



STATE BOARD OF EQUALIZATION
450 N STREET, SACRAMENTO, CALIFORNIA
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0082
TELEPHONE 916-324-2657 • FAX 916-323-3387
www.boe.ca.gov

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May 29, 2008

**Re: Base Year Value Transfers
Assignment No. 07-475**

Dear Dr. _____ :

This is in response to your November 1, 2007, letter to Assistant Chief Counsel Robert Lambert, in which you requested a legal opinion regarding a taxpayer’s ability to transfer his home’s base year value to his rental property with or without the use of an intermediary such as yourself. As explained more fully below, a taxpayer can only transfer the base year value of his home to a qualified replacement property if that replacement property is actually acquired or newly constructed after the taxpayer’s home is substantially damaged or destroyed by a Governor declared disaster, or purchased or newly constructed within two years of when the home is sold. Therefore, the taxpayer may not transfer his home’s base year value to a rental property that he owns at the time his home is sold or substantially damaged or destroyed by a Governor declared disaster, and was not purchased or newly constructed within two years of the sale of his home. In addition, a county assessor should not recognize an arrangement whereby the taxpayer sells or transfers his rental property to you and you sell or transfer the property back to the taxpayer as creating the required acquisition or purchase.

Factual Background

In your letter you explain that you have a friend (taxpayer) who lost his home in a 2007 wildfire, which we assume was one of the numerous Governor declared disasters listed on the Board’s Website at www.boe.ca.gov/proptaxes/pdf/DisasterList.pdf.¹ The taxpayer is a senior citizen and, based upon his age, would qualify to transfer his home’s base year value to another residence under Revenue and Taxation Code section² 69.5, discussed below. However, the

¹ Disasters included on this list are considered “disasters” for which base year value transfer relief is available under Revenue and Taxation Code sections 69 and 69.3.

² Section references are to the Revenue and Taxation Code unless otherwise indicated.

taxpayer does not want to rebuild the home that was destroyed and does not want to buy another house. Rather, he would prefer to transfer his home's base year value to a rental property he already owns, and which is suitable for him to occupy.

A county assessor's staff has informed you that the taxpayer cannot transfer his home's base year value to the rental property under the circumstances you describe, but suggested that you could contact the Board of Equalization for additional guidance. Your letter suggests that you are considering a "paper sale" transaction in which the taxpayer would sell the rental property to you at a price equal to his income tax basis and then purchase the property back from you for the same amount, if it would help the taxpayer qualify to transfer his base year value. However, you are aware of the step-transaction doctrine and are only willing to do the "paper sale" if it will help facilitate the transfer of the taxpayer's base year value and the "paper sale" is disclosed to the county assessor in an ethical manner.

Law and Analysis

Section 69 allows any person to transfer the base year value of property that was substantially damaged or destroyed by a Governor declared disaster to comparable replacement property located in the same county that is acquired or newly constructed within three years after the disaster, if other statutory requirements are satisfied. Section 69.3 allows a person to transfer a base year value of property destroyed or damaged by a Governor declared disaster to comparable replacement property located in another county, if the county where the replacement property is located adopts an ordinance permitting the base year value transfer. Section 69.5, subdivision (a)(1) allows any person who is 55 years of age or older or severely and permanently disabled to transfer his or her home's base year value to a replacement dwelling, located in the same county, that is purchased or newly constructed within two years after the taxpayer's home is sold, if other statutory requirements are satisfied. Section 69.5, subdivision (a)(2) extends this relief to a replacement property located in another county, if the county where the replacement property is located adopts an ordinance permitting the base year value transfer, and the other requirements of section 69.5 are satisfied. As of January 1, 2007, Alameda, Los Angeles, Orange, San Diego, San Mateo, Santa Clara, and Ventura counties had adopted ordinances pursuant to section 69.5, subdivision (a)(2).

Under section 69, subdivision (a) and section 69.3, subdivision (a)(1), a person is not allowed to transfer the base year value of property that was substantially damaged or destroyed by a Governor declared disaster to replacement property the person owned prior to the damage or destruction because the replacement property must be acquired or newly constructed within three years *after* the damage or destruction. Section 69.5, subdivisions (a)(1) and (b)(5), only allow a person to transfer his or her home's base year value to a replacement dwelling the taxpayer owned at the time his or her home was damaged or destroyed, if the replacement dwelling was purchased or newly constructed "within two years of the sale" of the taxpayer's original property. Therefore, the taxpayer referred to in your letter would not be able to transfer the base year value of his home to rental property the taxpayer owned before his home was substantially damaged or destroyed by a Governor declared disaster under sections 69 or 69.3, and would only be able to transfer its base year value under section 69.5 if he sells the damaged or destroyed property within two years of when he purchased the rental property.

Although the taxpayer could sell or otherwise transfer his rental property to you and have you either sell or transfer the rental property back to the taxpayer for purposes of making it appear as if the taxpayer acquired the rental property after his home was sold or substantially damaged or destroyed by a Governor declared disaster, or purchased it within two years of when the home was sold, county assessors can disregard such a transfer under the step-transaction doctrine. The step-transaction doctrine allows county assessors to disregard the intermediary steps in what is in substance a single, unitary or indivisible transaction and thereby apply the tax laws to the substance of the transaction and not the form of its steps. The step-transaction doctrine applies to multi-step transactions when:

- The parties have a binding commitment to carryout each step in the transaction before the first step is executed; or
- All of the steps are so interdependent that the parties would not have executed any of the steps unless they were reasonably certain that they would complete all the steps; or
- All of the steps appear to be prearranged parts of a single transaction that was intended to reach a certain ultimate result from the outset.

(See Property Tax Annotation 220.0666 (C. March 8, 1990).)³

The step-transaction doctrine could be applied to the taxpayer's transfer or sale of his rental property to you and your transfer or sale of the rental property back to the taxpayer because either you and the taxpayer would have a binding commitment to carry out all of the steps before executing the initial transfer, or, the taxpayer would not make the first transfer if he was not reasonably certain you would make the second transfer, and both transfers would be parts of a single, prearranged transaction intended to reach the end result of circumventing the statutory requirements of sections 69, 69.3, and 69.5. The Legal Department is not aware of any exceptions that would prevent the application of the step-transaction doctrine under the circumstances you describe.

³ Property Tax Annotations are summaries of the conclusions reached in selected legal rulings of Board counsel published in the Board's Property Tax Law Guide. (See Cal. Code Regs., tit. 18, § 5700 for more information regarding annotations.)

May 29, 2008

The views expressed in this letter are only advisory in nature; they represent the analysis of the Board's Legal Department based on present law and the facts set forth herein, and are not binding on any person or public entity.

Sincerely,

/s/ Bradley M. Heller

Bradley M. Heller
Tax Counsel III (Specialist)

BMH:pb

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cc: Honorable Kenneth Stieger, President
California Assessors' Association
3701 Power Inn Road, Suite 3000
Sacramento, 95826-4329

Mr. David Gau	MIC:63
Mr. Dean Kinnee	MIC:64
Mr. Todd Gilman	MIC:70