



# Are Parent-Child Transfers Done Under Prop 19?

Ryan Lockhart  
McKenna Brink Signorotti LLP  
[ryan@mckennabrink.com](mailto:ryan@mckennabrink.com)

Marie Quashnock  
Alvis Quashnock and Associates  
[marie@aqalegal.com](mailto:marie@aqalegal.com)

# Introduction to Proposition 19

Recently passed law significantly changes California's real property tax laws:

- expands the ability of seniors, disabled persons and people affected by natural disasters to transfer their tax base to a replacement property
- limits the availability of the parent-child exclusion for purposes of real estate tax assessments.

## Outline

- Introduction to Proposition 13 (1978) and exemptions
- Summary of Proposition 19 (2020) changes
- Calculation of Base Year Value Transfers
- Planning strategies and thoughts on future of Prop 19

## Current Law: Proposition 13 (Cal. Const., Art. XIII A)

- Officially the "People's Initiative to Limit Property Taxation"
- Commonly referred to as "Prop 13"
- Amended the California Constitution
- Rolls Back Property Values to 1975 Lien Date
- Caps annual property tax increases at 2 %
- Prohibits reassessment of the base year value, except following a change in ownership or completion of new construction
- Locks in Tax Rate at 1% of Assessed Value
- Proposition 8 - Guarantees Annual Assessment at the Lower of Either: Adjusted Base Year Value or Fair Market Value as of Jan. 1



# Prior Law: Exemption for Seniors (55+) and Disabled Persons

## Rev & T C §69.5

- Under the prior law, homeowners 55 years of age or older or severely and permanently disabled persons may transfer the base year value of their present principal residence to a replacement dwelling.
- Must be of equal or lesser value; no exemption for more \$\$ property
- Transfers within county ok
- Transfers between two counties permitted if receiving county passes an ordinance (only 10 counties have ordinances)
- One-time exclusion unless person becomes disabled after receiving the exclusion based on qualifying age
- Two-year time limit between sale of “original property” and purchase of “replacement property.”

## New Law: Prop 19's Expansion of Rev & T C §69.5: Cal. Const., Art. XIII A, Section 2.1(b)

- Took effect on April 1, 2021
- Expands the class of homeowners to include victims of wildfires or other natural disasters, regardless of age or disability status.
- May now transfer their tax basis anywhere within the State
- May purchase a property of greater value; increase added to the transferred taxable value of the old home, i.e. blended tax value.
- Eligible homeowner may transfer their tax assessment up to three times now (up from one).
- Tax exemption form filed in the county where the replacement property located.

# Prior Law: California's Parent-Child Transfer Exemption

## Rev & T C § 63.1

- Parent could transfer to child without triggering a property tax reassessment: (1) California principal residence, regardless of how child uses the residence; and (2) other California real property up to \$1 million of assessed value.
- Covered transfers by gift, sale, during lifetime, at death or through trust.
- Child could use parents' residence as a vacation home or rental.
- The exemption also applied to transfer from child to parent.
- Included transfers from grandparent to grandchild where intervening child/parent has died.

# New Law: California's Parent-Child Transfer Exemption

## Rev & T C § 63.1

- Took effect on February 16, 2021
- Requires child to use parent's primary residence as their own principal residence or it will be reassessed.
- Exclusion is no longer unlimited in value; only excludes up to an additional \$1 million of value.
- \$1 million additional California property prong under current law is eliminated entirely.
- If the child chooses to keep parent's residence as a second home, vacation home or rental, residence will be reassessed to fair market value at the time of the transfer.



# Board of Equalization Interpretational Questions and Answers

## Published January 8, 2021

- Must both the sale of the primary residence and the purchase of a replacement primary residence be completed on or after April 1, 2021? Answer: No
- Must a claimant be “severely disabled” or “severely and permanently disabled” under Prop 19? Answer: No
- On what date is the value of the original and replacement primary residences determined for purposes of calculating the transferrable taxable value? Answer: as of date of sale or purchase or date of completion of new construction.
- How many times may spouses transfer an original primary residence pursuant to Prop 19? Answer: Each spouse up to 3 times.
- Since February 15, 2021 was a state holiday, are purchases or transfers that occur on February 16, 2021 eligible for the previous parent-child exclusion? Answer: yes except for transfers of property by inheritance.
- Prop 19 requires that a family home continue as the family home of the transferee. Must the family home continue as the family home of all transferees? Answer: No, only one needs to maintain the family home as their residence.



# Board of Equalization Interpretational Questions and Answers

## Continued

- By what date must a transferee establish the family home as her family home? Answer: One year of purchase or transfer
- How long must a transferee maintain the property as her family home for continued exclusion? Answer: The exclusion applies only as long as the transferee or another transferee maintains the property as his or her family home
- Prop 19 makes the parent-child exclusion applicable to family farms. What familial relationship will establish a farm as a “family farm”? Answer: farm that is transferred between parents and children or when applicable, between grandparents and grandchildren.
- Must a family farm also be the principal residence of the transferee? Answer: No.
- What is the proper forum for appeal for a transferee denied the homeowner’s exemption? Answer: County where property is located and if denied, appeal to Superior Court.

# Calculation of Base Year Value Transfers of Primary Residence (Example 1)

- Transfer of primary residence base year value:
  - The factored base year value of Owner's original primary residence is \$300,000. Owner sells their original primary residence for \$550,000. Owner purchases a replacement primary residence for \$500,000. Since the full cash value of Owner's replacement primary residence (\$500,000) is less than the full cash value of the original primary residence (\$550,000), the new base year value of the replacement primary residence is \$300,000.

# Calculation of Base Year Value Transfers of Primary Residence ( Example 2)

- What if the replacement residence costs more?
  - The factored base year value of Owner's original primary residence is \$300,000. Owner sells their original primary residence for \$550,000. Owner purchases a replacement primary residence for \$600,000. Since the full cash value of Owner's replacement primary residence (\$600,000) is greater than the full cash value of the original primary residence (\$550,000), the new base year value of the replacement primary residence is \$350,000 (\$300,000 factored base year value of original primary residence plus \$50,000, which is the difference between the full cash value of the replacement primary residence (\$600,000) and the full cash value of the original primary residence (\$550,000).

# What About Parent-Child Transfers?

- **How Are These Calculated?**
  - Exemption is limited to base year value of parents' primary residence or farm PLUS \$1 million.
  - Example: Parents' FBV is \$250,000. Excluded amount is \$1,250,000 (\$1,000,000 plus \$250,000).



# Parent-Child Examples

- From Letter to Assessors 2021/008
- **Question: I moved back into the house I grew up in to live with my aging mother who needs care. She wants to give the house to me on my next birthday, which is May 1, 2021. The current taxable value of the house on which my mother pays property tax is \$200,000. When she transfers the house to me, will the taxable value on which I have to pay property tax change?**
- Answer: It depends. If the fair market value of the house on May 1, 2021, is less than or equal to \$1,200,000 (\$200,000 taxable value + \$1,000,000), your taxable value will not change. If the fair market value of the house on that date is an amount greater than \$1,200,000, your new taxable value will be \$200,000 plus that excess amount above \$1,200,000. For example, if the fair market value of the house on May 1, 2021, is \$1,500,000, your new taxable value will be \$500,000 (\$200,000 taxable value + \$300,000 excess amount).

# Parent-Child Examples

- **What about transfers of partial interests?**
  - Mother transfers 25% of home to child. If the taxable value of the mother's family home is \$600,000 and its fair market value is \$800,000 when 25 percent is transferred to the child, the fair market value (\$800,000) is less than the excluded amount of \$1,600,000 ( $\$600,000 + \$1,000,000$ ). Thus, the taxable value of your 25 percent interest is not increased and remains at \$150,000 ( $\$600,000 \times 25\%$ ).
  - However, if the fair market value of the family home is \$2,000,000 when 25 percent is transferred to you, the fair market value (\$2,000,000) is greater than the excluded amount (\$1,600,000) by \$400,000. Therefore, 25 percent of \$400,000, or \$100,000, will be added to the taxable value of your 25 percent interest (\$150,000) to arrive at a new taxable value of \$250,000 for your 25 percent interest, which results in a new taxable value for the entire family home of \$700,000 (your 25 percent interest of \$250,000 + your mother's remaining 75 percent interest of \$450,000).

# What Can We Do to Mitigate Prop 19 Impact on Parent-Child Transfers?

- Use legal entities to move at least a portion of the property.
- Do nothing??

# Using Legal Entities

- Limited Liability Companies (LLCs) are the most common
- Different property tax rules apply to entities\*
  - Change in Control: no member/shareholder/partner gains a more than 50% interest
  - Change in Ownership: No more than 50% of entity interests have transferred
- Avoids the severe restrictions of Prop 19
- The rules are very technical. Ensure you understand them before embarking on transfers.



\*Revenue and Taxation Code sections 61 and 64. See also Legal Entity Ownership Program at Board of Equalization.



# Legal Entities (Cont.)

- Transfer up to 50% of legal entity without triggering reassessment
  - Family forms family LLC for property. Parents are initial members and then gift up to 50% of the LLC interests to children.
  - Family may choose to dissolve the LLC after the gift. Family may choose to form new LLC and gift another 50% of parents' interest.
  - Beware the Step-Transaction Doctrine. Risk tolerance of utmost importance when considering the multi-step approach.

# Do Nothing!

- No guarantee that the portion of Prop 19 that applies to parent-child transfers will stay.
- Already a movement underway to get a modification to parent-child transfers on the next electoral ballot.
- Waiting for change may not be feasible if estate/gift tax changes impact the client's planning objectives.



# Thank You!

-Marie Quashnock & Ryan Lockhart