State of California

Board of Equalization
Property Tax Department – MIC:63
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M e m o r a n d u m

To: Ms. Yvette M. Stowers

Date: August 12, 2024

From: David Yeung, Deputy Director
Property Tax Department, MIC:63

Subject: **Property Tax Relief Provisions for Properties Negatively Impacted by Special Circumstances**

At the May 29, 2024, Board Meeting, the issue of providing property tax relief to homeowners when sexually violent predators are released into a neighborhood was agendized for discussion. While no action was taken, the issue was brought back and expanded at the June 25, 2024, Board Meeting, where the Board instructed the Executive Director to review the current laws that may provide tax relief and to review the Board's guidance on the impact of special circumstances on property values. The following report will discuss the current programs available for providing property tax relief for properties experiencing a decline in value, our current guidance on the methodology to value such property, and potential remedies and limitations available when there is a special circumstance such as a sexually violent predator moving into a neighborhood. An appendix listing the guidance and resources is attached to this report.

Currently Available Relief

Proposition 8 – Decline in Value

In November 1978, California voters passed Proposition 8, which amended Article XIII A to allow temporary reductions in assessed value in cases where real property suffers a decline in value for any reason. Proposition 8 is codified by section 51(a)(2) of the Revenue and Taxation Code (RTC).

Under the state's current property tax system, pursuant to Article XIII A (commonly referred to as Proposition 13), a property's base year value is the market value of real property as established in 1975 or when the property last changed ownership or underwent new construction. The base year value is adjusted annually by the lower of the percentage change in the California Consumer Price Index, or 2 percent. The adjusted base year value is also known as the factored base year value.

A decline in value occurs in any year in which the current market value of real property is less than its factored base year value as of the January 1 lien date. All factors causing a decline in value, including physical, functional, and economic depreciation, are considered.

The market value of real property may decline from one lien date to the next lien date; however, the property will not benefit from a lower assessment unless its market value falls below its current factored base year value.

When the market value of a property on the January 1 lien date falls below its factored base year value, the County Assessor will review the property's assessment and enroll the lesser of the factored base year value or market value.

Once a property's assessment has been reduced under Proposition 8, the County Assessor reviews the assessment annually to determine whether it should remain in decline in value status. The assessed value of a property in decline in value status may be increased each lien date by more than the standard two percent maximum allowed for properties assessed under Proposition 13; however, unless there is a change in ownership or new construction, a property's assessed value can never increase above its existing factored base year value. These concepts are illustrated by the example below.

Example

On January 1, 2020, property A has a factored base year value of $800,000. On January 1, 2021, the market has suffered decline in demand and property A has a fair market value of $700,000. The assessment for fiscal year 2021-2022 will be reduced to $700,000. On January 1, 2022, the fair market value of property A has increased to $750,000, and accordingly will be assessed at that amount. Finally, on January 1, 2023, the market has recovered, and the property has a fair market value of $900,000. The base year value factored to 2023, based upon the 2020 factored base year value, is $840,943 ($800,000 x 1.01036 x 1.02 x 1.02 =$840,943) which is now lower than the fair market value. Thus, the property is assessed at the factored base year value of $840,943, and not at its $900,000 fair market value.

Disaster Relief

A temporary reduction in assessed value may also be granted under disaster relief provisions. Existing law allows a reduction in the assessed value when property is damaged by a disaster. In addition, the property owner can either exclude the new construction from reassessment when rebuilding such damaged property, or transfer the factored base year value of the damaged property to a replacement property.

Reduction in Assessed Value

- RTC section 170 provides that if a calamity such as fire, earthquake, or flooding damages or destroys property, the property owner may be eligible for property tax relief in the form of a reduced assessment if the county has adopted an ordinance allowing such reduction and if the property was damaged or destroyed property without fault from the owner. In such cases, the County Assessor will reappraise the property to reflect its damaged condition. In addition, when it is rebuilt in a like or similar manner, the property will retain its prior value (Proposition 13) for tax purposes as provided by RTC section 70. All California counties have adopted an ordinance for disaster relief.
- To qualify for property tax relief, the owner must file a claim with the County Assessor within the time specified in that county's ordinance, or 12 months from the date of damage or destruction, whichever is later. The loss estimate must be at least $10,000 of current market value to qualify the property for this relief. The property will be reassessed according to its damaged state, and property taxes will be adjusted accordingly.
- This property tax relief is available to owners of real property, business equipment and fixtures, orchards, or other agricultural groves, and to owners of aircraft, boats, and certain manufactured homes – it is not available to property that is not assessable, such as state licensed manufactured homes or household furnishings.

Example

Property B has a factored base year value of $250,000. In July 2022, the property sustained damage from a wildfire that caused $200,000 of damage. The fair market value of the property immediately before the damage was $800,000. The property is entitled to proportional reduction in its assessed value and will have its assessed value reduced to $187,500. ($200,000/$800,000) x $250,000 = $62,500. $250,000 - $62,500 = $187,500. When the property is rebuilt substantially back to its original equivalent, the factored base year value is restored.

Factored Base Year Value Transfers

If the property owner does not elect to rebuild and the Governor has proclaimed a state of emergency, three different base year value transfer options exist. Each of these provisions was enacted by Constitutional amendment and implemented by statute.

- On June 3, 1986, the voters of California approved Proposition 50, adding subdivisions (e) and (f) to section 2 of article XIII A of the California Constitution to allow the transfer of the base year value of real property that is substantially damaged or destroyed by a disaster for which the Governor proclaims a state of emergency to comparable replacement property located within the same county. These provisions are implemented by RTC section 69.

- On November 2, 1993, California voters approved Proposition 171, which amended section 2(e) of article XIII A, to allow the base year value of a principal residence substantially damaged or destroyed in a disaster for which the Governor proclaims a state of emergency to be transferred to a replacement principal residence located in another county, provided that the replacement residence is located in a county that has adopted an ordinance to accept such base year value transfers. These provisions are implemented by RTC section 69.3.

- On November 3, 2020, California voters approved Proposition 19, which added section 2.1 to article XIII A, to allow, as relevant here, an owner of a primary residence who is a victim of a wildfire or natural disaster to transfer the taxable value of their original primary residence to a replacement primary residence that is purchased or newly constructed as that person's principal residence within two years of the sale of the original primary residence. Proposition 19 became operative as of April 1, 2021. These provisions are implemented by RTC section 69.6.

Example

Using property B from the previous example, the owner decides not to rebuild but instead purchases a replacement property for $800,000. The factored base year is transferred, and the replacement will be assessed at $250,000.

Contaminated Property

Base Year Value Transfer – Qualified Contaminated Property (RTC section 69.4)

Similar to disaster relief, there are also provisions in law to provide relief to owners whose property has become contaminated. RTC section 74.7 provides that *new construction* does not include the repair or replacement of a substantially damaged or destroyed structure on qualified contaminated real property where the remediation of the environmental problems required the destruction of, or resulted in substantial damage to, a structure located on that property. The repaired or replacement structure must be similar in size, utility, and function to the original structure.

For owners who choose not to rebuild or remediate their qualified contaminated property, RTC section 69.4 allows the owner to sell or transfer that property, purchase or newly construct a replacement property, and transfer the factored base year value to the replacement property if certain requirements are met.

One of the requirements is that upon the sale or transfer of the qualified contaminated property, the qualified contaminated property must be reassessed to current market value. RTC section 69.4(c) specifies that upon the sale or transfer, the qualified contaminated property must be subject to a change in ownership that results in either of the following:

- A reappraisal at its current fair market value; or
- Receipt of a base year value transferred from another property under the provisions of RTC section 69 (intracounty disaster relief base year value transfer), RTC section 69.3 (intercounty disaster relief base year value transfer), or RTC sections 69.5 and 69.6 (principal residence base year value transfer).

In addition, RTC section 69.4(d) specifies that this property tax relief is not available if the owner of the qualified contaminated property either (1) rebuilds and receives the new construction exclusion for qualified contaminated property under RTC section 74.7, or (2) signs a parent-child exclusion claim under RTC sections 63.1 and 63.2, allowing the base year value to stay with the qualified contaminated property. Simply stated, the property owners may rebuild without reassessment or transfer the Proposition 13 factored base year value, but not both.

Guidance

The Board has issued extensive guidance on Proposition 8 decline in value, disaster relief, and relief for contaminated properties. As examples, the Board has promulgated property rules under Title 18 of the California Code of Regulations, issued Assessors' Handbook sections and advisory Letters To Assessors, annotated rulings of Counsel, and developed Frequently Asked Questions. Since the body of guidance is substantial, an appendix listing the guidance is attached to this report. As well, the following is a discussion summarizing the guidance on Proposition 8 but is applicable to each form of property tax relief.

As discussed earlier, decline in value pursuant to Proposition 8 can provide temporary relief. The County Assessor reviews the property value as of the lien date, January 1, and if the fair market value is lower than the factored base year value, the lower value is enrolled. Once under Proposition 8, the assessment is reviewed annually until the fair market value exceeds the factored base year value at which time the factored base year value is restored as the assessed value.

When reviewing property for a potential Proposition 8 decline in value, all circumstances that may affect value, including the presence of predators, are to be taken into consideration. Pursuant to Property Tax Rule 3, the comparative sales, cost and income approaches to value are all valid methods to value property; however, the most reliable approach will depend on what data is available. When reliable sales data is available, the preferred method is the comparative sales approach. Under this approach, the County Assessor would review the recent sales of comparable properties and make adjustments to their sale prices to estimate the market value of the subject property.

The income approach can also be utilized to estimate the value of taxable property. According to Property Tax Rule 8, the income approach is applicable when the property is typically purchased for an anticipated income stream. The income stream net of expenses is capitalized to determine its net present worth.

The cost approach to value can also be used to estimate fair market value. However, since this approach depends on estimating the cost of replacing taxable property with external obsolescence due to adverse circumstances, care must be exercised when quantifying the decline in value.

The primary consideration when using any of the approaches to estimate the value of property that has suffered a decline in value due to special and adverse circumstances is the use of sales that are subject to the same adverse circumstances as the subject property and to also use the net income attributable to similarly affected properties. The use of comparable sales and income data derived from property subject to the same or similar circumstances is widely accepted.

<u>Summary</u>

Under Proposition 8, relief can only be granted if the fair market value is lower than the factored base year value. Relief can also be granted only on the January 1 lien date and restored to the factored base year value on the lien date. Assessors have a long history implementing Proposition 8 relief and are familiar with valuation methodologies. Proposition 8 is available to all property owners under current law that qualify.

With disaster relief, property tax relief can be given without requiring the fair market value to be lower than the factored base year value. The County Assessor is tasked with determining the fair market value before and after the disaster and relief is granted as a proportional reduction in the factored base year value to the affected properties. While Proposition 8 can be considered when a sexually violent predator moves into a neighborhood, disaster relief is not an option since the criteria for physical damage is not met. To use disaster relief or a similar proportional model of relief, there would have to be a legislative change.

Finally, with contaminated property, tax relief is limited to the ability to transfer the base year value to a replacement property or to remediate the property without reassessment. Proportional reduction in the base year value similar to disaster relief is not available, however, Proposition 8 is available if the fair market value is less than the factored base year value. Contaminated property relief would be difficult to grant to property that has had a predator move into the area as there is a requirement to have the state or federal government designate the area as a toxic or environmental hazard.

APPENDIX

DECLINE IN VALUE RESOURCES

Law

- California Constitution article XIII A, section 2(b)
- Revenue and Taxation Code section 51

Property Tax Rules

- Rule 461 (e), *Real Property Value Changes*
- Rule 474 (d), *Petroleum Refining Properties*

Assessors' Handbook

- Section 401, *Change in Ownership*: Chapter 1
- Section 410, *Assessment of Newly Constructed Property*: Chapter 3
- Section 501, *Basic Appraisal*: Chapter 8, Appendix A
- Section 502, *Advanced Appraisal*: Chapters 1, 2, 6
- Section 511, *Assessment of Manufactured Homes and Parks*: Chapter 3
- Section 521, *Assessment of Agricultural and Open-Space Properties*: Part II
- Section 560, *Assessment of Mining Properties*: Chapter 8

Guidelines

- Assessment Appeals Manual: Chapter 6

Letters To Assessors

- Annual Increases in Value … 2004/060
- Errors in Assessed Values … 2009/038
- First Lien Date … 86/36
- Floating Homes … 2011/051
- Fractional Interests … 86/04
- Informal Assessment Review … 96/52
- Machinery and Equipment … 79/143
- Manufactured Homes … 2011/051
- New Construction Exclusion … 2009/024
- Notice … 93/71
- Proposition 8 … 80/129, 81/19, 82/25, 92/24, 92/63, 93/71, 96/52, 2004/060, 2011/051
- Questions and Answers … 79/39
- Roll Corrections … 95/54, 2009/038

Annotations

- Assessment, Stagnant or Declining Values 170.0090
- Value, Decline in Value (First Lien Date): 850.0015
- Value, Decline in Value (Appraisal Unit): 850.0016, 850.0017
- Value, Decline in Value (Assessor's Duty): 850.0018
- Value, Decline in Value (Recognizable Income Impairments): 850.0019
- Value, Decline in Value (Usable Value Approaches): 850.0020
- Value, Lesser of Market Value or Factored Value: 850.0031

- Value, Notice: 850.0045
- Value, Taxable Value Less than Trended Base Year Value: 850.0080

BOE Website (www.boe.ca.gov/proptaxes/decline-in-value)

- Description
- How it works
- FAQs

DISASTER RELIEF RESOURCES

Law

- California Constitution article XIII, section 15
- Revenue and Taxation Code sections 51, 69, 69.3, 69.6, 70(c), 70.5, 170, 172, 172.1, 194, 194.1

Property Tax Rule 461(e), *Real Property Value Changes*

Assessors' Handbook

- Section 401, *Change in Ownership*: Chapters 14 and 16
- Section 410, *Assessment of Newly Constructed Property*: Chapters 5 and 6
- Section 501, *Basic Appraisal*: Appendix A
- Section 510, *Assessment of Taxable Possessory Interests*: Chapter 4
- Section 511, *Assessment of Manufactured Homes and Parks*: Chapter 2
- Section 542, *Assessment of Water Companies and Water Rights*: Part II, Chapter 3
- Section 560, *Assessment of Mining Properties*: Chapter 9
- Section 566, *Assessment of Petroleum Properties*: Chapter 6
- Section 576, Assessment of Vessels: Chapters 3 and Chapter 4

Guidelines

- Assessment Appeals Manual: Chapter 6
- Guidelines for Active Solar Energy Systems New Construction Exclusion

Letters To Assessors

- Application of New Construction Exclusion … 79/39, 79/207, 81/123, 82/12, 82/49
- Assessment Appeal Filing Deadline Extension … 2001/063, 2002/040
- Base Year Value Transfer (Propositions 50 and 171) … 87/23, 92/45, 94/49, 95/16, 97/58, 2006/052, 2010/010, 2012/012, 2021/026
- Base Year Value Transfer (Proposition 19) … 2020/061, 2021/019, 2021/026, 2021/063
- Comparability Standards … 87/23, 92/45, 2012/012
- Disabled Persons (Proposition 110) … 2002/016, 2006/010
- Disabled Veterans' Exemption … 2008/082
- Fault … 96/59
- Filing Deadline Extension … 2001/077
- Fire Prevention Fee … 2014/071
- Frost Damage … 91/13, 92/09, 99/52, 2007/057
- Homeowners' Exemption … 2004/069, 2005/073, 2006/049, 2007/051, 2008/063, 2009/053, 2011/004
- Ineligibility Notification … 2019/002

- Intercounty Transfer of Base Year Value (Proposition 171) … 94/49, 95/16, 2012/012
- Intracounty Transfer of Base Year value (Proposition 50) … 87/23, 92/45, 94/49, 95/16, 97/58, 2006/052, 2010/010, 2012/012, 2021/026, 2024/003
- Manufactured Homes … 82/139, 88/72, 99/87
- New Construction Exclusion … 79/39, 79/207, 81/123, 82/12, 82/49, 2021/004
- New Construction Exclusion – Governor-Proclaimed Disasters … 2021/004, 2024/003
- Northridge Earthquake, Extension of Time Limits … 97/58
- Notice … 2019/002
- Ordinances for Intercounty Transfers … 2021/017
- Persons Over Age 55 (Propositions 60/90) … 2002/016, 2006/010
- Property Tax Deferral … 86/33, 87/98
- Proposition 50 (Intracounty Transfers) … 87/23, 92/45, 2006/052, 2012/012
- Proposition 171 (Intercounty Transfers) … 94/49, 95/16, 2012/012, 2018/026, 2020/018
- Removal of Property … 86/09
- Repair, Restoration, or Reconstruction … 95/31
- Replacement Property … 87/23, 94/49, 97/58, 2006/052
- Restricted Access … 2001/102
- September 11 Events … 2001/063, 2001/077, 2001/102, 2002/009, 2002/037, 2006/031
- Substantially Damaged or Destroyed … 2012/012
- Supplemental Assessments … 83/128, 85/75, 86/09, 95/31
- Trees and Vines … 91/13, 92/09, 99/52, 2007/057, 2008/084

Annotations

- Base Year Value Transfer, Disaster Relief: 200.0402 – 200.0450
- Disaster Relief: 360.0001 – 360.0050
- Golf Courses: 480.0025
- Homeowners' Exemption: 505.0019
- Mobilehome: 600.0015
- Newly Constructed Property: 610.0034
- Parent-Child Transfer: 625.0059

BOE website: www.boe.ca.gov/proptaxes/disaster-relief.htm

FAQs: www.boe.ca.gov/proptaxes/disaster-relief.htm#FAQs

CONTAMINATED PROPERTY RESOURCES

Law

- California Constitution Article XIII A, section (i)
- Revenue and Taxation Code sections 69.4 and 74.7

Assessors' Handbook

- Section 410, *Assessment of Newly Constructed Property*: Chapter 6 (pages 75-77)
- Section 501, *Basic Appraisal*: Chapter 4 (page 43), Footnote 57 (page 52)

- Section 502, Advanced Appraisal: Chapter 3 (page 43)

Letters To Assessors

- Base Year Value Transfers … 99/23, 2000/012, 2007/047, 2023/046, 2023/052
- Fair Market Value … 2000/056
- New Construction Exclusion … 2003/078, 2007/047

Annotations

- Assessment Appeals, Transfer of Base Year Value: 180.0120
- Base Year Value Transfer, Contaminated Property: 200.0520 – 200.0580
- Corrections, Nonjudgmental Error: 285.0060
- Newly Constructed Property: 610.0013

BOE Website

- New Construction: New Construction (ca.gov) (list of new construction exclusions)