

**Initial Statement of Reasons for
Proposed California Code of Regulations, Title 18,
Section 462.520, *Exclusion from Change in Ownership – Intergenerational Transfers***

**SPECIFIC PURPOSE, PROBLEM INTENDED TO BE ADDRESSED, NECESSITY,
AND ANTICIPATED BENEFITS**

Current Law

Proposition 13 was adopted by the voters at the June 1978 primary election and added article XIII A to the California Constitution. Article XIII A generally limits the amount of ad valorem tax to a maximum of one percent of the full cash value of real property. For purposes of this limitation, section 2 of article XIII A defines full cash value to mean a county assessor's valuation of real property as shown on the 1975-76 tax bill, or thereafter, the appraised value of that real property when purchased, newly constructed, or a change in ownership has occurred. The California Legislature codified the definition of "change in ownership" in Revenue and Taxation Code (RTC) section 60 and codified other provisions regarding whether a transfer of property results in a change in ownership or is excluded from the definition of "change in ownership" in RTC sections 61 through 69.5.

Relevant to this Proposed Rule, voters amended Article XIII A of the constitution to add two exclusions from change in ownership. Specifically, Proposition 58, effective November 6, 1986, excluded from change in ownership transfers of real property between parents and children and Proposition 193, effective March 27, 1996, excluded from change in ownership transfers of real property from grandparents to grandchildren, provided that all of the parents of the grandchildren who qualify as children of the grandparents are deceased as of the date of transfer. These two constitutional amendments are reflected in section 2, subdivision (h) of article XIII A of the California Constitution, codified at section 63.1 of the RTC, and are referred to as the Parent-Child and Grandparent-Grandchild Exclusions, respectively.

In the November 3, 2020 general election, the voters amended the constitution by approving Proposition 19 (Prop 19), which, amongst other things, created a new intergenerational transfer exclusion (by adding Section 2.1, subdivisions (c) and (e) to article XIII A of the California Constitution) and adopted a sunset date of February 15, 2021 (pursuant to Section 2.1, subdivision (d)) for the Parent-Child and Grandparent-Grandchild Exclusions.

Under Government Code section 15606, subdivision (c), the Board is authorized to prescribe rules and regulations to govern local boards of equalization and assessment appeals boards when equalizing and county assessors when assessing. The Board proposes to adopt Property Tax Rule 462.520, *Exclusion from Change in Ownership – Intergenerational Transfers* to implement, interpret, and make specific the change in ownership provisions instituted by Prop 19. In particular, Property Tax Rule 462.520 implements, interprets, and makes specific California Constitution, Article XIII A, section 2.1, subdivision (c), which provides that:

(c) Property Tax Fairness for Family Homes. Notwithstanding any other provision of this Constitution or any other law, beginning on and after February 16, 2021, the following shall apply:

(1) For purposes of subdivision (a) of Section 2, the terms “purchased” and “change in ownership” do not include the purchase or transfer of a family home of the transferor in the case of a transfer between parents and their children, as defined by the Legislature, if the property continues as the family home of the transferee. This subdivision shall apply to both voluntary transfers and transfers resulting from a court order or judicial decree. The new taxable value of the family home of the transferee shall be the sum of both of the following:

(A) The taxable value of the family home, subject to adjustment as authorized by subdivision (b) of Section 2, determined as of the date immediately prior to the date of the purchase by, or transfer to, the transferee.

(B) The applicable of the following amounts:

(i) If the assessed value of the family home upon purchase by, or transfer to, the transferee is less than the sum of the taxable value described in subparagraph (A) plus one million dollars (\$1,000,000), then zero dollars (\$0).

(ii) If the assessed value of the family home upon purchase by, or transfer to, the transferee is equal to or more than the sum of the taxable value described in subparagraph (A) plus one million dollars (\$1,000,000), an amount equal to the assessed value of the family home upon purchase by, or transfer to, the transferee, minus the sum of the taxable value described in subparagraph (A) and one million dollars (\$1,000,000).

(2) Paragraph (1) shall also apply to a purchase or transfer of the family home between grandparents and their grandchildren if all of the parents of those grandchildren, who qualify as children of the grandparents, are deceased as of the date of the purchase or transfer.

(3) Paragraphs (1) and (2) shall also apply to the purchase or transfer of a family farm. For purposes of this paragraph, any reference to a “family home” in paragraph (1) or (2) shall be deemed to instead refer to a “family farm.”

(4) Beginning on February 16, 2023, and every other February 16 thereafter, the State Board of Equalization shall adjust the one million dollar (\$1,000,000) amount described in paragraph (1) for inflation to reflect the percentage change in the House Price Index for California for the prior calendar year, as determined by the Federal Housing Finance Agency. The State Board of Equalization shall calculate and publish the adjustments required by this paragraph.

(5) (A) Subject to subparagraph (B), in order to receive the property tax benefit provided by this section for the purchase or transfer of a family home, the transferee shall claim the homeowner’s exemption or disabled veteran’s exemption at the time of the purchase or transfer of the family home.

(B) A transferee who fails to claim the homeowner's exemption or disabled veteran's exemption at the time of the purchase or transfer of the family home may receive the property tax benefit provided by this section by claiming the homeowner's exemption or disabled veteran's exemption within one year of the purchase or transfer of the family home and shall be entitled to a refund of taxes previously owed or paid between the date of the transfer and the date the transferee claims the homeowner's exemption or disabled veteran's exemption.

Property Tax Rule 462.520 also implements, interprets, and makes specific Section 2.1, subdivision (e), which provides, in relevant part, that:

(e) For purposes of this section:

(1) "Disabled veteran's exemption" means the exemption authorized by subdivision (a) of Section 4 of Article XIII.

(2) "Family farm" means any real property which is under cultivation or which is being used for pasture or grazing, or that is used to produce any agricultural commodity, as that term is defined in Section 51201 of the Government Code as that section read on January 1, 2020.

(3) "Family home" has the same meaning as "principal residence," as that term is used in subdivision (k) of Section 3 of Article XIII.

(4) "Full cash value" has the same meaning as defined in subdivision (a) of Section 2.

(5) "Homeowner's exemption" means the exemption provided by subdivision (k) of Section 3 of Article XIII.

(6) "Natural disaster" means the existence, as declared by the Governor, of conditions of disaster or extreme peril to the safety of persons or property within the affected area caused by conditions such as fire, flood, drought, storm, mudslide, earthquake, civil disorder, foreign invasion, or volcanic eruption.

(7) "Primary residence" means a residence eligible for either of the following:

(A) The homeowner's exemption.

(B) The disabled veteran's exemption.

(8) "Principal residence" as used in subdivision (b) has the same meaning as that term is used in subdivision (a) of Section 2.

(9) "Replacement primary residence" has the same meaning as "replacement dwelling," as that term is defined in subdivision (a) of Section 2.

(10) “Taxable value” means the base year value determined in accordance with subdivision (a) of Section 2 plus any adjustment authorized by subdivision (b) of Section 2.

Here, the relevant Proposition 19 provisions became effective as of February 16, 2021. The Board seeks to promulgate new Property Tax Rule 462.520 to provide clarity of the relevant provisions within Section 2.1 of article XIII A of the California Constitution. Specifically, the Board is proposing this rule to implement, interpret, and make specific subdivisions (c) and (e) of section 2.1 of article XIII A of the California Constitution. Proposed Rule 462.520, subdivision (a) makes explicit or provides clarification for specific provisions of Section 2.1, subdivision (c), including:

- That the transferred property must continue to be the principal residence or family farm of an eligible transferee or the exclusion is removed;
- That the transferred property must become the principal residence or family farm of a subsequent eligible transferee within one year of the initial eligible transferee in order for the exclusion to be retained;,
- That a claim for a family farm can be filed separately from a claim for a principal residence;
- That the parent of a child must be deceased for the transfer of the property, between a grandparent and grandchild, to be excluded, but not the son-in-law or daughter-in-law of the grandparent;
- That there is no limit on the number of principal residences or family farms of a transferor that may be transferred to an eligible transferee and excluded; and
- Filing requirements

Importantly, the proposed rule provides clarification for valuation of real property under the intergenerational transfer exclusion. In subdivision (b)(1), the Proposed Rule explains that a new base year value is calculated upon transfer of real property, but subdivision (b)(2) explains that if the qualifications for exclusion enumerated in subdivision (a) are met, the property will be assessed at its New Taxable Value as provided in Section 2.1, subdivisions (c)(1) to (c)(3) rather than at its new base year value. Subdivision (b)(3) explains the consequences to taxable value when the real property is no longer the principal residence of an eligible transferee. Examples 1 and 2 demonstrate the calculation of the new base year value of the property. The calculation of the New Taxable Value, which applies when the requirements for the intergenerational transfer exclusion have been met, is demonstrated under various scenarios in Examples 3 to 6.

The calculation of the assessed value when the intergenerational transfer exclusion is removed is explained in subdivision (d). Examples 7 and 8 illustrate the change in value when the eligible transferee no longer uses the property as a family home, when another eligible transferee moves in within one year and uses the property as a family home, when an eligible transferee transfers his interest to another eligible transferee, and when the transferor only transfers a portion of their property interest.

Subdivision (e) of the Proposed Rule provides definitions for terms used throughout the Rule and which are required for its implementation. It includes certain definitions (such as “family farm”,

and “homeowner’s exemption”) or clarifies other definitions (such as “full cash value” and “principal residence”) that are found within Section 2.1, subdivision (e).

The Proposed Rule is reasonably necessary to carry out the purpose of clarifying the relevant provisions of Proposition 19 so that individuals may more easily comply with and assessors may more easily administer Proposition 19. Further, the Proposed Rule is reasonably necessary for uniformity of administration amongst the 58 California Assessors.

DOCUMENTS RELIED UPON

The Board relied upon Assembly Constitutional Amendment Number 11 (ACA 11), legislative analyses for ACA 11, the Proposition 19 ballot pamphlet, the January 8, 2021 Chief Counsel Memorandum, the Letters to Assessors Nos. 2020/061 (dated Dec. 11, 2020), 2021/007 (dated Feb. 5, 2021), 2021/008 (dated Feb. 16, 2021), and 2021/010 (dated March 5, 2021), comments received in response to LTA 2021/010 (dated March 5, 2021), and related correspondence submitted for and comments made during the Board’s Discussion of the issues at its December 17, 2020, January 14-15, 2021, and February 11, 2021 meetings in deciding to propose the new rule described above.

ALTERNATIVES CONSIDERED

The Board considered whether to begin the formal rulemaking process to adopt the proposed property tax rule, to issue some form of informal guidance or, alternatively, whether to take no action at this time. The Board decided to begin the formal rulemaking process to adopt the proposed property tax rule at this time because the Board determined that the proposed new property tax rule is reasonably necessary for the reasons set forth above.

The Board did not reject any reasonable alternative to the proposed property tax rule that would lessen any adverse impact the proposed action may have on small business or that would be less burdensome and equally effective in achieving the purpose of the proposed action. No reasonable alternative has been identified and brought to the Board’s attention that would lessen any adverse impact the proposed action may have on small business, be more effective in carrying out the purpose for which the action is proposed, would be as effective and less burdensome to affected private persons that the proposed action, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or other provision of law than the proposed action.

INFORMATION REQUIRED BY GOVERNMENT CODE SECTION 11346.2, SUBDIVISION (b)(5) AND ECONOMIC IMPACT ASSESSMENT REQUIRED BY GOVERNMENT CODE SECTION 11346.3, SUBDIVISION (b), AND DETERMINATIONS AND ESTIMATE REQUIRED BY GOVERNMENT CODE 11346.5 SUBDIVISIONS (a)(5), (6), AND (8)

Section 2.1, subdivision (c) may, arguably, create a large impact for many Californians. This proposed property tax rule, however, merely implements, interprets, and makes specific Section 2.1, subdivision (c)’s provisions. Thus, the Board anticipates limited certain costs related to the

communication and implementation of this regulation. The Board anticipates a one-time absorbable cost to the State Board of Equalization of \$856 to update its website, issue letters regarding this rule to interested parties, and to train county assessors on how to assess property under this rule after the proposed Rule is completed. Even though county assessors' offices will be required to process claims for the intergenerational transfer exclusion, they are already required to process the parent-child exclusion and grandparent-grandchild exclusion claims, and will be required to process the intergenerational transfer exclusion even in the absence of this Proposed Rule. The Board does not believe that the processing of the intergenerational transfer exclusion claims will lead to an ascertainable difference of claim volume for the county assessors' offices. In the long term, the Board believes that because the qualification for the intergenerational exclusion is narrower, the number of claims may decrease leading to decreased processing times for county assessors.

Since this regulation interprets, clarifies, and implements Section 2.1, subdivision (c), which provides for a property tax exclusion for transfers of family homes or family farms between parents and their children and grandparents and their grandchildren, it does not impact the majority of small businesses as defined in Government Code section 11346.3, subdivision (b)(4)(B), except for businesses involving family farm property owned by individuals. However, the primary economic impact would not be on the business operations of the family farm but rather on considerations to whom the family farm will be transferred. Further, the majority of any such impact stem from the provisions of Section 2.1, subdivision (c), not this proposed regulation. Any impact that may exist on family farms as a result of this rule is indeterminable since it is not possible to estimate the effect of what a family farm owner might do in the future vis-a-vis their family farm operations knowing now that they must transfer the family farm to an eligible transferee to qualify for the exclusion.

This regulation is not expected to create or eliminate jobs within the state. The Board likewise does not expect any creation of new business or elimination of existing businesses within the state, nor does it expect an expansion of businesses currently doing business within the state. The Board expects that the adoption of the Proposed Rule will not affect the benefits of the rule to the health and welfare of California residents, worker safety, or the state's environment.

The forgoing information also provides the factual basis for the Board's initial determination that the adoption of the Proposed Amendments will not have a significant adverse economic impact on business.