

[Assembly Bill 2013](#) (Irwin)

Program: Property Taxes

Sponsor: California Assessors' Association

Revenue and Taxation Code Section 70.5

Effective: January 1, 2021

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Summary: For property that has been substantially damaged or destroyed by a Governor-declared disaster on or after January 1, 2017, this bill adds a new construction exclusion for comparable property that is reconstructed on the site of the damaged or destroyed property.

Fiscal Impact Summary: This bill would reduce annual property tax revenues at the basic 1 percent tax rate on average by as much as \$820 per replacement home and by as much as \$5,000 per commercial replacement property.

Existing Law: Under existing law, real property is generally reassessed to its current fair market value whenever it has undergone a change in ownership or new construction has been completed. The value initially established or reassessed upon a change in ownership or completion of new construction is referred to as the property's "base year value."¹ The assessment of real property may be temporarily reduced to reflect reductions in value due to damage, destruction, depreciation, obsolescence, removal of property, or other factors causing a decline in value.²

A reduction in value for disaster, misfortune, or calamity³ applies to major disasters affecting many properties, such as an earthquake, flood, or wildfire, as well as a disaster affecting an individual property, such as a house fire. The reduced value of a damaged property will continue until the real property is reconstructed. The reconstruction of real property that has been damaged or destroyed by disaster, misfortune, or calamity is not subject to reassessment as new construction under RTC section [70\(c\)](#), if the property meets the following requirements:

- Reconstructed in a timely fashion, and
- Reconstruction is substantially equivalent to the property prior to the damage or destruction.

New construction following damage to real property by a calamity or misfortune is not eligible for disaster relief if the rebuilt improvements are not substantially equivalent to the property prior to damage or destruction. Only that portion of the reconstruction that exceeds substantial equivalence to the property prior to damage or destruction will have a new base year value.

Under RTC section [170](#),⁴ relief may be applied immediately as of the date of the disaster, misfortune, or calamity if the loss in a property's market value is \$10,000 or more.⁵ Under section 170, when property has been fully repaired, restored, or reconstructed, as of the date of completion of construction, the

¹ Revenue and Taxation Code (RTC) section [110.1](#).

² Section [51\(b\)](#).

³ The term *misfortune or calamity* is defined by case law. The court of appeal, in *T.L. Enterprises, Inc. v. County of Los Angeles* (1989) 215 Cal.App.3d 876, held that a misfortune or calamity is a sudden, unforeseeable event.

⁴ All 58 counties have enacted disaster relief ordinances pursuant to section 170.

⁵ Section 170(b).

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.

assessor will restore the lower of (1) the full cash value, (2) the damaged property's factored base year value, or (3) its factored base year value as adjusted pursuant to section 70(c).

Proposed Law: For property that has been substantially damaged or destroyed by a Governor-declared disaster on or after January 1, 2017, this bill adds a new construction exclusion for comparable property that is reconstructed on the site of the damaged or destroyed property, under the following conditions:

- **Disaster.** Property must be substantially damaged or destroyed by a disaster, misfortune, or calamity, as declared by the Governor. *RTC section 70.5(a) and (c)(3)*
- **Substantially Damaged or Destroyed.** Property is substantially damaged or destroyed if the improvements sustain physical damage amounting to more than 50 percent of the improvements' full cash value immediately prior to the disaster. *RTC section 70.5(c)(1)*
- **Comparable Reconstruction.** Reconstructed property is comparable if it is similar in function, size, and utility. *RTC section 70.5(c)(2)*
 - **Function.** Property is similar in function if it is subject to similar governmental restrictions, such as zoning. *RTC section 70.5(c)(2)(A)*
 - **Size and Utility.** Size and utility are interrelated and associated with value. Property is similar in size and utility if it is used or intended to be used in the same manner and its full cash value does not exceed 120 percent of the full cash value of the damaged original property, determined just prior to the date of damage/destruction. *RTC section 70.5(c)(2)(B)(i)*
 - **Partial Relief.** If the full cash value of the reconstructed property exceeds the 120 percent threshold, the amount above 120 percent will be added to the transferred base year value. *RTC section 70.5(b)(2)(B)*
- **Ownership.** Only the owner(s) of the property substantially damaged or destroyed is eligible to receive relief under this section. *RTC section 70.5(d)*
- **Timing.** Construction must be completed within five years of the date of the damage or destruction. *RTC section 70.5(a)*

This bill provides that these provisions apply to real property damaged or destroyed by misfortune or calamity on or after January 1, 2017. *RTC section 70.5(e)*

In General: Article XIII A of the California Constitution, as approved by the voters in June 1978, did not contain any language indicating that property values might decline in value for any reason, including disasters. To remedy this problem and alleviate tax burdens on the ensuing "new construction" for disaster-damaged property, Proposition 8 amended article XIII A in November 1978 to provide that: (1) the full cash value base may from year to year not only reflect the inflation rate, but "may be reduced to reflect substantial damage, destruction or other factors causing a decline in value," and (2) when property is damaged or destroyed through a disaster, reconstruction of the property is excluded as "new construction" when the restored structure is comparable in value to the original. (art. XIII A, [section 2\(a\)](#)). The legislation implementing these provisions is found in section 70(c).

The State Board of Equalization (BOE) enacted Property Tax Rule [463](#) to implement the new construction statutes. Rule 463(f) addressed disaster relief and provided that newly constructed property does not

include any land, improvement, or fixture that is restored, reconstructed, or repaired in a timely manner following a disaster and which is substantially equivalent in size, use, and quality to that which existed prior to the disaster. Subdivision (f) was removed from Rule 463, effective June 12, 1998.⁶

Substantially Equivalent. The reconstruction of real property that has been damaged or destroyed by disaster, misfortune, or calamity is not subject to reassessment as new construction under RTC section [70\(c\)](#), if the property is timely reconstructed and the reconstruction is substantially equivalent to the property prior to the damage or destruction. These provisions apply to any type of disaster, misfortune, or calamity, including those caused by disaster for which the Governor proclaimed a state of emergency.

The term "substantially equivalent" is not defined by statute or rule. In Assessors' Handbook Section [410](#), *Assessment of Newly Constructed Property*, Chapter 5, the BOE recommends that the replacement property is comparable to the damaged or destroyed property in design type and use. The handbook provides two examples of reconstruction that is not substantially equivalent to the destroyed property, and thus would not be eligible for this new construction exclusion.⁷

Example 1. A taxpayer owned a 1,200 square-foot residence that was totally destroyed when his property was flooded. He timely replaced the damaged property with a 3,500 square-foot residence. The additional square footage which exceeded the original 1,200 square-foot structure was assessed as new construction. Under these circumstances, the rebuilt structure will have two base year values. The pre-existing base year value will continue for the 1,200 square-foot portion of the rebuilt structure, and the additional 2,300 square feet will be appraised at market value as of the date of completion and a separate base year value will be established for that portion.

Example 2. A taxpayer owns a vacation home which is destroyed by a fire. He decides that building a motel on his property in place of his vacation home would be more profitable. Under these circumstances, the taxpayer's replacement of the home with a motel is not eligible for disaster relief. The reconstructed property is not substantially equivalent to the property prior to the damage or destruction. Accordingly, the motel is considered new construction.

Governor State of Emergency Proclamations. The Government Code⁸ authorizes the governor to proclaim a state of emergency under specified circumstances, including:

- "State of war emergency" means the condition which exists immediately, with or without a proclamation thereof by the governor, whenever this state or nation is attacked by an enemy of the United States, or upon receipt by the state of a warning from the federal government indicating that such an enemy attack is probable or imminent.
- "State of emergency" means the duly proclaimed existence of conditions of disaster or of extreme peril to the safety of persons and property within the state.
- "Local emergency" means the duly proclaimed existence of conditions of disaster or of extreme peril to the safety of persons and property within the territorial limits of a county, city and county, or city.

⁶ See Letters To Assessors No. [98/07](#) and No. [98/48](#).

⁷ Assessors' Handbook Section 410, pages 48-49.

⁸ Government Code (GC) sections [8558](#) and [8625](#).

Background: Disaster Relief Base Year Value Transfer. Exceptions to the reassessment requirement upon a change in ownership have been enacted, including two base year value transfers for property owners whose property has been damaged or destroyed in a disaster for which the Governor proclaimed a state of emergency.

1. **Intracounty Transfers.** Existing law⁹ allows a person who owns property substantially damaged or destroyed in a Governor-proclaimed disaster to transfer the base year value of the damaged property to a comparable replacement property, as long as the replacement property is:
 - Located within the same county,
 - Purchased or newly constructed within five years of the date the disaster occurred, and
 - Similar in size, utility, and function.
 - Property is similar in *size and utility* if the market value of the acquired property does not exceed 120 percent of the fair market value of the damaged or destroyed property in its pre-damaged condition. If the market value of the replacement property exceeds 120 percent, partial relief is available. Specifically, the value above 120 percent is added to the transferred base year value.
 - Property is similar in *function* if the replacement property is subject to similar governmental restrictions, such as zoning. The replacement property must be used in the same manner as the damaged or destroyed property.

Any type of property that is damaged or destroyed in a disaster for which the Governor proclaimed a state of emergency may qualify for this intracounty base year value transfer, including multifamily, commercial, or industrial property.

2. **Intercounty Transfers.** Existing law¹⁰ allows a homeowner whose principal residence was substantially damaged or destroyed in a Governor-proclaimed disaster to transfer the base year value to a replacement property that is purchased or newly constructed in a different county, as long as the replacement property is located in a county that has enacted an ordinance,¹¹ purchased or newly constructed within three years of the date of the disaster, the principal residence of the property owner, and of equal or lesser value.

Legislative History. In 2019, the Legislature approved Assembly Bill [885](#) (Irwin), which provided that "substantially equivalent" meant the reconstructed improvement does not exceed 120 percent of either the size or full cash value of the improvement before the damage or destruction (substantially similar to this bill prior to the May 11, 2020 amendment). However, Governor Newsom vetoed this measure on the grounds that the proposed bright-line test should be narrowed to minimize negative impacts on local revenues.

⁹ RTC section [69](#).

¹⁰ RTC section [69.3](#).

¹¹ Contra Costa, Los Angeles, Modoc, Orange, San Francisco, Santa Clara, Solano, Sonoma, Sutter, and Ventura Counties.

Commentary:

1. **Summary of Amendments.** The **August 7, 2020** amendment clarifies the proposed definition of "disaster" in section 70.5(c)(3) for property damaged or destroyed by misfortune or calamity, as proclaimed by the Governor. The **May 11, 2020** amendment (1) eliminates the proposed definition of "substantially equivalent" in section 70(c) for property damaged or destroyed by misfortune or calamity, and (2) adds a separate new construction exclusion for comparable property reconstructed on the site of property that was substantially damaged or destroyed in a Governor-proclaimed disaster.
2. **Governor's Proclamation of State of Emergency or State of Disaster.** This bill provides that its provisions apply to property that is substantially damaged or destroyed by a disaster, "as declared by the Governor." However, under the Government Code, governors issue proclamations of state of emergency for conditions of disaster or extreme peril. The text of the proclamation itself may or may not refer to the existence of conditions of disaster. Nonetheless, the governor does not "declare" a disaster. The governor proclaims a "state of emergency." In place of "as declared by the Governor," the author may want to consider that this phrase instead read "as proclaimed by the Governor to be in a state of emergency or disaster" in subdivisions (a) and (c)(3), to be consistent with the Government Code and the governors' actions.
3. **New Construction Exclusion.** Even though this bill characterizes this relief as a base year value transfer, it is essentially a new construction exclusion. Relief will apply as long as the comparable reconstructed improvement is located on the same site as the damaged or destroyed improvement. Under this bill, a property owner is not limited to using the same footprint as the damaged or destroyed improvement.
4. **Comparable.** This bill provides that a reconstructed improvement is comparable if the reconstructed improvement is used or intended to be used in the same manner as the original improvement and does not exceed 120 percent of full cash value of the improvement, determined just before the damage or destruction. The physical size or square footage of the structure is not an issue.

Issues have previously arisen where homeowners who had their property destroyed by fire have rebuilt homes that are larger in size than the destroyed home. Under current law, the additional square footage must be reassessed to current market value as of the date of completion of construction. Under this bill, a structure that is larger in size may be considered comparable if its full cash value is within 120 percent of the value of the damaged or destroyed structure. Partial relief is available if the reconstructed improvement exceeds 120 percent of value.

5. **Five-Year Period to Complete Construction.** This bill requires reconstruction to be completed within five years of the disaster. For counties such as Butte and Sonoma that had a large number of structures destroyed in wildfires, completing construction within a five year period may be difficult if there are permit and other delays. However, while any reconstruction completed after the five-year period would not qualify for relief under this new section, it may qualify for relief under sections 70(c) and 170 if the construction is substantially equivalent to the damaged or destroyed structure.

6. **Requesting Relief.** This bill does not contain provisions on how a property owner is to request this relief. For administrative purposes, the author may want to consider adding filing provisions, a filing period, and prospective relief for late-filed claims.
7. **Retroactive Application.** While this bill, if enacted, would take effect on January 1, 2021, AB 2013 specifically provides that it applies to real property substantially damaged or destroyed by a Governor-declared disaster that occurs on or after January 1, 2017.
8. **Sections 70(c) and 170 Disaster Relief.** Section 170(h) allows the factored base year value as adjusted under section 70(c) to be re-enrolled immediately upon completion of repair, reconstruction, or restoration. It is unclear how the provisions of this bill fit in with section 170 since section 170(h) still references only section 70(c). This creates confusion as to which section to use in determining the value to restore upon reconstruction.

Costs: The BOE will incur absorbable costs to update its documents, website materials, and provide guidance to assessors.

Revenue Impact: AB 2013 allows a comparable replacement property to exceed the original property in value by an additional 20 percent. It is difficult to estimate revenue impact based on the increased value of a replacement property, as property values may vary. However, staff can attempt to estimate the revenue impact per replacement property based on average assessed values across the state.

Using the most recent data available, staff estimates the average assessed value of a home statewide is \$412,000, meaning a replacement home valued at 120 percent of value is about \$494,000, resulting in an assessed value difference of \$82,000. Therefore, revenue loss at the basic 1 percent property tax rate is:

$$\$82,000 \times 1 \text{ percent} = \$820 \text{ per home}$$

The average assessed value of a commercial property in California is \$2.5 million. Under AB 2013, an average replacement property valued at 120 percent is then \$3.0 million, resulting in an assessed value difference of \$500,000. Revenue loss at the basic 1 percent property tax rate is:

$$\$500,000 \times 1 \text{ percent} = \$5,000 \text{ per commercial property}$$

Revenue Summary. This bill would reduce annual property tax revenues at the basic 1 percent tax rate on average by \$820 per replacement home and by \$5,000 per commercial replacement property.

Qualifying Remarks. Based on past history, this revenue estimate assumes some owners choose to reconstruct more valuable replacement properties without regard to any statutory changes. AB 2013 is limited to Governor-declared disasters. This revenue estimate does not account for any changes in economic activity that may or may not result from the enactment of the proposed law.