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June 19, 1987

Honorable Emil G. Shubat
Assessor of Sutter County
Office of the Assessor
P.O. Box 1555
Yuba City, CA 95992

Dear Mr. Shubat:

Your letter to Mr. James J. Delaney dated May 28, 1987 and the attached letter from H... dated May 22, 1987 have been referred to me for reply. Ms. H... requests an opinion as to whether certain transfers to and from a testamentary trust would be changes in ownership and further asks what effect Proposition 58 would have on such transfers when the trustor and beneficiaries are parents and children. The facts as related in Ms. H... 's letter are as follows:

"The proposed transfers are transfers into and out of a testamentary trust created in 1984 upon the death of John Doe. Mr. Doe's will left his share of the community real property to a testamentary trust. Mrs. Doe owns the other half of the real property outright. Since the property is difficult to administer with title held half by Mrs. Doe as an individual and half by the trust, we are contemplating transferring Mrs. Doe's share of some of the property into the trust and the trust's share of other properties out of the trust.

"The applicable paragraph of the trust concerning the beneficiaries reads as follows:

"If my wife survives me, the trustee shall pay to her or apply for her benefit during her lifetime, quarter annually or at more frequent intervals, the entire net income of the trust.

"If the trustee shall deem such income payment to be insufficient, the trustee shall, from time to time, pay to my wife or apply for the benefit of my wife such sums out of principal that the trustees in the trustees' discretion shall deem necessary for her proper support, care, and maintenance. The trustees

may also, in the trustees' absolute discretion, pay to or apply for the benefit of any one or more of my children such sums out of the principal as the trustee may deem necessary for their support, care, maintenance, and education."

Question 1:

Would a transfer of real property to the trust by Mrs. Doe constitute a change in ownership?

Response:

Revenue and Taxation Code* section 62 states in pertinent part that:

Change of ownership shall not include:

(d) Any transfer by the trustor or the trustor's spouse, or by both, into a trust for so long as (1) The transferor is the present beneficiary of the trust, or (2) The trust is revocable; or any transfer by a trustee of such a trust described in either clause (1) or (2) back to the trustor; . . .

Section 462(i)(2) of Title 18 of the California Administrative Code (Property Tax Rule 462(i)(2)), which interprets section 62(d), further states in relevant part that:

A transfer to a trust is not a change in ownership upon the creation or transfer to a trust if:

(A) Trustor-transferor beneficiary trusts. The trustor-transferor is the sole present beneficiary of the trust; provided, however, a change in ownership of trust property does occur to the extent that persons other than the trustor-transferor are present beneficiaries of the trust.

Based on the foregoing provisions, Mrs. Doe's transfer of real property to the trust would not constitute a change in ownership if she is the sole present beneficiary of the trust. Under the terms of the trust, Mrs. Doe is the sole income beneficiary. In addition, the trust provides that if the income payment is insufficient, the trustee shall pay to Mrs. Doe or apply for her benefit such sums out of the principal that the trustees in their discretion deem necessary for her

*All statutory references are to the Revenue and Taxation Code unless otherwise indicated.

proper support, care and maintenance. The trust also provides, however, that the trustees may, in their absolute discretion, pay to or apply for the benefit of any one or more of the trustor's children such sums out of the principal as the trustees may deem necessary for their support, care, maintenance, and education.

Under provisions such as the latter regarding the trustor's children, the interest of the beneficiary is at most a mere expectancy. (Estate of Canfield (1947) 80 Cal.App.2d 443, 451; Estate of Johnson (1961) 198 Cal.App.2d 503, 510.) Similarly, the interest created by such a provision has been characterized as a future interest for federal gift tax purposes since the discretion of the trustees is a barrier to the children's present enjoyment of the trust principal. Jacobson v. U.S. (1978) 42 AFTR 2d 78-6499. It is therefore our opinion that Mrs. Doe is the sole present beneficiary of the trust and that her transfer of real property to the trust accordingly would not be a change in ownership.

Question 2:

Would a transfer of real property from the trust to Mrs. Doe constitute a change in ownership?

Response:

Section 63 provides in relevant part that:

Notwithstanding any other provision in this chapter, a change in ownership shall not include any interspousal transfer, including but not limited to: (a) [t]ransfers to a trustee for the beneficial use of a spouse, or the surviving spouse of a deceased transferor, or by a trustee of such a trust to the spouse of the trustor. (Emphasis added.)

Since the proposed transfer from the trust to Mrs. Doe is expressly excluded by the language of section 63, such transfer would not constitute a change in ownership.

Question 3: Would transfers of real property from the trust to the children be excluded from change in ownership under Proposition 58 as transfers between a parent or parents and children?

Response: Proposition 58 was adopted by California voters in the November 1986 election and added subdivisions (g), (h) and (i) to section 2 of article XIII A of the California Constitution. Subdivision (g) essentially restates the

provisions of section 63 relating to interspousal transfers. Subdivision (h) provides in pertinent part that

[f]or purposes of subdivision (a), the terms "purchased" and "change of ownership" shall not include the purchase or transfer of the principal residence of the transferor in the case of a purchase or transfer between parents and their children . . . and the purchase or transfer of the first \$1,000,000 of the full cash value of all other real property between parents and their children. . . .

Subdivision (i) provides that unless otherwise provided the amendments to section 2 apply to change of ownerships occurring after the effective date of the amendment (i.e., on or after November 6, 1986).

The implementing legislation for Proposition 58 is AB 47 which adds section 63.1 to the Revenue and Taxation Code. Section 63.1 reiterates the exclusion of Proposition 58 for transfers between parents and children but makes no reference to transfers to and from trusts. Section 2 of AB 47, however, provides in relevant part:

SEC. 2. It is the intent of the Legislature that the provisions of Section 63.1 of the Revenue and Taxation Code shall be liberally construed in order to carry out the intent of Proposition 58 on the November 4, 1986, general election ballot to exclude from change in ownership purchases or transfers between parents and their children described therein. Specifically, transfers of real property from a corporation, partnership, trust, or other legal entity to an eligible transferor or transferors, where the latter are the sole owner or owners of the entity or are the sole beneficial owner or owners of the property, shall be fully recognized and shall not be ignored or given less than full recognition under a substance-over-form or step-transaction doctrine, where the sole purpose of the transfer is to permit an immediate retransfer from an eligible transferor or transferors to an eligible transferee or transferees which qualifies for the exclusion from change in ownership provided by Section 63.1. . . .

We recognize that from the second sentence of section 2 quoted above it is possible to argue that transfers in trust are not intended to be excluded from change in ownership under Proposition 58 and that real property must be transferred out of trust and retransferred directly to an eligible transferee in order to qualify for the exclusion.

Such a conclusion is inappropriate in our view, however, because it is inconsistent with the first sentence of section 2 which evidences the intent of the Legislature to liberally construe the provisions of section 63.1 to carry out the intent of Proposition 58. By its express terms, the intent of Proposition 58 is to exclude the described transfers between parents and their children from change in ownership. It is common knowledge that the persons best able to take full advantage of Proposition 58 use trusts extensively to effect transfers of real property to their children both during their lifetime and particularly at death. To conclude that such transfers are not transfers between parents and children would clearly frustrate the intent of Proposition 58. Moreover, it is our opinion, as indicated below, that such transfers are properly characterized legally as transfers between parents and children.

For purposes of determining whether a transfer of real property from the trust to the children is excluded from change in ownership under Proposition 58 as a transfer between parents and children, it is helpful to remember that a change in ownership requires the "transfer of a present interest in real property, including the beneficial use thereof" rather than a transfer of bare legal title. Section 60, Parkmerced Co. v. San Francisco (1983) 149 Cal.App.3d 1091. When Mr. Doe died in 1984, the beneficiaries of the trust created by his will became the equitable or beneficial owners of the trust property and the legal title to the trust property vested in the trustees at that time. (Estate of Feuereisen (1971) 17 Cal.App.3d 717, 720; Allen v. Sutter County Board of Equalization (1983) 139 Cal.App.3d 887, 890.) At the time of Mr. Doe's death, therefore, the beneficial interest in the real property passed from him to his wife as income beneficiary for life and to his children as equitable remaindermen. The transfer of the beneficial interest in real property was accordingly from a parent to his spouse and his children and not from an individual to an entity.

Similarly, the transfer from the trust to the children at the termination of the trust would not be a transfer of a beneficial interest in the real property from an entity to individuals because the trustees own only the legal and not the beneficial interest in the real property. The beneficial interest in the property was transferred only by Mr. Doe to his children. No other person or entity had beneficial ownership of the property transferred. It is therefore clear that the transfers into the trust by Mr. Doe and out of the trust to his children are transfers between a parent and his children. The same is true with respect to any real property transferred to the trust by Mrs. Doe.

With respect to the real property transferred to the trust by Mr. Doe at his death in 1984 and to be distributed from the trust to his children in the future, there is the further question as to the date of Mr. Doe's transfer to his children for purposes of Proposition 58.

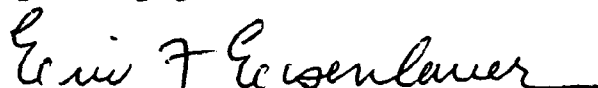
As indicated above, subdivision (i) which Proposition 58 added to section 2 of article XIII A provides that Proposition 58 is "effective for change of ownerships which occur . . . after the effective date of the amendment." Section 63.1(f) provides that "[t]his section shall apply to purchases and transfers of real property completed on or after November 6, 1986."

Transfers which are not changes in ownership are not affected by Proposition 58 and section 63.1. It would obviously make no sense, therefore, to construe the word "transfer" to include transfers which are not changes in ownership. Further, the word "transfer" is used with the word "purchase" in Proposition 58 and section 63.1 and "purchase" is defined by section 67 as "a change in ownership for consideration." It is therefore our opinion that the word "transfer" as used in Proposition 58 and section 63.1 means a change in ownership without consideration.

When John Doe died in 1984, he transferred equitable remainder interests to his children. Such transfers, however, were not changes in ownership under section 60 because they were not present interests in real property and the interests transferred were not substantially equal to the value of the fee interests. A change in ownership will occur, however, under section 61(f) when the children's equitable remainders become possessory upon the termination of Mrs. Doe's life estate. Since such change in ownership or transfer will occur after November 6, 1986, Proposition 58 and section 63.1 will be applicable to exclude such transfer from change in ownership.

We hope the foregoing discussion has been responsive to your inquiry. If you have further questions regarding this matter, please let us know.

Very truly yours,



Eric F. Eisenlauer
Tax Counsel

EFE:cb

cc: Hon. Patricia A. Bluett, Assessor of Yuba County
Hon. Roger G. F. Fong, Assessor of Sacramento County
Ms. Amey S. Hempel

Hon. Emil G. Shubat

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June 19, 1987

bc: Mr. James J. Delaney
Mr. Gordon P. Adelman
Mr. Robert H. Gustafson
Mr. Verne Walton
Mrs. Margaret S. Boatwright

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