



STATE BOARD OF EQUALIZATION

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Executive Director

February 25, 2009

Re: *Change in Ownership – Transfers in Trust*
Assignment No.: 08-213

Dear Ms. :

This is in response to your letter of October 6, 2008, letter to Assistant Chief Counsel Randy Ferris, wherein you requested our opinion regarding certain transfers of property in trust. As explained below, it is our opinion that the settlors of the revocable trust are the transferors of the property.

Facts

Your clients (the "settlors") would like to create a revocable trust funded with real estate including their residence. Upon the death of the last settlor the trust will become irrevocable and the settlors' children will become the income beneficiaries. Upon the death of a child, that child's share will go to that child's issue, if any, and so on until the perpetuities period requires distribution of the trust assets.

Law and Analysis

"Change in ownership" is defined by Revenue and Taxation Code¹ 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. Section 63.1, which implements the parent-child and grandparent-grandchild exclusions, excludes from change in ownership the transfer, between parents and children, of any number of principal residences and the first \$1 million of full cash value of other real property. (Rev. & Tax. Code, § 63.1, subd. (a)(1) and (2).)

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

The grandparent-grandchild exclusion excludes from change in ownership transfers between a grandparent and grandchild if, among other requirements, all of the parents of that grandchild or those grandchildren who qualify as the children of the grandparents are deceased as of the date of the transfer. (Rev. & Tax. Code, § 63.1, subd. (a)(3).)

Subject to certain exceptions under Property Tax Rule² (Rule) 462.160, subdivision (b), the transfer of real property into an irrevocable trust, or the date that a revocable trust becomes irrevocable, is a change in ownership of the trust property. In addition, under section 61, subdivision (g), any vesting of the right to possession or enjoyment of a remainder interest that occurs upon the termination of a life estate or other similar precedent property interest, except as provided in subdivision (d) of section 62 and in section 63, is a change in ownership. Where, as here, the trustors grant to the trust beneficiaries life estates in the trust property of a trust that becomes irrevocable, changes in ownership may occur upon both the date the trust becomes irrevocable and the date the life estates terminates, unless an exclusion applies.

Under the life estate exclusion of section 62, subdivision (e), the creation of an estate for life in the transferor or the transferor's spouse does not constitute a change in ownership. If the creation of the life estate is in the children of the grantor/transferor, then the parent/child exclusion under section 63.1 may apply. Further, if the beneficiaries of the life estate (the life tenants) are the children of the transferor, and the ultimate beneficiaries are remainderpersons who qualify as the grandchildren of the transferor, then both the parent/child exclusion and the grandparent/grandchild exclusion under section 63.1 may apply. In that case, both the creation and the termination of the life estate (including the vesting in the remainderpersons) could be excluded from change in ownership.

Where a life estate terminates as a result of the death of the life tenant, the transfer to the remainderperson is from the creator of the remainder interest, not from the life tenant. This is because the statutory language in section 61, subdivision (g), section 61, subdivision (h), and section 62, subdivision (d) identifies the grantor of a life estate as the "transferor" of the remainder or reversionary interest. (See Property Tax Annotation 220.0786.)

In the instant case, the settlors, as grantors/trustors, propose to grant each child a life estate and direct that on the date of the child's death, her life estate will terminate and her percentage interest will transfer to that child's issue. When the trust becomes irrevocable, a change in ownership will occur unless a parent-child exclusion claim is timely filed. As explained above, the settlors, not the deceased child life tenant, would be the "transferors" of remainder interests to each child's issue. Since the settlors would be the transferors, the grandparent-grandchild exclusion under section 63.1 could apply to exclude from change in ownership the vesting of each remainder in a grandchild, provided that all of the parents of that grandchild that qualify as children of the settlors are deceased. However, there would be no exclusion available for any subsequent transfer to the great-grandchildren of the settlors.

As your letter acknowledges, the subject of life estates and change in ownership is before the California Supreme Court in the case of *Steinhart v. County of Los Angeles*, case number S158007. The outcome of that case may affect our analysis regarding life estates. However, until the Supreme Court issues a ruling, the Legal Department will not speculate as to any possible consequences.

² All subsequent references to "Rules" are section references to title 18 of the California Code of Regulations.

February 25, 2009

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/ Daniel Paul

Daniel Paul
Tax Counsel

DP:cme

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cc: Honorable Dan Goodwin, MAI
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