STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
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January 24, 1997

In Re: **Change in Ownership - Transfer of Leased Land by Homeowner/Lessee.**

Dear Mr. H

This is in response to your letter of October 9, 1996, to Mr. Eric Eisenlauer in which you request our opinion as to whether the transfers of assignments of leases of real properties to you and to others who purchased residences on leased lands are changes in ownership under Revenue and Taxation Code Section 61(c).

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

1. Mr. and Mrs. H purchased a weekend/vacation residence at y in Ventura County in 1993. The purchase included the transfer of (a) ownership of the structure, and (b) assignment of the seller/lessee's interest in a lease of the land, which, at the time of purchase, had 27 years remaining.

2. The Ventura County Assessor viewed the purchase/transfers of both the structure and the leased land as changes in ownership, reassessed the structure, and reassessed the leased land pursuant to Section 61(c)(2). Subsequently, Mr. and Mrs. H requested the Ventura County Assessor to redetermine whether the leased land should be reassessed, because: (a) the conclusive presumption at the end of Section 61(c)(2) is not applicable to residences that are not eligible for the homeowners' exemption and the lease assigned had a remaining term of less than 27 years; and (b) the conclusive presumption at the end of Section 61(c)(2) was never intended to apply to transfers of a leasehold interest by the lessee/homeowner under Section 61(c)(1).

3. Upon reconsideration of evidence submitted by Mr. and Mrs. H that their residence was not eligible for the homeowners' exemption and the remaining lease term was less than 35 years, the Assessor canceled the reassessment on the leased land, on the grounds that the conclusive presumption in Section 61(c)(2) is not applicable in the case of a residence that is not eligible for the homeowners' exemption, and the lease assigned had a remaining term of less than 35 years. The Assessor refused to agree, however, that the conclusive presumption was not applicable to transfers by lessee/homeowners, or that the provisions of Section 62(g) would exclude the lease transfer from change in ownership. Therefore, other lessee/homeowners have filed applications for reassessment for the purpose of challenging the Assessor's determination regarding similar transfers or assignments of leases that have been regarded as changes in ownership and subject to reassessment.

You believe that in light of the legislative history and express language of the exclusion in Section 62(g), the conclusive presumption in Section 61(c) is intended to apply, and is properly applied, only to transfers or assignments of leases by lessors, and not by the lessee/homeowners. For the reasons hereinafter explained, we respectfully disagree and support the Assessor's change in ownership determinations and reassessments in those matters.

LAW AND ANALYSIS

As you are aware, Revenue and Taxation Code Section 60 defines a change in ownership 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."

Whether or not a particular transaction involving real property falls within this definition depends upon the facts in each case. To be a "change in ownership" under Section 60, the particular transaction must embody the following three characteristics contained in the definition:

(1) It transfers a present interest in real property;
(2) It transfers the beneficial use of the property; and
(3) The property rights transferred are substantially equivalent in value to the fee interest.

Also within that definition is the provision of Section 61(c) which includes as a change:

"(1) The creation of a leasehold interest in taxable real property for a term of 35 years or more (including renewal options), the termination of a leasehold interest in taxable real property which had an original term of 35 years or more (including renewal options), and any transfer of a leasehold interest having a remaining term of 35 years or more (including renewal options); or

"(2) any transfer of a lessor's interest in taxable real property subject to a lease with a remaining term (including renewal options) of less than 35 years.

"Only that portion of a property subject to that lease or transfer shall be considered to have undergone a change of ownership.

"For the purpose of this subdivision, for 1979-80 and each year thereafter, it shall be conclusively presumed that all homes eligible for the homeowners' exemption, other than manufactured homes located on rented or leased land and subject to taxation pursuant to Part 13 (commencing with Section 5800), that are on leased land have a renewal option of at least 35 years on the lease of that land, whether or not in fact that renewal option exists in any contract or agreement."

The exclusion from change in ownership applicable to the foregoing transfers under Section 61(c)(1) and (2) is found in Section 62(g), which provides as follows:

"Change in ownership shall not include:

* * *

"(g) Any transfer of a lessor's interest in taxable real property subject to a lease with a remaining term (including renewal options) of 35 years of more. For the purpose of this subdivision, for 1979-80 and each year thereafter, it shall be conclusively presumed that all homes eligible for the homeowners' exemption, other than mobilehomes located on rented or leased land and subject to taxation pursuant to Part 13 (commencing with Section 5800), which are on leased land and have a renewal option of at least 35 years on the lease of that land, whether or not in fact that renewal option exists in any contract or agreement."

Your concern is the interpretation and applicability of the conclusive presumptions stated in Sections 61(c) and 62(g) on transfers by a **lessee**/homeowner of a leasehold interest having a remaining term of 35 years or more, pursuant to Section 61(c)(1). Specifically, you wish to know why the State Board staff and the Ventura County Assessor interpret the conclusive presumption in Sections 61(c) and 62(g) so as to result in any transfer of a lessee/homeowner's interest in leased land being a change in ownership and subjecting the land to reappraisal. In your view, the legislative purpose of the conclusive presumption in both Sections 61(c) and 62(g) was to protect lessee/homeowners from change in ownership and reassessment of the leased lands, regardless of whether the lessor or the lessee executed the transfer or assignment.

Unfortunately, this view is inconsistent with the clear intent and language of the statutory scheme pertaining to leases. Our position is: 1)that the conclusive presumption in Section 61(c) makes the lessee/homeowner of a home eligible for the homeowners' exemption on leased land equivalent to the "**owner**" of the land for change in ownership purposes, with the result that transfers by the lessor are not a change in ownership but transfers/assignments by a lessee/homeowner are; and 2) that the change in ownership exclusion (including the conclusive presumption) in Section 62(g) limits its application exclusively to lessors' transfers of lands subject to leases of 35 years or more, and does not extend to transfers by lessee/homeowners.

Section 61(c) conclusive presumption makes the lessee/homeowner of a home eligible for the homeowners' exemption on leased land equivalent to the "owner" of the land for change in ownership purposes.

In implementing Proposition 13, the Legislature, from the outset, took a "one-owner approach" to all change in ownership determinations. In lease transactions, the tenant was always

treated as the **owner** of property subject to a lease with a remaining term (including renewal options) of 35 years or more. The rationale behind the 35-year "dividing line" was and is that long term leases (35 years or more) are "substantially equivalent in value to the fee interest" per Section 60, while in cases of leases that are less than 35 years, the value equivalent to the fee interest is retained by the lessor. A thorough analysis of this distinction was stated by the Court of Appeal in *Howard v. County of Amador* (1990) 220 Cal.App.3d 970. In its discussion, the court quotes at length (page 974) from the Report of the Task Force on Property Tax Administration, presented to the Assembly Committee on Revenue and Taxation (1979), as follows:

> As the task force explained it, "[t]he 'value equivalence' test is necessary to determine who is the primary owner of the property at any given time. Often two or more people have interests in a single parcel of real property. Leases are a good example. The landlord owns the reversion; the tenant, the leasehold interest. Suppose the landlord sells the property subject to the lease and the lessee assigns the lease. Which sale or transfer is the change in ownership?
>
> The example illustrates that in determining whether a change in ownership has occurred it is necessary to identify but ***one*** primary owner. Otherwise assessors would be forced to value, and account for separate base year values for landlords and tenants on all leases, and for other forms of split ownership. This would enormously complicate the assessor's job.
>
> A major purpose of this third element, therefore, is to avoid such unwarranted complexity by identifying the primary owner, so that only a transfer by him will be a change in ownership, and when it occurs the *whole* property will be reappraised. If the hypothetical lease previously mentioned was a short term lease (the landlord owned the main economic value), the landlord's sale, subject to the lease would count. If, on the other hand, the lease was a long term lease (the lessee's interest was the main economic package), the lease assignment would count. In either case the entire fee value of the leased premises would be reappraised." (Rep. of the Task Force on Property Tax Admin., presented to the Assem. Com. on Rev. & Tax. (1979) pp. 39-40, italics in original.)
>
> The task force recommended the use of statutory examples to elaborate on common transactions. "Leases are a good illustration of the necessity of concrete statutory examples. Both taxpayers and assessors need a specific test--rather than the broad 'value equivalence' test--to determine the tax treatment of leases. The specific test[,] however, must be consistent with the 'value equivalence' rule and have a rational basis. Lenders will lend on the security of a lease for 35 years or longer. Thus, 35 years was adopted as a concrete dividing line. If the term of a lease, including options to renew, is 35 years or more, the creation of the lease is a change in ownership and so is its expiration. If a lessee under such a lease assigns or sublets for a term of 35 years or more, that is another change in ownership. However, if the lease, including options, is for less than 35 years the lessor remains the owner and only the transfer of his interest is a change. In all cases, the entire premises subject to the lease in question are reappraised." (Id. at p. 41.).

It is clear from the foregoing that under a standard lease situation, if the lessor creates a leasehold of 35 years or more and the tenant subleased the property or assigned the leasehold interest for the remaining term (35 years or more), the property would undergo a change in ownership and reappraisal, since the tenant was considered the "owner". The Legislature expressly stated this conclusion in the first sentence in Section 61(c)(1). Conversely, if the property is subject to a lease with a remaining term of less than 35 years, the lessor is treated as the "owner," and the transfer of the property by the lessor triggers a change in ownership and reappraisal. This general rule of "equivalent fee ownership," based upon a 35-year term, governed all leases and transfers involving leased real property with a single exception.

In 1979, shortly after the original statute was adopted, the Legislature confronted a unique problem pertaining to certain leased lands in Orange County. A large number of residential lots, some improved with single family homes, were transferred by the lessor to the Irvine Company. Many of the lots were leased to homeowners under leases that had less than 35 years to run, subjecting those properties to change in ownership and reappraisal. To avoid that result, the Legislature adopted the conclusive presumption language in Sections 61(c) and 62(g), which expressly provides that wherever a home eligible for the homeowners' exemption is on leased land, the term of such lease shall be conclusively presumed to have a 35-year renewal option for all purposes. Under this "fictional term exception," the real term of the lease was to be disregarded by the assessor, and the 35-year "fictional term" applied. The fact that the remaining term of the lease may actually be less than 35 years is not relevant or material, because the conclusive presumption makes the tenant the "property owner" for all transfers. (See Rigby Letter, 5/4/82, copy enclosed.)[1]

There is no ambiguity either in the express language or placement of the conclusive presumption at the conclusion of Section 61(c). The presumption clearly establishes that the "equivalent fee interest" in property where "homes eligible for the homeowners' exemption ... are on leased land" is "owned" by the lessee, because the lease is presumed to have a 35-year renewal option. The placement of this conclusive presumption at the end of Section 61(c) does not mean that the presumption applies only to paragraph (2) and not to paragraph (1) of subdivision (c) as you indicate in your letter. The language in the conclusive presumption states that it applies "for the purposes of this subdivision...". The term "subdivision" refers to the entirety (both paragraphs (1) and (2)) of subdivision (c) in Section 61, not merely to paragraph (2) of subdivision (c). In the Legislative Drafting Manual, 1975, Legislative Counsel of California, George H. Murphy, #462, where a cross-reference is made to a subdivision of a section of codified law, the word "subdivision" refers to the lettered subdivision (subsection) of a section of that law. The following instruction on page 28 of the Legislative Drafting Manual, section 73 is dispositive on this point:

> "73. *Enumerations Within Sections.* Small letters in parentheses are used for the designation of enumerated paragraphs and arabic numbers for the designation of enumerated subparagraphs within sections. Example:

[1] Where the law raises a conclusive presumption, evidence cannot be received to the contrary. A conclusive presumption is, in reality, not a rule of evidence but a substantive law so fixed by the legislative body as to admit no controverting proof. 31 Cal.Jur.3rd 104.

'912.6 (a) In the case of a claim ..., the board may act in one of the following ways:

'(1) If the board finds the claim is a proper charge, it shall allow the claim.

'(2) If the liability is disputed, the board may reject the claim.

'(b) If the board allows the claim, it may require the applicant to accept it in full settlement.'

For reference purposes, paragraphs are termed 'subdivisions' of the section in which they are contained and subparagraphs are called 'paragraphs' of subdivisions. Thus, a reference to the first subparagraph of the first paragraph in the above example would be: 'paragraph (1) of subdivision (a) of Section 912.6...'."

Based on the foregoing authority, there is no question that the phrase, "For the purposes of this subdivision...", introducing the conclusive presumption, refers to subdivision (c) of Section 61. Had the author intended for the conclusive presumption to apply only to paragraph (2) of subdivision (c), the legislative drafters would have referred to "this paragraph" rather than "this subdivision".

Moreover, in light of the legislative purpose and history of the conclusive presumption (discussed above), there is no ambiguity in ascertaining that its proper application is to both paragraphs (1) and (2) of subdivision (c). The conclusive presumption establishes a "fictional" long term lease held by each succeeding lessee "...whether or not in fact that renewal option exists...". so that the lessee is "protected" from any transfers by the lessor. The perpetual 35-year term creates a "fee ownership interest" in the land on the part of the lessee, with the result that the lessor will <u>never</u> be considered the "fee owner," and therefore, will never by his or her transfer of his or her lease interest trigger a change in ownership and reappraisal of the property. The Legislature's simultaneous enactment of Section 62(g) provided double assurance that no transfer made by the lessor in these circumstances would ever trigger a change in ownership.

Because the <u>lessee</u> will always be the "fee owner" for change in ownership purposes, the only time the underlying land can or will undergo change in ownership is on transfer by the lessee. This is consistent with the legislative scheme in Section 61(c)(1) and (2), which provides in Section 61, "Except as otherwise provided ... change in ownership ... **includes** ..." [Section 61(c)(1)] "...any transfer of a leasehold interest having a remaining term of 35 years or more." There is no ambiguity in this provision; the transfer or assignment of leased land for a term of 35 or more years is a change in ownership apart from an applicable exclusion. Moreover, even if there were uncertainty, under accepted principles of statutory interpretation, unless its would lead to absurd results, courts will follow the actual language used and give to it its plain meaning, even if it appears that a different object was in the mind of the Legislature. <u>County of Sacramento v. Hickman</u>, 66 C2d 841.

<u>The exclusion in Section 62(g), including the conclusive presumption, is limited to lessors' transfers of lands subject to leases of 35 years or more, and does not extend to transfers by lessee/homeowners.</u>

As indicated above, the history and purpose of the Legislature in enacting the conclusive presumption language in Sections 61(c) and 62(g) was to exclude from change in ownership transfers of the lessor's interests in the lands underlying all homes eligible for the homeowners' exemption. In the legislative summary of the Revisions to AB 1488, August 31, 1979, (see Augusta Memorandum, Sept. 5, 1979, Status of AB 1019 and AB 1489, copy enclosed), this purpose is stated as follows:

> Leases
> 1. Adds conclusive presumption that all homes eligible for the homeowners exemption which are on leased land shall have a "renewal option" of at least 35 years, whether the lease so specifies or not. This will ensure that such homeowners will not receive increased assessments due to a transfer, not by them, but by the lessor, if at such time there is less than 35 years remaining on the lease, without such a renewal option. (61(c), 62(g) R&TC)

It is clear from the second sentence in the phrase,"... **not by them**, but by the lessor,..." that the conclusive presumption added to Section 62(g) was intended to apply to transfers of the leased land by the lessor, not by the lessee. In a letter dated September 20, 1979, by the author of the legislation, Assemblyman Thomas M. Hannigan, to Governor Edmund G. Brown (copy enclosed), summarizing the important provisions of the bill, the exact same language as that used in the legislative analysis was set forth as an explanation for Sections 61(c) and 62(g). Clearly, the intent of the author of the legislation was that the conclusive presumption was applicable only to lessor transfers, and that lessee transfers of land presumed to be under a 35-year lease were not excluded from change in ownership.

Further evidence of the legislative intent indicating that the conclusive presumption language of Sections 61(c)(2) and 62(g) applies to transfers by the lessor, not the lessee, is found in a report issued by the Assembly Revenue and Taxation Committee stating the following:

> "The purpose of this provision is to protect those homeowners who own the dwelling but lease the land, where the lessor sells his interest in the land. Prior to passage of AB 1019, in cases where a homeowner's remaining lease term was less than 35 years, reassessment would occur without this provision. The immediate problem was on Irvine Company land in Orange County. With many leases of less than 35 years remaining, the recent acquisition of the Irvine Company constituted a change of ownership of the lessor, which would have initiated reappraisal for perhaps thousands of such tenant-homeowners. Given the unlikely prospect of evicting a homeowner from land where he actually OWNS the dwelling on that land, it was felt that an inherent renewal option existed, and that such a conclusive presumption was warranted." (1 Assem. Rev. & Tax. Com. Rep. on Property Tax Assessment (Oct. 29, 1979) p. 26.)

Considering the purpose of the Legislature in including the conclusive presumption language in Sections 61(c) and 62(g), the exclusion under Section 62(g) does not apply to transfers of the lessees' interests per the conclusive presumption at the end of Section 61(c).

Moreover, the statutory language chosen by the Legislature expressly indicates that lessors' transfers are not entitled to the same treatment as lessees' transfers under Section 62(g). The language of Section 62(g) is clear and unambiguous in this regard. It excludes from change in ownership "Any transfer of a **lessor's interest** in taxable real property subject to a lease with a remaining term (including renewal options) of 35 years or more. (Emphasis added.) It then goes on to state that the conclusive presumption applies "For the purpose of this subdivision....[meaning Section 62(g)]... it shall be conclusively presumed that all homes eligible for the homeowners' exemption,...which are on leased land..." are excluded from change in ownership.

There is no language indicating that the exclusion applies to "any transfer of a lessee's interest." Where "the words of a statute, when given their ordinary and popular meaning, are reasonably free of uncertainty, courts will look no further to ascertain the statute's meaning." (County of Orange v. Flournoy (1974) 42 Cal.App.3d 908, 912.) See also, Delaney v. Superior Court (1990) 50 Cal.3d 785, 798-800. Moreover, under the principle *expressio unius est exclusio alterius*, which applies in any event of statutory ambiguity, the specific enumeration of an act or thing within the operation of a particular statute necessarily involves the exclusion of other things not expressed. Since the Section 62(g) exclusion is expressly stated as applicable only to transfers of leased property by the lessor, and transfers by the lessee are not similarly excluded, the exclusion cannot be interpreted in a manner applicable to lessee transfers.

Finally, we note that if your view were adopted and the exclusion in Section 62(g) was held to be applicable to transfers/assignments of long term leases by lessee/homeowners, the leasehold property would escape reappraisal entirely. Obviously, if any transfer by the lessor would be excluded, (as is expressly declared), and any transfer by the lessee was likewise excluded, (based upon the statutory interpretation you suggest) land under a long term lease and eligible for a homeowner's exemption would avoid change in ownership and reappraisal in perpetuity. For this reason, no doubt, the Legislature chose to limit the exclusion set forth in Section 62(g) to "any transfer of a lessor's interest," and provided no exclusion for lessees' transfers.

Although a change in ownership occurs in a lessee/homeowner transfer when the lessee's real remaining term in the lease has as little as only one year remaining, because of the conclusive presumption the lessee is always presumed to be the "owner," of the leased property, having the right to renew for 35 or more years. Thus, the lessee here is in exactly the same position as a fee owner who sells his property only one year after purchasing it. Transfers by both homeowners, the lessee and the owner of land not under a lease, are changes in ownership and subject to reappraisal.

The views expressed in this letter are, of course, advisory only and are not binding upon the county assessor or the assessment appeals board of any county.

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

Sincerely,

Kristine Cazadd
Senior Tax Counsel

KEC:jd
precednt\13leases\97001.kec

Attachments

cc: The Honorable Glenn E. Gray
Ventura County Assessor

Mr. James Speed, MIC:63
Mr. Richard Johnson, MIC:64
Ms. Jennifer Willis, MIC: 70