

First Supplement to Memorandum 2006-19

Beneficiary Deeds (Material Received at Meeting and Additional Communications)

At its meeting on June 22, 2006, the Commission received the Memorandum of Charlotte Ito of the State Bar Trusts & Estates Section (6/21/06) attached as Exhibit pages 1-7.

The Commission has also received the petition of eight signatories concerning Revocable Transfer on Death Beneficiary Deeds (undated), attached as Exhibit pages 8-9. The petition requests the Commission to recommend enactment of TOD deed legislation.

The Commission has received a communication from David Mandel of Senior Legal Hotline. Mr. Mandel indicates that his comments attached to Memorandum 2006-19 at Exhibit pages 19-21 contain a garbled sentence. The third paragraph on Exhibit page 21 should read:

If the TOD deed takes effect upon the death of the first joint tenant, its beneficiary would immediately become a tenant in common with the surviving former joint tenant, despite, in most cases, having no equitable interest in the property. The former joint tenant's stake in the property during her or his remaining years would be vulnerable to the new co-owner's debts; a refinance on terms available to low income seniors may be unavailable, as would a reverse mortgage that might be the only way s/he could afford to remain in the home. A reassessment for property tax purpose might occur, straining the survivor's resources. In the worst cases (and we have seen these), the new co-owner could turn into an abuser whose co-ownership rights force the senior out of the home.

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
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Date: June 21, 2006

Re: Revocable Transfer on Death Deeds

ISSUES:

1. What is the appropriate waiting period for the transfer of property pursuant to a transfer on death ("TOD") deed?
2. May a contestant file a contest as soon as he or she learns about the TOD deed or must the contestant wait until after the transferor's death to file a contest?
3. May a TOD deed be challenged pursuant to a substituted judgment proceeding during a conservatorship?
4. What is the appropriate statute of limitations period?
5. What are the grounds for contest?
6. Should Probate Code Section 850 be expanded to cover contests of **any** nonprobate transfer authorized by Section 5000?
7. Should a TOD deed be subject to creditor claims?
8. Should a TOD deed be subject to claims from an omitted spouse or child?
9. Should property subject to a TOD deed be included as part of the decedent's estate for protection of omitted spouses and children?
10. Should a TOD deed be subject to the family allowance and probate homestead provisions?
11. Should property subject to a TOD deed be included as part of a conservatee's estate?

12. Should property subject to a TOD deed be subject to recovery by the department of Health Services?
13. Should a conservator be able to sell property subject to a TOD deed?

SECTION POSITIONS:

1. There should be a 120-day waiting period before the successor in interest of a TOD deed may seek the transfer of the interest.
2. There is no right to contest a TOD deed during the grantor's lifetime.
3. A conservator may challenge a TOD deed pursuant to a Probate Code Section 2580 petition for substituted judgment.
4. The statute of limitations period should be 3 years after the transferor's death or 1 year after recording the affidavit of death.
5. The grounds for contest may include but are not limited to lack of capacity of the transferor, improper execution or recordation, invalidating cause for consent to a transfer of community property, and transfer to a disqualified person.
6. Probate Code Section 850 should be available for the TOD deed.
7. TOD deeds should be subject to creditor claims under the alternate approach recommended by the CLRC Staff, that is, to incorporate existing California liability concepts for a successor that takes a decedent's property without probate under small estate or spousal affidavit procedures. The beneficiary may return the property to the estate to be free of personal liability. A TOD deed is subject to abatement in the same class as a specific gift.
8. The omitted spouse and child provisions should apply to TOD deeds.
9. Property subject to a TOD deed should be included in the decedent's estate for purposes of protecting omitted spouses and children under Probate Code Sections 21600 – 21630.
10. Property subject to a TOD deed should not be subject to the family allowance and probate homestead provisions.
11. ExComm recommends adoption of the CLRC Staff's position that property subject to a TOD deed be included in the conservatee's estate.

12. ExComm agrees with the CLRC Staff's position that property subject to a TOD deed be subject to recovery by the Department of Health Services.

13. A conservator should have the authority to sell property subject to a TOD deed.

EXECUTIVE COMMITTEE VOTE:

1. 14 votes in favor of and 3 votes in opposition to a rule requiring a 120-day waiting period after the death of the TOD deed grantor before the successor in interest may seek the transfer of the real property to himself or herself.

2. 15 votes in favor of and 2 votes in opposition to a prohibition of a contest of a TOD deed during the grantor's lifetime.

3. Unanimous vote in favor of allowing a conservator to challenge a TOD deed in a petition for substituted judgment under Probate Code Section 2580.

4. Unanimous vote in favor of the 3 year statute of limitations period after the transferor's death and 1 year after the beneficiary's recordation of the affidavit of death.

5. Unanimous vote in favor of adopting the CLRC Staff's proposal to include the following as grounds for contest: lack of capacity of the transferor, improper execution or recordation, invalidating cause for consent to a transfer of community property, and transfer to a disqualified person.

6. Unanimous vote in favor of expanding Probate Code Section 850 to cover contests of TOD deeds.

7. Unanimous vote in favor of adopting the CLRC Staff's alternate approach so that TOD deeds do not have a level of creditor protection not available to other nonprobate transfers. The TOD deed would be subject to abatement in the same class as a specific gift.

8. 7 votes in favor of and 10 votes in opposition to disallowing claims from an omitted spouse or child.

9. 10 votes in favor of and 5 votes in opposition to including property subject to a TOD deed in the decedent's estate for family protection purposes.

10. 3 votes in favor of and 11 votes in opposition to subjecting property subject to a TOD deed to the family allowance and probate homestead provisions.

11. Unanimous vote in favor of the CLRC Staff's position that property subject to a TOD deed be included in the conservatee's estate.

12. Unanimous vote in favor of the CLRC Staff's position that property subject to a TOD deed be subject to recovery by the Department of Health Services.

13. Unanimous vote in favor of providing authority to a conservator to sell property subject to a TOD deed.

ANALYSIS:

1. **Waiting Period.** The interests to be balanced in determining a meaningful waiting period before effecting the transfer of interest after the death of the TOD deed grantor are (a) the marketability of property and (b) the ability of individuals to file a contest against the TOD deed. That is, on the one hand, a long waiting period adversely affects the marketability of the property. On the other hand, if the waiting period is too short, there would be no protection afforded to contestants.

The 6 month period for nonprobate transfers of real property was perceived to adversely affect the marketability of the property, and the 40-day period for small estates was deemed too short a period for potential contestants to evaluate the merits of a contest much less file a petition in Probate Court. The most relevant waiting period was determined to be 120 days, consistent with the waiting period of a foreclosure or redemption action.

2. **Prohibition Against Contests During the TOD Deed Grantor's Life.** With the exception of a substituted judgment proceeding during a conservatorship, wills and revocable trusts generally may not be challenged during the life of the testator or settlor. Because a TOD deed, like a will or revocable trust, is revocable, it should be subject to the same rule. Furthermore, because a TOD deed, unlike a will or revocable trust, must be recorded and therefore easily discovered pre-death by potential contestants, the rule prohibiting contests during the grantor's life should be made explicit lest pre-death contests be encouraged.

3. **Petition for Substituted Judgment.** A conservator should be allowed to challenge a TOD deed consistent with the provision allowing a conservator to challenge a will or revocable trust pursuant to a substituted judgment petition under Section 2580.

4. **Statute of Limitations.** ExComm fully agrees to the CLRC Staff's proposal of a statute of limitations of 3 years after the transferor's death or 1 year after the beneficiary establishes the fact of the transferor's death under the procedure provided in Chapter 2 (commencing with Section 210) of Part 4 of Division 2.

5. **Grounds for Contest.** The CLRC Staff's proposed comment regarding grounds for contest would be useful. Because the grounds for contests of instruments is well-developed, however, new legislation should not include a section that purports to establish the grounds for contest. The CLRC

Staff's proposed section modeled on Probate Code Section 5015 makes clear that the well-developed law of contests is not being altered.

6. **Probate Code Section 850.** ExComm agrees with the CLRC Staff that Probate Code Section 850 was an established and reasonably expeditious procedure for contesting a TOD deed. It also has the benefit of bringing the action into the probate department (in most cases), which is well-suited to dealing with the competency and undue influence issues that will be raised in TOD deed contests.

7. **Creditors' Claims.** ExComm concurs with the CLRC Staff's comment that the "treatment of the decedent's creditors has emerged as a major concern" as a result of the increased use of nonprobate transfers. There is no consistency in the treatment of creditors rights with respect to the different forms of nonprobate transfers. ExComm believes that this issue needs to be addressed in a global and comprehensive manner rather than with a piecemeal approach.

With respect to the rights of creditors during the transferor's life, ExComm agrees with the proposal advanced by the CLRC Staff and has no other comment in this regard. With respect to the rights of creditors after the transferor's death, ExComm believes that the CLRC Staff's adaptation of the Uniform Probate Code for application to TOD deeds raises a significant concern. Specifically, the UPC provision creates a claim hierarchy by requiring exhaustion of a transferor's estate and trust before TOD deed property can be reached by creditors. Thus, this proposal would provide TOD deeds with a level of creditor protection not available to nonprobate transfers to revocable trusts. ExComm does not believe this differential treatment is justified and believes that adoption of this hierarchy may have the unintended effect of encouraging the use of TOD deeds as a creditor protection device.

The disparate treatment of nonprobate transfers is magnified by the absence of a comprehensive approach to creditors rights. By way of example, POD accounts are not expressly made subject to the claims of creditors. Thus, with respect to creditors' rights, a transfer through a POD account may be treated differently than a transfer by TOD deed.

For these reasons, ExComm recommends that the CLRC Staff's alternate approach be adopted, that is, to incorporate and adapt existing affidavit procedure provisions for application to the TOD deed. Until a global solution to the creditors' rights issue is implemented, ExComm believes this alternate approach is preferable to adopting a modified version of the UPC.

8. **Rights of Family Members.** ExComm agrees with the CLRC Staff that the nonprobate transfer instrument is subject to the statement of title in the record and that family protection statutes need to be globally addressed in light of the nonprobate revolution, and not on a piecemeal basis. ExComm believes that the omitted spouse and child provisions should be extended to the TOD deed.

9. **Family Protection.** Property subject to a TOD deed is similar to property funded in a revocable living trust and should therefore be included within Probate Code Sections 21600-21630.

10. **Family Allowance and Probate Homestead.** ExComm agrees with the CLRC Staff position and shares the frustration of addressing each nonprobate transfer instrument on a piecemeal basis. The problems related to nonprobate transfer instruments and creditor rights against nonprobate assets need to be addressed globally.

11. **Subsequent Incapacity of Owner.** The CLRC Staff's analysis of the problem created when a grantor becomes incapacitated after creation of a TOD deed is complete and accurate. If a conservator believes fraud or undue influence was a factor in creation of the deed, the conservator would proceed using the same remedies that are available now to deal with a suspect will, trust or conveyance. Incapacity of the grantor may well make the problem more difficult to resolve, but the problem is the same whether the questioned document is a will, a trust, a beneficiary designation on an IRA or insurance policy, or a TOD deed.

A practical difficulty for a conservator may occur if the conservator wishes to sell real property which is subject to a TOD deed, but the same problem occurs fairly frequently when a conservator wishes to use funds held in an account bequeathed to a particular beneficiary, or subject to a TOD designation. As the CLRC Staff commented, under Probate Code Section 2580 *et seq*, the conservatee's plan must be taken into account and notice provided to the intended beneficiary. These are practical problems that the courts resolve routinely.

Perhaps it is inconsistent (as the CLRC Staff comments) that an attorney in fact can, with express authorization in the instrument, modify the principal's trust or beneficiary designation but cannot modify principal's will, but we have lived with these rules for a long time. If a TOD deed form is authorized, Probate Code Section 4264 should be amended to include revocation of TOD deeds, or sale or property subject to a TOD deed. A section similar to the Missouri statute should also be added to the Probate Code.

12. **Effect of TOD Deed on Medi-Cal Recovery.** The CLRC Staff memorandum is correct in that a property that belongs to the Medi-Cal recipient at the time of the recipient's death is subject to recovery for medical services provided and certain other personal care services under the present legal and regulatory scheme established in federal law (42 USC § 1396p(b)) and the proposed regulations released by OAL and not yet final (22 CCR §§ 50960-50965, Regulatory package R-32-00). The state can seek recovery against any property that passes by distribution or survival.

There are presently three statutes that require notification of the Department of Health Services on the death of a Medi-Cal recipient. Probate Code Section 215 requires "the estate attorney [sic], ... the beneficiary, the personal representative, or the person in possession of property" to notify the Director of DHS within 90 days of the death of a decedent who received Medi-Cal or who is the surviving spouse of a decedent who received Medi-Cal. The statute does not require all such persons to send the notification. Thus, a recipient of real property under a TOD deed does not have a legal

requirement to notify the Department. Probate Code Sections 9202 (probate administrations) and 19202 (trust administrations) incorporate Probate Code Section 215 language and require notification to the Department when the personal representative (Section 9202) or the trustee (Section 19202) knows that the decedent (or, in the case of probate, the predeceased spouse of the decedent) or settlor, was a Medi-Cal recipient. SB 1197 (Soto) seeks to address problems of harmonization and inconsistencies among these statutes.

Recovery against property that passes to a TOD beneficiary would come under Section 215 since the property conveyed by the deed would not fall under either a probate or trust administration. Since vesting is automatic upon death, the property would pass to the beneficiary prior to the satisfaction of any claims that the Department would make. One consequence of this is that interest on the claim would begin to accrue when the Department presents its claim, which is must do within four months of being notified of the death (the Soto bill is clarifying this point in the case of non-court situations); but it is not inconceivable that the Department would seek interest from date of death on its claims, on the theory that since the property passes on death, and since the claim was not satisfied prior to distribution of the property, it is entitled to interest.

Since there is no requirement for the recipient of any particular piece of property to notify the Department, it is possible that property could pass to a TOD recipient and that many months could go by before the Department learns of the death and identifies the recipient of the TOD property. But since this is presently the situation with joint tenancy property, or property that passes from a living trust that is not subject to an administrative proceeding under Probate Code Sections 1900 *et seq.*, it does not necessarily lead to the conclusion that creation of a TOD deed should lead to a modification of the recovery provisions.

13. **Sale of Property in a Conservatorship.** A TOD deed has the same status as a specific gift (and subject to abatement claims) and therefore should be treated similarly in conservatorships. Accordingly, proceeds from the sale of property subject to a TOD deed should be set aside for the TOD deed grantee.

cc: 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
James B. MacDonald, Vice Chair, Estate Planning Subcommittee

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 beneficiary 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 - 3467B - Bahia Blanca West
Mary Pat Toups Laguna Woods, CA, 92637

2.

3. Colleen Woodward - 2087-A RONDA GRANADA
Colleen Woodward LAGUNA WOODS, CA 92637

4.

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NAME:

ADDRESS

1. *Sample* Mary Pat Toups 3467B-Bahia Blanca West
Mary Pat Toups Laguna Woods, CA, 92637
2. Sarah Shena 41006 Meadow Drive
Sarah Shena Three Rivers, CA 93271
3. *Desirée Cortez* 4125 W. Noble Ave., #222
Desirée Cortez Visalia, CA 93277
4. Zelma E Howard 418 W. Deodar Drive
Zelma E. Howard Remoore, CA 93245
5. Linda Luke 5600 W Walnut Ave Visalia CA 93277
LINDA LUKE
6. Ruth E. Rossiter 13787 Ave. 232 Tulare 93274
Ruth E Rossiter
7. Colette Elaine Ezell 2610 W Marquette Ave Exeter Ca 93221
Colette Elaine Ezell
8. Alfred J. Pasos 616 E. Tulare Ave "G" Visalia CA 93277
Alfred J. Pasos
- 9.

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