



Practice Update

California Supreme Court Affirms Transfer Tax on Entity Control Change

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California allows cities and counties to impose a tax on certain real estate transfers at a rate of 0.11 percent of the sales price. Los Angeles County enacted an ordinance to impose the tax on transfers within the county. Recently, the county took the position that a change of control of an entity holding real property in the county constituted a taxable transfer of the underlying real property. The California Supreme Court recently agreed, setting the stage for cities and counties throughout the United States to adopt a similar approach.

The factual background of the case of *926 North Ardmore Avenue, LLC v. County of Los Angeles* involved a series of deeds and transfers of entity interests. However, the ultimate fact was that the limited liability company held real property, and beneficial interests in the trusts that controlled the company, were sold causing a change of control of that entity. A change of control requires taxpayers to notify the state. That notification is used by local property appraisers to reassess the property so that the valuation increase caps contained in Proposition 13 can be reset and a new baseline established. Using the information in that notice, Los Angeles County imposed a transfer tax.

The taxpayer challenged the imposition of the tax and the case ultimately ended up in California's Supreme Court. The court reviewed the state statute, the county ordinance, the Federal Stamp Tax (now repealed) upon which the statute and ordinance were modeled, and a host of stamp tax decisions from various courts. In its decision, the Court reasoned, "Combining all of these principles, we conclude that the critical factor in determining whether the documentary transfer tax may be imposed is whether there was a sale that resulted in a transfer of beneficial ownership of real property... Thus, we agree with the Court of Appeal's conclusion. Section 11911 permits the imposition of a documentary transfer tax whenever a transfer of an interest in a legal entity results in a change in ownership of real property..."

Based upon this case, it is highly likely that other cities and counties will take a similar approach and begin imposing tax on entity transfers in their respective jurisdictions. The decision was not predicated upon the fact that the entity in question only held real estate. Theoretically, a change of control of any entity that happens to own real estate in the applicable county could be taxable. Practitioners and real estate investors that deal with the sale of businesses that own property in California should check to see if there is a taxing ordinance in the city or county where the property is located, and whether or not that jurisdiction is following the *Ardmore* approach.

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