Summary: Extends the Government Owned Property Exemption to an interest in real property, including a possessory interest, that is used to provide rental housing for government employees. Also clarifies that the Public School Exemption applies to a public school or community college employee’s possessory interest in such housing, whether it is newly constructed or restored, rehabilitated, renovated, or reconstructed.

Fiscal Impact Summary: The revenue impact is indeterminable.

Existing Law: Section 1 of article XIII of the California Constitution provides that all property is taxable unless explicitly exempted. The California Constitution exempts from property taxation property owned by the state or local governments (Government Owned Property Exemption) and property used exclusively for public schools, community colleges, state colleges, and state universities (Public School Exemption).

In certain instances, a property tax assessment may be levied when a person or entity has an exclusive use in publicly owned exempt real property. These uses are commonly referred to as "possessory interests" and are typically found where an individual or entity leases, rents, or uses federal, state, or local government facilities and/or land.

Possessory Interest: Government Employee Housing. The law does not provide a possessory interest exemption for an employee’s interest in government-owned employee housing. Case law has found that a taxable possessory interest may exist based on the facts of each case. As such, Property Tax Rule 28 lists, as an example of commonly encountered taxable possessory interests, "[t]he possession of an employee in housing owned by a public agency, irrespective of whether occupancy of the housing is a condition of employment except when the facility also serves as the employee’s work area to which the employer has full access."

Possessory Interest: Public School and Community College District Employee Housing. The law provides that the Public School Exemption applies to state, county, city, school district, or community college district-owned rental housing for employees of public school districts or community college districts, including a public school or community college employee’s possessory interest in the housing. The Public School Exemption is based on use of the property as of each January 1 lien date.

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1 California Constitution, article XIII, section 3(a) and (b); Revenue and Taxation Code (RTC) section 202(a)(4).
2 Article XIII, section 3(d); RTC section 202(a)(3).
3 RTC section 107.
5 RTC section 202(b)(2).

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.
New Construction. For property that is not specifically exempted, the Constitution limits the assessed value of property upon which the property tax is imposed. Generally, the law establishes a property's assessed value at its market value on the date it changes ownership or is newly constructed (called the base year value). A supplemental assessment is generated when property is reassessed, which is the difference between the old value and the new value, prorated for the remainder of the fiscal year. For property that is newly constructed, generally only the new construction is reassessed; the base year value of the remainder of the property is not affected.

Proposed Law: This bill provides that the Government Owned Property Exemption applies to an interest in real property, including a possessory interest, that is used to provide rental housing for state and local government employees, whether that housing is newly constructed or restored, rehabilitated, renovated, or reconstructed.

In addition, this bill clarifies that the exemption from possessory interest applies to employees of one county, city, or district living in housing owned by another and that the Public School Exemption applies to rental housing, whether that housing is newly constructed or restored, rehabilitated, renovated, or reconstructed.

In General:

Public School Exemption. Property used exclusively for public schools, community colleges, state colleges, and state universities is exempt from property taxation under article XIII, section 3(d), of the California Constitution and RTC section 202(a)(3). The property is exempt from taxation on the basis of its exclusive use for public school purposes. If the property is not owned by the public school, the owner of the property may file a claim for the Lessor's Exemption, or, if the owner of the property does not claim the Lessor's Exemption, the public school may file the Public School Exemption claim.

To apply for the Public School Exemption, a claim form must be filed each year with the assessor of the county where the property is located. To receive the full 100 percent exemption for property owned or leased and used for public school purposes on the January 1 lien date, the claim must be filed by February 15.

Lessor's Exemption. In general, the Lessor's Exemption is available on certain types of leased property, when the exemption of property taxes benefits the lessee institution in the form of rental reduction or a refund. The Lessor's Exemption is available to property that is leased, as of the lien date, January 1, for uses such as:

- Free public libraries and museums
- Leased property used exclusively for public schools, community colleges, state colleges, or state universities, including the University of California
- Leased property used exclusively for education purposes by a nonprofit institution of higher education

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6 Article XIII A, sections 1 and 2.
7 The assessed value is based on 1975 market value for property that has not changed ownership since that date.
8 BOE-268-A, Exemption for Property Used Exclusively by a Public School, or BOE-263, Lessor's Exemption Claim (if the property is leased).
9 RTC sections 254 and 255.
10 RTC section 202.2.
**Possessory Interests.** In certain instances, a property tax assessment may be levied when a person or entity has an exclusive use in publicly owned real property that, with respect to its public owner, is either immune or exempt from property taxation. A taxable possessory interest must be independent, durable, and exclusive, all terms of which are defined by statute and case law.\(^\text{11}\) These uses are commonly referred to as “possessory interests” and are typically found where an individual or entity exclusively leases, rents, or uses federal, state, or local government facilities and/or land. RTC section 107 establishes parameters within which assessors and judicial authorities are to determine the existence of taxable possessory interests. Generally, those determinations are made according to the facts and circumstances in each individual case.

**Government-Owned Employee Housing:** Depending on the facts, federal-employee and state-employee residents of government owned employee housing may owe tax related to their possessory interest. Additionally, the courts have held that an irrigation district employee residing in a single-family residence owned by the district owes tax on the possessory interest.\(^\text{12}\) With respect to military housing, both on-base and off-base, the courts have ruled that military personnel residing in the homes do not have a taxable possessory interest.\(^\text{13}\) Regarding student housing, the courts ruled that the possessory interests of students residing in university family housing are exempt from taxation under article XIII, section 3(d) of the California Constitution.\(^\text{14}\)

**State and Local Governments Report to County Assessor.** RTC section \textit{480.6} requires every state or local governmental entity that is the fee owner of real property in which one or more taxable possessory interests have been created or renewed to provide the County Assessor of the county in which the property is located information identifying the holders of a taxable possessory interest, the property involved, and the terms and conditions of the agreement giving rise to the taxable possessory interests.\(^\text{15}\)

**Public School and Community College District Employee Housing Exemption.** The Teacher Housing Act of 2016\(^\text{16}\) creates a state public policy supporting affordable rental housing on school district-owned land (K-12) restricted to occupancy for teachers and school district employees. Subsequently, RTC section 202 was amended to provide that the Public School Exemption applies to state, county, city, school district, or community college district-owned properties used to provide rental housing for employees of public school districts (K-12) or community college districts, including the public school or community college employee’s possessory interest in the housing.

**New Construction.** For property that is not specifically exempted, property is reassessed to current market value\(^\text{17}\) on the date it changes ownership or is newly constructed (called the base year value). The California Constitution does not define the terms “new construction” or “newly constructed.” RTC section \textit{70} defines these terms to mean:

- Any addition to real property, whether land or improvements (including fixtures), since the last lien date.

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\(^{11}\) RTC section 107; Property Tax Rule 70.
\(^{13}\) \textit{United States v. Humboldt County} (1980) 628 F.2d 549.
\(^{14}\) \textit{Mann v. County of Alameda} (1978) 85 Cal.App.3d 505.
\(^{15}\) BOE-502-P, Possessory Interests Annual Usage Report.
\(^{17}\) The assessed value is based on 1975 market value for property that has not changed ownership since that date.
• Any alteration of land or any improvements (including fixtures) since the last lien date that constitutes a “major rehabilitation\textsuperscript{18}” or that converts the property to a different use.

As with all other newly constructed real property, the assessment of new construction associated with a taxable possessory interest is governed by these provisions. This includes new construction that is directly related to the exercise of the rights held under the subject taxable possessory interest.

**Background:** Assembly Bill 1157 (Stats. 2018, ch. 717), which amended section 202 to provide that the Public School Exemption includes the public school or community college employee’s possessory interest in the housing, also proposed to extend the Government Owned Property Exemption to possessory interests for employees of the state, a county, a city, a school district, a community college district. However, these provisions were amended out.

**Section 11 Property.** Article XIII, section 11, of the California Constitution generally provides that real property owned by a local government is taxable if the property is located outside its boundaries and was taxable when acquired. Section 11 specifically prescribes a method for the valuation of taxable government-owned lands (known as “section 11 property”). In addition to the value standard established by the express language of section 11, the California Supreme Court held\textsuperscript{19} that the value limitation standard of article XIII A of the California Constitution (Proposition 13) also applies to taxable government-owned lands in counties other than Inyo and Mono.\textsuperscript{20}

**Commentary:**

1. **Author’s comment.** As Californians struggle with extremely high housing costs, many individuals that work for public agencies are unable to live in the communities that they serve. AB 2852 would exempt all city, county, state and special district employees from possessory interest tax when living in workforce rental housing provided by a school district, community college district, city, county, or state, whether owned by one public entity or a combination of public entities. AB 2825 clarifies that local agencies may collaborate in their efforts to provide housing for their employees.

2. **Applies to state and local government-owned property, not federal property.** This bill provides that the Government Owned Property Exemption applies to an interest in real property, including a possessory interest, that is used to provide rental housing for state and local government employees. Federal-employee residents of government-owned employee housing may owe tax related to their possessory interest.

3. **Jurisdictional boundaries of county-owned property.** RTC section 202(a) specifically excepts section 11 property (taxable property located outside a government entity’s boundaries) from the Public School Exemption or Government Owned Property Exemption. This bill would not affect section 11 assessments.

4. **Exemption applies to employees of other agencies.** This bill provides that the Government Owned Property Exemption applies to government-owned rental housing for employees of any state or local government entity, and is not limited to the government entity’s own employees.

\textsuperscript{18} A major rehabilitation is any rehabilitation, renovation, or modernization that converts an improvement or fixture to the substantial equivalent of a new improvement or fixture.

\textsuperscript{19} City and County of San Francisco v. County of San Mateo et al. (1995) 10 Cal.4th 554.

\textsuperscript{20} See Letter To Assessors No. 2000/037 for further information on the assessment of section 11 property.
5. **Exemption applies to new construction.** Once an interest or a possessory interest in housing owned by a school district and rented by an employee is exempted under the Public School Exemption, this bill clarifies that any subsequent new construction would also be exempt. Similarly, once an interest or a possessory interest in government-owned rental housing is exempt under the Government Owned Property Exemption, any subsequent new construction would also be exempt.

6. **Creation of Possessory Interest.** While real property owned by government within its boundaries is exempt upon acquisition, the Public School Exemption applies as of the lien date. Would either exemption also cover the supplemental assessment generated for the creation of a possessory interest for the portion of the fiscal year remaining after the creation of the possessory interest?

**Costs:** The BOE would incur absorbable costs to update forms; property tax rules; and Assessors' Handbook Section 510, *Assessment of Taxable Possessory Interests.*

**Revenue Impact:** This bill’s revenue impact depends on how many possessory interests will qualify for the Government Owned Property Exemption and the assessed value of each of those properties. However, the assessed value of any property is variable and depends on the facts of each property on a case by-case basis. It is unknown how many residential housing properties are owned by state and local government agencies. It is also unknown how many of those housing properties are rented to government employees. The BOE does not have this data available; thus, the revenue impact is indeterminable.