



STATE BOARD OF EQUALIZATION  
450 N STREET, SACRAMENTO, CALIFORNIA  
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0082  
916-324-2579 • FAX 916-323-3387  
www.boe.ca.gov

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July 25, 2006

**Re: Parent-Child Exclusion - Sale of Trust Property to Trust Beneficiary**

Dear Mr. \_\_\_\_\_ :

This is in response to your letter dated May 3, 2006, requesting our opinion as to whether the sale of real property held by an irrevocable trust to a trust beneficiary qualifies for the parent-child exclusion under Revenue and Taxation Code<sup>1</sup> section 63.1. For the reasons set forth below, we conclude that the beneficiary’s purchase of 5/6 interest in the real property does not qualify for the parent-child exclusion.

**Factual Background**

Your letter provides the following facts and information:

1. You represent Mr. Gary \_\_\_\_\_ (Gary), a beneficiary of a trust (“Trust”). Gary is the trustors’ child.
2. An asset of the Trust is the trustors’ family home located in \_\_\_\_\_, California.
3. You state that “Paragraph 6.9 of the Trust allows non-pro rata distribution” and that Exhibit B to the Trust states:

“ . . . If the property is sold [by the trustee], any of our surviving children who desire to do so, may purchase the interests of the others at fair market value.”

4. A copy of the Trust document provided to us states, in relevant part:

Unless specifically provided to the contrary in any other provisions of this Trust Declaration, the TRUSTEE is vested with, in addition to those powers now or hereafter conferred by law, the following powers . . . .

<sup>1</sup> All statutory references are to the Revenue and Taxation Code unless otherwise indicated.

6.9 Division and Distributions. In any case in which the TRUSTEE is required, pursuant to the provisions of any Trust created herein, to divide any Trust property into parts or shares for the purpose of distribution, or otherwise, to make the division and distribution (pro-rata or otherwise) in kind . . . and for this purpose to make such sales of Trust property as the TRUSTEE may deem necessary . . . .

5. We note that Paragraph 6.9 above does not restrict a non-pro rata distribution of the family home.
6. However, Exhibit B of the Trust appears to impose three conditions on the trustee's power to distribute the family home:

Upon the death of the surviving Trustor, all of the assets shall be divided equally between our surviving children, in equal shares, or to their issue per stirpes, except as provided for in the following paragraphs.

\* \* \*

- B. By unanimous consent of the surviving beneficiaries, the family home may be distributed to them as co-tenants by the terms of which they all agree. Short of unanimous consent, the family home shall be listed and sold by the Trustee. If the property is sold, any of our surviving children who desire to do so, may purchase the interests of the others at fair market value.

### Law and Analysis

#### **Does the sale of the family home to Gary, as a beneficiary, qualify for the parent-child exclusion?**

Only Gary's 1/6 interest in the family home qualifies for the parent-child exclusion. Gary's purchase of the other beneficiaries' 5/6 interest in the family home does not qualify for the parent-child exclusion.

A "change in ownership" is defined 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. (Rev. & Tax. Code, § 60.) For irrevocable trusts, the beneficiaries are considered to be the present beneficial owners of the trust property. (Property Tax Rule 462.160.)

As applicable herein, section 63.1, subdivision (a) excludes from the definition of change in ownership the transfer or purchase of principal residence between parents and their children. Letter to Assessors (LTA) No. 91/08 advises that a key in determining whether a change in ownership occurs upon a distribution of real property under the terms of a trust is whether the trust instrument limits the trustee's power to distribute property. Specifically, the LTA provides that absent a restriction in the trust instrument, the trustee has the power to distribute trust assets in kind either on a pro rata or non-pro rata basis. We have previously opined that when a trustee

has the power to distribute trust assets on a pro-rata or non-pro rata basis, the distribution of real property to one child qualifies for the parent-child exclusion if the value of the property does not exceed that child's interest in the total trust property. (LTA No. 91/08; Property Tax Annotation No. 220.0767.)

Further, California trust law recognizes that the administration of a trust is governed by the trust instrument. (*Union Bank and Trust Co. v. McColgan* (1948) 84 Cal.App.2d 208.) Thus, where the trust instrument conflicts with statutory power, the instrument controls unless a court, pursuant to Probate Code section 1620.1, relieves the trustee of the restriction in the instrument.

In this case, the trustors' revocable trust became irrevocable upon the death of the surviving trustor and the beneficiaries became the beneficial owners of the family home. In other words, Gary obtained 1/6 ownership interest in the family home upon the death of the surviving trustor. The transfer of 1/6 interest in the family home from the trustors, the parents, to Gary qualifies for the parent-child exclusion under section 63.1. As to Gary's purchase of the remaining 5/6 interest in the family home, such purchase from the other beneficiaries would not qualify 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. Therefore, they are not binding on your office or on any person or entity.

Sincerely,

/s/ Sam Chon

Sam Chon  
Tax Counsel

SYC:eb  
Prec/Trust/06/263.syc

cc: Honorable  
County Assessor

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