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March 10, 2005

Honorable Stephen L. Vagnini  
Assessor, Monterey County  
P.O. Box 570  
Courthouse  
Salinas, CA 93902

***Re: Revenue and Taxation Code Section 63.1, Non Prorata Distribution/Sale to Child***

Dear Mr. Vagnini:

This is in response to your August 13, 2004 letter to Ms. Kristine Cazadd, wherein you request our opinion regarding the applicability of the parent-child exclusion pursuant to Revenue and Taxation Code section 63.1, to the purchase of a 75 percent interest in the property by one beneficiary of an estate from the executor in exchange for cash to three other beneficiaries in accordance with the Order (as defined herein). Based on this Order, the beneficiaries' attorney contends that 100 percent of the real property interests were distributed to the beneficiary directly from the decedent. Consequently, the attorney believes that the parent-child transfer would apply to 100 percent of the real property interests transferred. For the reasons set forth below, it is our opinion that the parent-child exclusion from change in ownership would apply to exclude the entire value of the real property because the court ordered the executor to sell three-fourths of the real property interests to one beneficiary and to distribute the proceeds of the sale to the other three beneficiaries. Since the court ordered this method of equalizing the real property shares to be distributed among the four children, the beneficiary's purchase of the property interests was from the executor and not from his siblings.

Your office provided the following documents via mail or facsimile:

1. Letter dated November 13, 2001 with a copy of a "Change in Ownership Statement – Death of Real Property Owner" from Attorney to the Assessor.
2. Copy of Claim for Reassessment Exclusion for Transfer between Parent and Child dated November 27, 2001.
3. Copy of Consent to Proposed Action and Waiver of Accounting Requirement filed on March 14, 2002 for residuary beneficiaries SGL, LGC, and FF.
4. Copy of the Order on First and Final Report of Executor on Waiver of Accounting and Petition for its Settlement; Petition for Authorization to Sell Real Property to Executor; for Confirmation of Preliminary distributions; for Allowance of Compensation to Attorney for Ordinary Services and for Final Distribution (Order) filed with the Superior Court of California, County of Monterey on March 15, 2002.

5. Copy of Grant deed recorded April 30, 2002, by AF, executor of the Estate of MDG granting to AF and AP, an undivided 50 percent interest as Tenants in Common.
6. Copy of Beneficial Ownership Statement dated January 22, 2003, signed by beneficial owner AF and non-beneficial owner AP.
7. Copy of Grant deed recorded on January 22, 2003, by AF and AP granting to AF.
8. Letter dated August 10, 2004, from Attorney to the Monterey County Assessor's Office.

On February 8, 2005, we contacted the taxpayer's former legal representative and obtained a copy of decedent's (MDG) will.

Your office has reached the conclusion that the transfer is not an equalization of the estate, but rather a purchase of a 75 percent interest in the property by one sibling from the other three siblings resulting in a change in ownership of that interest. Based on our review of the documents, including the Court Order, we respectfully disagree with that conclusion.

### **Relevant Facts**

The following facts were established from the above mentioned documents:

Decedent Marian ("mother") died on June 11, 2001. Her son, AF is the executor and one of four beneficiaries.

The will, in the Third paragraph, bequeathed all tangible personal property to decedent's children, SGL, LGC, FF, and AF, in equal portions, share and share alike. In the Fifth paragraph, the residue of the estate (comprised primarily of a residence) was to be distributed equally to the four children, SGL, LGC, FF, and AF -- one-fourth (1/4) to each child or to his or her issue by right of representation if the child predeceased MDG.

The executor's power of distribution as stated in Seventh paragraph of the will provided in pertinent part:

I authorize the Executor of my Will to sell, at either public or private sale, any property belonging to my estate . . . . .

I further authorize the Executor, on any preliminary or final distribution of the property in my estate, to partition, allot, and distribute my estate, pro rata or otherwise, in kind, including undivided interest in my estate or any part of it, or partly in cash, and partly in kind, or entirely in cash, in the Executor's absolute discretion.

Thus, based on this provision, the will clearly grants the executor the authority to sell the real property, and also grants the executor broad discretion in distributing property in kind on a pro rata or non prorata basis. Following the decedent's death, however, the Superior Court of Monterey County specified the method by which distribution of her assets would occur and to that extent modified the decedent's plan.

Regarding the actual distribution of the estate assets, including the real property, the Final Order for Distribution confirmed the appointment of AF as the executor, and in Paragraph 7, authorized the residence to be sold by the executor to AF, either alone or with a partner under the following relevant terms and conditions:

- The net selling price shall be \$240,000.
- The full purchase price of \$240,000 is to be payable to the estate.
- From the \$240,000 allocable to the estate, the sum of \$75,000 shall be distributed to the other three beneficiaries, LGC, FF, and SGL, for a total distribution of \$225,000.
- The distributions may be structured as a direct distribution from the escrow as opposed to distributing the funds first to the estate, depositing the funds in the estate account and then making the distribution.

Beneficiaries LGC, FF, and SGL each signed a “Consent to Proposed Action and Waiver of Accounting Requirement” document consenting to the sale of the property to their brother AF. Each agreed that his or her interest in the estate was fixed at \$75,000.

### **Law and Analysis**

Revenue and Taxation Code section 63.1 generally provides, in relevant part, that a transfer or transfers of a principal residence and other real property interests with a value not in excess of one million dollars between eligible transferors and eligible transferees are excluded from change in ownership if they meet all other statutory requirements. Subdivision (c)(5) defines an “eligible transferor” as a “grandparent, parent, or child of an eligible transferee.” Subdivision (c)(6) defines an “eligible transferee” as “a parent, child or grandchild of an eligible transferor.” Thus, only transfers from an eligible transferor to an eligible transferee qualify for the exclusion. Therefore, if AF’s purchase of the subject property qualifies as a transfer from the decedent pursuant to the terms of the will, then the transfer qualifies for exclusion from change in ownership under section 63.1.

The Board has addressed the applicability of section 63.1 to a transfer by will that provides for distribution on a “share and share alike” basis in Letters to Assessors (LTA) 91/08 dated January 23, 1991, enclosed herein. The key to whether a change in ownership occurs when the property is distributed according to a will on a share and share alike basis is whether the will limits the executor’s powers to distribute property.

Many wills contain provisions that grant discretion to distribute the property in kind on a pro rata or non-pro rata basis or something equivalent. The LTA cites former Probate Code section 6140, subdivision (a), renumbered as Probate Code 21102, subdivision (a), which provides that the intention of the testator as expressed in the will controls the legal effect of the dispositions made in the will. However, a clear grant of broad discretion to distribute the property in kind on a pro rata or non-pro rata basis must be given due recognition.

If the will directs a distribution of prorata shares in each and every property, then a distribution of an interest greater than the prorata share in any one property to one heir is considered a transfer of that interest from the other heir or heirs and not from the decedent. In that event, the parent-child exclusion would not apply because the property transfers prorata from the decedent to all the children, and then a partial interest transfer or transfers between the children. If an executor has the power to distribute estate property on a non prorata basis, the executor may allocate specific assets to individual beneficiaries so long as the value of their shares are equal. Thus, the transfer of an undivided interest in real property from the executor is considered a direct transfer from decedent to the beneficiary to the extent that the value of the property does not exceed the value of the beneficiary's share of the estate. See for example, Annotation No. 625.0235, Eisenlauer Letter, 9/10/96, attached.

Thus, the key to a share-and-share alike distribution to children is that no change in ownership occurs upon distribution by the executor, unless a beneficiary receives property or assets valued in excess of the value of his or her share. Regardless of the mixture of real property and assets constituting the shares ultimately distributed to each child, the value of each share is the determining factor. If one sibling receives more value than the others, the result is a transfer from the other siblings to the one with the excess value.

At issue is the sale of the residence to AF, one of four beneficiaries, and whether that "sale" was a transfer between siblings or a transfer and equal shares distribution from the executor to the beneficiaries.

According to the will (Seventh paragraph), executor, AF, has the power to sell the real property to equalize the shares among MDG's children, LGC, FF, SGL, and AF. The language of the will directs that all of the property and assets in the estate be distributed to the four children on a share-and-share alike basis (Third and Fifth paragraphs of the will). However, the Order does not execute this instruction by distributing to each child an equal one-fourth share in the total net worth of the assets. Rather, the Order required the executor to sell the real property to AF as beneficiary for an agreed upon selling price of \$240,000. The executor was then required to distribute to the remaining children LGC, FF, and SGL, \$75,000 each representing the value of their equal share in the property. Therefore, AF received the real property with a net worth of approximately \$240,000, \$15,000 of which was distributed to the estate to pay any remaining administration expenses, and LGC, SGL, and FF each received \$75,000 in cash. Thus, other than the \$15,000 for estate administration and the specific distributions required in Paragraph 13 of the Order, the distribution appears to be in equal shares between the four children, assuming that AF's one-fourth share that he did not sell to the executor was also valued at approximately \$75,000.

The question here is whether the agreement among the four children that provided that AF would receive the real property in exchange for payment of cash to the remaining beneficiaries, constitutes an agreement for a sibling-to-sibling transfer, even though it was formalized in the court's Order. We find that it does not.

Children LGC, FF, and SGL signed "Consent to Proposed Action and Waiver of Accounting Requirement" forms consenting to the following: (1) The real property (residence) would be sold to brother, AF, executor; (2) The purchase price shall be \$240,000 plus all the costs of escrow, title insurance, taxes, etc.; and, (3) By consenting to the sale of the subject property at the above-referenced price, the interest of each residuary beneficiary, other than AF,

in the estate shall be fixed at \$75,000. A review of the documents show that they were signed prior to the issuance of the Order. In addition, the Order shows each item formalized as a term and condition to the sale of the real property.

In view of the forgoing, we conclude that the sale of the real property was not a sibling-to-sibling transfer of the real property interests of LGC, SGL, and FF to AF. The consent documents signed by the other beneficiaries were essential for the issuance of the Final Order for Distribution. Since the court ordered this method of equalizing the real property shares to be distributed among the four children, the beneficiary's purchase of the property interests was from the executor and not from his siblings. Accordingly, AF's acquisition of the real property resulted in 100 percent of the property being eligible for the parent-child exclusion.

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.

Very truly yours,

*/s/ Shirley Johnson*

Shirley Johnson  
Tax Counsel

SJJ:jlh

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Enclosure: Letter to Assessors No. 91/08  
Eisenlauer Letter, 9/10/96

cc:

Mr. David Gau, MIC:63  
Mr. Dean Kinnee, MIC:64  
Ms. Mickie Stuckey, MIC:62  
Mr. Todd Gilman, MIC:70  
Ms. Glenna Shultz, MIC: 64