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Proration, Collection and Refund of Taxes Under Revenue and Taxation Code Section 4986

When a transfer of title or possession of real property occurs between a private owner and a public entity, the property ceases to be subject to ad valorem taxation, provided that the property is within the territorial limits of the acquiring agency.¹ The legislature has prorated these taxes to the date of acquisition, and this formula is consistent with the taxpayer's duty to pay only for the benefits afforded his property while he has the use thereof.²

The Revenue and Taxation Code sets forth the formulae for the proration, collection and cancellation of taxes secured by liens on property when such property is acquired by a public entity for public purposes.³ Where the property is acquired by negotiated purchase, taxes, assessments, penalties and costs are prorated to, but not including, the date title passes to the public entity.⁴ The date of acquisition is taken as the date that the governing board or other designated officer accepts the deed on behalf of the public entity.⁵ Where the property is acquired through condemnation proceedings the date of proration is the date title passes or possession is taken, whichever occurs first.⁶ The Code of Civil Procedure states that title passes when a certified copy of a final order of condemnation is filed with the county recorder.⁷ It also provides that the effective date of possession is the earliest date on which the plaintiff would be entitled to take possession of the property if the plaintiff had given the defendants the required twenty days notice of the order of possession on the date the order is made, unless the order specifies a different date.⁸

It is good practice among condemnors to state in the order of possession the date upon which or after which the plaintiff is entitled to take possession. This is the date which is normally considered to be the "taking" date for tax purposes.⁹ However, the term "possession" is not defined by section 4986 and the situation could arise where physical possession is not taken on the effective date of possession. The condemnor can receive a set-off for the rents, issues and profits the taxpayer obtains after this date.¹⁰ While there is no provision for taxation of the fee during this interim period, if the time in possession by the taxpayer were significant, his use of the property could be taxed as a possessory interest.¹¹ Where possession is taken prior to the final order of condemnation, it is common practice to include in the final order a recitation of the effective date of the order of possession. This assists the assessor, tax collector, title companies and the public generally in ascertaining the date of possession.

¹ CAL. CONST. art. XIII, § 1.

² *Committee Report of the California State Bar Committee on Condemnation Law and Procedure (Southern Section)*, 36 CAL.S.B.J. 447, 456 (1961).

³ CAL. REV. & TAX. CODE § 4986. All statutory citations refer to the California Revenue and Taxation Code, unless otherwise indicated.

⁴ CAL. REV. & TAX. CODE § 4986.

⁵ CAL. GOV. CODE § 27281.

⁶ CAL. REV. & TAX. CODE § 4986(2)(b).

⁷ CAL. CODE CIV. PROC. § 1253.

⁸ CAL. CODE CIV. PROC. § 1243.5(b)(4).

⁹ CAL. CODE CIV. PROC. § 1243.5(b).

¹⁰ CAL. CODE CIV. PROC. § 1255b(b).

¹¹ CAL. REV. & TAX. CODE §§ 104, 107.

MECHANICS

The mechanics for this proration, collection and refunding should now be examined. First, consider the situation where property is acquired by negotiated purchase under section 4986(2)(a). If the purchase occurs prior to September, the tax collector will normally be able to furnish the assessee with his tax bill showing the prorated amount of taxes. In cases of partial takings, the tax bill is prepared on the basis of the new segregated values, the property transferred to the unsecured roll, and the tax collected as a personal liability of the former private owner.

When the date of acquisition occurs after September, the taxpayer can pay the first installment. If the property is acquired thereafter, the taxpayer will be sent an amended bill for his share, if unpaid. If he has paid more than his share, he can obtain the amount of the overpayment as part of the purchase price of his property or arrange for a refund through the public agency. The public entity is then "deemed" to have paid the overpayment, which in turn is "deemed" to have been erroneously collected and refundable to the public entity by the taxing agencies.¹²

Where the county collects the taxes for a city, the consent of the city attorney is necessary before cancellation of the taxes accruing after the date of proration.¹³ The code does not specify whether the consent of the city attorney is necessary in order to refund taxes which have been deemed to have been erroneously collected.¹⁴ The board of supervisors, however, may include in the refund taxes collected by county officers for a city or a revenue district.¹⁵

Seemingly, if the taxes are unpaid, the consent of the city attorney is needed to cancel taxes after the date of acquisition; whereas, if an overpayment of taxes has occurred, no consent is needed in order to refund the money. The question then arises whether the taxes accruing after the date of proration can be canceled where there has been a "prepayment" or an overpayment of the taxes. This results from the fact that section 5096.3 speaks only in terms of refunds and Code of Civil Procedure section 1252.1 only in terms of liability for the tax as between the plaintiff and defendant.

In theory, this legislative gap leaves uncollectible taxes on the books unless it can be said the power to refund taxes implies the power to cancel them on the roll.¹⁶ It is clear that the taxpayer's share of these taxes is not a cloud on the title held by the acquiring public entity in that the lien dissolves when the property is transferred to the unsecured roll.¹⁷ The taxes accruing after the date of proration are not legally collectible taxes, and if a county lien ever attached, it is extinguished by operation of law.¹⁸

¹² CAL. CODE CIV. PROC. § 1252.1, CAL. REV. & TAX. CODE § 5096.

¹³ CAL. REV. & TAX. CODE § 4986(2)(a).

¹⁴ CAL. REV. & TAX. CODE § 5096.3.

¹⁵ CAL. REV. & TAX. CODE § 5099.

¹⁶ See 40 OPS. CAL. ATT'Y GEN. 6 (1962).

¹⁷ CAL. REV. & TAX. CODE § 4986(2)(a), *State of California v. Clyne*, 175 Cal.App.2d 204, 209, 345 P.2d 474, 477 (1959).

¹⁸ *City of Long Beach v. Board of Supervisors*, 50 Cal.2d 674, 328 P.2d 964 (1958).

POSSESSION AND TITLE

The California Law Revision Commission study¹⁹ relating to taking possession and passage of title in eminent domain proceedings and other legislative history does not disclose the reason why the legislature treats differently the acquisition of property by deed from the acquisition through condemnation actions. In addition to the difference of the date of proration, there is a difference of administrative burden in the collection of the taxes. Under section 4986(2)(a), the burden is wholly on the tax collector. Under section 4986(2)(b), the taking agency is necessarily involved as a defendant in a condemnation case with the attendant burden of obtaining legal representation.²⁰

Another problem arises when the public entity acquires possession of property by negotiation, trespass or an order of possession and subsequently acquires the property by a negotiated purchase.²¹ Section 4986(2)(a) has been interpreted to mean that the phrases "acquired by a negotiated purchase and sale" and "the portion of such taxes . . . which are allocable to that part of the fiscal year which begins *on the date of acquisition of the property*" refer to the date that title to the property vests in the public entity.²² Since the taking of possession does not vest the full fee simple title in the public agency, the proration date is the date of the acceptance of the deed by the public entity.²³ Thus, the unwary taxpayer is liable for taxes, penalties and costs for months and perhaps years intervening between the taking of possession and the passage of title.

It can be argued that "acquired" refers to the taking of possession. The legislature's use of the words "purchase and sale" indicate the transfer of some or all of the indicia of ownership—here the right to possession.²⁴ The acquisition of possession is constitutionally a "taking" and thereafter the public agency has "acquired" the property for all practical purposes.²⁵ It is unjust to require the taxpayer in this situation to sustain the burdens of society relative to property from which he could not enjoy the benefits.

RECOMMENDATIONS

The answer is that section 4986(2)(b) in dealing with a condemnation action, differentiates between "acquisition" and "possession" and makes an express provision that the earlier of the two controls. The legislature made no similar differentiation when considering acquisitions by negotiated purchase under section 4986(2)(a). While the "possession before title" cases appear to be a trap for the unwary, they are really not, since usual business prudence in buying and selling real estate includes consideration of taxes, insurance, and the like. To avoid the payment of taxes during possession in this case, the only means available presently would be for the public entity to go to a stipulated judgment of

¹⁹ California Law Revision Commission Recommendation and Study B-61 (Oct. 1960).

²⁰ CAL. CODE CIV. PROC. § 1246.1.

²¹ California Law Revision Commission Recommendation and Study B-62 (Oct. 1960).

²² Emphasis supplied.

²³ CAL. GOV. CODE § 27281.

²⁴ CAL. REV. & TAX. CODE § 4986(2)(a).

²⁵ *People v. Peninsula Title Guaranty Co.*, 47 Cal.2d 29, 33, 301 P.2d 1, 3 (1956).

condemnation and obtain a final order of condemnation. This is an expensive and time consuming solution for the parties involved, especially for the attorneys of the acquiring agency and the taxing jurisdiction.

To remove the inequity in this unusual situation, legislative change is needed to make the effective date of possession or passage of title, whichever is first, the controlling date. As an alternative, "acquisition" could be defined to include the taking of possession under a court order or declaration of taking.

As to matters pending on July 1, 1962, the legislature by its 1961 amendments provided for a refund to the property owner who pays more than his pro rata share of taxes. Under Code of Civil Procedure section 1252.1, as between the plaintiff and defendant, the former is made liable for the overpayment. Notice should be taken that this section applies to condemnors who are public entities or private persons suing under Code of Civil Procedure section 1238(8). While it is doubtful that a public entity could be "liable" for taxes, the net effect of the 1961 legislation is to put the administrative burden of seeking a refund for the property owner upon the condemnor. Under section 5096.3 the overpaid tax is deemed to have been erroneously collected; a claim against the taxing agency is therefor in order.²⁶

FINAL PROBLEM

One final problem relates to the division of valuations on the roll where a partial taking occurs.²⁷ To provide for the orderly administration of the county's agencies, it is advantageous for condemnors to ask the tax collector for a separate valuation, furnishing him with a copy of the complaint and information relative to the recording of the *lis pendens*. This procedure enables the county departments to spread the workload over a longer period of time and allows the taxpayer to pay separately the taxes on the part taken and on the remainder.²⁸

The time and expense of collecting taxes in condemnation suits when handled as a matter of litigation generally has been incommensurate with the amount of taxes collected. Notwithstanding the fact that forms and procedures have been developed to streamline the litigation, the basic consideration remains that collection of taxes, even in a condemnation setting, is an administrative and not a legal problem.

The value in claiming taxes as part of the court proceeding is that the tax lien usually has priority over all other claims to the award; the award is security for the payment of the taxes which the tax collector does not have under section 4986(2)(a). Whether taxes should be collected through court when the property is acquired by condemnation is an economic problem: that is, whether the value of having the security furnished by the award is sufficient to justify the legal and administrative costs to collect the taxes through court. The tax collector could handle the entire matter by sending the condemnee an amended tax bill after the final order has been recorded.

²⁶ CAL. REV. & TAX. CODE § 5096.

²⁷ CAL. CODE CIV. PROC. § 1252.2.

²⁸ CAL. REV. & TAX. CODE § 2801.

Legislative change is needed to insure that the proper date for proration is used. If possession is taken prior to recording the final order, it should recite the date of the order of possession and the date that the right to take possession accrues. A suitable amendment of Code of Civil Procedure section 1253 to require such a statement would enable the tax collector and assessor to ascertain the date of possession with some degree of certainty.

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