

220.0207 **Exclusions.** When determining if a transfer to a legal entity is excluded from change-in-ownership because only a change in the manner of holding title, without any change in the proportional ownership interests of the transferors, has occurred, amounts paid by the legal entity to one partner, stockholder, etc. for extra services rendered are not taken into consideration. Guaranteed payments (the term used in Internal Revenue Code section 707) which are determined without regard to the income of the legal entity and which are paid in consideration of the performance of services by the recipient on an arm's-length basis do not constitute additional ownership interests in the legal entity for purposes of Revenue and Taxation Code section 62(a)(2). C 8/14/89.



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August 14, 1989

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Dear _____

I am writing in response to your letter dated June 20, 1989, wherein you request an opinion on the change in ownership consequences of a series of proposed transactions.

The facts set forth in your letter and as related to me via our telephone conversation are summarized below:

Facts

1. Your client owns a 50 percent interest in a partnership with her ex-spouse. The partnership owns certain real property together with the retail business situated thereon.
2. While the beneficial ownership of such real property is held by the partnership, record title is held 50 percent by the taxpayer and 50 percent by her ex-spouse (pursuant to the parties' 1978 marriage dissolution decree). Due to the confused state of the record, you are uncertain as to whether or not such record title is as joint tenants or tenants-in-common. In its records, the Los Angeles County Assessor incorrectly shows the taxpayer and her son as the co-owners of the property.
3. There is no written partnership agreement. All partnership capital is owned 50/50, and all net partnership income and loss is equally allocated between the taxpayer and her ex-spouse. The ex-spouse, however, contributes more of his time to the partnership than the taxpayer. In return, he receives "compensation" of \$500.00 per week, as opposed to the taxpayer's \$300.00 per-week draw. The partnership accountant characterizes the \$200.00 difference in weekly draws as a guaranteed payment, which he treats as a tax expense, offsetting gross revenue.
4. You have formed a revocable living trust for your client, of which she is the sole trustee during her lifetime and

70

August 14, 1989

capacity. The taxpayer has assigned her interest in the partnership to the revocable trust.

Law and Analysis

Unless otherwise specifically indicated, all section references are to the Revenue and Taxation Code.

Initially, we note the following:

(1) The fact that the Los Angeles County Assessor may erroneously reflect the taxpayer and her son as the owners on the tax rolls is, for our purposes, irrelevant. To correct this error, you must bring it to the assessor's attention.

(2) This office has previously concluded that, for property tax purposes, revocable trusts are deemed to be solely beneficially owned by their trustors. Therefore, a transfer from a trustor to a revocable trust is not generally deemed to be a transfer of a beneficial interest. Any questions from the assessor's offices regarding the trust can best be satisfied by providing a copy of the trust instrument.

(3) Section 662 of the Evidence Code sets forth a presumption that a deed grants full beneficial title to its recipient, unless such presumption is overcome by clear and convincing proof to the contrary. Therefore, the county assessor will be justified in assuming that the taxpayer and her ex-spouse individually co-own the property (as set forth in the official records), unless you can establish that the partnership is, in fact, the beneficial owner by clear and convincing proof.

With the above in mind, the specific proposed transactions are analyzed below:

Step 1

Proposed action: Record deed from taxpayer and ex-spouse to taxpayer and ex-spouse as 50/50 tenants-in-common.

Analysis: As indicated above, it is unclear as to whether or not record title is presently held in the name of the taxpayer and her ex-spouse as joint tenants or as tenants-in-common. This proposed step would, in any event, clarify the issue by implementing the 1978 dissolution decree dividing the property, for purposes of record title, into two separate estates.

Assuming that the two individuals (and not the partnership) beneficially own the property, such transfer would merely carry out the provisions of the parties' marriage dissolution decree,

August 14, 1989

however long after the fact. Under such assumption, we would agree with your conclusion that the transfer is exempt from change in ownership consequences under section 63(c).

On the other hand, assuming that the partnership (and not the two individuals) beneficially owns the property, the transfer would have to be analyzed under section 62(a)(2), as set forth below in the "Step 2" analysis.

Step 2

Proposed action: Record deed from taxpayer and ex-spouse to the partnership.

Analysis: You state that the partnership beneficially owns the property. Section 62(b) provides that:

Change in ownership shall not include:

* * *

(b) Any transfer for the purpose of perfecting title to the property.

Providing that you can prove by clear and convincing evidence that beneficial ownership of the property is, in fact, vested in the partnership, the transfer will be exempt from change in ownership consequences under said section 62(b).

In addition, section 62(a)(2) provides in pertinent part as follows:

Change in ownership shall not include:

* * *

(a)(2) Any transfer between an individual or individuals and a legal entity or between legal entities, such as a cotenancy to a partnership, a partnership to a corporation, or a trust to a cotenancy, which results solely in a change in the method of holding title to the real property and in which proportional ownership interests of the transferors and transferees, whether represented by stock, partnership interest, or otherwise, in each and every piece of real property transferred, remain the same after the transfer. . . .

August 14, 1989

If we assume that the taxpayer and her ex-spouse beneficially own the partnership on a 50/50 basis, any transfer from a 50/50 co-tenancy to the partnership will be excluded from change in ownership consequences under said section 62(a)(2). Here, however, the ex-spouse receives larger weekly distributions than the taxpayer. The partnership accountant describes the excess portion as a guaranteed payment. The question, therefore, arises as to whether or not the ex-spouse's right to receive such guaranteed payment from the partnership causes his actual beneficial ownership interest in the partnership to be in excess of 50 percent. If so, section 62(a)(2) will be inapplicable to the proposed transfer as the parties' respective proportional ownership interests in the partnership will differ from their interests in the co-tenancy.

We have not been given sufficient information with regard to the specific details of the subject guaranteed payment to render an opinion in the instant case. However, it appears to us that guaranteed payments (as the term is used in Internal Revenue Code section 707) which (i) are determined without regard to the income of the partnership, and (ii) are paid in consideration of the performance of services by the recipient on an arm's-length basis, should not be deemed to constitute additional partnership interest on the part of such recipient for purposes of section 62(a)(2). On the other hand, guaranteed payments which (i) are determined with regard to partnership income or (ii) are not related to the performance of services, might, under the particular facts presented, cause the recipient to be deemed to have received additional interest in the partnership for purposes of section 62(a)(2).

Step 3

Proposed action: Record quitclaim deed from ex-spouse's current wife to ex-spouse.

Analysis: As this deed is between spouses, the transfer is exempt from change in ownership consequences pursuant to section 63(d).

Step 4

Proposed action: Record statement of partnership showing the taxpayer and her ex-spouse as equal members of the partnership.

Analysis: The recording of the statement of partnership is only significant as an indication of the ownership of the subject partnership. Here, the statement represents that the taxpayer and her ex-spouse are equal partners. Whether or not

August 14, 1989

the local assessor's office is satisfied with the statement is in its judgment. It is possible (but not necessarily likely) that a copy of a written agreement tax return or other document might be requested in confirmation of the statement.

The views expressed in this letter are advisory only and are not binding upon the assessor of any county. You may wish to consult the Los Angeles County Assessor and any other involved assessor in order to confirm that the subject property or properties will be assessed in a manner consistent with the conclusions stated above.

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

Very truly yours,



Robert W. Lambert
Tax Counsel

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cc: Los Angeles County Assessor
Mr. John W. Hagerty
Mr. Verne Walton