STATE OF CALIFORNIA

505.0121

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RAMON J. HIRSIG
Executive Director

August 24, 2010

Re: Request for Legal Opinion – Property Tax Homeowners' Exemption
Assignment No.: 10-094

Dear Ms. :

This is in response to your June 1, 2010, and June 24, 2010, letters wherein you requested our opinion concerning the availability of the property tax homeowners' exemption for real property located in County and owned by an irrevocable inter-vivos trust, A Trust I.

We first note that the homeowners' exemption is administered by county assessors, as are most exemptions from property taxation. Accordingly, it is the County Assessor who will ultimately determine eligibility of the property for exemption. That said, in our view, the property is not eligible for the homeowners' exemption, which is available to principal residences owned and occupied by individual homeowners, because:

1. The property is owned by an irrevocable trust of the kind that has been regarded a Massachusetts trust or business trust by California courts, beginning with *Goldwater v. Oltman* (1930) 210 Cal.408, because of their trust provisions;

2. Massachusetts trusts or business trusts are regarded as legal entities in California, as corporations for purposes of corporate taxation and as legal entities for property tax law purposes. See, for example, Property Tax Annotation Numbers 220.0398 and 220.0399; and

3. Properties of legal entities are not eligible for the homeowners' exemption. See, for example, the March 23, 1982, Letter to Assessors No. 82/50, <u>1982 Homeowners' Exemption – Questions and Answers</u> G5. through G7.; and Property Tax Annotation Numbers 505.0017 and 505.0063.

Thus, it is the provisions[1] of the trust document or documents, not the name of the trust, that are determinative. According to Black's Law Dictionary, a Massachusetts trust, or business trust, is the name given to a business organization wherein property is conveyed to trustees and managed for the benefit of holders of certificates like corporate stock certificates. Such is the nature of A Trust I and the provisions thereof.

Finally, in some cases, property held in a trust, defined as any arrangement whereby property is transferred with the intention that it be administered by the trustee for another's benefit, can be eligible for the homeowners' exemption if all the requirements for the exemption are met. See, for example, the March 23, 1982, Letter to Assessors No. 82/50, Questions and Answers E5. and E6.; and the October 23, 1970, letter upon which Property Tax Annotation Number 505.0120 is, in part, based. However, the provisions of A Trust I preclude trust property contained in it to be considered by the Santa Cruz County Assessor for eligibility for the homeowners' exemption.

Contract and Declaration of A Trust I

The documents submitted include a Contract and Declaration of Trust[2] (Contract) between D B , designated as the "Creator," and S K , designated as the "Independent Trustee." The Contract states that the Creator intends to and does create a trust, and it authorizes the two newly-designated trustees, the Creator and the Independent Trustee, to operate the trust under the name A Trust I. It further states that:

1. The trustees shall hold all property of the trust in joint tenancy and shall comprise the Board of Trustees for conducting the affairs of the trust.
2. The Creator does not reserve or retain any dominion or control over the trust, or over the principal or income of the trust, nor any power to control the trust, to change certificate holders, to exercise administrative powers over the trust or its property, or to revoke, modify, terminate or change in any manner this trust instrument.
3. The Creator has no possessory interest in the trust, no reversionary interest, and no retained interest whatsoever.

Under the Contract, which is irrevocable, the Creator transferred real property,[3] personal property, and promissory notes to A Trust I in exchange for trust certificates for 75 and 25 certificate of interest units (CIUs) of an authorized 100 CIUs. The CIUs entitle the holders, the Creator's daughters, to their proportionate shares of any distributions made by the trustees.

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[1] Whether any party to a Massachusetts trust, or business trust, the creator, the trustees, and/or the certificate holders, has or has had a business is not a consideration.

[2] A provision entitled "Domicile" states:

> THIS TRUST was created and the trust instrument was executed in the State of CALIFORNIA. The construction of this trust instrument shall be determined primarily in accordance with the express terms of this instrument where the trust instrument does not speak, or the validity, construction, or administration of the trust must not be viewed by a court of law with respect to a particular state law.

The second sentence is unclear.

[3] In 1993, there was a Capitola property and the Santa Cruz property. The Capitola property was sold on January 16, 1998.

The trustees are authorized to exercise collectively the control of the trust property and affairs. One of the trustees must always be an independent trustee who is not related to the Creator by blood, marriage or employment, and the trust must always maintain an independent trustee status. The trustees exercise collectively the exclusive management and control of the trust property. Their decisions must always be unanimous.

The trustees are specifically precluded from carrying on, on behalf of the trust, any business for profit, provided that the trustees may receive on behalf of the trust, passive income, including but not limited to rents, royalties, capital gains, dividends and interest.

The trustees have no general powers but rather, have numerous specified, specific powers, such as the power to hold, manage or acquire properties, the power to lease or rent and the power to pledge to secure loans. Notwithstanding any other provision in the trust instrument, no power can be exercised, nor any action taken, by the trustees except upon the unanimous consent of all trustees having authority to exercise that power.

The trustees may accumulate for or distribute to any certificate holder such portions of the income or corpus of the trust as the trustees deem necessary for the support, care, maintenance, education, medical expense or emergencies of the certificate holder. No distribution from the trust can be made except in conformity with this external ascertainable standard, except on a prorata basis of the certificate holders.

The trustees have power to distribute principal and/or income to the certificate holders, or to make decisions or distributions of the trust estate in whole or in part, for delivery or transfer to the certificate holders of any part of any portion thereof. Each distribution, payment of income or corpus, or any other action affecting the beneficial enjoyment of the property of this trust, must be approved and exercised only by independent trustees, that is by trustees not including the Creator.

As to certificate holders and CIUs, the Contract provides that the CIUs are non-assessable, non-taxable and non-negotiable. No certificate holder may transfer any unit of interest to anyone else, without the approval of at least one other certificate holder of the trust other than the person to whom the units of interest are being transferred. Ownership of a certificate, and the units represented thereby, does not entitle the holder to any legal title in or to the trust property, nor any say or power in the management thereof.

No interest of any certificate holder is subject to or liable for attachment, execution, or other processes of law. No certificate holder has the right to encumber, hypothecate, or alienate his/her interest in this trust in any manner, without the written approval of an adverse party.

Ownership of CIUs does not entitle the holder to any legal title in or to the property, nor any undivided interest herein, nor in the management thereof, nor does the death of a certificate holder entitle his/her heirs or legal representative to demand any portion or division of the property of the trust, but said successor may succeed to the same equitable or distributable interest.

Finally, the trust may be terminated only by the unanimous approval of the Board of Trustees. Otherwise, it expires at 12:00 noon on the day before the end of the running of twenty-one years after the death of the last survivor of one of the following: the Creator, the initial

Trustees, and the children and grandchildren of said parties, which survivor must have been alive on the date of the creation of the trust.

ANALYSIS AND CONCLUSION

Article XIII, section 3(k) of the California Constitution exempts from property taxation $7,000 of the full value of a dwelling, as defined by the Legislature, when occupied by an owner as his principal residence, unless the dwelling is receiving another real property tax exemption. Revenue and Taxation Code section 218 and Property Tax Rule 135, Homeowners' Property Tax Exemption, copies enclosed, implement and discuss various aspects of the exemption.

From the inception of the homeowners' exemption, "owner" has been interpreted to mean an individual or individuals, not an entity or entities and not combinations of individuals and entities. See, for example, the March 23, 1982, Letter to Assessor No. 82/50, 1982 Homeowners' Exemption – Questions and Answers G5. through G7., copies enclosed, which state:

> G5. May a person receive the homeowners' exemption on property that is recorded in the name of a business (d.b.a.)?
>
> ANSWER: YES. He must be the sole owner of the business and there must not be a separate legal entity which owns the property. The claimant should sign a statement under penalty of perjury that clearly states that he is the sole owner of the business.
>
> G6. How does the county assessor determine from the roll whether a business is a corporation, a partnership, or a proprietorship when it is listed by d.b.a. only?
>
> ANSWER: The assessor must inquire. If the owner can prove ownership, even through title is recorded in a different name, he may be entitled to the exemption. See G7.
>
> G7. May a person receive the homeowners' exemption on property that is recorded in the name of a wholly-owned corporation?
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> ANSWER: NO. The property is owned by a separate legal entity that does not qualify for the exemption. See M6 for cooperatives.

See also Property Tax Annotation Numbers 505.0017 and 505.0063 and the respective December 29, 1980, and November 27, 2001, letters upon which each is based, copies also enclosed.

We have previously had occasion to consider contracts and declarations of trust quite similar to this Contract and have concluded that they have created legal entities for property tax purposes. See Property Tax Annotation No. 220.0398 and the April 26, 1994, memorandum upon which it is based, copies enclosed. The letter cites *Goldwater v. Oltman* (1930) 210 Cal. 408, 416 wherein the California Supreme Court stated:

> Generally stated, a trust of this nature is created wherever several person transfer the legal title in property to trustees, with complete power of management in such trustees free from the control of the creators of the trust, and the trustees in their discretion pay over the profits of the enterprise to the creators of the trust or their successors in interest. As thus defined it is apparent that such a trust is created by the act of the parties and does not depend on statutory law for its validity. In the case of *Hecht v. Malley*, 165 U. S. 144, 146 [68 L. Ed. 949, 44 Sup. Ct. Rep. 462, 463], Mr. Justice Sanford referred to such organizations as follows:
>
> The 'Massachusetts trust' is a form of business organization, common in that state, consisting essentially of an arrangement whereby property is conveyed to trustees, in accordance with the terms of an instrument of trust, to be held and managed for the benefit of such persons as may from time to time be the holders of transferable certificates issued by the trustees showing the shares into which the beneficial interest in the property is divided. These certificates, which resemble certificates for shares of stock in a corporation and are issued and transferred in like manner, entitle the holders to share ratably in the income of the property, and, upon termination of the trust, in the proceeds.
>
> "Under the Massachusetts decisions these trust instruments are held to create either pure trusts or partnerships, according to the way in which the trustees are to conduct the affairs committed to their charge. If they are the principals and are free from the control of the certificate holders in the management of the property, a trust is created; but if the certificate holders are associated together in the control of the property as principals and the trustees are merely their managing agents, a partnership relation between the certificate holders is created."

The April 26, 1994, memorandum went on to apply the Goldwater decision to the facts presented there, stating:

> The [*Goldwater*] court went on to adopt the foregoing view as California law. Thus, if the Trustee or Trustees in this case are free from the control of the TCU [Trust Certificate Units which are similar to CIUs in your trust] holders in the management of the property, a trust is created. Otherwise, a partnership is created among the TCU holders.
>
> It is clear under the contract provisions here that the Trustees and not the TCU holders have the full management control of the trust estate. The organization in this case, therefore, can properly be characterized as a "Massachusetts trust" or business trust rather than a partnership. Such trusts, however, are distinguishable from ordinary or traditional trusts. (*Koenig v. Johnson* (1945) 71 Cal.App.2d 739, 749-750; see also 88 ALR 3d §5, pp. 720-722.) Accordingly, we have taken the position that such trusts should be treated as legal entities rather than as ordinary or traditional trusts for property tax purposes. The contract in this case is consistent with that treatment in that it provides (1) that the organization is a separate legal entity having its own common law identity; (2) that the Trustees shall hold both legal and equitable title to the property of the organization; and (3) that the ownership of TCU's, which are in the nature of shares of stock, shall not entitle the holder to any legal or equitable title or any undivided interest in the property of the organization.

> Such characteristics distinguish Crescent from traditional or ordinary trusts. For example, it is a rudimentary principle of trust law that the creation of a trust divides title by placing legal title in the trustee and equitable title in the beneficiaries. (*Gonsalves v. Hodgson* (1951) 38 Cal.2d 91, 98.)
>
> Consequently, although Crescent can reasonably be characterized as a Massachusetts or business trust rather than a partnership, it should, in our view, still be treated as a legal entity rather than a traditional or ordinary trust for property tax purposes.

(See also Property Tax Annotation No. 220.0399 and the January 13, 1998, letter upon which it is based, copies also enclosed.)

Being legal entities then, Massachusetts trusts or business trusts, including A Trust I, do not qualify for the homeowners' exemption, and their properties are not eligible for the exemption. Consistent therewith, recitations in A Trust I assert that the Creator has not reserved or retained any dominion or control over the trust and/or trust property and that the Creator has no interest of any kind in the trust. To be eligible for the homeowners' exemption, an individual must have either legal and equitable title or equitable title in the property for which the exemption is sought.

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. Therefore, they are not binding on any office, or any person or public entity.

Sincerely,

/s/ J. K. McManigal, Jr.

J.K. McManigal, Jr.
Senior Tax Counsel

JKM:yg
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Enclosures [Letter To Assessors 82/50; Annotations 220.0399, 505.0017, 505.0063, and 505.0120]

cc: Honorable
County Assessor

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