

SUPREME COURT COPY

CASE NO.: S222329

IN THE SUPREME COURT OF CALIFORNIA

926 NORTH ARDMORE AVENUE, LLC,
Plaintiff and Appellant,

SUPREME COURT
FILED

v.

NOV - 9 2015

COUNTY OF LOS ANGELES,

Frank A. McGuire Clerk

Defendant and Respondent.

Deputy

After a Decision of the Court of Appeal,
Second Appellate District, Division Seven,
on Appeal from the
Superior Court for the County of Los Angeles,
The Honorable Rita Miller, Judge Presiding
Trial Court Case No. BC 476670
Court of Appeal Case No. B248356

CONSOLIDATED ANSWER TO AMICUS CURIAE BRIEFS SUPPORTING APPELLANT

MARY C. WICKHAM, Interim County Counsel
*ALBERT RAMSEYER, Principal Deputy County Counsel
State Bar No. 131570
648 Kenneth Hahn Hall of Administration
500 West Temple Street
Los Angeles, California 90012-2713
Tel: (213) 974-0809
Fax: (213) 617-7182

aramseyer@counsel.lacounty.gov

Attorneys for Defendant and Respondent

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I.

INTRODUCTION

Respondent County of Los Angeles files this combined answer to the six amicus briefs filed in support of Appellant.¹ Although numerous, the briefs do not substantially advance the analysis of the matter before the Court. The issues raised in the briefs center generally on one or more of three topics, all of which have already been covered in the parties' briefs : 1) the scope of the term "realty sold"; 2) the supposed anomalies of Rev. & Tax. § 11925; and 3) the contention that it is unconstitutional to assess a documentary transfer tax where realty is sold by means of a transfer of interests in a legal entity.

II.

THE AMICI'S POSITION REGARDING "REALTY SOLD" ACTUALLY ADVANCES RESPONDENT'S POSITION

Several amici curiae including the California Taxpayer Association ("CalTax"), the California Society of Certified Public Accountants ("CalCPA"), and the California Association of Realtors ("CAR") argue that the California Documentary Transfer Tax ("DTT") is in the nature of a

¹ Briefs were filed by each of the following: California Taxpayers' Association, California Association of Realtors, California Society of CPAs, Council on State Taxation, Institute of Professionals in Taxation, and California Alliance of Taxpayer Advocates.

recording tax. This position is contrary to informed opinion on the subject which finds that the DTT is due upon the delivery of a writing that transfers a real property interest. The assessment is made upon the privilege of transferring rights in realty, not the recordation of a writing. (See, e.g., Cruz, *2015 Update: Transfer Taxes in California*, California Real Property Journal, vol. 33, no. 3, 2015, 5, 10, fn. 66, citing to *Berry v. Kavanagh* (6th Cir. 1943) 137 F.2d 574; *Fielder v. City of Los Angeles* (1993) 14 Cal.App.4th 137, 145.)

CalTax argues that a prior federal treasury regulation is the basis for the understanding that the incidence of the DTT is upon the delivery of a writing transferring a real property interest. This point, though, is mistaken. As noted above, and discussed in both the parties' briefs and the brief of amici curiae County of Tehama, et al., the federal tax was never limited to *recorded* documents. ". . . Because section 11911 was patterned after the former federal act and employs virtually identical language as the act, we must infer that the Legislature intended to perpetuate the federal administrative interpretations of that act. . . ." (*Thrifty Corp. v. County of Los Angeles* (1989) 210 Cal.App.3d 881, 884, citing *Estate of Morse* (1970) 9 Cal.App.3d 411, 415.)

The CalCPA argues that the incident of the DTT is upon recorded documents, and that its interpretation of the levy as a recording tax (a point

also shared by CalTax) is compelled because otherwise the measure lacks a collection mechanism. To the contrary, Local agencies have numerous collection tools (including California's robust system of courts). Other taxing schemes leave it to local agencies to create a collection structure without difficulty (e.g., business license taxes, Rev. & Tax. Code § 7284; transient occupancy taxes, Rev. & Tax. Code §§ 7283; 7283.51).

The CAR brief argues that the character of real property transfers has recently changed and that the use of "holding vehicles" have become much more prevalent in real estate transactions. This point supports the Respondent's position. The contral point made by the Court of Appeal is that such "holding vehicle" transactions are merely new *forms* for accomplishing *the same basic real property sales transactions*, which are within the ambit and intention of the DTT Act. As CAR acknowledges, holding vehicles are in fact routinely used to accomplish the transfer of real property ownership by means of a writing. A DTT is properly owed in such circumstances involving a sale. Neither CAR nor any of the other amici supporting Petitioner have provided any persuasive reason why these mere formal changes, not affecting the substance of the transactions, should affect the application of the DTT.

III.

THE COURT OF APPEALS' DETERMINATION THAT THE DTT APPLIES TO REALTY TRANSFERRED BY MEANS OF MEMBERSHIP INTERESTS IN LEGAL ENTITIES IS CONSISTENT WITH THE SCOPE OF THE DTT ACT, THE INTENT OF THE LEGISLATURE, AND SOUND PUBLIC POLICY

The Institute of Professionals in Taxation ("IPT") contends that certain anomalies result were the Court of Appeal's decision upheld that a DTT is due upon a property tax change in ownership of a legal entity that holds real property. The flaw with this reasoning is that much greater anomalies would result were the DTT not applied to such transfers. In order to avoid minor quirks (of the sort endemic in tax practice) arising under obscure and unlikely hypotheticals, IPT would create a scheme under which the application of DTT was dependent not upon the substance of the transaction, but *solely* upon the owner's choice of holding vehicles. As anomalies go, IPT would create a mountain to avoid a molehill.²

² Even under IPT's construction, such "quirks" are unavoidable. For example, under Revenue and Taxation Code section 11925, subdivision (b), the technical termination of an LLC that has elected to be treated as a partnership for federal income tax purposes will result in DTT liability for LLC property. However, under IPT's proposed scheme, the identical transaction would result in no DTT liability if the same LLC, owning the same property, had elected to be treated as a corporation for federal income tax purposes. The suggestion that the application of DTT should be solely dependent upon the entity's choice of treatment for *income tax* purposes, divorced from any connection to the actual substance of the transaction, is a

The entire point of the Legislature's enactment of change in ownership statutes is to discern between mere paper transactions and true changes in ownership. (*Sav-On Drugs v. County of Orange* (1987) 190 Cal.App.3d 1611, 1618.) Amicus IPT identifies curiosities in the property tax law, but offers no policy justification for exempting from the DTT the transfer of real property undertaken by means of holding vehicles. The Legislature, on the other hand, has suggested through its amendments, Statutes of 2009, ch. 622 [SB 816], and Statutes of 2011, ch. 320 [AB 563], its intent for a comprehensive application of the DTT to all real property transfers, including both conventional transactions and those by means of a transfer of ownership interests in legal entities.

The Court of Appeal's affirmation that an administrator of the DTT may rely upon a change in ownership determination of an assessor to identify an assessable transaction is consistent with recent legislative direction in this area and makes sound policy sense. A touchstone of a property tax change in ownership event is the present transfer of a beneficial interest in real property that is substantially equivalent to a fee interest. (Rev. & Tax. Code § 60.) The same standard may reasonably be applied to evaluate whether a transfer of membership interests in a legal

(...continued)

substantially greater incongruity than any of the hypotheticals advanced by IPT.

entity constitutes a transfer of ownership of realty for purposes of the DTT. Whatever inconsistencies exist between the administration of the DTT and the property tax law, they are of the sort that exist in any tax scheme, and can be easily addressed in subsequent administrative and judicial review. To not address realty sold through holding vehicles when it is undisputed that this has become increasingly a significant method of effecting real property transfers, undercuts the rationale, efficacy, and legitimacy of the DTT, and neglects the role of the Legislature and others to adapt the broad principles of the DTT Act to the evolving realities of the marketplace.

IV.

THE NEWLY ADVANCED ARGUMENTS THAT RESPONDENT'S INTERPRETATION OF THE DTT ACT IS UNCONSTITUTIONAL ASSUMES THE CONCLUSION THAT A TRANSFER OF INTERESTS IN A LEGAL ENTITY IS AN IMPERMISSIBLE EXTENSION OF THE DTT ACT.

The California Association of Tax Advocates ("CATA"), the Council on State Taxation ("COST"), and CalTax make the claim that the imposition of the DTT upon transfers of real property by means of legal entity membership interests is an unconstitutional expansion of the tax. This point was abandoned by Appellant in the trial court and should not be reached for the first time in this forum. Even if it were to be reached, the point would not be meritorious.

Amici's argument that it is unconstitutional to levy the DTT upon the transfer of legal entity membership interests, proceeds upon the premise that the tax administrator is *burdening an incident of real property ownership*. By raising this argument, these amici implicitly accept Respondent's central point that a transaction involving a holding vehicle *actually represents a transfer of real property*. As such, Appellant's transaction was properly encompassed by Rev. & Tax. Code § 11911, and a tax was owing.

With regard to the arguments premised on Propositions 218 and 26, the central question before the Court is whether the statutory term "realty sold" encompasses indirect transfers of real property. If so, there is no "extension" of the tax, and therefore no constitutional concern; if not, then the imposition of the tax would fail on statutory grounds, and there is likewise no constitutional concern. In short, this issue is a chimera, and is not truly present in this case.

The DTT Act, which includes Rev. & Tax. § 11925, contemplates the levy of a DTT upon an indirect change in ownership of realty. The type of transaction that is before the Court was properly subject to a DTT assessment since the advent of the California DTT Act, but was not the active subject of collection until after becoming a more prevalent method of sale. The recent increase in the use of holding vehicles, and the

Legislature's guidance in allowing such transactions to be more readily identified, provides for more effective and equitable administration of the tax. The challenged assessment is not unconstitutional, but rather is entirely within the ambit and consistent with the spirit of the 1967 DTT Act and the Legislature's recent work in this area.

V.

CONCLUSION

The claim is made that the Court of Appeal in *Ardmore*, undercuts settled expectations and reliance of property owners who understood the DTT to be a recording tax. This understanding, however, has not been shared by practitioners in this area. (See, e.g., Cruz and Rogers, *A Practical Guide to Transfer Taxes in California*, California Real Property Journal, Spring 2005, Vol. 23, No. 2, p. 14, ["The scope of the Transfer Tax Act is extremely broad. . . ¶ Contrary to popular misconception, transfer tax is due and payable on transfers irrespective of whether the transfer instrument is submitted for recording in the county real estate records. . . ."]). To the extent that DTT was owed on prior untaxed transactions and was unpaid, a tax administrator's ability to issue escape assessments would be limited by a statute of limitations.

The role of the tax administrator is to ultimately abide by the requirements of law. The expectations and reliance of property owners

cannot trump the Legislature's clear indications with its two recent bills (and the very public efforts of many counties - ranging from urban Los Angeles to rural Mono - to implement these provisions and collect DTT.) Misplaced understandings of the law do not warrant ignoring the Legislature's actual intentions.

The County's interpretation of the DTT Act is consistent with the scope of the Act as originally enacted, and as clarified by the Legislature's most recent work in this area. The transfer of real property through a "special purpose entity" or by means of a holding vehicle – such as the transaction before the Court – is a transfer of realty by a writing for consideration. It is properly subject to DTT assessment.

We urge that the judgment of the Court of Appeal be affirmed.

DATED: November 6, 2015 Respectfully submitted,

MARY C. WICKHAM
Interim County Counsel

By Albert Ramseyer
ALBERT RAMSEYER
Principal Deputy County Counsel

Attorneys for Respondents and Appellees

CERTIFICATE OF WORD COUNT PURSUANT TO RULE 8.360

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DATED: November 6, 2015 Respectfully submitted,

JOHN F. KRATTLI
County Counsel

By 
ALBERT RAMSEYER
Principal Deputy County Counsel

Attorneys for Defendants and
Respondents.

DECLARATION OF SERVICE

STATE OF CALIFORNIA, County of Los Angeles:

Baron Kishimoto states: I am and at all times herein mentioned have been a citizen of the United States and a resident of the County of Los Angeles, over the age of eighteen years and not a party to nor interested in the within action; that my business address is 648 Kenneth Hahn Hall of Administration, 500 West Temple Street, County of Los Angeles, State of California; that I am readily familiar with the business practice of the Los Angeles County Counsel for collection and processing of correspondence for mailing with the United States Postal Service; and that the correspondence would be deposited within the United States Postal Service that same day in the ordinary course of business.

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**CONSOLIDATED ANSWER TO AMICUS CURIAE BRIEFS
SUPPORTING APPELLANT**

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Baron Kishimoto

Service List

926 N. Ardmore v. County
S222329

Clerk of the Court
Court of Appeal,
Second Appellate District, Div. 7
300 S. Spring Street, 2nd Flr.
North Tower
Los Angeles, CA 90013

Hon. Rita Miller
Los Angeles Superior Court
Dept. 16
111 North Hill Street
Los Angeles, CA 90012

Lemoine Skinner III
Fisher Broyles LLP
1334 8th Avenue
San Francisco, CA 94122

Daniel M. Kolkey
Julian W. Poon
Lauren M. Blas
Gibson Dunn & Crutcher
555 Mission Street, Ste. 3000
San Francisco, CA 94105-2933

Arthur J. Wylene
County Counsel
County of Tehama
727 Oak Street
Red Bluff, CA 96080

C. Stephen Davis
Cris K. O'Neill
Andrew W. Bodeau
Greenberg Traurig, LLP
3161 Michelson Drive, Ste. 1000
Irvine, CA 92612

Richard J. Ayoob
Christopher J. Matarese
Gregory R. Broege
Ajalat, Polley, Ayoob & Matarese
500 N. Brand Blvd., Suite 1870
Glendale, CA 91203

June Babiracki Barlow
Neil Kalin
Jenny Li
California Association of Realtors
525 South Virgil Avenue
Los Angeles, CA 90020

Stephen G. Larson
Steven A. Haskins
Arent Fox LLP
555 West Fifth Street, 48th Floor
Los Angeles, California 90013

Kevin M. Fong
Jeffrey M. Vesely
Kerne H.O. Matsubara
Pillsbury Winthrop Shaw Pittman LLP
Four Embarcadero Center, 22nd Floor
San Francisco, CA 94111

Peter Michaels
Law Office of Peter Michaels
6114 La Salle Avenue, #445
Oakland, CA 94611