

Issue Paper Number 00-017



- Board Meeting
- Business Taxes Committee
- Customer Services and Administrative Efficiency Committee
- Legislative Committee
- Property Tax Committee
- Other

Guidelines for the Assessment of Taxable Government-Owned Properties

I. Issue

1. Should the proposed Guidelines for the Assessment of Taxable Government-Owned Properties advise that the value limitations prescribed by article XIII, section 11 (Phillips Factor value), is applicable to properties acquired after March 1, 1975?
2. Should the Guidelines advise that for properties acquired after March 1, 1975, base year values are determined in the same manner as for privately owned, locally assessed real property?
3. Should the Guidelines advise that taxable government-owned properties are subject to supplemental assessments?

II. Staff Recommendation

Staff recommends that the Guidelines advise that (1) Phillips Factor values are applicable to taxable government-owned properties acquired after March 1, 1975, (2) base year values for Section 11 properties acquired after March 1, 1975 are to be determined in the same manner as for privately owned, locally assessed real property, and (3) taxable government-owned properties are subject to supplemental assessment.

III. Other Alternative(s) Considered

The Board could specify that (1) the value limitations prescribed by section 11 do not apply to properties acquired after March 1, 1975, (2) the base year value for taxable government-owned property acquired after March 1, 1975 is the lower of current market value as of the date of acquisition or the 1967 assessed value times the appropriate Phillips Factor as of the date of acquisition, and (3) taxable government-owned properties are not subject to supplemental assessments.

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IV. Background

Article XIII, section 11, of the California Constitution generally provides that real property owned by a local government that is located outside its boundaries is taxable if it was taxable when acquired and specifically prescribes a method for the valuation of taxable government-owned lands. Section 11 prescribes a valuation standard requiring assessment of such taxable lands at the lower of current fair market value or a value based on the 1966 assessed value for lands located in Inyo County and the 1967 assessed value of the land in all other counties. The restricted value prescribed by section 11 (Phillips Factor value) is determined by multiplying the 1966 assessed value of the land in Inyo County and the 1967 assessed value of the land in all other counties by the Phillips Factor (a Constitutionally provided formula).

On June 6, 1978, the voters passed Proposition 13, which added article XIII A to the California Constitution, imposing a valuation standard limitation on real property for property tax assessment purposes. Subsequently, in 1979, an Assembly Revenue and Taxation Committee Task Force on Property Tax Administration studied the effects of Proposition 13 and concluded that Proposition 13 did not repeal section 11. The Task Force issued a recommendation that resulted in the addition of section 52 of the Revenue and Taxation Code. Subdivision (d) of section 52 provides that property assessed pursuant to section 11, would continue to be assessed pursuant to that section.

In addition to the value standard established by the express language of section 11, the California Supreme Court in *City and County of San Francisco v. County of San Mateo et al.* (1995) 10 Cal.4th 554 held that article XIII A (Proposition 13) did not repeal section 11 and that both apply to extraterritorial government owned land in counties other than Inyo and Mono. Thus, the court concluded that the value standard applicable to Section 11 assessments in counties other than Inyo and Mono is the lowest of (1) the current fair market value, (2) the factored base year value (Prop. 13 value), or (3) the 1967 assessed value times the appropriate Phillips Factor.

It is the combined interpretation and implementation of article XIII, section 11, and article XIII A that has generated controversy and necessitated the creation of these guidelines. Property Taxes Department and Legal Division staff drafted proposed Guidelines for the Assessment of Taxable Government-Owned Properties to provide advisory guidance in the assessment of these properties. Board staff received input from assessors, local government, and industry.

On April 10, 2000, staff held a meeting in Sacramento with interested parties to listen to comments, suggestions, and interpretive opinions regarding the combined application of article XIII, section 11, and article XIII A as it applies to properties subject to section 11. Interested parties were unable to reach agreement or consensus on three issues at the meeting.

Accordingly, the Board is asked to decide three issues that will determine the direction of the Guidelines for the Assessment of Taxable Government-Owned Properties. Following the Board's adoption of the Committee's recommendation, staff will finalize the guidelines and distribute them through a Letter to Assessors.

V. Staff Recommendation 1

Continue to apply the valuation method prescribed by section 11, article XIII, to all taxable lands acquired by local governments before and after March 1, 1975.

A. Description of the Staff Recommendation

Staff recommends that the Guidelines advise that the valuation limitation provision of section 11, subdivision (b) of article XIII, applicable to taxable local government-owned lands located outside Mono and Inyo counties, applies to all such taxable lands including those acquired by a local government after March 1, 1975. Section 11, subdivision (b), provides generally that taxable property owned by a local government and located outside Mono and Inyo counties is assessed at the lower of fair market value or a value based on the 1967 assessed value (Phillips Factor value). The Court in *City and County of San Francisco v. County of San Mateo* held that the valuation limitations of article XIII A also apply to taxable lands owned by the City and County of San Francisco that are located in the counties of San Mateo and Alameda, and that the application of article XIII A's valuation limitations to San Francisco's lands does not conflict with section 11 of article XIII. The lands in issue had been acquired by the City and County of San Francisco prior to March 1, 1975. However, the Court held that taxable local government-owned land is to be assessed at the lowest of the three values: fair market value, Phillips Factor value or the article XIII A value (factored base year value). The Court did not limit this three-part test to properties acquired before March 1, 1975.

B. Pros of the Staff Recommendation

Staff's recommendation is consistent with the findings of the Assembly Revenue and Taxation Committee Task Force Report and the holding in *City and County of San Francisco v. County of San Mateo*.

In 1979, an Assembly Revenue and Taxation Committee Task Force prepared the Report of the Task Force on Property Tax Administration, dated January 22, 1979 (Report), in which the Task Force advised that article XIII A (Proposition 13) did not repeal section 11 and recommended that property assessed pursuant to section 11 continue to be assessed pursuant to that section (Report at p.33). In response to this recommendation, the Legislature adopted section 52, subdivision (d), of the Revenue and Taxation Code, which provides that property subject to valuation pursuant to section 11 shall be valued in accordance with that section. The recommendation and statutory provision make no distinction between property acquired prior to March 1, 1975 and property acquired after that date.

The Supreme Court in *City and County of San Francisco v. County of San Mateo et al.* (1995) 10 Cal.4th 554 held that article XIII A (Proposition 13) did not repeal section 11 and that both apply to extraterritorial government-owned land in counties other than Inyo and Mono. The Court did not hold that property acquired after March 1, 1975 was subject to different treatment than property acquired prior to that date. Thus, the value standard applicable to Section 11 lands for property tax assessment purposes regardless of acquisition date is the lowest of either (1) the current fair market value, (2) the factored base year value, or (3) the 1967 assessed value multiplied by the appropriate Phillips Factor.

C. Cons of the Staff Recommendation

The Court in *City and County of San Francisco v. County of San Mateo* did not examine whether or not article XIII A and section 11 could be harmonized in the context of real property that has changed ownership and has become subject to valuation and taxation under section 11 after 1975. The Court harmonized those provisions only insofar as they both apply to property that was subject to valuation under section 11 when article XIII A became law. Consequently, those constitutional provisions, read together, must exclude the use of a fictitious pre-1975 section 11 value where none has heretofore existed, because the property did not become subject to section 11 until after the enactment of article XIII A.

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The purpose of the 1914 amendment to the Constitution that first provided for taxation of extraterritorial local government-owned lands was to protect the property tax base revenue of smaller counties in which large cities had purchased extensive holdings which would otherwise be exempt from local taxation by those counties. In response to allegations that extraterritorial lands were unfairly overvalued by the assessing county, section 11 was amended in 1968 to add a value limitation to ensure that land owned by local governments would be assessed comparably to privately owned land, both from the perspective of the local government that owned the land and of the county in whose taxing jurisdiction the land was located. As a result of the decision in *City and County of San Francisco v. County of San Mateo*, the purpose of the 1968 amendment -- to assure that land owned by a local government not be assessed at a value higher than if owned by a private party -- is protected by application of article XIII A's change of ownership provision.

However, if the value limitations of both section 11 and article XIII A are applied to lands acquired after March 1, 1975, an unforeseen result occurs that is not consistent with the principles of the 1914 and 1968 amendments. The value yielded by the Phillips Factor formula may be substantially lower than either the fair market value or the factored base year value. Therefore, the continued application of the value limitation prescribed by section 11 to such post-1975 acquired extraterritorial land subverts the intent of the 1914 amendment to protect the tax base of the taxing county.

D. Statutory or Regulatory Change

None

E. Administrative Impact

None

F. Fiscal Impact**1. Cost Impact**

None

2. Revenue Impact

None

G. Taxpayer/Customer Impact

None

H. Critical Time Frames

No critical time frame for this issue.

VI. Alternative 1 (For Staff Recommendation 1)**A. Description of the Alternative**

Direct assessors not to apply the value limitation prescribed by section 11, for properties acquired after March 1, 1975. This alternative was proposed by Amador County.

B. Pros of the Alternative

The alternative position effectuates the intent of the 1914 and the 1968 amendments to the California Constitution relating to the taxability of extraterritorial property by applying the value limitation provisions of article XIII A, and not applying the value limitation provisions of section 11, to extraterritorial lands acquired after March 1, 1975. As a result of the holding in *City and County of San Francisco v. County of San Mateo*, the alternative position assumes that for extraterritorial property acquired after 1975, article XIII A renders inapplicable the value limitations of section 11.

The purpose of the 1914 amendment to the Constitution that first provided for taxation of extraterritorial lands has been set forth in numerous cases. The object of the 1914 amendment was to safeguard the tax revenue of smaller counties where large cities had purchased extensive holdings, which would otherwise be exempt from local taxation. If such holdings were exempt from taxation "...impending disaster would result to smaller counties by the removal from the local tax rolls of lands and water rights acquired by [the large cities]." By adopting the 1914 amendment, the voters expressed their intent that the acquisition of such lands and water rights was meant to be "without prejudice to the outlying counties whose existence from an economic and governmental standpoint depended upon the tax revenues derived" from such holdings. *San Francisco v. County of Alameda* (1936) 5 Cal. 2d 243.

The intent was that such holdings should be taxed by the taxing counties at fair market value. By 1968, however, the voters were faced with an entirely different problem. In a number of cases, the extraterritorial lands were difficult to value because of their uniqueness and the lack of transactions involving comparable land in the open market. The large cities had come to believe that the taxing counties were overvaluing that land in order to exploit a distant deep-pocket taxpayer which had no vote in the county and which, because of the uniqueness of its land, was unlikely to sell its land and relocate. The purpose of the 1968 amendment, therefore, was to ensure that land owned by local governments and located outside their boundaries would be taxed comparably to privately owned land, both from the perspective of the local government that owned the land and from the perspective of the local government in whose taxing jurisdiction the land was located. As the ballot argument stated, "This measure will assure continuance of an adequate tax base related to these lands. It will also assure public agencies owning the property that their citizens will not bear more than an equitable share of taxes levied in the taxing counties."

The San Francisco Court held that article XIII A applied to Section 11 property, but it did not have the opportunity to examine the effect of this holding on property that was owned privately and did not become Section 11 property until its transfer to a local-government entity after 1975. The alternative position assumes that, having applied article XIII A's valuation and taxation limitations to extraterritorial properties, the Court would also apply Proposition 13's "catch-up" provisions allowing establishment of a new base year value upon change of ownership.

C. Cons of the Alternative

The alternative would violate the constitution by failing to apply the value limitation standard prescribed by section 11. The plain language of section 11 does not indicate in any manner that the value limitation provision under discussion is applicable only to lands acquired before March 1, 1975. Indeed, section 52, subdivision (d), was added to the Revenue and Taxation Code after the adoption of article XIII A (Proposition 13) to provide that the value limitation standard prescribed by section 11 is to continue for taxable-government owned property in the aftermath of Proposition 13.

D. Statutory or Regulatory Change

None

E. Administrative Impact

Assessors would not be required to calculate Phillips Factor values annually for taxable government-owned lands acquired after March 1, 1975 for comparison with the fair market and factored base year values. This may result in a slight cost savings at the county level.

Assessed values may increase due to the absence of the Phillips Factor value because that value is typically the lowest of the three values. Therefore, the Board's assessment appeals workload may increase as a result of more appeals by local governments. Any increase in workload would be negligible and absorbed by current staff.

F. Fiscal Impact

1. Cost Impact

None

2. Revenue Impact

Values would increase for those lands for which the Phillips Factor is the lowest value which would increase property tax revenue to local governments in the county where the assessed property is located. However, the increase may only result in a shift of monies among local governments because the property tax liability is being paid by the local government that owns the property. Local revenue increases would reduce the level of expenditure from the General Fund for public school appropriations since schools receive approximately 54% statewide of every dollar increase in property tax revenue.

G. Taxpayer/Customer Impact

Assessed values would increase for some local governments that own taxable property while property tax revenues would increase for local governments in counties where those taxable properties are located.

H. Critical Time Frames

No critical time frame for this issue.

V. Staff Recommendation 2

The base year values for taxable government-owned properties acquired after March 1, 1975 should be determined in the same manner as for privately owned, locally assessed real property; that is, using the current fair market value as of the date of change in ownership.

A. Description of the Staff Recommendation

The Court in *City and County of San Francisco v. County of San Mateo* held that article XIII A (Proposition 13) did not repeal section 11 and that both apply to extraterritorial government-owned land in counties other than Inyo and Mono. The Court affirmed that for all real property subject to article XIII A the "full cash value" equals the fair market value when real property is first purchased, newly constructed, or otherwise changes ownership after March 1, 1975. By holding that article XIII A applies to taxable government-owned properties, the case decided that the base year values for taxable government-owned properties should be determined in the same manner as other privately owned, locally assessed real property.

B. Pros of the Staff Recommendation

Staff's recommendation is consistent with *City and County of San Francisco v. County of San Mateo*, which held that section 11 and article XIII A apply concurrently to taxable land owned by a local government and located outside its boundaries. Because the court held that taxable government-owned properties receive the taxable value ceiling provided by article XIII A (i.e., factored base year value), that value must be determined in the same manner as base year values for other properties.

C. Cons of the Staff Recommendation

Staff's recommendation advising assessors to establish base year values at fair market value as of the date of change in ownership is contrary to the holding in *City and County of San Francisco v. County of San Mateo*. The court held that the "base year value" of San Francisco's lands in San Mateo and Alameda which were acquired before 1975 was determined by starting with their valuation under section 11 for the 1975-1976 tax year (the "county assessor's valuation" for that tax year) and increasing it by the rate of inflation to a maximum of 2 percent per year. Therefore, when taxable land is acquired by a local government after March 1, 1975, and if the Phillips Factor value is lower than fair market value at the time of acquisition, then the Phillips Factor value becomes the base year value for the property.

D. Statutory or Regulatory Change

None

E. Administrative Impact

There would be no administrative impact in any county except Los Angeles as all other counties determine the base year values for taxable government-owned properties in the same manner as locally assessed, privately owned properties (taxable government-owned properties in Inyo and Mono counties are not subject to article XIII A). Los Angeles County determines the base year values for Section 11 property differently than all other counties. Los Angeles County defines the base year value for taxable government-owned property acquired after March 1, 1975 as the lower of (1) current market value as of the date of acquisition or (2) the 1967 assessed value multiplied by the appropriate Phillips Factor as of the date of acquisition. There would be an administrative impact in Los Angeles County as staff's recommendation would necessitate the creation of new base year values for taxable Section 11 properties acquired after March 1, 1975 according to the method recommended by staff. Additionally, Los Angeles County would have to track the factored base year value in addition to the section 11 value.

Assessed values for some taxable government-owned lands would increase in Los Angeles County and, therefore, the Board's assessment appeals workload may increase as a result of more appeals by local governments. Any increase in workload would be negligible and absorbed by current staff.

F. Fiscal Impact

1. Cost Impact

There would be no cost impact to the counties that would be unaffected. There would be a minimal limited term cost impact for Los Angeles County as that county does not determine the base year values for Section 11 properties in the same manner as privately owned, locally assessed property.

2. Revenue Impact

Values would increase for those lands in Los Angeles County acquired after March 1, 1975 for which the Phillips Factor value was lower than the fair market value as of the date of change in ownership. This assessed value increase would increase property tax revenue to local governments in the county. However, the increase may only result in a shift of monies among local governments because the property tax liability is being paid by the local government that owns the property. Local revenue increases would reduce the level of expenditure from the General Fund for public school appropriations since schools receive approximately 54% statewide of every dollar increase in property tax revenue.

G. Taxpayer/Customer Impact

Assessed values would increase for some local governments that own taxable property while property tax revenues would increase for local governments in Los Angeles County.

H. Critical Time Frames

No critical time frame for this issue.

VI. Alternative 1 (For Staff Recommendation 2)

A. Description of the Alternative

The Board could specify that the base year value for taxable government-owned property acquired after March 1, 1975 is the lower of (1) current market value as of the date of acquisition or (2) the 1967 assessed value times the appropriate Phillips Factor as of the date of acquisition. This alternative was proposed by the Los Angeles County Assessor's Office.

B. Pros of the Alternative

This alternative is consistent with the *City and County of San Francisco v. County of San Mateo* decision which held that both section 11 and article XIII A apply to taxable local government owned lands. Section 11 requires assessment at the lower of fair market value or Phillips Factor value. Once that value is determined upon a change in ownership, it becomes the base year value, the value limitation standard established by article XIII A.

C. Cons of the Alternative

This method of determining the base year value is inconsistent with the holding in *City and County of San Francisco v. County of San Mateo* which held that taxable local government-owned properties are subject to the provisions of article XIII A in the same manner as other locally assessed real property. Section 2 of article XIII A provides, in relevant part, that full cash value for real property is the fair market value as of the date of change in ownership, with increases for inflation limited to 2 percent per year. Thus, the base year value for all real property subject to article XIII A, including taxable local government-owned lands, is the fair market value as of the date of change in ownership or, in this case, the date of acquisition by the local government.

D. Statutory or Regulatory Change

None

E. Administrative Impact

There would be no administrative impact in Los Angeles County. For the other counties (other than taxable government-owned lands located in Inyo and Mono counties which are not subject to article XIII A), this alternative would result in establishing new base year values for taxable government-owned properties acquired after March 1, 1975. Thus, for the other counties, the alternative base year value determination method would result in short-term increased workload due to the need to establish new base year values.

F. Fiscal Impact

There would be a minimal short-term administrative cost impact with this alternative for 55 counties.

1. Cost Impact

This alternative would result in a minimal limited-term increase in administrative costs at the local assessors' level. The extent of the cost impact is indeterminable at this time.

2. Revenue Impact

The Phillips Factor value is typically lower than fair market value and, thus, base year values determined for lands acquired after March 1, 1975 would decline. Lower assessed values would result in a loss of tax revenue to counties where taxable local government-owned property is located. The extent of the revenue loss is indeterminable at this time. Local revenue losses would increase the level of expenditure from the General Fund for public school appropriations since schools receive approximately 54% statewide of every dollar increase in property tax revenue.

G. Taxpayer/Customer Impact

Assessed values would decrease for some local governments that own taxable property acquired after March 1, 1975.

H. Critical Time Frames

No critical time frame for this issue.

V. Staff Recommendation 3

Apply supplemental assessments to taxable government-owned properties.

A. Description of the Staff Recommendation

Staff recommends that the Guidelines advise that the supplemental assessment provision, section 75.14 of the Revenue and Taxation Code, is applicable to all property subject to article XIII A, including taxable government-owned properties acquired by a local government after March 1, 1975. Section 75.14 provides that all property subject to the assessment limitations of article XIII A are subject to supplemental assessments and that all property that is not subject to the assessment limitations of article XIII A are not subject to supplemental assessments. The California Supreme Court in *City and County of San Francisco v. County of San Mateo* (1995) 10 Cal.4th 554 held that the value limitations of article XIII A applied to San Francisco's lands and does not conflict with section 11 of article XIII. Based on the court's interpretation that taxable government-owned properties are subject to the provisions of article XIII A, Section 11 properties are, therefore, subject to supplemental assessments.

B. Pros of the Staff Recommendation

Staff's recommendation is consistent with case law interpretation of article XIII A and the plain language of section 75.14, which support the application of supplemental assessment provisions to Section 11 properties. The California Supreme Court in *City and County of San Francisco v. County of San Mateo* (1995) 10 Cal.4th 554 held that the value limitations of article XIII A applied to San Francisco's lands and did not conflict with section 11. Based on the court's interpretation that taxable government-owned properties are subject to the provisions of article XIII A, Section 11 properties are, therefore, subject to supplemental assessments.

C. Cons of the Staff Recommendation

Staff's recommendation would frequently result in increased supplemental assessments as of the date of change in ownership, with likely assessed value reductions on the following lien date. For example, a private party sold land to a local government in 1998 for \$2,500,000. The land is located outside the purchaser's boundaries and was taxable when acquired. The land was valued on the tax roll at its 1975-76 value (assume \$750,000) plus 2% per year inflation factor since 1975-1976. The land was assessed in 1967 at \$50,000.

According to staff's proposed assessment guidelines, the new base year value is \$2,500,000. In accordance with this determination, the assessor issues a supplemental assessment for the year in which the change in ownership occurs based on the new value. The new government owner would receive a supplemental assessment for the difference between the roll value and the new base year value. However, in the following year, the taxing county must go back to determine the 1967 value and apply the Phillips Factor to determine whether that valuation is lower than the new factored base year value. We have assumed that the land was valued at \$50,000 in 1967. A new lower limit based on the 1967 valuation times a Phillips Factor of approximately 27 would result in a Phillips Factor value of \$1,350,000. Because the Court has ruled that both article XIII A and section 11 of article XIII apply, the taxable value would be the lesser of the (1) factored base year value, (2) fair market value, and (3) Phillips Factor value, the taxable value would be reduced to the Phillips Factor value. In summary, staff's recommendation would likely result in supplemental assessments, followed by value reductions, as illustrated by this example.

D. Statutory or Regulatory Change

None

E. Administrative Impact

None

F. Fiscal Impact

1. Cost Impact

None

2. Revenue Impact

None

G. Taxpayer/Customer Impact

None

H. Critical Time Frames

No critical time frame for this issue.

VI. Alternative 1 (For Recommendation 3)

A. Description of the Alternative

The Board could specify that the supplemental assessments do not apply to taxable government-owned properties. This alternative was proposed by the Los Angeles County Assessor's Office.

B. Pros of the Alternative

Supplemental assessments are applicable when the base year value is established by determining fair market value as of the date of change in ownership or completion of new construction. However, according to Los Angeles County, base year values for taxable government-owned properties are established at the lower of fair market value or Phillips Factor value as of the date of acquisition. Because a different value standard is used to determine base year values for taxable government-owned lands, supplemental assessments are not applicable.

C. Cons of the Alternative

This alternative is inconsistent with the holding in *City and County of San Francisco v. County of San Mateo* which held that taxable local government-owned properties are subject to the provisions of article XIII A in the same manner as other locally assessed real property. Section 75 and following sections set forth provisions for supplemental assessments. Section 75.14 provides that all property subject to the assessment limitations of article XIII A shall be subject to the supplemental assessment provisions. Therefore, taxable government-owned properties must be subject to supplemental assessment.

D. Statutory or Regulatory Change

None

E. Administrative Impact

None

F. Fiscal Impact

None

1. Cost Impact

None

2. Revenue Impact

Minimal revenue impact.

G. Taxpayer/Customer Impact

None

H. Critical Time Frames

No critical time frame for this issue.