STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
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January 21, 1992

Re: Proposition 58

Dear Mr.

This is in response to your letter of December 8, 1991, to me in which you request our opinion as to the applicability of Proposition 58 and Revenue and Taxation Code Section 63.1 under the following facts and proposed transactions described in your letter.

B died June 1, 1991. Under the terms of the R and B Living Trust (the "Trust"), the Trust assets were to have been divided equally between Trust A (a continuing revocable living trust for the husband's share of the community property) and Trust C (an irrevocable QTIP trust of which husband was the income beneficiary for his life). R died July 4, 1991. On the death of husband, all of Trust A and all of Trust C is to be distributed, free of trust, to C their only child and sole beneficiary of the Trust.

The Trust document also provides for a Trust B (a standard bypass trust). However, both of the had fully used their unified credits against gift and estate taxes to make gifts of other than real property to their daughter, such that Trust B does not get funded at the death of B. Because of the proximity of their deaths, the executor will not elect to have Trust C qualify for the marital deduction. Trust C contains B community and any of her separate property interests in the Trust.

You have been advised by of the San Diego County Assessor's Office that, under the terms of the Trust, Trust C is treated as a spousal transfer on the death of (under §63) and only the property passing from Trust A on

death is eligible for the $1.0 million exclusion under section 63.1. Such being the position of the County Assessor, you asked Ms. C whether, if the executor of the estate of makes a disclaimer of his interest in all real property in Trust C (or all of Trust C) in accordance with Probate Code section 277(b), the half of the real property passing to Trust C on B death would thereby qualify as having passed from B to C for purposes of section 63.1.

After discussing this question with her supervisor, Ms. C informed you that it is the position of the San Diego County Assessor that the disclaimer would not permit the real property passing from B to C through Trust C to qualify under section 63.1.

After reading your letter, it was not clear to me why the assessor was taking the position that only the property passing from Trust A on R death would be eligible for the $1 million exclusion. I called the Assessor's office to find out and was advised by Mr. Q that such conclusion was based on a letter I had written to the San Diego County Assessor dated May 21, 1991, a copy of which is enclosed.

In that letter, we concluded that the $1 million exclusion was available with respect to the bypass trust as well as the trust containing the surviving spouse's share of the community property as long as the surviving spouse did not have a general power of appointment over the principal of the bypass trust. We concluded on page 4 that the power to invade principal by the trustee did not constitute a general power of appointment in the surviving spouse over the Trust B principal because the surviving spouse was not the trustee and because the trust specifically prohibited any trustee who was also a beneficiary from invading trust principal for his own benefit.

Mr. Q apparently concluded that since the surviving spouse in your case was a trustee and since the trust did not specifically prohibit invasion of trust principal by a trustee who was also a beneficiary, the surviving spouse must have a general power of appointment over the assets of Trust C because of the following language found in Article III(E)(2):

> If at any time the surviving Trustor is in need of funds for his or her reasonable support or maintenance, the Trustee shall pay to or apply for the use or benefit of the surviving Trustor such amounts of the principal of Trust C, up to the whole thereof, as is required therefor;

provided, however, that the Trustee shall not make any distribution from Trust C under this provision until Trust A has been exhausted.

Civil Code section 1381.2 defines general and special powers of appointment as follows:

> (a) A power of appointment is "general" only to the extent that it is exercisable in favor of the donee, his estate, his creditors, or creditors of his estate, whether or not it is exercisable in favor of others.
>
> (b) A power to consume, invade, or appropriate property for the benefit of a person or persons in discharge of the donee's obligation of support which is limited by an ascertainable standard relating to their health, education, support, or maintenance is not a general power of appointment.
>
> (c) A power exercisable by the donee only in conjunction with a person having a substantial interest in the appointive property which is adverse to the exercise of the power in favor of the donee, his estate, his creditors, and creditors of his estate is not a general power.
>
> (d) All powers of appointment which are not "general" are "special".
>
> (e) A power of appointment may be general as to some appointive property or an interest in or a specific portion of appointive property and be special as to other appointive property.

Under Civil Code section 1381.1(b), "donee" means the person to whom a power of appointment is given or in whose favor a power is reserved.

Internal Revenue Code section 2041 contains similar definitions of powers of appointment for purposes of federal estate tax.

Article V(G) of the Trust provides, in effect, that R and C shall act as co-trustees on the death of the first spouse unless either is unable or unwilling to act.

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Assuming both were willing and able to act as of the date of B death, R power would appear not to be general pursuant to Civil Code section 1381.2(c) because it could only be exercised in conjunction with C (Probate Code §15620) and C as the sole beneficiary on R death would seem to clearly have a substantial interest in the Trust C property which would be adverse to the exercise of the power in favor of R In that event, no disclaimer of Trust C would be necessary in our view.

It is also arguable that R power is not general pursuant to Civil Code section 1381.2(b), however, we could find no California law on this question.

With respect to the disclaimer issue, Probate Code section 282(a) provides in relevant part that "...the interest disclaimed shall descend, go, be distributed, or continue to be held (1) as to a present interest, as if the disclaimant had predeceased the creator of the interest.... A disclaimer relates back for all purposes to the date of death of the creator of the disclaimed interest...." (Emphasis added.) Also, Probate Code section 277(b) permits the executor of a decedent's estate to disclaim on behalf of the decedent.

Under the Trust, the real property passing to Trust C on B death would have passed directly to C had R predeceased B Thus, under Probate Code section 282(a), a valid disclaimer of all interests in Trust C on behalf of R would relate back to the date of B death so that as of the date of B death the property in Trust C would be deemed to have passed from B to C for all purposes. In our view, this would include the purpose of the parent-child exclusion under Proposition 58 and section 63.1.

The views expressed in this letter are, of course, advisory only and are not binding upon the assessor of any county. You may wish to consult the San Diego County Assessor in order to determine whether the described property 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,

Eric F. Eisenlauer

Eric F. Eisenlauer
Senior Tax Counsel

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Enclosure