

[Assembly Bill 2715](#) (Fong)

Date: February 20, 2020 (Introduced)

Program: Property Taxes

Sponsor: Author

Revenue and Taxation Code Section 218

Effective: Upon chaptering

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**Summary:** Increases the property tax homeowners' exemption from \$7,000 to \$14,000 of assessed value and allows an annual inflation adjustment thereafter.

**Fiscal Impact Summary:** Initial estimated revenue loss of \$412 million.

**Existing Law:** The California Constitution<sup>1</sup> exempts from property tax the first \$7,000 of assessed value for owner-occupied principal places of residence, commonly known as the "homeowners' exemption." The Constitution<sup>2</sup> also requires the state to reimburse local government for the property tax revenue loss associated with this exemption.

The Constitution authorizes the Legislature to increase the homeowners' exemption amount if the state:

- reimburses local governments for the revenue loss; and
- increases the benefits provided to renters (i.e., the renters' income tax credit) by a comparable amount.<sup>3</sup>

The implementing statute<sup>4</sup> specifies exemption amounts, eligibility requirements, and filing requirements.

**Proposed Law: Homeowners' Exemption.** Beginning with the January 1, 2021 lien date, this bill increases the homeowners' exemption amount from \$7,000 to \$14,000. Thereafter, beginning with the January 1, 2022 lien date, this bill provides an annual adjustment based on the percentage change in the Federal Housing Finance Agency's published [House Price Index](#) (HPI) for California for the first three quarters of the prior calendar year.<sup>5</sup>

**Renters' Credit.** This bill also revises the personal income tax rates and increases the renters' income tax credit, as specified. This analysis does not address these provisions, since the Franchise Tax Board administers the personal income tax and renters' credit.

**In General: Creation of Homeowners' Exemption.** Prior to Proposition 13's<sup>6</sup> enactment in 1978, property tax reform advocates in the 1960's and 1970's put forth various reform proposals that departed from a market value-based property tax system. At that time, the law required the assessor to

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<sup>1</sup> Article XIII, section [3\(k\)](#).

<sup>2</sup> Article XIII, section [25](#).

<sup>3</sup> Article XIII, section 3(k).

<sup>4</sup> Revenue and Taxation Code (RTC) section [218](#).

<sup>5</sup> The [HPI](#) is a weighted, repeat-sales index. It measures average price changes in recent sales or refinancing on the same properties.

<sup>6</sup> [Article XIII A](#) of the California Constitution

cyclically reassess property to its current market value. These periodic reassessments resulted in substantial property tax increases due to escalating real estate values during that time period. In 1968, voters enacted the homeowners' exemption to provide some property tax relief.<sup>7</sup> Initially, the exemption amount was \$3,000<sup>8</sup> of assessed value. In 1972, legislation increased the exemption amount to its current level of \$7,000, effective in 1974.<sup>9</sup>

Between 1972 and 1978, the Legislature introduced numerous bills to increase the exemption amount. All were rejected. The prevailing view was that continuous increases in the homeowners' exemption would, at best, only provide temporary property tax relief in inflationary times. Thus, those holding this view argued that fundamentally changing the property tax system to contain rapidly increasing property taxes was the better approach. Ultimately, voters adopted Proposition 13.

**Property Tax System Reform.** Voters changed California's property tax system through Proposition 13, which replaced a current market value-based system with an acquisition value-based system. Under the new law, 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 percent, for as long as the property's ownership remained unchanged and the property was not substantially improved (i.e., new construction). Proposition 13 also limited the basic property tax rate to 1 percent, plus voter-approved bonded indebtedness. Previously, the statewide average tax rate was 2.67 percent, as each taxing agency could set and levy its own rate to meet its budgetary needs.

The current system provides certainty to property owners regarding future property tax liability. The 2 percent maximum inflation adjustment ensures only modest assessed value increases, assuming no ownership changes or substantial property improvements.

**Background:** The Legislature and initiative proponents have considered numerous ways to increase the homeowners' property tax exemption, including:

- one-time flat increase for all homeowners,
- increase limited to certain homeowner class (age, disabled, first-time buyer)
- variable exemption amount according to the purchase year, and
- annual inflation adjustment.

The following table summarizes these attempts.

| Bill Number | Legislative Session | Author          | Type                                  |
|-------------|---------------------|-----------------|---------------------------------------|
| AB 1922     | 2017-18             | Fong            | Increase to \$14,000; inflation index |
| AB 1100     | 2017-18             | Chen and Harper | Increase to \$25,000; inflation index |
| AB 476      | 2015-16             | Chang           | Increase to \$25,000; inflation index |

<sup>7</sup> Proposition 1-A; SCA 1 and SB 8, Statutes of 1968.

<sup>8</sup> The actual exemption amount was \$750 of assessed value; however, at that time, property was assessed at 25 percent, rather than 100 percent, of market value. To compare the exemption amounts on the same mathematical basis, the "equivalent" amount of \$3,000 is referenced ( $\$750 \times 4 = \$3,000$ ).

<sup>9</sup> SB 90, Statutes of 1972, provided for a \$1,750 exemption amount. But assessments were set at 25 percent of market value. To compare the exemption amounts on the same mathematical basis, the equivalent amount of \$7,000 is referenced ( $\$1,750 \times 4 = \$7,000$ ).

| Bill Number | Legislative Session             | Author                                      | Type  |
|-------------|---------------------------------|---|---|
| AB 2097     | 2013-14                         | Morrell                                     | Increase to \$20,000; inflation index               |
| SB 1216     | 2013-14                         | Morrell                                     | Increase to \$20,000; inflation index               |
| SB 1430     | 2009-10                         | Walters                                     | Increase to \$27,000 for over 62; inflation index   |
| AB 293      | 2007-08                         | Strickland                                  | Increase to \$22,000; inflation index               |
| AB 351      | 2007-08                         | Symth                                       | Increase to \$27,000 for over 62                    |
| AB 388      | 2007-08                         | Gaines                                      | Increase to \$25,000                                |
| AB 968      | 2007-08                         | Walters                                     | 25% exemption for first time homebuyers             |
| AB 972      | 2007-08                         | Walters                                     | 25% exemption                                       |
| AB 457      | 2007-08                         | Tran  | Increase to \$25,000 for over 62; inflation index   |
| AB 1922     | 2005-06                         | Walters                                     | 25% exemption, no assessed value cap                |
| AB 2738     | 2005-06                         | Wyland                                      | Increase to \$27,000 for over 62                    |
| AB 185      | 2005-06                         | Plescia                                     | Increase to \$15,000 for over 62                    |
| AB 62       | 2005-06                         | Strickland                                  | Increase to 25% for first time homebuyers           |
| AB 2357     | 2003-04                         | Plescia                                     | Increase to \$10,000 for over 62                    |
| AB 211      | 2003-04                         | Maze  | Increase to \$17,000 for over 62, disabled, blind   |
| AB 82       | 2003-04                         | Dutton                                      | Increase to \$32,000, inflation index               |
| Initiative  | Inadequate signatures - 11/6/02 | Howard-Jarvis Taxpayers Assoc. & Bill Simon | Increase to \$32,000, inflation index               |
| AB 1844     | 2001-2002                       | Mountjoy                                    | Increase to \$17,000 for over 62, disabled, blind   |
| SB 48       | 2001-2002                       | McClintock                                  | Inflation index by California CPI                   |
| SB 48       | 2001-2002                       | McClintock                                  | Increase to \$25,000, inflation index               |
| AB 218      | 2000-2001                       | Dutra                                       | Increase for first time homebuyers                  |
| AB 2288     | 1999-2000                       | Dutra                                       | Increase for first time homebuyers                  |
| AB 2158     | 1999-2000                       | Strickland                                  | Increase to \$8,750 for persons over 62             |
| SCA 8       | 1999-2000                       | Johannessen                                 | Increase to \$20,000; delete renters' credit parity |
| AB 2060     | 1997-1998                       | Granlund                                    | Increase to \$20,000                                |
| ACA 43      | 1997-1998                       | Granlund                                    | Increase to \$20,000                                |
| ACA 5       | 1991-1992                       | Elder                                       | Variable, according to assessed value               |
| ACA 31      | 1991-1992                       | Frizzelle                                   | Index for inflation by California CPI               |
| ACA 47      | 1991-1992                       | Jones                                       | 25% exemption; no assessed value cap                |
| ACA 3       | 1989-1990                       | Elder                                       | Variable, depending on year acquired                |
| ACA 9       | 1989-1990                       | D. Brown                                    | 25% exemption; \$250,000 assessed value cap         |
| ACA 31      | 1989-1990                       | Hannigan                                    | 15% exemption; \$150,000 assessed value cap         |
| ACA 55      | 1989-1990                       | Wright                                      | Increase to \$48,000                                |
| ACA 1       | 1987-1988                       | Elder                                       | Increase to \$25,000, inflation index               |
| ACA 25      | 1987-1988                       | D. Brown                                    | 25% exemption; \$250,000 assessed value cap         |
| AB 2141     | 1985-1986                       | Klehs                                       | 20% exemption; \$50,000 exemption cap               |
| AB 2496     | 1985-1986                       | Cortese                                     | Increase in years with General Fund Reserves        |
| AB 3086     | 1985-1986                       | Elder                                       | Variable, depending on year acquired                |
| AB 3982     | 1985-1986                       | La Follette                                 | Increase for first time home buyers                 |
| ACA 49      | 1985-1986                       | Elder                                       | Variable, depending on year acquired                |

**Commentary:**

1. **Author's Statement.** AB 2715 would make California more affordable for middle and working class individuals and businesses. This measure would help offset California's increasing cost of living by doubling the homeowner's property tax exemption, raising the personal income tax renter's credit, eliminating the \$800 franchise tax on small businesses, and lowering the state personal income tax for middle class individuals and families.
2. **The Constitution specifies the minimum exemption amount.** The \$7,000 amount specified in the Constitution is the *minimum* exemption amount. The Constitution provides that the homeowners' exemption can be statutorily increased if the Legislature provides an equivalent increase in the renters' credit and the state reimburses local governments for the property tax revenue loss. This bill provides the required renters' credit increase, while existing law (article XIII, section 25) requires the state to reimburse local governments for the property tax revenue loss.
3. **No local government revenue loss reimbursement?** Section 11 of this bill provides that local governments will not be reimbursed for the revenue loss associated with this bill. This conflicts with the constitutional provision as noted above. (See Footnote 2.) An amendment may be necessary to correct Section 11 of this bill to reference state-mandated costs rather than local government revenue loss reimbursement.
4. **Exemption amount unchanged since Proposition 13's enactment.** First enacted in 1968, the homeowners' exemption has only increased one time (in 1974) to its current level. Despite many attempts, the exemption amount has not changed in more than 40 years. Historically, exemption increase opponents generally have argued that California property tax law provides sufficient property tax relief and protections for homeowners via Proposition 13. Additionally, they cite the negative fiscal impact due to the requirement that the state both (1) reimburse local governments for the revenue loss and (2) provide a comparable increase in benefits to renters via the renters' state income tax credit.
5. **Negative housing price index change adjustment?** There are periods when the change in the housing price index is negative. From 1992 to 1996, and between 2007 and 2011, the California HPI averaged a negative year-to-year percentage change. This bill provides that the assessor is to "adjust" the exemption amount. Thus, it appears that assessors would be required to reduce the exemption amount previously provided when the HPI is negative.
6. **Technical change.** This bill provides an annual adjustment based on the percentage change in the "federal" Housing Finance Agency's published House Price Index (HPI) for California for the first three quarters of the prior calendar year. The author may want to consider capitalizing "federal" as their [website](#) lists the agency as the "Federal Housing Finance Agency."
7. **Rounding exemption amounts.** The proposed annual exemption amount should be rounded to the nearest whole dollar. The bill's language requires rounding the *HPI index change* to the nearest one-thousandth of a percent (language based on the annual CPI adjustment in RTC [section 51](#)). But the *annual exemption amount* should be rounded to the nearest whole dollar since assessed values are rounded to the nearest dollar rather than cents. The following amendment is suggested to address this concern.

(B) Beginning with the lien date for the 2019–20 fiscal year and for each fiscal year thereafter, the assessor shall adjust the exemption amount of the prior fiscal year by the percentage

change, rounded to the nearest one-thousandth of 1 percent, in the House Price Index for California for the first three quarters of the prior calendar year, as determined by the federal Housing Finance Agency. The actual exemption amount each year shall be rounded to the nearest whole dollar (\$1).

8. **Should the BOE announce and post the annual exemption amount to ensure statewide uniformity and avoid duplicate efforts?** This eliminates the need for each county assessor to calculate the adjustment.
9. **The State subvenes homeowners' exemption property tax revenue loss.** The homeowners' exemption is the only property tax exemption for which the state fully reimburses local governments. The state also makes subvention payments to offset property tax reductions for open space and agricultural property that receive preferential assessment treatment under the Williamson Act. These rates are \$1 per acre for non-prime land and \$5 per acre for prime land. However, in recent years Williamson Act subventions have not been fully funded.

**Costs:** Counties administer the homeowners' exemption and would incur costs to modify their systems to reflect a variable homeowners' exemption. The BOE would incur some minor absorbable costs to inform and advise county assessors, the public, and staff of the law changes and address ongoing implementation issues and questions.

**Revenue Impact: Background, Methodology, and Assumptions.** According to the FY 2020-21 California Governor's Budget, the estimated homeowners' property tax relief reimbursement to the counties for FY 2020-21 is \$412 million. Given that this proposal basically doubles the exemption from \$7,000 to \$14,000, staff estimates that the initial estimated revenue loss will be \$412 million.

**Summary.** This bill would initially decrease local revenues by \$412 million, and further adjust annually with the California House Price Index. Staff expects the increase to grow significantly over time due to the compounding effect of the adjustment.

**Qualifying remarks.** While the historical average change in the California House Price Index generally trends upward, the index is also subject to sustained year-to-year decreases. From 1992 to 1996, and between 2007 and 2011, the California HPI averaged a negative year-to-year percentage change.