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March 30, 1990

, Esq.

, CA

Dear Ms. :

This is in response to your letter requesting advice on whether your client, , can qualify for the benefits of Proposition 60 by transferring the base year value of his original property to a replacement dwelling in which 8 percent of the ownership was acquired by by virtue of his uncle's revocable living trust. is purchasing the remaining 92 percent interest in the property from 14 other trust beneficiaries. You ask whether this transaction constitutes a "purchase" within the meaning of Revenue and Taxation Code section 69.5 (implementing Proposition 60) and qualifies him for the benefits of this provision.

Your letter states that uncle, , a widower without children, passed away on January 3, 1989. Under a revocable living trust executed in May of 1988, the residue of the estate was left in varying percentages to some 15 nieces and nephews, including The residue includes a residence which would like to acquire as a replacement dwelling. Under the trust, he received an 8 percent interest in the property and would, in effect, purchase the remaining 92 percent interest from the other 14 beneficiaries through a distribution in kind arrangement. That is, his interest in other portions of the residue would be used as consideration for the transfer of the interests of the other beneficiaries in the subject property to

Section 69.5 permits a person over age 55 years to transfer the base year value of an original property to a replacement dwelling which is "purchased" by that person as his or her principal residence within two years of the sale by that person of the original property. The term "purchased" is defined in Revenue and Taxation Code section 67 as a change in ownership for consideration. For that reason, we have taken the position that property acquired by gift or device, without the benefit of consideration, cannot qualify as a replacement dwelling for purposes of section 69.5. Thus, had acquired a 100

74

percent interest in the subject property by virtue of his uncle's trust, we would conclude that the property cannot qualify as a "purchased" replacement dwelling. On the other hand, had Mr. Rehburg acquired a zero percent interest in the property via his uncle's trust and then purchased a 100 percent interest in the property by exchanging his interest in other residue property, we would conclude that he had purchased the property and that it can qualify as a replacement dwelling.

The difficult question that you present is whether 8 percent interest disqualifies the property from being considered to be "purchased" for purposes of section 69.5. In reviewing this question, it is apparent at the outset that there are no provisions in section 69.5 which expressly deal with this issue. Thus, the conclusion we reach must be based upon inferences derived from relevant portions of the statute. As a result, it is fair to state that our conclusions are not necessarily free of doubt.

Section 69.5 authorizes the transfer of the base year value of an original property which is eligible for the homeowner's exemption to a replacement dwelling which is occupied as the claimant's principal place of residence and is eligible for the homeowner's exemption. The section deals with the original property and the replacement dwelling as single integrated units. The definitions of these terms found in subdivisions (g)(3) and (4) refer to "a building, structure, or other shelter constituting a place of abode, whether real or personal property, which is owned and occupied by a claimant as his or her place of residence, and any land owned by the claimant on which the building, structure, or other shelter is situated." These definitions support our conclusion that the terms "original property" and "replacement dwelling" are intended to refer to the entire property as single integrated units and not to fractional interests in such property. For that reason, we have generally followed this interpretation for purposes of applying the various requirements of section 69.5. For example, where a 50 percent interest in a replacement dwelling was acquired by inheritance, and the remaining 50 percent interest was purchased from other heirs, we have concluded that the replacement property could not be considered to be "purchased" for purposes of section 69.5. Logically, this analytical approach suggests that, since we treat the original property and replacement dwelling on a single-unit basis, anything less than a 100 percent purchase of the replacement dwelling will not qualify for the benefit.

We recognize, of course, that it may be reasonable to conclude that at some point an ownership interest is so small that it should be considered de minimis and ignored for purposes of

applying section 69.5. Unfortunately, we have not been able to find anything in section 69.5 which seems to support this conclusion or to provide guidance as to when such an interest should be considered to be de minimis.

The Legislature has enacted a general change in ownership de minimus rule in subdivision (a) of Revenue and Taxation Code section 65.1. That provision excludes from reappraisal the purchase of an interest in real property if the interest has a market value of less than 5 percent of the value of the total property and the market value of the interest is less than $10,000. In the absence of any other guidance from the Legislature, we conclude that if a de minimis standard is to be applied to section 69.5, that such a standard should be consistent with the limits set forth in section 65.1. For that reason, we must conclude that 8 percent interest in his uncle's property would prevent that property from being considered to be a "purchased" replacement dwelling for purposes of section 69.5.

The views expressed herein are advisory only and are not binding upon local assessors. You may wish to consult with the assessor in the county in which the subject property is located in order to determine whether the property will be treated in a manner consistent with the views expressed above.

Our intention is to provide timely, courteous and helpful responses to inquires such as yours. Suggestions that help us to accomplish this goal are appreciated.

Very truly yours,

Richard H. Ochsner
Assistant Chief Counsel

RHO:cb
2416D

cc: Mr. John W. Hagerty
Mr. Verne Walton
Mr. Dennis Miller

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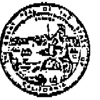

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Executive Director

January 28, 2000

In Re: ***No Transfer of Base Year Value to Replacement Dwelling Devised in Part and Purchased in Part from Parents' Trust.***

Dear Mr. :

This is in response to your letter of September 25, 1999, to Ms. Janet Saunders requesting an opinion as to whether your client may qualify for the benefits of Proposition 60 (California Constitution Article XIIIA, Section 2) implemented under Revenue & Taxation Code Section 69.5. The issue is whether the transfer of base year value benefit is available where 33.1/3% of ownership interests in the replacement dwelling were gifted or devised to Mrs. S as a beneficiary under her parents' trust, and the remaining 66.2/3% were purchased by Mr. and Mrs. S. Please accept our apologies for this delayed response, due to our work on prescheduled Board matters.

You have described the following set of facts for purposes of our analysis:

1. When the mother of Mrs. S died, Mrs. S became the sole trustee of her parents' trust and divided the assets of the trust estate into three parts for distribution to herself, her brother, and the children of her predeceased sister. (Mr. S was not an heir or distributee of any interest or part of the trust.) One of these assets was the principal residence of her parents located in Piedmont, California. Mrs. S filed a parent/child claim to exclude the transfer of the residence from change in ownership. In October 1997, Mr. and Mrs. S sold their own principal residence (also in Alameda County) for $735,000.

2. At the same time, Mr. and Mrs. S purchased the Piedmont residence from the trust for the full $600,000 value. The proceeds of the sale became assets of the trust. When Mr. and Mrs. S applied to the Alameda County Assessor to transfer the base year value under Section 69.5 from their original dwelling to the replacement dwelling they purchased from the trust, the benefit was denied. The Assessor's view is that Mr. and Mrs. S did not "purchase" 100% of the Piedmont residence, since Mrs. S had already received a 33 1/3% interest as a trust beneficiary.

You believe that the requirements of Section 69.5 have been met, in that Mr. and Mrs. S actually paid for or purchased 100% of the replacement dwelling from the trust at its full cash value. In your view, Mr. and Mrs. S are in factual compliance with all of the statutory prerequisites, and the assessor should allow the benefit.

Your questions are two-fold. First, does Mr. and Mrs. S's purchase of the replacement dwelling from the trust constitute a purchase of 100% of the Piedmont residence for purposes of obtaining the benefit under Section 69.5? Secondly, even if it were determined that Mrs. S received a one-third interest in the replacement dwelling based on the distribution she received from the trust, is Mr. S's purchase of his partial interest in the Piedmont residence sufficient for purposes of qualifying for the benefit? As hereinafter explained, the answer to both questions is no. We agree with the assessor that the requirements of Section 69.5 have not been met.

1. **As Beneficiary of her Parents' Trust, Mrs. S became Part Owner of the Trust Property - Her "Purchase" from the Trust did not subject the Replacement Dwelling to a Change in Ownership for Consideration, per Sections 67 and 69.5(a) and (g).**

As you are aware, Section 69.5 permits a person over the age of 55 years to transfer the base year value of an original property which is "sold," to a replacement dwelling "of equal or lesser value" which is "purchased" (as a principal residence) within two years of the sale by that person of the original property. The term "purchase," as a requirement for the replacement dwelling, is used in Section 69.5(a)(1) and (g)(5), (6), and (7). [1]

For all property tax purposes, the word "purchase" is defined in Section 67 as "*a change in ownership for consideration.*" Thus, while the provisions of Section 69.5 do not specifically state that the replacement dwelling must be subject to reappraisal, the word "purchase," together with its statutory meaning (as a change in ownership), establishes that the replacement dwelling must be acquired in a manner that causes it to be reappraised and enrolled at a new base year value, e.g., as a change in ownership. In explaining Proposition 60 Chapter 186, Statutes of 1987 (Assembly Bill 60), Letter to Assessors, No. 87/71 September 11, 1987, outlined key elements of Section 69.5 and emphasized the Legislature's intent that any qualifying transfer, e.g., sale of the original property or purchase of the replacement property, must be made for consideration, as opposed to a transfer by gift or devise.

The present beneficiary of a trust is not required to "purchase" his/her interests in the trust property and assets, but becomes the beneficial or equitable "owner" of that portion

[1] Subdivision (g)(6), in describing the value of any replacement dwelling at the time of acquisition, expressly states that it requires a "purchase," i.e., "'Full cash value of the replacement dwelling' means its full cash value, determined in accordance with Section 110.1 as of the date on which it was purchased or new construction was completed, and after the purchase or the completion of new construction." Subdivision (a)(1), for example, provides for the transfer of "... the base year value of that [original] property to any replacement dwelling of equal or lesser value ... and is purchased or newly constructed by that person as his or her principal residence within two years of the sale by that person of the original property...".

designated as his/her share by gift or devise at the time the trust becomes irrevocable. That is, when the lifetime beneficiary's interest terminates, i.e., on the date of death of the surviving spouse, the present beneficial interests transfer without consideration to the trust beneficiaries. Even though the property and assets in this trust remained undistributed for a substantial time period after her mother's death, Mrs. S acquired beneficial ownership at that time. Thus, Mrs. S became the "owner" of a 33 1/3% interest in the Piedmont residence when her mother died and the trust became irrevocable.

The principle that the present beneficiary of an irrevocable trust is always considered the "owner" of the property in the trust (in contrast to the trustee who merely holds legal title) has been manifest since the enactment of the change in ownership statutes implementing Proposition 13. (Sections 61(h) and 62(d), and *Allen v. Sutter County Board of Equalization*, 1983, 149 Cal.App.3d 1091.) Moreover, the trust itself is never viewed as a separate entity for purposes of "owning" the real property or assets in the trust. Rather, the assessor must look through the trust to determine who has a vested present beneficial and equitable interest in the trust property.[2] The only exception is stated in Property Tax Rule 462.160 (e). A trust formed and operating as a Massachusetts business trust or similar trust, which is taxable as a legal entity and managed for profit for the holders of transferable certificates which entitle the holders to share in the income of the trust property, is treated as a separate legal entity.

Based on the foregoing, the "purchase" by Mr. and Mrs. S of the Piedmont residence from the trust does not meet the requirements of Section 69.5. Mrs. S's 33 1/3% interest was <u>not</u> a transfer resulting in a change in ownership *for consideration*, since she acquired it by gift or devise as a present beneficiary of the trust on the date of her mother's death. Even if the parent/child claim filed by Mrs. S under the Section 63.1 exclusion had been denied by the assessor and a change in ownership did result,[3] Mrs. S did not "purchase" her interest as required under Section 69.5 (a)(1) and (g)(5), (6), and (7). Instead, 33 1/3% of the $600,000 "purchase price" that she and her husband paid the trust in exchange for title to the replacement property she received back upon distribution from the trust, as the result of the trust interest acquired on her mother's death.

2. **<u>Partial Interest Purchase does not Qualify; the Entire Residence must be Purchased as an Appraisal Unit under Section 69.5(d) and (g).</u>**

The availability of the base year value transfer benefit to persons who are coowners in a given residence is provided for in Section 69.5(d). Under this provision, the benefit shall be available to a claimant who is the coowner of original property, as a joint tenant, tenant in common, or as a community property owner, "(1) If a single replacement dwelling is purchased or newly constructed by all of the coowners and each coowner retains an interest in the

[2] In contrast to federal income tax and estate tax law, California property tax statutes do not recognize the estate as a property owner, since a deceased person cannot possess beneficial title to real property.

[3] If the parent/child claim was granted, the provisions in Section 63.1 would have excluded the transfer of the residence from any change in ownership on her mother's death.

replacement dwelling ...". In such case, the claimant will be eligible for the benefit, whether or not any or all of the remaining coowners would otherwise be eligible claimants. This statutory language specifically allows the benefit to one coowner when the entire replacement dwelling is purchased by two or more coowners. The provision does not under any circumstances authorize the purchase of a partial interest in a replacement property.

The definitions of both "original property" and "replacement dwelling" found in Section 69.5(g)(3) and (4) also establish that 100% of the ownership interests in each appraisal unit must be sold and purchased, respectively. One reason for this requirement is that subdivisions (g)(5) and (6) mandate the assessor to make the "equal or lesser value" comparison of the full cash value between the whole original property sold and the entire replacement property purchased.

If the assessor here were to consider only the interest in the replacement dwelling purchased by Mr. S, the determination would be that Mr. S bought a partial or 50% interest from the trust, not in conformity with the requirements of Section 69.5. When Mrs. S used her share of the community property proceeds from the sale of their original dwelling in exchange for her 50% community property interest in the replacement dwelling, she received back 33 1/3% by devise under her parents' trust, such that 33 1/3% was a "gift" and not a "purchase." The remaining 16 2/3% was not remitted back, but "paid" for part of the trust distributions made to the other beneficiaries. Mr. S purchased his 50% community property interest in the replacement dwelling with his 50% share of proceeds from the sale of their original dwelling. Thus, the partial interests actually "purchased" in the replacement dwelling were 16 2/3% by Mrs. S and 50% by Mr. S; leaving 33 1/3% that was gifted or devised and not purchased. Under these facts, only 66 2/3% of the ownership interests in the replacement dwelling were "purchased" by Mr. and Mrs. S. The assessor could not make the equal or lesser value comparison based on a purchase of only 66 2/3% of the replacement dwelling. Accordingly, that Mr. S was not an heir or distributee of any interest of the trust is not determinative.

You contend, in effect, that whether or not Mrs. S received back part of the cash proceeds from the sale of their original property as part of her 33 1/3% share under the trust is immaterial to the determination that the entire replacement property was paid for by Mr. and Mrs. S. Unfortunately, where a particular property tax benefit requires by statute that 100% of the ownership interests in the appraisal unit must be purchased, failure to comply with the requirement disqualifies the taxpayer from receiving the benefit.[4]

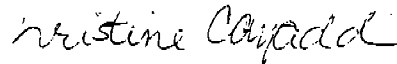
You also suggest that Mrs. S could have sold her interests in the replacement dwelling to Mr. S, thereby making him a qualifying purchaser of 100% of the dwelling. However, Article XIII A, Section 2(g) of the California Constitution expressly states what must be excluded from the term "purchase" in regard to a replacement dwelling. The language in Article XIII A,

[4] Your argument would be persuasive had the transaction between Mr. and Mrs. S and the trust been structured differently. If, for example, Mrs. S had disclaimed her interest under the trust and thereafter, she and her husband had purchased the entire replacement dwelling, the transfer of base year value benefit would have been available. In that case, Mr. and Mrs. S would have been purchasing 100% of the replacement dwelling from the other beneficiaries under the trust, the transfer would have been a change in ownership, and no interests would be transferred to Mrs. S by gift or devise.

Section 2(g) provides: "For purposes of subdivision (a), the terms "purchased" and "change in ownership" do not include the purchase or transfer of real property between spouses since March 1, 1975, ...". This provision is similar to and consistent with the interspousal exclusion from change in ownership in Section 63, which excludes from reappraisal any "purchase" or transfer between spouses.[5] Even if Mrs. S's 50% interest in the replacement dwelling had initially been her separate property, and even if Mr. S had acquired it from her as his separate property, a transfer between spouses is expressly precluded from being considered a "purchase" or "change in ownership" under Article XIII A, Section 2(g).

The views expressed in this letter are, of course, advisory only. They represent the analysis of the legal staff of the Board based on present law and the facts set forth herein, and are not binding on any person or public entity.

Sincerely,



Kristine Cazadd
Senior Tax Counsel

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Mr. David Gau, MIC:64
Mr. Charlie Knudsen, MIC:62
Ms. Jennifer Willis, MIC:70

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[5] Section 63 is quoted in pertinent part as follows:
"Notwithstanding any other provision in this chapter, a change of ownership shall not include any interspousal transfer, including but not limited to: * * *
(d) The creation, transfer, or termination, solely between spouses, of any coowner's interest."