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June 12, 2012

Honorable David E. Cogdill  
Stanislaus County Assessor  
1010 Tenth Street, Suite 2400  
Modesto, California 95354

***Re: Change in Ownership – Sprinkle Power  
Assignment No. 12-033***

Dear Mr. Cogdill:

This is in response to your letter dated February 14, 2012 to Dean Kinnee, Chief of the County-Assessed Property Division, for a legal opinion as to whether there was a change in ownership of certain California real property upon their transfer to an irrevocable trust.<sup>1</sup> Mr. Kinnee forwarded that request to the Legal Department to respond. For the reasons explained below, it is our opinion that the transfers resulted in a change in ownership of the property.

### **Facts**

Husband (H) and Wife (W) acquired two parcels of California real property (the Property) in 1994 and 1995, and transferred the Property to an irrevocable trust (the Trust) on September 14, 2010. The Trust<sup>2</sup> refers to H as the Settlor of the Trust, and names two persons as trustees and states they shall be referred to collectively as "Trustee"<sup>3</sup> (the Trustee). The Trust also names a person as the protector of the Trust (the Protector) who has broad powers to oversee and approve the actions of the Trustee.<sup>4</sup>

The Trust is an inter vivos trust and is irrevocable by the Settlor.<sup>5</sup> Absent action by the Trustee, the beneficiaries of the Trust are the Settlor, the Settlor's spouse, and an individual<sup>6</sup> who is later identified as the "Child"<sup>7</sup> (the Child). We are told by the Stanislaus County Assessor's Office (the Assessor's Office) that Child is the granddaughter to W and that both parents of the Child are still living.<sup>8</sup> Additionally, the Trust provides that the Trustee, with the consent of the

<sup>1</sup> This opinion is requested in connection with an assessment appeal filed with the Stanislaus County Assessment Appeals Board (AAB), and the matter will be set for hearing pending the outcome of this opinion. The parties are aware that we will be issuing this opinion, and were given an opportunity to provide any relevant information.

<sup>2</sup> The Trust document is titled "Trust Instrument of Settlement" and is dated August 18, 2010.

<sup>3</sup> See Trust document, first paragraph.

<sup>4</sup> See Article IV, pages 16-18.

<sup>5</sup> See Article I, subd. (B).

<sup>6</sup> See Article II, subd. (A)(1).

<sup>7</sup> See Article II, subd. (E)(1).

<sup>8</sup> For purposes of this letter, we assume the Child is also the grandchild of H.

Protector, at any time during the lifetime of the Settlor, "may designate any member or members of a class consisting of the descendants of the Settlor's parents, and the spouses of such individuals, or any charitable organization" to be a beneficiary.<sup>9</sup> No further action has been taken by the Trustee and the beneficiaries remain as originally named by the Settlor.

The dispositive provision of the Trust provides that the Trustee, with the consent of the Protector, at any time during the lifetime of the Settlor, shall have the power to pay or apply "the whole or any part or none of the income or principal or both of the Trust Property to, or for the benefit of, all or such one or more or none of the Beneficiaries in such shares and in such manner generally as the Trustee shall consider advisable."<sup>10</sup> Upon determining there had been a change in ownership of the Property when H and W transferred their interests in the Property to the Trust, the Assessor's Office reassessed the Property.

### **Law and Analysis**

Article XIII A, section 2 of the California Constitution requires the reassessment of real property upon a "change in ownership," unless an exclusion from change in ownership applies. A "change in ownership" is defined as a transfer of a present interest in real property, including the beneficial use thereof, the value of which is substantially equivalent to the value of the fee interest. (Rev. & Tax. Code, § 60.)

As a general rule, a change in ownership includes the transfer of real property into a trust at the time of transfer.<sup>11</sup> In an irrevocable trust, a change in ownership of real property occurs to the extent that persons other than the trustor-transferor are or become present beneficiaries of the irrevocable trust unless otherwise excluded from change in ownership. (Rule 462.160, subd. (b)(1).)

Rule 462.160, subdivision (b)(1)(A) further provides that:

[w]here a trustee of an irrevocable trust has total discretion ("sprinkle power") to distribute trust income or property to a number of potential beneficiaries, the property is subject to change in ownership, because the trustee could potentially distribute it to a non-excludable beneficiary, unless all of the potential beneficiaries have an available exclusion from change in ownership. (See Example 2 of Rule 462.160.)

Revenue and Taxation Code<sup>12</sup> section 63.1, which implements the parent-child and grandparent-grandchild exclusions, excludes from change in ownership the transfer between parents and children of any number of principal residences and the first \$1 million of full cash value of other real property. (Rev. & Tax. Code, § 63.1, subds. (a)(1) and (2).)

Here, the Trust contains a sprinkle power which gives the Trustee total discretion to distribute trust property to a number of potential beneficiaries. In addition to the named

<sup>9</sup> See Article II, subd. (A)(2).

<sup>10</sup> See Article II, subd. (A)(3).

<sup>11</sup> Cal. Code Regs., tit. 18, § 462.160, subd. (b)(1)(A). All subsequent references to Rules are to sections of title 18 of the California Code of Regulations.

<sup>12</sup> All section references are to the Revenue and Taxation Code unless otherwise specified.

beneficiaries, the Trustee is given authority to designate any members of a class of persons or any qualified charitable organization as beneficiaries. However, no additional beneficiaries have yet been named. Because a change in ownership requires a transfer of a *present* interest in real property and future interests in real property are not assessed, only the beneficiaries originally named by the Settlor are the present beneficiaries of the Trust.

Therefore, the Trustee could potentially distribute all or a portion or none of the Property to H or to W or to Child. When a trust contains a sprinkle power, *all* of the persons included as beneficiaries must be eligible for an exclusion. If even one person included as a beneficiary is not excludable, a change in ownership of all real property owned by the Trust will occur. (Property Tax Annotation 625.0236 (4/18/01); Rule 462.160, subd. (b)(1).) A distribution to W is excludable under the interspousal exclusion. (Rev. & Tax. Code, § 63.) However, there is no exclusion available if the Trustee distributes any portion or all of the Property to Child because under section 63.1, subdivision (a)(3) a transfer of real property from grandparent to grandchild can only be excluded from reassessment if all of the parents of the grandchild are deceased. Since the Child's parents were both living on the date the Property was transferred to the Trust, the transfer would not qualify for the grandparent-grandchild exclusion. Therefore, we conclude that because the Trustee has the discretion to distribute any portion of the Property to the Child, a non-excludable beneficiary, a change in ownership of the Property occurred at the time the Property was transferred to the Trust.

The views expressed in this letter are 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 on any person or public entity.

Sincerely,

/s/ Susan Galbraith

Susan Galbraith  
Tax Counsel

SG:mcb

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cc:     Mr. David Gau           MIC:63  
          Mr. Dean Kinnee        MIC:64  
          Mr. Todd Gilman        MIC:70