



**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS**

Date Introduced:	1/23/01	Bill No:	AB 136
Tax:	Property	Author:	Corbett
Board Position:		Related Bills:	

BILL SUMMARY

This bill would annually increase the current \$20,000 property tax exemption for hand tools in accordance with a specified inflation adjustment.

ANALYSIS

Current Law

Section 3(m) of Article XIII of the California Constitution and Section 224 of the Revenue and Taxation Code exempt from property tax household furnishings and personal effects which are not held or used in connection with a trade, profession or business.

Section 224 states:

The personal effects, household furnishings, and pets of any person shall be exempt from taxation.

The phrase "personal effects, household furnishings, and pets" does not include boats, aircraft, vehicles, or personalty held or used in connection with a trade, profession or business or pets so held or used.

For purposes of this section, "pets" mean and include any animals held for noncommercial purposes and not as an investment.

Revenue and Taxation Code Section 241 exempts from property tax the first twenty thousand dollars (\$20,000) of hand tools owned by an employee who is required, as a condition of employment, to supply his or her own hand tools. "Hand tools" means hand-held implements and equipment, including hand-held power tools, of which any one may be transported to and from the workplace and which are necessary for the ordinary and regular performance of the employee's work. The exemption also extends to appropriate storage containers for the implements and equipment.

Proposed Law

This bill would, beginning on January 1, 2002, annually adjust the exemption amount for hand tools. The inflation adjustment factor to be used is the annual percentage change, measured from February to February, of the two previous assessment years, in

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the California Consumer Price Index (CCPI) for all items as determined by the Department of Industrial Relations.

In General

The taxation of personal property which is not exempted by the California Constitution is discretionary with the Legislature. Section 2 of Article XIII of the California Constitution provides that the Legislature, two-thirds of the membership in each house concurring, may classify personal property for differential taxation or exemption.

Personal property used in a trade or business is generally taxable, and its cost must be reported annually to the assessor on the business property statement as provided for in Section 441. Personal property is not subject to the limitations of Proposition 13. Instead, it is valued annually at its current fair market value as of January 1 (the lien date). The business property statement shows all taxable property, both real and personal, owned, claimed, possessed, controlled, or managed by the person filing the property statement. The assessor may request a signed business property statement from any person owning taxable personal or real property. When the aggregate cost of the taxable personal property is \$100,000 or more, the person is required to file a signed property statement each year with the assessor.

In the annual determination of "current fair market value" of personal property, the valuation method generally used is based on the acquisition cost of the property. The acquisition cost is multiplied by a price index, an inflation trending factor based on the year of acquisition, to provide an estimate of its replacement cost new. The replacement cost new is then multiplied by a depreciation index, also called percent good tables, to provide an estimate of the depreciated replacement cost of the property (replacement cost new less depreciation). The replacement cost new less depreciation value becomes the taxable value of the property for the following fiscal year.

Background

In 1994, Assembly Bill 3514 (Ch. 527, Stats. 1994, Costa) was enacted to create the hand tool exemption. AB 3514 was sponsored by the International Association of Machinists. At that time, two or three counties had just begun to tax the privately owned tools of auto and aircraft mechanics who use their tools in their employer's business. Apparently, in those counties, owners of smaller independent businesses who supply their employees with tools (and thus pay taxes on the tools) had complained that they were at a competitive disadvantage. Some larger businesses required their employees to provide their own tools and therefore those businesses did not pay any taxes on the tools. Although technically the employee-owned tools were subject to property tax from the employee-owner, they had not previously been assessed. The assessment of personal property owned by an employee and used in connection with the employee's profession, trade, or business (e.g. beauticians, plumbers, carpenters, dental hygienists) is of low priority and is not readily discoverable. The staff resources needed to locate and tax this type of property could often exceed the revenue collected. However, because of the complaints, an effort was made to begin the taxation of this property. The employees who subsequently received tax bills

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for their tools felt this was unfair because, while employers could pass on their property tax costs to their customers, the employees had to bear the costs themselves. AB 3514 was subsequently introduced and enacted to address their concerns.

COMMENTS

1. **Sponsor and Purpose.** This bill is sponsored by the California Conference of Machinists for the purpose of ensuring that the exemption level currently provided keeps pace with inflation.
2. **The taxation of personal property is discretionary with the Legislature.** Section 2 of Article XIII of the California Constitution provides that the Legislature, two-thirds of the membership in each house concurring, may classify personal property for differential taxation or exemption. In contrast, real property exemptions generally require a constitutional amendment.
3. **Personal property when it is used in a trade, profession, or business, whether owned by an individual or a business, is subject to property tax.** While employee-owned tools are legally subject to property tax, in practice, this property generally is not assessed.

COST ESTIMATE

With respect to property taxes, the Board would incur some minor absorbable costs in informing and advising local county assessors, the public, and staff of the annual change in the exemption amount.

REVENUE ESTIMATE

Background, Methodology, and Assumptions

This bill would, beginning on January 1, 2002, annually adjust the exemption amount for hand tools. The inflation adjustment factor to be used is the annual percentage change, measured from February to February, of the two previous assessment years, in the California Consumer Price Index (CCPI) for all items.

As an example of the effect of indexing this exemption, the percentage change in the CCPI from February 1999 to February 2000 was 3.3%. Applying this factor to the current \$20,000 hand tool exemption amount would adjust the exemption amount to \$20,660, an increase of \$660. The revenue from the property tax at 1% would amount to \$6.60.

The exemption for hand tools was enacted in 1995. At that time, only a few counties were assessing hand tools. We are not aware of any county that is assessing hand tools currently. Since the proposal would change the exemption amount by such small increments and since few, if any, counties are assessing hand tools, we believe that the revenue loss from this proposal would not be significant.

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Revenue Summary

The revenue impact from increasing the current \$20,000 property tax exemption for hand tools annually in accordance with a specified inflation adjustment is not expected to be significant.

Analysis prepared by:	Rose Marie Kinnee	445-6777	3/05/01
Revenue estimate by:	Aileen Takaha Lee	445-0840	
Contact:	Margaret S. Shedd	322-2376	

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