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450 N STREET, SACRAMENTO, CALIFORNIA  
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0082  
TELEPHONE (916) 324-2655  
FAX (916) 323-3387  
[www.boe.ca.gov](http://www.boe.ca.gov)

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August 10, 2000

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Mr. James B. Lindholm, Jr.  
County Counsel  
County of San Luis Obispo  
County Government Center, Room 386  
San Luis Obispo, CA 93408

Attn: Mr. A. Edwin Olpin  
Deputy County Counsel

Dear Mr. Olpin:

This is in response to your letter to Assistant Chief Counsel Larry Augusta, requesting our opinion regarding a change in ownership question in the matter of \_\_\_\_\_, L.P. You set forth the following facts and the concerns, comments and questions of your Assessment Appeals Board, and ask whether the Assessor was correct in reassessing the subject properties for a 100% change in ownership as of the date of death of the trustor of the revocable living trust pursuant to Revenue and Taxation Code section 64(c) and/or section 64(d). For the reasons set forth below, we agree that the Assessor was correct, and that there was a 100% change in ownership under both section 64(c) and section 64(d), the change in ownership under section 64(c) taking precedence over that of section 64(d).

1. Mrs. \_\_\_\_\_ created a revocable living trust known as the Revocable Trust (hereafter "the Trust") on November 19, 1981. Subsequently, she transferred all of her 100% interest in the properties involved, known as the \_\_\_\_\_ Motel property, to the Trust. The transfer was excluded from reassessment under Revenue and Taxation Code (hereafter "R & T") section 62(d).
2. By deeds recorded on July 3, 1997, Mrs. \_\_\_\_\_ partially revoked the Trust as to a 4% interest. She then transferred 1% to her son, H \_\_\_\_\_, and 1% each to her three grandchildren. The 1% interest transferred to her son was excluded from reassessment under R & T section 63.1. The 3% interest transferred to her grandchildren (the children of H \_\_\_\_\_) was reassessed.
3. Subsequently, by deeds recorded on July 18, 1997, H \_\_\_\_\_, the three grandchildren, and the trustees of the Trust, transferred their interests in the properties to \_\_\_\_\_, L.P. These transfers were excluded from reassessment under R & T section 62(a)(2).
4. The 1% general partner of the \_\_\_\_\_ L.P. is H \_\_\_\_\_, who assumed the management of the motel properties in 1997. The limited partners are Mrs. \_\_\_\_\_'s

grandchildren, each owning a 1% limited partnership interest, and the Trust, owning a 96% limited partnership interest.

5. On July 7, 1998, Mrs. \_\_\_\_\_ died and the Trust became irrevocable. Under the terms of the Trust, her son H \_\_\_\_\_ acquired a lifetime beneficial interest in the Trust. Following his death, the Trust will be distributed outright to the three grandchildren. The Assessor reassessed the properties 100% effective on Mrs. \_\_\_\_\_'s date of death under R & T section 64(c). The owner of the properties has appealed the change in ownership.

The properties in question are owned by \_\_\_\_\_, L.P., a legal entity. Therefore, Revenue and Taxation Code section 64, which applies the general definition of "change in ownership" found in Revenue and Taxation Code section 60<sup>1</sup> specifically to transfers involving legal entities, is applicable in the situation you present. Subdivision (c) of section 64 provides, in relevant part:

(c)(1) When a . . . person obtains . . . a majority ownership interest in any partnership . . . through the purchase or transfer of . . . partnership . . . interest, . . . the purchase or transfer of that . . . interest shall be a change of ownership of the real property owned by the . . . partnership . . . in which the controlling interest is obtained.

In the facts presented, the transfer to H \_\_\_\_\_ which occurred in July 1998, upon the death of Mrs. \_\_\_\_\_, was of a life estate in the Trust which owned a 96% interest in the partnership that owns the real property. The creation, or transfer, of a life estate in real property in trust constitutes the transfer of the present beneficial ownership of the trust real property. *Leckie v. County of Orange* (1998) 65 Cal.App.4<sup>th</sup> 344. The difference here is that it was a life estate in the Trust which owned the partnership interest in the partnership that owned the real property which transferred, not a life estate in trust real property. However, the result is the same.

For property tax change in ownership purposes, the owners of the present beneficial interests of a trust which owns an interest in real property, directly or indirectly, are the beneficial owners of the interest in the property. And, the trustee of the trust, unless he also has a beneficial interest in the trust, is the holder of merely the bare legal title to trust property. Thus, a transfer of the present beneficial interest in a trust owning real property is a transfer of the property interest for change in ownership purposes. *Allen v. Sutter County Bd. of Equalization* (1983) 139 Cal.App.3<sup>rd</sup> 887; Annotation No. 220.0769, Ochsner letter dated 12/11/91 (enclosed). Similarly, a transfer of the present beneficial interest in a trust owning an interest in a partnership that owns real property is a transfer of the partnership interest for change in ownership purposes (Section 60 and Section 64) that can result in a change in ownership of the partnership real property (Section 64).

Thus, when the present beneficial interest in the Trust, in the form of a life estate, transferred to H \_\_\_\_\_, the 96% interest in the partnership owned by the Trust transferred to him as well. By virtue thereof, H \_\_\_\_\_ "obtained a majority ownership interest" in the partnership, and that transfer was a change in ownership of the property owned by the partnership, pursuant to

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<sup>1</sup> Pursuant to section 60, a "change in ownership" means 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 64(c). The argument advanced by the property owner that since the trustees of the trust owned the 96% limited partnership interest both before and after the death of Mrs. , there has been no change in the ownership of the property, is legally incorrect. As indicated above, it is the present interest in trust property, including the beneficial use thereof, that is determinative for change in ownership purposes, and it is the beneficiary or beneficiaries of a trust who hold those interests, not the trustees.

The owner has also argued, and the Assessment Appeals Board has expressed some concern, that H , with his 1% general partner interest, operates and controls the partnership property business; and the Trust, owning a 96% interest as a limited partner, has no control over nor participation in the day to day operations of the partnership. Thus, there has been no "change in control" by virtue of the transfer of the present beneficial interest in the Trust to H . This confuses "control of the partnership business" with the ultimate issue for partnership change in ownership purposes, "change in ownership" as the result of acquisition of a majority ownership interest in any partnership.<sup>2</sup>

As is noted above, section 64(c) is quite clear that a change in ownership occurs in partnership real property when a person obtains a majority ownership interest in the partnership. With respect to corporate legal entities, section 64(c) speaks of obtaining "control through direct or indirect ownership or control of more than 50 percent of the voting stock of any corporation" and "any purchase or transfer of 50 percent or less of the ownership interest through which control ... is obtained." However, in this context, "control" is used with reference to control of the units of *ownership*, the same as "majority ownership interests" for partnerships, not with reference to control over the *management* of the entity's property.<sup>3</sup> The purpose of section 64(c) is to define those circumstances in which a change in the ownership of a legal entity is deemed to be a change in ownership of the entity's real property for property tax reassessment purposes. See Property Tax Rule 462(d) (18 Cal. Code of Regs. § 462.180(d)). Therefore, the test is the degree of the change in the ownership of the legal entity owning the real property, not the control of the management of the partnership property business.

Along this same vein, there has been some confusion expressed about whether it makes a difference that the Trust owns a limited, rather than a general partnership interest, and whether a transfer of a limited partnership interest can ever constitute a change in control for purposes of section 64(c). Whether an ownership interest is a general partnership interest or a limited partnership interest is irrelevant in analyzing property tax limited partnership change in ownership situations. What is relevant is the percentage of ownership acquired or transferred. The degree of ownership is determined by the direct or indirect ownership of the interests in partnership capital and partnership profits. See Rule 462.180(d)(1)(B); Annotation 220.0387, 6/19/98 Cazadd Letter (enclosed). Here, the Trust held a 96% capital and profits interest in the partnership, and therefore 96% of the partnership's interests were transferred to H upon the creation, and transfer, of the life estate on Mrs. 's death. By that transfer, H "obtained a majority

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<sup>2</sup> Also in this regard, "control" as used in section 64(c) refers to control of voting stock of a corporation. For partnerships, as here, the test is majority ownership interest."

<sup>3</sup> Under the owner's approach, there would have been a change in "control", and presumably a reassessment, upon the 1997 formation of the limited partnership and H 's assumption of the general partnership interest and duties.

ownership interest” in the partnership, triggering a change in ownership in the partnership's real property pursuant to section 64(c), quoted above.

You note the further contention by the owner that there is a “spendthrift” clause in the Trust that prohibits his interest from being alienated or encumbered. He contends, therefore, that his Trust interest is not equivalent in value to the fee. Spendthrift clauses are not uncommon in trust instruments, and, in our opinion, do not prevent the creation of a life estate from constituting a change in ownership. Restrictions on the use of trust property are inherent in trust interests; admittedly, the holder of the interest is not receiving the actual fee title to the property. However, statutorily and in reality, it is recognized that the holder of the present beneficial interest in a trust, as the beneficial owner of the trust property and/or property of an entity owned by the trust, is the property's actual owner. We have, in the past, recognized numerous limitations on the use of the property by the life estate owner, which we concluded did not prevent treatment as a change in ownership, including termination of the life estate upon the failure of the life tenant to reside on the property; prohibition on the transfer, sale, conveyance, disposition, hypothecation or encumbrance of the property; termination on remarriage; and maintenance of the property. “Such conditions . . . do not invalidate the grant of a life estate which, as in the case of any other freehold estate, can provide for a termination upon the occurrence of a certain event such as for failure to reside on the premises. *Taylor v. McCowen* (1908) 154 Cal. 798.” (Annotation No. 220.0369, 6/30/83 Eisenlauer Letter, enclosed). Also, discretion to accumulate or distribute income (Annotation Nos. 220.0762, 625.0203), and withholding distribution until the happening of specified events, such as the death of the trustor or the reaching of a particular age by the beneficiary (Annotation Nos. 625.0204, 625.0208).

In fact, in *Leckie, supra*, 65 Cal.App.4<sup>th</sup> 334, 340, the life tenant made essentially the same argument as the owner is here, that the life estate was of “questionable value” which did “not approach that of a fee.” The Court rejected that argument and, applying the “value equivalence” test, found a change in ownership. Therefore, in our opinion, the existence of a spendthrift clause in the Trust in question would not prevent the creation of the life estate from constituting a change in ownership.

Finally, for similar reasons, the 1998 transfer initially would result in a change in ownership under section 64, subdivision (d), as well. The partnership ownership interests, including those of the Trust, were created in a transfer that was “a transaction excluded from change in ownership by paragraph (2) of subdivision (a) of Section 62.” As such, those interests would be considered held by “original coowners.” As discussed above, more than 50 percent of those ownership interests transferred from Mrs. \_\_\_\_\_ to H \_\_\_\_\_ when Mrs. \_\_\_\_\_ died in 1998. The transfer of these partnership interests met the condition of subdivision (d) that “[w]henver 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 that was previously excluded from change in ownership under the provisions of paragraph (2) of subdivision (a) of Section 62 shall be reappraised.”

However, that subdivision provides: “[a] transfer of shares or other ownership interests that results in a change in control of a corporation, partnership, limited liability company, or any other legal entity is subject to reappraisal as provided in subdivision (c) rather than this subdivision.” Therefore, given our conclusion above that the 1998 transfer caused a change in

ownership subjecting the partnership real property to reappraisal under section 64(c), this provision of section 64(d) instructs that the change in ownership results from subdivision (c) rather than under subdivision (d).

The views expressed in this letter are advisory only; 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/ Daniel G. Nauman

Daniel G. Nauman  
Senior Tax Counsel

Enclosures

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cc: Mr. Richard Johnson, MIC:63  
Mr. David Gau, MIC:64  
Mr. Charles Knudsen, MIC:62  
Ms. Jennifer Willis, MIC:70