November 29, 2021

Hon. Rob Bonta
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Anabel Renteria
Initiative Coordinator

Dear Attorney General Bonta:

Pursuant to Elections Code Section 9005, we have reviewed the proposed constitutional and statutory Tax Cut and Housing Affordability Act of 2022 initiative (A.G. File No. 21-0032, Amendment #1).

Background

Property Taxes and Income Tax Credits

Local Governments Collect Property Taxes From Property Owners. California local governments—cities, counties, schools, and special districts—levy property taxes on property owners. Property taxes are paid based on the taxable value of the property. Property taxes are a major revenue source for local governments, raising about $75 billion per year statewide.

How Is a Property Tax Bill Calculated? Each property owner's annual property tax bill is equal to the taxable value of their property multiplied by their property tax rate. The typical property owner's property tax rate is 1.1 percent. In the year a new owner takes over a property, its taxable value typically is its purchase price. Each year after that, the property's taxable value is adjusted for inflation by up to 2 percent. When a property changes ownership again, its taxable value typically is reset to its new—usually higher—purchase price.

Homeowners' Exemption Reduces Taxable Value of Primary Homes. A state law, known as the homeowners' exemption, reduces the taxable value of primary homes by $7,000. This typically reduces a homeowner's tax payment by about $80 annually. The state reimburses local governments for their property tax losses from the homeowners' exemption, which total around $400 million per year.

Counties Manage the Property Tax. County assessors determine the taxable value of property. County tax collectors bill property owners and collect payments. County auditors distribute tax revenue to local governments. Statewide, counties spend about $800 million each year on these activities.

Legislative Analyst's Office
California Legislature
Gabriel Petek, Legislative Analyst
925 L Street, Suite 1000, Sacramento, CA 95814
(916) 445-4656

California Taxes Personal Income. The state collects a personal income tax on income earned within the state. The personal income tax raises over $120 billion each year.

Renters Can Receive an Income Tax Credit. Low-income renters may claim the renters' tax credit, which reduces how much income tax they owe. Single renters with incomes of less than about $43,500 can claim a renters' credit of up to $60. Married couples and heads of households with incomes of less than about $87,000 can claim a credit of up to $120. The amount of the renters' credit may not exceed how much tax someone owes. The renters' credit reduces state income tax revenues by about $150 million annually.

Local Land Use Authority and Housing Approval Process

Local Land Use Responsibilities. California's cities and counties make most decisions about when, where, and to what extent housing will be built. The state requires cities and counties to carry out certain planning exercises in an attempt to ensure they accommodate needed home building.

Housing Developers Must Obtain City or County Approval. Before housing developers can build new housing, they generally must obtain one or more permits from city or county planning departments and, in many cases, must also obtain approval from local planning commissions and city councils or county boards of supervisors.

Some Projects Permitted Via an Administrative Process. Some housing projects can be permitted by city or county planning staff without further approval from elected officials. These projects are typically referred to as "by right." By-right projects require only an administrative review designed to ensure they are consistent with existing local laws and building standards.

Additional Public Review Often Required. Most large housing projects and some other smaller projects are not allowed by right. Instead, these projects are vetted through both public hearings and administrative review. In addition, local planning commissions and, in some cases, elected city councils or county boards of supervisors must give their consent. This additional review typically makes it longer for those housing projects to be approved.

Proposal

Increases Homeowners' Property Tax Exemption. The measure increases the homeowners' exemption from $7,000 to $200,000. This would increase the reduction to a typical homeowner's property tax payment from around $80 to roughly $2,200 per year. The measure would require the amount of the exemption to increase annually by 2 percent or the rate of inflation, whichever is lower.

Increases Renters' Income Tax Credit. The measure increases the renters' tax credit to $1,000 per year for single renters that earn $200,000 or less annually and $2,000 per year for married couples and heads of households that earn $400,000 or less annually. These amounts would be increased annually by 2 percent or the rate of inflation, whichever is lower.

Establishes a Property Tax Surcharge. The measure establishes an annual property tax surcharge on most properties with a taxable value over $4 million. Properties with a taxable value over $5 million would be assessed a 1 percent surcharge, while the surcharge would be adjusted downward for properties with a taxable value between $4 million and $5 million. The measure exempts some high-value properties like land used for commercial agriculture and parks.

Provides Reimbursements to State and Local Governments. The measure says that the surcharge revenue can be used for only three purposes: (1) reimburse local governments for their property tax losses from the increase to the homeowners' exemption, (2) reimburse the state for the income tax losses from the measure, and (3) reimburse the state and local governments for their costs of carrying out the measure. If the surcharge does not raise enough to cover these costs, it can be adjusted up to 1.2 percent. If that is not enough, the homeowners' exemption and renters' credit would be reduced so that the surcharge can cover the costs. Alternatively, if in the previous three years the surcharge revenue significantly exceeded the amount of revenue needed to cover costs, the measure requires the excess funds be refunded to qualified renters. The measure also allows the state to borrow for up to three years against the surcharge revenue to cover the cost of state and local reimbursements.

Establishes Administrative Approval Process for Certain Housing Projects. The measure would require local governments to provide by-right approval of housing projects that abide by local requirements and that meet two conditions: (1) new housing projects that set aside at least half of the units for middle- and working-class households and (2) projects proposed on a site that the city or county has designated for regionally needed housing. While approval of housing projects that meet the criteria generally would be required without discretionary review or a public hearing, the measure would allow a local government to deny or require modifications of housing projects that create *specific* adverse impacts on public health or safety. The measure also establishes a review process for projects seeking by-right approval, including setting timeliness for local government review and allowing for appeals of project denials.

Revenues Exempt From State Spending Limit and Minimum Education Funding Levels. The State Constitution contains various rules affecting the state budget. For example, the State Constitution specifies a state spending limit and requires a minimum level of annual funding for K-12 education and the California Community Colleges. This measure would amend the State Constitution to exempt the measure's revenues and spending from these constitutional requirements.

Fiscal Effects

Increased Revenue Resulting From Property Tax Surcharge. Most owners of property with a taxable value of more than $4 million would pay higher property taxes due to the property tax surcharge. The tax rate would be set to collect enough money to cover the costs of the measure. This means the property tax surcharge probably would raise between $16 billion and $19 billion annually.

Increased State and Local Government Costs. The measure sets aside the revenue derived from the property tax surcharge to reimburse the state and local governments for the various costs and revenue losses created by the measure:

- ***Increased State Costs to Reimburse for Homeowners' Exemption.*** By increasing the homeowners' exemption, the measure would reduce local property tax revenues statewide by $12 billion to $14 billion annually. State costs to reimburse local governments for these losses would increase by the same amount.
- ***State Revenues Losses From Renters' Credit.*** Expanding the renters' tax credit would reduce state income tax revenues, likely by about $4 billion annually. These revenue losses would be higher in years when the measure requires the state to pay additional tax

refunds to certain renters. The amount of these additional costs is unknown and would vary from year to year.

- ***Increases County Administrative Costs.*** By requiring new and expanded responsibilities for county assessors and other county officials, the measure likely would result in costs of tens of millions of dollars annually.

Local Fiscal Effects Associated With By-Right Housing Approval Process. Local governments would incur minimal, one-time costs to establish the administrative housing project approval processes required by the measure. If the measure spurs additional housing development, local governments could experience some unknown level of economic growth.

State Appropriations Limit Considerations. The State Constitution limits how much tax revenues the state can spend each year. However, certain types of spending, like some funding to local governments, are excluded from this limit. In recent years, the limit has been an important consideration in state budgeting decisions. Because this measure would require the state to provide local governments with more funding, depending on how it were implemented, this measure could increase the amount the state spends on excluded purposes by roughly $12 billion to $14 billion. As a result, it could significantly increase the amount of revenue the state spends on purposes excluded from the limit. Spending more on purposes excluded from the limit would reduce the chances the state spends revenues in excess of the limit. Revenues in excess of the limit, over a two-year period, trigger a requirement for taxpayer rebates and additional school payments.

Summary of Fiscal Effects. We estimate that this measure would have the following major fiscal effects.

- Increased property taxes on property with a taxable value of more than $4 million providing $16 billion to $19 billion in new revenue.

- Increased state costs resulting from the increases to the homeowners' property tax exemption and renters' tax credit. Increased costs to local governments for carrying out the measure. Total costs would be $16 billion to $19 billion annually and likely would be fully offset by revenue from increased property taxes on higher value properties.

Sincerely,

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for Gabriel Petek
Legislative Analyst

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for Keely Martin Bosler
Director of Finance