

## NEW CALIFORNIA REAL PROPERTY TAX LAW EFFECTIVE JANUARY 1, 2010: CHANGES TO PENALTY FOR FAILURE TO REPORT CHANGES OF OWNERSHIP IN ENTITIES

Owners of real property should take note of a new California property tax law that is effective on January 1, 2010. Senate Bill 816, signed into law by Governor Schwarzenegger on October 11, 2009, establishes a stricter penalty when a legal entity does not report a change in control or a change in ownership to the State Board of Equalization within 45 days of the event.

There are three common classes of events that may cause California real property to be reassessed: *first*, new construction; *second*, transfers of real property or of interests in real property (collectively, "real property"); and *third*, transfers of interests in entities that own real property such as corporations, partnerships and limited liability companies (collectively, "legal entities"). The new law relates only to transfers of interests in legal entities.

Transfers of interests in a legal entity will cause a reassessment of the California real property owned by the entity in two circumstances: *first*, if some person or entity that previously did not have *control* ends up with *control*; *second*, in certain situations when there has been a cumulative transfer of more than 50% of the interests in the entity, even if no person or entity ends up with *control*. "Control" here means a greater than 50% interest in the entity. The law ignores certain transfers where the ownership of the transferor and the transferee is identical as well as certain other transfers that are not discussed here.

Under pre-2010 law, where a legal entity owns California real property and a person or entity acquires control of the property-owning entity (the first rule above), or there is a transfer of control in the property-owning legal entity (the second rule above) then the acquiring person or entity or the transferring legal entity was required to file a change in ownership statement within 45 days of the event. However, there was no penalty if the required filing was not made. Rather, a penalty could apply only if the State Board of Equalization contacted the entity in writing and then only if the entity still failed to file the statement within 60 days. Even if the 60-day filing window was missed, the legal entity could still apply to the State Board of Equalization to have the penalty abated.

The new law imposes the penalty if the entity or person required to file does not report the change of ownership within 45 days from the *earlier* of the date of the change of ownership or the date of a written request by the State Board of Equalization to report the transfer. In other words, the taxpayer can no longer just wait to be prompted by the authorities. Further, the penalty is no longer automatically extinguished if a change of ownership statement is filed within 60 days of being notified of the penalty. Nonetheless, the assessee may still apply to the relevant county board of supervisors (as opposed to the State Board of Equalization) to have the penalty abated.

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The law does not change the rules for reporting changes in ownership that are related to the transfer of real property or transfers involving trusts owning real property. For these transfers, the penalty applies only if the assessor has made a *written request* for the change of ownership statement and the property owner has failed to file the statement within 45 days of the request.

The amount of the assessable penalty can be substantial. Under the new law, a failure to file a change in ownership statement can result in an assessable penalty of ten percent of the taxes applicable to the legal entity's real property.

The rules relating to changes of ownership can be subtle; slight structural variations can sometimes yield vastly different results. Before-the-fact transaction planning is often critical in minimizing after-the-fact transaction property tax increases.

*For more information, such as to determine if you are required to report a transfer of interests in an entity or to discuss structuring options for transfers of ownership interests, please contact:*

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