STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Date Introduced	**2/22/02**	Bill No:	**ACA 18**
Tax:	**Property**	Author:	**Wiggins**
Board Position:	**Support**	Related Bills:	**ACA 19 (Nation)**

BILL SUMMARY

This bill would place a constitutional amendment before voters to expand the grandparent-grandchild change in ownership exclusion for grandchildren who have a developmental disability and whose parents are not deceased.

ANALYSIS

Current Law

Under existing property tax law, real property is reassessed to its current fair market value whenever there is a "change in ownership." (*Article XIIIA, Sec. 2; Revenue and Taxation Code Sections 60 - 69.7)*

Article XIIIA, Sec 2 of the California Constitution and Revenue and Taxation Code Section 63.1 exclude from the definition of change in ownership transfers of certain property between parents and children occurring on or after November 6, 1986. Specifically, transfers between parents and children of

- principal places of residences <u>and</u>
- the first $1 million of real property other than principal residences.

The parent-child change in ownership exclusion may be extended to the purchase or transfer of real property from grandparents to their grandchild if all of the parents of that grandchild who qualify as the children of the grandparents are deceased as of the date of purchase or transfer. The grandparent-grandchild exclusion is available to transfers of property occurring on or after March 27, 1996.

Proposed Law

This bill would amend subdivision (h) of Section 2 of the California Constitution to provide that the parent-child transfer provision may apply to any qualifying transfers of property occurring on or after November 6, 2002 between a grandparent and a grandchild who is developmentally disabled, thereby deleting the requirement that all the parents of that grandchild be deceased.

This bill would define "'developmental disability'' to mean a disability originating before the age of 18 that continues, or can be expected to continue, indefinitely, and constitutes a substantial disability for that individual.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

The bill would specifically provide that the term “disability” includes, but is not limited to, “mental retardation, cerebral palsy, epilepsy, autism, and any disabling condition that is found to be closely related to mental retardation or to require treatment similar to that required for individuals with mental retardation.”

The bill would specifically exclude from the definition of disability “other handicapping conditions that are solely physical in nature.”

In General

Property Tax System. California's system of property taxation under Article XIIIA of the State Constitution (Proposition 13) values property at its 1975 fair market value, with annual increases limited to the inflation rate, as measured by the California Consumer Price Index, or 2%, whichever is less, until the property changes ownership or is newly constructed. At the time of the ownership change or new construction, the value of the property for property tax purposes is redetermined based on current market value. The value initially established or redetermined, where appropriate, is referred to as the "base year value." Thereafter, the base year value is subject to annual increases for inflation. This value is referred to as the "factored base year value."

Background

Change in Ownership Exclusions. Article XIIIA, §2 provides for certain exclusions from the meaning of “change in ownership” and “newly constructed.” Additionally, certain definitional “exclusions” were embodied in the initial statutory definitions to implement Proposition 13 immediately after its passage. The following exclusions were statutorily provided.

Bills	Year	Change In Ownership Exclusion	R&T Code
AB 1488	1979, Ch. 242	Interspousal Transfers (later amended into the Constitution via Prop. 58)	§63
AB 2718	1982, Ch. 911	Parent to Minor Child Upon Death of Parent-Residence	§62(m)
AB 2890	1984, Ch. 1010	Parent to Disabled Child - Residence	§62(n)

Since the enactment of Proposition 13 and the initial implementing statutory legislation, the Constitution has been amended twice to provide for additional change in ownership exclusions. These transfers will not trigger a reassessment of the property to current fair market value. Instead, the property will retain the prior owner’s base year value.

Prop.	Election	Change In Ownership Exclusion	R&T Code
58	Nov. 6, 1986	Parent-Child Interspousal- statutorily provided since 1979	§63, §63.1
193	March 26, 1986	Grandparent–Grandchild	§63.1

Other legislation previously before the Legislature but not enacted to exclude certain transfers from change in ownership either through constitutional amendment or statutory amendment include:

Bills	Year	Change in Ownership Exclusion
AB 1419	1981	Transfers between family members – spouse, brother, sister, lineal ancestor, or lineal issue.
ACA 8	1987	Transfers of principal place of residence between siblings who lived together two years prior.
ACA 55	1988	Transfers of principal place of residence between siblings who lived together two years prior.

Additionally, Proposition 36 of November 1984, a "Save Proposition 13" constitutional initiative sponsored by Howard Jarvis, would have, among other things, excluded certain family transfers from change in ownership. That proposition failed.

Prop.	Election	Change in Ownership Exclusion
36	Nov. 6, 1984 45.2% - 54.8%	Transfers to parents, grandparents, grandchildren, stepparents, uncles, aunts, spouses, stepchildren, siblings, and lineal descendants of the owner.

COMMENTS

1. **Sponsor and Purpose.** This bill is sponsored by the author to place a constitutional amendment on the ballot to allow the grandparent-grandchild change in ownership exclusion to be extended to a developmentally disabled person, as defined, where the grandchild still has a parent living. Currently, direct transfers of real property from a grandparent to a grandchild are eligible for a change in ownership exclusion only when all of the parents of the grandchild are deceased. The author's office is addressing those situations where a grandparent is attempting to ensure the future financial security of a grandchild whose parent(s) are living, but not in a position to reliably care for, or provide for, matters related to the grandchild.

2. **Under current assessment practices, two separate parent-child transfers could be used to effectively transfer a property from a grandparent to a grandchild without triggering a reappraisal of the property.** In Letter to Assessors 1998/23, dated April 22, 1998, Board staff opined that a two-step transfer, where each transfer separately qualified for the parent-child change in ownership exclusion, was permissible provided that the intervening parent was not subject to a "restriction" requiring that he or she transfer the property to the grandchild. http://www.boe.ca.gov/proptaxes/ltacont.htm

   15. **Question:** Can an unrestricted transfer from grandparent to parent immediately followed by a transfer from parent to child qualify for the parent-child exclusion?

   Answer: Yes. Chapter 48 of the Statutes of 1987 states that it is the intent of the Legislature to liberally construe section 63.1 to carry out the purpose of Proposition

58. Therefore, as long as each transfer is **unrestricted** and is otherwise eligible (e.g., between parents and children), the exclusion is applicable. If the parents are restricted to transferring the property to their child, then the step transaction doctrine would apply and these steps would be collapsed into one transaction, i.e., a transfer from grandparent to grandchild. Since the parents are living, the grandparent-grandchild exclusion would not apply, and this transaction would not be excluded from change in ownership.

3. **This bill would allow direct transfers between grandparents and grandchildren.** It is possible under current law to use two transfers to transfer property from a grandparent to a grandchild and not subject the property to reappraisal. However, family members may not be aware of this possibility, it may be unacceptable to the parties involved, or the parent, for whatever reason, cannot be used or is unavailable to perfect the transfer.

4. **The existing statutory definition of "parent" is rather broad, thereby limiting the grandparent-grandchild exclusion even though both biological or adoptive parents of a person are deceased.** In general terms, "parent" means a grandchild's parent who is a natural or legally adopted child of the grandparent(s). "Parent" also includes a stepchild or in-law child of the grandparent(s), unless the marriage on which the relationship was based was terminated by divorce. However, where the marriage on which the relationship was based was terminated not by divorce, but instead by the death of the grandparent's natural or legally adopted child, the surviving spouse (i.e., the stepchild or in-law child of the grandparent(s)) is considered a "child" of the grandparent(s) until he/she remarries. The broad definitions work to the benefit of those claiming the parent-child exclusion but work against those seeking to claim the grandparent-grandchild exclusion.

5. **"No Double Benefits" Provision.** For the parent-child change in ownership exclusion, there is no limitation on the number of principal residences that may be transferred between parents and children. However, when a grandparent-grandchild exclusion is claimed on a grandparent's principal residence, certain limitations apply. Under existing law, if a child previously received a change in ownership exclusion on a parent's principal residence prior to that parent's death, the child could not also receive an exclusion on the grandparent's principal residence, unless a portion of the parent's one million dollar cap was still available. This limitation exists to prevent double benefits of the change in ownership exclusion from using the provisions for both grandparents and parents (Art. XIIIA Sec. 2, (h)(2)(B)). The same limitation would apply under this bill. If a child already received an exclusion on a parent's principal residence, the child could not receive an exclusion on the grandparent's principal residence in the future unless it could be excluded under the parent's one million dollar cap. There does not appear to be a limitation on the number of exclusions permitted on principal residences if the grandparent's principal residence is transferred to the grandchild prior to a transfer of a parent's principal residence to a child. In this case, both principal residences could be excluded from reappraisal and neither would count towards the one million dollar cap.

6. **If a transfer of real property from a grandparent to a grandchild is not excluded under the principal residence portion and is instead counted toward the parent's one million dollar exclusion and the parent is not deceased, this will limit the parent's ability to use his/her $1 million exclusion (i.e., he/she will have less than $1 million to use, since his/her parent has already used a portion).** Transfers from a grandparent to a grandchild would count towards the parent's $1 million exclusion cap. As addressed in Comment #5 and in Letter to Assessors 1997/32, dated June 5, 1997, transfers to a child from a grandparent are limited based upon the amount of the parent's one million dollar cap that has not been previously used, as the one million dollar exclusion available to grandchildren from their grandparents is the same one million dollar full cash value exclusion which remains from their parents (i.e., the child of the grandparents). Thus, it is possible that in situations where the parent also intends to transfer property to the child in the future, some of that property will not receive the parent-child change in ownership exclusion if the one million dollar cap was in part consumed or exceeded by previous transfers from the grandparent to the grandchild.

7. **In the 2000-01 Property Taxpayers' Bill of Rights Annual Report, the California Taxpayers' Rights Advocate identified the limitations of the grandparent-grandchild change in ownership exclusion as an emerging issue that should be addressed.** The Taxpayers' Rights Advocate notes the need to revisit the extent of the definition of "parent" as it relates to the grandparent-grandchild exclusion. It appears that the advocates of Proposition 193 considered the situation where property would be transferred from grandparents to their own grandchildren where "both" parents (i.e., limited to two) are deceased; they did not necessarily consider that the broad definition of "parents" including more than the birth or adopted parents, such as a surviving step-parent who never remarried or the parent(s) of the person's spouse. The report can be obtained at http://www.boe.ca.gov/tra/taxcont.htm

8. **This constitutional amendment is prospective, therefore it only applies to transfers occurring on or after November 6, 2002.** This constitutional amendment is not retroactive or retrospective as currently drafted. It would therefore only apply to transfers **first** occurring on or after November 6, 2002, if enacted by the voters. Any transfer between a grandparent and their developmentally disabled grandchild occurring prior to this date, such as contacts from constituents to the author's office for events that have already transpired, would not be affected. As currently drafted, the November 6, 2002 date would be embedded in the Constitution requiring another constitutional amendment to change its application with respect to retroactivity. Consequently, if enacted, similarly-situated taxpayers with a qualifying grandparent-grandchild transfer occurring prior to November 6, 2002 may mistakenly believe that the constitutional amendment will reverse the reappraisal of the property in question, leading to disappointment and eventual requests for another constitutional amendment.

9. **If prospective application to transfers first occurring on or after November 6, 2002 is not the author's intent, then clarity on the retroactive/prospective/retrospective application of the bill and explicit**

language that matches that intent will avoid future frustration and conflict for all parties involved. Because of ongoing taxpayer objections from persons where the parent-child or grandparent-grandchild change in ownership exclusion would have been available but a claim was not filed within the time permitted, legislation was eventually enacted in 1996 to give retrospective relief upon application (i.e., no refunds for prior tax years, relief granted prospectively). This constitutional amendment could be amended to similarly apply to transfers on a "retrospective basis" beginning with the original Proposition 193 amendment of March 27, 1996.

10. **Related Legislation.** ACA 19 (Nation) would provide for a greater expansion of the grandchild-grandparent change in ownership exclusion to include transfers under all circumstances where the grandchild still has a parent living. However, ACA 19's expansion is limited to principal residences whereas this bill would apply to both principal residences and other real property up to the $1 million cap.

COST ESTIMATE

With respect to property taxes, the Board would incur some minor absorbable costs in informing local county assessors, the public, and staff of the law changes if this constitutional amendment is adopted by the voters of California.

REVENUE ESTIMATE

Background, Methodology, and Assumptions

Current property tax law excludes from the term "change in ownership", the purchase or transfer of principal places of residence or the first million dollars of all other property 1) between parents and children or 2) between a grandparent to a grandchild whose parents are deceased.

Under this bill, the grandparent/grandchild change-in-ownership exclusion would be extended to transfers between a grandparent to a grandchild who is developmentally disabled. The revenue effect is difficult to pinpoint due to the lack of predictability of the factors involved, including which properties would be affected, their assessed value and their market value at the time of transfer.

It is likely that the number of affected transfers in a year would be small (fewer than 100) and the bulk of these would be transfers of principal places of residence. Based on reports from county assessors, the average assessed value of properties receiving the homeowners' exemption in 2000 was $176,000. The median home price in December 2001, according to the California Association of Realtors, was $285,000.

The total amount of affected value can be estimated as [$285,000 - $176,000] x 100, or $10.9 million.

Revenue Summary

The annual revenue impact at the basic one percent property tax rate from extending the grandparent/grandchild change-of-ownership exclusion to transfers between a grandparent and a grandchild who is developmentally disabled is $10.9 million x 1 percent, or $109,000.

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