Kerr	2177-O Via Puerta Laguna Woods CA 92637
9. Ruth M. Belew: Ruth M. Belew	2176 "S" Via Puerta Laguna Woods CA 92637
10. DOROTHY E. REILLY: Dorothy E. Reilly	2176 VIA PUERTA LAGUNA WOODS, CA 92637

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The first name is to be used as an example.

	NAME:	ADDRESS
1.	Mary Pat Toups Mary Pat Toups	3467B-Bahia Blanca West Laguna Woods, CA, 92637
2.	Annie B Maner Annie B. Maner	3039-C Via Vista Laguna Woods, CA 92637
3.	Jefferson G. Maner Jefferson G. MANER	3039-C Via Vista Laguna Woods, CA 92637
4.	Shirley Witt Shirley WITT	31391 EL Horno ST SJC 92675
5.	Sandra A Ito Sandra A. Ito	29921 Aberdin Court Laguna Niguel, CA 92677
6.	Jeanette Garcia JANET GARCIA	P.O. Box 1656 L.F 92609 3127 Via Serena N
7.	Janet Garcia	Laguna Woods CA 92653
8.	Margaret Naylor MARGARET NAYLOR	33852 Del Obispo #36 Dana Point CA 92629
9.		
10.		

Law Revision Commission
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