SENATE COMMITTEE ON APPROPRIATIONS
Senator Anthony Portantino, Chair
2021 - 2022 Regular Session

AB 1933 (Friedman) - Property taxation: welfare exemption: nonprofit corporation: low-income families

Version: June 28, 2022
Urgency: No
Hearing Date: August 1, 2022

Policy Vote: GOV. & F. 5 - 0
Mandate: Yes
Consultant: Robert Ingenito

Bill Summary: AB 1933 would add a new welfare exemption from property tax for charitable organizations that develop affordable housing subject to a recorded agreement with a local agency.

Fiscal Impact:

- The Board of Equalization (BOE) indicates that it would incur minor and absorbable administrative costs to update claim forms, the Assessors Handbook, and Publication 149: Property Tax Welfare Exemption.

- BOE indicates that this bill would result in lower property taxes in the near-term, which would be more than offset by higher property tax revenues in the long run (See Staff Comments); however, the respective magnitudes are unknown. Lower local property tax revenues lead to increased General Fund Proposition 98 spending by up to roughly 50 percent (the exact amount depends on the specific amount of the annual Proposition 98 guarantee, which in turns depends upon a variety of economic, demographic and budgetary factors).

- By changing the manner in which assessors value real property, this bill creates a state-mandated local program. To the extent the Commission on State Mandates determines that the provisions of this bill create a new program or impose a higher level of service on local agencies, local agencies could claim reimbursement of those costs (General Fund). The magnitude of these costs is unknown.

Background: Under the California Constitution, all property is taxable unless explicitly exempted by the Constitution or federal law. In addition, the Constitution permits the Legislature to exempt property used exclusively for charitable purposes so long as it is owned by non-profit entities organized and operated for charitable purposes, such as universities, hospitals, and libraries (commonly referred to as the “welfare exemption”).

The welfare exemption includes property used for rental housing, if it meets several requirements, including that there is an enforceable and verifiable agreement with a public agency, a recorded deed restriction, or other legal document that restricts the project’s usage, and provides that the units designated for use by lower income households are continuously available to or occupied by lower income households. For projects with both low-income and market rate units, the owner can claim a partial exemption, equal to that percentage of the value of the property equal to the percentage that the number of units serving lower income households represents of the total number of residential units.

The Constitution also exempts from taxation buildings under construction, land required for its convenient use, and equipment in the building if its intended use qualifies for the exemption, for several Constitutional exempt purposes, including the welfare exemption. State law implements this Constitutional provision to apply the exemption to facilities in the course of construction together with the land on which the facilities are located as may be required for their convenient use and occupation. As long as construction has started, state law can consider the property exempt, unless construction is subsequently abandoned; reasonable delays in construction are usually not considered abandonment.

The welfare exemption generally applies to property owned by qualified nonprofit organizations used exclusively for charitable purposes. In two instances, the Legislature has allowed charitable organizations to claim the exemption for vacant land subsequently developed into housing for subsequent purchase by income-eligible individuals. First, the "Habitat for Humanity" exemption (AB 1559, Wiggins, 1999), to allow the welfare exemption to also apply to property that is owned and operated by a nonprofit corporation, which is organized and operated for the specific and primary purpose of building and rehabilitating single or multifamily residences for sale at cost to low-income families, and (2) the sale of which is financed by a zero interest rate loan and without regard to religion, race, national origin, or the sex of the head of household.

Second, the Community Land Trust (CLT) welfare exemption applies to property owned by a community land trust, under the following circumstances (SB 196, Beall, 2018): (1) the property is being or will be developed or rehabilitated as an owner-occupied single-family dwelling, unit in a multifamily dwelling, a member-occupied unit in a limited equity housing cooperative, or as a rental housing development, (2) improvements on the property are or will be available for use and ownership or for rent by persons and families of low or moderate income, including persons and families of low or moderate income that own a dwelling or unit collectively as member occupants or resident shareholders of a limited equity housing cooperative, and (3) a deed restriction or other instrument, requiring a contract or contracts serving as an enforceable restriction on the sale or resale value of owner-occupied units or on the affordability of rental units is recorded on or before the lien date following the acquisition of the property by the community land trust.

SB 196 made the community land trust liable for property taxes in years the property was exempt if the CLT does not develop or rehabilitate it within five years of the lien date following the CLT's acquisition of the property. The exemption is due to sunset after the January 1, 2025 lien date.

AB 1559 and SB 196 apply to very specific models for developing affordable housing, so do not include other potential ways of doing so. Heritage Housing Partners (HHP) is a 501(c)(3) non-profit that builds and sells affordable units to very low, low, and moderate income, first-time homebuyers in the Los Angeles Area. Prospective homebuyers procure a first mortgage on their own, and then HHP uses public sector subsidies to pay the difference between the full cost of development and its "affordable sales price," an amount determined for each unit that ensures the typical buyer does not spend more than 35% of his or her monthly total income on housing expense. The homebuyer must make a down payment of around 5% and pay closing costs of 3%. At sale, the public sector subsidy is recast as a non-performing, zero interest junior loan with a 30-45 year repayment to the homebuyer. The homebuyer only pays principal and interest payments on the conventional first mortgage; however, because the home can only be sold to another income-qualified, first-time homebuyer, any gain is limited to the gain in the “affordable sales price” between purchase and sale. Because the Habitat for Humanity exemption requires a zero interest rate loan, and HHP homebuyers obtain a conventional one, their projects do not qualify for an exemption. Neither do they qualify for the CLT exemption because HHP is not a CLT.

Proposed Law: This bill, among other things, would do the following:

- Provide, for lien dates occurring on or after January 1, 2023, and before January 1, 2028, that property is fully exempt from property taxation and is also within that welfare exemption if that property is owned and operated by a nonprofit corporation, as described, that is organized and operated for the specific and primary purpose of building and rehabilitating single or multifamily residential units and the-property has units that meet specified requirements.

- Limit the exemption to the portion of the property proposed to be built or rehabilitated with units meeting the requirements and would limit, following completion of construction, the exemption to the portion of the property with units that meet the requirements, as specified.

- Prohibit the denial of this exemption for property not previously designated as open space on the basis that the property does not currently include a single or multifamily residential unit, as described, or a single or multifamily residential unit, as described, that is in the course of construction.

- Require a nonprofit corporation that utilizes this welfare exemption to be subject to an annual independent audit and to make the audit available to specified entities in order to continue to qualify for the exemption.

- Make a nonprofit corporation liable for property tax for the years for which the property was exempt from taxation pursuant to the bill’s provisions if the property was not developed or rehabilitated, or if the development or rehabilitation is not in the course of construction, by specified dates depending on the date the nonprofit corporation acquired the property.

- Require a nonprofit corporation claiming the exemption to sign under penalty of perjury an affidavit affirming to the county assessor that the property owned and operated by the nonprofit corporation is for the future construction of single or multifamily residential units on that property, as described.

- Require BOE to annually collect and report to the Legislature, by June 1, 2025, and every June 1 thereafter until June 1, 2028, data from county assessors to quantify the amount of assessed value exempted and the number of owner-occupied dwelling units created by nonprofits granted the exemption in the bill.

> The bill would require nonprofits to provide information to county assessors about the additional dwelling units created under the exemption.

Staff Comments: BOE notes that "estimating the future revenue impact of this bill is difficult as it is unknown how many properties would be subject to the bill, the number of units sold, the sale price of those units, the purchase price of the development property, construction time and the amount of tax that would be paid during the construction phase." As an example of how the revenue impact of the bill would work over time, BOE staff offer the following:

> The bill's sponsors provided data for 11 housing development projects (all located in Los Angeles County) that they have built dating back to 2005 including the development locations, sum of property taxes paid by the sponsor during the course of construction, and the property taxes paid by the new homeowners. This data can be used to hypothetically map out the revenue impacts of this bill.
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> BOE staff analyzed three of the 11 developments that seemed to be strictly low-income and found they were in the course of construction for 5, 6 and 5 years, respectively. During that time, the bill's sponsors reported they paid $130,575 in local property taxes for these low-income developments. Under this bill, 100 percent of this would qualify for the welfare exemption. If the exemption applied to these developments with an average construction time of 5 years, Los Angeles County would have lost an average of $26,115 in local property tax revenue. Upon completion of construction, the sponsor sold all units to low-income homebuyers and the property's net assessed value increased due to the new construction. The units in the analysis above were sold from (1) July 2011 to August 2011, and (2) August 2020 to October 2020.
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> Since these units were sold, the bill's sponsors estimate based on the property's net assessed value that homeowners have paid $233,785 in local property taxes over the time period from when the units were sold. When adding the homeowner property tax payments to the amount of tax that would be exempted, BOE staff estimated a net local property tax revenue gain of approximately $103,210.

Any local government costs resulting from the non-assessor mandates in this measure are not state-reimbursable because the mandate only involves the definition of a crime or the penalty for conviction of a crime.

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