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CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION ONE

RICK AUERBACH, as Assessor, etc., Plaintiff and Appellant, v. ASSESSMENT APPEALS BOARD NO. 1 FOR THE COUNTY OF LOS ANGELES, Defendant and Respondent; NORTHERN TRUST BANK OF CALIFORNIA, as Trustee, etc., Real Party in Interest and Respondent.	B173649 (Los Angeles County Super. Ct. No. BS084737)

APPEAL from a judgment of the Superior Court of Los Angeles County. Joanne B. O'Donnell, Judge. Reversed with directions.

Raymond G. Fortner, Jr., County Counsel, Albert Ramseyer, Principal Deputy County Counsel, for Plaintiff and Appellant.

No appearance for Defendant and Respondent.

Rodi, Pollock, Pettker, Galbraith & Cahill, Cris K. O'Neall and Wade E. Norwood for Real Party in Interest and Respondent.

Rick Auerbach, the Los Angeles County Assessor (Assessor), appeals from a judgment denying his petition for a writ of mandate seeking to reverse the decision of Los Angeles County Assessment Appeals Board No. 1 (Board) reassessing commercial real property subject to a 20-year lease (Property) and applying the $1 million grandparent-grandchild exclusion from assessment under Revenue and Taxation Code section 63.1.

Both the Board and the trial court determined that the lessee was the "owner" of the improvements which it had constructed on the Property and that a grandparent-to-grandchild transfer of the lessors' interest in the Property transferred only the land and not the improvements and thus concluded that the Assessor erred in including the improvements in the calculation of the exclusion. We disagree and reverse the judgment because, notwithstanding the lessee's construction of the improvements, both the land and the improvements are subject to, and included in the calculation of, the grandparent-to-grandchild exclusion.

BACKGROUND

Real party in interest Northern Bank of California (Trustee) is the cotrustee of two trusts which together hold a 50 percent interest in the Property, located on North Rodeo Drive in Beverly Hills. In 1999, the Property was valued at about $21 million, with the land valued at about $9.5 million and the improvements, a two-story retail building, valued at about $11.5 million. Robert and Electra Anderson, the grandchildren of Stanley and Marguerite Anderson, are each a beneficiary of one of the two trusts.

In February 1996, the two trusts, with two other trusts not involved in this action, entered into a lease agreement (Lease) by which the trusts leased the Property to Tommy Hilfiger Retail, Inc. (Hilfiger) for an initial term of ten years, with two five-year options to extend the Lease. In 1996, the Property was improved with a 14,400-square-foot retail building, which was occupied by another tenant.

The Lease provisions required Hilfiger either to renovate the existing building with a minimum expenditure of $2 million or to demolish it and build a new one with a minimum expenditure of $4 million. Hilfiger took possession under the Lease and elected to demolish the existing building and to build a new one, which it completed and occupied in about November 1997. Hilfiger's parent company paid about $20 million in cash to construct the new building.

A Lease provision captioned "Ownership" stated that "[d]uring the term of this Lease, the Improvements shall be the property of and owned by Lessee but considered a part of the Premises. The Improvements shall, at the expiration or earlier termination of this Lease, become the property of Lessor and remain upon and be surrendered by Lessee with the Premises."

The Lease further stated: "Lessor acknowledges Lessee's intention to construct a 'Flagship' location which may require extensive changes to the building storefront and Lessor agrees to cooperate. However, Lessor expressly prohibits Lessee from taking any action that would reduce the square footage of the building footprint or would reduce the frontage of the building facing Rodeo Drive or facing Santa Monica Boulevard. Lessor will have the right to approve any plans but will be reasonable in allowing Lessee to create and sign this building to its requirements."

The Lease provided that "Lessor and Lessee acknowledge and agree that as a material inducement to Lessee to enter into this Lease, Lessor has agreed that its consent to the Improvements (as hereinafter defined) shall be liberally granted even in the event that Lessee's plans and specifications call for the razing and rebuilding of the Premises or dividing the Premises into separate units; and Lessor and Lessee further acknowledge and agree that as a material inducement to Lessor to enter into this Lease, Lessee has agreed to either, at Lessee's option, substantially renovate the building on the Premises and the Premises in general . . . or to raze and completely rebuild a new building on the Premises . . . ."

The Lease also required the lessors' consent for Hilfiger to mortgage or encumber the improvements, to assign or transfer the leasehold, and lessors' approval of any architectural plans, alterations, or construction of new improvements. And although the Lease required Hilfiger to pay the real property taxes, the lessors were required to pay any increase in real property taxes due to, or resulting from, the sale of the Property. In the event of partial damage or total destruction of the property, Hilfiger was required, at its expense, to repair such damage, but if the damage was an insured loss, the lessors were required to make any insurance proceeds available to Hilfiger for purposes of repair.

On June 16, 1999, John Anderson, the father of Robert and Electra Anderson, died. Under the terms of the trusts, John Anderson's death resulted in a transfer of the grandparents' interests in the Property to the grandchildren. The grandchildren, through the Trustee, applied for a grandparent-grandchild exclusion (exclusion) pursuant to Revenue and Taxation Code section 63.1.[1] In December 2001, the Assessor's office granted the exclusion. The Assessor applied the $1 million exclusion to the land and the improvements, allocating approximately 8 percent of the exclusion to the land and 92 percent of the exclusion to the improvements on a pro rata basis. The Trustee filed an application with the Board, contesting the Assessor's calculation of the exclusion.[2] The

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[1] An April 22, 1998 letter from the Property Taxes Division of the State Board of Equalization to county assessors explained the history of the grandparent-grandchild exclusion as follows: "On November 4, 1986, the voters of California adopted Proposition 58, which added section 2(h) to article XIII A of the California Constitution to provide that the terms 'purchased' and 'change in ownership' do not include the purchase or transfer of (1) principal residences between parents and children and (2) the first $1 million of real property other than principal residences between parents and children. Section 63.1 was added to the Revenue and Taxation Code to implement the parent-child exclusion provisions of Proposition 58 and applies to any purchases or transfers between parents and children which occur on or after November 6, 1986. [¶] On March 26, 1996, the voters of California adopted Proposition 193, which amended section 2(h) of article XIII A to exclude from the definition of 'change in ownership' certain transfers from grandparents to their grandchildren. Section 63.1 was amended to reflect the grandparent-grandchild provisions. [Fn. omitted.]"

Unless otherwise specified, statutory references are to the Revenue and Taxation Code.

Section 63.1 provides in pertinent part: "(a) Notwithstanding any other provision of this chapter, a change in ownership shall not include the following purchases or transfers for which a claim is filed pursuant to this section: [¶] . . . [¶] (2) The purchase or transfer of the first one million dollars ($1,000,000) of full cash value of all other real property of an eligible transferor in the case of a purchase or transfer between parents and their children. [¶] (3)(A) Subject to subparagraph (B), the purchase or transfer of real property described in paragraphs (1) and (2) of subdivision (a) occurring on or after March 27, 1996, between grandparents and their grandchild or grandchildren, if all of the parents of that grandchild or those grandchildren, who qualify as the children of the grandparents, are deceased as of the date of purchase or transfer. [¶] . . . [¶] (c) As used in this section: [¶] . . . [¶] (8) 'Real property' means real property as defined in Section 104. Real property does not include any interest in a legal entity. [¶] (9) 'Transfer' includes, and is not limited to, any transfer of the present beneficial ownership of property from an eligible transferor to an eligible transferee through the medium of an inter vivos or testamentary trust."

[2] The Trustee's attachment to its application for a changed assessment stated that "[i]f correctly applied to the land only, [the grandparent-grandchild exclusion] would have prevented any reappraisal of the land at the Property because the trended Proposition 13 base-year value of the land as of June 16, 1999 [(the grandparent-to-grandchild transfer date)] was $938,365 for the full 100% interest in the Property. The interest that the [Trustee]
(footnote continued on next page)

Trustee contended that the exclusion should have been applied only to the land, arguing that the grandchildren did not have a "present beneficial ownership" interest in the improvements constructed by Hilfiger.

A hearing on the Trustee's application was held before the Board. Henry Pramov, Jr., an attorney, testified for the Trustee. Pramov had a general business practice with an emphasis in real estate law, but he had no expertise in property tax law. Pramov represented the trusts in negotiating the Lease. According to Pramov, the provision of the Lease providing that Hilfiger was the owner of the improvements during the Lease term was for tax purposes and so that Hilfiger would be able to depreciate the improvements over the term of the Lease. The Lease contained larger rent concessions or reductions for year three of the Lease term if Hilfiger chose to rebuild rather than renovate the improvements on the Property. The consideration to the trusts for the rent reductions was that the trusts would eventually own the improvements upon the expiration or termination of the Lease. In an economic sense, the transaction was equivalent to a commercial lease in that the trusts "have the benefit of rental payments for their land during the term of the lease and then the benefit of having the improvements revert to them in the end." According to Pramov, the improvements in this case had a life of 20 years or more. Pramov also testified that if the trusts had undertaken the cost of the improvements, the rent exacted from Hilfiger would have been higher, but because Hilfiger paid for the improvements, the rent paid by Hilfiger was essentially "ground rent." The trusts received the property tax bills, but sent them to Hilfiger. Hilfiger paid the property taxes.

Pramov noted that the Lease did not contain any provision allocating the rent between the land and the improvements, but testified that the rent paid under the Lease was not for the improvements but for the use of the land. According to Pramov, the trusts had a "remainder interest" or a "springing interest" in the improvements that would

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held in the land only and that transferred on June 16, 1999 had a trended base-year value of one-half that amount, which was far less than the remaining combined exclusion . . . ."

"come into play when the lease terminates," but the trusts had no ownership interest in the improvements in June 1999.

Steven Brown, an employee in the Assessor's office, testifying for the Assessor, stated that the property tax bill for the Property was sent out in the name of the record owners of the land, the trusts. For purposes of the Lease, Hilfiger may have "owned" the building, but not for property tax purposes. For property tax purposes, the trusts were the primary owners of the Property because the Lease term was less than 35 years. And the trusts had present beneficial interests in the Property represented by the rent received and the expectation of the reversion of the improvements upon the termination of the Lease.

In April 2003, the Board issued its decision determining that on the June 16, 1999 transfer date, there was no change in ownership of the improvements, which were owned by Hilfiger. The grandchildren did not have a "present beneficial ownership" interest in the improvements within the meaning of section 63.1 because of the "Ownership" and other provisions of the Lease and because Hilfiger paid the costs of the new improvements. The Board determined that the grandchildren held a "non-possessory future remainder interest in the improvements; this was not a 'present' interest that benefited the Grandchildren. In addition, to the extent that this future interest was transferred, such transfer was not a change of ownership." The Board thus concluded that the exclusion should have been applied only to the land and not to the improvements constructed by Hilfiger.

The Board rejected the Assessor's argument that property tax rule 462.100[3] applied to the transaction. The Assessor argued that under Rule 462.100, a lease for a term less than 35 years is not equivalent to a fee simple interest. Because the total term of Hilfiger's lease was only 20 years, Hilfiger did not have an ownership interest in the Property under property tax principles. Thus, according to the Assessor, the June 1999 transfer to the grandchildren constituted a change in ownership of both the land and the improvements.

The Board rejected application of Rule 462.100 on the ground that the improvements were not subject to the Lease. The Board determined that Hilfiger "did not lease the new improvements, but only the land underlying them; no rental was paid for the new improvements; and the Trusts . . . had no right to exercise any form of 'landlord control' over the new improvements." The Board directed the Assessor to correct the assessment so that the exclusion applied only to the land and not to the improvements.

The Assessor filed a petition and a motion for a writ of mandate, seeking to vacate the Board's decision and to direct the Board to enter a new decision that both the land and the improvements on the Property were subject to reassessment and application of the exclusion. The Trustee filed opposition to the motion, and the Assessor filed a reply. After oral argument, the trial court denied the petition and motion for a writ of mandate. In its statement of decision, the trial court supported its ruling with the same arguments

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[3] Rule 462.100 was promulgated by the State Board of Equalization and is codified in 18 California Code of Regulations section 462.100. We refer to this provision as Rule 462.100.

Rule 462.100 provides in pertinent part: "(a) The following transfers of either the lessee's interest or the lessor's interest in taxable real property constitute a change in ownership of such real property: [¶] (1) Lessee's Interest: [¶] (A) the creation of a leasehold interest in real property for a term of 35 years or more. [¶] . . . [¶] (2) Lessor's Interest: [¶] (A) The transfer of a lessor's interest in taxable real property subject to a lease with a remaining term of less than 35 years. [¶] . . . [¶] (b) The following transfers of either the lessee's interest or the lessor's interest in taxable real property do not constitute a change in ownership of such real property. [¶] (1) Lessee's interest: [¶] (A) The creation of a leasehold interest in real property for a term of less than 35 years. [¶] . . . [¶] (c) Once a change in ownership of taxable real property subject to a lease has been deemed to have occurred, the entire property subject to the lease is reappraised (i.e., the value of both the lessee's interest and the reversion)."

made by the Trustee and adopted by the Board. The trial court's statement of decision concluded: "The determinative facts of this case were undisputed: (1) Under the terms of the Lease, Hilfiger owned the improvements it constructed both before and after the June 1999 transfer; (2) the Lease is a ground lease under which no rent is paid for the improvements; and (3) the grandchildren have only a future interest in Hilfiger's improvements and do not participate in any way in the operation of the improvements. Given these undisputed facts, the Board correctly determined . . . that the grandparent-grandchild exclusion should not have been applied to Hilfiger's improvements." The Assessor appealed from the judgment.

DISCUSSION

A. Standard of Review and Applicable Law

We agree with the trial court and the Board that the underlying facts concerning the Lease are undisputed. But we disagree with their legal conclusions. And this is not an appropriate case to defer to the Board's interpretations of the governing statutes and Rule 462.100. (See *Bonnell v. Medical Board* (2003) 31 Cal.4th 1255, 1264–1265 [no deference accorded administrative agency's statutory interpretation where no agency-promulgated regulation at issue, agency had no particular expertise in interpreting statutes, and board's interpretation was incorrect in light of unambiguous statutory language].)

"[T]he definitions of property embodied in the Revenue and Taxation Code prevail for tax purposes even if they are inconsistent with the common law definitions codified in the Civil Code. [Citation.]" (*Pacific Southwest Realty Co. v. County of Los Angeles* (1991) 1 Cal.4th 155, 163, fn. 3 (*Pacific Southwest Realty*).) Under section 104, "real property" includes: "(a) The possession of, claim to, ownership of, or right to the possession of land" and "(c) Improvements." Under section 105, "Improvements" include "(a) All buildings, structures, fixtures, and fences erected on or affixed to the land."

And an agreement between the parties, whether express or implied, is not binding on the taxing authorities when classifying improvements for property tax purposes.

(*Trabue Pittman Corp. v. County of L. A.* (1946) 29 Cal.2d 385, 397 [for taxation purposes, trade fixtures are classified and assessed as realty].)

"Article XIII A of the California Constitution (Proposition 13) provides that real property shall be reassessed for property tax purposes when a 'change in ownership' occurs or the property is 'newly constructed' or 'purchased.' (Cal. Const., art. XIII A, § 2, subd. (a); Rev. & Tax. Code, §§ 60 et seq., 70 et seq.; Cal. Code Regs., tit. 18, § 463.) The Supreme Court in *Amador Valley Joint Union High School Dist. v. State Board of Equalization* (1978) 22 Cal.3d 208, 245, determined the meaning of 'change of ownership' was left for resolution 'by the contemporaneous construction of the Legislature or of the administrative agencies charged with implementing the new enactment.' [Citations.] [¶] The Legislature subsequently enacted provisions defining 'change in ownership' and based on those statutes, the State Board of Equalization adopted detailed regulations explaining the statutory scheme. (Rev. & Tax. Code, §§ 60–66; Cal. Code Regs., tit. 18, § 462.)" (*Shuwa Investments Corp. v. County of Los Angeles* (1991) 1 Cal.App.4th 1635, 1645 (*Shuwa Investments*).)

"What constitutes a 'change in ownership' is a question of law subject to this court's independent de novo judicial review. [Citation.] We are, therefore, not bound by the trial court's conclusions." (*Shuwa Investments*, *supra*, 1 Cal.App.4th at p. 1644.)[4]

Section 60 provides: "A 'change in ownership' means 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." Section 60's governing test for a change of ownership contains three parts: "'[1] a transfer of a present interest in real property, [2] including the beneficial use thereof, [3] the value of which is substantially

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[4] See also section 1605.5, which provides in pertinent part: "(a)(1) The county board shall hear applications for a reduction in an assessment in cases in which the issue is whether or not property has been subject to a change in ownership, as defined in Chapter 2 (commencing with Section 60) of Part 0.5 . . . . [¶] . . . [¶] (3) This subdivision shall not be construed to alter, modify, or eliminate *the right of an applicant under existing law to have a trial de novo in superior court with regard to the legal issue of whether or not that property has undergone a change in ownership* . . . so as to require reassessment." (Italics added.)

equal to the value of the fee interest.'" (*Pacific Southwest Realty*, *supra*, 1 Cal.4th at p. 162.) As explained in the Report of the Task Force on Property Tax Administration, dealing with the implementation of Proposition 13, the task force "'sought to distill the basic characteristics of a "change in ownership" and embody them in a single test [now section 60] which could be applied evenhandedly to distinguish between "changes" and "non-changes" . . . .'" (*Leckie v. County of Orange* (1998) 65 Cal.App.4th 334, 338 (*Leckie*).)

"The task force discussed the 'value equivalence' test [(that is, the third element)] as 'necessary to determine who is the primary owner of the property at any given time. . . . [¶] A major purpose of this third element . . . is to avoid . . . unwarranted complexity by identifying the primary owner, so that only a transfer by him will be a change in ownership and when it occurs the *whole* property will be reappraised. If [a] . . . lease . . . was a short term lease (the landlord owned the main economic value), the landlord's sale subject to the lease would count [as a change in ownership]. If, on the other hand, the lease was a long term lease (the lessee's interest was the main economic package), the lease assignment would count [as a change of ownership]. In either case the entire fee value of the leased premises would be reappraised.'" (*Leckie*, *supra*, 65 Cal.App.4th at p. 338.)

The task force further "recommended the use of statutory examples to elaborate on common transactions. 'Leases are a good illustration of the necessity of concrete statutory examples. Both taxpayers and assessors need a specific test — rather than the broad "value equivalence" test — to determine the tax treatment of leases. The specific test[,] however, must be consistent with the "value equivalence" rule and have a rational basis. Lenders will lend on the security of a lease for 35 years or longer. Thus 35 years was adopted as the concrete dividing line. If the term of a lease, including options to renew, is 35 years or more, the creation of the lease is a change in ownership and so is its expiration. If a lessee under such a lease assigns or sublets for a term of 35 years or more, that is another change in ownership. However, if the lease, including options, is for less than 35 years the lessor remains the owner and only the transfer of his interest is a change.'" (*Howard v. County of Amador* (1990) 220 Cal.App.3d 962, 974, fn. 5 (*Howard*).)

Following the recommendation of the task force, section 61, subdivision (c) was passed, adopting the 35-year rule.

"Because . . . section [60] was 'intended as a guidepost in cases not covered by the specific inclusions or exclusions' in Revenue and Taxation Code sections 61–66, it is inapplicable in a case such as this where specific provisions cover the transactions which occurred. [Citation.]" (*Shuwa Investments*, *supra*, 1 Cal.App.4th at p. 1648, fn. 14.) "The Legislature intended that [the 35-year rule for leases under section 61, subdivision (c)] would be a concrete example of the application of the basic definition of a change of ownership and was particularly concerned that this and the other statutory examples set forth in sections 61 and 62 be consistent with the general test." (*Howard*, *supra*, 220 Cal.App.3d at p. 974.)

B. Section 61, subdivision (c)

The issue before us is whether the transfer from the grandparents to the grandchildren in 1999 included the improvements. We conclude that it did, because the transaction falls squarely within section 61, subdivision (c).

In pertinent part, section 61 provides that a "change in ownership, as defined in Section 60, includes, but is not limited to: [¶] . . . [¶] (c)(1) The creation of a leasehold interest in taxable real property for a term of 35 years or more (including renewal options) . . . or (2) any transfer of a lessor's interest in taxable real property subject to a lease with a remaining term (including renewal options) of less than 35 years. [¶] Only that portion of a property subject to that lease or transfer shall be considered to have undergone a change in ownership."

The Legislature determined, in section 61, subdivision (c), that when a property is leased for a term of *less than 35 years*, the main economic value of the property resides with the lessor and not the lessee. "[The Task Force on Property Tax Administration] decided that the creation, transfer or termination of a leasehold of 35 years or more should achieve a change in ownership because in that case the primary economic value of the land resides in the lease. [Citations.] The Legislature followed that recommendation. (§ 61, subd. (c).)" (*Pacific Southwest Realty*, *supra*, 1 Cal.4th at p. 167.) Rule 462.100(b)(1)(A) also adopts the bright-line 35-year rule and provides that the creation of a leasehold interest of *less* than 35 years does *not* constitute a change in ownership. (See fn. 3, *ante*.)

"[T]he creation of a 35-year lease would achieve a change in ownership (§ 61, subd. (c)(1)) because the length of the lease would give the lessee's interest some of the practical attributes of a conveyance of fee simple. A lease of such duration will constitute the *main economic value* of the land, even though the leaseholder does not own a freehold estate — lenders are, in the report drafters' view, willing to lend on the security of such an instrument." (*Pacific Southwest Realty*, *supra*, 1 Cal.4th at p. 165, italics added.)

"Section 61, subdivision (c) was intended to provide a concrete example of a change of ownership consistent with the general definition in section 60. The application of section 61, subdivision (c) to estates for years [(another name for a leasehold estate)] is consistent with section 60, and the determining period of 35 years has been judicially upheld against claims that it is arbitrary and unreasonable. (*E. Gottschalk & Co. v. County of Merced* (1987) 196 Cal.App.3d 1378, 1385–1386.)" (*Howard*, *supra*, 220 Cal.App.3d at p. 975.)

Here, under the bright-line 35-year rule of section 61, subdivision (c) and Rule 462.100(b)(1)(A), the 20-year Lease did not constitute a change in ownership of the Property. Notwithstanding Hilfiger's construction of the new improvements, section 61, subdivision (c) mandates the conclusion that the main economic value of the Property resided with the lessors. Thus, under section 61, subdivision (c)(2), the 1999 transfer from the grandparents to the grandchildren constituted a change in ownership and included both the land and the improvements.

The lessors argue without citation of authority that because Hilfiger constructed and paid for the new building, it was not "subject to the lease" within the meaning of Rule 462.100(c). We disagree. Such construction of the rule and the Lease is unreasonable. All of Hilfiger's rights and obligations, as well as the restrictions, with respect to the improvements, including the right to either renovate or demolish the existing building and to construct a new one, derived from the Lease. While Hilfiger may have had valuable contractual rights under the Lease, which included the right to elect to construct a new building, the exercise of that contractual right was "subject to the lease" within the meaning of Rule 462.100(c).

And under the 35-year rule, it is of no import that the Lease stated that Hilfiger was the owner of the improvements during the term of the Lease. It was undisputed that the purpose of such provision was to afford Hilfiger the right to depreciate the cost of the improvements under federal tax law. Because the foregoing Lease provision is not binding on the taxing authorities (*Trabue Pittman Corp. v. County of L. A.*, *supra*, 29 Cal.2d at p. 397), it does not control the analysis of whether section 61, subdivision (c) and Rule 462.100(c) apply here.

The lessors also contend that the testimony of Pramov and Brown established that the Lease was a ground lease and that the rent was paid only for the use of the land and not for the improvements, notwithstanding that there was a 14,400-square-foot retail building on the land at the time the Lease was executed.[5] Premised on Hilfiger's having constructed and paid for the new building, the lessors contend that Hilfiger "owned" the improvements and therefore the improvements were not part of the transfer from the grandparents to the grandchildren. But such testimony amounts to the assertion of legal conclusions which are not binding upon our de novo review. Even assuming that the lessors have properly characterized the Lease as a ground lease, such characterization is

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[5] "The term 'ground lease' is somewhat of a misnomer. 'Ground lease' is simply a euphemism for a long-term lease, often involving vacant land upon which the tenant is permitted (or required) to build improvements. A 'ground lease' has no defined legal significance and could just as easily be (and often is) denominated a 'lease,' 'land lease' or any other designation indicating a leasehold. Thus, a ground lease involves all of the legal and practical issues associated with most any lease." (Greenwald & Asimow, Cal. Practice Guide: Real Property Transactions (The Rutter Group 2004) ¶ 7:1, p. 7-1.) "Perhaps the most obvious difference between a ground lease and other leases is the duration of the term. The term of a ground lease is typically very long — 35, 50 or 99 years." (*Id.*, ¶ 7:3, p. 7-2.)

Thus, the total term of the instant Lease, 20 years, is shorter than the term of a typical ground lease.

not binding for property tax purposes (*Trabue Pittman Corp. v. County of L. A.*, *supra*, 29 Cal.2d at p. 397) and is irrelevant to the application of section 61, subdivision (c).

Thrifty Corp. v. County of Los Angeles (1989) 210 Cal.App.3d 881 (*Thrifty*) is instructive. The court in *Thrifty* held that a 20-year lease with a 10-year option to renew was not of sufficient longevity to approximate a transfer in fee and thus did not fall within the meaning of the phrase "realty sold" in the documentary transfer tax statute, section 11911. The court in *Thrifty* explained that "the issue boils down to whether as a matter of law Thrifty's 20-year lease with an option to renew for 10 years is of sufficient longevity under California law to approximate an '"ownership" right rather than a mere "temporary right of possession."' [Citation.] The Legislature has provided us with guidance in making this determination. [S]ection 61, subdivision (c)(1) (section 61) defines 'change in ownership' for property tax purposes in part as '[t]he creation of a leasehold interest in taxable real property for a term of 35 years or more (including renewal options), . . .' [¶] . . . [¶] While the Document Transfer Tax Act does not define 'realty sold' that phrase is sufficiently similar to the phrase 'change in ownership' contained in the same code and governing an analogous subject, to warrant that each phrase be defined to have the same meaning." (*Thrifty*, *supra*, 210 Cal.App.3d at pp. 885–886.)

The *Thrifty* court also rejected the assertion that it was "a question of fact whether a lease of a shorter duration than that specified in section 61 approximates an interest in fee. The determination of what the Legislature intended when it employed the term 'realty sold' in section 11911 is a question of law. [A]s a matter of law Thrifty's 20-year lease with an option to renew for 10 years was not of sufficient longevity to constitute 'realty sold' under section 11911." (*Thrifty*, *supra*, 210 Cal.App.3d at p. 886.)

For reasons akin to those in *Thrifty*, we conclude that this case falls squarely within section 61, subdivision (c). Accordingly, a factual analysis of the factors in section 60 is unnecessary. (*Shuwa Investments*, *supra*, 1 Cal.App.4th at p. 1648, fn. 14; see *Howard*, *supra*, 220 Cal.App.3d at p. 974.)

C. Conclusion

In sum, Hilfiger's 20-year Lease did not constitute a change in ownership of the Property from the lessors to Hilfiger within the meaning of section 61. But the transfer from the grandparents to the grandchildren did. And as noted, both the land and the improvements were "subject to the lease" so that the 1999 transfer from the grandparents to the grandchildren necessarily transferred both the land and the improvements.[6] "Once a change in ownership of taxable real property subject to a lease has been deemed to have occurred, the entire property subject to the lease is reappraised (i.e., the value of both the lessee's interest and the reversion)." (Rule 462.100(c); see fn. 3, *ante*.) Accordingly, the Assessor may properly include the improvements in the calculation of the grandparent-grandchild exclusion.

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[6] Based on the assumption that in 1999 Hilfiger was the owner of the improvements for property tax purposes, the lessors contend that the grandparent-grandchild exclusion cannot be applied to the improvements because Hilfiger, a corporation, is not an "eligible transferee" under section 63.1. (See fn. 1, *ante*.) Even though Hilfiger may not be an eligible transferee under section 63.1, the point is irrelevant in this case. As explained above, Hilfiger was not the owner of the improvements for property tax purposes. The land and the improvements were owned by the grandparents and then transferred to the grandchildren within the meaning of section 63.1.

DISPOSITION

The judgment is reversed and on remand the trial court is directed to vacate its order denying the petition for a writ of mandate and to enter a new order granting the petition for a writ of mandate. The parties shall bear their own costs on appeal.

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MALLANO, Acting P. J.

I concur:

SUZUKAWA, J.*

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* Judge of the Los Angeles Superior Court, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.

VOGEL, J.

For reasons too numerous to summarize in an introductory paragraph, I dissent.

A.

In February 1996, the Anderson Trusts (acting through their trustee, Northern Trust Bank of California) leased real property at the corner of North Rodeo Drive and Little Santa Monica Boulevard to Tommy Hilfiger Retail, Inc. for a term of ten years, with two five-year options to extend the lease.[1] The ground lease gave Hilfiger the property "as is," and allowed Hilfiger to either renovate an existing structure or construct a new building.[2] Hilfiger demolished the old structure, constructed a large new building (23,509 square feet), and (in November 1997) moved in. Hilfiger pays rent for the land, not for the building (referred to by the parties as the "Improvements"), and pays all costs of operating the building (insurance, property taxes, maintenance, and repairs).

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1 Stanley and Marguerite Anderson are the trustors of the two trusts at issue in this case. Their grandchildren, Robert and Electra Anderson (the children of John Anderson), are the beneficiaries of those trusts. The trusts provided that, upon John Anderson's death, the trust estate would be transferred to Robert and Electra.

2 It is important to note that we are dealing with a ground lease. "Unlike many other leases, ground leases usually involve property that is initially either completely unimproved, minimally improved, or in need of rebuilding (hence, the term 'ground' or 'land' lease). Also, in contrast to most other landlord-tenant relationships, the ground lease *tenant* (rather than the landlord) constructs (and often initially owns) the improvements." (Greenwald & Asimow, Cal. Practice Guide: Real Property Transactions (The Rutter Group 2004) ¶ 7:16, p. 7-5.)

Under the express terms of its lease, Hilfiger owns the building, and the trusts do not have the ordinary powers of a landlord: "During the term of this Lease, the Improvements shall be the property of and owned by Lessee but considered a part of the Premises. The Improvements shall, at the expiration or earlier termination of this Lease, become the property of Lessor and remain upon and be surrendered by Lessee with the Premises." With this provision, Hilfiger (having spent a substantial amount of money constructing the building) was able to depreciate the cost of construction for federal tax purposes and to limit its rent to the cost of the ground. Both Henry P. Pramov, Jr. (the lawyer who drafted the lease) and Stephen Brown (the Assessor's own appraiser) testified that Hilfiger owns the building, ***that neither the trusts nor the grandchildren receive any rent for the building***, and that the grandchildren have only a future interest in the building.

B.

John Anderson died in June 1999, triggering the transfer of the trust's assets to the trustor's grandchildren, Robert and Electra. Proposition 13 (Cal. Const., art. XIII A, § 2, subd. (a)) requires a reassessment of real property when there is a change of ownership but grants a $1 million exclusion to transfers from grandparents to their grandchildren, and Robert and Electra, acting through the trustee, applied for that exclusion. (Rev. & Tax. Code, §§ 60, 63.1.)[3] The

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[3] Undesignated section references are to the Revenue and Taxation Code. Section 60 defines "change in ownership" for Proposition 13 purposes 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." (Emphasis added.) As relevant, section 63.1 provides that, "[n]otwithstanding any other provision of this chapter, a change in ownership shall not include [the first $1 million of the full cash value of] . . . the purchase or transfer of real property . . . between grandparents and their . . . grandchildren, if all of the parents of . . . those grandchildren . . . are deceased as of the date of . . . transfer. . . . 'Transfer' includes . . . any

(footnote continued on next page)

Los Angeles County Assessor granted the exclusion, but applied the $1 million to both the land and the building -- and allocated only 8 percent of the exclusion to the land, and the remaining 92 percent to the building.[4]

The trustee challenged the allocation before the Assessment Appeals Board, pointing out that the grandchildren had no present beneficial interest in the building, and that the value of the improvements would not be allocable to Robert and Electra until the end of the lease term, at which time they would then have a present beneficial interest in the building. The Assessor claimed the lease was immaterial for property tax purposes, that a lease by any other name is still a lease -- and that a transfer of a lessor's interest in a lease for a term of less than 35 years is a change of ownership within the meaning of section 60. (§ 62, subd. (g); Cal. Code Regs., tit. 18, § 462.100 [Rule 462.100].)[5] The Assessor also claimed the building was a fixture which (according to the lease the Assessor said couldn't be considered) could not be removed from the land, and that the economics of this transaction are indistinguishable from any other lease (an

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transfer of the ***present beneficial ownership*** of property from an eligible transferor to an eligible transferee through the medium of an inter vivos or testamentary trust." (Emphasis added.)

4 The Assessor said the total cash value of the property was $21,046,340. This valuation was challenged by the trustee, and will ultimately be determined by the Assessment Appeals Board in the second part of a bifurcated proceeding, the first part of which is before us on this appeal.

5 Subdivision (g) of section 62 provides that a change in ownership does not include a "transfer of a lessor's interest in taxable real property subject to a lease with a remaining term . . . of 35 years or more." Rule 462.100 provides (at subdivision (a)(2)(A)), as relevant, that a transfer of a lessor's interest in taxable real property constitutes a change in ownership (provided there is also a transfer of a present beneficial interest) if the "real property [is] subject to a lease with a remaining term of less than 35 years." The rule also provides (at subdivision (c)) that, "[o]nce a change in ownership of taxable real property subject to a lease has been deemed to have occurred, the entire property subject to the lease is reappraised (i.e., the value of both the lessee's interest and the reversion)." (See Part D.4, *post*.)

argument that ignores the function of a ground lease and in any event has nothing to do with the issue of ownership).

C.

After a hearing at which both oral and documentary evidence was presented, the three-member Assessment Appeals Board agreed with the Trustee and issued a decision that included findings of fact consistent with the evidence I have summarized above -- and also found that Robert and Electra, who have "never exercised any of the common indicia of ownership" with regard to the building, have only "a 'remainder' or 'springing' interest in the [building] that will come into play when the [lease] terminates."

Because I believe the Assessment Appeals Board's factual findings are supported by substantial evidence (most of which is undisputed) and are binding on this appeal (*Shell Western E & P, Inc. v. County of Lake* (1990) 224 Cal.App.3d 974, 979-980; *Dennis v. County of Santa Clara* (1989) 215 Cal.App.3d 1019, 1026), and because I believe our independent review of the legal issues starts with a strong presumption that the administrative decision is correct (*Fukuda v. City of Angels* (1999) 20 Cal.4th 805, 817; *Select Base Materials v. Board of Equal.* (1959) 51 Cal.2d 640, 647-658; *Clayton v. County of Los Angeles* (1972) 26 Cal.App.3d 390, 396; *Bret Harte Inn, Inc. v. City and County of San Francisco* (1976) 16 Cal.3d 14, 23 [when the challenge is to the validity of a determination made by the Assessment Appeals Board the issue is whether the challenged finding "is arbitrary, in excess of discretion, or in violation of the standards prescribed by law"]) and, most importantly, because I believe the Board reached the right result, I quote its decision at length:

"In analyzing this question, the Board is first guided by the provisions of . . . [s]ections 63.1(c)(9) and 60, which set forth the requirements for the Grandparent-Grandchild Exclusion and the basic change of ownership requirements and, therefore, appl[y] directly and specifically to this matter. Both of those code sections require that a 'transfer' or 'change of ownership' be of a 'present beneficial interest' in the property transferred. The meaning of 'present' and 'beneficial' are straightforward, requiring that the transferee be able to immediately enjoy the use, occupancy or possession of the property ***at the time of the transfer***.

"The Board's understanding of the word 'present' in . . . [s]ections 63.1(c)(9) and 60 is supported by the discussion in the ***State Board of Equalization's Letter to Assessors . . . No. 98/23, [which] indicates that a . . . Grandparent-Grandchild Exclusion[] may only be obtained when a nonpossessory remainder interest becomes possessory***. The Board understands the term 'beneficial' in these two statutes to mean possession or occupancy or, in the case of a lessor, receipt of rental for the property which has been leased.

"The facts in this matter, which are not disputed, show that . . . Robert and Electra did <u>not</u> have a 'present beneficial ownership' interest in the [building] on the June 16, 1999 transfer date. Those facts fall into two distinct categories: (a) evidence of the Trusts' and Hilfiger's intent as shown by the [lease] and (b) the actions and practices of the Trusts (including . . . Robert and Electra) and Hilfiger with regard to the [building].

"The [lease] states that ownership of the [building] was held by Hilfiger once the [building was] completed in 1997. Other provisions in the [lease] support the conclusion that the Trusts and Hilfiger intended the [building] to be owned by Hilfiger for as long as Hilfiger was leasing the land on which the [building was] located. For example, the elimination of all references in the [lease] to lessor ownership of improvements, the provisions relating to payment of rent only for the use of the land, and the requirement that insurance loss proceeds received by the Trusts for any damage to the improvements be forwarded to Hilfiger all demonstrate that Hilfiger owned the new improvements constructed at the Property.

"The actions and practices of the Trusts, Robert, Electra, and Hilfiger also support the conclusion that Hilfiger owned the new improvements as of June 16, 1999. First, Hilfiger built the [building] at its own cost. Second, Hilfiger paid all expenses related to operation of the [building]. Third, the Trusts, Robert and Electra had no right or claim to possess or occupy the [building] in 1999, nor did they do so any time. All benefits associated with the use and occupancy of the [building] went to Hilfiger, and not to the Trusts or to Robert and Electra. ***This is most clearly supported by the absence of any rental payments by Hilfiger for the new improvements***.

"In light of the provisions of . . . [s]ections 63.1 and 60 cited above, and the facts just stated, the Board finds that the Trusts and . . . ***Robert and Electra did not have a 'present beneficial ownership' interest in the [building] under the Revenue and Taxation Code provisions which specifically and directly apply to the circumstances at hand***. Instead, . . . Robert and Electra held a non-possessory future remainder interest in the improvements; this was not a 'present' interest that benefited the Grandchildren. In addition, to the extent this future interest was transferred, such transfer was not a change of ownership.

"The Board, therefore, concludes that the Grandparent-Grandchild Exclusion, which the Assessor granted to [the Trustee], should only have been applied to the land . . . , and not to the [building] constructed and owned by Hilfiger. The Assessor should not have extended the Grandparent-Grandchild Exclusion to the new improvements because there was no transfer of a 'present beneficial ownership' interest in [the building] on June 16, 1999.

"The Assessor's primary argument, that the lessor's interest in the new improvements was transferred because the Agreement leased the land for [fewer] than 35 years, and that under that circumstance the 'full fee simple' of land and improvements had to be reappraised, fails for several reasons. First, the [lease] was entered into in 1996, three years [before] the transfer date. That [lease] did not trigger a change of ownership on June 16, 1999. Second, the [lease] specified that [a new building] would be constructed, and that [the building] would be owned by Hilfiger. ***The [lease] did not [provide for the lease of] the [building], but only the land underlying [it]; no rental was paid for the [building] and the Trusts, Robert and Electra had no right [to] exercise any form of 'landlord control' over the [building]***. Third, the [building was] constructed in 1997 and never belonged to the Trusts or to . . . Robert and Electra, either before June 16, 1999 or after that date.

"[T]he authorities cited by the Assessor support the Board's conclusion. The Assessor refers to . . . Rule 462.100(c) to support his position. That provision states: 'Once a change of ownership of taxable real property *subject to a lease* has been deemed to have occurred, the entire property *subject to the lease* is reappraised.' . . . [¶] ***The Assessor's reliance on this provision cannot succeed because it only calls for reappraisal of the property 'subject to the lease.' In this matter, only the land was leased to Hilfiger***. The [building], which did not come into existence until three years after the [lease] was executed, [was] built and owned by Hilfiger and [was] never leased to Hilfiger.

"Finally, the Assessor's contention that leased property can only be assessed to 'one primary owner' . . . is undermined by the provisions of [the] Revenue and Taxation Code which permit[] separate assessments of land and improvements at the same location to the person who owns the land and the person who owns the improvements. This is consistent with . . . [s]ection 405, which permits the Assessor to assess taxable property (whether land or improvements) to the person who owns, claims, possesses or controls that property.

"The Assessor shall correct the assessment . . . so that the Grandparent-Grandchild Exclusion is only applied to the land and not to the [building] . . . ." (Bold italics added, other emphasis in original.)

D.

The trial court reviewed the decision of the Assessment Appeals Board, found the Board's decision was supported by substantial undisputed evidence and legally correct, denied the Assessor's petition, and entered judgment in favor of the trustee and the grandchildren. (Code Civ. Proc., § 1094.5.) I would affirm that judgment for the reasons stated by the Assessment Appeals Board, and for the following additional reasons.

1.

First, there is implicit in the majority's opinion a belief (expressed at oral argument) that acceptance of the Board's decision would mean that anybody could make a deal like the one the Trusts made with Hilfiger. So what? Tax deferral is as much a part of the American way as apple pie, and there is nothing legally or morally wrong with this deal.[6]

2.

Second, the majority's reliance on section 61 is misplaced where, as here, there is no change of ownership of the building erected by the lessee, only in the land on which it sits. As I have said, we are dealing with a ground lease -- which in contrast to most other leases generally (as here) requires the tenant, not the landlord, to construct the improvements, and which quite commonly (as here) results in the tenant's ownership of the improvements. (Greenwald & Asimow, Cal. Practice Guide: Real Property Transactions, *supra,* ¶ 7:19, pp. 7-5 to 7-6.) The Assessor side-steps this issue by contending the parties cannot by contract alter the rule that "'real estate is generally taxed as a unit to the owner of the fee interest without separate listing or taxation of leasehold or other interests in the property'" (which the Assessor supports with a citation to Hellerstein & Hellerstein, *State and Local Taxation: Cases and Materials* (West Pub. Co., 5th ed. 1988) p. 121).

The Hellerstein text does not support the Assessor's position -- because its discussion is based on an unspecified Maine statute that provided (according to Hellerstein) that "real estate, for purposes of taxation, includes all lands and all buildings erected on or affixed to land" (there is no suggestion in Hellerstein or by the Assessor that California has a similar statute). (Hellerstein & Hellerstein, *State*

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6 The use of a ground lease is not a novel concept (see fn. 2, *ante*), and although a ground lease usually provides tax advantages to both landlord and tenant, it also provides a number of other advantages to both parties. (See Greenwald & Asimow, Cal. Practice Guide: Real Property Transactions, *supra,* ¶ 7:45 et seq.)

and Local Taxation: Cases and Materials, supra, pp. 121-122.) According to Hellerstein, there is a "Massachusetts rule" (the lease is irrelevant) and a "New York rule" ("it is competent for parties by contract to so regulate their respective interests that one may be the owner of the buildings, and another the land"). According to the Assessor, California follows the Massachusetts view.

I think not. Ground leases are common in California, and legally recognized as a specific form of lease (e.g., Code Civ. Proc., § 1298, subd. (a)). They commonly provide for separate ownership interests (Greenwald & Asimow, Cal. Practice Guide: Real Property Transactions, *supra,* ¶ 7:45 et seq.), and the Assessor offers no authority to suggest the parties cannot do likewise for tax purposes.

Noticeably absent from the Assessor's analysis is any recognition of the fact that the "leasehold" interest in this property is limited to the land, and does not include the building, and the two cases he cites do not support his position vis-à-vis ownership. Both *Clayton v. County of Los Angeles, supra,* 26 Cal.App.3d 390, and *Carlson v. Assessment Appeals Bd. I* (1985) 167 Cal.App.3d 1004, address disputes arising out of the ***valuation*** of property, not the ***ownership*** of property, and while both generally would support a claim that, in determining fair market value, private agreements will not be considered, neither has anything to do with our consideration of an agreement that divests one party of an ownership interest and grants it to another. (Compare *Cox Cable San Diego, Inc. v. County of San Diego* (1986) 185 Cal.App.3d 368, 379-381 [proper to separately assess possessory interests].)

But the issue in the Assessor's cases -- whether estates for years and reversionary interests should be valued together -- has nothing to do with the issue in this case, which is whether improvements are automatically reassessable when the underlying land, but not the improvements, changes hands.[7] As the Assessment Appeals Board explained, the answer to that question is found not in section 61, subdivision (c)(1), or Rule 462.100(a)(2)(A), which apply only to property "subject to a lease," but rather in section 60, which provides for reassessment only when there is a transfer of a "present beneficial interest."

For the same reason, the *holding* (as opposed to the analysis) in *Pacific Southwest Realty Co. v. County of Los Angeles* (1991) 1 Cal.4th 155, one of the major hooks on which the majority hangs its hat, is inapposite. *Pacific Southwest* (a sale and leaseback transaction) finds a beneficial interest in a lease based on the tenant's ***payment of rent***. (*Id.* at p. 164.) Because it is undisputed in our case that ***no rent is paid for the building,*** and that neither the trusts nor the grandchildren have any other present beneficial interest in the building, the result reached in *Pacific Southwest* has nothing to do with the price of tomatoes. It is the ***analysis*** of *Pacific Southwest* (as discussed below) that ought to govern our resolution of this case, not its holding.

3.

Third, it is immaterial that the trusts (or the grandchildren), rather than Hilfiger, are the assessees -- because the identity of the assessee does not affect ownership, and assessees are not necessarily owners. (*T.M. Cobb Co. v. County*

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7 As noted above and explained by the Assessment Appeals Board in its decision, the matter now before us is the first part of a bifurcated proceeding in which the Board "addressed the proper application of the . . . [s]ection 63.1 Grandparent-Grandchild Exclusion to the Property. [This decision] address[es] that issue alone. ***The second part of the bifurcated hearing, to be held at a later date, will address the issues relating to the assessed value of the Property***." (Emphasis added.) It is at that time that valuation will be an issue.
(footnote continued on next page)

of Los Angeles (1976) 16 Cal.3d 606, 625-626.) Indeed, when property is subject to a lease, the Assessor can and sometimes does assess tenant-owned improvements to the landowner. (§ 2188.2 [when "improvements are owned by a person other than the owner of the land on which they are located, the owner of the improvements or the owner of the land may file with the assessor a written statement . . . attesting to their separate ownership, in which event the land and improvements shall not be assessed to the same assessee"].)

Of course, it is equally immaterial that the land and the building were and are included on the same tax bill, and the Assessor offers no authority at all to support his claim to the contrary. (*T.M. Cobb Co. v. County of Los Angeles, supra,* 16 Cal.3d at pp. 625-626 ["Although section 2188.2 requires the assessor to assess improvements to someone other than the owner of the land when a statement is filed, the assessor is not prohibited from doing so when such a statement has not been filed"].) To state the obvious, the Assessor's tax bill cannot change the ownership of property, real or personal, and this fact alone compels rejection of the Assessor's assertion that, for purposes of administrative convenience and regardless of the law, the tax bill gives the grandchildren a beneficial interest in a building owned by Hilfiger.

The majority opinion says that "the 1999 transfer from the grandparents to the grandchildren constituted a change in ownership and included both the land and the improvements. " (Typed opn., p. 13.) Since the "improvements" (the building built by Hilfiger) did not exist at the time the lease was executed, I fail to see how anybody could have transferred an interest in it, beneficial or otherwise; since the lease provided that, upon its completion, Hilfiger would own the building for the term of the lease, I fail to see how the lease can be construed to give the grandchildren any interest in the building, beneficial or otherwise. Of course, the majority's entire discussion is based on the erroneous assumption that, contrary to the undisputed evidence, Hilfiger paid rent for the building.

4.

Fourth, the history of the 35-year rule defeats rather than supports the Assessor's position.

According to the Proposition 13 Task Force Report (the genesis of section 60), a change of ownership within the meaning of section 60 occurs ***only when a transfer "has all three of the following characteristics***: (1) It transfers a <u>present interest</u> in real property; (2) It transfers the <u>beneficial use</u> of the property; and (3) The property rights transferred are <u>substantially equivalent in value</u> to the fee interest." (Report of the Task Force on Property Tax Administration presented to the Assembly Committee on Revenue and Taxation, January 22, 1979, p. 38, underscoring in original, bold italics added (Task Force Report).)[8] In our case,

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8 "Because Proposition 13 did not explicate the meaning of 'change in ownership' . . . , it fell to the Legislature to define the phrase, a task it has striven to perform . . . since Proposition 13 was adopted by the electorate. The main effort to create consistent and uniform guidelines to implement Proposition 13's undefined 'change in ownership' provision was undertaken by a 35-member panel that included legislative and [B]oard [of Equalization] staff, county assessors . . . , trade associations, and lawyers in the public and private sectors. The panel's work culminated in the Report of the Task Force on Property Tax Administration . . . . [¶] . . . The Legislature adopted some of the recommendations verbatim or with non-substantive technical revisions, and others with rather minor changes. The report's key change-in-ownership test was adopted verbatim and is now codified in section 60 . . . ." (*Pacific Southwest Realty Co. v. County of Los Angeles, supra,* 1 Cal.4th at pp. 160-161.)

the Assessor's claim is that, because Hilfiger's lease is for a term of less than 35 years, the 35-year-lease rule by itself means the grandchildren obtained a present beneficial interest in the building as well as the lease. But that is not what the Task Force or the Legislature intended.

To the contrary, the idea was that both "taxpayers and assessors need[ed] a specific test -- rather than the broad 'value equivalence' test -- to determine the tax treatment of leases. . . . Lenders will lend on the security of a lease for 35 years or longer. Thus 35 years was adopted as the concrete dividing line." (Task Force Report, p. 41.) What this means is that the *third element* of the test -- that the rights transferred are <u>substantially equivalent</u> in value to the fee interest -- is satisfied by the transfer of a 35-year or longer leasehold estate in the property. (*Pacific Southwest Realty Co. v. County of Los Angeles, supra,* 1 Cal.4th at p. 167 [in the case of a lease for 35 years or more, the primary economic value of the land resides in the lease, meaning it is substantially equivalent in value to the fee interest].)

But the rule most assuredly does *not* provide that the mere existence of a 35-year or longer lease satisfies the other two components (a present interest, and beneficial use), nor does it give the lessor an ownership interest in the tenant's improvements. To effect a change of ownership for Proposition 13 purposes, all three components must be satisfied. (*Leckie v. County of Orange* (1998) 65 Cal.App.4th 334, 339 [the trial court erred when it "construed the value equivalency prong of section 60's three-pronged test as determinative of the change of ownership question rather than looking at all three prongs"]; see also *Pacific Southwest Realty Co. v. County of Los Angeles, supra,* 1 Cal.4th at pp. 162, 166 ["Because the Legislature, in enacting section 60, adopted its language verbatim after reviewing the task force report, it is evident that the Legislature intended for section 60 to contain the overarching definition of a 'change in ownership' for reassessment purposes," and holding that a change of ownership occurred because "all prongs of section 60's test" were met].)

Here, it is immaterial that the lease was not for a term of 35 years or longer because (according to the uncontroverted evidence) Robert and Electra did not acquire a present or beneficial interest in the building in June 1999, which means the first two elements of the test were not satisfied. Indeed, the example the State Board of Equalization gave to its assessors about the parent-child exclusion (which for this purpose is the same as the grandparent-grandchild exclusion) proves the point. The question posed was this: "A mother died. In her will she granted a life estate in real property to a friend with the remainder to her children. Should the parent-child claim be filed upon the death of the mother or the termination of the life estate?" The answer given was this: "[A] change in ownership occurs when the life estate terminates and the property passes to the remainder person. However, upon the termination of the life estate, the remainderman rights of the children become possessory. The filing period for the parent-child exclusion begins to run when their interest becomes possessory -- upon the termination of the life estate."[9]

As I said earlier in this dissent, the grandchildren's interest in the building will become present and beneficial upon the termination of the lease, at which time their interest will be subject to reassessment under Proposition 13.

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[9] The State Board of Equalization's Letters to Assessors are entitled to significant deference. (*Yamaha Corp. of America v. State Bd. of Equalization* (1999) 73 Cal.App.4th 338, 350-354.)

5.

Fifth, the building is not a fixture within the meaning of Civil Code section 1013 because the statute does not apply where, as here, the parties have agreed otherwise.[10] (*Board of Education v. Grant* (1897) 118 Cal. 39, 41; *R. Barcroft & Sons Co. v. Cullen* (1933) 217 Cal. 708, 712; *Morse Signal Devices v. County of Los Angeles* (1984) 161 Cal.App.3d 570, 580-581 [under parties' agreement, permanent improvement may be separately assessed to cable provider]; *Realty Dock etc. Corp. v. Anderson* (1917) 174 Cal. 672, 676.) Any other result would be inconsistent with section 2188.2 -- and there is no way under the sun to treat Hilfiger's building as a "trade fixture." (Typed opn., p. 9.) (See *County of Ventura v. Channel Islands State Bank* (1967) 251 Cal.App.2d 240, 247-250 [section 1013 does not apply to the determination of ownership for property tax purposes].)

6.

To paraphrase Justice Mosk's decision in *Pacific Southwest Realty Co. v. County of Los Angeles, supra,* 1 Cal. 4th at pages 167-168, 170, the legislative intent is apparent when viewed through the filter of sections 60 and 62 and the Task Force Report. "Both the report and the statutes demonstrate that the drafters and the Legislature intended to find a change in ownership [only] when the primary economic value of the land is transferred from one person or entity to another," that a "transaction [does] not trigger reassessment unless it transfers

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10 Civil Code section 1013, which was enacted in 1872, provides: "When a person affixes his property to the land of another, without an agreement permitting him to remove it, the thing affixed, except as otherwise provided in this chapter, belongs to the owner of the land, unless he chooses to require the former to remove it or the former elects to exercise the right of removal provided for in Section 1013.5. . . ."

the interest of the party carrying the primary economic weight of the property," that "section 60 . . . was intended as the fundamental rule implementing Proposition 13" while sections 61 and 62 "were [intended by the Legislature] to be derivative or explanatory, and not to conflict with section 60's general rule" and that, in addition to the "substantial equivalency" requirement, a change of ownership occurs only when, in addition, the transfer is of a "present interest" in a "beneficial use" of the property.

Because neither the trusts nor the grandchildren obtained a present interest or beneficial use of the building owned by Hilfiger, there was no change of ownership within the meaning of section 60. I would affirm the trial court's judgment.

VOGEL, J.