STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Date Introduced:	**2/23/07**	Bill No:	**SB 984**
Tax:	**Property**	Author:	**Ashburn**
Related Bills:			

BILL SUMMARY

Related to base year value transfers for both persons over the age of 55 and the disabled, this bill would modify, on a county optional basis, the inflation factor used to calculate whether a replacement property purchased after the sale of the original home, but within 2 years, meets the "equal or lesser value" requirement.

ANALYSIS

CURRENT LAW

Under existing law, real property is generally reassessed to its current fair market value whenever there is a "change in ownership." However, under certain circumstances, property owners may avoid reassessment of a particular property by way of either a change in ownership exclusion or a base year value transfer. (Article XIII A, Sec. 2; Revenue and Taxation Code Sections 60 - 69.5)

Section 69.5 of the Revenue and Taxation Code provides that persons over the age of 55 and disabled persons may transfer their base year value (i.e., their Proposition 13 assessment) if they purchase a new home of equal or lesser value that is located in the same county. Additionally, seven counties (Alameda, Los Angeles, Orange, San Diego, San Mateo, Santa Clara, and Ventura) permit persons to transfer values from homes located in other counties. This once-in-a-lifetime benefit allows seniors to pay the same level of taxes if they choose to move and continue to enjoy relatively low property taxes by avoiding the reassessment provisions of Proposition 13 when purchasing a qualifying new home.

Section 69.5 details the provisions for qualifying for a base year value transfer. Relevant to this bill, one requirement is that the replacement dwelling be of "equal or lesser value" than the original property. Determining whether a replacement dwelling meets the "equal or lesser value" requirement depends on when the replacement dwelling is purchased. Generally, the purchase price of each home is used as the basis of the value test. However, since the replacement dwelling need not be purchased for up to 2 years after the sale of the original property, the law allows for an inflation adjustment as follows:

- If it is purchased prior to the sale of the original property, then it must be 100% or less.

- If it is purchased within the first year of the sale, then it can be up to 105% of the value of the original.
- If it is purchased within the second year of the sale, then it can be up to 110%.

For example if the original property is sold for $500,000 then the maximum value of the replacement dwelling would be:

Purchase of Replacement	Equal or Lesser Comparison	Maximum Value of Replacement
Prior to	$500,000 x 100%	$500,000
Within 1 year	$500,000 x 105%	$525,000
Within 2 years	$500,000 x 110%	$550,000

PROPOSED LAW

This bill would amend Section 69.5 to provide that on a county optional basis, rather than using the flat inflation factor of 105% or 110%, the inflation factor instead would be based upon the actual California House Price Index (HPI), as determined by the Office of Federal Housing Enterprise Oversight, for the period in question.

IN GENERAL

Under Proposition 13, property is reassessed to its current market value only after a change in ownership. Generally, the sales price of a property is used to set the property's assessed value and annual increases to that value are limited to the rate of inflation, not to exceed 2%.

Base Year Values. At the time of the ownership change, the value of the property for property tax purposes is redetermined based on current market value. The value initially established is referred to as the "base year value." Thereafter, the base year value is subject to annual increases for inflation, but at no more than 2% per year. This value is referred to as the "factored base year value." This system, established by Proposition 13, results in substantial property tax savings for long term property owners.

Base Year Value Transfers. Voters have approved three constitutional amendments permitting persons 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.

- Proposition 60, approved by the voters on November 6, 1986, amended Section 2 of Article XIII A of the California Constitution to allow persons over the age of 55 to sell a principal place of residence and transfer its base year value to a replacement principal place of residence within the same county.

- Proposition 90, approved by the voters on November 8, 1988, extended these provisions to a replacement residence located in another county on a county optional basis. Currently seven counties accept transfers from outside their county.
- Proposition 110, approved by the voters on June 5, 1990, extended these provisions to severely and permanently disabled persons of any age.

Section 69.5 of the Revenue and Taxation Code provides the statutory implementation for these propositions.

COMMENTS

1. **Sponsor and Purpose.** The California Assessors' Association is sponsoring this measure to provide a more realistic inflation factor.
2. **The current 5% and 10% inflation adjustments are arbitrary**. Using an inflation factor based on an established index which is directly related to California housing prices rather than a fixed arbitrary allowance will allow more taxpayers to qualify for a base year value transfer in periods when home prices are escalating more rapidly than 5% per year.
3. **Base Year Value Transfers Extend Proposition 13 Protections.** A "base year value transfer" allows eligible homeowners to preserve the Proposition 13 protected value of their prior residence by transferring it to the new residence. This essentially allows a homeowner who qualifies to continue to pay the same basic amount of property taxes. Without this provision, the property taxes on the new residence would be based on its current fair market value, which is usually the sales price, because of the change in ownership.

COST ESTIMATE

The Board would incur some minor absorbable costs in informing local county assessors, the public, and staff of the law changes.

REVENUE ESTIMATE

BACKGROUND, METHODOLOGY, AND ASSUMPTIONS

Existing property tax law specifies that a severely disabled person or a person over 55 years of age may transfer their base year value, as defined, to a dwelling of "equal or lesser value" located within the same county as the original property. In order to qualify for a base year transfer, the full cash value of a purchased or newly constructed dwelling within the first year following the date of sale of the original property cannot exceed 105% of the full cash value of the original property, or 110% of the full cash value of the original property, within the second year.

According to the Board of Equalization's 2005-06 Report on Budgets, Workloads, and Assessment Activities, the statewide number of claims granted for qualified base year transfers for that fiscal year was 12,358. Since 1975 the HPI has annually been below

5% about one-third of the time, and above 10% about half the time. The average change in the HPI factor from 1975-2006 was approximately a 9% increase per year.

The 2005 California median home sale price was $524,000. Applying both the one and two-year existing limits for full cash value, as well as the average HPI factor of 9%, we can estimate the average full cash value of a qualified replacement dwelling in the first year of this bill to be:

Replacement within one year	$524,000 x 1.09 = $571,160
Replacement within two years	$524,000 x 1.19 = $623,560

The average assessed value of properties receiving the homeowners' exemption for 2005 was $256,000.

Therefore, the estimated affected assessed value difference per home would be:

Within one year	$571,160 - $256,000 = $315,160
Within two years	$623,560 - $256,000 = $367,560

According to the U.S. Census Bureau's 2005 American Housing Survey, almost 7 in 10 senior homeowners 65 years and older owe nothing on their home. Of those who do, 75% have mortgages under $100,000. We can assume that a large number of claimants that qualify for base year transfers are empty-nest seniors over 55 years of age who are downsizing their residence and therefore most likely will purchase their replacement property at about the same time that they sell their original property, for about the same price.

Staff estimates that while limits may increase on the full cash value of a replacement dwelling under this bill, seniors will generally remain in a similarly or lower priced home when transferring their base year value to a replacement property. Staff further estimates that in the first year of this bill, no more than 500 qualified claimants would utilize increased limits of full cash value beyond 105% within the first year, or beyond 110% within the second year.

Based on a ceiling of 500 qualified claimants under this bill, with 400 claimants purchasing a home within the one year timeframe and the remaining 100 claimants purchasing a home within the two year timeframe, we can calculate the initial revenue impact at the basic 1% rate as follows:

Within one year	400 x $315,160 x 1% = $1, 260,640
Within two years	100 x $367,560 x 1% = $ 367,560

REVENUE SUMMARY

This bill would initially reduce property tax revenues at the basic 1 percent tax rate by no more than $1.6 million annually when the adjustment for the California HPI exceeds 5 percent.

QUALIFYING REMARKS

This estimate assumes that all counties would adopt an ordinance authorizing the use of the proposed factor instead of the current factors. The revenue impact would be significantly lower if few counties were to authorize the use of an HPI-based factor in determining the full cash value limit of a replacement property.

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