

Rent Stabilization Board

COMMUNICATION ACCESS INFORMATION:

This meeting is being held in a wheelchair-accessible location. To request disability-related accommodation(s) to participate in the meeting, including auxiliary aids or services, please contact Aimee Mueller at 981-4932 or 981-6903 (TDD) *at least three business days before* the meeting date.



Please refrain from wearing scented products to this meeting.

RENT STABILIZATION BOARD
IRA / AGA / REGISTRATION COMMITTEE MEETING

Tuesday, August 6, 2019 – 4:00 p.m.

2001 Center Street, Law Library, 2nd Floor

Teleconference location: 2003 Stuart Street, Berkeley, CA 94703

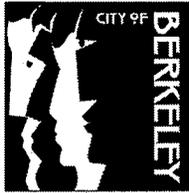
This meeting will be conducted in accordance with the Brown Act, CA Government Code Section 54953(b)(2), and Teleconferencing. Any member of the public may attend this meeting at either location. Questions regarding this matter may be addressed to Jay Kelekian, Executive Director and Secretary to the Board at (510) 981-7368.

AGENDA

1. Roll call
2. Approval of the agenda
3. Public Comment
4. Discussion and possible action to clarify whether properties held in revocable living trusts qualify for Golden Duplex exemption (Staff memo attached)
5. Discussion and possible action regarding future agenda items
6. Confirm next meeting date
7. Adjournment

STAFF CONTACTS: Matt Brown, Staff Attorney (510) 981-4930

COMMITTEE: Soli Alpert, Paola Laverde, Leah Simon-Weisberg (Chair)



Rent Stabilization Board
Legal Department

MEMORANDUM

DATE: August 6, 2019

TO: Honorable Members of the IRA/AGA/Registration Committee

FROM: Jay Kelekian, Executive Director

By: Matt Brown, Senior Staff Attorney
Brendan Darrow, Staff Attorney

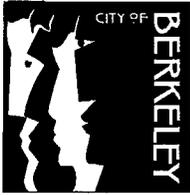
SUBJECT: Proposed Amendment to Regulation 503 – Definition of Principal Residence

Recommendation:

Consider amendments to Regulation 503 that would allow claims of exemption for properties held in trusts where the grantor and trustee differ and bring a recommendation back to the full Board regarding this matter.

Background and Need for Rent Stabilization Board Action:

At its July 2, 2019 meeting, the IRA/AGA/Registration Committee unanimously recommended changes to Regulation 503 that would clarify that the term “natural person” includes a grantor of a revocable trust who also serves as trustee. After the meeting, community members raised concerns that were not discussed by the Committee. Those concerns were detailed in a staff report for the July 18, 2019 Board meeting, which was canceled. The staff report is attached hereto.



Rent Stabilization Board
Legal Department

MEMORANDUM

DATE: July 18, 2019

TO: Honorable Members of Rent Stabilization Board

FROM: Honorable Members of the IRA/AGA/Registration Committee

By: Matt Brown, Senior Staff Attorney
Brendan Darrow, Staff Attorney

SUBJECT: Proposed Amendment to Regulation 503 – Definition of Principal Residence
[First Reading]

Recommendation:

That the Board adopt amendments to Regulation 503, clarifying that the term “natural person” includes a trustee of a revocable trust that owns the subject property under the limited circumstances in which the property is held in trust solely for estate planning purposes. The IRA/AGA/Registration Committee unanimously recommended these changes at its July 2, 2019 meeting.

Background and Need for Rent Stabilization Board Action:

Owner-occupants of duplexes that were owner-occupied on December 31, 1979 are exempt from the Rent Stabilization and Eviction for Good Cause Ordinance, as are owner-occupants who share kitchen or bath facilities with their tenants. Regulation 503 sets forth criteria for assessing “occupancy” by a landlord for purposes of enforcing these occupancy-based exemptions.

During the foreclosure crisis, attorneys for banks successfully argued that their clients had “stepped into the shoes” of foreclosed-upon owners and therefore were entitled to exemptions that apply only to owner-occupants. In 2013, the Board adopted amendments to Regulation 503 to preclude banks, corporations, or other business entities from claiming to “occupy” the property for purposes of evading rent control.

1. Revocable trusts are not natural persons, but they are controlled by natural persons and are not business entities.

Recently, several landlords who hold their properties in revocable trusts have inquired about their status under Regulation 503. These concerns were also raised at the meeting of the 4x4 Joint Task Force Committee on Housing on May 21, 2019. The 4x4 Committee unanimously referred the issue to the Rent Board IRA/AGA/Registration Committee for consideration.

Legal staff has drafted proposed language that would clarify the regulation by narrowly permitting landlords who hold property in revocable trusts to claim the exemption to which they would otherwise be entitled, should they exercise their option to revoke the trust.

The IRA/AGA/Registration Committee considered the matter at their July 2, 2019 meeting and recommended the adoption of the proposed regulation, with one revision, adding the word “surviving” to the language governing the rights of a sole beneficiary after the death of the grantors who set up the trust.

2. Background on the nature of revocable trusts.

Revocable living trusts are an instrument created solely for the purpose of avoiding the probate process upon the death of the trustee. A person who creates a revocable living trust *grants* assets to the trust (making that person the “grantor” for purposes of the trust). In order for the trust to be revocable, specific language must be included in the trust document and generally the same person who grants the assets into the trust is also named as the trustee. The result of this arrangement is that the assets held by the trust do not technically belong to any natural person, thus they do not have to be transferred to heirs by a probate court. There are no tax benefits to creating a revocable trust where the grantor and the trustee are the same person, because the IRS treats the grantor as the owner of the property contained within the trust and thus the grantor would remain responsible for property and income tax related to the rental property even after the property has been transferred to the trust.¹

3. Recognizing revocable living trusts can be accomplished without creating new exemptions or avenues for subterfuge.

Members of the 4x4 Committee expressed concerns that allowing a person who is not the owner of record would have unintended consequences. Staff has taken care to draft language (attached to this Memorandum) that would apply narrowly and predictably. It would *not* permit a landlord to claim exemption for a property that is actually owned by another person, or a property that is owned by any sort of business entity. It would *not* permit a landlord to claim owner occupancy of a property that is held in any other type of trust for tax or business purposes. Lastly, the draft language would not permit a landlord to claim exemption for children or spouses who did not own the property before it was held in trust.

No additional exemptions would be created by the proposed language. On the contrary, any exemptions that are not currently recognized by the Board because the property is held in a

¹ The original memorandum presented to the IRA/AGA/Registration Committee conflated concerns of administrative practicality and IRS treatment of trusts with the legal standard for revocability. To be clear, the IRS treats the grantor of a revocable trust as the owner of the trust’s assets **only where the grantor retains control over those assets**. This means that the grantor continues to pay taxes on the property and its revenues as if the trust did not exist. (Internal Revenue Code §§ 671-679.) The most common arrangement is to name the grantor as trustee, and that is also the most straightforward way to confirm that the grantor retains control of the property, but it is not strictly required by state or federal law.

revocable trust are illusory; the landlord can revoke the trust and gain exemption at any time. The draft language merely corrects an unintended consequence of the Board's actions to prevent abuse of exemptions by foreclosing banks.

4. Sole beneficiaries of revocable living trusts may be treated as owners upon the death of the grantor.

Whereas the grantor of a revocable living trust retains control over property that they grant to the trust, the beneficiaries of the trust do not. However, upon the death of the grantor/trustee(s), the beneficiaries typically take control of the property, and are treated as "owners" for tax purposes. Where multiple beneficiaries are named in the trust, the nature of their control and ownership over the property may be convoluted or even contested, and a successor trustee retains control until the assets are transferred. On the other hand, a sole beneficiary has a plain and incontrovertible right to own the property contained in a revocable trust upon the death of the grantor. For that reason, the City of Santa Monica Rent Control Board lost a case in Superior Court on the grounds that the sole beneficiary of a revocable living trust becomes the owner of the trust's assets upon the death of the grantor (*Solomon v. SMRCB*). In light of that Santa Monica case, staff recommends adoption of a provision that would recognize the sole beneficiary of a revocable trust as the owner for purposes of the Rent Ordinance upon the death of the trustee.

5. The process for evaluating the owner's principal residence.

At its July 2, 2019 meeting, the IRA/AGA/Registration Committee requested further information about making public records regarding ownership readily available to tenants, and about the process for evaluating the owners' principal residence. It bears emphasis that the proposed amendments recommended by the IRA/AGA/Registration Committee would not relax the criteria for establishing residency in order to claim exemption.

If the proposed amendments are adopted, natural persons who hold their rental property in a revocable living trust will be held to exactly the same standard as any other owner of rental property who seeks to claim exemption. Staff can make the records verifying the ownership of the rental property available to the public upon request, and they would be a part of the record of any petition filed to dispute an owner's claim of exemption for owner occupancy.

6. Alternative proposal would allow exemption where the owner does not serve as trustee.

After the July 2, 2019 meeting of the IRA/AGA/Registration Committee, community members asked staff to reconsider the proposed requirement that the grantor be the same person as the trustee, on the grounds that trusts can be designed in a way that makes them legally revocable and does not avoid taxes without naming the same individual as the grantor and trustee.

Where the trustee and the grantor are different people, it is generally the *trustee* who bears all of the rights and responsibilities of a landlord. This means that although the grantor might reside in the property and maintain a right to revoke the trust, it is the trustee who would have the separate

right to evict any tenant or raise their rent.² However, a trust may be written in such a way that the grantor retains the right to maintain control over the property, including the rights and obligations of a landlord.

It is administratively burdensome for Rent Board staff to review trust documents to assess the respective rights of the grantor and trustee. Where they are the same person, it is not necessary to conduct that analysis. Trust documents are not public records whose authenticity can easily be confirmed by staff, as compared with the grant deed which must be recorded and names the grantor and the trustee. The privacy implications and complexity of such arrangements are significant. However, the need to review the trust documents can be eliminated by requiring an affidavit signed by the grantor and trustee clearly establishing that the grantor retains control over the property.

The IRA/AGA/Registration committee recommended that the Board adopt language permitting a natural person to claim owner-occupancy exemptions where they are both the grantor and the trustee of a revocable trust and would otherwise qualify for exemption. In the alternative, the Board may wish to send this issue back to the IRA/AGA/Registration Committee to determine whether it recommends that Regulation 503(B) be further amended to allow for an exemption in certain circumstances where the grantor and trustee are not the same person. Legal staff is prepared to answer questions regarding the implications of this potential revision and will advise the Board regarding the potential amendments after it fully explores the issue.

Conclusion

Regulation 503 should be amended to clarify that the term “natural person” includes a grantor of a revocable trust that owns the subject property under the limited circumstances in which the property is held in trust solely for estate planning purposes. Legal staff further recommends that the IRA/AGA/Registration Committee further examine the issue of whether the exemption should extend to trusts where the grantor and trustee differ and bring a recommendation back to the full Board regarding this matter.

Proposed Regulation 503 is attached hereto. Additions are underlined.

Name and Telephone Number of Contact Person:

Matt Brown, Senior Staff Attorney (510) 981-4930
Rent Stabilization Board

² The naming of a non-person entity (such as a financial institution) as a trustee, and thereby installing that institution as the landlord, would directly contradict the original purpose of subsection B, which was to prevent financial institutions from claiming occupancy-based exemptions under the ordinance.

503. Definition of Principal Residence

(A) **Background and Purpose.** Like many of the exemptions listed in Berkeley Municipal Code Section 13.76.050, the exemptions identified in Berkeley Municipal Code Sections 13.76.050F. and 13.76.050G. (Sections 5(f) and 5(g) of the Ordinance) are transitory. A landlord may not claim an exemption pursuant to Sections 5(f) or 5(g) of the Ordinance unless the landlord occupies a unit on the property as his/her principal residence at the time the landlord asserts or claims the exemption.

(B) "Person" limited to "natural person." Only a natural person may claim principal residence in a unit when claiming an exemption under Sections 5(f) or 5(g) of the Ordinance. For purposes of this Regulation, "person" shall mean only a "natural person." A successor in interest is not entitled to the exemptions in either Sections 5(f) or 5(g) of the Ordinance merely because a previous landlord claimed entitlement to one of these exemptions. A bank, corporation, or other business entity may never claim a unit as exempt under Sections 5(f) or 5(g) of the Ordinance as such entities are not natural persons. A natural person who is both the grantor and trustee of a revocable living trust may claim principal residence. The spouse of the trustee of a revocable living trust may claim principal residence only if he or she was a grantor of at least 50% interest in the property at the time it was granted to the trust. A natural person who is the sole beneficiary of a revocable living trust for which all grantor(s)/trustee(s) are deceased may claim principal residence. All applicable criteria set forth in Subsections C and D shall apply equally to natural persons claiming principal residence pursuant to a revocable living trust as if those persons were owners of record.

(C) Principal residence, as used in Sections 5(f) and 5(g) of the Ordinance, is that dwelling place where the person actually resides a majority of the time. For the purpose of this Ordinance, a person may have only one principal residence.

(D) In the determination as to the principal residence status of the dwelling place, the following factors shall be considered:

- (1) whether the person carries on basic living activities at the dwelling place;
- (2) whether the person maintains another dwelling and, if so, the amount of time that the person spends at each dwelling place;
- (3) whether the person has filed for and obtained a homeowner's exemption for the dwelling place;
- (4) whether the person is a registered voter at the dwelling place;
- (5) other relevant factors.

[Effective Date: 11/26/80; renumbered 04/09/99; added new sections A and B, and enumerated sub-section identifiers of new Section D (previously A through D) 06/17/13; _____, 2019.]