

Real Estate Co-Ownership Brief

A Series of Briefs on Legal Issues Regarding Co-Ownership of Real Property



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Property Tax Re-assessment Upon Transfer of Co-owned Real Property

By Scott M. Toussaint

As most California real property owners know, when property sells, the real property taxing agency (i.e., the County Assessor) typically re-appraises the property at the sales price. But what if only a portion of the property is sold? What if the property is co-owned by multiple people, each with their own fractional interest in the property, and less than all of them sell their interests?

When it comes to the most common form of co-ownership for unrelated persons, tenancy-in-common, *the general rule is that the sale of a tenant-in-common interest triggers re-appraisal of that interest but only that interest.*¹

For example, say Alex and Bill purchase an office building as tenants-in-common, for \$10 million, with Alex receiving a $\frac{2}{3}$ share of the property and Bill receiving the remaining $\frac{1}{3}$. Five years later, when the fair market value of the property is \$15 million, Bill sells his $\frac{1}{3}$ of the property to Carol for \$5 million. Carol's $\frac{1}{3}$ share of the property is now re-assessed, while Alex's $\frac{2}{3}$ share of the property is not.²

There are certain *exceptions* to the general rule. For example, when spouses or lineal descendants are involved, or when small interests are transferred, it may be possible to transfer a tenant-in-common interest without triggering re-assessment. While it is important to be mindful of possible exceptions, the rule of thumb is that the transfer of a tenant-in-common's interest in real estate ordinarily triggers re-assessment on that portion of ownership – but only that portion.

Attorney's Tip:

The written co-ownership agreement for this property – assuming there is one – should anticipate this scenario, and provide that the purchasing co-owner (Carol) is responsible for all of the extra property taxes triggered by his purchase of Bill's interest. If, instead, the agreement simply allocates the expenses of ownership (such as property taxes) on a pro rata basis in accordance with percentage of ownership, then Alex will be paying a share of the property tax burden created by an activity (Bill's sale to Carol) in which he did not participate and from which he did not benefit. Tenants-in-common should be wary of this trap, and craft their co-ownership agreements accordingly.

¹ Tenancy-in-common should not be confused with other common multi-party property ownership arrangements, such as partnerships and limited liability companies, to which an entirely different set of reassessment rules applies.

² This example ignores the transfer tax burden, which can be significant. For example, if the office building in this example happened to be located in Palo Alto, the total City and County transfer tax bill for the sale of Bill's interest to Carol would be \$22,000.

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