Date of Hearing: April 10, 2023

ASSEMBLY COMMITTEE ON REVENUE AND TAXATION
Jacqui Irwin, Chair

AB 1066 (Joe Patterson) – As Amended March 23, 2023

2/3 vote. Tax levy. Fiscal committee.

SUBJECT: Property taxation: exemption: low-value properties

SUMMARY: Increases the low-value property tax exemption from $10,000 to $15,000, among other provisions. Specifically, **this bill**:

1) Increases the maximum value of property that may be exempt from property taxation due to its low-value from $10,000 to $15,000.

2) Applies an annual adjustment for inflation to personal property.

3) Eliminates the existing 2% limitation to the annual adjustment for inflation on real property.

4) Provides that no appropriation is made by this bill and that the state shall not reimburse any local agency for any property tax revenue losses resulting from this bill.

5) Takes immediate effect as a tax levy.

EXISTING LAW:

1) Provides that all property is taxable unless otherwise provided by the California Constitution or the laws of the United States. (California Constitution, Article XIII, Section 1.)

2) Authorizes the Legislature, by a two-thirds vote, to exempt personal property from taxation. (California Constitution, Article XIII, Section 2.)

3) Authorizes the Legislature, by a two-thirds vote, to permit county boards of supervisors to exempt real property having a full value so low that, if not exempt, the total taxes on the property would amount to less than the cost of assessing and collecting them. This exemption is commonly referred to as the "low value ordinance exemption", because the board of supervisors must enact a county ordinance and determine the value threshold appropriate for the county. (California Constitution, Article XIII, Section 7.)

4) Implements the Legislature's constitutional authority to authorize a low value ordinance exemption by limiting the base year value of real property, or the full value of personal property, to $10,000. In the case of real property, existing statute allows an adjustment for inflation of the base year value not to exceed 2% annually. Counties are required to undertake a study to evaluate the appropriate level for the value of the exemption, subject to the maximum limit. (Revenue and Taxation Code (R&TC) Section 155.20)

5) Requires that the state reimburse any classification or exemption of property for purposes of ad valorem property taxation. (R&TC Section 2229.)

FISCAL EFFECT: Unknown

COMMENTS:

1) The author has provided the following statement in support of this bill:

   It takes more time and local government resources to asses low value property items than the amount of revenue that can be collected. AB 1066 provides flexibility to local governments to exempt those assessments that take too many staff resources only after the local government does a fee study. This bill provides locals with an option to save money.

2) Committee Staff Comments:

   a) *The Low Value Ordinance Exemption*: In November of 1974, Proposition 8 established the low value ordinance exemption authorization by adding Section 7 to Article XIII of the California Constitution, which incorporated recommendations made by the Constitution Revision Commission (Commission). The contemporary practice by assessors was to not assess certain real property interests when the administrative costs would outweigh the revenue proceeds derived from taxing that real property. In essence, making the assessment was not prudent from an administrative perspective, and the Commission sought to ensure that assessors had legal authority for this practice. County boards of supervisors now have explicit authority to set a low value threshold by ordinance; correspondingly, thresholds may be set at different levels for different property types. When implementing this Constitutional authorization, the Legislature distinguished between real property and personal property by providing an inflationary adjustment factor on the maximum base year value for real property, up to 2% annually.

   b) *What does this bill do*? As currently drafted, this bill has three main components. The first is increasing the maximum limit that a county board of supervisors may adopt as the threshold for a low value ordinance exemption from $10,000 to $15,000. The second is to apply an inflation adjustment factor to the maximum limit for personal property. The third is to remove any cap on the inflation adjustment factor for all amounts.

      The maximum limit for the low value ordinance exemption has been raised numerous times over the course of the exemption's history, being adjusted upwards approximately every 10 to 15 years. The last time this amount was increased was in 2009. Accounting for inflation, the $10,000 limit set in 2009 would be equal to nearly $14,000 today.

   c) *Inflation nation*: Recently, inflation, which is the rate of increase in prices over a given period of time, has risen significantly. From February 2022 to February 2023, inflation rose at an average rate of 6%.

      While applying and adjustment inflation adjustment factor for the maximum limit for the low value ordinance exemption would benefit taxpayers, as the maximum amount that a county may exempt would annually increase with inflation, removing the existing 2% cap on the inflation adjustment for the base year value of real property would likely negatively impact taxpayers because the base year value of the property could increase at a faster rate than under existing law, which would likely result in the value of the property surpassing the maximum limit sooner than with the cap. The author has indicated that this is not the intent, and the author and Committee may wish to amend this bill to reinstate the cap on the inflation adjustment factor to the base year value of the property that may be exempt.

d) *Proposition 98*: In 1988, voters established a minimum funding requirement for schools and community colleges, commonly referred to as the "minimum guarantee", by approving Proposition 98. The guarantee is calculated through a series of formulas stipulated in the Constitution, and encompasses state General Fund (GF) and local property tax revenues. In any given year, the inputs used to calculate the minimum guarantee may vary. The state determines which inputs to use based on the formulas in the Constitution or "tests". Depending on certain inputs, such as GF revenue and changes in student attendance, the state determines the test that will be operative, and that test sets the minimum guarantee for that year. Thus, the amount of property tax revenue that schools and community colleges receive impacts the minimum guarantee calculation. However, the extent of that impact varies based on the type of test used. In Test 1 years, the minimum guarantee equals a fixed percentage of state GF revenues, plus any amount of property tax revenues that the schools and community colleges receive in that year. Fluctuations in property tax revenue have a dollar-for-dollar effect on school funding in Test 1 years. In years where the other tests are operative, changes in property tax revenues do not affect the minimum guarantee or overall school funding, but do impact the amount of GF the state must allocate to meet the guarantee[1]. The LAO predicts that Test 1 is likely to remain operative for the next three years of the budget period[2]. This bill could result in a reduction of local property tax revenues by increasing the maximum amount under the low value ordinance exemption.

e) *Drafting concern*: This bill's current drafting is unclear. While the intent is to apply an inflation adjustment factor to this bill's maximum limit for the low value ordinance exemption, this bill is not clear on that application. The author and Committee may wish to consider amending this bill as follows:

   i) On Page 2, Line 18, delete the phrase "($15,000) as adjusted by an annual inflation"; and

   ii) On Page 2, Line 18, insert, "($15,000). This figure shall be adjusted by an inflation factor equivalent to the annual inflation adjustment"

f) *What is a "tax expenditure"?* Existing law provides various credits, deductions, exclusions, and exemptions for particular taxpayer groups. In the late 1960s, United States Treasury officials began arguing that these features of the tax law should be referred to as "expenditures" since they are generally enacted to accomplish some governmental purpose and there is a determinable cost associated with each of them, in

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[1] LAO, *Excess ERAF*: *A Review of the Calculations Affecting School Funding* (2020) <https://lao.ca.gov/Publications/Report/4193> accessed March 2023.
[2] LAO, *Proposition 98 Overview and K-12 Spending Plan* (2023) <https://lao.ca.gov/Publications/Report/4670> accessed March 2023.

the form of forgone revenues. This bill would increase the maximum amount that a county may exempt from property taxation due to the costs of assessment and collection outweighing revenues, thereby constituting a tax expenditure.

g) *Committee's tax expenditure policy*: SB 1335 (Leno), Chapter 845, Statutes of 2014, added R&TC Section 41, which recognized that the Legislature should apply the same level of review used for government spending programs to tax credits introduced on or after January 1, 2015. AB 263 (Burke), Chapter 743, Statutes of 2019, extended the requirements in R&TC Section 41 to all tax expenditure measures under the Personal Income Tax Law, the Corporation Tax Law, and the Sales and Use Tax Law introduced on or after January 1, 2020. While R&TC Section 41 does not apply to proposals related to property taxation, this Committee treats all tax expenditures in a similar manner and applies the requirements of R&TC Section 41 to bills that confer a property tax expenditure. A tax expenditure proposal must outline specific goals, purposes, and objectives that the tax expenditure will achieve, along with detailed performance indicators for the Legislature to use when measuring whether the tax expenditure meets those stated goals, purposes, and objectives. In addition to the R&TC Section 41 requirements, this Committee's policy also requires that all tax expenditure proposals contain an appropriate sunset provision to be eligible for a vote[3]. Sunsets are required because eliminating a tax expenditure generally requires a two-thirds vote. These requirements must be satisfied before a bill can receive a vote in this Committee. This bill does not comply with R&TC Section 41 and does not include an appropriate five-year sunset.

h) *Previous legislation*:

i) AB 608 (Petrie-Norris), Chapter 92, Statutes of 2019, expanded the higher limit low value ordinance exemption of $50,000 for certain possessory interests to include all possessory interests.

ii) SB 822 (Committee on Revenue and Taxation), Chapter 204, Statutes of 2009, increased the general low value ordinance exemption limit from $5,000 to $10,000.

iii) SB 33 (Maddy), Chapter 106, Statutes of 1997, expanded the higher low value ordinance exemption limit of $50,000 to include possessory interests in fairgrounds or fairground facilities.

iv) SB 1737 (Alquist), Chapter 570, Statutes of 1996, created a higher low value ordinance exemption limit of $50,000 for taxable possessory interests in publicly owned convention or cultural facilities.

v) SB 722 (Committee on Revenue and Taxation), Chapter 497, Statutes of 1995, increased the general low value ordinance exemption limit from $2,000 to $5,000.

vi) SB 367 (Craven), Chapter 441, Statutes of 1991, created a higher low value ordinance exemption limit of $5,000 for mobilehome accessories.

[3] An "appropriate sunset provision" shall mean five years, except in the case of a tax expenditure measure providing relief to California veterans, in which case "appropriate sunset provision" shall mean 10 years.

REGISTERED SUPPORT / OPPOSITION:

Support

None on file

Opposition

None on file

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