

WealthCounsel

CA Proposition 19: Changes to Property Tax Rules

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Proposition 19 – Overview

- In the November elections, California voters passed Proposition 19 by a 51.1% majority
- Prop. 19 (with variations) had been on prior years' ballots but did not receive enough votes
- Major selling point was that tax dollars would go towards wildfire response

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Proposition 19 – Overview

- ▶ Prop. 19 brings two major changes to the property tax rules
- ▶ (1) Restricting parent-child transfer exclusions; and
- ▶ (2) Expanding rules for homeowners age 55 and older, disabled homeowners, and natural disaster victims

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Proposition 19 – Overview

- ▶ Prop 19 was put forth by California realtors to increase sales. The virtual elimination of the parent-child exclusion and the extension of the Over 55 Base Year Transfer will likely increase sales volumes.

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Background – Proposition 13

- ▶ Prop. 13 limited annual increases in assessed value of real property to an inflation factor, not to exceed 2% per year (“Trended Base Year Value”)
- ▶ Prohibited reassessment of a new base year value except upon:
 - a) Change in ownership or
 - b) Completion of new construction

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Background – Definition of Change in Ownership

- ▶ Three Elements:
 1. Transfer of a present real property interest;
 2. Including the beneficial use thereof; and
 3. The value of the interest is substantially equal to the value of the fee.

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Background – Trusts and CIO

- ▶ 462.160(a),(c) – Transfer in and out of trust and termination of trust is a change in ownership, unless an exception applies.
See 462.160(b), (d) for exceptions.
- ▶ Always look through Trust to determine present beneficial ownership.
- ▶ In a Revocable Trust, the Trustor has present beneficial ownership interest.
- ▶ In an Irrevocable Trust, the present beneficiaries have present beneficial ownership interest.
- ▶ Trustees never have beneficial ownership interest of Trust Property.

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Parent-Child Exclusion (Current Law)

- ▶ Revenue & Taxation Code §63.1 provides that a change in ownership does not include the transfer between parents and children (in either direction) of:
 1. A Principal residence; and
 2. The first \$1 million of Trended Base Year Value of all other real property

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Parent-Child Exclusion

- ▶ “Principal residence” means a dwelling for which a homeowner’s exemption or a disabled veterans’ residence exemption has been granted in the name of the eligible transferor
- ▶ “Principal residence” includes only that portion of the land underlying the principal residence that consists of an area of reasonable size that is used as a site for the residence

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Parent-Child Exclusion

- ▶ “Child” generally means:
 1. Any child born of the parents except a child who has been adopted by another person;
 2. Any stepchild of the parents and the spouse of the stepchild;
 3. Any son-in-law or daughter-in-law of the parents until divorce or death of the child and re-marriage of the son/daughter-in-law; or
 4. Any child adopted by the parents other than a child adopted after the age of 18.

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Parent-Child Transfers

Current Law Example 1:

- ▶ Mother transfers 100% of Blackacre to child and Blackacre is the mother's principal residence
- ▶ The assessed value is \$3,500,000
- ▶ The fmv of Blackacre is \$8 million
- ▶ No reassessment

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Parent-Child Transfers

Current Law Example 2:

- ▶ Mother transfers 100% of Blackacre to child and Blackacre is not a principal residence
- ▶ The assessed value is \$350,000
- ▶ The fmv of Blackacre is \$1.2 million
- ▶ No reassessment. \$350,000 of the mother's \$1 million exclusion is used.

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Prop. 19 Parent-Child Transfers

- ▶ Effective 2/16/21, the parent-child exclusion remains in a limited fashion
 - The parent-child exclusion applies for the transfer of a parent's (or child's) principal residence to a child (or parent), who uses it as his or her principal residence (the child must file for the homeowner's exemption within one year of the transfer).
 - The exclusion is further limited to the house's base year value plus one million dollars, as adjusted annually by the State Board of Equalization.

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Prop. 19 Parent-Child Transfers

- ▶ Effective 2/16/21, the parent-child exclusion remains in a limited fashion
 - The \$1 million for non-principal residence property is eliminated.

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Prop. 19 Parent-Child Transfers

Example 1:

- ▶ Mother transfers 100% of Blackacre to child, and child uses Blackacre as its principal residence
- ▶ The assessed value is \$350,000, and the adjusted \$1 million exclusion is \$1.1 million
- ▶ The fmv of Blackacre is \$1.2 million
- ▶ No reassessment because Blackacre's fmv is less than the assessed value plus the exclusion

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Prop. 19 Parent-Child Transfers

Example 2:

- ▶ Mother transfers 100% of Blackacre to child
- ▶ The assessed value is \$350,000, and the adjusted \$1 million exclusion is \$1.1 million
- ▶ The fmv of Blackacre is \$2 million
- ▶ Reassessment results in \$900,000 valuation

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Prop. 19 Parent-Child Transfers

- ▶ There may be ways to plan around the limitations imposed on the parent-child transfer exclusion by Proposition 19 (using legal entity rules, estates for years, etc.)
- ▶ Proper documentation and timely submissions are critical to ensure application of the parent-child exclusion or to avoid a change in ownership altogether

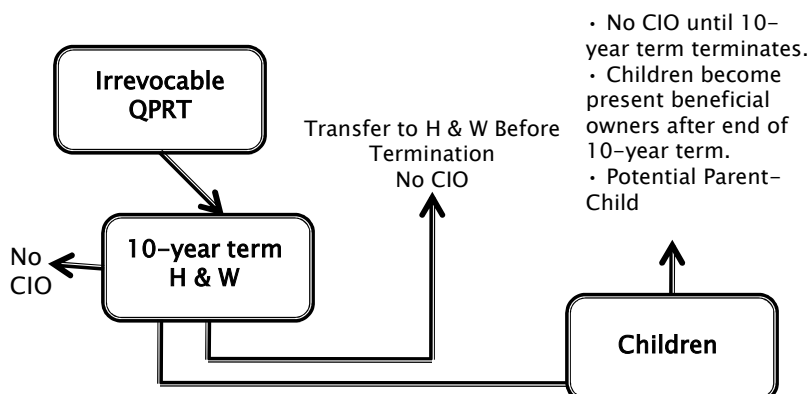
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§ 62(e) – Excluded if Transferor Reserves Estate for Life or Estate for Years

Example: Qualified Personal Residence Trust

H & W = Trustors

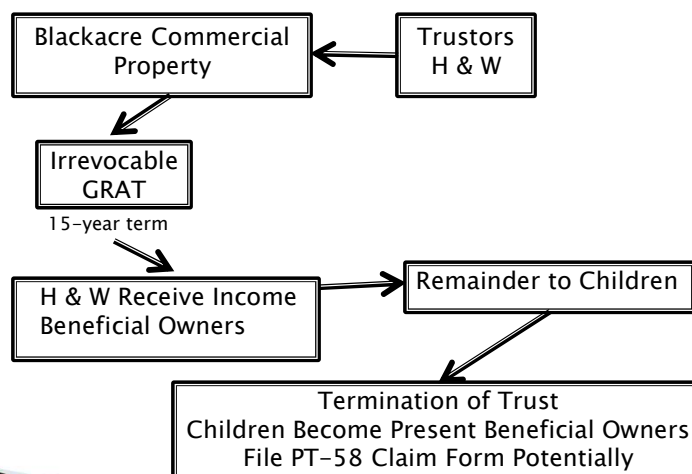


Property Tax Annotation 220.0792_s

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§ 62(e) – Excluded if Transferor Reserves Estate for Life or Estate for Years

Example: Grantor Retained Annuity Trust



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Over Age 55 Transfers (Current Law)

- ▶ Section 69.5 allows for a transfer of base year value for any person over the age of 55 who resides in property eligible for the homeowner's or veteran's exemption.
- ▶ The section 69.5 transfer can only be done once unless a person becomes severely and permanently disabled.
- ▶ The new home must be of "equal or lesser value."

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Over Age 55 Transfers

- ▶ “Equal or lesser value” means:
 1. 100% of the value of the original property if the new home is purchased or newly constructed prior to the date of sale of the original property;
 2. 105% if the new home is purchased within one year following the date of sale of the original property; or
 3. 110% of the amount of the value of the original property if the new home is purchased within the second year following the date of sale of the original property.

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Over Age 55 Transfers

- ▶ If the replacement dwelling is purchased and, in part, newly constructed, the relevant date is the latter of the purchase date or the completion of construction.
- ▶ The new home must be in the same county as the original home or a county that has reciprocity.

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Prop. 19 Special Transfers

- ▶ Effective 4/1/2021, such transfers are expanded greatly
 - Applicable to homeowners age 55 and older, disabled homeowners, and natural disaster victims
 - The transfer is permitted three times, not just once
 - The new home can be anywhere in CA so long as it is purchased or newly constructed within two years of the sale of the old home

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Prop. 19 Special Transfers

- ▶ No longer limited to new homes of “equal or lesser value”
- ▶ If the new home’s assessed value is equal to or less than the old home’s assessed value, the base year value transfers over
- ▶ If the new home’s assessed value is greater than the old home’s assessed value, the new base year value is increased by the difference in fmV

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Prop. 19 Special Transfers

- ▶ Homeowner age 56's old home has an assessed value of \$150,000.
- ▶ Homeowner sells old home for \$500,000, and purchases new home for \$400,000.
- ▶ New home's assessed value will be \$150,000.

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Prop. 19 Special Transfers

- ▶ Homeowner age 56's old home has an assessed value of \$150,000.
- ▶ Homeowner sells old home for \$500,000, and purchases new home for \$900,000.
- ▶ New home's assessed value will be \$550,000.

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Prop 19 Guidance

- ▶ Clarifying statutes, regulations, and guidance in the forms of annotations and letters to the Assessors are expected to follow and hopefully answer ambiguities and question that arise from Prop 19.

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Thank you!

Additional resources on this
topic will be added to the
WealthCounsel website soon!

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