STATE OF CALIFORNIA

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April 30, 1991

Honorable Richard D. Hongisto, Assessor
CITY AND COUNTY OF SAN FRANCISCO
City Hall, Room 101
San Francisco, CA 94102
Attn: Henry F. McKenzie, Chief Appraiser

Re: Homesavers of America - Trust
Block 5387, Lot 2A; 1606 Wallace Avenue

Dear Mr. McKenzie:

This is in response to your letters to the attention of Verne Walton of January 14, 1991, and March 25, 1991 in which you request our opinion whether a trust document submitted with your letters could be a valid revocable trust.

The Declaration of Trust in question was executed July 30, 1990. The preamble of the trust recites that Ervin and LaVonne Morgan are the "Trustor", Homesavers of America (Vernon L. Bradley), the "Trustee", and John T. Jones, the "Beneficiary". Article I of the trust recites that both the Trustor and the Beneficiary are beneficiaries.

Article II provides that the Beneficiary may apply for a refinance of the subject real property held in trust and that upon the funding of such a refinance, a portion of the proceeds are to be distributed to the Trustor as the parties agree. When that occurs, Article II provides that Trustor shall cease to be a beneficiary of the trust, the Trustee shall resign and the Beneficiary or his nominee shall become the Trustee. Article II further provides that the trust shall terminate upon the earliest to occur of the sale of the property, the expiration of five years, or if the Trustor does not receive distribution of the agreed upon portion of the proceeds of the refinancing within specified time periods.

Article III recites that John T. Jones is an individual with excellent credit and that the property was transferred in trust for the consideration of Beneficiary (Jones) extending his credit for the purpose of obtaining new financing on the property and for the benefit of the Trustor saving the home from foreclosure.

Although the trust recites that the subject property was transferred into the trust, the only deeds we have copies of are a grant deed dated August 27, 1990 and recorded August 31, 1990 from the Morgans (Trustor) to Jones (Beneficiary) and a grant deed from Jones to Ervin Morgan, dated October 24, 1990, which is unrecorded and held in Trustee's safe. Apparently, the transaction was presented to the lending institution not as a refinancing of the property, but rather as a sale from the Morgans to Jones as indicated by the buyer and seller settlement statements which were provided with your letters.

Under Article III, Trustor is to pay Beneficiary or Trustee the identical amount that Beneficiary must pay on the new loan obtained for Trustor with Beneficiary's credit. Also, Trustor must, among other things, keep the property in good condition and repair; provide fire, earthquake and liability insurance with loss payable to Beneficiary and his lender with any excess payable to Trustor; pay taxes and assessments affecting the property and to pay a fee of $13,500 for the advancing of credit. If Trustor defaults on his loan payments to Beneficiary or Trustee, the property can be sold. Under Article III, Trustor is to retain possession of the property and is entitled to claim the interest on the loan as an income tax deduction.

Article III further provides that Trustor has two years to assume the loan or relieve Beneficiary of the ongoing liability for extension of credit by Beneficiary. Should Trustor fail to maintain his credit so as to be able to assume the underlying indebtedness of Beneficiary or to remove Beneficiary by way of payment of all of the underlying indebtedness within a period of two years from the date the loan was obtained by Beneficiary for Trustor and Beneficiary is required to continue on the loan for Trustor, the Beneficiary shall be entitled to fifty percent of the equity increase retroactive to the date the loan was obtained to the date Trustor relieves Beneficiary of any and all liability for his note, but in no event exceeding five years.

Trustor acknowledges that the only obligations under the trust agreement of Beneficiary are to obtain refinancing for Trustor and to convey the property to Trustor if all the obligations of Trustor are paid and are met. The Trustee shall collect the payments (made by Trustor) on behalf of Beneficiary and forward the same to Beneficiary's lender and sell the property at the direction of Beneficiary in the event of default.

Although you ask whether a valid revocable trust was created by the document described above, the question here is whether the

transfer of the real property subject to the terms of the described document, however it may be labeled, is a change in ownership.

Revenue and Taxation Code* section 60 defines "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.

Section 62, however, provides in relevant part that "change in ownership" shall not include:

> . . .
>
> (c)(1) The creation, assignment, termination or reconveyance of a security interest, ...
>
> (d) Any transfer by the trustor, or by 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; or, any creation or termination of a trust in which the trustor retains the reversion and in which the interest of others does not exceed 12 years duration.

The Board has interpreted the foregoing provisions in Property Tax Rule 462 in relevant part as follows:

> (i) TRUSTS.
>
> (1) Creation. Except as is otherwise provided in subdivision (2) the transfer by the trustor, or any other person, of real property into a trust is a change in ownership of such property at the time of the transfer.
>
> (2) Exceptions. A transfer to a trust is not a change in ownership upon the creation of or transfer

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

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.

(B) Revocable Trusts. The transfer of real property or an ownership interest(s) in a legal entity by the trustor(s) to a trust which is revocable by the trustor(s); provided, however, a change in ownership does occur at the time the revocable trust becomes irrevocable unless the trustor-transferor remains or becomes the sole present beneficiary.

(C) Trustor Reversion Trusts. The trustor-transferor retains the reversion, and the beneficial interest(s) of persons(s) other than the trustor-transferor does not exceed 12 years in duration.

. . .

(k) MISCELLANEOUS ARRANGEMENTS

(1) Security transactions. There are transactions that may be interpreted to be either a conveyance of the property or a mere security interest therein, depending on the facts. There is a rebuttable presumption under Civil Code Section 1105 that a conveyance is what it is purported to be, a transfer of property. In overcoming this presumption, consideration may be given to, but not limited to, the following factors:

(A) The existence of a debt or promise to pay.

(B) The principal amount to be paid for reconveyance is the same, or substantially the same, as the amount paid for the original deed.

(C) A great inequality between the value of the property and the price alleged to have been paid.

(D) The grantor remaining in possession with the right to reconveyance on payment of the debt; and

(E) A written agreement between the parties to

> reconvey the property upon payment of the debt. The best evidence of the existence of such factors shall be a judicial finding or order. Proof may also be made by declarations under penalty of perjury (or affidavits) accompanied by such written evidence as may reasonably be available, such as written agreements, cancelled checks, insurance policies and tax returns.

With respect to whether the transfer should be analyzed as a transfer in trust, there is a question as to whether a valid trust exists. Under Probate Code section 15205(a), a trust, other than a charitable trust, is created only if there is a beneficiary. As indicated above, when a portion of the proceeds of the refinancing are distributed to the Trustor, the Trustor shall cease to be a beneficiary of the trust, the Trustee shall resign and the Beneficiary or his nominee shall become the Trustee. Apparently, a portion of the proceeds of the refinancing has been distributed to the Trustor as indicated by the settlement statements of the buyer and seller. Thus, under the foregoing express provisions of the trust, there would be no beneficiary of the trust and therefore no trust would exist. Also, as a general rule, a security arrangement is not a trust (11 Witkin, Summary of Cal. Law (9th ed. 1990) p. 885).

However, assuming that Trustor could be characterized as a beneficiary of the trust because Trustor has the beneficial use of the trust property through use and possession, the transfer would be excluded from change in ownership under section 62(d) and Property Tax Rule 462(i)(2)(A) because the trustor-transferor would be the sole present beneficiary of the trust.

Property Tax Rule 462(i)(2)(B) would not be applicable in our view because Trustor cannot revoke the trust until the conditions of the trust are met (i.e., payment of the loan obtained by Jones). Further, Property Tax Rule 462(i)(2)(C) would not be applicable because Trustor has a present beneficial interest in the property rather than a reversion.

Although the transaction was apparently presented to the lender as a sale and called a trust arrangement by the parties other than the lender, it seems to resemble more closely a security transaction or agreement.

The trust agreement clearly satisfies factors (A), (D) and (E) of Rule 462(k)(1). With respect to factor (B), however, the amount paid for the original deed is nominally $225,000, while the principal amount to be paid for reconveyance is $180,000,

the amount of the new loan by the lender. It therefore appears from the information submitted that the principal amount to be paid for reconveyance is not substantially the same as the amount paid for the original deed and that factor B is not satisfied.

Since factor (C) involves the value of the property, it is up to the assessor to determine whether the requirement of that factor is satisfied.

Although it appears that the transaction in question may be a security transaction, it is our recommendation that since the transaction was presented to the lender as an outright sale and to you other than as an outright sale, you should obtain declarations under penalty of perjury to the effect that all of the factors of Rule 462(k)(1) have been satisfied (especially factor (B) "the amount paid for the original deed" and factor (C) "the price alleged to have been paid") as well as other documentary evidence in support of those factors including cancelled checks, insurance policies, and tax returns. See Evidence Code section 662 which requires clear and convincing proof to rebut the presumption that the owner of the legal title to property (i.e., John T. Jones) is the owner of the beneficial title.

The additional proof which we recommend that you obtain along with the information you already have should provide clear and convincing proof that Trustor (Morgan), rather than Beneficiary (Jones) has the beneficial use of the subject property. If, however, after receiving the information requested, your determination is otherwise, then, based upon the statutory presumption that the beneficial ownership was transferred to Beneficiary (Jones), it would be appropriate to conclude that a change in ownership had occurred.

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,

Eric F. Eisenlauer
Tax Counsel

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cc: Mr. John W. Hagerty
Mr. Verne Walton