SUPREME COURT COPY

No. S222329

IN THE SUPREME COURT OF CALIFORNIA

926 NORTH ARDMORE AVENUE, LLC,

Plaintiff and Appellant

v.

COUNTY OF LOS ANGELES,

Defendant and Respondent.

SUPREME COURT
FILED

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After A Decision By The Court Of Appeal,
Second Appellate District, Division Seven, Case No. B248356
Los Angeles County Superior Court, No. BC 476670
The Honorable Rita Miller, Judge Presiding

926 NORTH ARDMORE AVENUE, LLC'S ANSWER BRIEF TO THE AMICI CURIAE BRIEF OF COUNTY OF TEHAMA ET AL.

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I. INTRODUCTION

The amici curiae brief of Tehama County and fourteen other counties, and various clerks, assessors, or recorders of those counties (collectively, the "Counties") boils down to two related contentions: (1) this Court should interpret the Documentary Transfer Tax Act ("DTTA") to cover "new transactional forms" in light of "[t]he economic reality of such transactions" in order to avoid "[p]etrify[ing] California's transfer tax system . . . circa 1967" (Counties' Amici Brief ("CAB"), pp. 1, 4); and (2) a conveyance of "realty sold" under the DTTA should be interpreted the same as "change in ownership" under Proposition 13's statutory scheme because the two statutory schemes are closely related (*id.*, pp. 16, 19-20) and such an interpretation would serve the DTTA's revenue-raising purpose (*id.*, p. 3) and avoid a "regressive" tax (*id.*, p. 1).

But the Counties' desire to cover "new transactional forms" is not a ground for disregarding the DTTA's statutory language and legislative intent. "The fundamental task of statutory construction is to 'ascertain the intent of the lawmakers so as to effectuate the purpose of the law.'" (*People v. Cruz* (1996) 13 Cal.4th 764, 774-775.) And here, it is settled that "the Legislature intended to perpetuate the federal administrative interpretations of [the] federal [Stamp A]ct." (*Thrifty Corp. v. County of Los Angeles* (1989) 210 Cal.App.3d 881, 884 (*Thrifty*).) Those federal interpretations consistently applied the documentary transfer tax to conveyances of *realty*, not transfers of ownership

in *legal entities that hold realty*. (See Ardmore's Opening Brief on the Merits ("OBM"), pp. 25-26, 33-35; Reply Brief on the Merits ("RBM"), pp. 7-9, 11-14.) Indeed, the Counties themselves acknowledge that "the parties have been unable to unearth any contemporary Stamp Tax precedents addressing anything remotely resembling the transaction under review here." (CAB, p. 6.) Instead, when a law must be adapted to new circumstances, democracies amend statutes; the courts do not usurp that role, given that only legislatures are equipped to hold the hearings that can evaluate the impact of a tax law's expansion. (E.g., *People v. Prescott* (2013) 213 Cal.App.4th 1473, 1478.)

Likewise, the Counties' suggestion that a conveyance of "realty sold" under the DTTA should be interpreted the same as a "change in ownership" under Proposition 13's statutory structure fails on multiple grounds that go to the core of statutory construction: (1) The Legislature could hardly have intended to interpret the DTTA pursuant to a standard that did not exist at the time of the DTTA's enactment a decade earlier; (2) the phrase "realty sold" is not similar to the phrase "change in ownership" such that it should be given the same meaning (see OBM, pp. 39-43); (3) Proposition 13 creates a *constitutional constraint* against construing a statute to dramatically extend its tax to "new transactions" beyond that which was understood at the time of the statute's enactment (*id*., pp. 43-46, 49-50); (4) "[i]n case of doubt," tax statutes should be construed "to favor the taxpayer rather than the government" (*Edison Cal. Stores, Inc. v. McColgan* (1947) 30 Cal.2d 472, 476 (*Edison*)),

and not construed to favor the generation of more revenue; and (5) since the documentary transfer tax is calculated based on the value of the particular realty transferred, the tax is not regressive.

However, one of the most fundamental obstacles to the Counties' effort to interpret the DTTA to expand its reach to a new set of transactions is that Proposition 13 embodies a constitutional prohibition against "new ad valorem taxes on real property, or sales or transaction taxes on the sales of real property." (Cal. Const., art. XIIIA, § 3, subd. (a).) To construe the DTTA beyond the federal interpretations that it was intended to codify would circumvent the voters' mandate against new transaction taxes on the sale of real property. Indeed, in its contemporaneous analysis of Proposition 13 for the Legislature in 1978, the Legislative Analyst advised that "[a]n extension of the existing documentary transfer tax ... probably would be prohibited" by Proposition 13. (Legis. Analyst, Analysis of Proposition 13, The Jarvis-Gann Property Tax Initiative (1977-1978 Reg. Sess.) p. 42 [Ardmore's Motion for Judicial Notice, Exh. F, p. 91].) The courts cannot interpret a law to extend it beyond that which the Legislature is authorized to enact.

Significantly, if the Counties' view of statutory interpretation were to govern, laws would be little more than policy statements.

II. THE COUNTIES' INTERPRETATION OF THE DTTA TO CONFORM TO "ECONOMIC REALITY" IGNORES FUNDAMENTAL PRINCIPLES OF STATUTORY CONSTRUCTION.

A. A Statute's Plain Meaning And Legislative Intent Must Control Over "Economic Reality."

The Counties argue that Revenue and Taxation Code section 11911[1] authorizes a county to impose a documentary transfer tax based on a change in ownership of a legal entity that directly or indirectly owns property in light of "[t]he economic reality of such transactions." (CAB, p. 4.)

But economic reality does not trump statutory language and statutory intent. In interpreting a statute, this Court's fundamental task is to "ascertain the intent of the Legislature so as to effectuate the purpose of the law." (*Preston v. State Bd. of Equalization* (2001) 25 Cal.4th 197, 213.) And "[i]n interpreting a statute ... statutory language typically is the best and most reliable indicator of the Legislature's intended purpose." Only if the language remains ambiguous after considering the text and statute's structure does the court "look to various extrinsic sources, such as legislative history, to assist ... in gleaning the Legislature's intended purpose." (*Larkin v. Workers' Comp. Appeals Bd.* (S216986, Oct. 26, 2015) __ Cal.4th__, slip opn., pp. 5-6; see OBM, p. 17.)

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[1] All statutory references are to the Revenue and Taxation Code unless otherwise indicated.

Neither the text nor the practice under section 11911 covers a "writing" by which "a change in ownership" of realty has been effectuated. Instead, as demonstrated in the opening brief, the text of section 11911 provides for a tax to be imposed only "on each deed, instrument, or writing by which any lands, tenements, or other realty sold ... shall be granted, assigned, transferred, or otherwise conveyed to ... the purchaser." (§ 11911, subd. (a).) The neighboring statutory provisions in the DTTA also confirm that documents directly conveying realty, not the conveyance of *interests in entities* that indirectly hold realty, are what are subject to a tax under the Act. For example, section 11911.1 authorizes a city or a county to require a writing by which realty is conveyed to note the tax roll parcel number. And section 11932 requires the writing to show the location of the realty on the document's face. This would not make sense for documents that transfer interests in legal entities. (OBM, pp. 31-33.)

And as noted by the amicus brief of the California Taxpayers Association, the DTTA envisioned that the vast majority of writings under the DTTA would be recorded and thus that the tax would be paid at the time of recordation. That accounts for the fact that there is no penalty or interest imposed for non-payment because the remedy for non-payment is the refusal

to record. (California Taxpayers Association Amicus Brief, pp. 9-12, citing section 11933.)[2]

B. The DTTA Was Enacted To Perpetuate The Federal Administrative Interpretations Of The Federal Stamp Act.

As discussed in the opening brief, it is settled that "the Legislature intended to perpetuate the federal administrative interpretations of [the] federal [Stamp A]ct" when it enacted section 11911 of the DTTA. (*Thrifty, supra,* 210 Cal.App.3d at p. 884; OBM, pp. 33-37.) And the federal administrative interpretations of that tax never extended it to any writings other than those that directly conveyed a form of realty. (OBM, pp. 25-26.)

The Counties, however, contend that the interpretation of the federal Stamp Act, on which the DTTA is patterned, "provide[s] a starting point, but d[oes] not dictate the outcome" and that the court in *Thrifty* "explicitly declined to adopt the federal analysis ... but instead looked to California's property tax statutes." (CAB, p. 15.)

However, *Thrifty, supra*, 210 Cal.App.3d 881, 884, acknowledged that because "section 11911 was patterned after the former federal [Stamp] [A]ct and employs virtually identical language as that act, [courts] must infer that

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[2] Los Angeles County argues that "other taxing schemes leave it to local agencies to create a collection structure without difficulty." (Consolidated Answer to Amicus Curiae Briefs Supporting Appellant, p. 3.) But the statutes cited there—Revenue and Taxation Code sections 7284, 7283, and 7283.51—all authorize the enactment of collection structures. No such collection structure is authorized in the DTTA.

the Legislature intended to perpetuate the federal administrative interpretations of that federal act." (See OBM, pp. 34-36; RBM, pp. 19-21.) Thus, *Thrifty*'s analysis *looked first* to "regulations interpreting the former federal act" (*Thrifty, supra*, 210 Cal.App.3d at p. 884) and *followed* those federal regulations to analyze whether the conveyance of the 20-year lease in that case could be considered "realty sold." (See *ibid.*) *Thrifty* turned to state law only because it could not find adequate federal guidance as to whether a 20-year lease with a 10-year option to renew constituted "realty sold" under section 11911. (*Id.* at p. 886.)

Although the Counties initially claim that "[w]hat constitutes 'lands, tenements, or other realty' is determinable by the law of the State in which the property is situated," they appropriately recognize that former 26 C.F.R. section 47.4361-1(a)(3), which interpreted the federal Stamp Act, provided, "For purposes of the tax imposed by section 4361, the determination of what constitutes 'realty' is not controlled by the definition or scope of that term under State law. State law determines the character of the rights conveyed by an instrument, but whether such conveyance constitutes a conveyance of 'realty' is to be determined under Federal law." (CAB, p. 14, fn. 25, quoting former 26 C.F.R § 47.4361-1(a)(3) [2CT242, 305].) Thus, what constitutes a conveyance of realty under the DTTA is governed by the federal administrative interpretations, not the Proposition 13 statutory regime.

Finally, citing *People By and Through Dept. of Public Works v. Santa Clara County* (1969) 275 Cal.App.2d 372 (*Public Works*), the Counties argue that "the California courts made clear that although the taxability inquiry might start with federal law, it could not end there." (CAB, p. 14.) But *Public Works* did not expressly address the issue whether federal or state law should be followed, and cases are not authority for propositions not considered. (*McDowell & Craig v. Santa Fe Springs* (1960) 54 Cal.2d 33, 38.) In any event, the decision in *Public Works, supra*, 275 Cal.App.2d 372, conformed with federal law. It involved a forced *sale* of *realty* effected by court order, concluded that a "final order of condemnation" was an instrument within the meaning of section 11911 (*id.* at p. 377), but declined to impose the documentary transfer tax because "the State, for whose benefit the instrument is made, is not liable for the tax pursuant to . . . section 11922 which exempts the State from payment" (*id.* at p. 379). The court observed that "the federal government never applied the tax to conveyances by condemnation" either. (*Id.* at p. 374, fn. 3.)

In sum, the DTTA should be construed to "perpetuate the federal administrative interpretations of [the] federal [Stamp A]ct" (*Thrifty, supra*, 210 Cal.App.3d at p. 884), and no case prior to the decision at issue here has ruled otherwise.

C. The Authorities Cited By The Counties Do Not Demonstrate The "Evolutionary" Nature Of The DTTA, But Consistently Adjudicated Whether The Transaction Constituted The Sale Of Realty.

The Counties claim that various cases and revenue rulings "clearly show the flexibility and adaptability of the Stamp Tax to accommodate new and different types of real property transactions." (CAB, p. 9.)

But each of these examples affirms that the DTTA and its federal predecessor have been consistently applied only to different types of real property *interests* (CAB, p. 9), where they approximate a fee simple interest in realty. Indeed, the Counties acknowledge that "[t]he available authorities ... are ... striking in the fact that none of them even remotely resembl[e] the [transaction] at issue here." (*Ibid.*) This, in fact, disproves the Counties' conclusions regarding the adaptability of the DTTA to the transaction here.

The Counties claim that "[c]ontemporary federal authorities showed ... attention to economic reality when determining the scope and application of the Stamp Tax." (CAB, p. 11.) In fact, none of these decisions were made on the basis of economic reality; rather, they were premised on the plain language of the federal Stamp Act. For instance, in *Berry v. Kavanagh* (6th Cir. 1943) 137 F.2d 574, 575, cited by the Counties at page 9 of their brief, the court noted that the federal Stamp Act is "an excise [tax] upon the privilege of selling lands, tenements or other realty" and that the "burden of the tax attaches when the property is sold." There, the court found that "the transaction was not a sale, but an agency agreement," and because the

acquiring party had "not yet received the beneficial title to the real estate," no tax should be imposed. (*Id.* at p. 576.)

Likewise, in *Berkeley Saving & Loan Assn. of Newark, N.J. v. United States* (D.N.J. 1969) 301 F.Supp. 22, 25-26, cited by the Counties at page 9 of their brief, the court conducted an "examination of the transaction being considered to see if there is a sale of realty" and found that the "transactions were not sales of realty" because the change in legal title was "for the purpose of security, and not for the purpose of sale."

Similarly, *United States v. Niagara Hudson Power Corp.* (S.D.N.Y. 1944) 53 F.Supp. 796, 801 (*Niagara Hudson Power*), did not apply the federal Stamp Act where there was "no conveyance of 'realty sold'... where a change of title to real estate is effected solely as a result of the filing of a Certificate of Consolidation" for a merger. Significantly, *Niagara Hudson Power* confirms that transfers of non-realty interests, in that case corporate stock, did not trigger the federal Stamp Act, even though realty was transferred as a result of the merger. (*Id.* at p. 798 [shares converted to those of acquirer].)

Citing *Socony-Vacuum Oil Co. v. Sheehan* (E.D. Mo. 1943) 50 F.Supp. 1010, 1012 (*Socony-Vacuum*), the Counties argue that "while the federal regulations and case law often spoke of conveyances transferring 'title' to real property, the authorities were quite clear that this meant functional ownership, rather than simply legal title." (CAB, p. 11.) But *Socony-Vacuum* found that no tax was owed where a parent company obtained title to wholly-owned

subsidiaries' realty upon acquisition of all of the subsidiaries' assets as a result of dissolution. Like *Niagara Hudson Power*, the court found there was no sale, and therefore no tax should be imposed. (*Socony-Vacuum, supra*, 50 F.Supp. at p. 1012.)

The Counties also claim that *United States v. Seattle-First National Bank* (1944) 321 U.S. 583 (*Seattle-First*), "looked to the economic reality of the transaction there to determine that the banks' realty had not been 'sold' in any meaningful sense." (CAB, p. 10.) Instead, the U.S. Supreme Court held that a statutory consolidation of banks, by which title to property and other assets passed to the consolidated entity, was not subject to the documentary transfer tax because the "realty was not conveyed to or vested ... by means of any deed, instrument or writing." (*Seattle-First, supra*, 321 U.S. at p. 590.) The high court specifically premised its decision on the language of the federal Stamp Act, stating that "[n]or can the realty be said to have been 'sold' or vested in a 'purchaser or purchasers' within the ordinary meaning of those terms." (*Ibid.*)

If statutory mergers involving the transfer of real estate from the disappearing corporation to the surviving or new corporation are not subject to the DTTA—notwithstanding the "economic reality" of such a transfer—then neither can the transfer of interests in a legal entity that holds realty, where no writing conveys title to that realty.

In sum, contrary to the Counties' spin, these cases each find that there was no "sale" of realty, as required by the plain language of the federal Stamp Act. They did not premise their decisions on the "economic reality" of the transactions, but instead on the statute's plain language.

Finally, the Counties argue that "[t]he adaptability of the Stamp Tax to cover evolving transactional forms is aptly demonstrated by examining the development of oil and gas 'production payments,' a type of interest in mineral rights that gained prominence in the 1950s and 1960s." (CAB, pp. 12-13.) The Counties argue that although "the IRS initially concluded that transfers of production payments were not taxable," the IRS reversed course in 1959 and concluded that the interests qualified as "realty." (CAB, p. 13.)

These authorities do not suggest that the federal Stamp Act's requirement of a conveyance of "realty sold" extends to the transfer of ownership of an *entity* holding realty. The memorandum of the IRS General Counsel, cited by the Counties, determined that "[a] production payment is the right to receive a specified share of future production from mineral property" and thus constituted an interest in realty. (GCM 37079 (April 5, 1977), attached as Exh. I to Counties' Mot. for Jud. Notice.) As the federal cases addressing carved-out oil-production payments observe, these payments "convey an interest in 'land, tenements, or other realty'" because they give the holder "'the right to sever and remove for all time from the underlying mineral

reserve all or a proportionate part of the mineral in place.'" (*Texaco, Inc. v. United States* (5th Cir. 1980) 624 F.2d 20, 22 & fn. 4; see RBM, pp. 11-12.)

In conclusion, under the federal Stamp Act, the federal courts determined what constituted a form of realty; they applied the statutory language and never applied the documentary transfer tax to a document that transferred interests in entities holding realty.

D. Changed Circumstances Justify Amending A Tax Statute, Not Judicially Expanding Its Interpretation.

The Counties argue that in 1967, the California Legislature could not have foreseen the need to add language to the DTTA in order to cover writings that conveyed interests in legal entities, like LLCs, that held realty. They argue that when the DTTA was enacted "corporations were the dominant form of business entity [fn.]—and both federal and state law ... severely disincentivized use of the corporate form for small businesses." (CAB, p. 5.) Likewise, they argue that S-corporations were only created in 1958 (to allow corporations to avoid double taxation) and that "high personal income tax rates hindered LLC expansion until the late-1980s." (*Id.*, pp. 6, 7.)

This does not advance the Counties' claim that the DTTA, as enacted in 1967, should be construed to cover writings that transfer control or ownership of entities holding realty.

First, at the time that section 11911 was first enacted in 1967, legal entities, including corporations and partnerships, held realty. The Counties

even acknowledge that corporations were well known at the time of the DTTA's enactment. Yet, the California Legislature decided not to enact that portion of the federal act imposing documentary transfer taxes on transfers of shares or certificates of stock (see former 26 U.S.C. § 4321 [1CT88]), reflecting the Legislature's deliberate decision to limit the tax to documents evidencing conveyances of realty.

Second, the purported fact that the Legislature saw no need in 1967 to impose a tax on instruments that transferred interests in entities holding property is no excuse for interpreting the DTTA to cover what the Legislature saw no need to impose. This merely demonstrates that new legislation is required if the DTTA is to be interpreted to impose a tax on writings that transfer ownership of legal entities that hold property.

"Courts properly have been reluctant to depart from an interpretation of tax law which has been generally accepted when the departure could have potentially far-reaching consequences. When a principle of taxation requires reexamination, Congress is better equipped than a court [to do so]." (*U.S. v. Byrum* (1972) 408 U.S. 125, 135.)

However, citing a 1964 federal advisory commission report, the Counties suggest that California did not adopt a documentary transfer tax on sales of stock, and limited the tax to conveyances of realty sold, because "very few stock transactions actually occurred in California." (CAB, p. 18, quoting

the advisory commission as saying "'almost 80 percent of the dollar value of stock transfers occurs in New York City.'")

The dollar value of stock transfers is both irrelevant and misleading. The fact that the Legislature was aware of such transactions, but decided not to cover them because the revenue raised purportedly would not be significant, does not alter the fact that the Legislature did not intend to cover transactions involving the sale of interests in corporations. It matters not why the transactions were not covered.

Second, the Counties distort the amount of the revenue benefit from a documentary transfer tax on sales of stock. The federal advisory commission report stated that "three-fourths of the Federal documentary tax revenue comes from the taxes on the issue and transfer of stocks and bonds" and that "States obtained $120 million, more than half of which came from New York State's stock transfer tax." (Counties' Motion for Judicial Notice, Exh. Q, pp. 2, 18.) This suggests that substantial revenue was available from such taxes. But whether the revenue was substantial or only significant, California's deliberate decision to adopt only those sections of the federal Stamp Act authorizing a transfer tax on documents conveying realty, and not those federal provisions applying the tax to the transfer of stock and certificates, indicates a deliberate choice to restrict California's DTTA to sales of realty. "In the construction of a statute ..., the office of the Judge is simply to ascertain and declare what is

in terms or in substance contained therein, not to insert what has been omitted." (Code Civ. Proc., § 1858; see OBM, pp. 20, 36.)

Finally, if new circumstances warrant extending the documentary transfer tax to transfers of control or ownership of entities holding realty, that is an argument for a legislative amendment, not an expansion of the reach of section 11911, assuming such an amendment conforms with the requirements of Proposition 13. Indeed, both Florida and New York have amended their documentary transfer tax legislation to cover new forms of conveyances. (N.Y. Local Law No. 71 (1986); 2009 Fla. Laws Ch. 2009-131, § 3(3) ["[I]t is the Legislature's intent by this act to impose the documentary stamp tax when the beneficial ownership of real property is transferred to a new owner or owners ... in combination with transfers of ownership of, or distributions from, artificial entities"].)[3]

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[3] California's Legislature attempted a similar amendment to extend section 11911, but the bill died in committee on January 31, 2014. That proposed bill's stated purpose was to "bring the Documentary Transfer Tax Act into conformance with the definition of 'realty sold' under California property tax law." (Ardmore RJN in Support of Ardmore's Reply Brief on the Merits, Ex. D [Assem. Com. on Local Gov't, analysis of Assem. Bill No. 561 (2013-2014 Reg. Sess.), as amended Apr. 30, 2013]; see RBM, pp. 22-23.) The bill's demise certainly does not support incorporating its text into the DTTA.

E. The Counties' "Economic Reality" Argument Creates Numerous Problems.

The Counties' "economic reality" argument that the DTTA should be expanded to impose taxes based on a change in ownership or control of a legal entity holding title to property also creates serious structural problems.

First, the Counties' "economic reality" argument is in tension with the fact that many tax statutes "employ[] relatively artificial, relatively self-contained, concepts." (*King v. State Bd. of Equalization* (1972) 22 Cal.App.3d 1006, 1010-1011.) The fact that tax laws often draw artificial distinctions (like taxing income over arbitrary levels at higher rates) cannot be used as an argument for ignoring them; otherwise, the statutory language of the tax laws would lose the virtue of predictability upon which transactional decisions must rely. (See California Society of Certified Public Accountants' Amicus Brief, p. 12.) Because the DTTA and its federal predecessor have never been interpreted to apply to transfers of ownership or control of legal entities holding realty, the DTTA should not now be extended in contravention of the long-settled expectations of California residents. (*Ibid.*)

Second, the Counties' "economic reality" argument would appear to justify only the imposition of the tax on a writing that transfers ownership of a legal entity that holds a *single parcel* of property. In the Counties' view, entities could otherwise avoid the documentary transfer tax by having an entity hold title to realty (CAB, p. 27) and then transfer ownership of that entity,

even though "[e]very incident of control, possession, and practical value of the underlying real property vests in the entity's new owners with the stroke of the pen upon the transfer agreement." (*Id.*, p. 4; accord, *id.*, pp. 13, 25.)

But this "economic reality" argument does not apply to the transfer of ownership of a corporation or other entity that holds a vast portfolio of realty or a combination of realty and other assets. The transfer of ownership of those latter entities is not the effective conveyance of realty; it is the conveyance of a business enterprise with a portfolio of assets. Yet, there is no principled way, particularly in light of the DTTA's statutory language, to distinguish the transfer of entities that hold a single parcel from those holding a portfolio of assets that include realty. In that connection, the transfer of interests in BA Realty here involved a partnership that held a portfolio of securities, a minority interest in an LLC that owned real estate, and four LLC's that owned real estate, not merely the Ardmore apartment building. (See Answering Brief on the Merits ("ABM"), p. 18, citing Pl. Ex. 43[GWP000906].) Thus, the Counties' "economic reality" argument proves too much and would not even justify its application to this case.

Finally, the Counties' "economic reality" argument appears to be concerned with sham transactions, which are not at issue here. (See RBM, pp. 4-5.) Corporations and single-member LLCs pay franchise taxes for the privilege of existing as separate entities; thus, any tax-avoidance concern is diminished by the costs of forming and maintaining limited liability

companies and other non-partnership entities. (See RBM, p. 30.) In the absence of legislation or circumstances justifying the application of the step transaction, alter ego, or substance-over-form doctrines, their separate existence must be respected. "It is well established that corporate form is not to be disregarded for tax purposes unless the corporation is created for illegitimate purposes or conducts no business activities." (*Kleinsasser on Behalf of Kleinsasser v. United States* (9th Cir. 1983) 707 F.2d 1024, 1027.)

F. The Counties' Claim That The DTTA Should Be Expanded Because It Is "Regressive" Does Not Withstand Scrutiny.

Finally, the Counties claim that limiting the DTTA to writings that convey realty would create a "regressive" tax because "ordinary homeowners would almost universally pay the tax" but "corporate property owners would have an easy escape." (CAB, p. 28.)

First, numerous "everyday, ordinary homeowners" use LLCs and other ownership vehicles for residential property transactions. (California Association of Realtors Amicus Brief, pp. 2-4.) Thus, interpreting the DTTA so as not to reach LLCs and other corporate forms (except where provided in section 11925) is not regressive.

Second, while the documentary transfer tax is technically an excise tax, the tax is calculated based on the value of the property so that its imposition is not regressive: The lower the value of the property, the lower the tax. This is the opposite of a regressive tax, which is defined as a "tax structured so that

the effective tax rate decreases as the tax base increases." (Black's Law Dict. (10th ed. 2014) p. 1687.)

III. THE DTTA CANNOT BE INTERPRETED TO IMPOSE A DOCUMENTARY TRANSFER TAX BASED ON A CHANGE IN OWNERSHIP OR CONTROL OF A LEGAL ENTITY THAT HOLDS TITLE TO REALTY.

Aside from the "economic reality" argument, the Counties make some additional statutory arguments for the proposition that a conveyance of "realty sold" under the DTTA should be interpreted the same as a change in ownership under Proposition 13's statutory scheme. (CAB, p. 4.)

Ardmore's opening brief has already shown why such an interpretation is contrary to the statute's plain language, the legislative history, the rules of statutory construction, and the constraints of Proposition 13. It will not repeat those arguments here.

However, the Counties have made some specific arguments in support of their position that the DTTA should be interpreted to embrace changes in ownership under Proposition 13's statutory structure. Ardmore will respond to those arguments below.

A. The Counties Misapply The Doctrine Of *In Pari Materia.*

A major theme throughout the Counties' amici brief is that "from the very beginning, the Legislature has understood the close connection between the Documentary Transfer Tax and the property tax." (CAB, p. 1.) The Counties then claim that the DTTA and property tax statutes should be

construed *in pari materia* to apply Proposition 13's change-in-ownership standard to the DTTA. (*Id.*, pp. 19-20.)

Both the premise—that the documentary transfer tax and property tax involve the same purpose or object—and the application of the rule of construction, *in pari materia*, are wrong.

First, the Counties' authorities do not show that the DTTA and property tax laws involve the same purpose or object. Citing a 1939 memo from the Chief Counsel of the Bureau of Internal Revenue, the Counties argue that "the federal authorities themselves would look to state *property tax* law where relevant to determine whether a particular instrument effected a taxable sale of realty." (CAB, p. 16.) Yet, that memorandum did not look to "state property *tax* law." It merely looked to state law to determine that "an oil and gas lease ... does not constitute a conveyance of realty and is, therefore, not subject to stamp tax under section 3482 of the Internal Revenue Code." (Counties' Motion for Judicial Notice, Exh. J.) It does not stand for the proposition that the documentary transfer tax—an *excise* tax—is related to *property* tax.

The Counties next argue that an Advisory Commission on Intergovernmental Relations in 1964 "proposed ceding the transfer tax to the states" because "state and local governments relied heavily on the sales information generated by the transfer tax in the administration of their property tax systems." (CAB, p. 17.) But the cited pages of the advisory commission's report do not suggest that the transfer tax and property tax relate

to the same purpose or object: Those pages assert only that the documentary transfer tax "provide[s] an indication . . . of the price . . . paid for real estate," which is "useful to tax administrators concerned with the assessment of real estate for property purposes." (Counties' Motion for Judicial Notice, Exh. Q, p. 22.)

Yet, since the documentary transfer tax *excludes* the value of any lien or encumbrance remaining on the realty in calculating the tax (§ 11911, subd. (a)), the report acknowledged that the "stamp value frequently bears little relationship to actual selling price." (Counties' Motion for Judicial Notice, Exh. Q, p. 5.) This, too, does not suggest that the statutes governing the scope of the documentary transfer tax and the property tax should be construed together.

Having failed to establish their premise that documentary transfer taxes and property taxes involve the same subject or purpose, the Counties stretch the doctrine of *in pari materia* far beyond its appropriate use.

Two statutes are considered to be *in pari materia* when they "relate to the same person or thing, to the same class of person[s or] things, or have the same purpose or object." (*People v. Tran* (2015) 61 Cal.4th 1160, 1168.)

Here, the DTTA and property tax do not relate to the same thing since the DTTA is "an excise tax rather than a property tax." (*Fielder v. City of Los Angeles* (1993) 14 Cal.App.4th 137, 145.) Moreover, the DTTA and property tax do not have the same purpose or object—the former taxes *writings* that

convey realty sold; the latter assesses a tax for the privilege of *owning the property*. (*City of Huntington Beach v. Superior Court* (1978) 78 Cal.App.3d 333, 340.)

Also relevant to the inapplicability of the doctrine of *in pari materia* is that the documentary transfer tax and property tax statutes are found in separate divisions of the Revenue and Taxation Code, were enacted more than a decade apart, and have directly conflicting goals. (OBM, pp. 43-48.)

Additionally, even though each tax is calculated by multiplying a rate against the consideration or value of the property, the DTTA now makes clear that "the value of the property established for purposes of determining the amount of documentary transfer tax due *shall not be binding* on the determination of the value of that property for property tax purposes . . . ." (§ 11935; italics added.)

Finally, "[t]hough it is often presented as effectuating the legislative 'intent,' the related-statute canon [that is, *in pari materia*] is not, to tell the truth, based upon a realistic assessment of what the legislature actually meant. That would assume an implausible legislative knowledge of related legislation in the past, and an impossible legislative knowledge of related legislation yet to be enacted." (Scalia and Garner, Reading Law: The Interpretation of Legal Texts (2012), p. 252.) Instead, it is simply a canon to harmonize statutes so that they "make sense." (*Ibid.*) Given their different subjects, different

phrasing, and different purposes, no harmonization of documentary transfer taxes and property taxes is necessary.

Tellingly, the cases cited by the Counties apply the doctrine of *in pari materia* only in relation to statutes that are closely related, enacted closely in time, or that interpret the same word, phrase, or situation. For instance, in *Isobe v. Unemployment Insurance Appeals Board* (1974) 12 Cal.3d 584, 590-591, cited by the Counties at page 19, the court, applying *in pari materia*, determined that Unemployment Insurance Code sections 1334 and 1336 should be read together since section 1334 explicitly refers to section 1336 in its text, and both provisions relate to the time provided to appeal a determination on whether benefits would be provided to employees.

Estate of Jacobs (1943) 61 Cal.App.2d 152, cited by the Counties at page 19 of their brief, merely sought to harmonize competing statutes setting the priorities for charges against an estate to avoid interpreting the statutes in a manner that would result in an "unreasonable" or constitutionally questionable result. (*Id.* at pp. 157-158.)

In *Old Homestead Baker, Inc. v. Marsh* (1925) 75 Cal.App. 247, 260-261, also cited by the Counties on page 19, the court found that two taxation statutes relating to motor vehicles were *in pari materia*, where they were enacted by the *same* legislature and related to taxes (gas taxes and registration fees) paid by vehicle owners.

Finally, the Counties contend that "it would appear hard to argue that the 1967 Legislature *didn't* intend that the transfer tax be construed in light of the property tax." (CAB, p. 19.) To the contrary, it is impossible to credibly argue that the 1967 Legislature intended to construe the documentary transfer tax in light of the property tax scheme enacted over a decade later by Proposition 13. It is equally impossible to credibly argue that the DTTA should be construed to reach new transactions that convey the ownership of entities holding realty when the voters adopted Proposition 13 to constrain property taxes and prohibit "new ad valorem taxes on real property, or sales or transaction taxes on the sales of real property." (Cal. Const., art. XIIIA, § 3, subd. (a); see OBM, pp. 43-48.)

B. The Counties Misinterpret Section 11925 In Order To Support Their Interpretation Of Section 11911.

The Counties argue that the language of section 11925 "plainly reflects an underlying tax structure in which such 'transfer(s) of an interest in the partnership' would otherwise be taxable, but for these provisions" and that "this clearly supports a conclusion that other transfers of legal entity interests *may* be subject to tax, leaving only the question of *which* such transfers qualify." (CAB, p. 24.)

This argument ignores the legislative history of section 11925, particularly that of its federal predecessor, former 26 U.S.C. § 4383, upon which it is patterned. As shown in the opening brief, section 11925 was not an

exemption from the levy of a tax on transfers of interests in legal entities, as the Counties argue. Rather, it was a measure designed to address the anomalies arising from the then-existing "aggregate" approach to partnerships, which treated any change in a partnership's composition as a dissolution of the partnership, thereby transferring the underlying assets and thereby triggering the federal Stamp Act. (See OBM, pp. 28-29.) The enactment of section 11925's federal predecessor codified the Internal Revenue Service's adoption of an entity approach so as *not* to impose a tax unless there was a change in legal title resulting from the termination of the partnership. (See *id.*, p. 29.)

Indeed, the Counties quote the legislative history of section 11925's federal predecessor, which supports Ardmore's position. The Counties write that "[s]ection 4383 was added in 1958 to address 'a question as to whether [transfer] tax is presently imposed where there is merely a change of interests in the partnership and no change in legal title of real property.' [Citation.] The House Ways and Means Committee report explained that '[t]he Internal Revenue Service has taken the position that no tax is to be imposed until there is a change of legal title to the real property, irrespective of the changes of interests in the partnership. The Service position in the case of real property thus to a substantial degree follows the 'entity' approach for partnerships.' [Citations.]" (CAB, pp. 24-25, citing federal legislative history.)

While this supports Ardmore's position, the Counties claim that "Congress … opted to focus on the economic reality of such transactions,

avoiding taxation of 'minor changes in a partnership'" and enacted "a federal rule strikingly similar in concept and operation to our 'change in ownership' provisions" because section 11925 applies the tax to a sale of 50% or more of the total interest in partnership capital and profits within a 12-month period (that is, a "technical 'termination' of the partnership under Section 708 of the Internal Revenue Code"). (CAB, p. 25.)

This is creative spin, but legally wrong. Both section 11925 and its federal predecessor treated the termination of a partnership as the single event by which an entity holding realty could be deemed to have executed an instrument conveying all realty held by the partnership. (§ 11925; former 26 U.S.C. § 4383.) To claim that this limited exception, authorizing the imposition of a documentary transfer tax under section 11925, enacted a rule similar to the far-reaching "change in ownership" provisions under Proposition 13 ignores the limited statutory authorization under section 11925. And to claim that section 11925 implies a vast expansion of the documentary transfer tax to conveyances of ownership of entities when its *express* language broadly bars such taxes "by reason of any transfer of an interest in the partnership" (§ 11925, subd. (a)), with the limited exception of partnership terminations, affronts common sense.

Moreover, Internal Revenue Code section 708, 26 U.S.C. § 708 ("section 708") (which defines a continuing partnership for purposes of section 11925), and section 64 cannot be harmonized, which further evinces

that the DTTA was not intended to be read in conjunction with the property tax provisions of the subsequently enacted section 64.

Specifically, under section 708, a technical termination triggering the DTTA occurs if there is a transfer of 50 percent or more of partnership interests within a 12-month period. In contrast, under section 64, a change in ownership occurs if a person, directly or indirectly, *acquires over* 50 percent of the ownership interests of a legal entity, without regard to the time period over which this occurs.

As a result, a transfer of partnership interests under section 708 may be a technical termination triggering the DTTA, but not a change in ownership under section 64, and vice versa. For example, in *Ocean Avenue LLC v. County of Los Angeles* (2014) 227 Cal.App.4th 344, 351-352 (*Ocean Avenue*), the court found that there was no section 64 change in ownership over property held by an LLC where all of its membership interests were sold on a single day, but no one person or entity obtained, directly or indirectly, greater than a 50-percent interest in the underlying property. (*Ocean Avenue*, *supra*, 227 Cal.App.4th at pp. 346-347.) This same transaction would have triggered technical termination under section 708, though, because greater than 50 percent of the partnership interests were transferred within a 12-month period.

This contradictory outcome demonstrates that the Legislature never intended these disjointed statutes to be applied together for DTTA purposes. (See also Institute for Professionals in Taxation Amicus Brief, pp. 6-7.)

Indeed, these incoherent results occur in a number of factual scenarios, underscoring the unconnected nature of the DTTA and property tax statutes. (*Id.*, pp. 7-9.)

C. The Counties Cannot Use The 2009 And 2011 Enactments To Expand The Interpretation Of The DTTA.

Like the County of Los Angeles, the Counties rely on "more recent[] legislation" that purportedly "has confirmed the Legislature's intent that transfer tax liability ... attach[es] to changes in ownership and control of business entities that owned real property interests at the time they are taken over." (CAB, p. 20.) Citing Senate Bill No. 816 in 2009 and Assembly Bill No. 563 in 2011, the Counties claim that because the term "realty sold" requires construction, "the Legislature is perfectly capable of interpreting that phrase, without any constitutional infirmity—particularly ... to address emergent forms of property transactions." (CAB, pp. 22-23.)

The 2009 and 2011 statutes cannot shed light on the interpretation of the 1967-enacted DTTA. First, "[t]he declaration of a later Legislature is of little weight in determining the relevant intent of the Legislature that enacted the law." (*Peralta Community College Dist. v. Fair Employment and Housing Com.* (1990) 52 Cal.3d 40, 52; see OBM, pp. 43-46, 48-52; RBM, p. 26.)

Secondly, the 2009 and 2011 legislation did not expressly amend the DTTA in any way. "[T]he principle of amendment ... by implication is to be employed frugally, and only where the later-enacted statute creates such a

conflict with existing law that there is no rational basis for harmonizing the two statutes ....'" (*McLaughlin v. State Bd. of Education* (1999) 75 Cal.App.4th 196, 222-223.) There is no conflict here.

The Counties infer that because the 2009 and 2011 statutes provide county recorders and city finance officials with *access* to statements of change-in-ownership of legal entities (§§ 408, subd. (b), 408.4), they were meant to allow the documentary transfer tax to be applied to all change-in-ownership transactions. The Counties point to the fact that the committee analysis for Senate Bill No. 816 indicated that it would help "recorders determine whether the DTT applies to certain changes of ownership." (CAB, p. 20, citing Counties' Motion for Jud. Notice, Exh. R.) But that committee report stated that the "legally required forms" that provide for change of ownership "*may or may not* trigger the DTT." (Sen. Rev. & Tax. Comm., Analysis of Sen. Bill No. 816 (2009-2010 Reg. Sess.), Counties' Mot. for Jud. Notice, Exh. R, p. 4; italics added.) This suggests that all changes in ownership of realty are *not* subject to the DTTA. As stated in Ardmore's opening brief, this merely reflects that changes in ownership in partnerships holding realty under section 11925 may trigger a documentary transfer tax as expressly authorized under that statute.[4]

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[4] The Counties argue in a footnote that there is no support in the legislative history that the purpose of the bill was to permit taxation of conveyances

[Footnote continued on next page]

Third, a subsequent Legislature could not amend the DTTA to "address emergent forms of property transactions" because any such statutory amendment would have to comply with the requirements of Proposition 13, which clearly were not satisfied here. (See OBM, pp. 49-50.) As noted earlier, Proposition 13 amended the Constitution to (1) require that "any change in State taxes ... whether by increased rates or changes in methods of computation must be imposed by an Act passed by not less than two-thirds of all members elected to each of the two houses of the Legislature" and (2) prohibit "new ad valorem taxes on real property, or sales or transaction taxes on the sales of real property." (Former Cal. Const., art. XIIIA § 3[5]; OBM, pp. 49-50.) These 2009 and 2011 bills were not enacted by the required super-majority, and if interpreted to enlarge the scope of the DTTA, would run afoul of the prohibition against new transaction taxes on sales of real property. (OBM, p. 50; RBM, p. 26.)

[Footnote continued from previous page]

of realty under section 11925. (CAB, p. 22, fn. 31.) But given that the legislative history expressly acknowledges that changes in ownership may not be subject to the documentary transfer tax and given that the Legislature was not expressly amending the DTTA, Ardmore's interpretation is the only reasonable one.

[5] There have been no material changes in the relevant wording of Article XIIIA since the enactment of Senate Bill No. 816 and Assembly Bill No. 563.

The Counties' citation of *Sav-On Drugs, Inc. v. County of Orange* (1987) 190 Cal.App.3d 1611, 1623-1625 (*Sav-On*), for the proposition that "similar [constitutional] arguments against the change in ownership statutes" were "reject[ed]" (CAB, p. 23) is of no assistance. Those "change-in-ownership" statutes *implemented* Proposition 13. *Sav-On* merely ruled that "section 64 is the Legislature's interpretation of the Constitution, specifically article XIIIA" (*id.* at p. 1623) and "implemented the will of the electorate" (*id.* at p. 1624). The same cannot be said about statutes in 2009 and 2011 if they are applied to *expand* the scope of the DTTA in violation of article XIIIA of the California Constitution.

D. The Objective Of Raising Revenue Does Not Permit An Interpretation That Extends Beyond The Statute's Ordinary Meaning.

The Counties argue that "the fundamental purpose of the Documentary Transfer Tax to raise revenue cannot be ignored in the interpretation of its provisions" and that "[t]his plain reality was influential in the broad interpretation of the federal Stamp Tax." (CAB, pp. 27-28; accord, *id.*, p. 3.)

First, the cases cited by the Counties for the latter proposition, *Royal Loan Co. v. United States* (8th Cir. 1946) 154 F.2d 556 (*Royal Loan*), and *Stuyvesant Town Corp. v. United States* (Ct. Cl. 1953) 111 F.Supp. 243 (*Stuyvesant Town*), merely stated that in light of the fact that the federal stamp tax is a revenue measure, they would not interpret the term at issue there—"corporate security" (whose transfer was subject to the tax)—so as to be

"restricted by technical refinements in construction" since it was "not a technical term." (*Royal Loan, supra*, 154 F.2d at p. 558; *Stuyvesant Town, supra*, 111 F.Supp. at p. 696 ["income debenture certificates" are "well within the class of investment securities which Congress intended to tax"].)

This approach comports with Ardmore's approach to interpret the DTTA based on the common meaning of its statutory language. Those cases in no way suggest that the DTTA should be construed differently than its plain language simply because the tax seeks to raise revenue.

Second, the Counties' suggestion that the DTTA's revenue-raising purpose justifies expanding its scope violates the canon that "courts, in interpreting statutes levying taxes, may not extend their provisions, by implication, beyond the clear import of the language used," and "[i]n case of doubt construction is to favor the taxpayer rather than the government." (*Edison, supra*, 30 Cal.2d at p. 476.)

Finally, the Counties' invention of a "revenue-raising" canon to expand the interpretation of a tax statute to maximize revenue conflicts with the voters' enactment of Proposition 13, which is intended to constrain tax increases. As this Court has recognized, "[t]h[is] constitutional provision imposes a limit on the power of state and local governments to adopt and levy taxes." (*County of Fresno v. State of California* (1991) 53 Cal.3d 482, 486, internal citations omitted; see also *Greene v. Marin County Flood Control and Water Conservation Dist.* (2010) 49 Cal.4th 277, 284 ["The purpose of

Proposition 13 was to cut local property taxes," internal quotations omitted].) As a result, the Counties cannot rely on the *revenue-generation purpose* of tax statutes—a trait universally shared by tax statutes—in the face of a *constitutional provision that constrains the expansion of taxes*.

IV. CONCLUSION

For the reasons set forth herein and in Ardmore's briefs, section 11911 does not authorize the imposition of a documentary transfer tax based on a change in ownership or control of a legal entity that directly or indirectly holds realty. The statute's plain language, rules of statutory construction, its legislative history, the federal interpretation of section 11911's predecessor, and past practice only authorize the imposition of a tax on writings that directly convey realty itself.

Consequently, this Court should reverse the judgment, grant Ardmore's request for a refund, and remand for a determination of Ardmore's right to attorney's fees and costs.

Dated: November 13, 2015

Respectfully submitted,

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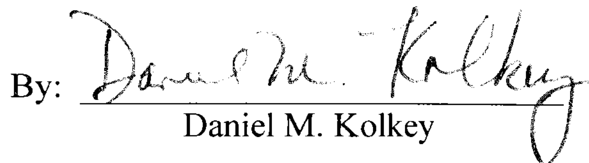
By: 
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CERTIFICATE OF WORD COUNT

In accordance with rule 8.520(c) of the California Rules of Court, the undersigned hereby certifies that this Answer Brief contains 8,177 words, as determined by the word processing system used to prepare this brief, excluding the cover information, the tables, the signature block, and this certificate.

Dated: November 13, 2015

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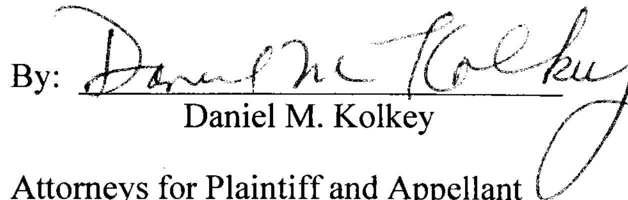

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PROOF OF SERVICE

I, Carol Aranda, declare as follows:

I am employed in the County of San Francisco, State of California; I am over the age of eighteen years and am not a party to this action; my business address is 555 Mission Street, San Francisco, California 94105 in said County and State. On November 13, 2015, I served the within:

926 NORTH ARDMORE AVENUE LLC'S ANSWER BRIEF TO THE AMICI CURIAE BRIEF OF COUNTY OF TEHAMA ET AL.

to each of the persons named below at the address(es) shown, in the manner described below:

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☑ **BY MAIL**: I placed a true copy in a sealed envelope addressed as indicated on the attached service list for collection and mailing at my business location, on the date mentioned above, following our ordinary business practices. I am readily familiar with this business's practice for collecting and processing correspondence for mailing with the United States Postal Service. On the same day that correspondence is placed for collection and mailing, it is deposited in the ordinary course of business with the U.S. Postal Service in a sealed envelope with postage fully prepaid. I am aware that on motion of the party served, service is presumed invalid if the postal cancellation date or postage meter date on the envelope is more than one day after the date of deposit for mailing contained in the proof of service.

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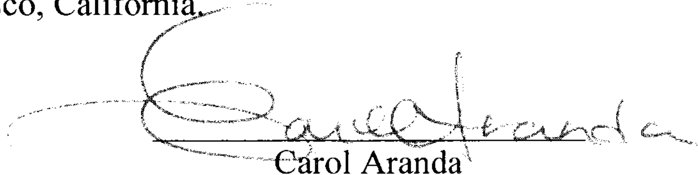

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