



STATE BOARD OF EQUALIZATION

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Executive Secretary

February 8, 1988

Dear Mr. :

Re: Proposition 58 - Your File No. 3679.1

This is in response to your letter of January 18, 1988 to the attention of the Legal Staff of the State Board of Equalization in which you request our opinion as to the applicability of Proposition 58 and Revenue and Taxation Code* section 63.1 to the following two factual situations presented in your letter.

1. Mrs. X is left all of Mr. X's estate. The will provides that Mrs. X disclaim any and all of the amounts given to her under the will, the property is to pass to Mr. Y as trustee for the benefit of the X's two children. The trust terms are as follows: While the children are minors, the trustee can either pay out or accumulate the income depending on the needs of the minor; when the child obtains majority, the trustee is obligated to pay all of the trust income to the child and may pay any portion of the corpus to the child if the child is in need of such funds for his health, education and welfare; lastly, the trustee is obligated to distribute one-half of the trust principal to the child when he attains age 25 and the other one-half when the child attains age 30. The trust further provides that in the event a child dies before attaining age 30, the child's interest in the trust is to pass to his issue and if none, then to any other child of the X's and in the event there are no children of the X's and no issue of the deceased child, then the property is to pass to the issue of the X's. A failure of these beneficiaries results in the property passing to a charity designated by the trustee.

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

February 8, 1988

For the purpose of this discussion, the fair market value of the property transferred into the trust is less than \$1,000,000 and constitutes a portion of the decedent's family residence.

Response:

As you know, Proposition 58 amended article XIII A of the California Constitution to provide among other things that the terms "purchase" and "change in ownership" do not include the purchase or transfer of the principal residence and the first \$1 million of the full cash value of other real property between parents and children. Chapter 48 of the Statutes of 1987 (AB 47) is the implementing legislation for Proposition 58. Chapter 48 added section 63.1 to the Revenue and Taxation Code and applies to purchases and transfers of real property completed on or after November 6, 1986.

For purposes of reappraising real property as of the date of change in ownership (purchase or transfer) of real property, Property Tax Rule 462(n)(3) (Title 18, California Administrative Code section 462(n)(3)) provides that the date of death of the decedent shall be used with respect to transfers by will or intestate succession.

It is our position that Proposition 58 and section 63.1 are applicable to transfers through the medium of a trust provided the requirements of those provisions are otherwise satisfied. See enclosed Board Letter to Assessors dated September 11, 1987, No. 87/72, question No. 9. Although Proposition 58 and section 63.1 do not specifically deal with transfers in trust, the change in ownership rules relating to trusts in effect provide that subject to exceptions not here relevant, the present beneficiary of the trust is the beneficial owner of the trust property. Section 62(d), Property Tax Rule 462(c)(2)(A). Further, it is our position that one may be a present trust beneficiary even though the right to receive income is discretionary as long as no one else presently has a right to income or principal.

*STATUTE
Amended to
incl. trust*

Since nobody but decedent's children presently has a right to receive the income or principal of the trust, we are of the opinion that the transfer by will is between a parent (Mr. X) and his children for purposes of proposition 58 and section 63.1. This, of course, would include property passing to the trustee as a result of a valid disclaimer by Mrs. X. (Probate Code § 282(a).) Accordingly, if the date of death of Mr. X was

February 8, 1988

on or after November 6, 1986 and the full cash value of the real property transferred was less than \$1,000,000** as you indicate, the transfer would be excluded from change in ownership under Proposition 58 and section 63.1.

Further, even if someone other than the children had a present interest in the trust property, a change in ownership would not necessarily result. For example, had Mr. X given Mrs. X a life estate in that portion of the family residence which is in the trust and she did not disclaim it either intentionally or because she accepted the life estate and was thus precluded from disclaiming it by Probate Code Section 285(a), the transfer of such interest to Mrs. X would be excluded from change in ownership as an interspousal transfer under section 63. In our view, a change in ownership would result, however, to the extent that persons other than decedent's spouse or children received a present interest in the trust property.

2. Under factual situation number 2, Mr. A is married to Mrs. A. This is his second marriage. The property in question constitutes the sole and separate property of Mr. A. The children who are to be the beneficiaries of the trust are the children of Mr. A. Mrs. A is their stepmother. Mr. A creates a trust for the benefit of his three children. The trust is to terminate upon the death of Mr. A. During the term of the trust, the trustee may distribute income to any of the children if they are in need of funds for their health, education, maintenance and welfare. Upon the death of Mr. A, the property is to be distributed in equal shares to the three children of Mr. A. In the event any child predeceases Mr. A, the property shall pass in accordance with the terms and conditions of a limited power of appointment held by such child. (By limited power of appointment, it is meant that the child cannot appoint to his estate or to his creditors.) The property is commercial real property. All of the parties are adults. For purposes of discussion, the fair market value of the property is \$1,500,000. Further, it is contemplated that Mrs. A will join Mr. A in making the gift in determining federal gift tax liability. Please advise as to whether

**Under Proposition 58 and section 63.1, the \$1 million full cash value limitation applies to real property other than the principal residence of the transfer. Thus, if the only real property transferred by Mr. X was his interest in his principal residence, the \$1 million full cash value limitation is not applicable.

February 8, 1988

the transfer by Mr. A to the trust is a transfer necessitating reevaluation and, further, please advise as to whether Mrs. A can join with Mr. A in the gift transfer for purposes of determining the amount of property exempt from reevaluation.

Response:

As explained above, since there will be no present beneficiary of the income or principal of the trust other than Mr. A's children the transfer is between a parent and his children for purposes of Proposition 58 and section 63.1. Only \$1,000,000 of full cash value will be excluded from change in ownership, however, unless Mr. A first conveys an undivided interest in the real property to Mrs. A. Such a transfer would be excluded from change in ownership by section 63. If such a transfer is made, Mr. A as a parent and Mrs. A as a stepparent can combine their separate \$1,000,000 exclusions and jointly transfer the property to the trust without reappraisal (§ 63.1(a)(2)), (b)(2) and (c)(2)(B).

Since section 2 of chapter 48 expresses the intent of the Legislature that section 63.1 shall be liberally construed in order to carry out the intent of Proposition 58 and since section 2 expressly approves specified step transactions, it is our view that a preliminary transfer by Mr. A to Mrs. A should be fully recognized for purposes of excluding the transfer in trust from change in ownership.

Lastly, you request that we make available to you copies of any rulings we have issued on the subject of transfers to trusts and the result of such transfers on the reappraisal of property for property tax purposes.

In response to your request, we are enclosing copies of representative opinion letters under my signature regarding the applicability of Proposition 58 and section 63.1 to transfers into and out of trusts dated June 19, 1987 and December 11, 1987.

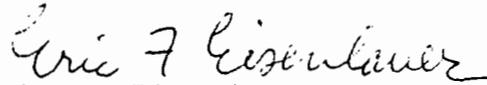
In addition to the foregoing, we are enclosing copies of pages 5410.2, 5411 and 5412 of the Property Tax Law Guide. As you can see, these pages contain annotations of opinion letters concerning whether transfers into and out of trusts are changes in ownership without regard to Proposition 58 and section 63.1. If you desire copies of any of these opinion letters, please let us know. There is a charge of \$3.00 plus \$.10 per page for each letter.

February 8, 1988

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 property will be assessed in a manner consistent with the conclusion stated above.

If we can be of further assistance in this matter, please let us know.

Very truly yours,



Eric F. Eisenlauer
Tax Counsel

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Enclosures

cc: Mr. Gordon P. Adelman
Mr. Robert H. Gustafson
Mr. Verne Walton