



Legislative Bill Analysis

[Senate Bill 1456](#) (Stern)
Date: March 31, 2022 (Amended)
Program: Property Taxes
Revenue and Taxation Code section 214
Effective: Immediately

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Summary: Amends Revenue and Taxation Code (RTC) section 214 to remove the welfare exemption cap of \$20 million in assessed value that certain housing providers may receive each fiscal year beginning after the effective date of the bill.

Summary of Amendment: The **March 31, 2022**, amendment adds legislative coauthors and makes a non-substantive technical change.

Fiscal Impact Summary: Based on information provided by County Assessors, the current revenue impact is zero as it is unclear whether any organizations appear to be over or near the cap at the present time.

Existing Law: Under the California Constitution, all property is taxable, unless otherwise provided for by the State Constitution or the laws of the United States.¹ The Legislature may exempt from property taxation in whole or in part, property used exclusively for religious, hospital, scientific, or charitable purposes and owned or held in trust by nonprofit corporations or other entities, if certain criteria are met.²

This exemption is known as the "welfare exemption" and is implemented pursuant to RTC³ section [214](#).

Section 214 generally exempts from taxation, subject to certain conditions and qualifications, property that is (1) owned by nonprofit organizations organized and operated for charitable purposes, and (2) used exclusively for those purposes.

Section 214(g)(1) provides generally that property used exclusively for low-income rental housing owned and operated by nonprofit organizations, including limited partnerships in which the managing general partner is an eligible nonprofit corporation, shall be deemed to be within the exemption authorized by section 214.

The State Board of Equalization (BOE) and 58 County Assessors are jointly responsible for administering the welfare exemption. The BOE is responsible for determining whether an organization is qualified for either an Organizational Clearance Certificate (OCC) or a Supplemental Clearance Certificate (SCC), while the County Assessor is responsible for determining whether the use of a qualifying organization's property is eligible for the welfare exemption. The County Assessor shall not grant the welfare exemption on an organization's property unless the organization holds either a valid OCC or SCC issued by the BOE. However, the County Assessor may deny a welfare exemption claim based on non-qualifying use of the

¹ California Constitution, [article XIII, section 1](#).

² California Constitution, [article XIII, section 4, subdivision \(b\)](#) and [Revenue and Taxation Code section 214, subdivision \(a\)](#).

³ All statutory references are to the Revenue and Taxation Code, unless otherwise provided.

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.

property, notwithstanding that the BOE has issued the organization an OCC or SCC. The BOE tracks [eligible nonprofit organizations and Limited Liability Companies](#) who hold valid OCCs and SCCs and monitors those organizations for continued eligibility.

Once an OCC or an SCC is issued by the BOE to a qualified organization, the organization will then file a claim for the welfare exemption with the County Assessor where the property is located. The County Assessor is responsible for evaluating the application, determining whether the use of the property meets the statutory requirements for receiving the welfare exemption, and for ultimately granting or denying the exemption to claimants.

Under existing property tax law, property that meets these requirements and is used exclusively for rental housing and related facilities is entitled to a partial exemption, equal to that percentage of the value of the property that is equal to the percentage that the number of units serving lower income households represents of the total number of residential units, in any year that certain criteria apply, including that the property be subject to a legal restriction that provides that units designated for use by lower income households are continuously available to or occupied by lower income households, at rents not exceeding specified limits.⁴

Taxpayers who provide housing where 90% or more of the occupants of the property are lower income households whose rent does not exceed the rent prescribed by Health and Safety Code (HSC) section 50053, have their total exemption amount capped at \$20 million in assessed value per fiscal year. Under this definition, affordable rent for lower income households is defined as “the product of 30 percent times 60 percent of the area median income adjusted for family size appropriate for the unit.”⁵

Proposed Law: Removes Cap on Welfare Exemption. Under existing law, low-income housing providers that meet certain requirements under section 214, may receive the welfare exemption with respect to a single property or multiple properties for any fiscal year not to exceed \$20 million in assessed value. This bill would remove the \$20 million in assessed value cap, thus, allowing these providers to receive the welfare exemption greater than \$20 million in assessed value beginning on and after the effective date of the bill.

2023 Lien Date. The bill states amendments made with respect to the removing of the \$20 million assessed value cap shall apply to lien dates occurring on and after the effective date of the act, which would be the 2023 lien date.

No Reimbursement Revenues. Any local agencies that lose local property tax revenues because of the removal of the welfare exemption cap proposed by this bill will not be reimbursed by the State unless the Commission on State Mandates determines this act contains costs mandated by the state.

Effective Immediately. If signed by the Governor, the bill will go into effect immediately.

In General: Under section 4(b) of article XIII of the California Constitution, the Legislature is authorized to exempt from taxation, in whole or in part:

Property used exclusively for religious, hospital, or charitable purposes and owned or held in trust by corporations or other entities (1) that are organized and operated for those

⁴ Section 214, subdivision (g)(1) and subdivision (g)(2)(A)(i).

⁵ Health and Safety Code section 50053, subdivision (b)(4).

purposes, (2) that are nonprofit, and (3) no part of whose net earnings inures to the benefit of any private shareholder or individual.

In exercising the above constitutional authorization, the Legislature enacted section 214, which reiterates the constitutional authorization and outlines numerous conditions and qualifications for receiving the welfare exemption, and adds scientific as the fourth qualifying purpose. Section 214 provides that property used exclusively for charitable purposes owned and operated by corporations organized and operated for charitable purposes is exempt from taxation if the owner is not organized and operated for profit and the property is used for the actual operation of the exempt activity.

Charitable Purposes. An organization's primary purpose must be either religious, hospital, scientific, or charitable. Whether its operations are for one of these purposes is determined by its activities.

Exclusive Use. The Revenue and Taxation Code does not specifically define the term *used exclusively*; however, the courts have done so in a series of decisions. The California Supreme Court has stated that the phrase "exclusively used" may not be given a literal interpretation so as to mean that the property exempted must be used solely for the purposes stated to the total exclusion of any other use. The Supreme Court held that *used exclusively* for exempt purposes includes any property which is used exclusively for any facility which is incidental to and reasonably necessary for the accomplishment of the exempt purpose.⁶ Courts have applied this precedent to mean that a qualified organization's primary use of its property must be for exempt purposes and any other uses of property must be related to and reasonably necessary to the accomplishment of the exempt purpose.⁷

Housing Welfare Exemption. Property tax administrators have historically taken a narrow view of the exemption and have viewed much housing to be non-exempt on the grounds that the property is being used primarily for private residential purposes rather than exempt purposes and is not being used exclusively for exempt purposes as required by section 214.⁸

However, the courts have taken a broader view, consistent with the Supreme Court's directive that statutory and constitutional provisions granting exemptions are to be construed strictly, but reasonably.⁹

In 1999, the BOE adopted [Property Tax Rule 137](#), *Application of the Welfare Exemption to Property Used For Housing*, effective December 31, 1999.¹⁰ The purpose of Rule 137 is to clarify that the welfare exemption from property taxation applies to housing and related facilities owned and operated by qualified nonprofit organizations and to establish a single uniform statewide standard for determining qualification for the welfare exemption as it applies to such properties.¹¹

In addition, [Property Tax Rule 140](#) further specifies requirements for the welfare exemption for low-income housing properties.

Government Financing or Tax Credits: Unlimited Exemption. When a nonprofit organization owns and operates a low-income rental housing property that receives government financing or low-income

⁶ *Cedars of Lebanon v. County of Los Angeles* (1950) 35 Cal.2d 729, 736.

⁷ *Honeywell Information Systems, Inc. v. County of Sonoma* (1974) 44 Cal.App.3d 23; *YMCA v. County of Los Angeles* (1950) 35 Cal.2d 760; *St. Germain Foundation v. County of Siskiyou* (1963) 212 Cal.App.2d 911; *Greek Theatre Association v. County of Los Angeles* (1978) 76 Cal.App.3d 768.

⁸ Assessors' Handbook Section 267, *Welfare, Church, and Religious Exemptions*, p. 62.

⁹ *Ibid.*

¹⁰ All references to Property Tax "Rule" or "Rules" are to sections of title 18 of the California Code of Regulations.

¹¹ *Id.* at p. 65.

housing tax credits, the amounts that may be exempted from property tax are not capped. Generally, a low-income housing property, including a single-family home, may qualify for the welfare exemption provided:

- **Occupancy.** While there is no minimum percentage of units that must be occupied by lower-income households, the exemption only extends to the proportion of units serving lower-income households. (*§214(g)(1)*).
- **Use Restriction.** The property is subject to a recorded deed restriction, regulatory agreement, or other legal document¹² restricting its use for low-income housing purposes at specified rents. (*§214(g)(2)(A)(i)* and *Property Tax Rule 140*).
- **Rents Charged.** The rents charged to lower income household occupants do not exceed the rent prescribed by the deed restrictions or regulatory agreement. (*§214(g)(1)(A)* and *§214(g)(2)(A)(i)*).
- **Property Tax Savings.** The owner certifies that the funds otherwise spent to pay taxes are instead used to maintain affordability of, or reduce rents of units occupied by, the lower income households. (*§214(g)(2)(B)*).
- **Limited Partnership: Special Requirements.** In the case of housing owned by a limited partnership in which the managing general partner is an eligible nonprofit organization, use and rent restrictions must be contained in an enforceable and verifiable agreement with a public agency or in a recorded deed restriction. An “other legal document” is insufficient. (*§214(g)(2)(A)(ii)*).
- **Government Assistance.** The nonprofit organization owner receives low-income housing tax credits or government financing on the property.¹³ (*§214(g)(1)(A)* and *(B)*).

No Government Assistance: Capped Exemption. When a nonprofit organization owns and operates a low-income rental housing property that does not receive any government financing or low-income housing tax credits, an exemption is available, but these properties are subject to a statewide cap. The exemption is capped at \$20 million in assessed value. If it does not exceed the exemption cap, a particular low-income rental housing property may qualify for the welfare exemption provided:

- **Occupancy.** Ninety percent or more of the property's occupants are lower income households, as specified. With respect to the remaining occupancy, the law allows an exemption equal to the percentage of units serving lower-income households. For example, a 100% exemption would be allowed if all the units were occupied by low-income households. (*§214(g)(1)* and *§214(g)(1)(C)*).
- **Use Restriction.** The property is subject to a recorded deed restriction, regulatory agreement, or other legal document restricting the property's use to low-income housing. (*§214(g)(2)(A)(i)* and *Property Tax Rule 140*).

¹² An “other legal document” is not permissible if a limited partnership owns the property with a managing general partner that is a nonprofit organization. Section 214(g)(2)(A)(ii).

¹³ The exemption continues to apply if the government financing has been refinanced or paid in full or if the allocation of the low-income housing tax credits has terminated or expired, during the period of restricted use and rent levels provided that the government agency that is a party to the regulatory agreement continues to monitor and enforce compliance with the regulatory agreement. Property Tax Rule 140(c).

- **Rents Charged.** The rent charged does not exceed that prescribed in Health and Safety Code section 50053. (*§214(g)(1)(C)*).
- **Property Tax Savings.** The owner certifies that the funds otherwise spent to pay taxes are instead used to maintain the affordability for, or reduce rents of units occupied by, the lower income households. (*§214(g)(2)(B)*).
- **Limited Partnerships: Prohibited.** Limited partnerships with a nonprofit organization serving as a managing general partner are not eligible for any exemption under this provision. (*§214(g)(1)(C)*).

Background: Historical Qualifications. Prior to January 1, 2000, non-profit rental housing owners could generally claim the welfare exemption if one of the following requirements were met:

1. **Occupancy.** At least 20% of the property's occupants were low income.
2. **Government Financing.** The project was financed with tax-exempt bonds, government loans, or grants.
3. **Tax Credits.** The non-profit organization was eligible and received low-income housing tax credits.

More Stringent Qualifications. Beginning January 1, 2000, Assembly Bill 1559 (Stats. 1999, Ch. 927) deleted mere "occupancy" by persons with low income as a qualifying condition for the welfare exemption. Assembly Bill 1559 also imposed higher standards related to restrictive use documentation to substantiate that the property is dedicated to low-income rental housing. Accordingly, any deed restriction must be recorded, or a public agency must be a party to an enforceable and verifiable agreement regarding property use. Furthermore, "other legal documents" no longer sufficed to impose the necessary use restriction.

The Los Angeles Housing Law Project (Project) sponsored Assembly Bill 1559 to address welfare exemption abuse and misuse that permitted the owners of substandard housing properties to obtain a property tax exemption. While investigating various substandard housing properties, this organization discovered that some properties were receiving the exemption under the provision that permits the property to qualify solely on the basis that the rents were low and the residents were low-income households. It was alleged that substandard housing owners were partnering with nonprofit organizations in a limited partnership as a ruse to obtain the welfare exemption or were themselves creating non-profit organizations.

Exemption Cap. Assembly Bill 1559's changes also revoked the exemption from otherwise deserving charitable organizations providing adequate housing because they did not have government financing or tax credits. Consequently, the following year the Legislature reinstated exemption eligibility based on "occupancy" by low-income households with three changes:¹⁴

1. **Exemption Cap.** Set the welfare exemption cap allowed to a taxpayer with respect to a single property or multiple properties for any fiscal year to not exceed \$20,000 of tax.
2. **Occupancy Threshold.** Increased the occupancy threshold to 90%.

¹⁴ AB 659, Ch. 601, Stats. 2000.

3. **Excluded Limited Partnerships.** Limited partnerships in which the managing general partner is an eligible nonprofit corporation were specifically excluded.

In 2016, due in part to the rising cost of housing, the Legislature raised the cap to not exceed \$10 million in assessed value (\$100,000 of tax).¹⁵

In 2018, the Legislature raised the cap again to \$20 million in assessed value (\$200,000 of tax).¹⁶

Commentary:

1. **Removes Cap.** The bill removes the total exemption amount allowed to certain taxpayers that provide low-income housing that is currently statutorily set at \$20 million in assessed value per fiscal year.
2. **Lien Date.** The bill proposes to remove the welfare exemption cap of \$20 million in assessed value per fiscal year and apply the changes to the lien date occurring on and after the effective date of the bill. As a tax levy, the bill would go into immediate effect and apply to the 2023 lien date. This could potentially cause taxpayer confusion as the act would go into effect in the middle of the 2022 lien year, but would not apply until the January 1, 2023, lien date. Does the author intend for the act to go into effect for the January 1, 2023, lien date or apply to the 2022 lien year?
3. **The BOE Monitors the Statewide Cap.** Nonprofit organizations report their holdings to the local County Assessor via the annual welfare exemption claim form, and County Assessors annually transmit the information to the BOE.
4. **\$20,000 of Tax Exemption Cap.** For fiscal year 2016-17, according to information submitted to the BOE, 23 nonprofit organizations received exemptions on property that counted towards the \$20,000 cap. These 23 organizations owned 55 low-income rental housing properties of various types in 10 counties. Three organizations, located in Los Angeles, Marin, and Monterey Counties, exceeded the cap and were partially taxable.
5. **\$10 Million in Assessed Value Exemption Cap.** For fiscal year 2017-18, 18 counties submitted information to the BOE. This information indicates that 23 nonprofit organizations received exemptions on property that counted towards the \$10 million exemption cap. These 23 organizations own low-income rental housing properties of various types in 8 counties. Of these 23 organizations, none of the organizations exceeded the \$10 million cap.
6. **Potentially One Organization Has Exceeded the Current \$20 Million in Assessed Value Exemption Cap.** For fiscal year 2020-21, 19 counties submitted information to the BOE. This information indicates that 14 nonprofit organizations received exemptions on property that counted towards the \$20 million exemption cap. These 14 organizations own low-income rental housing properties of various types in 8 counties. In one county, it appears that one entity may have exceeded the cap; however, it is still being confirmed as to whether the information was reported correctly.
7. **No Other Property Eligible for the Welfare Exemption is Subject to an Exemption Cap.** The cap was instituted to address the exemption's misuse as it applied to low-income rental housing. In

¹⁵ SB 996, Ch. 836, Stats. 2016.

¹⁶ SB 1115, Ch. 694, Stats. 2018.

addition to the cap, other restrictions were enacted to reduce exemption abuse, such as excluding limited partnerships, requiring recorded deed restrictions, and requiring regulatory agreements with a public agency.

Costs: The BOE would incur costs of approximately \$1,734 and 21 personnel hours to update claim forms; Property Tax Rule 140; Assessors' Handbook Section [267](#), *Welfare, Church, and Religious Exemptions*; and [Publication 149](#), *Property Tax Welfare Exemption*.

Revenue Impact: This bill eliminates the current exemption cap of \$20 million in assessed value for non-government assisted low-income rental housing owned and operated by eligible nonprofit organizations.

Based on County Assessor data collected by the BOE Property Tax Department staff, it is unclear whether any organizations have exceeded the \$20 million cap at the present time. Consequently, the current revenue impact is zero.

Qualifying Remarks. The revenue impact to local jurisdictions could grow as organizations acquire more property subject to the \$20 million cap, or if the assessed values over time exceed \$20 million due to the application of the annual inflation factor of up to 2 percent.

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