STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

DRAFT

Date Amended:	**03/14/06**	Bill No:	**AB 1890**
Tax:	**Property**	Author:	**Mountjoy**
Related Bills:			

BILL SUMMARY

This bill would increase from three years to five years the timeframe a property owner has to acquire or construct a property to replace one damaged or destroyed in a Governor declared disaster and remain eligible to receive a base year value transfer.

ANALYSIS

Current Law

Revenue and Taxation Code Section 69 provides tax relief to persons who own property substantially damaged or destroyed in a Governor declared disaster. Among the various requirements and conditions, the base year value of the damaged property may be transferred to a comparable property within the same county within three years of the date the disaster occurred.

Proposed Law

This bill would amend Revenue and Taxation Code Section 69 to extend the number of years to acquire a replacement property from three to five years for disasters occurring on or after July 1, 2003.

In General

California's system of property taxation under Article XIII A of the State Constitution (Proposition 13) values property at its 1975 fair market value, with annual increases thereafter limited to the amount of inflation or 2%, whichever is less, until the property changes ownership or new construction occurs. Once a reassessable event occurs, (i.e., a change in ownership or new construction) the value of the property for tax purposes is redetermined based on its current market value. The value initially established, or redetermined where appropriate, is referred to as the "base year value."

Because real estate values generally appreciate at a rate greater than 2% per year, when an event occurs triggering a reassessment of property to its current market value, the reassessed value (i.e., its new base year value) will likely be substantially higher.

California property tax law provides for various situations where the base year value of a property is either: (1) retained, notwithstanding that new construction has taken place or that the property has changed ownership, or (2) transferred to another property,

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notwithstanding that the property has changed ownership. These special situations are provided pursuant to various constitutional amendments modifying the original Proposition 13 framework and serve to avoid the otherwise required reassessment of a property to its current market value.

For instance, related to the subject matter of this bill, Revenue and Taxation Code Section 70(c) provides that where property has been damaged or destroyed by a misfortune or calamity, the property will retain its previous assessed value after its reconstruction. Consequently, a property that is rebuilt after a fire will continue to be assessed at the same amount even though the property has been entirely newly constructed. (This new construction exclusion was provided by Proposition 8 in 1978)

Specifically related to this bill, Section 69 provides that persons who own property substantially damaged or destroyed in a Governor-declared disaster may transfer the base year value of that property to a property acquired or constructed as a replacement if it is acquired within three years after the disaster. "Substantially damaged" means physical damage amounting to more than 50 percent of its current market value immediately prior to the damage. Base year value transfers are available for all property types; with the limitation that the original property and the replacement property must be of the same property *type*: residential, commercial, agricultural, or industrial. The replacement property is "comparable" if it is similar in size, utility, and function to the destroyed property, and if the market value of the acquired property does not exceed 120% of the fair market value of the replaced property in its pre-damaged condition. Property owners may, nevertheless, still receive the disaster relief in cases where the value of the replacement property exceeds the 120% limitation. In such cases, the amount over this threshold is assessed at full market value and added to the transferred base year value. (Proposition 50 of 1986 authorized this base year value transfer provision.)

Section 69.3 provides similar disaster base year value transfer provisions but, unlike Section 69 which applies to all property types, it is limited to principal places of residences purchased in another county and only applies to homes purchased in counties where the board of supervisors has adopted an ordinance making this benefit available. Currently, only eight counties extend this relief to displaced homeowners who previously lived in another county: Contra Costa, Los Angeles, Modoc, San Francisco, Santa Clara, Solono, Sutter and Ventura. (Proposition 171 in 1995 authorized this base year value transfer provision.)

Background

In 1993, AB 1824 (Stats. 1993, Ch. 1053) extended the timeframe for Section 69 base year value transfers from 2 years to 3 years for all disasters occurring on or after October 20, 1991, the date of the Oakland hills fire. In 1997, SB 594 (Stats. 1997, Ch. 941) provided a special five year timeframe for any victim of the 1994 Northridge earthquake.

COMMENTS

1. **Sponsor and Purpose.** The author is sponsoring this bill to ensure that affected property owners have sufficient time to acquire a suitable replacement property.
2. **Base year value transfers provide tax relief to disaster victims. Permitting a person to "transfer" their base year value from one property to another property provides** tax relief by allowing the property owner to continue paying taxes on the replacement property equivalent to that paid on the property from which they were displaced. Without a base year value transfer, the taxes on the new property would likely be significantly more because, under the general change in ownership laws, the taxes would be based on the property's current fair market value. The rationale for providing a base year value transfer is that the tax laws should not further afflict disaster victims by imposing upon them higher property taxes. If the disaster had not occurred, those individuals would not have been compelled to relocate and thereby forfeit their Proposition 13 protected base year values.
3. **The three year timeframe is a statutory limitation.** The constitution provides that the Legislature shall provide for these base year value transfers and Section 69 is the implementing statute. Article XIII A, Section 2(e) of the California Constitution does not expressly authorize the Legislature to establish time requirements for acquiring a replacement property within the same county. It may be more appropriate to establish time periods that do not unnecessarily exclude taxpayers from receiving the benefits otherwise available. A more liberal time period could prevent constitutional challenges to establishing any time limit.
4. **Should the 120% threshold be increased to reflect the five year timeframe?** Under current law, a straight base year value transfer is allowed if the market value of the acquired property does not exceed 120% of the fair market value of the replaced property in its pre-damaged condition. If the value of the replacement property exceeds the 120% limitation, then the amount over this threshold is assessed at full market value and added to the transferred base year value. The author may wish to consider increasing the value threshold for an acquisition in the fourth or fifth year.
5. **Three years is not always enough time.** While most property owners will likely fit into the existing three year period, the financial impact to the individual property owner that doesn't can be significant. Delays occur for a variety of reasons: unsettled insurance claims, uninsured or underinsured property owners, limited supply of replacement properties available for purchase, and lack of construction workers. This is especially true where the disaster creates mass destruction in a localized area.
6. **This bill does not amend the three year timeframe for Section 69.3 base year value transfers because of constitutional constraints.** Section 69.3 provides similar tax relief for replacement principal places of residence located in a different county. However, the three year limit is expressly specified in the constitutional provision authorizing these transfers. Consequently, to extend this timeframe would require a constitutional amendment.

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COST ESTIMATE

The Board would incur some minor absorbable costs in informing and advising county assessors, the public, and staff of the law changes.

REVENUE ESTIMATE

Background, Methodology, and Assumptions

There have been eight governor declared disasters in California since July 1, 2003. None of those disasters will be affected by the three year transfer period until October 2006, when the Southern California wildfires disaster will be three years removed. With regard to disasters occurring before July 2003, including the El Niño storms of 1998, staff determined that in several counties, no requests for base year value transfers have been denied due to the three year requirement.

In looking at the October 2003 Southern California wildfires as an example, we know that 97 percent of the homes damaged or destroyed were in San Diego County or San Bernardino County. According to an October 2005 article in the *San Diego Union-Tribune*, 94 percent of those who lost their homes within San Diego city limits had acquired building permits, and two-thirds had already moved back in to their homes. In San Diego's unincorporated area, mountain communities in many cases, about one-third of the homes had been rebuilt, while over one-third of the destroyed homes had not yet begun construction. Also in October 2005, the *San Bernardino Sun* reported that in San Bernardino County about 1,000 homes, or 75 percent of homes damaged or destroyed by 2003 wildfires, had been built or approved for building.

Regarding the 2003 Southern California wildfires, according to an October 2004 report by the *Insurance Journal*, statistics from two insurance companies show that 95 percent of their claims have been settled. Those two companies handled nearly half of all claims filed following this disaster. While claim settlement is not necessarily a gauge in the rebuilding process, it is an indicator of progress.

The actual number of base year transfer requests that will be denied due to time following future disasters is highly uncertain. The nature and extent of the disaster will go a long way in determining that outcome. In the case of the 2003 Southern California wildfires, several factors unique to this disaster may contribute to a higher likelihood of transfers taking longer. Among the factors are the following:

- Delays in the building permit process due to an influx of requests, architectural changes to original designs, and property line disputes.
- Shortage of contractors and building materials due to the volume of rebuilding.
- The nature of the property; some of the damaged and destroyed homes were vacation homes in mountainous regions that may or may not be rebuilt.

Actions taken following governor declared disasters in previous years may not accurately reflect the actions taken following future disasters.

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Revenue Summary

Since no data are available on the numbers or percentages of property owners who would transfer their base year values, it is difficult to estimate the revenue impact at 1% of assessed values for transfer requests denied by the county due to time. Based on information obtained from several counties, and based on statistics like those obtained in the wildfires example above, staff estimates that very few requests for base year transfers are denied due to time in the wake of governor declared disasters, resulting in a very small revenue impact.

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