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March 14, 2000

E. L. SORENSEN, JR.
Executive Director

Re: **Parent/Child – Proper Allocation of the \$1 Million Exclusion.**

Dear Mr. :

This is in response to your letter of January 9, 2000, requesting our opinion as to whether the proposed distribution plan under an irrevocable trust properly allocates the assets for purposes of applying the \$1 million parent/child exclusion, thereby avoiding a change in ownership. Based on the following described facts, and for the reasons hereinafter explained, the exclusion would apply and no change in ownership will occur.

Factual Background

1. The decedent, “Mother” died on August 25, 1999. Her estate consisted of cash, securities, and five residential properties with improvements, and one unimproved lot, all located in two counties and held in Mother’s 1982 Revocable Living Trust. The Trust became irrevocable upon Mother’s death, and her four children were the sole present beneficiaries.
2. The Trust provided that upon the decedent’s death, the Successor Trustee should divide the trust estate into equal shares and distribute one share to each of the four children free of Trust, in cash or in kind, in divided or undivided interests. (Section 5.04, p. 14 of Mother’s Trust.¹)

¹ Section 5.04, p. 14 of the Trust provides that “the Trustee in its absolute discretion, may divide or distribute such assets in kind, or may divide and distribute undivided interests in such assets, or may sell all or any part of such assets and make division or distribution in cash or partly in cash and partly in kind. The decision of the Trustee, either prior to or on any division or distribution of such assets, as to what constitutes a proper division of such assets or the Trust Estate or any Trust provided for in this Declaration, shall be binding on all persons in any manner...”.

3. At the time of Mother's death, each of the improved parcels in the Trust Estate had an existing mortgage; only the unimproved lot was free of debt. The entire Trust Estate had a net worth of approximately \$738,698, with the real property valued at approximately \$453,247 and all other property valued at \$497,441, less \$211,990 in debt, taxes, and other costs. Pursuant to the Trust provisions, the Successor Trustee is proposing to distribute approximately \$222,475 net worth of assets to each child, totaling \$889,900. (This amount assumes increases between the net worth on date of death and the net worth on the date of future distribution).
4. Before making any distributions however, the Successor Trustee will sell Parcel 4 in order to raise the cash needed. Thereafter, \$222,475, mixed between real property and cash, will be distributed non pro rata to each child. Each share will be funded with unequal interests in the five remaining parcels together with cash and notes, as follows:
 - To M - \$216,841 net value in Parcel 3, and \$5,634 in cash;
 - To C - \$126,082 net value in Parcel 5, and \$96,393 in cash;
 - To E - \$222,475 net value (all in cash and notes)
 - To A - \$147,750 net value in Parcel 2, \$35,809 net value in Parcel 1, \$4,500 net value in the undeveloped lot, and \$34,416 in cash.

Each of the parcels, except the unimproved lot will continue to be encumbered by a mortgage.

Your questions are: 1) Will the proposed distribution plan qualify for the parent/child exclusion and avoid change in ownership, assuming timely claims are filed; 2) Would the parent/child exclusion apply to Parcel 4, assuming a timely claim is filed prior to its sale; and 3) Is it acceptable to equalize the children's net shares by considering the outstanding mortgage balances on the properties together with cash or other assets. As explained below, the answer to all three of these questions is yes.

Law and Analysis

As you are aware, Revenue and Taxation Code²section 61 provides that, subject to exceptions not here relevant, "change in ownership, as defined in section 60, includes, but is not limited to: ". (g) [a]ny interests in real property which vest in persons other than the trustor...when a revocable trust becomes irrevocable."

² All statutory references are to the Revenue and Taxation Code unless otherwise indicated.

The parent/child exclusion (Proposition 58) was added to section 2 subdivision (h) of Article XIII A of the California Constitution on November 6, 1986. It excludes from change in ownership the purchase or transfer of the principal residence of the transferor between parents and their children, as well as the purchase or transfer of the first \$1 million of the full cash value of all other real property *between parents and their children*. Section 63.1, which implements Proposition 58, also states in subdivision (a)(2) that the exclusion applies to “the purchase or transfer of the first \$1 million of the full cash value of all other real property *between parents and their children*.” For purposes of interpreting the exclusion, Section 63.1(c)(1) states that the date of any transfer between parents and their children under a will (or trust) or intestate succession shall be the date of the decedent’s death. Applied to the instant case, if the transfers of the six parcels in Mother’s Trust qualified under Section 63.1, as transfers between Mother and her four children on the date of death, and if the Trustee’s distribution plan merely executes such transfers based on the equal value of each child’s beneficial interests received on Mother’s death, then no change in ownership will occur.

1. Will the distribution plan, allocating equal shares of the Trust real property on a non-pro rata basis among the four children, qualify for the parent/child exclusion and avoid change in ownership, assuming timely claims are filed?

Yes. As we have explained in previous opinions, the property tax consequences of transferring property on a share-and-share-alike basis depend on whether the distribution plan conforms to the beneficiary provisions in the Trust instrument as of the date of death. You rely heavily on a Letter to Assessors No. 91/08, dated January 23, 1991, entitled “*Change in Ownership Consequences of Real Property in an Estate or Trust Distributed on a ‘Share and Share Alike’ Basis*,” which sets forth this position in detail. The discussion in LTA 91/08 makes it clear that where a trustee’s statutory powers over the property in an irrevocable trust are not limited by the trust instrument, and the trust instrument requires share-and-share alike distribution to children, no change in ownership occurs upon distribution, unless a trust beneficiary receives property or assets valued in excess of the value of his or her share. Regardless of the mixture of real property and assets constituting the shares ultimately distributed to each, the value of each share is the determining factor. If one sibling receives more value than the others, the result is a transfer from the other siblings to the one with the excess value. This view has been restated on numerous occasions since 1991, most notably in Annotation No. 625.0235 (attached).

The proposed distribution plan in the instant case falls squarely within the parameters of LTA No. 91/08 and Annotation No. 625.0235, in that the language of the Trust directs that all of the property and assets in the estate be distributed to the children on a share-and-share alike basis, and the Trustee’s distribution plan executes this instruction by distributing to each child an

equal share in the total net worth of the assets. Each child will receive \$222,475 in net worth, mixed between real property and cash, representing one quarter of the total net worth of the Trust Estate. Since each child received one quarter of the Trust Estate on the date of Mother's death (Article 3 of the Trust), and the share to each child will be equivalent on distribution, the result is no sibling-to-sibling transfer.

2. Would the parent/child exclusion apply to Parcel 4, assuming a timely claim is filed prior to its sale?

Yes. Equalizing the shares among the children is part of the job of the Trustee. The extent of the powers given to the Trustee to perform this function depends on the language in the Trust instrument. Where the Trust instrument confers on the Trustee broad powers to sell, encumber, lease, distribute, purchase or otherwise have unfettered discretion in dealing with all of the assets in the Trust Estate, then the sale of one parcel in order to gain cash for purposes of equalizing the shares upon distribution is permissible.

The trustee enjoys both the powers conferred by the trust instrument and the broad powers conferred by the provisions of the Probate Code, including Section 16246. Thus, the critical factor is whether the trust instrument limits the trustee's powers to distribute property. As indicated on pages 2-3 of LTA No. 91/08,

“Probate Code Section 16200 provides, in part, that a trustee has not only the powers conferred by the trust instrument but also, except as limited in the trust instrument, the powers conferred by statute. Following Probate Code Section 16200 are a number of provisions conferring express statutory powers on trustees. Among those provisions is Section 16246 which provides:

‘The trustee has the power to effect distribution of property and money in divided or undivided interests and to adjust resulting differences in valuation. A distribution in kind may be made pro rata or non-pro rata.’”

Consistent with the broad powers described in Probate Code Section 16246, there are no express limitations Mother's Trust that would prevent the Trustee from selling Parcel 4 in order to equalize the distribution or for any other reason. Rather, Section 4.02 of the Trust provides in part, the following unlimited discretion to the Trustee:

“The Trustee shall with respect to any and all property which may at any time be held by the Trustee pursuant to this Declaration, whether such property constitutes principal or accumulated income of the Trust provided for in this Declaration, have power, exercisable in the Trustee's discretion at any time and from time to time on such terms and in such manner as the Trustee may deem advisable, to:

(a) Sell, convey, exchange, convert, improve, repair, partition, divide, allot, subdivide, create restrictions, easements or servitudes thereon, manage, operate and control;”

Based on the foregoing provisions, the Trustee’s proposed sale of Parcel 4 from Mother’s Trust does not prohibit the application of the parent/child exclusion to the transfer of Parcel 4 that occurred on Mother’s death. Per the Trust instructions, each of the four children received a one-quarter beneficial interest in Parcel 4 at that time. Assuming a parent/child claim is filed and all of other requirements are met, that transfer will be excluded from change in ownership. If the Trustee then sells Parcel 4 in order to obtain sufficient cash to equalize the net worth of the Trust Estate into four shares (of \$222,475 each) for distribution, there is no sibling-to-sibling transfer or change in ownership, since no child will receive value in excess of the others. Accordingly, the Trustee’s proposed sale of Parcel 4 will not trigger a change of ownership as of the date of Mother’s death, because the sale and distribution of the proceeds from Parcel 4 is within the Trustee’s powers. As such, it constitutes a transfer from Mother to her children “through the medium of an inter vivos...trust” within the meaning of section 63.1(c)(7) and the guidelines of LTA 91/08.

3. Is it acceptable to equalize the children’s net shares by considering the outstanding mortgage balances on the properties together with cash or other assets?

Yes. Where the Trustee has broad powers as described above, and there is no restriction on that Trustee’s authority to encumber or to retain existing encumbrances, no change in ownership results, assuming the Trustee properly considers the value of the encumbrances on the Trust real property make distributions in equal shares.

That the proposed distribution allows the Trustee to calculate the existing mortgages on the parcels in equalizing the net value of the shares to be distributed among the four children, is not a change in ownership and is consistent with advice previously stated. As pointed out in the example in LTA 91/08, where a beneficiary receives real property that is encumbered, the encumbrance must be considered in determining whether a beneficiary has received real property valued in excess of his or her trust share.

In this proposal, no child will receive more than his/her share of the Trust estate. For example, Child A will receive the most real property, (three parcels), two of which are encumbered by existing mortgages. Based on the value of the mortgages at the time of the transfer, A’s share of the total Trust Estate will be exactly the same as E’s share, that contains only cash and notes with no real property. Accordingly, since the value of each child’s share is equal one quarter of the total Trust Estate, there will be no transfer of real property between siblings and thus, no change in ownership.

March 14, 2000

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The views expressed in this letter are, of course, 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 upon any person or entity.

Sincerely,

/s/ Kristine E. Cazadd

Kristine E. Cazadd
Senior Tax Counsel

KEC:tr

prop/precndt/parchild/00/04kec

Attachments: LTA No. 91/08, Annotation No. 625.0235

cc: Honorable
County Assessor

Honorable
County Assessor

Mr. Dick Johnson, MIC:63
Mr. David Gau, MIC:64
Mr. Charlie Knudsen, MIC:64
Ms. Jennifer Willis, MIC:70

ANNOTATION

PARENT-CHILD TRANSFER (Add to existing Annotation Nos. 220.0767 and 625.0235)

Trusts. A trust distribution is within the parent-child exclusion where a trustee's statutory powers are not limited by the trust instrument, the trust instrument requires distribution to children in equal shares, and the trustee encumbers the trust real property after the trustor's death for purposes of distributing the real property to one child subject to the encumbrance and cash in an amount equal to the equity in the real property to the other child. C 9/10/96, C 3/14/00.



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KATHLEEN CONNELL
Controller, Sacramento

E. L. SORENSEN, JR.
Executive Director

September 10, 1996

Attention: Ms.

Re: Proposition 58 Reassessment Exclusion

Dear Ms.

This is in response to your letter to me of August 8, 1996 in which you request our opinion as to whether a "change in ownership" for property tax purposes occurred and if so, to what extent under the following facts described in your letter and set forth below. For the reasons stated hereafter, we are of the opinion that no "change in ownership" occurred.

Factual Background

The decedent died on October 20, 1994. Her estate consisted of cash and her principal residence, all held in the ABC 1993 Family Trust. The decedent resided in the real property with her son prior to her death. The son still resides in the residence.

The Trust provides that following the decedent's death, the Successor Trustee should divide the trust estate into equal shares and distribute one share to each of the decedent's two children, a daughter and a son, free of trust. In the Trust, "trust estate" refers to "the assets listed in Schedule A and to any other property received by the Trustee." Furthermore, the Trust provides that "the Trustee is authorized to allot and make the division or distribution, pro rata or otherwise, in cash or in kind, including undivided interests in any property, or partly including undivided interest in any property, or partly in cash and partly in kind, in the Trustee's discretion." (Art. Sixth, Sec. A, p. 11.) The Trust also provides that the Trustee has the power to "encumber,

mortgage or pledge trust property for a term within or extending beyond the term of the trust in connection with the exercise of any power vested in the Trustee." (Art. Fourth, Sec. G, p. 7.)

The Successor Trustee believed that the Trust estate had a net worth of approximately \$322,000, with the real property valued at approximately \$310,000 and all other property valued at \$12,000. Pursuant to the Trust provisions, the Successor Trustee sought to distribute approximately \$161,000 net worth of assets to each child. On April 24, 1995, before making any distributions, the Successor Trustee obtained a loan and Deed of Trust against the Trust real property for \$160,000. The assets of the Trust then consisted of cash, including loan proceeds and the real property encumbered by the Deed of Trust.

On June 2, 1995, the Successor Trustee was ready to distribute the Trust property, and made a non pro rata distribution of \$150,000 of the Trust's cash to decedent's daughter. On June 22, 1995, the Successor Trustee made a non pro rata distribution of the real property to decedent's son individually, subject to the \$160,000 loan and Deed of Trust.

On June 22, 1995, the Successor Trustee executed a proper Claim for Reassessment Exclusion for Transfer Between Parent and Child. He submitted it to the Alameda County Recorder on June 26, 1995.

The Assessor issued a Notice of Supplemental Assessment on January 12, 1996 regarding the reassessment of one-half of the real property after the death of the parent and the distribution of the real property to the decedent's son. The property was previously on the tax roll at \$47,441. The Assessor appraised it at only \$220,000, one-half of which is \$110,000. Thus, the new assessed value is \$133,441. Subtracting the \$47,441 already taxed, the Assessor issued a Supplemental Assessment to the son of \$86,000 and a supplemental tax of 1.2990% thereon, or \$1,117.14.

The Assessor has indicated that the property was reassessed because "there was not enough money in the trust estate to equally distribute cash to [the daughter]...The Trustee obtained a cash loan to distribute cash to [the daughter] instead of a 50% interest in the above referenced property." The Assessor relies heavily on a Letter to Assessor dated January 23, 1991, No. 91/08, entitled "Change in Ownership Consequences of Real Property in an Estate or Trust Distributed on a "Share and Share Alike" Basis" (LTA 91/08).

Law and Analysis

As you are aware, Revenue and Taxation Code¹ 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."

¹ All statutory references are to the Revenue and Taxation Code unless otherwise indicated.

Section 61 provides that, subject to exceptions not here relevant, "change in ownership, as defined in section 60, includes, but is not limited to:...(g)[a]ny interests in real property which vest in persons other than the trustor...when a revocable trust becomes irrevocable."

Proposition 58 added subdivision (h) to section 2 of Article XIII A of the California Constitution. Briefly, subdivision (h) excludes from change in ownership the purchase or transfer of the principal residence of the transferor in the case of the purchase or transfer between parents and their children. It also excludes the purchase or transfer of the first \$1 million of the full cash value of all other real property between parents and their children.

Subdivision (h) is implemented by section 63.1. Section 63.1(c)(7), in part, defines "transfer" as including any transfer of the present beneficial ownership of property from an eligible transferor to an eligible transferee through the medium of an inter vivos trust. It seems clear, therefore, that if the transfer of the decedent's principal residence to the decedent's son qualifies as a transfer from decedent pursuant to the terms of her inter vivos trust, then the transfer qualifies for exclusion from change in ownership under Proposition 58 and section 63.1.

The Board has addressed this issue in its LTA 91/08, a copy of which is attached, which provides in part:

"The key to whether a change in ownership occurs when property is distributed according to a trust on a share and share alike basis is whether the trust instrument limits the trustee's powers to distribute property.

"Probate Code Section 16200 provides, in part, that a trustee has not only the powers conferred by the trust instrument but also, except as limited in the trust instrument, the powers conferred by statute. Following Probate Code Section 16200 are a number of provisions conferring express statutory powers on trustees. Among those provisions is Section 16246 which provides:

'The trustee has the power to effect distribution of property and money in divided or undivided interests and to adjust resulting differences in valuation. A distribution in kind may be made pro rata or non-pro rata.' (Added by Chapter 820 of the Statutes of 1986.)

"The statement 'a distribution in kind may be made pro rata or non-pro rata,' means that the trustee has a choice in how he/she distributes non-cash assets, such as real property. The trustee can either give the beneficiaries common ownership in all the assets of the trust estate (pro rata) or can allocate specific assets to individual beneficiaries (non-pro rata).

"California trust law recognizes that the administration of a trust is governed by the trust instrument. Union Bank and Trust Co. v. McClogan (1948) 84 Cal. App.

2d 208. Thus, where the trust instrument conflicts with statutory power, the instrument controls unless a court, pursuant to Probate Code Section [16201], relieves the trustee of the restriction in the instrument. Absent a restriction in the trust instrument, the trustee enjoys both the powers conferred by the trust instrument and those conferred by the provisions of the Probate Code, including Section 16246.

“Unless the trust instrument specifically states otherwise, the trustee has the power to distribute the trust assets in kind on either a pro rate or non-pro rata basis. Consequently, property in a trust, where the trustee has the power to distribute trust assets on a share and share alike basis can be treated as a direct transfer from parent to child to the extent that the value of the property does not exceed the value of the stipulated share of trust assets. This is because both statutory and case law recognize that, unless the trust instrument specifically states how the beneficiaries are to share the trust’s assets, the trustee has the power to distribute property as he/she wishes. Accordingly, the assessor should recognize these transfers of property as a parent to child transfer, which may qualify for the parent/child exclusion under Section 63.1.”

In this case, the Trust does not limit the statutory trustee powers contained in Probate Code sections 16220 through 16249. In fact, as indicated above, Article Sixth, Section A, of the Trust provides for the Trustee’s distribution powers similar to but no less broad than those specified in Probate Code section 16246. Also, as indicated above, the Trustee has the power to encumber, mortgage, or pledge trust property for a term within or extending beyond the term of the trust in connection with the exercise of any power vested in the Trustee. This provision is identical to Probate Code section 16228.

It is clear under LTA 91/08 discussed above that where a trustee’s powers are as broad as they are in this case and where the trust requires distribution in equal shares, a trustee may distribute a 100 percent interest in a parcel of real property to a beneficiary without triggering a change in ownership as long as the value of the parcel received by the beneficiary doesn’t exceed the value of his or her share of the trust property. Thus, where the trust property consists solely of two parcels of real property of equal value and the trust requires distribution in equal shares to the two children, the trustee may distribute one parcel to one child and one parcel to the other child without causing a change in ownership as long as the trustee’s statutory powers are not limited by the trust instrument.

Similarly, if the same trust contained one parcel of real property and cash in an amount equal to the value of the real property, no change in ownership would result from a distribution of the real property to one child and the cash to the other child.

This case is different from the latter example only in that the successor Trustee encumbered the Trust real property in order to distribute the trust estate in equal shares by distributing cash to one child and equity in the principal residence of equal value to the other

September 10, 1996

child. As indicated above, the Successor Trustee had the power to encumber the real property and to make the non-pro rata distribution. In effect, the Successor Trustee exercised his power to encumber in order to be able to exercise his non pro rata distribution power. The creation of a security interest or the substitution of a trustee under a security instrument, if that occurs, is not a change in ownership (§62(c)). Accordingly, it is our view that the distribution made by the Successor Trustee in this case does not result in a change of ownership because the distribution of the real property under the Successor Trustee's powers was a transfer from the decedent to her son "through the medium of an inter vivos...trust" within the meaning of section 63.1(c)(7) and the guidelines of LTA 91/08. The fact that the assessor valued the real property at an amount less than what the Successor Trustee believed the property was worth for purposes of encumbering the property and distributing the trust estate does not change that result. As LTA 91/08 makes clear, where a trustee's statutory powers are not limited by the trust instrument and the trust instrument requires a share and share alike distribution to children, no change in ownership resulting from a transfer between siblings occurs unless a trust beneficiary receives real property valued in excess of the value of his or her share. As pointed out in the example in LTA 91/08, where a beneficiary receives real property which is encumbered, the encumbrance must be considered in determining whether a beneficiary has received real property valued in excess of his or her trust share. In this case, the son did not receive more than his share of the trust estate and, based on the Assessor's valuation, in fact, received less than his share of the trust estate. Accordingly, there was no transfer of real property between siblings and thus, no change in ownership.

The views expressed in this letter are, of course, only advisory in nature. They are not binding upon the assessor of any county.

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
Senior Tax Counsel

EFE:sao

Attachment

cc: Honorable John N. Scott
Alameda County Assessor

Mr. James Speed - MIC:63

Mr. Dick Johnson - MIC:64

Ms. Jennifer Willis - MIC:70

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STATE OF CALIFORNIA

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January 23, 1991

CINDY RAMBO
Executive Director

No. 91/08
CORRECTION

TO COUNTY ASSESSORS:

CHANGE IN OWNERSHIP CONSEQUENCES OF REAL PROPERTY
IN AN ESTATE OR TRUST
DISTRIBUTED ON A "SHARE AND SHARE ALIKE" BASIS

This letter sets forth the change in ownership consequences of transfers of property from parents to children when property is distributed according to a will or trust and the language of the document directs that the assets of the estate or trust be distributed to the children on a "share and share alike" basis.

Currently, when an estate or trust is to be distributed on a share and share alike basis many assessors presume, for property tax purposes, that the beneficiaries of a trust or the heirs of a will have an equal interest in each and every property owned by the decedent. Consequently, in these counties a change in ownership occurs if any heir or beneficiary obtains an interest in any real property greater than his/her proportional interest in the estate or trust. For example, if property is left to four children and one child is granted a 100 percent interest in the parent's residence, the assessor would have determined that 75 percent of the property interests transferred. Using this policy, the percentage of interests transferred is the amount that the interest in the real property exceeds the proportional interest in the estate.

Our recommendations for the change in ownership consequences of property distributed on a share and share alike basis depend on the provisions of the trust instrument or the will.

TRUSTS

The key to whether a change in ownership occurs when property is distributed according to a trust on a share and share alike basis is whether the trust instrument limits the trustee's powers to distribute property.

Probate Code Section 16200 provides, in part, that a trustee has not only the powers conferred by the trust instrument but also, except as limited in the trust instrument, the powers conferred by statute. Following Probate Code Section 16200 are a number of provisions conferring express statutory powers on trustees. Among those provisions is Section 16246 which provides:

"The trustee has the power to effect distribution of property and money in divided or undivided interests and to adjust resulting differences in valuation. A distribution in kind may be made pro rata or non-pro rata." (Added by Chapter 820 of the Statutes of 1986.)

The statement "a distribution in kind may be made pro rata or non-pro rata," means that the trustee has a choice in how he/she distributes non-cash assets, such as real property. The trustee can either give the beneficiaries common ownership in all the assets of the trust estate (pro rata) or can allocate specific assets to individual beneficiaries (non-pro rata).

California trust law recognizes that the administration of a trust is governed by the trust instrument. Union Bank and Trust Co. v. McColgan (1948) 84 Cal. App. 2d 208. Thus, where the trust instrument conflicts with statutory power, the instrument controls unless a court, pursuant to Probate Code Section 1620.1, relieves the trustee of the restriction in the instrument. Absent a restriction in the trust instrument, the trustee enjoys both the powers conferred by the trust instrument and those conferred by the provisions of the Probate Code, including Section 16246.

Unless the trust instrument specifically states otherwise, the trustee has the power to distribute the trust assets in kind on either a pro rata or non-pro rata basis. Consequently, property in a trust, where the trustee has the power to distribute trust assets on a share and share alike basis can be treated as a direct transfer from parent to child to the extent that the value of the property does not exceed the value of the stipulated share of trust assets. This is because both statutory and case law recognize that, unless the trust instrument specifically states how the beneficiaries are to share the trust's assets, the trustee has the power to distribute property as he/she wishes. Accordingly, the assessor should recognize these transfers of property as a parent to child transfer, which may qualify for the parent/child exclusion under Section 63.1.

Example:

A parent leaves a trust estate with a net worth of \$500,000 to his four children on a share and share alike basis. Each child is to receive \$125,000 net worth of assets. The trust document does not limit the trustee's power to distribute the trust assets. Accordingly, as provided by Probate Code Section 16246, the trustee has the power to distribute sole ownership of any asset or a fractional interest in any asset to any of the children.

In distributing the trust, the trustee decides to deed the principal residence, worth \$112,500 and no outstanding loans, to one child. In our view, this would be considered a 100 percent transfer from parent to child which may be excluded from change in ownership under Section 63.1 if a proper claim form is filed. This is because the net worth of the property is under the child's \$125,000 share in the estate. If the property had a net worth which was more than \$125,000, a partial change in ownership

would have occurred. The following example outlines the procedures for such a situation.

If the trustee deeds another child an investment property, with a market value of \$225,000 and an outstanding mortgage balance of \$50,000 (encumbrances in the property should be considered), then a 28.57 percent reappraisable change in ownership would occur. This is calculated as follows: equity in the property minus child's share of the trust estate divided by the equity in the property ($\$175,000 - \$125,000 / \$175,000$). In this case, the equity in the property that the child receives exceeds his/her proportional share of the trust estate by 28.57 percent. In effect, this 28.57 percent interest in the property is a transfer of property between siblings. It does not qualify as a transfer from parent to child since it exceeds the direction that the children share and share alike. Therefore, a 28.57 percent change in ownership of the property has occurred while the remaining 71.43 percent may be excluded from change in ownership according to the provisions of Section 63.1 of the Revenue and Taxation Code.

In practice, assuming a 1975 factored base year value of \$75,000, the new base year value of the property would be calculated as follows:

1975	Factored base year value	\$ 75,000 x 71.43% = \$ 53,572
1990	Market value	\$225,000 x 28.57% = <u>64,282</u>
	Value to be enrolled for current roll	\$117,854

WILLS

Whether a change in ownership occurs when a child receives a 100 percent interest in real property from a parent's estate when the estate is distributed according to a will on a share and share alike basis depends on whether the will gives the executor a clear grant of broad discretion to distribute property in kind on a pro rata or non-pro rata basis.

Under the Probate Code provisions applicable to wills, the general rule is that a devise of property to more than one person vests the property in them as owners in common. Probate Code Section 6143 provides that unless a contrary intention is indicated in the will, "a devise of property to more than one person vests the property in them as owners in common." See also Estate of Pence (1931) 117 Cal. App. 323, at 331, holding that a devise to more than one person to share and share alike indicates a gift in common. See also Noble v. Beach (1942) 21 Cal. 2d 91, 94; and Estate of Russell (1968) 69 Cal. 2d 200, 214-215.

Of course, many wills contain provisions which grant discretion to distribute property in kind on a pro rata or non-pro rata basis or something equivalent. Probate Code Section 6140(a) states that the intention of the testator as expressed in the will controls the legal effect of the dispositions made in the will. In light of this general principle, a clear grant of discretion to distribute the property in kind on a pro rata or non-pro

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rata basis must be given due recognition. In the absence of such a clear grant of broad discretion in the will, however, or an appropriate judicial determination of the meaning of the provisions of the will, assessors are entitled to rely on the general rule set forth in Section 6143 of the Probate Code.

Therefore, if it is determined that the will clearly grants the executor broad discretion in distributing property in kind on a pro rata or non-pro rata basis, the change in ownership consequences are identical to those in the example illustrated for trusts above. If it is not certain or it has not been proved that the executor has this power, then the assessor is correct in allocating an equal fractional interest in each and every property owned by the parent to each child for property tax purposes. It follows that a partial change in ownership will occur if any child acquires an interest in any real property owned by the parent greater than the proportional interest in the estate. It is important to note that the taxpayer carries the burden of proving, to the assessor's satisfaction, that the will in fact grants the requisite discretionary power in distributing the property.

If you have any further questions, please feel free to contact our Real Property Technical Services Unit at (916) 445-4982.

Sincerely,



Verne Walton, Chief
Assessment Standards Division

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