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Transfer Tax Applies on Transfer of Controlling Interest in Legal Entity Holding California Real Property

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A recent, unprecedented case may open the door to a substantial increase in real property documentary transfer tax in California.

Historically, the traditional view of many practitioners in California has been that the transfer of interests in legal entities (other than certain transfers of interests in partnerships and limited liability companies treated as partnerships for income tax purposes), including the transfer of the membership interests in a single member limited liability companies, that hold California real property is not subject to documentary transfer tax (“DTT”). This is because the relevant statute applies to “realty sold” and therefore no DTT was determined to be due because no deed was recorded.

On September 22, 2014, a California Court of Appeals held otherwise. The court affirmed in *926 North Ardmore Avenue, LLC v. County of Los Angeles* (9/22/14, B248536) that DTT may be imposed upon a change in control of a legal entity owning California real property (including real property that is owned through an intermediate single member limited liability company). In general, a change in control of a legal entity (generally an acquisition that causes a single person or entity to hold more than 50 percent of the ownership interests of the legal entity) will be treated as a change of ownership of its underlying real property, thereby triggering DTT.

A few cities and counties in California had already amended their DTT statutes to adopt this approach, including San Francisco and Santa Clara Counties. Other counties, notably Los Angeles County, have not amended their statutes but have publicly stated that they follow this approach.

This decision means that California county recorders may now impose DTT in cases where a legal entity that holds real property undergoes a change in control (including cases in which real property is held through a single member limited liability company) without regard as to whether a deed is recorded, *even if* the relevant cities and counties do not revise their DTT statutes or otherwise announce their intention to impose DTT on such changes in control. As a result, a significant number of transactions that we normally would not have expected to trigger DTT in most California cities and counties, such as transfers of controlling interests in single member limited liability companies, may now trigger DTT. It is theoretically possible that county recorders will use this new case to retroactively impose DTT on such transactions, although this result has not yet been applied to our knowledge.

We encourage taxpayers to carefully consider the DTT implications of a transaction that will result in a change of control of a legal entity that directly or indirectly owns an interest in California real property and discuss any concerns with their tax attorney.

The full text of the case may be found [here](#).



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