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July 16, 2012

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Legal Affairs Administration Division
State Board of Equalization

Ms. Sherrie Kinkle
State Board of Equalization
PO Box 942879
Sacramento, CA 94279-0064

Re: ***Proposed Change to Property Tax Rule 462.040***

Dear Ms. Kinkle:

In reference to the current project to initiate the rulemaking process to amend Property Tax Rule 462.040, I would like to provide the following input for the interested parties meeting on August 27, 2012.

First, I think we all know these joint tenancy rules are quite complex, and so if I have misunderstood any point, please feel free to correct me.

(1) Removing the mixture of joint tenancy ownership with a trust ownership. This mixing of joint tenancy ownership with trust ownership was basically a fiction rather than a legal form of ownership in the property law. I concur that removing this provision in the current Rule makes sense.

(2) Reinstate the requirement that an additional person be added as a joint tenant in order to create original transferor status. Under Rev. & Tax. Code §§65(b), 62(f) and 65.1(a), there is no reassessment of a partial interest when the "additional person" would be added upon creation of the joint tenancy where the transferors are included in the grantee joint tenants. Subsequently, the additional person can transfer his/her joint tenancy title to the remaining joint tenants also without a reassessment as long as at least one original transferor remains on title, Rev. & Tax. Code §65(d). So the requirement for an additional person can be easily circumvented. This leads to the question of what is the material result of the rule change? What public good seeking to be served?

It is also difficult to reconcile the proposed rule change with the clear statutory language. Rev. & Tax. Code §62(f) excludes from a change in ownership "The creation or transfer of a joint tenancy interest if the transferor, after the creation or transfer, is one of the joint tenants as provided in subdivision (b) of Section 65." §65(b) states:

> There shall be no change in ownership upon the creation or transfer of a joint tenancy interest if the transferor or transferors, after such creation or transfer, are among the joint tenants. Upon the creation of a joint tenancy interest described in this subdivision, the transferor or transferors shall be the "original transferor or transferors" for purposes of determining the property to be reappraised on subsequent transfers. . . ."

Both statutes clearly give room for there being grantee joint tenants in addition to the transferor(s), but neither statute requires it.

In the February 8, 2007, letter to BOE, the California Assessors' Association had stated that their ultimate goal is to have the Legislature remove the original transferor exclusion in the statute inasmuch as they believe there is no longer need for it. They believe that currently, most estate planning is done by trusts and family limited partnership, and not by joint tenancy title, and other family-beneficial exclusions are in place (such as the parent/child exclusion) and use of joint tenancies "is incompatible with the type of estate planning commonly used today (trusts)." They state, " As responsible guardians of the public good, we should not encourage people to take irresponsible risks with their property titles by trying to mix the two types." This latter mixing of joint tenancy with trusts gets to the Assessor's desired rule change regarding the mixing of trusts and joint tenancy, and perhaps confuses the present issue of requiring what used to be called a "straw man."

The Association's opinion that currently title is not being taken in joint tenancy for estate planning purposes (we would say for probate avoidance) does not fit with our experience. We find real estate agents and brokers still routinely advise buyers to take title in joint tenancy to avoid probate, and we find middle- and lower-income persons who still routinely use joint tenancy title to avoid both probate and the cost of creating a trust. When we create new family trusts, we inevitably find title held as joint tenants.

In that same February 8, 2007, letter, the only illustration of abuse which this rule change sought to correct appeared to be a situation where, in order to transfer property to children which significantly exceeded the $1 million other than residence parent/child exclusion, parent made 1% gifts to children and then all (parents and children) converted title to joint tenancy, all becoming original transferors. Thereafter, parent made gifts of his joint tenancy interest to child(ren) who, being original transferors, now receives 100% of the property without reassessment. (Example 3 on Exhibit B of February 8, 2007, letter.)

It seems to me that in such a situation, the invoking the step transaction doctrine is the Assessor's remedy.[1] Also, the Rule change would not prevent this result. When parent and children converted to joint tenancy title, they would just add someone (e.g., uncle) to title and then parents, children and uncle all would become original transferors. Subsequently uncle could transfer his title to parent and children, and the same result as that Example 3 would occur.

In studying the various Prop. 13 implementing documents in the legislative history and the materials on the website concerning this rule change proposal, the following points all appear to be true:

1. The original transferor status was designed for family joint tenancies as will substitutes, however the Task Force and Legislature deliberately made it broader to go beyond solely family joint tenancies. (The Assembly Committee October 29, 1979, report's example is not a family joint tenancy.)

2. The illustration in both the Task Force and the Assembly Report do have an additional person(s) come on title, but there is not specific language or statement of intent which would necessarily preclude one from obtaining the original transferor status if additional persons were not added to the grantee joint tenants. The requirement that the transferors all be among the transferee joint tenants is what is emphasized.

3. The legislation contains no wording requiring additional grantee joint tenants, nor precluding application if an additional person was not among the grantee joint tenants. Its terms are satisfied when the transferors are all among the grantee joint tenants.

Finally, the fact that this issue has been debated by the BOE staff, Assessors and interested parties multiple times over the years is indicative that the issue is not straightforward in the statute. In looking at these sorts of issues, I often go back to the Supreme Court in *Amador Valley Joint Union H.S. Dist. v. State Bd. of Equalization* (1978) 22 Cal.3d 208, 248, which gave us the guideline for interpretation and application of Proposition 13, "Many, perhaps most, of the uncertainties . . . may disappear if a reasonable, common sense approach is used in the interpretation of article XIII A."

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[1] Incidently, one of the Assessors' notes on Exhibit B to their February 8, 2007, letter is the difficulty in training to understand application of the doctrine and not make mistakes. Good summaries are found in the federal tax cases such as *Smith v. Comm'r*, 78 T.C. 350, 398 (1982) and more recently in the 9th Circuit, *Linton v. U.S.* (2011) 2011 WL 182314.

This common sense approach returns me back to my original question: When there is no change in ownership with adding the additional person, and no change in ownership with the additional person later transferring his/her interest to the remaining joint tenants including an original transferor, what is the gain of this exercise? What public good does this serve?

(3) Require a grantor to also be a grantee in order to accord original transferor status to the grantor's spouse. In a joint tenancy, any time one joint tenant dies and the surviving spouse is not also a surviving joint tenant, then the decedent joint tenant's interest cannot go to a spouse. Therefore, the situation anticipated by this change to the rule can only be a lifetime transfer, not in an estate.

The effect of the Rule change, therefore, would be to have the addition of an original transferor's spouse on title to become an original transferor, but would provide that a replacement of an original transferor with his/her spouse would have that spouse only be an other than original transferor. Why the difference?

The California Assessors' Association letter to BOE dated February 8, 2007, addresses a situation where the sole original transferor of a joint tenancy comes off title at the same time the spouse comes on title. They point out that this is inconsistent with Rev. & Tax. Code §65(b) which requires the transferor of an interest to be among the joint tenants. Inasmuch as §65(b) deals with the creation of a joint tenancy, this is true. But that is not what is present in the situation of an already existing joint tenancy where one original transferor transfers a joint tenancy interest to his/her spouse, and so the §65(b) creation of joint tenancy rule cannot be authority of requirement upon a later transfer of a joint tenancy interest.

On the other hand, the last sentence in §65(b) does address a transfer of a joint tenancy interest to a spouse: "The spouses of original transferors shall also be considered original transferors within the meaning of this section." Clearly in the context of §65(b) which is identifying original transferors, it applies where

Example 1. A and B as tenants in common transfer to A, B and C as joint tenants. C is spouse of A. A and B are original transferors, and C is also an original transferor being spouse of A.

It also appears to have application in the following situation:

Example 2. A and B as joint tenants and original transferors transfer to A, B and C as joint tenants, where C is spouse of A and so also becomes an original transferor.

The transfer of Example 2 serves to add the spouse to an existing joint tenancy. It has the same result as a creation of a new joint tenancy.

But consider the situation of an existing joint tenancy where the spouses are replaced:

Example 3. A and B as joint tenants and original transferors. A transfers his 50% interest to C, his spouse. No reassessment of the transfer of an original transferor's interest due to the §63 spousal exclusion; no severance of the joint tenancy as a transfer to a spouse. C is an original transferor.

C receives the original transferor status per the last sentence of §65(b). This interpretation is consistent with the spousal exclusion inasmuch as it enables C to step into the shoes of A, receiving the same interest as A held (original transferor). (That is why there is no severance of the joint tenancy to a spouse.)

The Rule change's only purpose would be in an Example 3 situation, to not allow C to step into the shoes of a and receive the same interest as A held. This would be inconsistent with the policy that transfer to a souse does not sever a joint tenancy, and inconsistence with last sentence of §65(b) providing, "The spouses of original transferors shall also be considered original transferors within the meaning of this section." The purpose of subdivision (b) is designation of original transferors, and Example 3 falls within that parameter. Were the purpose of subdivision (b) how to create a joint tenancy, then Example 3 could be deemed to not fall within that parameter because Example 3 deals with a later transfer of an existing joint tenancy interest – but this is not the purpose of subdivision (b).

If the Rule change were adopted, it could be circumvented and a spouse still obtain an original transferor status provided that the only joint tenants were original transferors. Initially the transfer which adds C (A's spouse) as a joint tenant would keep A on title by having the grantees be A, B and C, all as joint tenants, all original transferors. Thereafter, A would transfer the JT interest to B and C No reassessment results under §65(c).

So similar to the above #2 proposed change of reinstating the requirement of adding an additional person, there seems to be questions of whether the Rule change would depart from the statutory framework, and at the same time, what is the gain and what public good is served when the Rule change can be so easily circumvented?

Comments on Rule Examples.

As long as the Rule is under consideration for modification, I have wrestled with some of the examples and would like to pass along the following points for consideration.

Example 7-1. Not specifying whether B and C are also original transferors or not does lead to the speculation of whether there is a reassessment upon A's death, and makes the example a bit of a confusing read. As a second point, if the rule is not modified, then another reason D does not become an original transferor is because D did not receive his interest from A, his original transferor spouse.

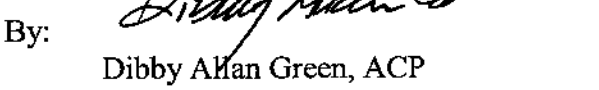
Example 8: If A and B were original transferors, then under §65(c) wouldn't there be no reassessment in a transfer to B, C and D as joint tenants? So to get a 66-2/3 reassessment I think it needs to be clear that B (at least) is an other than original joint tenant.

Example 10: It would be helpful to clarify at the beginning: "A and B as joint tenants as original transferors transfer to A, B, C and D as joint tenants. C and D are other than original transferors." The reason for this clarification is that if A and B are tenants in common (and silence presumes TIC ownership), then all of A, B, C and D would be original transferors; but the example implies that B is the only remaining original transferor.

Thank you for your and the Board's consideration of these comments. Again, this is difficult stuff, so I will be grateful for any correction if I've misunderstood something.

Sincerely,

AMBRECHT & ASSOCIATES

By: 

Dibby Allan Green, ACP
Paralegal

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