

Memorandum 2022-17

**Stock Cooperatives and Revocable Transfer on Death Deeds
(Draft Recommendation)**

At its January 2022 meeting, the Commission¹ directed the staff to prepare a draft recommendation for this study. The new draft would be based on the draft that was attached to Memorandum 21-62, with modifications to propose an amendment to Probate Code Section 5652(b). The amendment would create a narrow exception to the recordation requirement of that subdivision, for a property restriction that is expressed in a stock cooperative's governing documents or an agreement between the stock cooperative and the transferor.

The revised draft is attached for the Commission's consideration. The relevant changes from the earlier draft are as follows:

- On page 2, lines 31 and 32 are new. On page 3, lines 1 through 18 are new.
- On page 10, proposed Section 5652(c) is new.
- On page 11, lines 11 through 13 are new.

A few other minor technical and stylistic changes were made.

The Commission needs to decide whether to approve the draft recommendation as a final recommendation, for submission to the Governor and Legislature.

Respectfully submitted,

Brian Hebert
Executive Director

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

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

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STATE OF CALIFORNIA

CALIFORNIA LAW REVISION COMMISSION

STAFF DRAFT

RECOMMENDATION

Stock Cooperatives and
Revocable Transfer on Death Deeds

December 2021

California Law Revision Commission
c/o UC Davis School of Law
Davis, CA 95616
<commission@clrc.ca.gov>

SUMMARY OF RECOMMENDATION

In 2019, the Commission recommended that the revocable transfer on death deed statute not be made applicable to an interest in a stock cooperative (a type of common interest development where all of the real property is owned by a corporation and the separate interests consist of a share of stock in the corporation that creates an exclusive right to occupy a particular unit). The reason for that recommendation was purely technical. The Commission was unsure about the implications of using a deed to transfer a share of stock. Further study was required to determine whether a simple process could be created to transfer an interest in a stock cooperative on the owner's death, without probate administration.

The Commission has completed that study and recommends minor changes to the revocable transfer on death deed statute to make it applicable to an interest in a stock cooperative.

The Commission also recommends a substantive improvement to the revocable transfer on death deed statute generally, relating to the rules for resolving the effect of a conflicting dispositive instrument.

This recommendation was prepared pursuant to Resolution Chapter 108 of the Statutes of 2021.

1 STOCK COOPERATIVES AND REVOCABLE
2 TRANSFER ON DEATH DEEDS

3 In 2019, the Commission recommended against authorizing the use of a revocable
4 transfer on death deed (“RTODD”) to transfer an interest in a stock cooperative. That
5 recommendation was based on technical concerns rather than substantive policy. The
6 Commission sees no policy reason to deny the owners of interests in stock cooperatives a
7 simple way to transfer their property on death, without probate administration. The
8 question addressed in this study is how that result could best be achieved.

9 As the Commission explained:

10 A stock cooperative is a kind of common interest development where the
11 entirety of the development is owned by a corporation formed for that purpose.
12 The owners of separate interests hold shares in the corporation, which entitle them
13 to the exclusive right to occupy a specified apartment. Owners do not hold title to
14 any part of the development.

15 As a result, ownership of a separate interest in a stock cooperative is not
16 evidenced or conveyed by deed. Instead, it is conveyed by the sale of a share of
17 stock. For that reason, a deed would not be an appropriate instrument to use to
18 transfer ownership of a separate interest in a stock cooperative. A deed conveys
19 title to real property, not the ownership of a share of stock.

20 To avoid any confusion or legal problems that would result from the mismatch
21 between the use of a deed and the form of ownership in a stock cooperative, the
22 Commission recommends that stock cooperatives continue to be excluded from
23 the definition of “real property” that is used in the RTODD statute.

24 That approach would deny owners in stock cooperatives the benefits of using
25 an RTODD. However, it is possible that a share of ownership in a stock
26 cooperative could be transferred on death, outside of probate, under the existing
27 Uniform TOD Security Registration Act. The Commission plans to conduct a
28 separate study of that possibility, under its general authority to study the Probate
29 Code.¹

30 Having completed that study, the Commission decided against adapting the Uniform
31 TOD Security Registration Act for use in transferring a share of ownership in a stock
32 cooperative. There are significant substantive differences between the transfer of a
33 security generally and the transfer of a security that conveys an appurtenant interest in
34 real property. Properly accounting for those differences would have required adding
35 numerous provisions to the Uniform Act, which would have undermined its value as a
36 uniform statute.

37 Instead, the Commission concluded that the best way to address the substantive issues
38 that are involved in the transfer of an interest of real property would be to use the existing
39 RTODD statute, which already has the necessary provisions. After examining that
40 possibility, the Commission found that only a few adjustments to the existing statute

1. See *Revocable Transfer on Death Deed: Follow-Up Study*, 46 Cal. L. Revision Comm’n Reports 135, 157 (2019) (footnotes omitted).

1 would be required. This recommendation proposes those changes. They are explained
2 below.

3 In the course of its study, the Commission also discovered a way to simplify and
4 improve the existing RTODD statute’s treatment of conflicting dispositive instruments (a
5 will, trust, or other instrument that purports to dispose of property that is governed by an
6 RTODD). That general reform is also recommended and explained below.

7 USE OF RTODD TO TRANSFER
8 INTEREST IN STOCK COOPERATIVE

9 One potential problem with use of the RTODD statute to transfer an interest in a stock
10 cooperative is the apparent mismatch between the use of a “deed” to transfer an interest
11 that is not ordinarily evidenced or conveyed by a deed. As explained, an interest in a
12 stock cooperative is grounded in ownership of a share of the stock of the cooperative.
13 Having considered that problem, the Commission concluded that it could be solved by
14 adding language to affirmatively address the issue. The proposed law would revise the
15 definition of “revocable transfer on death deed” to expressly state:

16 A revocable transfer on death deed may be used to transfer real property even if
17 ownership of the property is not typically evidenced or transferred by use of a
18 deed.²

19 The Commission’s Comment to that provision would specifically state its application
20 to a stock cooperative.³ In addition, the “Common Questions” text on the statutory
21 RTODD form would be revised to explain the use of the form to transfer property in a
22 stock cooperative.⁴ Those changes should provide sufficient guidance to avoid any
23 problematic uncertainty on this fundamental point.

24 Another issue that must be addressed is the treatment of property use restrictions.
25 Many stock cooperatives place significant restrictions on the use of their separate
26 interests. Most notably, cooperatives may do one or more of the following:

- 27 • Require board approval of any new occupant.
28 • Reserve a right to repurchase a separate interest on the owner’s death.
29 • Restrict the purchase and sale price in order to provide affordable housing.⁵
30 • Restrict the development to providing housing for seniors.⁶

31 Such restrictions are typically not recorded. Instead, they are expressed in the stock
32 cooperative’s governing documents (e.g., articles of incorporation, bylaws) or in an

2. See proposed Prob. Code § 5614 *infra*.

3. *Id.*

4. See proposed Prob. Code § 5642 *infra*.

5. See Civ. Code § 817 (limited equity housing development).

6. See Civ. Code § 51.3 (senior housing).

1 agreement between the stock cooperative and the owner of the separate interest (e.g.,
2 proprietary lease, occupancy agreement).

3 That could lead to serious problems if the existing RTODD statute is applied to stock
4 cooperatives. Existing Probate Code Section 5652(b) provides that an unrecorded
5 restriction is not enforceable against property transferred by RTODD. Under that rule,
6 important restrictions on the use of property in a stock cooperative could be rendered
7 unenforceable by using an RTODD to transfer the property. In order to avoid that
8 problematic result, the stock cooperative would need to record a restriction in the time
9 period provided in Section 5652(b) (120 days after the beneficiary of the RTODD gives
10 notice to the transferor's heirs, a precondition to the effective operation of the RTODD).
11 If the stock cooperative does not record the restriction in time, it would become
12 unenforceable.

13 The Commission believes the risk of such a result is serious enough to outweigh other
14 considerations. It therefore recommends that an express exception be added to Section
15 5652, to provide that a restriction expressed in a stock cooperative's governing
16 documents or an agreement between the stock cooperative and the transferor would
17 remain enforceable against property transferred by RTODD, regardless of whether the
18 restriction has been recorded.⁷

19 The Commission also recommends that Section 5652 be revised to provide guidance
20 on how a reserved right to repurchase an interest in a stock cooperative would affect an
21 RTODD that transfers the interest.⁸

22 The Commission recommends the changes described above. Importantly, it also
23 recommends that the existing RTODD statute's definition of "real property" be revised so
24 that it would include stock cooperatives.⁹ Taken together, those reforms would ensure
25 that the RTODD statute would apply to stock cooperatives without causing any new
26 operational problems.

27 TREATMENT OF CONFLICTING DISPOSITIVE INSTRUMENTS

28 Existing Probate Code Section 5660 provides rules for determining the effect of an
29 RTODD when another instrument purports to dispose of the same property. That section
30 establishes the following priorities:

- 31 (1) If the other instrument is not recorded within 120 days after the beneficiary
32 gives notice of the RTODD, the other instrument does not operate.
- 33 (2) If the other instrument is recorded within 120 days after the beneficiary
34 gives notice, and the other instrument is irrevocable, the other instrument
35 operates and the RTODD does not.

7. See proposed Prob. Code § 5652(c) *infra*.

8. See proposed Prob. Code § 5652(d) *infra*.

9. See proposed Prob. Code § 5610 *infra*.

- 1 (3) If the other instrument is recorded within 120 days after the beneficiary
2 gives notice, and the other instrument is revocable, the later executed of the
3 two instruments operates and the earlier-executed instrument does not.

4 Under that provision, recordation is the primary consideration. An RTODD will always
5 prevail over an unrecorded instrument. The primacy of recordation reflects the
6 importance of the recording system and title insurance as the means by which a transfer
7 of property by RTODD will be effectuated. An effective transfer requires title insurance
8 to guarantee that the RTODD is valid, which in turn requires that all information that
9 might affect the validity of an RTODD be in the title records.

10 There is a significant disadvantage to that approach. An unrecorded conflicting
11 instrument will always fail, leaving the beneficiary of the other instrument without a
12 remedy. This is true even if the unrecorded instrument would otherwise have been given
13 effect by a court as the best expression of the transferor's intentions. That is a policy
14 compromise. The need for recordation as an operational matter is given priority over
15 maximizing the likelihood of effectuating the transferor's intentions.

16 The Commission no longer believes that this compromise is necessary. There appears
17 to be a fairly simple alternative approach that would provide sufficient record notice of a
18 conflicting claim, without invalidating all unrecorded conflicting instruments.

19 The alternative would be to treat a claim based on a conflicting instrument in the same
20 way as any other contest of an RTODD (e.g., a contest based on a claim of fraud,
21 mistake, undue influence, or incapacity). Under those existing rules, the relief available
22 for a successful contest will depend on whether the contestant recorded notice of the
23 contest (*a lis pendens*) within the 120-day period specified in Probate Code Section 5694,
24 or failing that, before the property is sold or encumbered. If the *lis pendens* is recorded in
25 time, a successful contest will void the RTODD, without any protection of a bona fide
26 purchaser or encumbrancer. If the *lis pendens* is not recorded in time, the RTODD will
27 operate and the interests of the bona fide purchaser or encumbrancer will be protected.

28 Importantly, a contestant who fails to record a timely *lis pendens* will still have a
29 meaningful alternative remedy — pecuniary recovery from the beneficiary. Even though
30 the contestant cannot obtain title to the property that was transferred by the RTODD, the
31 pecuniary value of the intended gift can still be realized.

32 The existing rules for treatment of a contest provide sufficient record notice of a
33 competing claim. Under those rules, title insurers will know that the validity of an
34 RTODD is uncertain during the time in which a *lis pendens* can be recorded. If no *lis*
35 *pendens* is recorded in that time period, title insurers will know that a bona fide purchaser
36 or encumbrancer will be protected against any subsequent contest that may be filed. That
37 provides the necessary certainty for the issuance of title insurance, once the time for
38 recording an effective *lis pendens* has run.

39 The Commission sees no reason why that system would be any less effective if applied
40 to a contest that is based on a conflicting dispositive instrument.

41 Under existing law, the failure to record a conflicting dispositive instrument in the 120-
42 day period specified in Section 5660 will invalidate the conflicting instrument, leaving
43 the beneficiary of the conflicting instrument without a remedy. If the recording

1 requirements were removed from Section 5660 and a conflicting instrument were treated
2 as just another kind of contest, that harsh result could be avoided. That would be a better
3 result as a matter of policy, as it would more faithfully reflect the transferor's intentions.

4 That change in the treatment of conflicting instruments would not cause any new
5 problems with regard to the availability of title insurance, because it would simply
6 incorporate the treatment of conflicting instruments into the rules that already govern
7 contests generally.

8 For the reasons discussed above, the Commission recommends that Section 5660 be
9 revised to (1) remove the requirement that a conflicting instrument be recorded in order
10 to be effective and (2) add language clarifying that a claim based on a conflicting
11 instrument should be treated in the same way as any other contest.

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PROPOSED LEGISLATION

Prob. Code § 5610 (amended). “Real property” defined

SECTION 1. Section 5610 of the Probate Code is amended to read as follows:

5610. (a) Except as provided in subdivision (b), “real property” means either of the following:

(1) A parcel of land that is improved with one to four residential dwelling units.

(2) A residential separate interest and its appurtenant common area in a common interest development, regardless of the number of separate interests in the common interest development.

(b) “Real property” does not include ~~either of the following:~~

~~(1) A separate interest in a stock cooperative.~~

~~(2) A~~ a parcel of agricultural land that is greater than 40 acres in size. For the purposes of this ~~paragraph~~ subdivision, “agricultural land” means land that is designated for agricultural use by law or by a document that is recorded in the county in which the land is located.

(c) The definition of “real property” shall be construed pursuant to the circumstances that existed on the execution date shown on the revocable transfer on death deed.

Comment. Section 5610 is amended to include an interest in a stock cooperative within the meaning of “real property.”

Prob. Code § 5614 (amended). “Revocable transfer on death deed” defined

SEC. 2. Section 5614 of the Probate Code is amended to read as follows.

(a) “Revocable transfer on death deed” means an instrument created pursuant to this part that does all of the following:

(1) Makes a donative transfer of real property to a named beneficiary.

(2) Operates on the transferor’s death.

(3) Remains revocable until the transferor’s death.

(b) A revocable transfer on death deed may also be known as a “revocable TOD deed.”

(c) A revocable transfer on death deed may be used to transfer real property even if ownership of the property is not typically evidenced or transferred by use of a deed.

Comment. Section 5614 is amended to make clear that a revocable transfer on death deed can be used to transfer real property of a type that is not typically transferred by use of a deed (e.g., an interest in a stock cooperative).

Prob. Code § 5614.5 (added). “Stock cooperative” defined

SEC. 3. Section 5614.5 is added to the Probate Code, to read:

5614.5. “Stock cooperative” has the meaning provided in Section 4190 of the Civil Code.

Comment. Section 5614.5 is new. It is added for drafting convenience.

1 **Prob. Code § 5642 (amended). Excerpt from Frequently Asked Questions**

2 SEC. 4. Section 5642 of the Probate Code is amended to read as follows:

3 5642. ...

4 COMMON QUESTIONS ABOUT THE USE OF THIS FORM

5 ...

6 CAN I USE THIS DEED TO TRANSFER NONRESIDENTIAL PROPERTY? No.
7 This deed can only be used to transfer residential property. Also, the deed cannot be used
8 to transfer ~~a unit in a stock cooperative~~ or a parcel of agricultural land that is over 40
9 acres in size.

10 ...

11 **Comment.** Section 5642 is amended to reflect that the revocable transfer on death deed can be
12 used to transfer an interest in a stock cooperative. See Section 5614.5 (“stock cooperative”
13 defined).

14 **Prob. Code § 5652 (amended). Effect of transfer**

15 SEC. 4. Section 5652 of the Probate Code is amended to read as follows:

16 5652. (a) A revocable transfer on death deed transfers all of the transferor’s interest in
17 the property on the transferor’s death according to the following rules:

18 (1) Subject to the beneficiary’s right to disclaim the transfer, the interest in the property
19 is transferred to the beneficiary in accordance with the deed.

20 (2) The interest of a beneficiary is contingent on the beneficiary surviving the
21 transferor. Notwithstanding Section 21110, the interest of a beneficiary that fails to
22 survive the transferor lapses.

23 (3) Except as provided in paragraph (4), if there is more than one beneficiary, they take
24 the property as tenants in common, in equal shares.

25 (4) If there is more than one beneficiary, the share of a beneficiary that lapses or fails
26 for any reason is transferred to the others in equal shares.

27 (b) Property is transferred by a revocable transfer on death deed subject to any
28 limitation on the transferor’s interest that is of record at the transferor’s death or that is
29 recorded no later than 120 days after the affidavit required by subdivision (c) of Section
30 5682 is recorded, including, but not limited to, a lien, encumbrance, easement, lease, or
31 other instrument affecting the transferor’s interest, whether recorded before or after
32 recordation of the revocable transfer on death deed. The holder of rights under that
33 instrument may enforce those rights against the property notwithstanding its transfer by
34 the revocable transfer on death deed. An enforceable restriction on the use of the
35 transferred property does not affect the transfer of title to the property by a revocable
36 transfer on death deed.

37 (c) Notwithstanding subdivision (b), an interest in a stock cooperative is transferred by
38 a revocable transfer on death deed subject to any limitation on the transferor’s interest
39 that is expressed in the governing documents of the stock cooperative or in a written
40 agreement between the stock cooperative and the transferor, without regard for whether
41 those instruments are recorded.

1 (d) If a stock cooperative exercises an option to purchase property transferred by a
2 revocable transfer on death deed on the transferor's death, the result is as follows:

3 (1) The property is transferred to the stock cooperative rather than the beneficiary.

4 (2) The purchase price is paid to the beneficiary. Unless the law or the governing
5 documents of the stock cooperative provide otherwise, the purchase price is the fair
6 market value of the property, less the amount of any liens or encumbrances on the
7 property at the time of the owner's death and less any amount that the decedent owed to
8 the stock cooperative.

9 (e) A revocable transfer on death deed transfers the property without covenant or
10 warranty of title.

11 **Comment.** Subdivision (c) is added to Section 5652 to create an express exception for certain
12 property restrictions in a stock cooperative. Such restrictions need not be recorded in order to
13 remain enforceable against an interest that is transferred by revocable transfer on death deed.

14 Subdivision (d) is added to provide guidance on the steps to be followed when a stock
15 cooperative exercises an option to purchase an interest that was transferred by revocable transfer
16 on death deed. Paragraph (2) makes clear that the price paid to purchase property in a stock
17 cooperative may be limited by law or the governing documents of the stock cooperative. For
18 example, in a limited equity housing cooperative, the amount paid will be based on a specified
19 transfer value, rather than fair market value. See Civ. Code § 817. See also Section 5614.5
20 (“stock cooperative” defined).

21 **Prob. Code § 5660 (amended). Conflicting instruments**

22 SEC. 6. Section 5660 of the Probate Code is amended to read as follows:

23 5660. (a) If a revocable transfer on death deed recorded on or before 60 days after the
24 date it was acknowledged before a notary public and another instrument both purport to
25 dispose of the same property:

26 ~~(a) If the other instrument is not recorded within 120 days after the affidavit required~~
27 ~~by subdivision (c) of Section 5682 is recorded, the revocable transfer on death deed is the~~
28 ~~operative instrument.~~

29 ~~(b) If the other instrument is recorded within 120 days after the affidavit required by~~
30 ~~subdivision (c) of Section 5682 is recorded and~~

31 (1) If the other instrument makes a revocable disposition of the property, the later
32 executed of the revocable transfer on death deed or the other instrument is the operative
33 instrument.

34 ~~(c) If the other instrument is recorded within 120 days after the affidavit required by~~
35 ~~subdivision (c) of Section 5682 is recorded and~~

36 (2) If the other instrument makes an irrevocable disposition of the property, the other
37 instrument and not the revocable transfer on death deed is the operative instrument.

38 (b) A claim that a revocable transfer on death deed is inoperative pursuant to this
39 section is grounds for a contest under Chapter 5 (commencing with Section 5970).

40 **Comment.** Section 5660 is amended to remove the requirement that a conflicting instrument
41 be recorded in order to be effective. The amendment also makes clear that a claim that a
42 revocable transfer on death deed is invalid pursuant to this section is a contest.