*California State Board of Equalization*
*Legislative, Research & Statistics Division*

# LEGISLATIVE BULLETIN

# PROPERTY TAX LEGISLATION
# 2020

# FOREWORD

The State Board of Equalization's (BOE) Legislative, Research & Statistics Division (LRSD) is responsible for all aspects of the BOE's legislation, research, and statistics for the tax programs that the BOE administers. The LRSD screens all introduced and amended bills, and the review is used to identify legislation that could impact or be of interest to the BOE.

The Property Tax Legislative Bulletin is an annual publication that describes the enacted legislation in the past year that impacts property tax programs administered by the BOE. This publication is a compilation of the legislative bill analyses issued by the BOE for bills that were enacted during 2020. The legislative bill analyses for 2020 are posted on the BOE's website at http://www.boe.ca.gov/app/proptax-leg-analyses.aspx?year=2019-2020.

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## Assembly Bill 107 (Budget Committee), Chapter 264
*Appeals Boards*

*Effective September 29, 2020.*

*Among others, amends section 1604 of, and adds sections 1616, and 1752.4 to, the Revenue and Taxation Code.*

*This bill analysis is limited to property tax-related provisions.*

**Summary:** This budget trailer bill extends to March 31, 2021 the two-year deadline by which an assessment appeals board is required to render a final determination on a qualified application. This bill also provides that nothing in existing law shall be construed to prohibit an assessment appeals board or a multijurisdictional assessment appeals board from conducting hearings remotely.

**Existing Law:** Under article XIII, section 1, of the California Constitution, all property is taxable and assessed at fair market value, unless otherwise provided by the California Constitution or the laws of the United States. Under article XIII A (aka Proposition 13), real property is reassessed to current market value when real property undergoes a change in ownership or new construction is completed (called the base year value).[1] Annual inflationary increases in base year values are limited to 2 percent or the inflation rate, whichever is less (called the "adjusted base year value"). When the market value of real property drops below its adjusted base year value, the assessor can temporarily lower the property's assessed value to its current market value.[2]

Personal property is not subject to the Proposition 13 limits but is annually assessed at its current market value.[3]

When a property owner disagrees with a property's value, the property owner can appeal that value with the county appeals board.

In each county, the County Board of Supervisors either sits as a local board of equalization or appoints an assessment appeals board to hear property tax appeals.[4] Existing law also allows counties to enter into an agreement to form a multijurisdictional appeals board to hear property tax appeals.[5]

**Hearings.** Existing law[6] requires the Los Angeles County Assessment Appeals Board to meet annually on the fourth Monday in September and to continue to meet, as necessary, until property tax appeals are disposed of. Similarly, all other counties are required to annually meet on the third Monday in July and to continue to meet, as necessary, until property tax appeals are

[1] California Constitution, article XIII A, section 2; Revenue and Taxation Code (RTC) section 110.1.
[2] RTC section 51(a).
[3] California Constitution, article XIII, section 2; RTC section 110(a).
[4] California Constitution, article XIII, section 16.
[5] RTC sections 1750 – 1756.
[6] RTC section 1604(a) and Property Tax Rule 309(a).

disposed of. Appeal hearings are open and public, with certain exceptions.[7] Before making any reduction in value, existing law requires the appeals board[8] to examine, on oath, the person affected or agent making the application regarding the value of the property. Under certain circumstances, the appeals board may waive the examination of the person or agent.[9] Property Tax Rule 317 requires an applicant to appear personally at the hearing or be represented by an agent, unless the appearance has been waived by the appeals board.

**Decision.** If an appeals board fails to make a final determination on an application for reduction in assessment within two years of the timely filing of the application, the taxpayer's opinion of value as reflected on the application must be enrolled on the assessment roll for the tax year(s) covered by the application, until a final determination is made.[10] The taxpayer and the appeals board may mutually agree to extend this two-year period. When the appeals board makes a final determination on the application, the value determined by the appeals board is entered on the assessment roll for the fiscal year in which the value is determined.

## Amended Law:

**Two-Year Period Decision Period.** This bill extends to March 31, 2021 the two-year deadline by which an appeals board is required to render a final determination on an application that was timely filed and has a two-year deadline occurring during the period beginning on March 4, 2020 and before March 31, 2021. *(RTC section 1604.)*

**Remote Hearings.** This bill provides that nothing in existing law shall be construed to prohibit an appeals board or a multijurisdictional assessment appeals board from conducting hearings remotely. Remotely conducted hearings include, but are not limited to:

- Use of video, audio, and telephonic means for remote appearances,
- Electronic exchange and authentication of documentary evidence,
- Use of remote interpreting, and
- Use of remote reporting and electronic recording to make the official record of an action or proceeding.

If an appeals board or multijurisdictional appeals board conducts a hearing remotely, this bill requires that the hearings comply with the appeals provisions of the Revenue and Taxation Code[11] and any rules and procedures adopted by the county board of supervisors pursuant to article XIII, section 16, of the California Constitution. *(New RTC sections 1616 and 1752.4.)*

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[7] RTC section 1605.4.

[8] For purposes of this analysis, the term "assessment appeals board" or "appeals board" includes both a County Board of Supervisors sitting as a county board of equalization and an assessment appeals board appointed by the County Board of Supervisors, as well as a multijurisdictional assessment appeals board.

[9] RTC sections 1607 and 1608 and Property Tax Rule 316.

[10] RTC section 1604(c) and (d) and Property Tax Rule 309(b) and (c).

[11] Chapters 1 (sections 1601-1721) and 1.5 (sections 1750-1756) of Part 3 of the RTC.

**In General:** Property owners can appeal the value of the property appearing on the regular assessment roll by filing an *Assessment Appeal Application*[12] for changed assessment during the regular assessment filing period with the Clerk of the County Board of Supervisors. The regular assessment filing period is July 2 through either September 15 or November 30. The earlier deadline applies in counties where the assessor has provided an assessment notice by August 1 to all taxpayers on the secured roll.[13]

Assessments made outside the regular assessment period (supplemental assessments and escape assessments) may be appealed within 60 days after the date the notice of change in assessment is mailed. An exception exists in Los Angeles County and in any other county where the County Board of Supervisors has adopted an alternative resolution. In these counties, such assessments may be appealed within 60 days of the date of mailing printed on the tax bill or the postmark date, whichever is later. For disaster relief assessment appeals, a claim must be filed within six months of the reassessment notice.

Once an assessment appeal application is timely filed, the appeals board has two years from the date of filing to make a final determination on that application. If an appeals board fails to make a final determination within two years of the timely filing of the application, the taxpayer's opinion of value as reflected on the application must be enrolled on the assessment roll until a final determination is made.

**Background:** At the BOE hearing on August 18-19, 2020, a lengthy discussion was held regarding the impact of COVID-19 on appeals boards, specifically regarding the challenges, opportunities, and perspectives on the following three items:

- Current status of remote procedural and evidentiary hearings
- Examination of business continuity plans
- Remote hearings

Speakers represented the Judicial Council of California, Superior Court judges, administrative law judges, the Office of Tax Appeals, the California Association of Clerks and Election Officials, the California Assessors' Association, and the California Alliance of Taxpayer Advocates.

**Legislative History.** In 1994, SB 95 (Kopp) proposed the addition of section 1604.1 to the RTC to allow counties to adopt an ordinance to extend the two-year period to three years for appeal applications that were filed between January 1, 1995 and June 30, 1995. This bill was vetoed.

## Commentary:

1. **COVID-19.** Many county offices are temporarily closed because of the COVID-19 virus. As a result, assessment appeals boards have postponed and continued appeals that were

[12] BOE-305-AH.

[13] A listing of assessment appeal filing deadlines by county is posted on the BOE's website at www.boe.ca.gov/proptaxes/pdf/filingperiods.pdf.

pending and/or in process when offices closed. These closures have increased the backlog of appeals that will have to be scheduled, heard, and finalized on a timely basis when county buildings reopen.

2. **Governor's Executive Order N-72-20**. On July 31, 2020, Governor Newsom issued Executive Order N-72-20 extending the two-year deadline within which an appeals board must make a decision. This executive order states:

   > Notwithstanding Revenue and Taxation Code section 1604 or any other law, for any pending assessment appeal filed with a County Assessment Appeals Board on or before March 4, 2020, the deadline within which the County Assessment Appeals Board must render a decision is hereby extended until January 31, 2021.

   As a result of this Executive Order, an appeals board has until January 31, 2021 to render a determination for any appeal application that was timely filed prior to March 4, 2020, and with a two-year deadline that falls between, and including, July 31, 2020 and January 31, 2021.[14] This bill codifies and makes retroactive the Governor's Executive Order, extending to March 31, 2021, the two-year deadline by which a county board is required to render a final determination on a qualified application.[15] The decision period under AB 107 is two months longer than the decision period under the Governor's Executive Order.

3. **Limited Applicability.** This bill extends the two-year decision period for qualified applications that were timely filed and have a two-year deadline occurring during the period beginning March 4, 2020 and before March 31, 2021. Effectively, this extension applies only to appeal applications that were timely filed beginning March 4, 2018 through March 30, 2019 and which are still pending. This measure will not impact those appeals filed before or after this period.

4. **Temporary Extension.** For timely filed appeals that have a two-year decision deadline occurring during the period beginning March 4, 2020 through March 30, 2021, the assessment appeals board would have until March 31, 2021 to make a decision on those applications that are still pending.

5. **Waiver to Extend Two-Year Decision Period.** Existing law[16] allows a taxpayer and an appeals board to mutually agree to an extension of time for hearing and determination past the two-year limitation.

6. **Remote Hearings.** This bill provides that nothing in existing law prohibits an appeals board or a multijurisdictional assessment appeals board from conducting hearings remotely, as long as hearings comply with the appeals provisions of the Revenue and Taxation Code and any rules and procedures adopted by the County Board of Supervisors.

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[14] See Letter To Assessors No. 2020/036.
[15] Assembly Budget Committee Analysis.
[16] RTC section 1604(c)(1).

## Assembly Bill 2013 (Irwin), Chapter 124
*New Construction Exclusion - Disaster*

*Effective January 1, 2021.*

*Adds section 70.5 to the Revenue and Taxation Code.*

**Summary:** For property that has been substantially damaged or destroyed by a Governor-declared disaster on or after January 1, 2017, this bill adds a new construction exclusion for comparable property that is reconstructed on the site of the damaged or destroyed property.

**Existing Law:** Under existing law, real property is generally reassessed to its current fair market value whenever it has undergone a change in ownership or new construction has been completed. The value initially established or reassessed upon a change in ownership or completion of new construction is referred to as the property's "base year value."[17] The assessment of real property may be temporarily reduced to reflect reductions in value due to damage, destruction, depreciation, obsolescence, removal of property, or other factors causing a decline in value. [18]

A reduction in value for disaster, misfortune, or calamity[19] applies to major disasters affecting many properties, such as an earthquake, flood, or wildfire, as well as a disaster affecting an individual property, such as a house fire. The reduced value of a damaged property will continue until the real property is reconstructed. The reconstruction of real property that has been damaged or destroyed by disaster, misfortune, or calamity is not subject to reassessment as new construction under RTC section 70(c), if the property meets the following requirements:

- Reconstructed in a timely fashion, and
- Reconstruction is substantially equivalent to the property prior to the damage or destruction.

New construction following damage to real property by a calamity or misfortune is not eligible for disaster relief if the rebuilt improvements are not substantially equivalent to the property prior to damage or destruction. Only that portion of the reconstruction that exceeds substantial equivalence to the property prior to damage or destruction will have a new base year value.

Under RTC section 170,[20] relief may be applied immediately as of the date of the disaster, misfortune, or calamity if the loss in a property's market value is $10,000 or more.[21] Under RTC section 170, when property has been fully repaired, restored, or reconstructed, as of the date of

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[17] RTC section 110.1.
[18] RTC section 51(b).
[19] The term *misfortune or calamity* is defined by case law. The court of appeal, in *T.L. Enterprises, Inc. v. County of Los Angeles* (1989) 215 Cal.App.3d 876, held that a misfortune or calamity is a sudden, unforeseeable event.
[20] All 58 counties have enacted disaster relief ordinances pursuant to RTC section 170.
[21] RTC section 170(b).

completion of construction, the assessor will restore the lower of (1) the full cash value, (2) the damaged property's factored base year value, or (3) its factored base year value as adjusted pursuant to RTC section 70(c).

**Amended Law:** For property that has been substantially damaged or destroyed by a Governor-declared disaster on or after January 1, 2017, this bill adds a new construction exclusion for comparable property that is reconstructed on the site of the damaged or destroyed property, under the following conditions:

- **Disaster.** Property must be substantially damaged or destroyed by a disaster, misfortune, or calamity, as declared by the Governor. *RTC section 70.5(a) and (c)(3)*
- **Substantially Damaged or Destroyed.** Property is substantially damaged or destroyed if the improvements sustain physical damage amounting to more than 50 percent of the improvements' full cash value immediately prior to the disaster. *RTC section 70.5(c)(1)*
- **Comparable Reconstruction.** Reconstructed property is comparable if it is similar in function, size, and utility. *RTC section 70.5(c)(2)*
  - **Function.** Property is similar in function if it is subject to similar governmental restrictions, such as zoning. *RTC section 70.5(c)(2)(A)*
  - **Size and Utility.** Size and utility are interrelated and associated with value. Property is similar in size and utility if is used or intended to be used in the same manner and its full cash value does not exceed 120 percent of the full cash value of the damaged original property, determined just prior to the date of damage/destruction. *RTC section 70.5(c)(2)(B)(i)*
  - **Partial Relief.** If the full cash value of the reconstructed property exceeds the 120 percent threshold, the amount above 120 percent will be added to the transferred base year value. *RTC section 70.5(b)(2)(B)*
- **Ownership.** Only the owner(s) of the property substantially damaged or destroyed is eligible to receive relief under this section. *RTC section 70.5(d)*
- **Timing.** Construction must be completed within five years of the date of the damage or destruction. *RTC section 70.5(a)*

This bill provides that these provisions apply to real property damaged or destroyed by misfortune or calamity on or after January 1, 2017. *RTC section 70.5(e)*

**In General:** Article XIII A of the California Constitution, as approved by the voters in June 1978, did not contain any language indicating that property values might decline in value for any reason, including disasters. To remedy this problem and alleviate tax burdens on the ensuing “new construction” for disaster-damaged property, Proposition 8 amended article XIII A in November 1978 to provide that: (1) the full cash value base may from year to year not only reflect the inflation rate, but “may be reduced to reflect substantial damage, destruction or other factors causing a decline in value,” and (2) when property is damaged or destroyed through a disaster, reconstruction of the property is excluded as “new construction” when the restored structure is comparable in value to the original. (art. XIII A, section 2(a)). The legislation implementing these provisions is found in RTC section 70(c).

The BOE enacted Property Tax Rule 463 to implement the new construction statutes. Rule 463(f) addressed disaster relief and provided that newly constructed property does not include any land, improvement, or fixture that is restored, reconstructed, or repaired in a timely manner following a disaster and which is substantially equivalent in size, use, and quality to that which existed prior to the disaster. Subdivision (f) was removed from Rule 463, effective June 12, 1998.[22]

**Substantially Equivalent.** The reconstruction of real property that has been damaged or destroyed by disaster, misfortune, or calamity is not subject to reassessment as new construction under RTC section 70(c), if the property is timely reconstructed and the reconstruction is substantially equivalent to the property prior to the damage or destruction. These provisions apply to any type of disaster, misfortune, or calamity, including those caused by disaster for which the Governor proclaimed a state of emergency.

The term "substantially equivalent" is not defined by statute or rule. In Assessors' Handbook Section 410, *Assessment of Newly Constructed Property*, Chapter 5, the BOE recommends that the replacement property is comparable to the damaged or destroyed property in design type and use. The handbook provides two examples of reconstruction that is not substantially equivalent to the destroyed property, and thus would not be eligible for this new construction exclusion.[23]

> *Example 1.* A taxpayer owned a 1,200 square-foot residence that was totally destroyed when his property was flooded. He timely replaced the damaged property with a 3,500 square-foot residence. The additional square footage which exceeded the original 1,200 square-foot structure was assessed as new construction. Under these circumstances, the rebuilt structure will have two base year values. The pre-existing base year value will continue for the 1,200 square-foot portion of the rebuilt structure, and the additional 2,300 square feet will be appraised at market value as of the date of completion and a separate base year value will be established for that portion.

> *Example 2.* A taxpayer owns a vacation home which is destroyed by a fire. He decides that building a motel on his property in place of his vacation home would be more profitable. Under these circumstances, the taxpayer's replacement of the home with a motel is not eligible for disaster relief. The reconstructed property is not substantially equivalent to the property prior to the damage or destruction. Accordingly, the motel is considered new construction.

[22] See Letters To Assessors No. 98/07 and No. 98/48.
[23] Assessors' Handbook Section 410, pages 48-49.

**Governor State of Emergency Proclamations.** The Government Code[24] authorizes the Governor to proclaim a state of emergency under specified circumstances, including:

- "State of war emergency" means the condition which exists immediately, with or without a proclamation thereof by the Governor, whenever this state or nation is attacked by an enemy of the United States, or upon receipt by the state of a warning from the federal government indicating that such an enemy attack is probable or imminent.
- "State of emergency" means the duly proclaimed existence of conditions of disaster or of extreme peril to the safety of persons and property within the state.
- "Local emergency" means the duly proclaimed existence of conditions of disaster or of extreme peril to the safety of persons and property within the territorial limits of a county, city and county, or city.

**Background: Disaster Relief Base Year Value Transfer.** Exceptions to the reassessment requirement upon a change in ownership have been enacted, including two base year value transfers for property owners whose property has been damaged or destroyed in a disaster for which the Governor proclaimed a state of emergency.

1. **Intracounty Transfers.** Existing law[25] allows a person who owns property substantially damaged or destroyed in a Governor-proclaimed disaster to transfer the base year value of the damaged property to a comparable replacement property, as long as the replacement property is:

   - Located within the same county,
   - Purchased or newly constructed within five years of the date the disaster occurred, and
   - Similar in size, utility, and function.
     - Property is similar in *size and utility* if the market value of the acquired property does not exceed 120 percent of the fair market value of the damaged or destroyed property in its pre-damaged condition. If the market value of the replacement property exceeds 120 percent, partial relief is available. Specifically, the value above 120 percent is added to the transferred base year value.
     - Property is similar in *function* if the replacement property is subject to similar governmental restrictions, such as zoning. The replacement property must be used in the same manner as the damaged or destroyed property.

   Any type of property that is damaged or destroyed in a disaster for which the Governor proclaimed a state of emergency may qualify for this intracounty base year value transfer, including multifamily, commercial, or industrial property.

[24] Government Code (GC) sections 8558 and 8625.

[25] RTC section 69.

2. **Intercounty Transfers.** Existing law[26] allows a homeowner whose principal residence was substantially damaged or destroyed in a Governor-proclaimed disaster to transfer the base year value to a replacement property that is purchased or newly constructed in a different county, as long as the replacement property is located in a county that has enacted an ordinance,[27] purchased or newly constructed within three years of the date of the disaster, the principal residence of the property owner, and of equal or lesser value.

**Legislative History.** In 2019, the Legislature approved Assembly Bill 885 (Irwin), which provided that "substantially equivalent" meant the reconstructed improvement does not exceed 120 percent of either the size or full cash value of the improvement before the damage or destruction (substantially similar to this bill prior to the May 11, 2020 amendment). However, Governor Newsom vetoed this measure on the grounds that the proposed bright-line test should be narrowed to minimize negative impacts on local revenues.

## Commentary:

1. **Governor's Proclamation of State of Emergency or State of Disaster.** This bill provides that its provisions apply to property that is substantially damaged or destroyed by a disaster, "as declared by the Governor." However, under the Government Code, Governors issue proclamations of state of emergency for conditions of disaster or extreme peril. The text of the proclamation itself may or may not refer to the existence of conditions of disaster. Nonetheless, the Governor does not "declare" a disaster. The Governor proclaims a "state of emergency."

2. **New Construction Exclusion.** Even though this bill characterizes this relief as a base year value transfer, it is essentially a new construction exclusion. Relief will apply as long as the comparable reconstructed improvement is located on the same site as the damaged or destroyed improvement. Under this bill, a property owner is not limited to using the same footprint as the damaged or destroyed improvement.

3. **Comparable.** This bill provides that a reconstructed improvement is comparable if the reconstructed improvement is used or intended to be used in the same manner as the original improvement and does not exceed 120 percent of full cash value of the improvement, determined just before the damage or destruction. The physical size or square footage of the structure is not an issue.

   Issues have previously arisen where homeowners who had their property destroyed by fire have rebuilt homes that are larger in size than the destroyed home. Under current law, the additional square footage must be reassessed to current market value as of the date of completion of construction. Under this bill, a structure that is larger in size may be considered comparable if its full cash value is within 120 percent of the value of the

[26] RTC section 69.3.

[27] Contra Costa, Los Angeles, Modoc, Orange, San Francisco, Santa Clara, Solano, Sonoma, Sutter, and Ventura Counties.

damaged or destroyed structure. Partial relief is available if the reconstructed improvement exceeds 120 percent of value.

4. **Five-Year Period to Complete Construction.** This bill requires reconstruction to be completed within five years of the disaster. For counties such as Butte and Sonoma that had a large number of structures destroyed in wildfires, completing construction within a five year period may be difficult if there are permit and other delays. However, while any reconstruction completed after the five-year period would not qualify for relief under this new section, it may qualify for relief under RTC sections 70(c) and 170, if the construction is substantially equivalent to the damaged or destroyed structure.

5. **Requesting Relief.** This bill does not contain provisions on how a property owner is to request this relief.

6. **Retroactive Application.** While this bill, if enacted, would take effect on January 1, 2021, AB 2013 specifically provides that it applies to real property substantially damaged or destroyed by a Governor-declared disaster that occurs on or after January 1, 2017.

7. **RTC sections 70(c) and 170 Disaster Relief.** RTC section 170(h) allows the factored base year value as adjusted under RTC section 70(c) to be re-enrolled immediately upon completion of repair, reconstruction, or restoration. It is unclear how the provisions of this bill fit in with RTC section 170 since RTC section 170(h) still references only RTC section 70(c). This creates confusion as to which section to use in determining the value to restore upon reconstruction.

## Assembly Bill 3373 (Revenue and Taxation Committee), Chapter 57
*Number of Assessment Appeals Boards*

*Effective January 1, 2021.*

*Amends section 1621 of the Revenue and Taxation Code.*

**Summary:** Authorizes a County Board of Supervisors to create as many assessment appeals boards as is necessary to timely process, hear, and dispose of property tax appeals.

**Existing Law:** For property tax purposes, real property is reassessed from its Proposition 13 protected value (called a "base year value") to its current market value when real property undergoes a change in ownership or new construction is completed.[28] Annual assessed value increases are limited to 2 percent or the inflation rate, whichever is less (called the "adjusted base year value"). When the market value of real property drops below its adjusted base year value, the assessor can temporarily lower the property's assessed value to its current market value. Business property is not subject to the Proposition 13 limits, but is annually assessed at its current market value.

When a property owner disagrees with a property's value, the property owner can appeal that value with the county appeals board.

In each county, the County Board of Supervisors either sits as a local board of equalization or appoints an assessment appeals board to hear property tax appeals. Former law provided that a county may have no more than five assessment appeals boards.[29]

If a county assessment appeals board fails to make a final determination on an application for reduction in assessment within two years of the timely filing of the application, the taxpayer's opinion of value as reflected on the application must be enrolled on the assessment roll until a final determination is made.[30] The taxpayer and the appeals board may mutually agree to extend this two-year period.

**Amended Law:** This bill allows a County Board of Supervisors to create as many assessment appeals boards as it deems necessary to timely process, hear, and dispose of property tax appeals.

**In General:** Property owners can appeal the value of the property appearing on the regular assessment roll by filing an *Assessment Appeal Application*[31] for changed assessment during the regular assessment filing period with the Clerk of the County Board of Supervisors. The regular assessment filing period is July 2 through either September 15 or November 30. The earlier

[28] California Constitution, article XIII A, section 2; RTC section 110.1.
[29] RTC section 1621.
[30] RTC section 1604(c) and (d).
[31] BOE-305-AH.

deadline applies in counties where the assessor has provided an assessment notice by August 1 to all taxpayers on the secured roll.[32]

Assessments made outside the regular assessment period (supplemental assessments and escape assessments) may be appealed within 60 days after the date the notice of change in assessment is mailed. An exception exists in Los Angeles County and in any other county where the County Board of Supervisors has adopted an alternative resolution. In these counties, such assessments may be appealed within 60 days of the date of mailing printed on the tax bill or the postmark date, whichever is later. For disaster relief assessment appeals, a claim must be filed within six months of the reassessment notice.

**Background:** **Change in Ownership Exclusions.** For a 10-year period (July 24, 1995 to January 1, 2005), the law allowed a county a maximum of 10 assessment appeals boards. Effective July 24, 1995, Assembly Bill 1620 (Stats. 1995, ch. 1164) expanded the number of assessment appeals boards from 5 to 10 until January 1, 1999. Effective January 1, 1996, Senate Bill 657 (Stats. 1995, ch. 498) set the maximum number of assessment appeals boards at 10 indefinitely. Effective July 17, 1996, Senate Bill 713 (Stats. 1996, ch. 171) restored the sunset date, but extended the sunset date to January 1, 2005.

The reasoning behind the increase from 1995 to 2005 was that an economic recession resulted in an unprecedented number of assessment appeals throughout the state. In Los Angeles County, the number of assessment appeals grew from 5,791 in 1990-91 to 36,177 in 1993-94. The backlog of appeals grew during that same period from 9,998 to 67,081. The appeals workload exceeded the abilities and resources of both the local assessment appeals boards and County Assessors' offices to timely resolve legitimate taxpayer appeals within the two-year period provided by law.

## Commentary:

1. **Number of Assessment Appeals Boards.** According to the BOE's publication *A Report on Budget, Personnel, and Appeals Data for 2017-18*,[33] which is the most recent data available, four counties (Fresno, Los Angeles, Orange, and Riverside) have the maximum number of appeals boards.

2. **Number of Assessment Appeals Boards Increased 1995-2005.** As noted above, the Legislature previously increased the maximum number of assessment appeals board to 10 from July 24, 1995 to January 1, 2005, because of the economic recession that resulted in an unprecedented number of assessment appeals throughout the state.

3. **Why Limit the Number of Appeals Boards?** Limiting the number of assessment appeals boards does not allow counties with a high volume of appeals the flexibility to address existing backlogs and relieve pressure to meet statutory time limits.

[32] A listing of assessment appeal filing deadlines by county is posted on the BOE's website at www.boe.ca.gov/proptaxes/pdf/filingperiods.pdf.
[33] https://www.boe.ca.gov/dataportal/dataset.htm?url=PropTaxAppealsBoardsHearingOfficers.

4. **COVID-19.** Many county offices are temporarily closed because of the COVID-19 virus. As a result, assessment appeals boards have postponed and continued appeals that were pending and/or in process when offices closed. These closures have increased the backlog of appeals that will have to be scheduled, heard, and finalized on a timely basis when county buildings reopen. Moreover, because of the Governor's stay-at-home order beginning in March this year, counties are anticipating an increase in assessment appeals filed for the upcoming fiscal year for commercial and industrial properties. These appeals typically take longer to hear than residential property appeals. Finally, to date, appeals boards have not been given relief from the requirement to decide appeals within two years, increasing the necessity for more capacity to hear appeals.

5. **Split Roll Initiative.** Typically, the term "split roll" means taxing various property types (for example, residential v. commercial) according to a different tax rate or value standard. A true "split roll" is not possible without a constitutional amendment. Proposition 15 (19-008A1), which is qualified for the November 3, 2020 ballot,[34] proposes to amend the California Constitution to require certain commercial and industrial real property to be taxed at fair market value. Counties anticipate that there would be an increase in assessment appeals, if Proposition 15 is enacted.[35]

[34] Proposition 15 on the November 3, 2020 ballot failed, 48 percent yes to 52 percent no.
[35] California Assessors' Association, 19-003 White Paper: Split Roll (www.calassessor.org/index.php/resources/publications).

## Assembly Constitutional Amendment 11 (Mullin), Res. Chapter 31
## Proposition 19 (November 3, 2020 Ballot)
*Home Protection for Seniors, Severely disabled, Families, and Victims of Wildfire or Natural Disasters Act*

*Proposition 19 effective upon voter approval; operative as specified.*

*Proposes to add sections 2.1, 2.2, and 2.3 to article XIII A of the California Constitution.*

*This analysis is limited to the property tax provisions.*

**Summary:** Subject to voter approval, this constitutional amendment proposes to make the following changes to article XIII A of the California Constitution:

- Adds a base year value transfer for homeowners who are over age 55, severely, disabled or victims of a wildfire or natural disaster to a replacement home in California, regardless of location or value. Operative April 1, 2021, if enacted.
- Replaces the parent-child and grandparent-grandchild exclusion with a new parent-child and grandparent-grandchild principal residence exclusion, if the property continues as the family home or farm of the transferee and the property meets a specified value test. Operative February 16, 2021, if enacted.

## Base Year Value Transfer for Age 55/Disabled/Major Disaster

**Existing Law:** For property tax purposes, the law requires assessors to reassess real property from its Proposition 13 protected value (called the "base year value") to its current market value whenever a change in ownership occurs.[36] Exceptions to this reassessment requirement have been enacted, including two base year value transfers for property owners whose property has been damaged or destroyed in a disaster for which the Governor proclaimed a state of emergency. In addition, subject to many conditions, the law[37] allows homeowners at least age 55 years or qualified disabled persons to sell their existing home (called the "original property"), buy or build a new one, and transfer their base year value to the new home (replacement home).

**Disaster Relief – Intracounty Transfers.** Existing law[38] allows a person who owns property substantially damaged or destroyed in a Governor-proclaimed disaster to transfer the base year value of the damaged property to a comparable replacement property, as long as the replacement property is:

- Located within the same county,
- Purchased or newly constructed within five years of the date the disaster occurred, and

[36] Article XIII A, section 2.
[37] Article XIII A, section 2(a), RTC section 69.5.
[38] RTC section 69.

- Similar in size, utility, and function.
    - Property is similar in *size and utility* if the market value of the acquired property does not exceed 120 percent of the fair market value of the damaged or destroyed property in its pre-damaged condition. If the market value of the replacement property exceeds 120 percent, partial relief is available. Specifically, the value above 120 percent is added to the transferred base year value.
    - Property is similar in *function* if the replacement property is subject to similar governmental restrictions, such as zoning. The replacement property must be used in the same manner as the damaged or destroyed property.

Any type of property that is damaged or destroyed in a disaster for which the Governor proclaimed a state of emergency may qualify for this intracounty base year value transfer, including multifamily, commercial, or industrial property.

**Disaster Relief – Intercounty Transfers.** Existing law[39] allows a homeowner whose principal residence was substantially damaged or destroyed in a Governor-proclaimed disaster to transfer the base year value to a replacement property that is purchased or newly constructed in a different county, as long as the replacement property is:

- Located in a county that has enacted an ordinance,[40]
- Purchased or newly constructed within three years of the date of the disaster,
- The principal residence of the property owner, and
- Of equal or lesser value.

Equal or lesser value means the current market value of the replacement property must be *equal to or less than* the market value of the damaged property immediately prior to the damage. A replacement property is considered comparable if its full cash value does not exceed one of the following:

- **105 percent** if the replacement property is purchased or newly constructed *within the first year* following the date of the damage or destruction of the original property
- **110 percent** if the replacement property is purchased or newly constructed *within the second year* following the date of the damage or destruction of the original property.
- **115 percent** if the replacement property is purchased or newly constructed *within the third year* following the date of the damage or destruction of the original property.

If the replacement home exceeds the applicable value test, the base year value transfer is unavailable. There are no provisions in law for partial relief in these circumstances.

[39] RTC section 69.3.

[40] Contra Costa, Los Angeles, Modoc, Orange, San Francisco, Santa Clara, Solano, Sonoma, Sutter, and Ventura Counties.

A claim for relief must be filed with the county assessor of the county in which the replacement property is located. The claim must be filed within three years after the replacement property is acquired or newly constructed. No prospective relief is available for late-filed claims.

**Over 55/Disabled Base Year Value Transfer.** Existing law[41] allows homeowners at least age 55 years or qualified disabled persons to sell their existing home (called the "original property"), buy or build a new one, and transfer their base year value to the new home (replacement home). This benefit gives homeowners property tax relief by allowing property taxes to remain essentially the same[42] after the move, provided they purchase a home of equal or lesser value. The replacement home must be purchased within 2 years, before or after, the original property's sale.

- **Principal Place of Residence.** To qualify for this benefit, both the original property and the replacement home must be eligible for either the homeowners' or the disabled veterans' exemption, based on the claimant's ownership and occupation of the home as a principal place of residence.[43]
- **Location Limitation.** The replacement home must be located either (1) in the same county as the original property, or (2) in a county that has enacted an ordinance accepting "intercounty" transfers. Currently, the 10 counties that have enabling ordinances are Alameda, Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Mateo, Santa Clara, Tuolumne, and Ventura.
- **One-Time Benefit.** Current law[44] allows homeowners to use this base year value transfer only one time. The sole exception is that if a homeowner is granted the age 55 base year value transfer, the homeowner may transfer the base year value a second time if the homeowner subsequently becomes physically and permanently disabled and must move because of the disability.

  **Statewide Tracking Database.** To monitor and enforce this one-time base year value transfer limit statewide, the law[45] requires the BOE to maintain a database to track persons granted a base year value transfer. When married persons file a claim to transfer the base year value of their current home to a newly purchased home to which they share title, their names and pertinent information are entered in the database. This ensures that neither person will be allowed a future transfer.
- **Value Limit.** To qualify for this benefit, the replacement home's market value as of the date of purchase must be *equal to or less than* the original property's market value on the date of its sale. If the replacement home does not satisfy the "equal or lesser value" test, then the benefit is not available. The meaning of "equal or lesser value" depends on when

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[41] Article XIII A, section 2(a); RTC section 69.5.
[42] The property tax bill for the new home may not be identical to the property tax bill of the original home because the precise tax rate and direct levies (special assessments, parcel taxes, etc.) differ for each home's location.
[43] RTC sections 69.5(b)(2), 69.5(b)(4), and 69.5(g)(10).
[44] RTC section 69.5(b)(7).
[45] *Ibid*.

the replacement home is purchased or newly constructed. In general, equal or lesser value means:[46]

- **100 percent** or less of the market value of the original property if a replacement home was purchased or newly constructed *before* the sale of the original property, or
- **105 percent** or less of the market value of the original property if a replacement home was purchased or newly constructed *within the first year* after the sale of the original property, or
- **110 percent** or less of the market value of the original property if a replacement home was purchased or newly constructed *within the second year* after the sale of the original property.
- If the replacement home exceeds the applicable value test, the base year value transfer is unavailable. There are no provisions in law for partial relief in these circumstances.

- A claim for relief must be filed with the county assessor of the county in which the replacement home is located. The claim must be filed within three years after the replacement home is acquired or newly constructed. If the claim is filed after the three-year deadline, prospective relief is available.[47]

**Amended Law:** If approved by the voters, this bill adds section 2.1 to article XIII A of the California Constitution. Operative April 1, 2021, these provisions allow homeowners who are over age 55, severely disabled, or victims of wildfire or natural disasters to transfer a base year value to a replacement home anywhere in California, regardless of the location or value.

**Original Property.** This bill requires the original property be sold.

**Replacement Property.** The replacement property must be purchased or newly constructed within two years of the sale of the original property.

**Location.** This bill allows a replacement property to be located anywhere in California.

**Value.** This bill allows the base year value to be transferred to a home of equal or lesser value. If the value of the replacement home is greater than the value of the original property, the difference in market values will be added to the transferred base year value of the original property.

**Limitation on Number of Base Year Value Transfers.** This bill allows persons over age 55 or severely disabled to transfer their base year value only three times.

**Victim of Wildfire or Natural Disaster.** This bill provides that "victim of a wildfire or natural disaster" means the owner of a primary residence which has been substantially damaged as a

[46] RTC section 69.5(g)(5).
[47] RTC section 69.5(f).

result of a wildfire or natural disaster that amounts to more than 50 percent of the improvement value of the primary residence immediately before the wildfire or natural disaster. This bill also provides that "damage" includes a diminution in the value of the primary residence as a result of restricted access caused by the wildfire or natural disaster. In addition, this bill provides the following definitions for wildfire and natural disaster.

- "Wildfire" has the same meaning as defined in GC section 51177(j), which is an unplanned, unwanted wildland fire, including unauthorized human-caused fires, escaped wildland fire use events, escaped prescribed fire projects, and all other wildland fires where the objective is to extinguish the fire.
- "Natural disaster" means the existence, as declared by the Governor, of conditions of disaster or extreme peril to the safety of persons or property within the affected area caused by conditions such as fire, flood, drought, storm, mudslide, earthquake, civil disorder, foreign invasion, or volcanic eruption.

**Filing.** This bill requires the homeowner to file an application with the county assessor where the replacement property is located.

**In General:** **Property Tax System.** In 1978, voters approved Proposition 13, which added article XIII A to the California Constitution. Under this system, property is valued at its 1975 fair market value, with annual increases thereafter limited to the amount of inflation or 2 percent, whichever is less, until the property changes ownership or new construction occurs. Once a reassessable event occurs (i.e., a change in ownership or new construction), the value of the property for tax purposes is redetermined based on its current market value. The value initially established, or redetermined where appropriate, is referred to as the "base year value." Because real estate values generally appreciate at a rate greater than 2 percent per year, when an event occurs triggering a reassessment of property to its current market value, the reassessed value (i.e., its new base year value) will likely be substantially higher.

California property tax law provides for various situations where the base year value of a property is either: (1) retained, notwithstanding that new construction has taken place or that the property has changed ownership, or (2) transferred to another property, notwithstanding that the property has changed ownership. These special situations are provided pursuant to various constitutional amendments modifying the original Proposition 13 framework and serve to avoid the otherwise required reassessment of a property to its current market value.

**Disaster Relief.** There are a variety of provisions in property tax law to provide property tax relief for disaster victims. These provisions address both the short-term and the long-term consequences of the disaster as it relates to current and future property tax liabilities. In the short term, property tax liability is redetermined to reflect the damage to the property. Additionally, some taxpayers may defer the next property tax installment payment. Over the long term, property owners may rebuild or repair damaged properties without incurring any increase in property tax liability. Alternatively, property owners may relocate rather than rebuild without being adversely impacted by the property tax consequences.

The various provisions of the RTC that provide property tax relief for disaster victims are as follows:

| RTC | Property Type | Type of Relief Available | Type of Disaster |
|---|---|---|---|
| Section 70 | All property types | New construction exclusion | Any disaster or calamity |
| Section 170 | All property types | Removal of value; New construction exclusion | Governor-proclaimed; Any disaster or calamity |
| Section 69 | All property types | Base year transfer within same county | Governor-proclaimed |
| Section 69.3 | Principal place of residence | Base year transfer to another county | Governor-proclaimed |
| Sections 172 & 172.1 | Manufactured home (license fee or property tax) | Base year transfer | Governor-proclaimed |
| Section 5825 | Manufactured home (property tax only) | Base year transfer; new construction exclusion | Any disaster or calamity |
| Section 194 | Real property and manufactured homes | Property tax deferral | Governor-proclaimed |

**Disaster New Construction Exclusion.** Related to the subject matter of this bill, RTC section 70(c) provides that "where real property has been damaged or destroyed by misfortune or calamity, 'newly constructed' and 'new construction' does not mean any timely reconstruction of the real property, or portion thereof, where the property after reconstruction is substantially equivalent to the property prior to damage or destruction." Any reconstruction of real property, or portion thereof, that is not substantially equivalent to the damaged or destroyed property, is treated as new construction. If this occurs, only that portion that exceeds what is deemed to be substantially equivalent reconstruction would be assessed at current market value. RTC section 70(c) does not provide any time limitation as to what is considered "timely" new construction for purposes of the exclusion.

Under this provision, however, reconstruction that does qualify means that the property will retain its previous assessed value after its reconstruction. Consequently, a property that is rebuilt after a fire will continue to be assessed at the same value even though the entire property has been newly constructed. (This new construction exclusion was provided by Proposition 8 in 1978).

**Disaster Base Year Value Transfers.** Voters have approved two constitutional amendments permitting persons to transfer their Proposition 13 base year value from one home to another in disaster situations. The base year value transfer avoids reassessment of the newly purchased home to its fair market value.

- **Intracounty.** In 1986, Proposition 50 amended the Constitution to allow property owners whose property was damaged or destroyed in a Governor-declared disaster to transfer its base year value to comparable property within the same county (implemented by RTC section 69).
- **Intercounty.** In 1993, Proposition 171 amended the Constitution to allow homeowners whose principal residence was damaged or destroyed in a Governor-declared disaster to be transferred to a replacement residence of equal or lesser value and located in another county if that county has enacted an ordinance approving such transfers (implemented by RTC section 69.3).

Specifically related to this bill, RTC section 69 provides that persons who own property substantially damaged or destroyed in a Governor-declared disaster may transfer the base year value of that property to a property acquired or constructed as a replacement if it is acquired within five years after the disaster. "Substantially damaged" means physical damage amounting to more than 50 percent of its current market value immediately prior to the damage. Base year value transfers are available for all property types, with the limitation that the original property and the replacement property must be of the same property *type*: residential, commercial, agricultural, or industrial. The replacement property is "comparable" if it is similar in size, utility, and function to the destroyed property, and if the market value of the acquired property does not exceed 120 percent of the fair market value of the replaced property in its pre-damaged condition. If the value of the replacement property exceeds the 120 percent limitation, the amount over this threshold is assessed at full market value and added to the transferred base year value.

RTC section 69.3 provides similar disaster base year value transfer provisions but, unlike RTC section 69, which applies to all property types, it is limited to principal places of residence purchased in another county where the board of supervisors has adopted an ordinance making this benefit available. Additionally, replacement homes must be purchased within three years rather than five years. Currently, there are 13 counties that have such an ordinance: Contra Costa, Glenn, Los Angeles, Modoc, Orange, San Diego, San Francisco, Santa Clara, Solano, Sonoma, Sutter, Ventura, and Yuba.

If a property owner transfers their base year value under either RTC section 69 or 69.3, then the new construction exclusion under RTC section 170 does not apply if the property owner subsequently rebuilds the damaged or destroyed structure.

**Over 55/Disabled Base Year Value Transfers.** Voters have approved three constitutional amendments permitting persons over age 55 or disabled to transfer their Proposition 13 base year value from one home to another that is of equal or lesser value. The base year value transfer avoids reassessment of the newly purchased home to its fair market value.

- **Intracounty.** In 1986, Proposition 60[48] amended the constitution to allow persons who are over the age of 55 to sell a principal residence and transfer its base year value to a replacement principal residence within the same county.
- **Intercounty.** In 1988, Proposition 90[49] amended the constitution to extend these provisions to a replacement residence located in another county on a county-optional basis. Relevant to this bill, the law gives each county board of supervisors the option to accept intercounty base year value transfers from homeowners moving from a different county. The boards of supervisors are required to consult with local affected agencies, cities, special districts, school districts, and community college districts, before making the decision to enact a necessary local ordinance.
- **Disabled Persons**. In 1990, Proposition 110[50] amended the constitution to extend these provisions to any severely and permanently disabled person regardless of age.

RTC section 69.5 implements all three propositions.

The BOE's Assessors' Handbook Section 401, *Change in Ownership*, chapter 14, provides more details, and the BOE's website includes FAQ's for Propositions 60/90 and Proposition 110.

## Background:

**Disaster Relief.** Initially, a replacement property located within the same county had to be purchased within two years of the date of the disaster. In 1993, AB 1824 (Stats. 1993, ch. 1053) extended the timeframe from 2 years to 3 years for all disasters occurring on or after October 20, 1991, the date of the Oakland Hills fire. In 1997, SB 594 (Stats. 1997, ch. 353) created a special 5-year period for any victim of the 1994 Northridge earthquake. In 2006, AB 1890 (Stats. 2006, ch. 317) extended the timeframe for RTC section 69 base year value transfers from 3 years to 5 years for all disasters occurring on or after July 1, 2003.

In 2018, two bills were introduced that would have allowed a base year value transfer to any county in California for property that was substantially damaged or destroyed by a Governor-proclaimed disaster that occurred between January 1, 2017 and July 1, 2018. ACA 20 (Steinorth) proposed changes to article XIII A, section 2, but was not assigned to committee. ACA 20 did not have a companion measure. SB 1091 (Stone) proposed changes to RTC section 69 that would have been operative upon voter approval of a constitutional amendment that was not introduced; SB 1091 was held in the Senate Appropriations Committee.

**Over 55/Disabled Base Year Value Transfer.** The following table lists previous legislative attempts to allow a partial benefit for replacement homes of greater value.

[48] Proposition 60, approved November 4, 1986.
[49] Proposition 90, approved November 8, 1988.
[50] Proposition 110, approved June 5, 1990.

| Bill Number | Session | Author | Disposition |
|---|---|---|---|
| SCA 24 | 2017-18 | Galgiani | Not assigned to committee. |
| ACA 20 / AB 1748 | 2017-18 | Steinorth | ACA 20 was not heard. AB 1748 failed passage in the Assembly Revenue and Taxation Committee. |
| ACA 12 / AB 2668 | 2015-16 | Mullin | ACA 12 was not heard. AB 2668 was held in the Assembly Appropriations Committee. |
| SCA 9 / SB 378 | 2015-16 | Beall | SCA 9 did not pass out of the Senate Elections and Constitutional Amendments Committee. SB 378 was held in the Senate Appropriations Committee. |
| SCA 11 / SB 274 | 2009-10 | Dutton | Did not pass out of Senate Revenue and Taxation Committee. This bill also expanded the purchase window from within two years to three years of the original property's sale date. |
| SCA 24 / SB 1610 | 2007-08 | Dutton | Did not pass out of Senate Revenue and Taxation Committee. This bill also expanded the purchase window from within two years to three years of the original property's sale date. |

The following table lists previous legislative attempts to require all counties to accept intercounty base year value transfers.

| Bill Number | Session | Author | Disposition |
|---|---|---|---|
| ACA 7 | 2017-18 | Bocanegra | Not assigned to committee. |
| AB 1172* as amended 3/21/13 | 2013-14 | Bocanegra | Limited to persons 65+. Not heard with the intercounty provisions. Amended out 01/06/14. |
| SCA 31 / SB 1415 | 2009-10 | Walters | Not heard. |
| ACA 39 / AB 1960 | 1997-98 | Takasugi | Held in Assembly Appropriations Committee. |
| ACA 57 / AB 3234 | 1987-88 | Mojonnier | Not heard. |

* Assembly Bill 1172 only applied to homeowners 65 years and older. Those between the ages of 55 and 64 remained limited to the county in which they currently reside or those counties with active ordinances.

Assembly Bill 1172, as amended January 6, 2014, would have required the California Research Bureau to evaluate the revenue impact if California enacted a statute similar to Florida's "Save Our Homes" portability statute. (Florida Stat., Sec. 193.155(8); we note that Florida's program is not age-restricted.) These provisions were amended out of that bill. However, a study was conducted under the Faculty Fellows Program. In 2016, The Center for California Studies published *Economic Impacts of a Property Assessment Portability Law*, by Dr. Adrian R. Flessig, California State University, Fullerton. The study concluded that Florida's portability law "will provide an additional incentive for residential property owners to sell their home and purchase another residence. This will increase turnover rates and homeowner mobility."

**Prior Initiative.** Proposition 5 on the November 6, 2018 ballot would have amended section 2 of article XIII A to allow a base year value transfer for property owners whose property has been substantially damaged or destroyed in a Governor-proclaimed disaster or homeowners age 55 or severely disabled to a replacement property located anywhere in California and of any value. If the market value of the replacement property is greater than the market value of the original property, the increase in value would be added to the transferred base year value. If the market value of the replacement property is less than the market value of the original property, there would be a proportional decrease in the transferred base year value. Proposition 5 failed to pass, 58.7 percent no to 41.3 percent yes.

## Commentary:

1. **No Companion Measure.** This constitutional amendment does not have an implementing companion measure.

2. **Conflicting Base Year Value Transfers.** Article XIII A, sections 2(a) and (e) provide base year value transfers for homeowners age 55/disabled and disaster relief. Does the author intend to replace these base year value transfers or add an additional base year value transfer that is limited to homeowners? We note that the existing disaster intercounty base year value transfer applies to any type of property, including commercial, industrial, and multifamily residential. While this bill provides a sunset date for the parent-child and grandparent-grandchild exclusion in section 2(h) of article XIII A, this bill does not provide a sunset date for the base year value transfers contained in sections 2(a) and (e). Consequently, this bill creates a new base year value transfer for homeowners, in addition to the existing base year value transfers. The competing base year value transfers may be confusing to homeowners.

3. **Sale of Original Property.** ACA 11 requires the original property to be sold and the replacement home must be purchased within two years of the sale in order to transfer the base year value. For property that has been damaged or destroyed, this two-year period may be difficult to meet if the homeowner purchases a replacement home first and then must sell the damaged or destroyed home within two years.

4. **New Value Comparison Test.** Currently, the market value of the replacement home on its date of purchase or completion of new construction is compared to the market value of the original property on its date of sale.

   For property that has been substantially damaged or destroyed, the market value just prior to the date of damage or destruction is used. For homeowners who have lost their home in a disaster, they can transfer their base year value to a replacement home within the same county that is 120 percent of the value of the home that was damaged or destroyed. Under this scenario, partial relief is available. Since this bill replaces the 120 percent value test with a 100 percent value test, this will mean that homeowners who stay in the same county will pay more if they buy a home of greater value.

For persons who are at least age 55 or disabled, if the replacement home's market value is equal or less than 100, 105, or 110 percent of the original property's market value (depending on the replacement home's date of purchase or completion of new construction and the original property's date of sale), then the replacement home will qualify value-wise for the base year value transfer). If the replacement home's value exceeds the applicable value test, no partial relief is available. Under this proposal, the equal or lesser value test is replaced with a 100 percent test. If the replacement home is of greater value, the difference in values is added to the original property's base year value so that partial relief is available.

For example, a couple sells their principal place of residence for $600,000. At the time of sale, this property had a factored base year value of $269,250.

- **Home of Greater Value.** If this couple purchases a replacement dwelling for $800,000, the new base year value is calculated as follows.
  - Difference between the full cash value of the original property and the full cash value of the replacement dwelling:

    $800,000 - $600,000 = $200,000

  - Add the difference to the base year value of the original property:

    $269,250 + $200,000 = $469,250

  Under this scenario, the replacement dwelling's new base year value is $469,250.

- **Home of Equal or Lesser Value.** If this couple purchases a replacement dwelling for $600,000, the replacement dwelling's new base year value will be the same as the factored base year value of the original property ($269,250).

- **Wildfire and Natural Disaster.** This bill provides definitions of wildfire and natural disasters by reverence to existing statutes. The meaning could change if the existing statutes are changed. The existing disaster base year value transfers apply to any disaster for which the Governor declares a state of emergency. By adding such definitions, this bill limits the application of this new base year value transfer to these itemized events.

- **Choice of relief.** Under current law, if a property owner chooses to transfer the base year value to another property under either of the disaster relief base year value transfers (RTC sections 69 and 69.3), the new construction exclusion under RTC section 70(c) or 170 is no longer available. If the substantially damaged or destroyed improvement is repaired or reconstructed, the new construction will be reassessed to current market value upon completion of construction.

5. **Number of Base Year Value Transfers for Homeowners Age 55 or Disabled.** Currently, persons over age 55 or disabled can transfer a base year value to a replacement home or a unit of a multi-unit dwelling generally one time. This bill allows three base year value transfers for homeowners who are over 55 or disabled.

## Parent-Child and Grandparent-Grandchild Exclusion

**Existing Law:** The law requires assessors to reassess real property from its Proposition 13 protected value (called the "base year value") to its current market value whenever a change in ownership occurs.[51] Exceptions to this reassessment requirement have been enacted, including exclusions from reassessment for transfers between parents and children. Under certain circumstances, the parent-child exclusion is extended to transfers of real property from grandparents to grandchildren.

Existing law[52] provides that the terms "purchased" and "change in ownership" does not include the purchase or transfer of a principal residence, or the first $1 million of all other real property, between parents and their children.

**Amended Law:** Operative February 16, 2021, this bill replaces the existing parent-child and grandparent-grandchild exclusion with a new parent-child and grandparent-grandchild exclusion that applies to a transfer of a family home, if the property continues as the family home of the transferee.

**Family Home.** This bill provides that "family home" includes a family farm, which means any real property that is under cultivation or being used for pasture or grazing or to produce any agricultural commodity, defined as any and all plant and animal products produced in California for commercial purposes.[53]

**Principal Residence Value Test.** This bill provides that the existing adjusted base year value of the principal residence will remain if the reassessed value is less than the sum of the adjusted base year value of the principal residence of the transferor plus $1 million. If the reassessed value is equal to or exceeds the sum of the adjusted base year value of the principal residence of the transferor plus $1 million, then the difference between (1) the sum of the adjusted base year value plus $1 million, and (2) the reassessed value, is to be added to the property's existing adjusted base year value.

**Adjustment of $1 Million.** This bill requires that, beginning February 16, 2023, the $1 million amount be annually adjusted by an inflation factor that is the percentage change in the House Price Index (HPI) for California for the prior calendar year, as determined by the Federal Housing Finance Agency. This bill requires the BOE to calculate and publish the adjustments required.

**Principal Place of Residence.** To qualify for this benefit, the home must be the principal residence of the transferee and requires the transferee to file for the homeowners' or disabled veterans' exemption. This bill provides that if the transferee fails to file for either exemption at the time of

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[51] Article XIII A, section 2.
[52] Article XIII A, section 2(h), and RTC section 63.1.
[53] GC section 51201 provides that "agricultural commodity" means any and all plant and animal products produced in California for commercial purposes, including, but not limited to, plant products used for producing biofuels, and industrial hemp cultivated in accordance with Food and Agricultural Code division 24 (commencing with section 81000).

transfer, the transferee is eligible for prospective relief if the claim for the homeowners' or disabled veterans' exemption is filed within one year of the transfer.

**Grandparent-Grandchild Middle Generation Limitation.** This bill provides that the exclusion applies to a transfer between grandparents and grandchildren if all of the parents of those grandchildren, who qualify as children of the grandparents, are deceased as of the date of the purchase or transfer.

**In General:** In 1986, the voters approved Proposition 58, which, in part, added subdivision (h) to section 2 of article XIII A of the California Constitution. Subdivision (h) provides that the terms *purchased* and *change in ownership* exclude the purchase or transfer of:

- A principal residence between parents and their children. There is no limit as to the value of the residence or how many principal residences may be transferred.
- The first $1 million of the base year value[54] of all real property other than a principal residence between parents and children (called "other property"). Each person may transfer real property to any combination of parents and/or children up to $1 million cumulatively over a lifetime.

RTC section 63.1 implements the parent-child exclusion. The parent-child exclusion applies to changes in ownership that occur on or after November 5, 1986.

In 1996, the voters approved Proposition 193, which amended subdivision (h) to extend the parent-child exclusion to transfers from grandparents to grandchildren if certain members of the intervening parent generation are deceased. RTC section 63.1 was subsequently amended to reflect these new provisions. The grandparent-grandchild exclusion applies to changes in ownership that occur on or after March 27, 1996.

To qualify for this exclusion, a claim form must be timely filed with the county assessor. If a claim is filed late, prospective relief is available if the transferee still owns the real property.

**Principal Place of Residence.** For a principal place of residence, there is no limit as to value or how many times a principal residence can be transferred to a qualifying parent, child, or grandchild. To qualify for the principal residence exclusion, the real property must be eligible for either the homeowners' exemption or the disabled veterans' exemption, based on the property owner's ownership and occupation of the home as a principal place of residence.[55] A "principal residence" includes only that portion of the land underlying the residence that consists of an area of reasonable size that is used as a site for the residence.

[54] Article XIII, section 2(h) uses the term "full cash value." RTC section 63.1 provides that "full cash value" means full cash value as defined in RTC section 110.1, which describes a property's base year value, not its current market value.
[55] RTC sections 63.1(b)(1).

**Statewide Tracking Database.** To monitor and enforce the $1 million limit statewide, assessors report information from approved claims[56] to the BOE to maintain a database to track the $1 million limit of transferors who transfer "other property" that receives the parent-child or grandparent-grandchild exclusion. The transferors' names and pertinent information are entered in the database. When a transferor cumulatively transfers more than $1 million of adjusted base year value, a report is sent to the county assessors to take action (i.e., verify information and, if necessary, reassess).

## Commentary:

1. **No Companion Measure.** This constitutional amendment does not have a companion measure that implements these provisions.

2. **Principal Residence Exclusion.** Currently, each transferor may transfer any number of principal residences to an eligible parent or child, or grandchild (under limited circumstances). There is no limit as to the value of a principal residence and no limit as to the number of principal residences a transferor can transfer to an eligible parent or child over a lifetime. A grandparent may transfer a principal residence to a grandchild as long as the deceased parent did not transfer a principal residence to their child (i.e., the grandchild); if the deceased parent transferred a principal residence to their child, then the grandparent's residence that transfers to the same child/grandchild is counted under the $1 million exclusion.

3. **Change in Ownership Exclusion.** Under article XIII A, property is reassessed to current market value upon a change in ownership. This bill provides that the purchase or transfer of a family home between parents and children and, under certain circumstances, between grandparents and grandchildren, is not a change in ownership. This means that the property retains its existing factored base year value and is not reassessed to current market value. However, this bill provides that a new taxable value (defined as a base year value) will be calculated.

4. **Principal Residence Value Test.** Under this bill, if the assessed value of the principal residence is *less than* the sum of the property's adjusted base year value and $1 million, it appears that the property's adjusted base year value will remain the same. If the assessed value of the principal residence is *equal to or greater than* the sum of the adjusted base year value and $1 million, then the difference between (1) the sum of the adjusted base year value and $1 million, and (2) the reassessed value, is to be added to the adjusted base year value. The term "assessed value" is not defined. This bill appears to require that all principal residences that transfer between parent and child be reappraised to verify qualification. This additional workload on the county assessor's appraisal staff could delay the approval of claims for the parent-child or grandparent-grandchild exclusion.

[56] RTC section 63.1(f).

5. **Exclusion Amount Adjustment.** This bill provides that the $1,000,000 amount be annually adjusted by the percentage change in the California HPI, rounded to the nearest one-thousandth of 1 percent, for the first three quarters of the prior calendar year, as determined by the Federal Housing Finance Agency. Base year values are annually adjusted by the percentage change in the California Consumer Price Index from October to October, not to exceed two percent.[57]

6. **Exclusion Amount Adjustment: Negative housing price index changes**? On occasion, the change in the housing price index (HPI) is negative. This bill provides that the assessor is to adjust the $1,000,000 amount by the difference in the HPI. Thus, it appears that assessors would be required to reduce the $1,000,000 amount when the HPI is negative. Why use the HPI? Other property tax annual inflationary adjustments (i.e., base year values and the disabled veterans' exemption limits[58]) are based on the California Consumer Price Index, which is generally considered a more stable index than the California HPI.

7. **Family Home includes Family Farm.** This bill specifies that the term "family home" also includes a family farm, which is defined as any real property under cultivation or being used for pasture, grazing, or production of any agricultural commodity. "Agricultural commodity" is defined as any and all plant and animal products produced in California for commercial purposes. This prohibits the exclusion from applying to the family-owned corner grocery store where the family home is on the second story. This bill creates an inequity between a family farm and other types of mixed-use properties that include a family home.

8. **Principal Residence of Transferee.** Under this proposal, the principal residence qualifies for the exclusion only if the property is the principal residence of the transferee and the transferee timely files for the homeowners' or disabled veterans' exemption. There is no requirement that the property be the principal residence of the transferor.

9. **Filing period.** This bill requires the transferee to file for the homeowners' or disabled veterans' exemption at the time of the transfer or purchase. If the transferee does not file for the homeowners' or disabled veterans' exemption at the time of the transfer, the transferee may get prospective relief if they file for the homeowners' or disabled veterans' exemption within one year of the date of transfer. There is no relief available, if the transferee fails to file for either exemption within one year. This bill does not provide any filing requirements for the parent-child or grandparent-grandchild exclusion.

[57] RTC sections 51(a)(1)(c).

[58] RTC sections 51(a)(1)(c) and 205.5(h).

## Senate Bill 364 (Mitchell), Chapter 58
*Nonresidential Active Solar Energy System Exemption*

*Effective September 9, 2020; operative only if Proposition 15 is approved.*[59]

*Amends section 73 of; adds Chapter 4.5 (commencing with section 83) to; and amends, repeals, and adds sections 105, and 106 of, the Revenue and Taxation Code.*

**Summary:** Subject to voter approval of Proposition 15 on the November 3, 2020 ballot, this bill specifies that nonresidential active solar energy systems are personal property and creates an exemption for nonresidential active solar energy systems until the solar energy system undergoes a subsequent change in ownership.

**Existing Law:** Under article XIII, section 1, of the California Constitution, all property is taxable and assessed at fair market value, unless otherwise provided by the California Constitution or the laws of the United States.

Personal property includes all property, except real property.[60] "Real property" includes land; all mines, minerals, and quarries in the land; all standing timber; and improvements.[61] "Improvements" include all buildings, structures, fixtures, and fences erected on or affixed to the land; all fruit, nut bearing, or ornamental trees and vines, not of natural growth, and not exempt from taxation, except date palms under eight years of age.[62] A "fixture" is considered real property if it is physically or constructively attached to real property with the intent that it remain attached indefinitely.[63]

**Personal Property Taxation.** Section 2 of article XIII authorizes the Legislature to provide for property taxation of tangible personal property. Generally, all tangible personal property is taxable except where specific exemptions are provided. Examples of taxable tangible personal property include portable machinery and equipment, office furniture, tools, and supplies. Examples of current exemptions include business inventories, personal household furnishings, personal effects, and pets.

Personal property is annually assessed at its current market value to persons owning, claiming, possessing, or controlling it on the lien date, January 1.

**Assessment of Interests in Real Property.** Section 2 of article XIII A of the California Constitution limits the assessed value of property upon which the property tax is imposed. For property tax purposes, real property is reassessed to its current market value when real property undergoes a change in ownership or is newly constructed.[64]

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[59] Proposition 15 on the November 3, 2020 ballot failed, 48 percent yes to 52 percent no.
[60] RTC section 106.
[61] RTC section 104.
[62] RTC section 105.
[63] Property Tax Rule 122.5.
[64] California Constitution, article XIII A, section 2; RTC section 110.1.

A change in ownership is a transfer of a present interest in real property, including the beneficial use thereof, the value of which is substantially equal to the value of the fee interest.[65] Generally, the law establishes a property's assessed value at its market value[66] on the date it changes ownership (base year value) and requires additional assessments to reflect certain construction activities that qualify as "new construction." The law requires the assessor to establish a "base year value" for real property at its 1975 market value and thereafter reset the value to current market value every time the property changes ownership or new construction is completed.[67] The base year value must be compounded annually by an inflation factor not to exceed 2 percent.[68] The inflation-adjusted value is called the "factored base year value."

**Transfer of Interests in Legal Entities.** RTC section 64 sets forth the change in ownership provisions for the purchase or transfer of ownership interests in legal entities (e.g., stock in a corporation, membership interests in a limited liability company, or interests in a partnership) that own real property. As a general rule, under RTC section 64(a), transfers of ownership interests in legal entities do *not* constitute a change in ownership (and, therefore, no reassessment) of the legal entity's real property. However, there are two exceptions wherein the transfer of ownership interests in a legal entity would trigger a change in ownership:

- **Change in Legal Entity Control.** RTC section 64(c)(1) requires reassessment when any person or entity obtains control through direct or indirect ownership or control of more than 50 percent of corporation voting stock, or obtains more than a 50 percent ownership interest in any other type of legal entity. The reassessment applies to all real property owned by the acquired legal entity (and any entity under its control).

- **Cumulative Transfers by "Original Co-owners**." RTC section 64(d) requires reassessment when voting stock or other ownership interests representing cumulatively more than 50 percent of the total interests in a legal entity are transferred by any of the "original co-owners" in one or more transactions.[69] The reassessment applies to only the real property previously excluded from change in ownership under RTC section 62(a)(2).

**New Construction.** When substantial additions or alterations occur, the law requires the assessor to increase the assessment to reflect the value of "newly constructed" property.[70] The

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[65] RTC section 60.

[66] The assessed value is based on 1975 market value for property that has not changed ownership since that date.

[67] RTC section 110.1(a) and (b).

[68] RTC sections 110.1(f) and 51.

[69] **Proportional Ownership Interests Exclusion Creates "Original Co-owner" Designation.** Under RTC section 62(a)(2), a transfer of real property to a legal entity does not result in a reassessment if the transfer is merely a change in the method of holding title and the proportional ownership interests in the real property are *exactly* the same before and after the transfer. However, after a transfer of real property qualifies for this exclusion from reassessment, the persons holding ownership interests in the legal entity immediately after the transfer are considered "**original co-owners**" for purposes of tracking subsequent transfers by original co-owners of those interests. When such transfers cumulatively exceed 50 percent, the real property previously excluded from reassessment under RTC section 62(a)(2), is deemed to undergo a change in ownership, and is, therefore, subject to reassessment under RTC section 64(d).

[70] Article XIII A, section 2 of the California Constitution (Proposition 13) and RTC section 70. Additionally, "supplement assessment" laws make the new construction taxable as of the completion date.

assessor assigns the assessable new construction with its own distinct base year value. The remainder of the property's assessment is unaffected and retains its base year value.[71] The Constitution allows the Legislature to provide that the term "newly constructed" does not include certain construction activities. These are commonly called "new construction exclusions." Any value added by these additions or alterations is not subject to the property tax, until the real property undergoes a change in ownership.

**Active Solar Energy System New Construction Exclusion.** The California Constitution[72] grants the Legislature the authority to exclude the construction or addition of any active solar energy system from the definition of assessable new construction. RTC section 73 implements the new construction exclusion, which is available through the 2023-24 fiscal year. RTC section 73 is scheduled to sunset on January 1, 2025. Any active solar energy system that was excluded prior to this date will continue to be excluded until a change in ownership occurs.

**Amended Law:** Subject to voter approval, until January 1, 2025, this bill provides that nonresidential active solar energy systems are personal property and exempt from taxation until the system undergoes a subsequent change in ownership.

**Effective Date.** This bill takes effect upon voter approval of Proposition 15 on the November 3, 2020 ballot, which proposes to add section 2.5 to article XIII A of the California Constitution. If enacted, effective with the operative date, the new construction exclusion contained in RTC section 73 will not apply to nonresidential active solar energy systems. The bill's proposed exemption of nonresidential active solar energy systems will apply to systems installed on or before January 1, 2025.

**Intent.** This bill specifies that it is the intent of the Legislature to ensure that active solar energy systems that would have been exempt from taxation because of the new construction exclusion continue to be exempt from taxation until there is a subsequent change in ownership of the active solar energy system.

**New Construction Exclusion for Active Solar Energy Systems.** This bill specifies that the existing new construction exclusion for active solar energy systems will not apply to nonresidential active solar energy systems, if this bill becomes operative.

**Nonresidential Active Solar Energy System.** A "nonresidential active solar energy system" is a system that uses solar devices to provide for the collection, storage, or distribution of solar energy, and that is not constructed or installed in or on residential property. Such a system does not include solar swimming pool or hot tub heaters.

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[71] Unless the new construction replaces certain types of existing improvements, in which case the value attributable to those preexisting improvements is deducted from the property's existing base year value.
[72] Article XIII A, section 2(c)(1).

A nonresidential active solar energy system may be used for any of the following:

- Recreational, therapeutic, or service water heating
- Space conditioning
- Production of electricity
- Heat processing
- Solar mechanical energy

Generally, the use of solar energy in the production of electricity involves the transformation of sunlight into electricity through the use of devices such as solar cells or other solar collecting equipment. A nonresidential active solar energy system includes storage devices, power conditioning equipment, transfer equipment, and parts related to the functioning of those items. "Parts" includes spare parts that are owned by the owner of, or maintenance contractor for, an active solar energy system for which the parts were specifically purchased, designed, or fabricated for installation in that system. Such a system includes only equipment used up to, but not including, the stage of conveyance or use of the electricity.

A nonresidential active solar energy system also includes pipes and ducts that are used exclusively to carry energy derived from solar energy. Pipes and ducts that are used to carry both energy derived from the sun and energy derived from other sources may be considered part of the nonresidential active solar energy system property only to the extent of 75 percent of their full cash value.

A nonresidential active solar energy system does not include auxiliary equipment, such as furnaces and hot water heaters, that use a source of power other than solar energy to provide usable energy. Dual use equipment, such as ducts and hot water tanks, that is used by both auxiliary equipment and solar energy equipment is considered part of the nonresidential active solar energy system property only to the extent of 75 percent of its full cash value.

**Residential Property.** "Residential property" means real property used as residential property, including both single-family and multiunit structures, and the land on which those structures are constructed or placed.

**Subsequent Change in Ownership.** This bill provides that a nonresidential active solar energy system constructed or installed before January 1, 2025 will be exempt from taxation until there is a subsequent change in ownership. A change in ownership will be deemed to have occurred if the transaction would have constituted a change in ownership under chapter 2 of the Revenue and Taxation Code (beginning with RTC section 60), had the nonresidential active solar energy system been real property instead of personal property.

**In General:** **Property Tax System.** Article XIII, section 1 of the California Constitution provides that all property is taxable at the same percentage of "fair market value," unless specifically exempted, or authorized for exemption.

**Business Personal Property.** All property, real and personal, is subject to property tax, unless a specific constitutional or statutory exemption applies. Generally, taxability is determined on the lien date, which is January 1 of each year. The Constitution allows the Legislature to exempt or provide for differential taxation of any personal property with a 2/3 vote.

Personal property used in a trade or business is taxable. Proposition 13's valuation limitations do not apply to business personal property. Consequently, the law requires the assessor to determine its current fair market value every year as of January 1. Mass appraisal techniques generally are necessary given the enormity of this task. To aid in the task, the law requires property owners to annually report their personal property holdings with an aggregate acquisition cost of $100,000 or more on a business property statement.[73]

The assessor determines the fair market value of most business personal property using the property's acquisition cost. The assessor multiplies acquisition cost by a price index (an inflation trending factor based on acquisition year) to estimate reproduction cost new. Next, the assessor multiplies reproduction cost new by a percent good factor (from BOE-issued percent good tables) to estimate depreciated reproduction cost (reproduction cost new less depreciation). The assessor uses the reproduction cost new less depreciation value as the property's taxable value for the fiscal year. The personal property tax rate is the same as the real property tax rate, which is 1 percent plus voter approved indebtedness in the locality. The BOE's Assessors' Handbook Section 504, *Assessment of Personal Property and Fixtures*, provides more detailed guidance.

**Real Property.** Article XIII A, section 2 defines "fair market value" as the assessor's opinion of value for the 1975-76 tax bill, or, thereafter, the appraised value of property when purchased, newly constructed, or a change in ownership has occurred. This value is generally referred to as the "base year value." Annual adjustments to the base year value are limited to 2 percent or the rate of inflation, whichever is less. Article XIII A, section 2 also provides for certain exclusions from consideration as a "change in ownership" and "newly constructed" as approved by voters via constitutional amendments.

**New Construction Exclusions.** Certain types of construction activity are excluded from assessment as "new construction" via constitutional amendment. Consequently, while these improvements may increase the value of the property, the additional value is not assessable. Relevant to this bill, Proposition 7, approved by California voters in November 1980, created an exclusion for active solar energy systems.

**Overview of Solar Energy New Construction Exclusion.** An "active solar energy system" is defined in RTC section 73 as a system that uses solar devices, which are thermally isolated from living space or any other area where the energy is used, to provide for the collection, storage, or distribution of solar energy. An active solar energy system may be used for any of the following:

- Domestic, recreational, therapeutic, or service water heating
- Space conditioning

[73] RTC section 441.

- Production of electricity
- Heat processing
- Solar mechanical energy

An active solar energy system includes storage devices, power conditioning equipment, transfer equipment, and parts related to the functioning of those items. "Parts" includes spare parts that are owned by the owner of, or maintenance contractor for, an active solar energy system for which the parts were specifically purchased, designed, or fabricated for installation in that system. Such a system includes only equipment used up to, but not including, the stage of conveyance or use of the electricity.

An active solar energy system also includes pipes and ducts that are used exclusively to carry energy derived from solar energy. Pipes and ducts that are used to carry both energy derived from the sun and energy derived from other sources may be considered active solar energy system property only to the extent of 75 percent of their full cash value.

This exclusion is scheduled to sunset on January 1, 2025. Any active solar energy system that was completed and excluded from assessment prior to this date will continue to be excluded until a change in ownership occurs.

An active solar energy system does not include auxiliary equipment, such as furnaces and hot water heaters, that use a source of power other than solar energy to provide usable energy. Dual use equipment, such as ducts and hot water tanks, that is used by both auxiliary equipment and solar energy equipment is considered active solar energy system property only to the extent of 75 percent of its full cash value.

RTC section 73 explicitly provides that the exclusion does not apply to solar swimming pool heaters or hot tub heaters. By definition, the exclusion does not apply to "passive" solar energy systems. Lastly, the exclusion does not apply to wind energy systems.

**Exclusion Extended to Initial Purchaser.** RTC section 73 was amended in 2008[74] to extend the new construction exclusion after a change in ownership if a new building is initially constructed with an active solar energy system incorporated and subsequently sold by the developer. Specifically, in the case where an active solar energy system is incorporated by an owner-builder in the initial construction of a new building that the owner-builder does not intend to occupy or use (i.e., a building offered for sale, such as a new home in a subdivision or a new warehouse), the exclusion for the system applies to the building's first buyer if (1) the owner-builder did not receive the exclusion for the same system, (2) if the initial buyer purchased the new building prior to that building becoming subject to reassessment to the owner builder,[75] and (3) a claim[76] is filed with the County Assessor.

[74] AB 1451 (Stats. 2008, ch. 538).
[75] RTC section 73(e)(1).
[76] RTC section 73(e)(1)(A); BOE-64-SES, *Initial Purchaser Claim for Solar Energy System New Construction Exclusion*.

If the exclusion is eligible to be extended to the initial purchaser, then in determining the base year value to be established as a result of the change in ownership, the base year value is reduced by the portion of the purchase price that is attributable to the active solar energy system. Thereafter, any subsequent change in ownership of the property ends the exclusion of the value of the active solar energy system from property tax.

**Common Transactions that may be Eligible for Federal Tax Benefits.** Under the legislative intent language contained in ABx1 15 (Stats. 2011, ch. 3), newly constructed active solar energy systems continue to receive the property tax exclusion if they are transferred using certain transactions that require the active solar energy system to be sold or transferred to a third party that may qualify for federal tax benefit. Transactions that may be eligible for federal tax benefits include, but are not limited to, the following:

- *Sale-leaseback transactions* involve the sale of a property in which the seller immediately begins to lease the property from the buyer. Thus, the seller no longer has ownership of the property, but operates it for the duration of the lease agreement.

- A *partnership flip transaction* is a financing arrangement between a renewable energy developer and a single or multiple tax investors whereby the parties form a partnership or limited liability company to develop and/or own an active solar energy system. This structure involves the tax investor making an investment in the partnership or limited liability company in exchange for the majority of the tax attributes (i.e., federal tax credits, depreciation, and net income) until the investor achieves its pre-established yield. The investor's share of these items is then reduced. The reduction is known as the "flip."

  In the case of a partnership flip transaction, if the investment made by the tax investor causes it to obtain more than 50 percent of the capital and profits interests of the partnership or limited liability company (either upon the making of the initial investment or pursuant to subsequent changes in the capital and profits percentages owned by the investor required by the partnership or operating agreement), the change in control is excluded by the new construction exclusion and no reassessment of the active solar energy system will occur. However, if the developer or a third party subsequently obtains more than 50 percent of the capital and profits interests of the partnership or limited liability company, a change in control and reassessment of the active solar energy system will occur.[77]

**Legal Entity Change in Control or Ownership.** County Assessors discover most real property changes in ownership via grant deeds or other documents recorded with the County Recorder. However, real property owned by a legal entity may undergo a "change in control or ownership" with no grant deed or other document recorded that could alert the County Assessor to a reassessment. These types of changes in control or ownership are reported directly to the State BOE's Legal Entity Ownership Program (LEOP) by the person or entity involved.

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[77] Letter To Assessors No. 2012/053, *Guidelines for Active Solar Energy Systems New Construction Exclusion*.

Existing law[78] requires legal entities to file a change in ownership statement (LEOP COS) with the BOE within 90 days of a change in control or ownership under RTC section 64(c) or (d). In the case of a change in control under RTC section 64(c), the person or legal entity that *acquired* control of the legal entity is responsible for filing the LEOP COS.

In addition to the self-reporting requirement to file a LEOP COS, the BOE may send a LEOP COS to an entity to complete and file with the BOE. Annually, the BOE canvasses legal entities with a query on the California Franchise Tax Board income tax return. County Assessors and other interested parties may send referrals reporting possible changes.

Once the BOE determines that a legal entity has undergone a change in control or ownership, the BOE notifies County Assessors of those legal entities' changes in control or ownership.

## Commentary:

1. **Split Roll Initiative.** Typically, the term "split roll" means taxing various property types (for example, residential v. commercial) according to a different tax rate or value standard. A true "split roll" is not possible without a constitutional amendment. Proposition 15 (Initiative 1870, 19-008A1), which will be on the November 3, 2020 ballot, proposes to amend the California Constitution to require certain commercial and industrial real property to be taxed at fair market value. If Proposition 15 is enacted, this bill, by classifying nonresidential active solar energy systems as personal property, will defer assessment of any system constructed before January 1, 2025 until the lien date following the date of change in ownership. Any nonresidential active solar energy system that is constructed on or after January 1, 2025 will be assessed at fair market value, along with other commercial and industrial property.

2. **Effective Date.** These provisions take effect only if Proposition 15, the split roll initiative, is enacted by the voters at the November 3, 2020 election.

3. **Personal Property Classification for Nonresidential Active Solar Energy System.** This bill specifies that a nonresidential active solar energy system is personal property, not real property, unlike a residential active solar energy system. This creates a hybrid type of property, in that a nonresidential active solar energy system is considered personal property, but will be subject to assessment only after it undergoes a change in ownership.

4. **Personal Property Exemption.** This bill specifies that a nonresidential active solar energy system that is installed on or before January 1, 2025 is exempt from taxation, until the system undergoes a subsequent change in ownership. This bill clarifies that the exemption applies to a nonresidential active solar energy system that is constructed or installed prior to the date Chapter 4.5 becomes operative, only if that system would have been excluded from assessment under RTC section 73, if the system had been real property instead of personal property. Essentially, this is treating a nonresidential active

[78] RTC sections 480.1 and 480.2.

solar energy system the same as a residential active solar energy system in that, upon installation, neither are assessable until the system undergoes a change in ownership.

5. **RTC section 73 is not a real property tax "exemption" for active solar energy systems, but a new construction "exclusion."** The new construction exclusion was created in 1980 via Proposition 7 to provide that the construction or addition of an active solar energy system to real property, by itself, would not lead to a revaluation of the property for property tax purposes. A new construction exclusion terminates if there is a transfer of the property resulting in a property's change in ownership (a reappraisal event).

6. **Termination of New Construction Exclusion.** Under RTC section 73, the new construction exclusion for an active solar energy system terminates if a change in ownership (a reappraisal event) occurs. For an excluded active solar energy system that is owned by a legal entity, if a person or entity subsequently obtains more than 50 percent of a corporation's voting stock or the capital and profits interests of a partnership or limited liability company that owns the active solar energy system, the change in control of the legal entity will result in a reassessment of any real property owned by the legal entity, including any excluded active solar energy systems.

   RTC section 73 is scheduled to sunset on January 1, 2025, unless this date is extended. This means that any active solar energy system that is constructed on or after January 1, 2025 will be assessable upon completion of construction. If this bill is enacted, any residential active solar energy system that is constructed on or after January 1, 2025 will be assessable, unless this sunset date is extended.

   Consistent with this sunset date in RTC section 73, this bill specifies that the exemption does not apply to a nonresidential active solar energy system that is constructed on or after January 1, 2025.

## Senate Bill 1473 (Governance and Finance Committee), Chapter 371
*Local Government Omnibus Act of 2020*

*Effective January 1, 2021.*

*Among others, amends sections 15643, 15645, and 15646 of the Government Code; and amends sections 214.18 and 439.2 of the Revenue and Taxation Code.*

*This analysis is limited to the effect on the State Board of Equalization-related tax programs.*

**Summary:** Among its provisions, this local government omnibus bill proposes the following BOE-sponsored changes:

- Extends the BOE's current county survey cycle for an additional five years. *(GC section 15643)*
- Clarifies that the BOE must issue a final county survey report within 12 months. *(GC section 15645)*
- Provides that the final county survey report that the BOE files with specified government officials is to include any addendums. *(GC section 15646)*
- For purposes of the welfare exemption, corrects an erroneous cross-reference in the definition of "community land trust." *(RTC section 214.18(c)(1))*
- Revises the interest component used for the assessment of historical property. *(RTC section 439.2)*

In addition, this bill includes a non-BOE-sponsored provision, for purposes of the welfare exemption with respect to a contract serving as an enforceable restriction on the affordability of rental units on property owned by a community land trust, that provides a restriction that the contract be an enforceable and verifiable agreement with a public agency, a recorded deed restriction, or other legal document that restricts the project's usage and imposes specified affordable rent requirements. *(RTC section 214.18(a)(3)(B))*

### BOE County Surveys
*Government Code Sections 15643, 15645, 15646*

**Existing Law:** Section 18 of article XIII of the California Constitution requires the BOE to measure county assessment levels annually and bring those levels into conformity by adjusting entire secured local assessment rolls. Under GC section 15640, the BOE must perform a survey to determine the adequacy of the assessment procedures and practices used by the County Assessor, which may include a sampling of the assessments from the local assessment roll in selected counties and cities and counties. GC section 15643 specifies the frequency of county surveys and the manner in which the BOE is required to select the counties or cities and counties that will be surveyed each year.

Current language provides for a survey of the assessment procedures and practices and a sample of assessments of the local assessment roll of the 10 largest counties and cities and counties (Group 1) and a random selection of counties and cities and counties in the 11th to 20th largest (Group 2) and the 21st to 58th largest (Group 3). Counties in these three groups are divided over a five-year cycle which provides for a total of 11 or 12 counties in each cycle year.

**Survey Cycle.** Each cycle year consists of two counties in Group 1, two counties in Group 2 (one county randomly selected for a survey of assessment procedures and practices and one county selected for a sampling of assessments on the local assessment roll), and five counties in Group 3 (three counties randomly selected for a survey of assessment procedures and practices and two counties randomly selected for a sampling of assessments on the local assessment roll). This makes a total of six surveys of assessment procedures and practices and five samplings of assessments that the BOE is to conduct each year.

The former language of this survey cycle sunset on December 31, 2020. Language that would have become operative January 1, 2021 was already written into GC section 15643.

The provisions that would have become operative January 1, 2021 remove the groupings of counties and require the BOE to conduct a survey of assessment practices in each county in the cycle year and conduct a sampling of assessments with the survey in the 10 largest counties and cities and counties, along with three additional randomly selected counties. This will make a total of 11 or 12 surveys (depending on the cycle year) of assessment procedures and practices and 5 samplings of assessments. This increases the number of surveys that must be performed by an additional 5 or 6 assessment practices surveys each year, which amounts to 28 additional surveys over the 5-year cycle.

**Response by Former Assessor.** Existing law requires an addendum to the final survey report be published that includes a former Assessor's written response to the findings and recommendations in the survey report which reviewed the former Assessor's procedures and practices, if any, and the BOE's comments, if any.

## Amended Law:

**Survey Cycle.** This bill (1) extends the current survey cycle for an additional five years, resulting in a new sunset date of January 1, 2026, and (2) delays the operative date for five years for the language that would have gone into effect on January 1, 2021, (new operative date of January 1, 2026).

**Final Survey Report.** This bill removes obsolete deadlines to issue prior survey reports and clarifies that the final survey report is to be issued within 12 months of the day that the BOE began the survey.

**In General:** The law requires the BOE to perform duties related to state oversight of local property tax administration. The Assessment Practices Survey Program is one of the state's major efforts to address these interests and to promote uniformity, fairness, equity, and integrity in the property tax assessment process. Specifically, the law requires the BOE to survey each county and city and county to determine the adequacy of the County Assessor's procedures and practices in property valuation.

Under this program, the BOE periodically reviews the practices and procedures of every County Assessor's office (called the survey program). The purpose of the survey is to determine the adequacy of the procedures and practices the County Assessor uses in valuing property and to evaluate the County Assessor's performance of mandated duties. The survey report concentrates on statutory mandates and revenue-related issues and provides useful information to the County Assessor and the taxpayer in determining the adequacy of the County Assessor's procedures and practices in valuing property and determining whether the total assessment roll complies with statutory standards. In some cases, the law requires the BOE's survey to include a "sampling" of assessments in the county. In the sampling, the BOE selects a statistically representative sample of property types, and BOE appraisers independently value the selected properties. The BOE's results are then compared to the County Assessor's results.

**Background:** Section 18 of article XIII requires the BOE to measure county assessment levels annually and bring those levels into conformity by adjusting entire secured local assessment rolls. In 1947, the Legislature initiated a survey program which required the BOE to conduct a study of each county's assessment practices. The findings of each survey were to be reported to the County Assessors, the board of supervisors, and the Legislature. One round of surveys was completed during the five-year period ending in 1952. No further surveys were conducted until the 1966 Property Tax Assessment Reform Law (Assembly Bill 80) was enacted. Assembly Bill 80 (Stats. 1966, ch. 147, First Extraordinary Session), changed the BOE's assessment practices survey program by expanding the timing, scope and content of the surveys.[79]

In 1957, to help fulfill its constitutional mandate to bring county assessment levels into conformity and to help achieve an equitable distribution of aid to school districts, the BOE sought to fulfill the objective of intercounty equalization (bringing about uniform assessment levels between counties). The BOE conducted independent appraisals of a sampling of each county's assessments and compared the results to the county's appraisals. The ratio of county to BOE total value was calculated, and each county's ratio was compared with the statewide ratio. Assessed values were adjusted accordingly for purposes of adjusting the amount of aid to each of the county's school districts. This was called the sampling program. The survey and sampling programs operated independently until after Proposition 13 passed in 1978. After Proposition 13, those ratios are not used to equalize assessment levels between counties, but to judge whether a county is in compliance with the laws requiring full value assessments. Effective January 1, 1997, Senate Bill 1827 (Stats. 1996, ch. 1087) scaled back the sampling part of the program.

**Legislative History.** AB 681 (Stats. 2015, ch. 404) gradually reduced the time period in which the BOE was to issue a final survey report from 2 years to 15 months to 12 months starting on or after July 1, 2017. To mitigate the impact of reducing the time period to publish final survey reports, AB 681 also modified the survey cycle for five years to reduce the number of surveys the

[79] Publication 216, *The First 100 Years* (https://www.boe.ca.gov/info/pub216/property_tax_reform.html).

BOE is required to conduct. These provisions were scheduled to sunset on January 1, 2021 and revert to the prior five-year schedule for all counties.

## Commentary:

1. **Survey Cycle.** The provisions that would have become operative January 1, 2021 removed the groupings of counties and require the BOE to conduct a survey of assessment practices in each county in the cycle year and conduct a sampling of assessments with the survey in the 10 largest counties and cities and counties, along with three additional randomly selected counties. This would have made a total of 11 or 12 surveys (depending on the cycle year) of assessment procedures and practices and 5 samplings of assessments. This would have increased the number of surveys that must be performed by 5 to 6 additional assessment practices surveys each year, which amounts to 28 additional surveys over the 5-year cycle. This significant increase, coupled with extensive staffing shortages, would add to an existing backlog of work for the BOE and possibly further delay issuing a final survey report.

2. **Issuance of Survey Reports.** GC section 15645 provides for a gradually-reduced time period in which the BOE was to issue a final county survey report from 2 years to 15 months to 12 months. The 12-month period applies to county surveys starting on or after July 1, 2017. This bill removes the obsolete deadlines that applied to surveys that commenced prior to July 1, 2017 and clarifies that the final county survey report is to be issued within 12 months of the date that the county survey begins.

3. **Response by Former Assessor.** Existing law requires the BOE to notify a former Assessor if the survey reviews the former Assessor's procedures and practices, but does not provide a deadline for the former Assessor to provide a response to the final survey report. Having an infinite time for a former Assessor to respond could possibly result in an addendum being published long after the final survey report was published.

## Welfare Exemption

*Revenue and Taxation Code Section 214.18*

**Existing Law: Welfare Exemption.** Existing law provides that low-income rental housing owned and operated by a qualifying nonprofit organization or a qualified claimant[80] may be exempt from property tax under the welfare exemption, provided various conditions and requirements are met. The law allows an unlimited exemption for rental housing owned by a nonprofit organization if it receives government financing or low-income housing tax credits.[81]

[80] In addition to qualifying organizations as defined in Property Tax Rule 136, a qualified claimant may also be a limited partnership in which the managing general partner is an eligible nonprofit corporation or eligible limited liability company.

[81] RTC section 214(g)(1)(A) and RTC section 214(g)(1)(B).

Property owned by a community land trust (CLT) qualifies for the welfare exemption if all of the following conditions are met:

- The property is being or will be developed or rehabilitated as an owner-occupied single-family dwelling, owner-occupied unit in a multifamily dwelling, a member-occupied unit in a limited equity housing cooperative, or a rental housing development;
- Improvements are or will be available for use and ownership by qualified persons; and
- A deed restriction or other instrument serving as an enforceable restriction on the sale or resale value of owner-occupied units or the affordability of rental units is recorded.

**Enforceable Restriction.** A deed restriction or other instrument requiring a contract or contracts serving as an enforceable restriction on the sale or resale value of the owner-occupied units or on the affordability of rental units must be recorded on or before the lien date following the acquisition of the property by the CLT. "A contract or contracts serving as an enforceable restriction on the sale or resale value of the owner-occupied units or on the affordability of rental units" is defined as a contract described in RTC section 402.1(a)(11), which provides that an enforceable restriction includes a contract that is a renewable 99-year ground lease between a CLT and the qualified owner of an owner-occupied single-family dwelling or an owner-occupied unit in a multifamily dwelling.

**Fair Market Value of Enforceably Restricted Property.** Existing law requires the County Assessor to reassess property to its fair market value when sold (i.e., "change in ownership"). The law provides that the property's "purchase price" is rebuttably presumed to be its "fair market value."[82] It also provides that "purchase price" means the total consideration provided by the purchaser or on the purchaser's behalf, valued in money, whether paid in money or otherwise.

**Nonprofit-Imposed Restrictions.** When determining a property's fair market value, existing law requires the County Assessor to consider the effect of legally enforceable property use restrictions, such as zoning or development limitations. Similarly, when determining land value, the law requires the County Assessor to consider the effect of enforceable restrictions on land use.[83]

In the case of a *nonprofit organization-imposed* use restriction, such as a CLT-imposed resale price restriction, the law generally prohibits the County Assessor from considering its negative value impact unless a specific statutory mandate exists.[84]

Currently, the law recognizes four non-governmental restrictions on value:

- Land easements granted to nonprofit organizations to preserve and protect land in its natural state.[85]

[82] RTC section 110(b).
[83] RTC section 402.1.
[84] *Carlson v. Assessment Appeals Board No. 1* (1985) 167 Cal.App.3d 1004.
[85] RTC section 402.1(a)(8)(A) – Added in 1993, but the law since 1984 via Civil Code section 815.10.

- Homes on land with a 30-year use restriction as owner-occupied housing available at affordable cost that are sold at cost to low-income families by qualifying nonprofit organizations[86] with no-interest financing (i.e., "silent second mortgage").[87]
- Greenway easements granted to nonprofit organizations to create paths along urban waterways.[88]
- Homes with CLT-imposed restrictions that have a renewable 99-year ground lease and limited equity due to resale price restrictions that are sold to low- and moderate-income buyers.[89]

For purposes of this restriction, a CLT is defined in RTC section 402.1(a)(11)(C)(ii) as a nonprofit corporation organized pursuant to Internal Revenue Code section 501(c)(3) that satisfies all of the following:

- Has as its primary purpose the creation and maintenance of permanently affordable single-family or multifamily residences.
- All dwellings and units located on the land owned by the nonprofit corporation are sold to a qualified owner and are to be occupied as the qualified owner's primary residence or rented to persons and families of low or moderate income.
- The land owned by the nonprofit corporation, on which a dwelling or unit sold to a qualified owner is situated, is leased by the nonprofit corporation to the qualified owner for the convenient occupation and use of that dwelling or unit for a renewable term of 99 years.

## Amended Law:

**Definition of Community Land Trust.** For purposes of the exemption for community land trust property, RTC section 214.18 defines "community land trust" by reference to RTC section 402.1(a)(11)(B)(ii). This bill corrects the cross-reference, as the definition is contained in RTC 402.1(a)(11)(C)(ii), not subparagraph (B)(ii).

**Enforceable Restriction.** For purposes of applying the exemption to rental housing, this bill defines "a contract or contracts serving as an enforceable restriction on the affordability of rental units" as an enforceable and verifiable agreement with a public agency, a recorded deed restriction, or other legal document described in RTC section 214(g)(2)(A).

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[86] RTC section 214.15 – Added in 1999, by AB 1559, this law extends the welfare exemption to the following property owned by nonprofit organizations that sell homes to low income persons at cost with zero percent financing: (1) vacant land held for future construction and (2) homes under construction. No other property being developed as homes for sale to low income persons qualifies for a property tax exemption under the welfare exemption. Moderate income rental housing qualifies for the welfare exemption only if the housing is for seniors and the disabled and includes supportive services based on their special needs.

[87] RTC section 402.1(a)(10) – Added in 2015. Health & Safety Code section 50052.5 defines "affordable housing cost."

[88] RTC section 402.1(a)(8)(B) – Added in 2015.

[89] RTC section 402.1(a)(11)(A) – Added in 2016.

**Background:** **Community Land Trust.** Federal law, the Cranston-Gonzales National Affordable Housing Act (Act), allows CLTs to obtain organizational support, technical assistance, education, training, and community support from the government in fulfilling their housing mission.[90] The Act defines "CLT" to mean a community housing development organization not sponsored by a for-profit organization, with a specified board membership, that is established to carry out the following activities:

- Acquire parcels of land, held in perpetuity, primarily for conveyance under long-term ground leases;
- Transfer ownership of any structural improvements located on the leased parcels to the lessees; and
- Retain a preemptive option to purchase any structural improvement at a price determined by a formula designed to ensure that the improvement remains affordable to low and moderate income families in perpetuity.

CLTs are nonprofit organizations governed by a board of CLT residents, community residents and public representatives that provide lasting community assets and shared equity homeownership opportunities for families and communities. CLTs develop rural and urban agriculture projects, commercial spaces to serve local communities, and affordable rental and cooperative housing projects, and conserve land or urban green spaces. However, the heart of their work is the creation of homes that remain permanently affordable, providing successful homeownership opportunities for generations of lower income families.[91]

CLTs provide an affordable housing model to help low- and moderate-income households that may not otherwise be able to purchase homes. The CLT acquires and develops properties for sale to income-qualified households, but then retains ownership of the underlying land and leases the land to the homeowner for a nominal fee through a long-term ground lease (usually a 99-year term). The home is, therefore, more affordable because the homeowner is only buying the building and leasing the land underneath. If the homeowner decides to sell the property, the home must be resold to another income-qualified household, and the original owner will only be eligible for a smaller share of its appreciated value. Since the CLT is the owner of the land, it will be a party to all future sales and enforce resale restrictions.

**Legislative History:** Effective September 27, 2016, Assembly Bill 2818 (Stats. 2016, ch. 701) amended RTC section 402.1(a) to require County Assessors to consider recorded restrictions imposed by a CLT that negatively impact property value when determining the assessed value of homes that have a 99-year ground lease and limited equity due to resale price restrictions and that are sold to low- and moderate-income buyers.[92]

Effective January 1, 2020, Senate Bill 196 (Stats. 2019, ch. 669) amended RTC section 402.1 regarding the assessment of property owned by community land trusts. In addition, SB 196 added

[90] 42 U.S.C. 12773
[91] https://groundedsolutions.org/strengthening-neighborhoods/community-land-trusts.
[92] Letter To Assessors No. 2017/008.

RTC section 214.18 to the RTC to provide that property owned by a CLT qualifies for the welfare exemption for a five-year period, if the property is being or will be developed or rehabilitated as low income housing, provided the CLT meets the various requirements set forth in RTC section 214(a). Property will be eligible for exemption for a specific five-year period, depending on the date the property was acquired by the CLT. RTC section 214.18 will be repealed on January 1, 2025.

## Commentary:

1. **Cross-Reference Correction.** For purposes of the exemption for community land trust property, RTC section 214.18 defines "community land trust" by reference to another code section. Specifically, RTC section 214.18(c)(1) provides that a "community land trust" has the same meaning as that term is defined in RTC section 402.1(a)(11)(B)(ii). The June 19, 2019 amendment of SB 196 added amendments to RTC section 402.1 not previously included in SB 196. This amendment moved the definitions of RTC section 402.1(a)(11) from subparagraph (B) to subparagraph (C). Thus, the definition of community land trust in RTC section 402.1(a)(11) is contained in subparagraph (C)(ii), not subparagraph (B)(ii). This bill corrects this cross-reference in RTC section 214.18.

2. **Community Land Trust Property Use Restriction.** When determining a property's fair market value, existing law requires the County Assessor to consider the effect of legally enforceable property use restrictions, such as zoning or development limitations. Similarly, when determining land value, the law requires the County Assessor to consider the effect of enforceable restrictions on land use. RTC section 402.1(a)(11) provides that an enforceable restriction includes a contract that is a renewable 99-year ground lease between a CLT and the qualified *owner* of an owner-occupied single-family dwelling or an *owner*-occupied unit in a multifamily dwelling.

3. **Exemption.** Existing law allows a CLT property to be exempt if certain qualifications are met, including the requirement that a deed restriction or other instrument requiring a contract or contracts serving as an enforceable restriction on the sale or resale value of the owner-occupied units or on the affordability of rental units must be recorded on or before the lien date following the acquisition of the property by the CLT. These provisions apply to both (1) the sale or resale value of the owner-occupied units, and (2) the affordability of rental units. This language is confusing as the definition of a "contract serving as an enforceable restriction" is made by cross-reference to RTC section 402.1, which does not pertain to rental housing. This bill eliminates that confusion by adding a definition of a contract serving as an enforceable restriction for rental housing purposes.

4. **Assessment of CLT Housing.** After the enactment of AB 2818 in 2016, BOE staff commenced the interested parties process to discuss proposed guidance on the assessment of CLT housing.[93] BOE staff met on multiple occasions with County Assessors, CLT representatives, and other interested parties in a joint effort to develop uniform

[93] All documents and comments related to this project are posted on the BOE's website at www.boe.ca.gov/proptaxes/assessment-of-community-land-trust-housing.htm.

guidance on the application of the bill's amendments. Staff's position was that, consistent with the County Assessor's constitutional and statutory duty to assess all taxable property, the value of land and improvements of a CLT property must be determined separately.[94] CLT representatives consistently maintained that, despite the specific language in the purchase agreements, the purchase prices are intended to cover both the improvements and the land, while the lease payments are for administrative services that bear no relationship to the market value of the land. Continued discussion between BOE staff, County Assessors, and CLT representatives resulted in the clarifying amendments to RTC section 402.1 by SB 196, effective January 1, 2020.

## Assessment of Historical Property

*Revenue and Taxation Code Section 439.2*

**Existing Law:** Section 8 of article XIII of the California Constitution authorizes the preferential property tax assessment of historically significant property that is enforceably restricted in order to encourage its preservation. Sections 439 through 439.4 were added to the RTC to implement this preferential treatment.

RTC section 439.2 requires the County Assessor to value historical property subject to a historical property (aka Mills Act[95]) contract by using a prescribed income capitalization method. Relevant to this bill, the law requires the BOE to determine and announce the interest component of the capitalization rate no later than October 1 each year. Formerly RTC section 439.2, subdivisions (b)(1) and (c)(1) specified that the interest component was the yield rate equal to the effective rate on conventional mortgages as most recently published by the Federal Housing Finance Agency (FHFA) as of September 1, rounded to the nearest 1/4 of 1 percent.

**Amended Law:** This bill replaces the effective rate on conventional mortgages as determined by the FHFA with the average interest rate as published by the Federal Home Loan Mortgage Corporation.

**In General:** On June 8, 1976, the voters of California approved Proposition 7 which amended section 8 of article XIII of the California Constitution, to authorize the Legislature to provide for the preferential property tax assessment of historically significant property that is enforceably restricted in order to encourage its preservation. The Legislature created a program known as the Mills Act detailing the requirements.[96] The Mills Act grants participating local governments (cities and counties) the authority to enter into a contract with a qualified historical property owner to enforceably restrict the historical property's use. In exchange for use restrictions and a pledge to restore, maintain, and protect the property's historical and architectural character, the

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[94] Language in AB 2818 that would have expressly provided that the purchase price of the improvements was presumed to be the value of the land *and* improvements was amended out of the bill in the May 31, 2016 version.
[95] The Mills Act is described on page 9 under the subheading "In General," *infra*.
[96] California Department of Parks and Recreation, Office of Historic Preservation, Mills Act Program.

property owner receives property tax relief in the form of a reduced assessed value (called the restricted value).

RTC sections 439 through 439.4 implement Proposition 7. These statutes, in particular RTC section 439.2, prohibit a valuation of enforceably restricted historical property based on sales data and instead require that such property be valued by a prescribed income capitalization method.

**Historical Property.** A qualified historical property[97] is privately-owned property that is not exempt from property taxation and that also meets either of the following criteria:

- The property is listed in the National Register of Historic Places, or is located within a registered historic district; or
- The property is listed in any official state, county, city, or city and county official register of historical or architecturally significant sites, places or landmarks, including the California Register of Historical Resources, California Historical Landmarks, State Points of Historical Interest, local landmarks, and local survey listings of historical properties.

**Historical Property Contract (aka Mills Act Contract).** The historical property contract[98] must have a minimum term of ten years, and, as applicable, must contain certain other elements, including the following:

- A provision relating to the preservation of the qualified historical property and, when necessary, the restoration and rehabilitation of the property in conformance with state historic preservation guidelines;
- A requirement for the periodic examination of the property to ensure compliance with the agreement;
- A requirement that the historical property agreement be binding upon successor owners of the qualified historical property; and
- A provision for an automatic one-year extension of the contract, with an additional year added to the initial contract term on each anniversary of the contract, unless either party provides notice of nonrenewal. If a notice of nonrenewal is given, the contract runs for its remaining term.

Once a contract is signed, accepted, and recorded, the property subject to the contract must be assessed under RTC section 439.2 beginning with the ensuing lien date.

**Annual Assessment of Enforceably Restricted Historical Property.** RTC section 439.2 provides a formula for calculating the annual value of historical properties for property tax purposes. The income to be capitalized when valuing a restricted historical property is the property's fair rent less allowed expenditures, or allowed expenses. The restricted value is the income to be capitalized, or net operating income, divided by one of the two types of capitalization rates. Once

[97] GC section 50280.1.
[98] GC section 50281 and 50282.

the restricted value is established, it is compared to the property's current market value and its factored base year value. The lowest of the three values is enrolled.

Information about this annual assessment is contained in the BOE's *Guidelines for the Assessment of Enforceably Restricted Historical Property*.[99]

**Capitalization Rate.** RTC section 439.2 prescribes two types of capitalization rates for restricted historical property, distinguished by the property's type and usage:

- Restricted historical property that is an owner-occupied single-family residence, and
- All other restricted historical property.

Both types of capitalization rates include components for interest (i.e., yield), risk, property taxes, and amortization of improvements. The two rates are identical, except for the amount of the risk component. The two capitalization rates contain the following components:

- An interest component based on the effective rate on conventional mortgages as determined by the FHFA. The interest component is announced annually by the BOE, via a Letter To Assessors, by October 1 of the preceding assessment year.[100]
- A historical property risk component determined by property type.
  - For owner-occupied single-family residences, the rate is 4 percent.
  - For all other types of restricted historical property, the rate is 2 percent.
- An amortization component for improvements which is the percentage equal to the reciprocal of the remaining life of the improvements.
- A property taxes component equal to the percentage of the estimated total tax rate applicable to the property for the assessment year multiplied by the assessment ratio.

**Interest Component.** The FHFA calculated the effective interest rate from a Monthly Interest Rate Survey (MIRS), which provided information on a monthly basis on interest rates, loan terms, and house prices by property type (all, new, previously occupied); by loan type (fixed- or adjustable-rate), and by lender type (savings associations, mortgage companies, commercial banks and savings banks); as well as information on 15-year and 30-year, fixed-rate loans. On May 29, 2019, the FHFA published its final MIRS, due to dwindling participation by financial institutions.[101] Staff at the FHFA verified that the FHFA is no longer calculating a comparable effective interest rate.

**Background:** The Federal Home Loan Mortgage Corporation, also known as Freddie Mac,[102] is a public government-sponsored enterprise. Freddie Mac was chartered by Congress in 1970 and

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[99] See Letter To Assessors No. 2005/035.
[100] See Letter To Assessors No. 2019/033.
[101] https://www.fhfa.gov/DataTools/Downloads/Pages/Monthly-Interest-Rate-Data.aspx.
[102] http://www.freddiemac.com/.

operates in the U. S. secondary mortgage market by purchasing mortgage loans from lenders so they in turn can provide more loans to qualified borrowers.

Freddie Mac conducts and publishes a Primary Mortgage Market Survey® (PMMS®)[103] which is a weekly survey of mortgage interest rates in the United States. This survey includes information on 30-year fixed rate mortgages, 15-year fixed rate mortgages, and 5/1-year adjustable rate mortgages.

## Commentary:

1. **Qualified Historical Property.** Not all historical property is eligible for preferential property tax treatment. To qualify, a property must be listed on a historical register or be located within a historical district and the property owner must enter into a Mills Act contract with their local government.

2. **Enforceably Restricted Historical Property.** Real property subject to a Mills Act contract is annually valued pursuant to article XIII, section 8. However, this annual valuation cannot exceed the subject property's current market value or its factored base year value established under article XIII A of the California Constitution and RTC section 110.1.[104]

3. **Capitalization Rate Interest Component.** Existing law provides that the interest component of the capitalization rate for the assessment on qualified historical property is the effective rate on conventional mortgages as determined by the FHFA as of each September 1. However, the FHFA no longer calculates this effective rate. The last published effective interest rate for conventional mortgages was issued on May 29, 2019. This effective interest rate will continue to be used without any update or change for future years, unless RTC section 439.2 is amended. Using a May 2019 effective rate for 2021 lien date assessments and following lien dates would not be consistent with the specified income approach method, which uses current market rents and expenses. Thus, this bill replaces the FHFA effective interest rate on conventional mortgages that is no longer being determined with the average interest rate on conventional mortgages as published by the Federal Home Loan Mortgage Corporation.

4. **Federal Home Loan Mortgage Corporation (aka "Freddie Mac").** According to the Federal Home Loan Mortgage Corporation's website,[105] the Primary Mortgage Market Survey® (PMMS®) has evolved since its inception in April 1971 into the foremost reliable, representative source of regional and national mortgage rate trends and is relied upon by the mortgage industry and the public in gauging market conditions and evaluating mortgage loan options. Each week, Freddie Mac surveys lenders on the rates and points for their most popular 30-year fixed-rate, 15-year fixed-rate and 5/1 hybrid amortizing adjustable-rate mortgage products.

[103] http://www.freddiemac.com/pmms/.
[104] RTC section 439.2(d).
[105] http://www.freddiemac.com/pmms/about-pmms.html.

5. **Alternatives Considered.** Since the FHFA no longer calculates effective interest rates for conventional mortgages as required to be used for the historical property capitalization rate interest component, the BOE consulted with the County Assessors' staff and searched, but did not find any other source of conventional rate mortgage loan information, other than the PMMS by Freddie Mac.

## TABLE OF SECTIONS AFFECTED

| SECTIONS | ACTION | BILL NUMBER | CHAPTER NUMBER | SUBJECT |
|---|---|---|---|---|
| **California Constitution, Article XIII A** | | | | |
| 2.1 | Add | ACA 11 | 31 | Base year value transfer for over 55, severely disabled, or victim of wildfire or natural disaster; parent-child and grandparent-grandchild exclusion |
| **Government Code** | | | | |
| 15643 | Amend | SB 1473 | 371 | County survey cycle frequency |
| 15645 | Amend | SB 1473 | 371 | County survey report |
| 15646 | Amend | SB 1473 | 371 | Filing final survey report and addendums |
| **Revenue and Taxation Code** | | | | |
| 70.5 | Add | AB 2013 | 124 | New construction exclusion – proclaimed disaster |
| 73 | Amend | SB 364 | 58 | New construction exclusion – residential active solar energy system |
| 83 | Add | SB 364 | 58 | Statement of legislative intent – nonresidential active solar energy system |
| 83.5 | Add | SB 364 | 58 | Exception to definitions for nonresidential active solar energy system |
| 84 | Add | SB 364 | 58 | Definition of "residential property" for nonresidential active solar energy system |
| 85 | Add | SB 364 | 58 | Definition of "nonresidential active solar energy system" |
| 86 | Add | SB 364 | 58 | Exemption for nonresidential active solar energy system |
| 87 | Add | SB 364 | 58 | Invalidity statement |
| 88 | Add | SB 364 | 58 | Operative date (upon voter approval of Proposition 15 on the November 3, 2020 ballot) |
| 105 | Amend, repeal, and add | SB 364 | 58 | Definition of "improvements" |
| 106 | Amend, repeal, and add | SB 364 | 58 | Definition of "personal property" |
| 214.18 | Amend | SB 1473 | 371 | Welfare exemption – community land trusts |
| 439.2 | Amend | SB 1473 | 371 | Historical property interest component |

| SECTIONS | ACTION | BILL NUMBER | CHAPTER NUMBER | SUBJECT |
|---|---|---|---|---|
| **Revenue and Taxation Code** (continued) | | | | |
| 1604 | Amend | AB 107 | 264 | Regular equalization period |
| 1616 | Add | AB 107 | 264 | Remote hearings |
| 1621 | Amend | AB 3373 | 57 | Number of assessment appeals boards |
| 1752.4 | Add | AB 107 | 264 | Remote hearings |