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September 10, 2010

**Re: Application of SB 816 to Transfers of Legal Entity Interests Held in Trusts
Assignment No: 10-113**

Dear Mr. _____ :

This is in response to your May 14, 2010 email to _____, Principal Property Appraiser with the Board of Equalization's County-Assessed Properties Division (CAPD), in which you asked two questions related to the application of Senate Bill 816 (Stats. 2009, Ch. 622) (SB 816) to the interspousal exclusion and to the transfer of legal entity interests held in trust. Because Ms. _____ answered your question regarding the interspousal exclusion, this letter only addresses your second question, in which you describe a "dilemma" created by provisions in the Revenue and Taxation Code enacted by SB 816.

Facts

You provide the following in your email:

This dilemma is best described using a hypothetical: Decedent, through her trust, held control of an LLC owning California real property on her date of death and her interests in that LLC are not "original co-owners" [sic] interests. Under the terms of the her [sic] trust, the successor trustee has broad discretion to distribute trust assets among several individuals subject to the trust's share and share alike provisions. Distribution of the trust assets, however, does not occur until six months after the decedent's date of death.

On the date of distribution one beneficiary obtains control of the LLC when he receives 60 percent of the LLC's membership interests. Property Tax Rule 462.260(c) tells us that the date of the change in ownership relates back to the date of the decedent's death. Yet, no one could have known about the change in control until the actual distribution six months later.

In theory the late-filing penalty attaches if the form BOE-100-B is not filed within 45 days of the date of the change in control (which relates back to the date of death). The problem is this: How can the trust beneficiaries avoid the late-filing penalty when the change in control does not become known until more than 45 days after the date of death?

Law

As you know, Article XIII A, section 2 of the California Constitution requires the reassessment of real property upon a “change in ownership.” A change in ownership is defined in section 60 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.” Property Tax Rule¹ 462.160, subdivision (b)(2) provides that a change in ownership does not include “The transfer of real property or an ownership interest in a legal entity holding an interest in real property by the trustor to a trust which is revocable by the trustor.” It goes on to state that:

However, a change in ownership does occur at the time that a revocable trust becomes irrevocable unless the trustor-transferor remains or becomes the sole present beneficiary or unless otherwise excluded from change in ownership.

Rule 462.260, subdivision (d) provides that for change in ownership purposes, the date of reappraisal for revocable trusts is the date the trust becomes irrevocable. Typically, a revocable trust becomes irrevocable upon the trustor’s death.

Section 64, subdivision (a), provides that a transfer of ownership interests in a legal entity, such as a partnership or a limited liability company, does not constitute a transfer of the real property held by the entity, and thus does not constitute a change in ownership of the real property of the entity. Section 64, subdivision (c)(1) provides, however, that:

When a corporation, partnership, limited liability company, other legal entity, or any other person *obtains control* through direct or indirect ownership or control of more than 50 percent of the voting stock of any corporation, or obtains a majority ownership interest in any partnership, limited liability company, or other legal entity through the purchase or transfer of corporate stock, partnership, or limited liability company interest, or ownership interests in other legal entities . . . the purchase or transfer of that stock or other interest shall be a change of ownership of the real property owned by the corporation, partnership, limited liability company, or other legal entity in which the controlling interest is obtained. (Emphasis added.)

Furthermore, section 64, subdivision (d) provides:

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 that 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 that was previously excluded from change in ownership under the provisions of paragraph (2) of subdivision (a) of Section 62 shall be reappraised.

¹ All references to Property Tax Rules or Rules are to the California Code of Regulations title 18.

Effective January 1, 2010, SB 816 amended, in part, Revenue and Taxation Code² sections 480.1, 480.2, 482, and 483, relating to the requirement for legal entities to file a *Form BOE-100-B, Statement of Change in Control and Ownership of Legal Entities* (Form 100B). As you know, the amendments made by SB 816 establish a penalty for those legal entities that do not file the Form 100B with the Board's Legal Entity Ownership Program (LEOP or Board) within 45 days of a change in control or change in ownership pursuant to section 64, subdivision (c) or (d), and in the case of an incomplete filing,³ if the missing information is not provided upon a second request.⁴ The penalty attaches regardless of whether the Board determines that no change in control or change in ownership occurred. (*Ibid.*) (Prior to the amendment, an entity undergoing such a change was subject to penalty only if it did not file a Form 100B within 45 days of a request from the Board to file.) The amount of the penalty is 10 percent of the taxes applicable to the new base year value of the real property owned by the legal entity.⁵

The penalty may be abated by the county board of supervisors, as provided in section 483, subdivision (c), as follows:

If a person or legal entity establishes to the satisfaction of the county board of supervisors that the failure to file the change in ownership statement within the time required by subdivision (b) of Section 482 was *due to reasonable cause and not due to willful neglect*, and has filed the statement with the State Board of Equalization, the county board of supervisors *may* order the penalty be abated, provided the person or legal entity has filed with the county board of supervisors a written application for abatement of the penalty no later than 60 days after the date on which the person or legal entity was notified of the penalty by the assessor. (Emphasis added.)

Analysis

In your hypothetical, a trust with multiple discretionary future beneficiaries holds 100 percent of a legal entity's ownership interests, and becomes irrevocable upon the trustor's death. You posit a dilemma created by SB 816's requirement to file a Form 100B within 45 days of a change in control or change in ownership under section 64, subdivision (c) or (d) when trust assets (in this case LLC interests) are not distributed until more than 45 days after the trust become irrevocable.⁶ Your hypothetical states that there is no way to know if a change in control of the legal entity that relates back to a date of death occurs until after the Form 100B filing deadline has passed, which we assume is because the allocation of interests to each beneficiary is

² All statutory references are to the Revenue and Taxation Code unless otherwise indicated.

³ While the information to be included in the filing shall be prescribed by the Board after consultation with the California Assessors' Association, the statutes require that this information include "the parties to the transaction" and the date of the ownership control or ownership interest acquisition. (Rev. & Tax. Code, §§ 480.1, subd. (b) and 480.2, subd. (b).)

⁴ Rev. & Tax. Code § 482, subd. (b).

⁵ If the change in control or change in ownership is otherwise excluded from reassessment, then the penalty is calculated based on the current year's taxes.

⁶ To the extent that trust assets consist of interests in real property, a change in ownership statement must be filed within 150 days of the date of death or 45 days of a request to file a change in ownership statement made by the assessor. (Rev. & Tax Code, §§ 480, subs. (b) and (e).) However, a penalty for failure to timely file is only imposed if the statement is not filed within 45 days of an assessor's request to file the statement. (Rev. & Tax Code, § 482, subd. (a).)

not finally determined until distribution occurs. In such a case, if ultimately no change in control has occurred, no penalty for failure to file the Form 100B would attach. However, if a change in control has occurred, the 10 percent penalty would apply even though there was no way to know within the 45 days that there was an obligation to file.

In our opinion, your hypothetical presents a situation where the Form 100B should be filed even before all information sufficient to determine whether a change in control or change in ownership has occurred becomes known. In such situations (including, but not limited to, lengthy trust administrations or probates), we recommend filing a Form 100B containing as much information as the parties have available to them within 45 days of the date of death. Such filing will avoid the imposition of the section 482, subdivision (b) penalty as long as the Form 100B clearly indicates that the ultimate distribution of the legal entity interests is uncertain, and is promptly amended as soon as information regarding the occurrence of a change in control or change in ownership is available. We believe this is the most prudent course of action since a change in control of the limited liability company (should one occur) would relate back to the time of the trustor's death. (See Rule 462.260, subd. (c) and Annotation 220.0136.)

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, and are not binding on any person or public entity.

Sincerely,

/s/ Mary Anne B. Tooke

Mary Anne B. Tooke
Tax Counsel

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cc: Honorable Ron Thomsen
President, California Assessors' Association
Alameda County Assessor

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