



WHAT THE KWOK! I KILLED MY CLIENT'S TITLE INSURANCE

The State Bar of California
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Costa Mesa, CA
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I. IS IT A TRUST “AGREEMENT”
OR A “DECLARATION”?

Probate Code section 15200

- 15200. Subject to other provisions of this chapter, a trust may be created by any of the following methods:
 - (a) A declaration by the owner of property that the owner holds the property as trustee.
 - (b) A transfer of property by the owner during the owner's lifetime to another person as trustee.
 - (c) A transfer of property by the owner, by will or by other instrument taking effect upon the death of the owner, to another person as trustee.
 - (d) An exercise of a power of appointment to another person as trustee.
 - (e) An enforceable promise to create a trust.



Identify Type of Trust

Revocable trusts are generally (1) agreements or (2) declarations.

- **Trust Agreement:** If the trust has a trustee other than the grantor, then the trust instrument is a “trust agreement” because both the grantor and the trustee must agree to the terms of the trust.
- **Declaration of Trust:** However, if the grantor is the sole trustee, then the trust instrument is a “declaration of trust,” since the grantor is the only party to the trust.

ELEMENTS OF A TRUST

- The essential elements of a trust (Prob. C. § 15200):
 - A settlor (the owner of the property that will be subject to the trust);
 - Settlor's intent to create a trust;
 - **Trust property**;
 - Trust beneficiary; and
 - Valid trust purpose

Trust Property

- A trust is created only if there is trust property. (Prob. C. § 15206.) For a trust to be effective, there must be an inter vivos transfer of the trust res to the trustee. *Reagh v. Kelley* (1970) 10 Cal. App. 3d 1082, 1094; Restatement (Second) of Trusts § 17 (1959).
- When there is no effective transfer to the trustee, the trust fails as to that asset.

TRUST FUNDING . . .

- Differences in *Res* of a Declaration of Trust v. a Trust Agreement

TRUST AGREEMENTS

- When the settlor and the trustee are not the same person, the trust will likely require a *transfer* to the trustee.
- For a simple example, see the following **Transfer to Trust**:
 - I, Mr. Settlor, hereby transfer and deliver to Mr. Trustee, without consideration, the property described in Schedule A, attached to this trust.

Declarations of Trust

- When the settlor is also the initial trustee, *the formalities of conveyance are relaxed and the declaration* of the trustee that he or she holds the asset in trust *may be sufficient*.
- **Declaration of Trust:** Ms. Settlor declares that she holds in trust the property described in Schedule A, attached to this trust. All property subject to this trust from time to time is referred to as the trust estate and shall be held, administered, and distributed according to this instrument.



II. PROBATE CODE

§ 15200; *ESTATE OF
HEGGSTAD*

Probate Code section 15200

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 - (a) A declaration by the owner of property that the owner holds the property as trustee.
 - (b) A transfer of property by the owner during the owner's lifetime to another person as trustee.
 - (c) A transfer of property by the owner, by will or by other instrument taking effect upon the death of the owner, to another person as trustee.
 - (d) An exercise of a power of appointment to another person as trustee.
 - (e) An enforceable promise to create a trust.

Real Property

- A trust in relation to real property usually must be evidenced by a writing. (Prob. C. § 15206)
 - “A trust in relation to real property is not valid unless evidenced by one of the following methods:
 - (a) **By a written instrument signed by the trustee**, or by the trustee’s agent if authorized in writing to do so.
 - (b) By a written instrument conveying the trust property signed by the settlor, or by the settlor’s agent if authorized in writing to do so.
 - (c) By operation of law.”

Estate of Heggstad

- In *Estate of Heggstad* (1993) 16 Cal. App. 4th 943, 950, the court held that a separate deed transferring real property from the settlor to himself as trustee was not necessary to create a valid trust, when a schedule attached to the written declaration of trust identified items of trust property.

Analysis of *Heggstad*

- Appellant contended decedent was required to execute a grant deed transferring property to himself as trustee.
- Court found there is no requirement that the settlor/trustee execute a separate instrument conveying property to the trust.
- A written declaration of trust by the owner is sufficient to create a trust in that real property.
- KEY: the settlor holds a property interest before the declaration, and after the declaration he holds a bare legal interest in the same property. The settlor has merely remained the owner of part of what he formerly owned.



III. CLARIFYING THE SCOPE OF *HEGGSTAD*

Heggstad's Limitations

- **Declaration of Trust:** In *Heggstad*, the settlors named themselves as trustees of their trust, and one of the court's findings, as noted above, was that a settlor can show intent to create a trust by declaring himself or herself trustee.
- **Trust Agreements:** It is not clear if a *Heggstad* petition can succeed if the settlors are not the trustees. Stated otherwise, a Declaration is NOT a transfer.

Osswald v. Anderson

- *Osswald v. Anderson*, (1996) 49 Cal. App. 4th 812, distinguished *Heggstad*
- Property description says see Schedule A: BUT there was no Schedule A
 - Insufficient proof that property was deeded to trust (only evidence was an inadmissible photocopy of a deed)
- Hence, the last deed determined ownership of property

Estate of Powell

- In *Estate of Powell*, (2000) 83 Cal. App. 4th 1434, Husband and Wife, joint tenants, executed a declaration of trust and listed property on Schedule A.
- Husband and Wife were Trustees
- Property never deeded to trust.
- Citing *Heggstad*, Declaration of Trust by all joint tenants along with the listing of property on Schedule A was sufficient to transfer joint tenancy property to trust.

Kucker v. Kucker

- In *Kucker v. Kucker*, (2011), 192 Cal App. 4th 90, the trustor's general assignment described "all of my right, title and interest in all property owned by me, both real and personal and wherever located" to be held in her revocable inter vivos trust.
- This was effective in transferring shares of stock to trust, but it was ineffective in transferring real property to trust because of the statute of frauds. The assignment failed to describe real property so that it could be identified.

Ukkestad v. RBS Asset Finance

- Ukkestad v. RBS Asset Finance was filed March 16, 2015, Fourth District, Div. One (Cite as C065630)
- In Ukkestad , the Settlor established a Trust which recited that all of his “right, title and interest” to “all of his real ... property” is included in the Trust’s assets (a “general assignment” type of reference). After the Settlor’s death, one of the Trustees brought a petition under Prob. C. § 850 for an order that two parcels held in the name of the Settlor were part of the Trust. Significant was the fact that the attorney filed a declaration stating that the Settlor’s real property was easily identifiable as the ownership was a matter of public record.

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- In reversing the trial court's denial of the petition, the appellate court held the transfer of the real property complies with the statute of frauds because it could be established by extrinsic evidence that the Settlor held title to the subject parcels.

Lessons of Heggstad, Osswald Powell, and Ukkestad

- Declaration of Trust in the Trust instrument
- A mere reference to “real property” should suffice
- The owner of the real property must be both Settlor and Trustee
- No deed of transfer needed



IV. PRACTICAL COMPLICATIONS

Complications of *Heggstad*

- There is abundant legal authority that a declaration of trust by the owner of real property is sufficient to create a trust in that property, and the law does not require a separate deed. See Restatement Second of Trusts, Section 17; Bogert, Trusts and Trustees.
- However, practice guides for years have recommended a deed by prepared conveying title to the settlor to provide solid evidence of the transfer.

Practical Implication

- Accordingly, the standard of practice which has become established is to treat a Declaration of Trust like a Trust Agreement for purposes of creating a trust in real property.

A Deed “Transfers” ...

- What is a "transfer"? The Probate Code defines a "transferor" and a transferee" at 81 and 81.5, but it does not define "transfer".
- Civil Code section 1039 defines a transfer as a conveyance of realty from one person *to another person*. With respect to real property, the Civil Code section controls.
- A trust transfer deed, from a very technical perspective, “conveys” property to a trustee.



V. KWOK

Kwok v. Transnation Title Ins. Co.

- In *Kwok v. Transnation Title Ins. Co.*, (2009) 170 Cal. App. 4th 1562, the court held that the transfer of real property from a wholly owned LLC entity to the members as trustees of their trust constituted a voluntary act that did not arise by operation of law and thus terminated their title insurance coverage.
- Here is what the policy stated: “the insured is that party named in Schedule A and those who succeed to the interest by operation of law”.
- The trial court granted a motion for summary judgment by the insurance company, finding that the undisputed evidence showed that the property was voluntarily transferred by grant deed. The Court of Appeals upheld that decision on appeal.

- The concern for estate planners as a result of *Kwok* is that the voluntary transfer of real property to a revocable trust may cause the loss of title insurance under the terms of some title insurance policy provisions.
- The language commonly included in the letter denying the claim follows something like...“Mr. and Mrs. White *transferred* their interest in Property to their Family Trust in 2012. Accordingly, Mr. and Mrs. White, as individuals, no longer held title to the Property when the Family Trust acquired a fee simple interest in the Property. Accordingly, *the transfer* to the Family Trust terminated coverage under the title insurance policy....”.

Deed Mechanics Issue Raised in *Kwok*

- The *Kwok* issue was the transfer occurring by use of a deed.
- A deed “grants” or “conveys,” which is the funding procedure for Trust Agreements under Prob. C. § 15200(b).

Deed Mechanics Cont.

- However, this really is the incorrect funding approach for a Declaration of Trust, as shown under Prob. C. § 15200(a).
- Probate Code section 15200 describes only two (2) methods for creating an inter vivos trust: (1) by declaration or (2) by transfer to a trustee. If you are the settlor and already own real property, why transfer it to yourself? The Probate Code says you should declare that you hold it in trust as the trustee.

What if a Declaration Were Used?

- According to *Heggstad*, no authority requires a settlor, who names himself as trustee of a revocable living trust, to convey his property to the trust by a separate deed. All that is required by the statute of frauds is a written document.”
-
- The Court went on to amplify the significance of declaring a trust in real property. The Court stated that if the trust is to be created by declaration there is no real transfer of any property interest to a trustee. The settlor holds a property interest before the trust declaration and after the declaration he holds a bare legal interest in the same property interest with the equitable or beneficial interest in the beneficiary. No new property interest has passed to the trustee. The settlor has merely remained the owner of part of what he formally owned.
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- Accordingly, if a declaration of trust in real property were utilized, there would seem to not be a *Kwok* issue. Legally, no “conveyance” or “transfer” has occurred.

Transfer of Title Issues

- Conclusion: Transfer of title by deed may affect liability and title insurance, real property assessment, and due-on-sale clauses.
- Lawyers...Beware!
 - I receive at least one email a month from lawyers who have had clients' claims for title insurance denied because of trust funding pursuant to a deed.



VI. CURRENT STATUS

Response to *Kwok*

In response to the Kwok decision, TEXCOM authored a legislative proposal to add Section 12419 to the Insurance Code.

Assembly Bill 2196 (Fox)

- The new Section 12419 would have read as follows:

“Coverage under a policy of title insurance shall continue to the transferee when title is transferred to a trustee of the insured’s revocable living trust of which the insured is a beneficiary with the power to revoke, or, if the trustee of a trust is the insured under the policy, when title is transferred by the trustee to the trust’s settlor in his or her individual capacity.”

Outcome

- A compromise was reached, whereby the bill was cancelled in exchange for an amendment to the *Kwok* policy to authorize transfers to revocable trusts.
- The updated policy was issued, and is effective as of, May 18, 2014.
- Properties purchased after May 18, 2014 should be free of the “Kwok” problem.
- However, ANY property purchased prior to May 18, 2014 may have a “Kwok” problem.
- Attorney should be most concerned where deeds were or are used to fund real property into trusts after 2009.

VII. PLANNING OPTIONS TO DEAL WITH *KWOK*

- 1. Obtain an Endorsement
- 2. Obtain Expanded Coverage (if possible)
- 3. Purchase a New Policy (if possible)
- 4. Use Affidavit of Owner Holding Real Property as Trustee
- 5. Don't record anything; rely on Probate Code section 850
- 6. Litigate Denial of Coverage
- 7. Disclose the risk to client, and let the client make an informed decision to record trust transfer deed



REVIEW OF POLICIES

ALTA Owner's Policy 1970, 1987, 1990, and 1992

- Under ALTA Owner's Policy 1970, 1987, 1992 and 1990, the definition of "insured" is the insured named in Schedule A and those who succeed to the interest by operation of law as distinguished from purchase.
- These policies do not extend coverage to transferees of voluntary transfers. A transfer of property by an owner to himself as trustee of his revocable trust is a voluntary act, and does not arise by operation of law.
- Thus, ALTA Owner's Policy 1970, 1987, 1992 and 1990 does not appear to extend coverage to transfers into a trust.

CLTA Standard Coverage Policy 1990

- CLTA Standard Coverage Policy 1990 was the policy at issue in *Kwok*. Under CLTA Standard Coverage 1990, the definition of “insured” is the same as under ALTA Owner’s Policy 1970, 1987, 1992 and 1990, *i.e.*, the insured named in Schedule A and those who succeed to the interest by operation of law as distinguished from purchase.
- This definition poses a problem for owners who want to transfer their interests in property into their revocable trusts, as it does not appear to extend coverage to transfers into trust.

ALTA Residential Title Insurance Policy 1979, 1987

- Under ALTA Residential Title Insurance Policy 1979, 1987, “insured” is not defined. Rather, in the “Continuation of Coverage” section, the policy provides:
 - “This Policy protects you as long as you: own your title or own a mortgage from anyone who buys your land or are liable for any title warranties you make. This Policy protects anyone who receives your title because of your death.”
- ALTA Residential Title Insurance Policy 1979, 1987 is ambiguous in light of *Kwok*. An insured under such a policy who transfers property into trust should take appropriate steps, such as seeking an endorsement, to ensure the coverage extends to transfers into revocable trusts.

CLTA/ALTA Homeowner's Policy of Title Insurance 1998 - Present

- CLTA/ALTA Homeowner's Policy of Title Insurance 1998 – Present defines “You/Your” as the insured named in Schedule A. The policy further provides: “This Policy also insures: (1) anyone who inherits Your Title because of Your death; (2) your spouse who receives Your Title because of dissolution of Your marriage; (3) the trustee or successor trustee of a Trust to whom You transfer Your Title after the Policy Date; or, (4) the beneficiaries of Your Trust upon Your death.”
- This policy specifically provides that a trustee of a trust to whom the insured transferred the property will be insured. Under CLTA/ALTA Homeowner's Policy of Title Insurance 1998 – Present, the policy covers transfers into trusts. The holding in *Kwok* does not alter this result.

ALTA Owner's Policy 2006 - Present

- ALTA Owner's Policy 2006 – Present defines “insured” as the insured named in Schedule A. The policy further provides: “The term ‘Insured’ also includes: (A) successors to the Title of the Insured by operation of law as distinguished from purchase; (B) a grantee of an Insured under a deed delivered without payment of an actual valuable consideration conveying the Title . . . (4) if the grantee is a trustee or beneficiary of a trust created by a written instrument established by the Insured named in Schedule A for estate planning purposes.”
- Similar to CLTA/ALTA Homeowner's Policy of Title Insurance 1998, this policy appears to include revocable trusts as additional insureds and eliminate the need for an endorsement by automatically extending coverage to trusts.



If you have a “Problem Policy”

- CYA Letter to Clients, or
- Obtain Endorsement.

Checklist for Obtaining an Endorsement for Title Insurance

□ Situations where an endorsement is needed (or, if not available, a new policy may be necessary):

- Transfer to a revocable trust
- Transfer from a revocable trust where trust is the insured
- Subtrust funding upon death of settlor
- Transfer to an irrevocable trust
- Transfer to a limited liability company, S corporation, or other entity
- Death of joint tenant (depending upon when joint tenant added to title)

Checklist Cont.

Obtain Title Insurance Information:

- Obtain title insurance policy

- Troubleshooting: Finding the policy:*

- Contact title company who handled escrow

- Review vesting deed for escrow company information

- Determine if title insurer is still in existence*

Checklist Cont.

If title insurer is no longer in existence, determine what title company currently holds the policy

○ Review title insurance policy

Type of Policy

Definition of Insured

Definition of Transfer

Transfer restrictions

Coverage upon transfer

Scope of coverage

Checklist Cont.

Obtain Title Insurance Endorsement:

- Contact title insurer to request endorsement
 - Provide copy of title insurance policy*
 - Provide copy of proposed transfer deed*
 - Provide copy of trust, entity agreement, etc.*
 - Determine price of endorsement*
- Record transfer deed
- Provide title insurance officer with a copy of the recorded deed
- Obtain endorsement form CLTA 107.9 for transfer to revocable trusts
- Obtain evidence of granting an endorsement for other transfers
- Keep endorsement with title insurance policy (in place of safekeeping, preferably with original estate planning documents)

Use Declarations, Not Deeds...

- Another solution may be to utilize the declaration provisions of Probate Code section 15200(a) to prepare and record an affidavit pursuant to which an owner declares he or she hold their real property as trustee in place of the standard trust transfer deed.
- Such a funding procedure is authorized in the Probate Code under sections 15200 and 15206.
- The Probate Code provides that a trust, which relates to real property, may be recorded in the office of the county recorder where the real property is located. California Prob. Code, section 15210. And, the recording statutes provide that any instrument affecting the title to real property may be recorded. California Gov. Code, section 27280(a)

Affidavit of Owner Holding Real Property as Trustee – Page 1

APN: _____

MAIL TAX STATEMENTS AND
WHEN RECORDED MAIL TO:

(SPACE ABOVE THIS LINE FOR RECORDER'S USE)

AFFIDAVIT OF OWNER HOLDING REAL PROPERTY AS TRUSTEE [Declaration under Cal. Prob. Code, §15200, subd. (a)]

OWNER: _____

REAL PROPERTY: That certain real property situated in the City of _____, County of _____, State of California, more particularly described as follows:

Commonly known address: _____

Page 1, Continued

TRUST: That certain written instrument, which is a grantor revocable inter vivos trust, which is described as follows:

Name of Trust: _____

Date of Trust: _____

TAX STATEMENTS: Mail Tax Statements as directed above.

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DECLARATION: With reference to the above descriptions, the undersigned Owner, being of legal age, declares that said Owner, as the current owner of the Real Property and settlor of the Trust, holds the Real Property as trustee of that same Trust.

This declaration is prepared and executed pursuant to California Probate Code sections 15200, subdivision (a), 15206, subdivision (a), and 15210.

I/We declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

DATED:

EXECUTION:

(type or print name(s) of Owner)

JURAT FOLLOWS.....

Use Probate Code section 850

- If clients don't record deeds, ***Ukkestad v. RBS Asset Finance*** now makes it fairly clear an “omnibus clause” describing real property suffices.
- Confirming real property as trust assets post-death avoids the risk of causing a loss of title insurance coverage via an inter vivos transfer.
- Although not “best practices”, this approach may be best in some circumstances.

Litigation

In *Kwok*, the policy stated:

“the insured is that party named in Schedule A and those who succeed to the interest by operation of law”.

- Transnation denied coverage on the grounds that the transfer of the property by Mr. and Mrs. Kwok to themselves as trustees was a voluntary act that did not arise by operation of law, which terminated coverage pursuant to the policy's terms.

- Interestingly, later provisions of the CLTA Standard Coverage Policy of Title Insurance at issue in *Kwok* state:
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- "The coverage of this policy shall continue in force as of Date of Policy in favor of insured only so long as the insured retains an estate or interest in the land, . . . or only so long as the insured shall have liability by reason of covenants of warranty made by the insured in any transfer or conveyance of the estate or interest."
- This provision is at Part II, Section 2, b of the CLTA 1990 Policy.

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- If title insurers allege the “voluntary act” of granting or quitclaiming title to a trust by deed caused a loss of coverage, this later provision arguably creates ambiguity.
 - Therefore, practitioners may consider litigation against title insurers who deny coverage.
 - Ambiguous insurance policy terms must be construed against the insurance company.

Inform Your Clients

- Disclose the risk to client, and let the client make an informed decision to record trust transfer deed.
- Provided you have, in writing, advised the client of the risk of recording a deed, and provided them options, the client may make an informed decision to:
 - Have the attorney obtain an endorsement
 - Use an Affidavit, instead of a deed
 - Refrain from recording anything
 - Or, record a deed and accept the risk that they may have a “Kwok-type policy”

BEST PRACTICES IS TO INFORM YOUR CLIENTS!



CONCLUDING THOUGHTS

Using a deed is dangerous for estate planners. The ramifications can be the loss of a client's title insurance, as well as other issues, such as triggering due on transfer clauses. Consider the planning options discussed to make sure you don't "kill your client's title insurance."