



STATE BOARD OF EQUALIZATION

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April 20, 2012

**Re: , Inc – Change in Ownership
 Assignment No.: 12-011**

Dear Mr. :

This is in response to your letter requesting our opinion on whether a proposed restructuring of the ownership of an office building constitutes a change in ownership. As explained fully below, we agree with you that the transfers will not result in any changes in ownership. However, we disagree with your conclusion that the transfers qualify for the exclusion from change in ownership for transfers among members of an affiliated group. Accordingly, the transfers, although excluded from change in ownership, will result in the holders of the interests in the transferee entities becoming "original co-owners" for purposes of future transfers of those interests.

Facts

The subject property is a high-rise office building at Street in . It consists of four office condominiums (collectively, the Parcels) currently owned as follows: Parcel 14 is owned by M L Company, a New York corporation (ML), and M T Company, a Delaware corporation (MT) owns Parcels 15, 16, and 17. Both ML and MT are wholly owned subsidiaries of M , Inc., a publicly-traded corporation (M). The parties want to restructure the ownership of the Parcels for proprietary purposes in a way that will retain the established base year assessed values.

The proposed structure is for both owners of record, ML and MT, to transfer their respective interests in the Parcels to a newly formed limited liability company, New Joint Venture LLC (NJV), in which ML will hold a 30 percent capital and profits interest and MT will hold a 70 percent capital and profits interest. M will continue to own 100 percent of the voting stock of both ML and MT. Subsequent to this transaction, NJV will transfer the Parcels to a newly formed 100 percent wholly owned subsidiary, New Joint Venture Subsidiary A (Subsidiary A). You ask whether these transfers will result in a change in ownership of the Parcels.

Alternatively, you ask whether ML and MT can convey their respective interests directly to Subsidiary A rather than first transferring their interests to NJV.

Law & Analysis

Article XIII A, section 2 of the California Constitution requires the reassessment of real property upon a "change in ownership," unless an exclusion from change in ownership applies. A change in ownership is defined in Revenue and Taxation Code section¹ 60 as "a transfer of a present interest in real property, including the beneficial use thereof, the value of which is substantially equal to the value of the fee interest."

Under section 61, subdivision (j) (hereafter Section 61(j)), the transfer of any interest in real property to or from a legal entity is a change in ownership and results in reappraisal of the property transferred. Section 62, subdivision (a)(2) (hereafter Section 62(a)(2)) provides an exclusion from change in ownership under Section 61(j), for proportional ownership interest transfers of real property between an individual and a legal entity or between legal entities. To qualify for the exclusion, such transfers must result solely in a change in the method of holding title to the real property, and the proportional ownership interests of the transferors and transferees in each and every piece of real property transferred must remain exactly the same both before and after the transfer.

Section 64, subdivision (d) (hereafter Section 64(d)), provides that when a transfer of real property is excluded from change in ownership under Section 62(a)(2), the holders of the legal entity interests immediately after the excluded transfer become "original co-owners" for purposes of determining the change in ownership consequences of any subsequent transfers of those legal entity interests. Subsequently, whenever voting shares or other ownership interests representing cumulatively more than 50 percent of the total interests in the legal entity are transferred by any of the original co-owners in one or more transactions, a change in ownership of that real property owned by the legal entity that was previously excluded from change in ownership under Section 62(a)(2) occurs. Proportional interest transfers of original co-owner interests are not cumulated or counted for this purpose. (Property Tax Rule² 462.180, subdivision (d)(2)).

Section 64, subdivision (b) (hereafter Section 64(b)) provides a second exclusion to changes in ownership under Section 61(j). It provides that any transfer of real property among members of an affiliated group is not a change in ownership. For purposes of Section 64(b), "affiliated group" is defined as one or more chains of corporations connected through stock ownership with a common parent corporation if: (1) 100 percent of the voting stock (exclusive of that owned by directors) of each of the corporations, except the parent corporation, is owned by one or more of the other corporations; and (2) the common parent corporation owns, directly, 100 percent of the voting stock (exclusive of that owned by directors) of at least one of the other corporations. Transfers that qualify under Section 64(b) do not result in the creation of original co-owner status under Section 64(d) as do transfers that qualify for exclusion under Section 62(a)(2).

¹ All further "section" references are to the Revenue and Taxation Code.

² Cal. Code Regs., tit. 18, § 462.180, subd. (d)(2). Further references to "Rules" are to sections of title 18 of the California Code of Regulations.

Section 64(b) Affiliated Group Transfers

Your letter states that the transfers qualify for the exclusion under Section 64(b). We disagree. Section 64(b), by its express terms, only applies to transfers among members of an affiliated group, and the definition of an affiliated group requires the common ownership to be among *corporations*. (See also Assessors' Handbook Section 401, page 52; Rule 462.180, subdivision (b)(1)). In this case, the transfers are to limited liability companies, so NJV and Subsidiary A are not members of an affiliated group with M, ML and MT. Accordingly, the exclusion under Section 64(b) is inapplicable.

Transfer of Parcel 14 to NJV

Because it is a transfer of real property from one legal entity to another, ML's transfer of Parcel 14 to NJV results in a change in ownership of Parcel 14 under Section 61(j), unless an exclusion applies. Because M would still indirectly own 100 percent of Parcel 14 through ML and MT, the transfer is excluded from change in ownership under Section 62(a)(2). However, under Section 64(d), ML and MT, as the holders of the ownership interests in NJV immediately after the transfer, are considered the original co-owners with respect to future transfers of the capital and profits interests in NJV.

Transfer of Parcels 15, 16 and 17 to NJV

Because they are transfers of real property from one legal entity to another, the transfers of Parcels 15, 16 and 17 to NJV result in changes in ownership under Section 61(j), unless an exclusion applies. Because M would still indirectly own 100 percent of Parcels 15, 16 and 17 through ML and MT, the transfers are excluded from change in ownership under Section 62(a)(2). As with the transfer of Parcel 14, under Section 64(d), ML and MT, as the holders of the ownership interest in NJV immediately after the transfers, are considered the original co-owners with respect to future transfers of the capital and profits interests in NJV.

Transfer of Parcels from NJV to Subsidiary A

Because they are transfers of real property from one legal entity to another, the transfers of the Parcels from NJV to Subsidiary A result in changes in ownership of the Parcels under Section 61(j), unless an exclusion applies. Because M would still indirectly own 100 percent of the Parcels through its direct ownership interest in ML and MT, and its indirect ownership interest in NJV, the transfers would qualify for the exclusion under Section 62(a)(2). Under section 64(d), NJV, as the holder of the ownership interests in Subsidiary A immediately after the transfers, would be considered the original co-owner with respect to future transfers of the capital and profits interests in Subsidiary A.

We note that after these transfers, ML and MT would remain original co-owners in NJV, such that future transfers of the NJV capital and profits interests would result in deemed indirect transfers of the Subsidiary A capital and profits interests for purposes of potential changes in ownership under Section 64(d).

Transfer of Parcels Directly From ML and MT to Subsidiary A

You ask whether it would make any difference if, instead of first transferring the Parcels to NJV, ML and MT transfer the Parcels directly to Subsidiary A. The change in ownership analysis would be the same. The transfers would result in changes in ownership of the Parcels under Section 61(j), but the transfers would be excluded under Section 62(a)(2). The only difference that arises between the different methods of restructuring the above interests is who ultimately becomes the original co-owner. In this case, only NJV would be an original co-owner in Subsidiary A, and ML and MT would not become original co-owners in NJV.

The views expressed in this letter are only advisory in nature. 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. Should you have any additional questions, please feel free to contact me.

Sincerely,

/s/ Neha Duggal

Neha Duggal
Tax Counsel

ND:mcb

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cc: Honorable

County Assessor

Mr. David Gau MIC:63

Mr. Dean Kinnee MIC:64

Mr. Todd Gilman MIC:70