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March 10, 1994

In Re: **Change in Ownership - Distribution of Partnership  
Interests Upon Death of Partners, Application of  
Parent-Child Exclusion.**

Dear \_\_\_\_\_

This is in response to your letter of January 25, 1994, requesting our opinion and any precedent letters concerning the change in ownership consequences and the application of the parent-child exclusion to the distribution of partnership interests upon the death of the each of the partners and the dissolution of the partnership.

You have submitted the following hypothetical situation for purposes of our analysis:

1. General Partnership was formed prior to March 1, 1975, by four siblings for the purpose of owning and managing certain real property in equal shares.
2. Several years ago, A died. His one fourth partnership interest was in a revocable trust, in which the remainder beneficiaries are his children and no distributions from the trust have yet been made.

3. B died six months after A, and his one fourth partnership interest was probated and thereafter distributed to a testamentary trust, in which his spouse is the sole income beneficiary.

4. C died six months after B, and her one fourth partnership interest was probated and thereafter distributed to her two children.

5. D just recently died, and her one fourth partnership interest is subject to probate. D's children are her sole beneficiaries, however, no distributions have been made.

6. Dissolution of the partnership, under the terms of the partnership agreement, occurred upon C's death. Thus, D intended to wind up the partnership and distribute the assets on a pro rata basis to the partners' successors in interest, but she died before the deeds were executed. D's executors will now complete the winding up and distribution by deeding co-tenancy interests in the real property to all successors in interest including D's children.

You wish to know the change in ownership consequences of the foregoing transfers and the availability of the parent-child exclusion with regard to the partnership distributions. For the reasons hereinafter explained, we reach the following conclusions: 1) the dissolution of a partnership due to the death of the partners and the winding up of the partnership by the sole surviving partner does not constitute a change in control/ownership of the partnership under Section 64, subdivision (c); 2) although the parent-child exclusion is not applicable to transfers of the partnership interests to the deceased partners' heirs, no change in ownership occurs if no heir receives more than 50% of the partnership interests; and 3) the partnership's distribution of interests in real property to the deceased partners' heirs may be excluded under Section 62, subdivision (a)(2), providing the percentages of the property interests transferred are exactly proportionate to the partnership interests held by each heir.

#### LAW AND ANALYSIS

Revenue & 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."

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Section 61, subdivision (i) states that a change in ownership includes:

The transfer of any interest in real property between a corporation, partnership, or other legal entity and a shareholder, partner, or any other person.

Dissolution/Winding Up of Partnership by D; No Change in Control.

Based on the hypothetical facts submitted, each of the partners (siblings) held an equal 25% ownership interest in the partnership (we assume this means partnership capital and profits) from the time of its formation through its termination. The partnership agreement apparently provided that upon a partner's death, the deceased partner's 25% partnership interest would pass to the heirs of the deceased partner, not to the surviving partners, and the business of the partnership would continue through the death of the third partner. At this time, the partnership would dissolve and the partnership interests would be liquidated and distributed pro rata by D to herself, as the surviving partner, and to the deceased partners' heirs.

We also assume that the agreement did not authorize any of these heirs to participate as a partner, since no such authorization is mentioned in your facts. Section 9762 of the California Probate Code provides that authorization permitting the decedent's representative to participate as a partner in a partnership in which the decedent was a general partner must be made in the written partnership agreement or by court order. Moreover, California Corporations Code Section 15018 provides that, subject to agreement between the partners, no person can become a member of a partnership without the consent of all the partners. Any purchase, assignment, or devise of a partner's interest does not make the purchaser, assignee, or personal representative a partner. Thus, at the time of the death of C, the heirs of the three deceased partners held beneficial interests in the partnership capital and profits (in proportion to the percentage held by the deceased partners), but were without all the rights, powers and duties accorded a partner. Only one partners, D, remained, so the partnership dissolved pending winding up by D.

Since none of the deceased partners' heirs became partners, and the sole remaining partner was D, it might be contended that D acquired control of the partnership, resulting in a change in ownership of the partnership, by virtue of her 100% termination

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rights over all of the partnership interests. However, it has never been our interpretation of the change in ownership statutes that one who is the surviving partner in a partnership (following the deaths of the other partners) and who thereby has exclusive authority over its winding up, is to be considered in control of the partnership, so that indirect ownership/control of the partnership can be attributed to him/her for change in ownership purposes, providing such surviving partner owns less than 50% of the partnership capital and profits.

We have consistently taken the position in the past that obtaining control of a partnership for change in ownership purposes requires the purchase or transfer of partnership interests within the meaning of Section 64, subdivision (c), which states in pertinent part:

When a corporation, partnership, or other legal entity or any other person obtains control, as defined in Section 25105, in any corporation, or obtains a majority interest in any partnership or other legal entity through the purchase or transfer of corporate stock, partnership interest, or ownership interests in other legal entities, such purchase or transfer of such stock or other interest shall be a change of ownership of property owned by the corporation, partnership, or other legal entity in which the controlling interest is obtained.

These statutory provisions are interpreted by Property Tax Rule 462 (j), which provides in part:

(3) Transfers of ownership interests in legal entities. Except as otherwise provided in subdivision (4), the purchase or transfer of corporate stock, partnership shares, or ownership interests in other legal entities is not a change in ownership of the real property of the legal entity.

(4) Exceptions:

(A) When any corporation, partnership, other legal entity or any person:

(ii) obtains direct or indirect ownership of more than 50 percent of the total interest in both partnership capital and profits,

Upon the acquisition of such direct or indirect ownership or control, all of the property owned directly or indirectly by the acquired legal entity is deemed to have undergone a change in ownership.

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Based on the foregoing, D at no time acquired more than her 25% interest in the partnership capital and profits. The fact that D was the only remaining partner after C's death and held 100% of the voting power and decision-making authority over the partnership affairs for purposes of winding up, does not mean that D acquired any greater interest in the partnership capital and profits. This conclusion is consistent with the Corporations Code and Probate Code provisions noted above stating that on the death of a partner, unless the decedent's personal representative is authorized to continue as a partner in the partnership, the surviving partner has the exclusive right and duty to continue in possession of the partnership and settle its business. (See Corporations Code Sections 15021-15045.)

As such, the surviving partner is similar to a trustee in that he/she has the right to possession and control of all the partnership property until the affairs of the partnership are wound up, but receives no vested or beneficial interest in the partnership or its assets by virtue of this "trust". Thus, where full authority equivalent to 100% voting control is given to one partner as a consequence of the death of the other partners and is solely for purposes of winding up the partnership and distributing its assets, we would conclude that it is not tantamount to control of the partnership within the meaning of Section 64, subdivision (c), resulting in a change in ownership of the partnership.

**Transfer of Partnership Interests to Partners' Heirs;  
Ineligible for Parent-Child Exclusion, but No Change in  
Control.**

As to the transfer of each deceased partner's 25% interest in the partnership to his/her heirs (children), the parent-child exclusion is not available for two reasons: 1) the exclusion is applicable only to transfers of real property, not interests in partnerships or other legal entities, and 2) by its terms it is applicable only to transfers between parents and their children, not between legal entities and children.

For purposes of determining whether a transfer is excluded from change in ownership consequences under Section 63.1, it is necessary to determine in each case whether an "eligible transferor" transferred real property to an "eligible transferee". Section 63.1 provides in relevant part:

(a) Notwithstanding any other provision of this chapter, a change in ownership shall not include either of the

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following purchases or transfers for which a claim is filed pursuant to this section:

(2) The purchase or transfer of the first one million dollars (\$1,000,000) of full cash value of all other real property of an eligible transferor in the case of a purchase or transfer between parents and their children.

(c) As used in this section:

(1) "Purchase or transfer between parents and their children" means either a transfer from a parent or parents to a child or children of the parent or parents or a transfer from a child or children to a parent or parents of the child or children.

Based on the facts you provided, the respective heirs (children) of the partners A, B, C, and D received a 25% partnership interest rather than an interest in real property at the time of each partner's death. Moreover, the transferor of the real property is the partnership and not the parents. Finally, there is no indication that all of the heirs of the deceased partners are the children of such partners as defined by Section 63.1, subdivision (c)(2). Accordingly, these transfers do not qualify for the parent-child exclusion.

However, Section 64, subdivision (a) provides that the purchase or transfer of ownership interests in legal entities, such as partnership interests, shall not be deemed to constitute a transfer of the real property of the legal entity unless, as previously noted, pursuant to Section 64, subdivision (c), the transfer results in an individual or an entity acquiring more than 50% of the ownership interests in the legal entity.

Under the assumed facts, each of a partners' collective heirs shared a 25% interest in the partnership capital and profits. Since none of these transfers presumably resulted in any heir obtaining an interest of more than 50 percent in the partnership's capital and profits, the transfer of each deceased partner's 25% partnership interest did not result in a change in ownership.

**Transfers of Interests in Real Property from Partnership;  
Excluded if Transferred in Same Proportionate Shares.**

The distribution of interests in the partnership's real property to the partners' respective heirs will constitute a

change in ownership unless excluded under the Section 62, subdivision (a)(2), which requires that the proportional ownership interests of the transferor (partnership) and the transferees (heirs) remain the same following the transfer.

Section 62, subdivision (a)(2) excludes from change in ownership:

Any transfer between an individual or individuals and a legal entity or between legal entities, such as a cotenancy to a partnership, a partnership to a corporation, or a trust to a cotenancy, which results solely in a change in the method of holding title to the real property and in which proportional ownership interests of the transferors and transferees, whether represented by stock, partnership interest, or otherwise, in each and every piece of real property transferred, remain the same after the transfer.

The statutory provisions of Section 62, subdivision (a)(2) have been interpreted by subdivision (j)(2)(B) of Property Tax Rule 462. That rule states in pertinent part:

[Excluded from the change in ownership provisions are] transfers of real property between separate legal entities or by an individual(s) to a legal entity (or visa versa), which result solely in a change in the method of holding title and in which the proportional ownership interests in the property remain the same after the transfer. (The holders of the ownership interests in the transferee legal entity, whether such interests are represented by stock, partnership shares, or other types of ownership interests, shall be defined as "original co-owners" for purposes of determining whether a change in ownership has occurred upon the subsequent transfer(s) of the ownership interests in the legal entity.)

With regard to the transfer of real property from a legal entity to the entity's partners/shareholders specifically, subdivision (j)(2)(B) provides the following examples:

Examples:

(iv) Corporation X owns Blackacre and Whiteacre (both are of equal value). A & B each own 50 percent of Corporation X's shares. X transfers Whiteacre to A and Blackacre to B. Change in ownership of 100 percent of both Blackacre and Whiteacre.

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(v) A transfer of real property from Corporation X to its sole shareholder. No change in ownership.

The hypothetical you have described may be a parallel situation to the example in subdivision (2)(B)(v). Partnership is terminating and distributing to each partner's heirs 25% of each real property owned by Partnership, based on the 25% partnership interest which each partner's heirs collectively own. However, to maintain exact proportionality as required, it will be necessary for the Partnership to identify the percentage of partnership interest currently held by each heir and to transfer to each heir the same percentage of interest in each of the partnership real properties. Thus, if A has two heirs each holding a 12 1/2% partnership interest, Partnership must distribute to each of these heirs an equivalent 12 1/2% interest in each of the real properties. The transfers will be excluded from change in ownership under Section 62, subdivision (a)(2) only if the exact percentage of interests in the real properties is transferred in return for the exact percentage of partnership interests, so that the transfer results solely in a change in the method by which heirs hold title to the real properties.

In response to your request for precedent letters, please find copies of the following letters enclosed which discuss the application of several change in ownership provisions to transfers of partnership interests under varying sets of circumstances.

Elbrecht Letter	June 4, 1986
McManigal Letter	May 18, 1989
Cazadd Letter	August 26, 1992

We suggest that you also review *Kern v. Imperial County*, 226 Cal.App.3d 391.

In addition, for your future reference on such matters, you may wish to purchase from the State Board of Equalization the Property Tax Law Guide, Volume 3, which contains annotations of our opinion letters and correspondence, interpreting property tax laws, rules, and court cases.

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 appropriate assessor in order to confirm that the described properties will be assessed in a manner consistent with the conclusions stated herein.

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

Sincerely,



Kristine Cazadd  
Tax Counsel

KEC:ba  
Attachments

cc:

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