



STATE OF CALIFORNIA

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Executive Director

May 18, 1993

Dear Mr. :

Re: Applicable Change in Ownership Exclusions
for Proposed Corporate Merger Transactions

Please excuse the delay in responding to your letter of January 26, 1993 to Mr. Verne Walton. Other matters requiring our attention have made such delay unavoidable.

Your letter requests advice with respect to the possible effect of certain change in ownership exclusions from property tax reassessment which may be applicable in connection with the following facts and circumstances:

Corporation A is a California domestic corporation which owns various California real property. Corporation A has two (2) classes of stock issued and outstanding, common and preferred. Each preferred share is entitled to 27.25 votes while each common share is entitled to 1 vote. As a result thereof, the holders of the preferred shares possess voting control over Corporation A, having approximately 84.2 percent of the total votes. The preferred shares of Corporation A are owned 96.3 percent by Corporation B, a California domestic corporation which also owns California real property and 3.7 percent by Individual Z. The common shares of Corporation A are owned 94.5 percent by the

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Trustees of a trust established for the children of Individuals X and Y, 3.7 percent by Individual Z and 1.8 percent by Corporation B. Corporation B only has common shares issued and outstanding which are owned 99.5 percent by Individuals X and Y and .5 percent by Individual Z. A diagram of the current stock ownership of Corporations A and B, as described above, together with each shareholder's percentage of votes in Corporation A, is attached hereto as Exhibit "A" for your convenience in review.

It is contemplated that Corporation B be merged into Corporation A, with Corporation A as the surviving corporation. In connection with the merger, Corporation A's preferred shares, Corporation A's common shares held by Corporation B, and Corporation B's common shares shall be canceled. In the merger, Individuals X and Y shall receive in exchange for their controlling interest in Corporation B, newly issued "Class B" common shares of Corporation A which will have substantially the same voting control feature as the existing preferred shares. In addition, Individual Z shall receive a small amount of newly issued Class B common stock of Corporation A in exchange for his small percentage of preferred shares in Corporation A and common shares in Corporation B. The existing common shares of Corporation A held by Individual Z and by the trust for the children of Individuals X and Y (hereinafter referred to as "Class A common shares") will remain outstanding and unaffected by the merger. Once the merger is complete, Corporation B will cease to exist and Corporation B's real property will thereafter be owned by Corporation A by operation of law. A diagram of the proposed stock ownership of Corporation A after the merger is attached hereto as Exhibit "B" for your convenience in review.

For purposes of this opinion, we assume that the stock held by Individuals X and Y is held by them equally both before and after the merger.

You have asked whether the proposed merger transaction will result in a change in ownership for property tax purposes of the real property owned by either Corporation A or Corporation B.

We will first consider whether there would be a change in ownership of the real property of Corporation B as a result of the proposed transaction.

As you know, 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 61 provides in relevant part that "[e]xcept as otherwise provided in section 62, change in ownership, as defined in section 60, includes, but is not limited to: ... (i) [t]he transfer of any interest in real property between a corporation, partnership or other legal entity and a shareholder, partner, or any other person."

Section 62 (a)(2) excludes from change in ownership "[a]ny 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 provisions of this paragraph shall not apply to transfers also excluded from change in ownership under the provisions of subdivision (b) of section 64."

Section 64(b) provides in relevant part that "[a]ny corporate reorganization, where all of the corporations involved are members of an affiliated group, and which qualifies as a reorganization under section 368 of the United States Internal Revenue Code and which is accepted as a nontaxable event by similar California statutes, or any transfer of real property among members of an affiliated group, ... shall not be a change of ownership...."

"For purposes of this subdivision 'affiliated group' means one or more chains of corporations connected through stock ownership with a common parent corporation if:

(1) One hundred percent of the voting stock, exclusive of any share owned by directors of each of the corporations, except the parent corporation, is owned by one or more of the other corporations; and

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

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(2) The common parent corporation owns, directly, 100 percent of the voting stock, exclusive of any shares owned by directors, of at least one of the other corporations."

Here, as a result of the merger transaction, Corporation B, would cease to exist and Corporation A would succeed to all of the property of Corporation B by operation of law. This would constitute a change in ownership under section 61(i) unless either section 62(a)(2) or 64(b) is applicable.

Since Corporations A and B are not affiliated corporations within the meaning of section 64(b) as set forth above, section 64(b) would not apply.

Prior to the merger, the proportional ownership interests in the real property of Corporation B as represented by the common shares of Corporation B are held 99.5 percent by Individuals X and Y and .5 percent by Individual Z.

After the merger, the proportional ownership interests in the real property transferred to Corporation A as represented by the Class A and Class B common shares of Corporation A would be held not only by Individuals X, Y and Z but also by the Trustees of the trust for the children of Individuals X and Y. Although it is not clear in what proportion these ownership interests would be held, since the trustees of the trust for the children of Individuals X and Y would hold ownership interests in the property transferred after but not before the transfer occurs, it is clear that the proportional ownership interests in the property transferred would not remain the same after the transfer. Accordingly, section 62(a)(2) would not apply. The merger would, therefore, result in a change in ownership of the real property transferred from Corporation B to Corporation A by merger.

With regard to the real property held by Corporation A prior to the proposed transaction, there would be no change in ownership under sections 60, 61 (i) because such real property would continue to be held by Corporation A after the proposed transaction occurs.

Further, except as provided in section 61(h) and sections 64(c) and (d), the purchase or transfer of corporate stock shall not be deemed to constitute a transfer of the real property of the corporation. (Section 64(a).)

Since Corporation A is not a cooperative housing corporation, section 61(h) is clearly inapplicable.

Sections 64(c) and 64(d) provide:

"(c) When a corporation, partnership, other legal entity or any other person obtains control, as defined in Section 25105, in any corporation, or obtains a majority ownership 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.

"(d) If property is transferred on or after March 1, 1975, to a legal entity in a transaction excluded from change in ownership by paragraph (2) of subdivision (a) of Section 62, then the persons holding ownership interests in such legal entity immediately after the transfer shall be considered the 'original coowners.' Whenever shares or other ownership interests representing cumulatively more than 50 percent of the total interests in the entity are transferred by any of the original coowners in one or more transactions, a change in ownership of that real property owned by the legal entity shall have occurred, and the property which was previously excluded from change in ownership under the provisions of paragraph (2) of subdivision (a) of Section 62 shall be reappraised."

Section 25105 defines ownership or control as direct or indirect ownership or control of more than 50% of the voting stock.

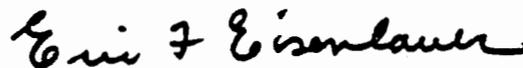
As indicated above, since Individuals X and Y will equally share voting control of Corporation A, no person or entity will obtain control of Corporation A as a result of the merger. Accordingly, no change in ownership of the real property held by Corporation A before the merger would occur under section 64(c) as a result of the merger.

Further, there is no indication here that there would be a transfer of more than 50 percent of the total shares of Corporation A by original coowners of such shares as a result of the merger. Thus, no change in ownership of the real property held by Corporation A before the merger would occur under section 64(d) as a result of the merger.

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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 conclusions stated above.

Very truly yours,



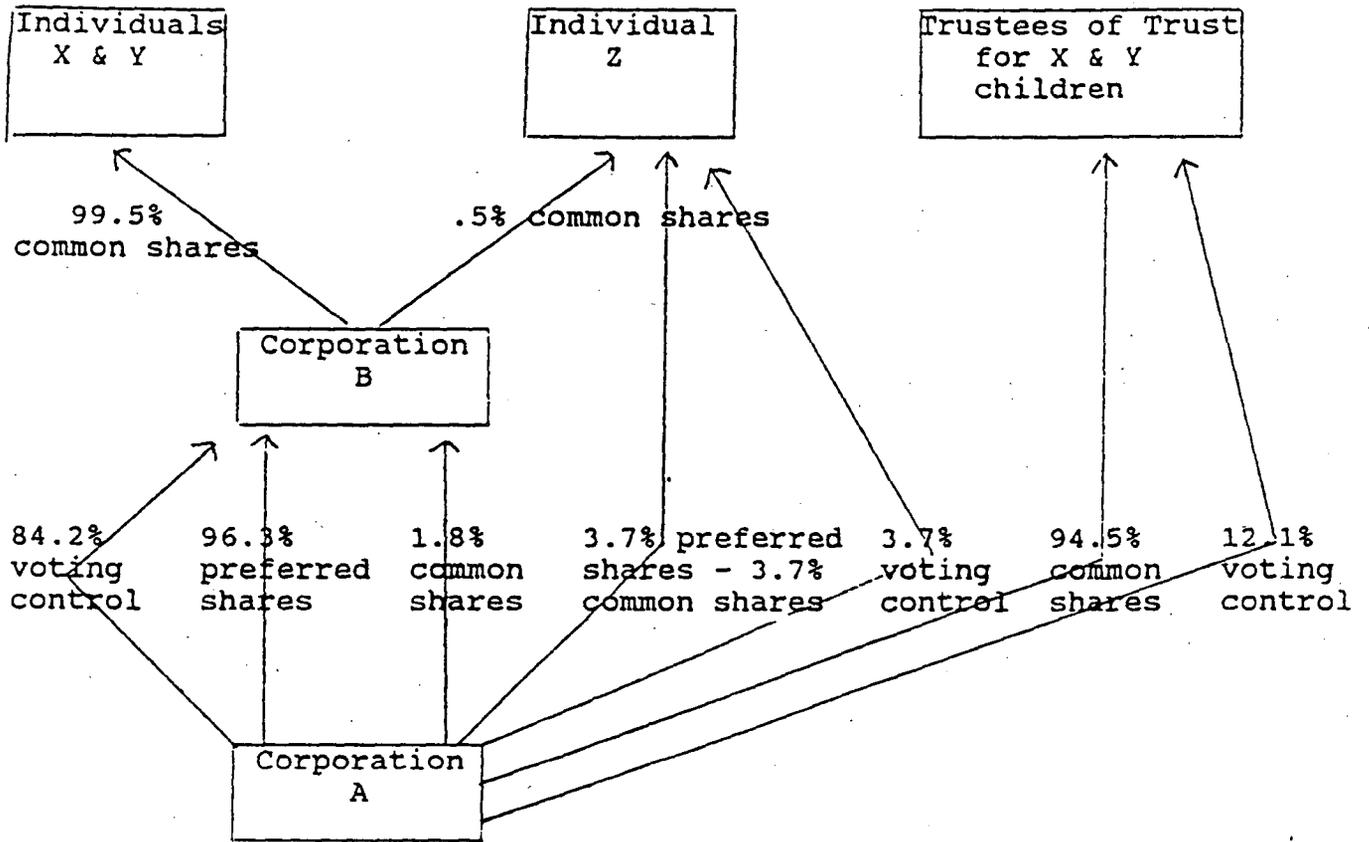
Eric F. Eisenlauer
Senior Tax Counsel

EFE:ba

cc: Mr. John Hagerty
Mr. Verne Walton

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CORPORATE STRUCTURE PRIOR TO MERGER



CORPORATE STRUCTURE AFTER MERGER

