STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Date Amended:	**4/24/01**	Bill No:	**AB 218**
Tax:	**Property**	Author:	**Dutra**
Board Position:	**Support**	Related Bills:	**SB 48 (McClintock)** **AB 2288 (2000)**

BILL SUMMARY

This bill would increase the homeowners' exemption for qualified first-time homebuyers who purchase a home after January 1, 2002 and before December 31, 2007, from $7,000 to $50,000 for the first 5 years of ownership.

ANALYSIS

Current Law

Article XIII, Section 3(k) of the California Constitution exempts from property tax the first $7,000 of assessed value of an owner-occupied principal place of residence. This exemption is commonly referred to as the "homeowners' exemption." The Constitution authorizes the Legislature to increase the amount of the homeowners' exemption, provided that:

1. Any increase is funded by increasing the "rate of State taxes" in an amount sufficient to reimburse local governments for property tax revenue loss[1] and
2. Benefits to renters, which under current practice are granted through the renters' tax credit, are increased by a comparable amount.

Section 218 of the Revenue and Taxation Code specifies eligibility for the exemption and sets the exemption in the amount of $7,000 of full cash value.

Proposed Law

This bill would amend Section 218 of the Revenue and Taxation Code to increase the amount of the homeowners' exemption for qualified first-time homebuyers by an additional $43,000, for a total exemption amount of $50,000 of assessed value, for up to five years if:

1. the income of the qualifying homebuyer does not exceed 150 percent of the median income for the county at the time of purchase; or in the case where there is more than one buyer, the annual combined income does not exceed 150% of the median household income.

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[1] Article XIII, Section 25 requires that the state reimburse local government for the property tax revenue loss resulting from the homeowners' exemption.

2. the homebuyer has not had an ownership in residential real property in the prior three years, and

3. the home is purchased after January 1, 2002 and before December 31, 2007.

This bill would also require the Board to report to the Legislature the number of first-time homebuyer exemption claims made and the State Controller to report the additional amount of subventions made for each fiscal year. It would also require the California Research Bureau to report, by June 30, 2003, the impact that this measure had on state fiscal affairs and home ownership levels.

Background

This bill is similar to AB 2288 of the 2000 legislative year, which did not pass out of the Assembly Revenue and Taxation Committee.

Over the years, numerous proposals have been before the Legislature to increase the amount of the homeowners' exemption. Those proposals used various methods, including increasing the exemption by a flat amount, indexing the exemption for inflation, and varying the exemption according to the year of purchase.

Previous legislative attempts are summarized in the following table:

Bill Number	Legislative Session	Author	Type
AB 2288	1999-2000	Dutra	Increase for 1st time homebuyers
AB 2158	1999-2000	Strickland	Increase to $8,750 for senior citizens
SCA 8	1999-2000	Johannessen	Increase to $20,000; delete renter's credit parity
AB 2060	1997-98	Granlund	Increase to $20,000
ACA 43	1997-98	Granlund	Increase to $20,000
ACA 5	1991-92	Elder	Variable according to assessed value
ACA 31	1991-92	Frizzelle	Index for inflation by California CPI
ACA 47	1991-92	Jones	25% exemption; no assessed value cap
ACA 3	1989-90	Elder	Variable depending on year acquired
ACA 9	1989-90	D. Brown	25% exemption; $250,000 assessed value cap
ACA 31	1989-90	Hannigan	15% exemption; $150,000 assessed value cap
ACA 55	1989-90	Wright	Increase to $48,000
ACA 1	1987-88	Elder	Increased to $25,000 + indexing for inflation
ACA 25	1987-88	D. Brown	25% exemption; $250,000 assessed value cap
AB 2141	1985-86	Klehs	20% exemption; $50,000 exemption cap
AB 2496	1985-86	Cortese	Increased in years with General Fund Reserves
AB 3086	1985-86	Elder	Variable depending on year acquired
AB 3982	1985-86	La Follette	Increase for 1st time home buyers
ACA 49	1985-86	Elder	Variable depending on year acquired

COMMENTS

1. **Sponsor and Purpose.** This bill is sponsored by the author in an effort to reduce property taxes for first-time homebuyers.

2. **Amendments.** The April 24 amendments address administrative concerns noted in the Board analysis of this bill as introduced. Specifically:

   - **Multiple Owners.** The bill was redrafted to address the situation where more than one taxpayer purchases a home. It additionally specifies that in this case incomes would be combined for purposes of the income threshold.
   - **Retroactive Effective Date.** The effective date of the bill's provisions was amended to January 1, 2002, so that it would not be retroactive.
   - **First-Time Homebuyer Verification.** The bill was amended to require a taxpayer to provide a written statement, under the penalty of perjury, that he or she is a first-time homebuyer, so that neither the assessor nor the Board would be required to expend resources to verify a person's eligibility.
   - **Reporting Requirements.** This bill as introduced required the Board to furnish to the Legislature data on the additional subvention amounts resulting from this measure. Since the State Controller's Office currently tracks subvention information, the bill was amended to provide that the Controller would furnish this information.

3. **Administrative Issues.** A few remaining technical remarks and recommended solutions are noted as follows, with suggested language.

   - **Tax Returns.** A homebuyer would provide the county assessor with a copy of their income tax return for the taxable year during which they purchased the home. However, that tax return would not be prepared until the following year. The suggested language below would provide that the most recently completed tax return be used.
   - **Median Income.** A qualified first-time homebuyer is defined to mean a taxpayer, who, *at the time of his or her purchase* had an annual income of less than 150% of the median income for the county. Data on median income for any particular tax year would not be known at the time of purchase. (It would not be available until almost two years later). The language suggested below would provide assessors, taxpayers, and loan agents with a convenient means of determining whether a homeowner would likely qualify by using income limits currently prepared and published by the Department of Housing and Community. The range of minimum median income using these as the measure of income would be a low of $57,900 ($38,600 x 150%) for 18 counties to a high of $130,950 ($87,500 x 150%) for the county of Santa Clara. Income limits for all counties can be viewed at http://www.hcd.ca.gov/hpd/hrc/rep/state/incNote.html.
   - Using the medium income limit "most recently published on the date of purchase" addresses the situation that HCD does not publish income limits for the current year until April of each year.

- Using the median income for a family of four as the measure of income for all persons addresses household income when multiple incomes are combined. Thus, the suggested language deletes the word "household."

- **Late-Filing Partial-Exemption Provisions.** Conforming amendments to Section 275 would be necessary to increase the amount of the partial exemption provided to persons who miss the February 15 deadline for filing a claim for the homeowners' exemption.

Suggested Language:

218. (a)(2)(A) The taxpayer had an annual income not in excess of 150 percent of the median income of the county in which the dwelling is located, or in the case where more than one taxpayer owns the home, the taxpayers' annual combined income did not exceed 150 percent of the median ~~household~~ income of the county in which the dwelling is located. A taxpayer, or taxpayers, shall comply with this subparagraph by providing the county assessor with a copy of the taxpayer's most recently completed personal income tax return, ~~for the taxable year during which the taxpayer purchased the dwelling~~, that shows an annual income level in compliance with this subparagraph. For purposes of this subdivision, the median income of the county shall be the four-person median income limit for the county that was most recently published on the date of purchase by the Department of Housing and Community Development pursuant to Sections 50079.5 and 50105 of the Health and Safety Code.

275. (a) If a claimant for the homeowners' property tax exemption fails to file the required affidavit with the assessor by 5 p.m. on February 15 of the calendar year in which the fiscal year begins, but files that affidavit on or before the following December 10, an exemption of the lesser of five thousand six hundred dollars ($5,600) or 80 percent of the full value of the dwelling, or, for qualified first-time homebuyers, the lesser of forty thousand dollars ($40,000) or 80 percent of the full value of the dwelling, shall be granted by the assessor.

4. **Exemption Amount Unchanged for 27 Years.** The homeowners' exemption was enacted in 1968 in the amount of $3,000 of full cash value and was increased in 1974 to its current level of $7,000 of full cash value. Arguments advanced against increasing the homeowners' exemption have centered on the point that Proposition 13, instituted in 1978 after the last increase in the homeowners' exemption, has provided sufficient property tax relief to all property owners, including homeowners.

5. **The $7,000 Exemption is a Minimum Amount.** The $7,000 amount specified in the Constitution sets forth the *minimum* amount of the exemption. The Constitution states that the homeowners' exemption can be increased, statutorily, as long as it is associated with an equivalent increase in the amount of the renters' credit. Presumably, it could be argued that the amount of the renter's credit for new renters

should also be increased. However, the renters' credit was suspended from the 1993 through the 1997 income tax years in accordance with budget agreements. It was restored in 1998 by AB 2797, a budget trailer bill. During this suspension period homeowners continued to receive the homeowners' exemption.

6. **Provides Additional Tax Savings of $430 per Year for Five Years (Total $2,150) for Qualified First-Time Homebuyers.** The homeowners' exemption, in the amount of $7,000 of full cash value, provides annual property tax savings of about $70 at the 1% tax rate. This measure would increase the annual property tax savings to $500 per year for the first five years of ownership.
7. **Five Year Tracking.** Counties would incur costs in tracking the exemption for five years in order to reduce the exemption to $7,000 in year six.
8. **Related Legislation.** SB 48 (McClintock) would increase the homeowners' exemption from $7,000 to $25,000, for all homeowners, and provide for future automatic increases through an annual inflation adjustment.

COST ESTIMATE

With respect to property taxes, the Board would incur some minor absorbable costs in revising exemption claim forms, updating Assessors' Handbooks, and addressing implementation issues raised by taxpayers and tax professionals including county assessors.

REVENUE ESTIMATE

Background, Methodology, and Assumptions

The state is required to pay subventions to counties for the homeowners' exemptions to offset the resulting county property tax loss. The state reimbursement to local governments for the homeowners' exemption totaled $397.1 million in 1999-00.

Under this proposal, the homeowners' exemption for certain homebuyers would be supplemented by $43,000 for up to five years if the income of the qualifying homebuyer does not exceed 150 percent of the median income for the county and the homebuyer neither has, nor has had, an ownership in a principal residence in the prior three years. It is difficult to predict the number of homebuyers that would meet these requirements. For the purposes of this estimate, therefore, it is assumed that the annual increase in the number of homeowners' exemptions can be substituted for the number of qualifying purchases.

Since 1994, the number of homeowners' exemptions has grown from 5.0 million to 5.2 million. However, the annual increase in the number of exemptions, as shown in the following table, has fluctuated substantially in the last seven years, ranging from the high of 123,179 in 1994 to the low of 12,067 two years later.

	Number of homeowners' exemptions	Increase from prior year	Percent change from prior year
2000	5,207,135	22,542	0.4%
1999	5,184,593	31,149	0.6
1998	5,153,444	15,758	0.3
1997	5,137,686	40,298	0.8
1996	5,097,388	12,067	0.2
1995	5,085,321	56,726	1.1
1994	5,028,595	123,179	2.5

The recent decline in the annual increase in homeowners' exemptions can be attributed, in great part, to the downward trend in housing affordability. According to the California Association of Realtors (C.A.R.), housing affordability in the state fell to 32 percent in December 2000, down 4 percentage points from December 1999. The monthly housing affordability index used by C.A.R. measures the percentage of California households that can afford to purchase a median-priced existing home, which was $249,350 in December 2000.

It is likely that the number of exemptions will grow between 12,000 and 120,000 annually and that the market value of these homes will each exceed $50,000. The latest available statewide average tax rate is 1.067 percent. The maximum increase in the subvention for the first year under this proposal is then [12,000 to 120,000] x $43,000 x 1.067%, or $5.5 million to $55.1 million.

Revenue Summary

The breakdown of the estimated maximum increase in the homeowners' exemption subvention for each of the first four years and for the fifth year and after is:

First Year	$5.5 million to $55.1 million
Second Year	$11.0 million to $110.1 million
Third Year	$16.5 million to $165.2 million
Fourth Year	$22.0 million to $220.2 million
Fifth Year and after	$27.5 million to $275.3 million

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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.