



STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
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Executive Director

April 6, 1992

Dear Mr.

Please excuse our delay in responding to your letter of January 13, 1992. Other matters requiring our attention have made such delay unavoidable.

You have requested our opinion as to whether one or two \$1,000,000 parent-child exclusions are applicable under the following facts contained in your letter and materials submitted therewith.

You represent Redacted hereinafter "Son." His father Redacted hereinafter "Dad," died on March 18, 1990. His mother, Redacted, hereinafter "Mom" died approximately 16 years earlier leaving a testamentary "A/B" trust.

Trust "A" consisted of Dad's one-half (1/2) of community property and one-half (1/2) of Mom's separate property. Dad was entitled to the the entire net income of Trust "A" during his lifetime. Dad also had a general power of appointment as to the assets in Trust "A". Failure to exercise the power of appointment by Dad at his death resulted, under the terms of the Trust, in a transfer of the assets to be held, administered and distributed as part of Trust "B".

Trust "B" consisted of Mom's share of the community property and one-half (1/2) of Mom's separate property. Dad was entitled to the entire net income of Trust "B" during his lifetime. Dad also had a right to receive from the Trustee "such sums from principal as he may from time to time request, but not exceeding in any calendar year, five-thousand dollars (\$5,000.00) or five percent (5%) of the aggregate value of the principal of the Trust estate at December 31st of such year, whichever is greater." That right was not cumulative. Upon Dad's death, Trust "B" terminated and all assets went to Son.

The Trust also provided for discretionary payments of principal by the Trustee from Trusts "A" and "B" except while the Trustee was also the beneficiary in which case the Trustee had no right to make such discretionary payments.

It is Son's position that under Proposition 58, he is entitled to a \$1,000,000 exclusion upon the transfer of one-half (1/2) of the property from Dad and an additional \$1,000,000 exclusion upon the transfer of one-half (1/2) of the properties from previously deceased Mom.

At the date of Dad’s death, Trusts “A” and “B” contained Dad’s principal residence valued for purposes of Proposition 58 at \$66,672, and two other parcels (B and C) valued for purposes of Proposition 58 at \$976,270. All three of these parcels were transferred into the Trust when Mom died. In addition, Trust “A” or Trust “B” or both owned an undivided one-half (1/2) interest in two parcels which one-half (1/2) interest for purposes of Proposition 58 was valued at \$490,688. The other one-half (1/2) interest in these two parcels was owned by Son.

No interest in either of these two parcels was transferred into the Trust when Mom died. The Trust, according to the Assessor’s Office, acquired its interest in these parcels in 1979. These parcels are hereafter referred to us the “Later Acquired Parcels”.

Law and Analysis

Revenue and Taxation Code¹ 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.”

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 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.

(b)

...

(2) For purposes of paragraph (2) of subdivision (a), the one million dollar (\$1,000,000) exclusion shall apply separately to each eligible transferor with respect to all purchases by and transfers to eligible transferees on and after November 6, 186, of real property, other than the principal residence, of that eligible transferor.

...

(c) As used in this section:

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

(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 of parents or a transfer from a child or children to a parent or parents of the child or children.

...

(4) “Eligible transferor” means a parent or child of an eligible transferee.

(5) “Eligible transferee” means a parent or child of an eligible transferor.

...

(7) “Transfer” includes, and is not limited to, any transfer of the present beneficial ownership of property from an eligible transferor to an eligible transferee through the medium of an inter vivos or testamentary trust.

...

(f) This section shall apply to purchases and transferors of real property completed on or after November 6, 1986, and shall not be effective for any change in ownership, including a change in ownership arising on the date of an decedent’s death, which occurred prior to that date.

From the foregoing provisions, it is clear that a \$1,000,000 exclusion is available with respect to real property of an eligible transferor, i.e., property which is or was owned by an eligible transferor and then transferred to an eligible transferee.

In this case, Dad received a general power of appointment over the Trust “A” assets at the death of Mom. Since a donee or holder of a general power of appointment may exercise it in his own favor, such a power, in legal effect, gives him an absolute ownership (Estate of Kuttler (1959) 160 Cal.App.2d 332, 338); Morgan v. CIR (1940) 309 U.S. 78, 81 (person who can appoint to his own estate or creditors has “as full dominion over the property as if he owned it”). In view of such rules, we have previously taken the position that for purposes of Proposition 58 and section 63.1, property with respect to which an eligible transferor has a general power of appointment is treated the same as property owned by the eligible transferor. Thus, for purposes of Proposition 58 and section 63.1, Dad was the owner of all property in Trust “A” at the time of his death. For purposes of Dad’s \$1,000,000 exclusion this would clearly include Trust “A”’s one-half (1/2) interest in parcels B and C valued at \$488,135. Also, assuming the Trust’s Later Acquired Parcels were allocated equally to Trust “A” and Trust “B”, another \$245,344 would be included in Trust “A” for a total of \$733,479. The Trust “A” real property was transferred from Dad to Son at Dad’s death and clearly qualifies as part of Dad’s \$1,000,000 exclusion under Proposition 58 and section 63.1.

Assuming none of the Trust “B” real property was transferred to Son by Dad, that property, excluding any interest in the Later Acquired Parcels, would constitute transfers from Mom to Son at the time of Dad’s death and would be part of Mom’s \$1,000,000 exclusion. Trust “B’s” one-half (1/2) interest in that real property is valued at \$488,135. No part of Trust “b”’s interest in the Later Acquired Parcels would constitute transfers from Mom to Son because Mom

never owned any interest in the Later Acquired Parcels. Thus, assuming that none of the Trust “B” real property was transferred by Dad and that the Later Acquired Parcels were allocated equally to Trusts “A” and “B”, Dad would be an eligible transferor of \$733,479 (Trust “A”) and Mom would be an eligible transferor of \$488,135 (Trust “B”).

In our view, however, a large part of Trust “B” was transferred by Dad to Son because of Dad’s \$5,000/five percent (5%) annual power of invasion over the principal of Trust “B”. Such a power constituted a general power of appointment as to the greater of \$5,000 or five percent (5%) of the principal of Trust “B” each year (Civil Code §1381.2). This power was noncumulative. Therefore, each year in which Dad did not exercise this power, the power lapsed. “Allowing a power to lapse each year is tantamount to releasing it or, more indirectly, to exercising the power and then transferring the property to the persons who would have taken if the power had been allowed to lapse”. (5 Bittker, Federal Taxation of Income, Estates and Gifts (1984) §128.3.4, p. 128-23; Treas. Regs. §20.2041 – 3(d) (3).) Assuming Dad never exercised this annual general power of appointment, it lapsed 11 years (1979-1989) as to Trust “B” ‘s interest in the Later Acquired Parcels and 16 years (1974-1989) as to Trust “B” ‘s interest in the other real property. In addition, Dad held this power and could have exercised it for 1990 at the time of his death since it had not lapsed for 1990 at that time. Arguably then, Dad, in legal effect, transferred, subject to his life estate, sixty percent (60%), (12 years x five percent [5%] of Trust “B” ‘s interest in the Later Acquired Parcels to Son and eighty five percent (85%) (17 years x five percent [5%]) of Trust “B” ‘s interest in the other real property to Son. Under this view, Dad would be an eligible transferor of \$562,121 (\$147,206 of Later Acquired Parcels and \$414,915 of the other real property in Trust “B”) of the Trust “B” real property. That amount, in addition to the amount contained in Trust “A”, would make Dad an eligible transferor of an amount in excess of his 1,000,000 exclusion.

As indicated above, Mom is not an eligible transferor of any portion of the Later Acquired Parcels allocated to Trust “B”. Mom would be an eligible transferor, however, as to fifteen percent (15%) of Trust “B” ‘s interest in the other real property which would amount to \$73,220.

Accordingly, in our view, \$1,073,220 would be eligible for exclusion under Section 63.1 (b) (2) as a result of transfers by Mom and Dad to Son as of the date of Dad’s death.

The views are 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’s Office in order to confirm that the described property will be assessed in a manner consistent with the conclusion stated above.

Sincerely,

Eric F. Eisenlauer
Senior Tax Counsel

EFE:rar

Cc: John Hagerty
Verne Walton
Hon. Gregory J. Smith
San Diego County Assessor