



STATE BOARD OF EQUALIZATION

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October 1, 2004

Re: Parent-child Exclusion – Effect of Disclaimer on Eligible Transferee’s Interest

Dear Mr. _____ :

This is in response to your June 29, 2004 email to Ms. Kristine Cazadd, Assistant Chief Counsel, requesting our opinion as to the applicability of the parent-child exclusion to a distribution of property from a father’s trust estate to his three children when two of the children disclaim their interests. You also ask whether the parent-child exclusion applies where two children quitclaim their interests to the third child. The final question concerns a distribution to a child who has a minor child and the application of the parent-child exclusion in the event the child files a disclaimer.

For the reasons set forth below, based on the information provided, we conclude that the parent-child exclusion would exclude all the interests if disclaimers filed by the children were legally valid and effective for purposes of renouncing their respective interests in the property. However, if there is an agreement between the beneficiary children by which a child compromised his interest bequeathed to him in the will, it may be considered a gift to the other sibling and not a disclaimed interest.

The hypothetical situations summarized below were presented in your email, along with additional information you provided during our July 20, 2004 telephone conversation. You ask whether the three situations regarding the transfers between the three children would result in a change in ownership. The hypothetical situations are restated below followed by our responses.

Law and Analysis

Relevant Law

Under California property tax law, real property must be reappraised at current fair market value when it undergoes a change in ownership. Revenue and Taxation Code¹ section 60 defines “change in ownership” to “mean 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

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

interest.” The Legislature has provided specific statutory examples in section 61 of transactions that constitute changes in ownership as defined by section 60. One such example that is relevant to the facts presented is found in subdivision (h) of section 61. A change in ownership under subdivision (h) occurs with respect to “[a]ny interests in real property which vest in persons other than the trustor . . . when a revocable trust becomes irrevocable.” See also 18 California Code of Regulations, section 462.160, subsection (b)(2), which provides that “a change in ownership does occur at the time the revocable trust becomes irrevocable unless the trustor-transferor remains or becomes the sole present beneficiary or unless otherwise excluded from change in ownership.”

Section 63.1 excludes from “change in ownership” specified purchases or transfers of real property between parents and their children for which a valid and timely claim is filed. Subdivision (h) of Section 2 of Article XIII A of the California Constitution provides, *inter alia*, that the terms “purchased” and “change in ownership” do not include the purchase or transfer of (1) principal residences between parents and children and (2) the first \$1 million of real property other than the principal residence of an “eligible transferor” to an “eligible transferee.” Section 63.1 was added to the Revenue and Taxation Code to implement the parent-child exclusion provisions described above and applies to purchases or transfers between parents and children, which occur on or after November 6, 1986, provided those transfers meet other requirements contained in statute. However, a transfer qualifying for an exclusion under section 63.1 is not made ineligible by virtue of its occurring by means of a trust. Subdivision (c)(9) of that section specifically provides that “‘Transfer’ includes, and is not limited to, any transfer of the present beneficial ownership of property from an eligible transferor to an eligible transferee through the medium of an inter vivos or testamentary trust.”

Analysis

- 1. Father, the trustor of his living trust, dies and leaves his principal residence to his three adult children in equal shares. One child wishes to buy the interests of the other two children by entering into an agreement with the other two children in which they disclaim their interests in the property in exchange for payment. Is the parent-child exclusion available to exclude the transfer of the residence to the child?**

Answer: No, unless the interests of the other two children are disclaimed or the alternative methods in Letter to Assessors No. 91/08 are followed. The agreement to disclaim would be considered a transfer from the two children to the one child. A valid disclaimer would be required by the other two children. The law permits any beneficiary to disclaim an interest, in whole or in part, in real property or personal property under a trust or will, by filing a disclaimer as provided in sections 260 through 295 of the Probate Code. Pursuant to Probate Code sections 278 and 279, to be effective, the disclaimer must be in writing, and (a) identify the creator of the interest, (b) describe the interest disclaimed, (c) state the disclaimer and the extent thereof, and (d) be filed (recorded if it involves an interest in real property) within a reasonable time after the person able to disclaim acquires knowledge of the interest.

Probate Code section 285, subdivision (b) provides that a disclaimer may not be made after the beneficiary has accepted the interest sought to be disclaimed. A beneficiary has “accepted the interest sought to be disclaimed” if he makes a voluntary conveyance or transfer of that interest, unless however, he “. . . makes a gratuitous conveyance or transfer of the beneficiary’s entire interest in property to the . . . persons who would have received the property

had the beneficiary made an otherwise qualified disclaimer. . .” Thus, a transfer or conveyance for consideration would constitute acceptance that would preclude a valid disclaimer.

In *Estate of Murphy*, (1979) 92 Cal.App. 3d 413, the court held that a disclaimer does not involve an agreement with other parties but rather implies a unilateral action which conveys no interest to other parties.” In *Estate of Murphy*, the court determined “an agreement between decedent’s former wife and his parents by which the former wife compromised her right to inherit the interest bequeathed to her in the will was an assignment and compromise, and not a disclaimer, where the parents’ acceptance of her as executrix of the estate as well as her retention of a share of the estate indicated that the former wife was bargaining.”

Based on the facts above, it appears to be an agreement between the children indicative of an assignment and compromise; thus, any disclaimer would be invalid. In order for 100% of the property to transfer from the parent to one child so that he may claim the parent-child exclusion for 100% of the interests in the property, the other two children must disclaim within a reasonable time after their interest was created upon the father’s death. However, pursuant to Probate Code section 285, if the two children accept their interests under the beneficiary they would be precluded from disclaiming. It is the responsibility of the persons disclaiming to establish to the satisfaction of the assessor that their interests were not, in fact, “accepted” and that their disclaimers are legally valid and effective for purposes of renouncing all of their interests in the residence.

2. What if instead of a disclaimer, the same children quitclaimed the property to the child who will have ongoing ownership. Would the parent/child exclusion apply under these circumstances?

Answer: No. A change in ownership results upon Father’s death at which time a 1/3 beneficial interest transfers to each child. (Section 61, subdivision (h).) However, the parent/child exclusion in section 63.1 applies to the transfer from the Father’s trust to his children upon his death, provided all requirements are met. The subsequent transfer by the two children by quitclaim deed to the one child is a change in ownership as defined in section 60, because it is a transfer between siblings and there are no exclusions for this type of transfer. Thus, a reassessment of 2/3 % interest in the property will occur. As an alternative, however, the trustee could deed 100% of the property to the one child if the trustee verifies that other assets or cash (including promissory notes) will be delivered to the other two children as the means of executing the Father’s instruction to leave equal shares to his three children. (See Letter to Assessor No. 91/08)

3. If a disclaiming child has minor children, and such a child disclaims so that the entire property interest vests in one of the children, may the child who receives the property qualify for the parent/child exclusion?

Answer: Yes. The child receiving the property must file a valid and timely claim and the minor children of the disclaiming child are not present beneficiaries of their grandfather’s trust estate. Pursuant to Probate Code section 277, if minor children are present beneficiaries under a grandfather’s (Father) trust and receive a partial interest in the property upon the grandfather’s death, they must validly disclaim their interests so that the parent becomes the sole present beneficiary and section 63.1 would exclude the transfer as a transfer between parent and child.

October 1, 2004

During our July 20, 2004 telephone conversation, you had stated that your client would probably not want to encumber the property. However, as we discussed, in the event your client may wish to do so, I have attached the legal opinions published under Annotation No. 625.0235. for your perusal as possible alternatives for application of 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
Legal Opinions – Annotation No. 625.0235

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