NO. S222329

IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

926 NORTH ARDMORE AVENUE, LLC,
Plaintiff and Appellant,

v.

COUNTY OF LOS ANGELES,
Defendant and Respondent

After a Decision by the Court of Appeal,
Second Appellate District, Division Seven, Case No. B248536
Los Angeles County Superior Court, No. BC 476670
The Honorable Rita Miller, Judge Presiding

APPLICATION FOR PERMISSION TO FILE *AMICUS CURIAE* BRIEF and BRIEF OF *AMICUS CURIAE* COUNCIL ON STATE TAXATION IN SUPPORT OF PLAINTIFF AND APPELLANT

Pillsbury Winthrop Shaw Pittman LLP
KEVIN M. FONG #91037
JEFFREY M. VESELY #67895
KERNE H.O. MATSUBARA #178895
Four Embarcadero Center, 22nd Floor
San Francisco, CA 94111
Telephone: (415) 983-1000

Attorneys for *Amicus Curiae* Council On State Taxation

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To The Honorable Chief Justice Cantil-Sakauye And Associate Justices Of The California Supreme Court:

Pursuant to California Rules of Court, Rule 8.200(c), the Council On State Taxation ("COST") respectfully requests permission to file the attached brief as *amicus curiae* in support of Plaintiff/Appellant 926 North Ardmore Avenue, LLC ("Ardmore"). Pursuant to Rule 8.520(f) of the California Rules of Court, COST states that (1) there is no party in the pending appeal who authored the proposed *amicus* brief in whole or in part; (2) there is no party or counsel for any party who made a monetary contribution intended to fund the preparation or submission of the brief; and (3) no other person or entity, other than the *amicus curiae* or its counsel, made a monetary contribution intended to fund the brief.

INTEREST OF *AMICUS*

COST is a nonprofit trade association based in Washington, D.C. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities. This is a mission COST has steadfastly maintained since its inception.

Today COST has grown to an independent membership of nearly 600 of the largest corporations engaged in interstate and international business representing a diverse range of multijurisdictional companies doing business in every state. COST members represent the part of the nation's business sector that is most directly affected by state taxation of interstate and international business operations. Thus, COST is very interested in cases such as this case that present issues significantly affecting the interpretation of the states' tax laws. COST members employ a substantial number of California residents, own extensive property in California, and conduct substantial business in California.

As *amicus*, COST has participated in several significant United States Supreme Court and state tax cases for over 40 years. COST's history of engaging in state and national arenas on state and local taxing powers in the context of our federal system, and our distinctive status representing the taxpayers most directly impacted by state and local efforts to unfairly tax business operations, gives COST the ability to provide a unique perspective to the Court.

Counsel for COST has reviewed the briefings submitted to this Court by the parties to date, and has determined it is important for COST to comment in this matter. COST's *amicus curiae* brief provides missing context and analysis from a national perspective, which is critical to an informed understanding of the history of California's application of its

documentary transfer tax system–separate and apart from its *ad valorem* tax system.

The issue in this case that most concerns COST's membership is Los Angeles County expanding the documentary transfer tax to encompass not only transfers or conveyances of real property, but also transfers of interests in legal entities that own real property. This change alters the way the documentary transfer tax has been administered and understood for nearly 50 years. Moreover, in making this determination, the Court of Appeal erroneously relied on change of ownership rules that apply only to *ad valorem* tax administration, not to the administration of the documentary transfer tax.

The rules of one tax system cannot be haphazardly applied to another tax system. Doing so, without the appropriate legislative action, will, at a minimum erode confidence in tax administration, deterring taxpayer compliance. COST's *amicus curiae* brief will provide this Court with the additional context and analysis critical to an informed decision on the matters at issue in this case.

Therefore, COST respectfully requests permission to file the attached *amicus* brief.

DATED: October 2, 2015.

Respectfully submitted,

PILLSBURY WINTHROP SHAW
PITTMAN LLP
KEVIN M. FONG
JEFFREY M. VESELY
KERNE H.O. MATSUBARA

By: Kevin M. Fong
Kevin M. Fong

BRIEF OF *AMICUS CURIAE*

THE COUNCIL ON STATE TAXATION IN SUPPORT OF PLAINTIFF AND APPELLANT

INTRODUCTION

The federal Stamp Act, which imposed a federal tax on the transfer or conveyance of real property, was repealed by Congress in 1965. However, the effective repeal date was delayed until January 1, 1968 to provide states the opportunity to enact their own versions of the act. The California legislature responded by implementing the Documentary Transfer Tax Act of 1967 ("DTTA"), codified in Revenue and Taxation Code § 11901, *et seq*. The DTTA authorized the counties and cities to impose a documentary transfer tax on "each deed, instrument, or writing by which . . . realty sold" is conveyed. As the title suggests, the DTTA is only a tax on the documents that convey realty.

The main issue in this case is whether the County of Los Angeles documentary transfer tax can be imposed on a change in ownership of a legal entity that holds title to real property. The County of Los Angeles alleges that the documentary transfer tax is imposed when an owner of more than fifty percent of a partnership interest ("BA Realty") transfers her partnership interest to two other trusts. BA Realty did not hold title to the real property at issue in this case, but owned North Ardmore, the entity which held title to the real property in question. Even though title to the

real property was never transferred, the County of Los Angeles imposed the documentary transfer tax on North Ardmore. The Court of Appeal upheld the imposition of the documentary transfer tax, relying on "change of ownership" rules found in the *ad valorem* tax statute,[1] not in the DTTA.

In doing so, without a legislative change, the Court of Appeal expanded the documentary transfer tax far beyond its historic scope. The Court of Appeal decision is the first published opinion in California holding the DTTA applies to transfers of interests in legal entities. The decision departs from nearly 50 years of utilization of the DTTA during which the transfer tax has only been applied to the transfer of real property, including some long-term leases. The DTTA has not applied to transfers of interest in legal entities that own real property merely because the ownership change impacts how the property will be valued for *ad valorem* tax purposes.

ARGUMENT

I. THE COURT OF APPEAL ERRONEOUSLY EXPANDED THE DOCUMENTARY TRANSFER TAX TO INCLUDE TRANSFERS OF INTERESTS IN LEGAL ENTITIES OWNING REALTY

Since its enactment by the California legislature in 1967, the DTTA has authorized cities and counties by ordinance to impose a tax upon the

[1] Revenue and Taxation Code § 64.

documents by which real property is transferred or conveyed. Revenue and Taxation Code § 11911 provides:

> *[O]n each deed, instrument, or writing by which any lands, tenements, or other* ***realty sold*** *within the county shall be granted, assigned, transferred, or otherwise conveyed to, or vested in, the purchaser or purchasers, or any other person or persons, by his or their direction, when the consideration or value of the interest or property conveyed (exclusive of the value of any lien or encumbrance remaining thereon at the time of sale) exceeds one hundred dollars ($100) a tax at the rate of fifty-five cents ($0.55) for each five hundred dollars ($500) or fractional part thereof.*

(Emphasis added.).

The County of Los Angeles has adopted the DTTA language verbatim in Los Angeles County Code § 4.60.020.

The plain language of § 11911 makes clear it only authorizes the DTTA to be imposed on documents by which "realty sold" is "granted, assigned, transferred or otherwise conveyed...." It does not impose a tax on transfers of interests in legal entities that directly or indirectly own realty.

The unambiguous meaning of the statute is buttressed by its legislative history and close connection to the nearly identical Federal Stamp Act (Former 26 U.S.C. §§ 4361, 4363). In 1967, the California legislature enacted the DTTA and patterned it after the Federal Stamp Act on conveyances of real estate. "Because section 11911 was patterned after the former federal act and employs virtually identical language as that act,

we must infer that the Legislature intended to perpetuate the federal administrative interpretations of that federal act." (*Thrifty Corp. v. County of Los Angeles* 210 Cal.App.3d 881, 884 (1989).)

The Court of Appeal's selective use of the canons of statutory interpretation was erroneous. The Court of Appeal cites the canon of *expressio unius est exclusio alterius* – which instructs that when the Legislature enumerates an object of legislation, any objects omitted are purposefully excluded – for the notion that the exception to the DTTA under § 11925 does not apply to North Ardmore. *See Clark v. Burleigh,* 4 Cal. 4th 474, 489 (1992). However, the Court of Appeal fails to apply the very same canon to § 11911 itself.

Former Internal Revenue Code § 4361 necessarily excluded transfers of legal entities and other similar transfers because those were subject to the federal stamp tax under wholly separate sections (*e.g.,* transfers of stock under I.R.C. § 4321, transfers of notes of indebtedness under I.R.C. § 4331, etc.). The California legislature chose only to adopt legislation modeled on § 4361, and not the other federal provisions. Unsurprisingly then, as with its federal counterpart, the DTTA only specifically applies to real estate-related "deeds," "instruments," etc. This principle therefore strongly underscores the California legislature's intent to impose the tax on the documents that transferred realty, not on changes of ownership interests in legal entities that own realty.

Additionally, Revenue and Taxation Code § 11911 is almost identical to former 26 U.S.C. § 4361 of the Stamp Act, which was repealed in 1967. Federal cases interpreting former 26 U.S.C. § 4361 found the tax only to apply "when the property is sold" and not when there is no transfer of title. *Berry v. Kavanagh*, 137 F.2d 574 (6th Cir. 1943).

Furthermore, since the DTTA's implementation in 1967, the California legislature has had nearly a half century to expand the scope of the documentary transfer tax to encompass changes of ownership in legal entities, but has chosen not to do so. The County of Los Angeles should not be allowed to overstep the Legislature's purview and enact its own rules extending the scope of the DTTA beyond its original intent. "[C]ourts, in interpreting statutes levying taxes, may not extend their provisions, by implication, beyond the clear import of the language used, nor enlarge upon their operation so as to embrace matters not specifically included." *Edison California Stores, Inc. v. McColgan*, 30 Cal. 2d 472, 476 (1947).

Instead of basing its decision on the solid foundation of the DTTA's legislative history and close connection to the provisions of the Federal Stamp Act relating to an almost identical documentary transfer tax, the Court of Appeal reached forward in time to ground its decision on provisions contained in the codification of Proposition 13 (specifically, Revenue and Taxation Code § 64), which, ironically, was intended to *restrain* the growth of state and local property taxes, not to significantly

expand the scope of a completely different tax (the DTTA) enacted more than a decade earlier.

The Court of Appeal, basing its decision on a misreading of *Thrifty Corp. v. County of Los Angeles*, 210 Cal.App.3d 881, concluded that "realty sold" was equivalent to a "change in ownership" for property tax purposes under Rev. & Tax Code § 64, *ipso facto* triggering transfer tax. (North Ardmore, Slip Op. at 21-22.) The flaw in the Court's analysis is that *Thrifty* did not hold in all instances a "change in ownership" of real property for property tax purposes is "realty sold" for transfer tax purposes, as required by § 11911. The issue in *Thrifty* was whether a 20-year lease of property with a ten-year option triggered transfer tax under § 11911. This issue was raised because leases generally did not trigger the federal stamp tax on conveyances of real property. (*Thrifty*, at p. 884.) However, a lease was subject to stamp tax "when it was of sufficient duration to approximate an interest such as an estate in fee simple or a life estate." *Id.*

With respect to a lease, "change in ownership" rules became an analytical framework for the *Thrifty* Court to determine whether the terms of a lease constituted adequate longevity to approximate a fee interest in real property and, therefore, "realty sold" subject to the documentary transfer tax. "In the present case 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.'" (*Thrifty,* at p. 885.)

The proposition in *Thrifty* therefore has no bearing here. The *Thrifty* Court did not conclude a transfer of stock or other interests in a *legal entity* constitutes a conveyance or transfer of *land* under § 11911. *Thrifty* "held that the phrase 'realty sold' used in § 11911 includes leaseholds of 35 years or more, including renewal options." (*McDonald's Corporation v. Board of Supervisors of Mendocino County,* 63 Cal.App.4th 612, 615 (1998).)

The Court of Appeal's reading of *Thrifty* as *carte blanche* to borrow concepts from other taxing regimes is dangerous to California tax policy and to the California fisc. Each different tax system in California relies on its own unique taxing structure and definitions. Borrowing concepts from one system and importing them into another can, therefore, have unintended results. The language and operation of one tax system reflects the Legislature's careful policy balances for that system and that system alone. Such is the case for the DTTA.

The DTTA only authorizes the imposition of tax on instruments conveying or transferring "land or other realty sold;" it does not authorize a tax on the transfer of the stock or other ownership interests in a legal entity that owns real property. Whether the DTTA should be expanded to include transfers of interests in legal entities that own real property is a policy question for the Legislature, not an interpretative question for the judiciary.

II. ANY EXPANSION OF THE DTTA MUST BE IN CONFORMITY WITH CALIFORNIA'S CONSTITUTION

In November 1996, California voters made it clear that many changes to expand the local tax base were subject to voter approval. *See* Legislative Analyst's Office, "Understanding Proposition 218", December, 1996.[2] The County of Los Angeles is attempting to circumvent the requirement that "[n]o local government may impose, extend, or increase any general [or special] tax unless and until that tax is submitted to the electorate and approved by a majority [or two-thirds] vote." *See* Cal. Const., art. XIII C, § 2.[3] As addressed above, given that the DTTA has been in place for almost half century in California, it is inappropriate for tax administrators, without going through the appropriate legislative process, to extend the scope of the DTTA.

Moreover, the change being made by the County is a significant extension of the tax base. A whole new class of transactions – sales of interests in business entities that own real property – heretofore not subject to the DTTA – are now within the scope of the transfer tax. This Court

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[2] Available at: http://www.lao.ca.gov/1996/120196_prop_218/understanding_prop218_1296.html.

[3] Amicus notes that Cal. Const., art. XIII D § 3 also imposes limitations on a local government's taxing powers and is at issue in litigation pending in the City and County of San Francisco. *See Hart Foundry Square IV, LLC v. City and County of San Francisco and Does 1 Through 10,* Case No. CGC-14-541722 (filed 9/18/14).

needs to make clear to local tax administrators that they cannot expand their tax base merely by posting a bulletin on a website as was done in this case. (*North Ardmore,* Slip Op. at p. 6.) Rather, they must follow the appropriate legislative process in order to extend the DTTA tax base. Expanding the DTTA to apply to situations where there is not a transfer of ownership interest in the realty, but merely a change in ownership of the legal entity owning the realty, is a policy decision that California law does not put in the hands of tax administrators. Rather, such an expansion must go through the legislative process.[4]

That the DTTA solely applies to transfers in realty and not mere changes in ownership of the legal entity owning the realty is also very consistent with the reasons why Proposition 13 and Proposition 218 were passed by California's voters. Proposition 13's purpose is clear in its title, "People's Initiative to Limit Property Taxation." It would produce an absurd result to allow tax administrators to use a constitutional amendment meant to *limit* the growth in *ad valorem* taxes to *increase* taxation under the DTTA. It would also seriously undermine the protections the voters sought when they approved Proposition 218 to require more local taxes to be subject to voter approval.

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[4] Proposition 218 also requires such change to be submitted to the electorate for approval.

Lastly, the County's attempt to raise an issue with Revenue and Taxation Code § 11925, amended by Senate Bill No. 816 and Assembly Bill No. 563, is a red herring. While subsection (b) of § 11925 provides for a constructive conveyance of title to realty when there is a termination of a partnership within the meaning of § 708 of the Internal Revenue Code of 1986, this is not applicable to the facts at hand. BA Realty did not terminate its ownership interest.[5] Merely providing the County with access to more information about when there is a change in control of an entity, as required by law, does not change the incidence of the transfer tax under § 11911.

CONCLUSION

For these reasons, the Court of Appeal decision should be reversed and the Plaintiff/Appellant should be entitled to a refund of its erroneously paid transfer tax.

Dated: October 2, 2015

Respectfully submitted,

PILLSBURY WINTHROP SHAW
PITTMAN LLP
KEVIN M. FONG
JEFFREY M. VESELY
KERNE H.O. MATSUBARA

By Kevin M. Fong
Kevin M. Fong

[5] *See* Plaintiff/Appellant Br. On the Merits 55. Additionally, this issue was not properly preserved by the County.

CERTIFICATE OF COMPLIANCE

Pursuant to California Rules of Court, 8.520(c), I hereby certify that the this *amicus curiae* brief is using 13-point type, and, according to the word count of the computer program used to prepare this brief, contains 3,390 words (including footnotes).

October 2, 2015.

Kevin M. Fong

Docket No. S222329

PROOF OF SERVICE BY MAIL

I, David A. Kramlick, the undersigned, hereby declare as follows:

1. I am over the age of 18 years and am not a party to the within cause. I am employed by Pillsbury Winthrop Shaw Pittman LLP in the City of San Francisco, California.

2. My business and mailing address is Four Embarcadero Center, 22nd Floor, San Francisco, CA 94111.

3. I am familiar with Pillsbury Winthrop Shaw Pittman LLP's practice for collection and processing of correspondence for mailing with the United States Postal Service; in the ordinary course of business, correspondence placed in interoffice mail is deposited with the United States Postal Service with first class postage thereon fully prepaid on the same day it is placed for collection and mailing.

4. On October 2, 2015, at Four Embarcadero Center, 22nd Floor, San Francisco, CA 94111, I served true copies of the attached document titled APPLICATION FOR PERMISSION TO FILE AMICUS CURIAE BRIEF and BRIEF OF AMICUS CURIAE COUNCIL ON STATE TAXATION IN SUPPORT OF PLAINTIFF AND APPELLANT by placing them in addressed, sealed envelopes clearly labeled to identify the persons being served at the addresses shown below and placed in interoffice mail for collection and deposit in the United States Postal Service on that date following ordinary business practices:

[See Attached Service List]

I declare under penalty of perjury that the foregoing is true and correct. Executed this 2nd day of October, 2015, at San Francisco, California.

David A. Kramlick

SERVICE LIST

Lemoine Skinner, III
FisherBroyles, LLP
1334 8th Avenue
San Francisco, CA

Daniel M. Kolkey
Julian Wing-Kai Poon
Lauren Margaret Blas
Gibson Dunn & Crutcher LLP
555 Mission Street, Suite 3100
San Francisco, CA

Attorneys for Plaintiff and Appellant 926 Ardmore Avenue

Albert Ramseyer
John F. Krattli
Office of the County Counsel
648 Kenneth Hahn Hall of Administration
500 West Temple Street
Los Angeles, CA

Attorneys for Defendant and Respondent County of Los Angeles

Neil D. Kalin
June Barlow
Jenny Yichhieh Li
California Association of Realtors
525 South Virgil Avenue
Los Angeles, CA

Attorneys for Amicus Curiae California Association of Realtors

California Court of Appeal
Second Appellate District
Division 7
300 S. Spring Street
Los Angeles, CA 90013

Superior Court of California
County of Los Angeles
Central Civil West Courthouse
600 South Commonwealth Avenue
Los Angeles, CA 90005