

[Senate Bill 404](#) (Stone)

Date: Introduced

Program: Property Taxes

Sponsor: Author

Revenue and Taxation Code Sections 51, 205.5, and 5813

Effective: Upon enactment, but operative for January 1, 2018 lien date for 2018-19 fiscal year.

Michele Pielsticker (Chief) 916.322.2376

Rose Marie Kinnee (Analyst) 916.445.6777

Chris Butler (Revenue) 916.445.0840

Summary: This bill provides two veteran-related property tax benefits:

- **Disabled veterans' exemption.** Exempts from property tax the home of any person eligible for the disabled veterans' exemption; and
- **Veterans 65+: Assessment freeze.** Eliminates annual inflation factor-related assessed value increases on homes owned by income-qualifying veterans 65 years and older.

Purpose: To provide a full property tax exemption to disabled veterans or their unmarried surviving spouses and property tax relief to income-qualifying senior veterans by freezing assessed values once they turn 65.

Fiscal Impact Summary: Annual revenue loss of \$73.9 million. (\$65.9 for disabled veterans' exemption and \$8 million for income-qualifying senior veterans.)

Disabled Veterans' Exemption

Revenue and Taxation Code Section 205.5

Existing Law: The California Constitution¹ authorizes the Legislature to exempt partially or fully from property tax, the home of a person or spouse, including an unmarried surviving spouse, if the person has incurred certain injuries, including blindness in both eyes, lost use of 2 or more limbs, or is totally disabled. The exemption also applies if a person's death is from a service-connected injury or disease, or occurs while on active duty in military service. This exemption is commonly referred to as the "disabled veterans' exemption."

Statutory Exemption Amount. Current law contains a partial exemption.² For the 2017-18 fiscal year, persons with household incomes below \$58,754 may receive an exemption of \$196,262. For all other eligible persons, the exemption amount is \$130,841.³

Proposed Law: This bill provides a full exemption for the home of any person qualified to receive the disabled veterans' exemption.

Effective Date. As a tax levy, this bill is effective immediately upon enactment. However, the bill provides that it applies commencing with the lien date for the 2018-19 fiscal year. (RTC Section 205.5(h))

In General: California law provides qualified disabled veterans and their unmarried surviving spouses with a property tax exemption that applies to their home's assessed value. To be eligible, the claimant must obtain a United States Department of Veterans Affairs (USDVA) disability rating that either (1) rates the veteran's disability at 100% or (2) rates the veteran's disability compensation at 100% because the veteran is unable to secure and maintain gainful employment.

¹ [Section 4\(a\)](#) of Article XIII of the California Constitution.

² Revenue and Taxation Code (RTC) Section [205.5](#).

³ This is the current exemption amount. Since 2006, RTC 205.5(h) allows a compounding inflation factor to apply to the \$150,000 and \$100,000 amounts. This is the current income threshold. Since 2002, RTC 205.5(g) allows a compounding inflation factor to apply to the \$40,000 income threshold. Letter to Assessors [2016/017](#), dated May 3, 2016, lists exemption amounts and household income limitations effective for lien dates 2002 through 2017.

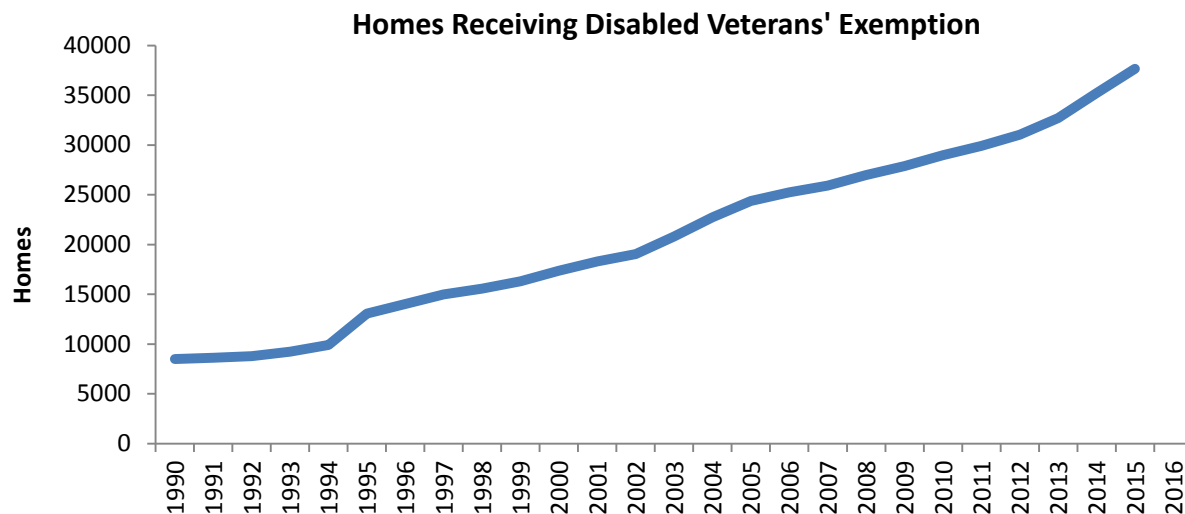
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The law also allows surviving spouses to receive the exemption if the spouse's death was service-connected. To be eligible for the exemption, surviving spouses must receive a USDVA determination that the spouse's death was service-connected. A USDVA determination is necessary for (1) active duty personnel deaths (i.e., the service person was not a "veteran") and (2) veterans without a 100% rating when alive, but whose cause of death is deemed service-connected. Surviving spouses of veterans with a 100% disability rating during their lifetime continue to receive the exemption after the veteran's death so long as they do not remarry.

The exemption amount depends upon the claimant's income. For the 2017-18 fiscal year, the basic exemption adjusted for inflation will be \$130,841. If the claimant's income is less than \$58,754, the exemption amount will be \$196,262. For the fiscal year 2015-16, 37,653 disabled veterans or their unmarried surviving spouses were granted the exemption.

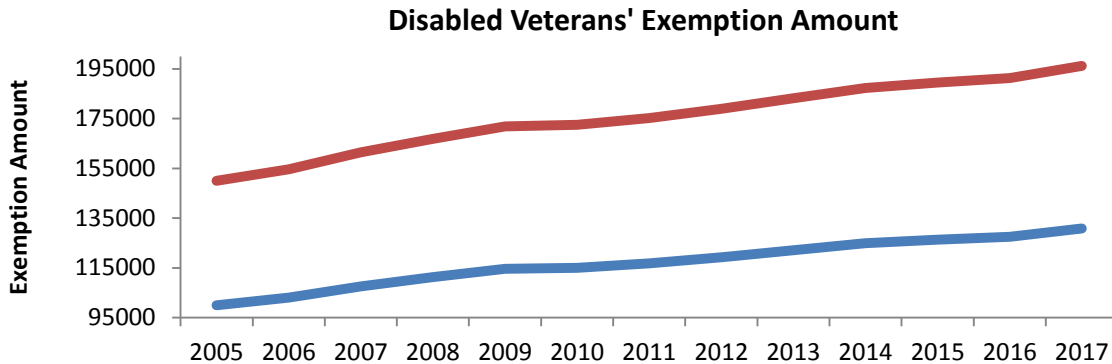
Qualification	Basic Exemption Amount	Lower Income Exemption Amount Income is less than \$58,754
<p style="text-align: center;">Disabled Veteran</p> <ul style="list-style-type: none"> • Disability Rating = 100% • Disability Compensation = 100% • Blind • Lost the Use of Two or More Limbs <p style="text-align: center;">Spouse of Military Personnel</p> <ul style="list-style-type: none"> • Surviving Spouse: Disabled Veteran • Surviving Spouse: Active Duty Death • Surviving Spouse: Posthumous service-connected death finding 	<p style="text-align: center;">\$100,000 adjusted for inflation</p> <p style="text-align: center;">\$130,841</p>	<p style="text-align: center;">\$150,000 adjusted for inflation</p> <p style="text-align: center;">\$196,262</p>
Claims Granted: 37,653	33,196	4,457

In 1990, 8,483 disabled veterans' exemptions were provided to eligible homeowners. For 2015, there were 37,653 eligible homeowners. In the last 25 years, this is a 344% increase.



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After 2005, the law allowed the \$100,000 and \$150,000 exemption amounts to annually increase by an inflation factor.



Legislative History: The following table lists the most recent proposals to increase the disabled veterans' exemption.

Year	Bill	Proposal
2016	SB 1104 (Stone)	Full Exemption
2016	AB 1556 (Mathis)	Increase to \$2.1 million
2016	SB 1183 (Bates)	Increase to \$1 million
2008	AB 2568 (Houston)	Full Exemption
2007	AB 1485 (Jefferies)	Full Exemption, as introduced
2007	AB 1485 (Jefferies)	Increase to \$200,000 and \$250,000, as amended
2005	SB 1005 (Florez)	Full Exemption for Spouses if Active Duty Death Full Exemption for Spouses if Public Safety Officer Death
2004	SB 764 (Morrow)	Inflation factoring commences January 1, 2006 (Enacted)
2003	SB 764 (Morrow)	Increase to \$200,000 and \$250,000, as introduced

Commentary:

- This bill fully exempts from property tax the homes of disabled veterans and their unmarried surviving spouses.** The California Constitution provides that the Legislature may exempt these homes in whole or in part. This bill proposes to modify the current partial exemption to a full exemption for all qualifying claimants. Additionally, by eliminating the income-based exemption amount, it eliminates the need for these claimants to annually reapply to verify their continued eligibility for the higher exemption amount.
- The state does not reimburse local governments for the property tax revenue loss from the Disabled Veterans' Exemption.** By contrast, the state fully reimburses local governments for the homeowners' exemption.
- Operative Date.** To transition from a partial to a full exemption at the least possible administrative cost, subdivision (h) of RTC 205.5 delays the operative date to coincide with the lien date for the 2018-19 fiscal year (i.e., January 1, 2018). Otherwise, as a tax levy, this bill would take effect immediately.
- How much is the exemption currently?** The exemption amount depends upon the claimant's income. For the 2017-18 fiscal year, persons with household incomes below \$58,754, may receive an exemption of \$196,262. For all other eligible persons, the exemption amount is \$130,841.⁴

⁴ This is the current exemption amount. Since 2006, RTC 205.5(h) allows a compounding inflation factor to apply to the \$150,000 and \$100,000 amounts. This is the current income threshold. Since 2002, RTC 205.5(g) allows a compounding inflation factor to apply to the \$40,000 income threshold.

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5. **How many persons claim the disabled veterans' exemptions?** For 2015, 37,653 exemptions were granted to eligible claimants: 33,196 basic exemptions and 4,457 lower income exemptions.
6. **Top 10 Counties.** For 2015, the counties with the most disabled veterans' exemptions in descending order include: (1) San Diego: 5,391; (2) Riverside: 3,732; (3) Sacramento: 2,422; (4) San Bernardino: 2,373; (5) Los Angeles: 2,092; (6) Solano: 1,764; (7) Orange: 1,691; (8) Contra Costa: 1,147; (9) Monterey: 990; and (10) Fresno: 959.

Costs: BOE would incur absorbable costs to modify forms, publications, and website materials.

Revenue Impact: Background, Methodology, and Assumptions. Existing property tax law provides a disabled veterans' exemption to military personnel, or their spouses, in the event of a service-connected injury, disease, or death, as specified. The law provides a basic exemption amount of \$100,000, but increases that amount to \$150,000 if the claimant's household income does not exceed \$40,000, with all amounts adjusted for inflation.

The following revenue impact estimate uses fiscal year 2015-16 data and exemption amounts for consistency, since this is the most recent year where all variables for the same year are available. For 2015-16, the basic exemption amount was \$126,380. The lower income exemption amount was \$189,571 for claimants with a household income below \$56,751.

To begin, staff estimated the number of disabled veteran owned homes currently receiving the exemption. In 2015-16, 37,653 disabled veterans' exemptions were granted: 33,196 at the basic level and 4,457 at the lower income level. Based on a survey of several counties, staff estimates that this bill will not impact 21% of homes receiving the basic exemption (6,971 homes) or 24% of homes receiving the lower income exemption (1,070 homes). These homes are already fully exempt because they have assessed values of less than \$126,380 and \$189,571, respectively. Thus, this bill will exempt from the property tax 29,612 homes: 26,225 (33,196-6,971) currently receiving the basic exemption and 3,387 homes (4,457-1,070) receiving the lower income exemption.

	Homes Granted Exemption	Homes Already Fully Exempt	Additional Homes Exempted
Basic	33,196	6,971	26,225
Lower Income	4,457	1,070	3,387
Total	37,653	8,041	29,612

Staff then estimated the additional amount of assessed value that this bill will exempt. Staff subtracted the current exemption amounts provided from the average assessed value (AV) of properties receiving the homeowners' exemption. For 2015-16, the average was \$356,370. The affected difference in value and revenue loss at the basic 1% property tax rate is then:

	Average Home AV	Exemption Current	Exemption Increase	Homes	Tax Rate	Tax Savings Per Home	Revenue Loss
Basic	\$356,370	\$126,380	\$229,990	26,255	1%	\$2,299	\$60.3 Million
Lower Income	\$356,370	\$189,571	\$166,799	3,387	1%	\$1,667	\$5.6 Million
Total				29,612			\$65.9 Million

Revenue Summary. The exemption of homes owned by persons qualified for the disabled veterans' exemption would result in a potential annual revenue loss of \$65.9 million.

Qualifying Remarks. For 2017, the basic disabled veterans' exemption amount increases to \$130,841, the lower income disabled veterans' exemption amount increases to \$196,262, and the household income limit increased to \$58,754. Counties will apply these amounts to their FY 2017-18 property tax rolls. The revenue estimate does not account for any changes in economic activity that may or may not result from enactment of the proposed law.

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Qualified Veterans 65+: Inflation Factoring

Revenue and Taxation Code Sections 205.5 and 5813

Existing Law: The California Constitution provides a **Veterans' Exemption**⁵ that applies to any property owned by a person who serves or has served in the military. However, this exemption has become effectively obsolete. For any veteran who owns a home, the homeowners' exemption provides greater tax savings.⁶ Veterans who do not own homes, but own other taxable property (i.e., a boat or business personal property) are disqualified if they own property worth more than \$5,000 (if single) or \$10,000 (if married). Thus, only two veterans in California currently qualify.

Inflation Adjustments. The law requires the assessor to establish a “base year value” for real property at its 1975 market value and thereafter reset the value to current market value every time the property changes ownership.⁷ The base year value must be compounded annually by an inflation factor not to exceed 2%.⁸ The inflation-adjusted value is called the “*factored* base year value.” Generally, every year the law requires a property’s assessed value to be based on its factored base year value or its current market value, whichever is lower.⁹

Relevant to this bill, the California Constitution¹⁰ specifies that a property’s base year value *may* reflect from year to year the inflationary rate not to exceed 2% for any given year.

Proposed Law. Beginning January 1, 2018, this bill eliminates future inflation factor increases for qualified veteran homeowners. To qualify, all of the following must apply.

- **Honorable Discharge.** The veteran must have been honorably discharged from military service.
- **Principal place of residence.** The inflation factor limitation only applies to a veteran's principal place of residence, including so much of the land surrounding it as is reasonably necessary for use of the dwelling as a home.
- **Age.** The veteran must be 65 on the lien date (January 1).
- **Household Income.** The veteran must have a household income, as specified, of less than \$50,000 if single or \$100,000 if married.

Effective Date. As a tax levy, this bill is effective immediately upon enactment. However, the bill first applies for any assessment year commencing on or after January 1, 2018. Generally, property taxes for the 2018-19 fiscal year¹¹ are based on the assessed value set for the January 1, 2018 lien date.

In General: Property Tax System. Voters changed California’s property tax system through Proposition 13, which replaced a current market value-based system with an acquisition value-based system. This tax system provides certainty to property owners regarding future property tax liability.

Specifically, under Proposition 13, real property assessed values were rolled back to 1975 market value levels and future assessed value increases were limited to the inflation rate, not to exceed 2%, for as long as the property’s ownership remains unchanged and the property is not substantially improved (i.e., new construction).

Thus, regardless of future real estate value increases, the 2% maximum inflation adjustment ensures limited assessed value increases. The acquisition-based system with the 2% inflation cap can result in substantial property tax savings for long-term property owners who do not move.

⁵ [Section 3\(o\)](#) of Article XIII of the California Constitution.

⁶ The veterans' exemption is \$4,000 and the homeowners' exemption is \$7,000.

⁷ RTC [Section 110.1](#) (a) and (b).

⁸ RTC Section 110.1 (f) and [Section 51](#).

⁹ RTC Section 51 (a)(1).

¹⁰ California Constitution Article XIII A, [Section 2\(b\)](#).

¹¹ July 1, 2017 to June 30, 2018

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Base Year Values. The “base year value” of real property is the Proposition 13 protected value of a property. Under existing law, once the base year value of real property is established, it subsequently must be adjusted by an inflation factor of no more than 2% per year.

Specifically, RTC Section 110.1 provides that the “full cash value” of real property means its fair market value as of the date on which a purchase or change in ownership occurs. Subdivision (b) of Section 110.1 provides that this value is to be known as the “base year value” while subdivision (f) of Section 110.1 requires that the base year value annually be adjusted by an inflation factor, as specified in subdivision (a) of Section 51. This bill proposes to amend Section 51 (a) to prohibit the adjustment for income-qualified seniors who are veterans.

Background: Veterans’ Exemption. At its peak, from 1956 through 1962, over one million persons received the veterans' exemption. Currently, only two people receive the exemption. The exemption’s usage declined for two reasons. First, in 1974, home-owning veterans transitioned to the homeowners' exemption when that exemption amount increased and provided greater tax savings. Second, the strict wealth limitations fixed in the California Constitution: \$5,000 if single and \$10,000 if married make most veterans ineligible.

Legislative History. Proposals to modify the veterans' exemption include:

Year	Bill	Proposal
2016	SB 1104 (Stone)	CPI-elimination for Income Qualified Senior Veterans. (Identical to this bill)
2005	SCA 14 (Morrow)	Create a Military and Veterans homeowners' exemption that is 10% greater than the homeowners' exemption for active military and veterans.
1997	ACA 9/AB 551 (Morrissey and House)	Increase the Veterans' Exemption to \$7,700 and eliminate the wealth cap. Held in Assembly Appropriations
1996	ACA 39/AB 2790 (Morrissey)	Increase the Veterans' Exemption to \$7,700 and eliminate the wealth cap. Failed in the Senate

Senior Provisions. Various age-based property tax benefits are available generally. This includes base year value transfers for persons 55+ that buy a qualifying home and a state program that allows income-qualified persons 62+ to postpone property taxes with interest.

Commentary:

- Provides financial relief to income and age qualifying home-owning veterans.** According to the author, capping the property tax assessment of veterans age 65 or older will help lower income veterans afford to stay in their own home and avoid homelessness. The author notes that homelessness is a significant issue for veterans.
- Freezes assessed values for income and age qualifying veterans 65+.** In practical application, this bill freezes the assessed values for income and age qualifying veterans at the home's factored base year value for the 2017-18 fiscal year, which is the factored base year value for the January 1, 2017 lien date. In addition, as other qualified veterans reach the age of 65, their home's assessed value will also be frozen.
- Historically, the inflation factor has applied equally to all property types and all property owners.** The Constitutional provision specific to “full cash value base” inflation adjustments does not appear to prohibit the Legislature from enacting a law that makes the inflation factor optional. The Constitution is silent on differential application of the inflation factor to the “full cash value base.” Section 2 (b) of Article XIII A of the Constitution reads:

The full cash value base *may reflect* from year to year the inflationary rate not to exceed 2 percent for any given year or reduction as shown in the consumer price index or comparable data for the area under taxing jurisdiction, or may be reduced to reflect substantial damage, destruction or other factors causing a decline in value.

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Nonetheless, Section 1 of Article XIII of the Constitution provides that:

All property . . . shall be assessed at the same percentage of fair market value. When a value standard other than fair market value is prescribed by this Constitution or by statute authorized by this Constitution, the same percentage shall be applied to determine the assessed value. The value to which the percentage is applied, whether it is to be the fair market value or not, shall be known for property tax purposes as the full value.”

Article XIII, Section 1 uses the terms “assessed value” and “full value.” It is unclear if the amendment to Section 51 prohibiting the application of an inflation adjustment to a limited class of properties could be interpreted to run counter to Section 1’s requirement, or if it could be interpreted as being “a statute authorized by this constitution.”

4. **Is basing the property tax on income level a new trend?** Last year, several bills proposed differential property tax assessed values on the basis of a homeowner's income rather than property value. None were enacted.
 - [SB 1126](#) - CPI-elimination seniors 65+ at \$25,000/50,000
 - [SB 1104](#) - CPI-elimination veterans 65+ at \$50,000/100,000
 - [AB 2668](#) – Permits base year value transfer for homes of greater values for 55+ if income at or below the area median income
5. **Assessment uniformity.** Assessed values lack uniformity under California's acquisition value based system. However, the acquisition-based standard is authorized by the Constitution and has been upheld by the courts. Adding an income-based element expands non-uniform assessment and complicates administration of the tax. This bill contains three qualifications (military service, age, and income) that the Constitution does not expressly authorize.
6. **The property tax is an ad valorem tax based on a property's assessed value.** Historically, the imposition of the property tax has not varied based on income. Likewise, the imposition of the sales and use tax and the various BOE-administered special taxes and fees is not impacted by one’s income. Property tax law does provide certain constitutionally-authorized *exemptions* to be applied to a property's *assessed value* and age-based *exclusions* from the definition of change in ownership.
7. **Annual income verification.** Should it become common to enact property tax laws that base assessed values on the property owner's income, independent verification of income eligibility would become increasingly important. Thus, assessors would need to delve into taxpayers’ private financial matters unrelated to property value. Assessors will need to establish a procedure to verify continued income eligibility specific to this bill's provisions. To this end, the bill allows the assessor to request additional proof of eligibility.
8. **Household income measure.** The bill uses the "household income" standard of RTC Section 20504, used for the Property Tax Postponement Program, the defunct Property Tax Assistance Program, and the disabled veterans' property tax exemption.
9. **Suggested technical amendment.** The income definition for a single veteran and a married veteran both specify income "as defined by RTC Section 20504," which defines *household* income, not an individual person's income. On its face, the language in the bill referring to "annual income" if single and "combined annual income" if married conflicts with the notion of “household income” in Section 20504. Corrective amendments consistent with intent are needed.
10. **Qualifying veterans will need to take action.** Assessors do not have information about homeowners’ veteran status, age, or income. The bill specifies a basic claim-filing requirement to request this tax benefit.

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11. **Excess land.** This bill expressly provides that the inflation factor limitation does not apply to land in excess of what is reasonably necessary for use of the property as a home. This is consistent with other property tax law provisions in which a “residential dwelling” means a dwelling occupied by the claimant as the principal place of residence, and so much of the land surrounding it as is reasonably necessary for use of the dwelling as a home. For example, for a home located on a parcel of land that is a large farm, the inflation factoring limitation would be limited to the home and the home site.

Costs: BOE would incur absorbable costs to modify forms, publications, and website materials.

Revenue Impact: Background, Methodology, and Assumptions. Generally, a property’s sales price is the assessed value (called the base year value), and annual increases to that value are limited to the rate of inflation, not to exceed 2% (called the factored base year value). This bill eliminates the annual inflation factor increase applied to the base year value of an age and income qualified veteran’s home.

Age. According to U.S. Census data, California veterans 65 and older account for 18% of all Californians 65 and over. Among this age group, there are roughly 750,000 owner-occupied homes in the state. While specific data does not exist, we can estimate the number of homes owned by veterans 65 and older as follows:

$$750,000 \text{ homes} \times 18\% = 135,000 \text{ homes}$$

Income. Based on a review of available data, we estimate that about 80% of veteran-owned homes will qualify given the income limits of \$50,000 if single and \$100,000 if married.

$$135,000 \text{ homes} \times 80\% = 108,000 \text{ homes}$$

For fiscal year 2016-17, the average assessed value (AV) of homes receiving the homeowners’ exemption was \$372,000. Eliminating the inflation factor for qualified veterans 65 and older results in annual revenue loss at the basic 1% property tax rate calculated as follows:

Average Home AV	Inflation Factor	AV Increase Avoided	Tax Rate	Tax Savings Per Home	Income Qualifying Veteran 65+ Homes	Revenue Loss
\$372,000	2%	\$7,440	1%	\$74.40	108,000	\$8 Million

Revenue Summary. By eliminating the inflation factor applied to a qualifying veteran’s home, this bill would result in a potential annual revenue loss of \$8 million.

Qualifying Remarks. This estimate assumes (1) a similar rate of homeownership for veterans 65 and over as for all Californians 65 and over and (2) a similar level of income for veterans 65 and over as for all Californians 65 and over.

This revenue estimate does not account for any changes in economic activity that may or may not result from enactment of the proposed law.