

[Senate Bill 1473](#) (Governance and Finance Committee)
Date: August 19, 2020
Program: Property Taxes
Government Code Sections 15643, 15645, 15646; and
Revenue and Taxation Code Sections 214.18 and 439.2
Effective: January 1, 2021

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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 State Board of Equalization (BOE)-sponsored changes:

- Extends the BOE's current county survey cycle for an additional five years. (*Government Code [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." (*Revenue and Taxation Code [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)*)

Summary of Amendments: Since the BOE's last bill analysis, SB 1473 has been amended to remove the proposed 60-day period in which a former assessor was to respond to the findings and recommendations in a survey report that reviewed the former assessor's procedures and practices.

Costs: The BOE will incur absorbable costs to update its documents and website materials, and provide guidance to County Assessors.

Fiscal Impact Summary: The revenue impact resulting from the change to the interest component for the assessment of historical property is indeterminable. None of the other BOE-sponsored provisions have a revenue impact.

However, the proposed non-BOE-sponsored change to the welfare exemption contract provisions in RTC section 214.18(a)(3)(B) may result in an indeterminable revenue loss.

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 BOE's formal position.

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, three 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 current language of this survey cycle sunsets December 31, 2020. Language that will become operative January 1, 2021 is already written into GC section 15643.

The provisions that 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.

Proposed 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.¹

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

¹ Publication 216, *The First 100 Years* (https://www.boe.ca.gov/info/pub216/property_tax_reform.html)

Commentary:

1. **Summary of Amendments.** The **August 19** amendment removed the proposed 60-day period in which a former assessor was to respond to the findings and recommendations in a final, published survey report that reviewed the former assessor's procedures and practices.
2. **Survey Cycle.** The provisions that become operative January 1, 2021 will 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 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.
3. **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.
4. **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 claimant² 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.³

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

² 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.

³ RTC section [214\(g\)\(1\)\(A\)](#) and RTC section 214(g)(1)(B).

- 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."⁴ 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.⁵

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.⁶

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

- 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 organizations⁷ with no-interest financing (i.e., "silent second mortgage").⁸

⁴ RTC section [110\(b\)](#).

⁵ RTC section 402.1.

⁶ *Carlson v. Assessment Appeals Board No. 1* (1985) 167 Cal.App.3d 1004.

⁷ 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.

⁸ RTC section 402.1(a)(10) – Added in 2015. Health & Safety Code section [50052.5](#) defines "affordable housing cost."

- Land easements granted to nonprofit organizations to preserve and protect land in its natural state.⁹
- Greenway easements granted to nonprofit organizations to create paths along urban waterways.¹⁰
- 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.¹¹

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.

Proposed 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).

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.¹² 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

⁹ RTC section 402.1(a)(8)(A) – Added in 1993, but the law since 1984 via Civil Code [section 815.10](#).

¹⁰ RTC section 402.1(a)(8)(B) – Added in 2015.

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

¹² [42 U.S.C. 12773](#)

- 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.¹³

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.¹⁴

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 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

¹³ <https://groundedsolutions.org/strengthening-neighborhoods/community-land-trusts>.

¹⁴ Letter To Assessors [2017/008](#).

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.¹⁵ BOE staff met on multiple occasions with County Assessors, CLT representatives, and other interested parties in a joint effort to develop uniform 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.¹⁶ 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.

Revenue Impact: The technical change to RTC section 214.18(c)(1) will not have a revenue impact. However, the change to RTC section 214.18(a)(3)(B) may have a revenue impact. It is unknown how many rental properties CLTs will develop. Revenue impact depends on (1) the number of rental properties owned by CLTs now and in the future; (2) the number of rental properties that will additionally qualify for exemption under this bill, and (3) the assessed value after considering the use and resale restrictions and the limited applicability of comparable market sales. At this time, based on these unknown factors, the revenue loss is indeterminable.

¹⁵ 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.

¹⁶ 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.

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 Act¹⁷) 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. RTC section 439.2, subdivisions (b)(1) and (c)(1) specify that the interest component is 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.

Proposed 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.¹⁸ 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 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 property¹⁹ 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.

¹⁷ The Mills Act is described on page 9 under the subheading "In General," *infra*.

¹⁸ California Department of Parks and Recreation, Office of Historic Preservation, [Mills Act Program](#).

¹⁹ GC section [50280.1](#).

Historical Property Contract (aka Mills Act Contract). The historical property contract²⁰ 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 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*.²¹

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.²²

²⁰ GC section [50281](#) and [50282](#).

²¹ See Letter To Assessors No. [2005/035](#).

²² See Letter To Assessors No. [2019/033](#).

- 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.²³ 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,²⁴ is a public government-sponsored enterprise. Freddie Mac was chartered by Congress in 1970 and 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®)²⁵ 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](#).²⁶
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.

²³ <https://www.fhfa.gov/DataTools/Downloads/Pages/Monthly-Interest-Rate-Data.aspx>.

²⁴ <http://www.freddie.com/>.

²⁵ <http://www.freddie.com/pmms/>.

²⁶ RTC section 439.2(d).

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,²⁷ 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.
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.

Revenue Impact: The interest component used for 2019 was 4.25 percent, based on the last published effective interest rate for conventional mortgages that was issued on May 29, 2019. Without this bill, the interest component will not change for future years. The revenue impact of this bill depends on (1) the number of historical properties subject to Mills Act contracts, and (2) the difference between the 4.25 percent effective interest rate and the future average interest rate as published by the Federal Home Loan Mortgage Corporation. At this time, since the average interest rate as published by the Federal Home Loan Mortgage Corporation is unknown, the revenue impact is indeterminable.

²⁷ <http://www.freddiemac.com/pmms/about-pmms.html>.