STATE OF CALIFORNIA

CALIFORNIA DEPARTMENT OF TAX AND FEE ADMINISTRATION
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GAVIN NEWSOM
Governor

YOLANDA RICHARDSON
Secretary, Government Operations Agency

NICOLAS MADUROS
Director

August 27, 2021

Dear Interested Party:

Enclosed is the Discussion Paper on proposed Regulation 35401, *Registration, Reporting, and Reimbursement*. We would like to invite you to discuss the issue and present any additional suggestions or comments. Accordingly, a virtual interested parties meeting is scheduled as follows:

September 8, 2021
10 a.m.
(Microsoft Teams)

You may join us on your computer or mobile app through Microsoft Teams or by calling 1-916-535-0987 and then entering the conference identification number 330 096 518. You are also welcome to submit your comments to me at the address or fax number in this letterhead or via email at BTFD-BTC.InformationRequests@cdtfa.ca.gov by September 24, 2021. You should submit written comments including proposed language if you have suggestions you would like considered during this process. Copies of the materials you submit may be provided to other interested parties, therefore, ensure your comments do not contain confidential information. Please feel free to publish this information on your website or distribute it to others that may be interested in participating in the meeting or presenting their comments.

If you are interested in other Business Taxes Committee topics refer to the CDTFA webpage at (http://www.cdtfa.ca.gov/taxes-and-fees/business-taxes-committee.htm) for copies of discussion papers and calendars of current and prior issues.

Thank you for your consideration. We look forward to your comments and suggestions. Should you have any questions, please feel free to contact Business Taxes Committee team member Robert Wilke at 1-916-309-5302, who will be leading the meeting.

Sincerely,

Aimee Olhiser

Aimee Olhiser, Chief
Tax Policy Bureau
Business Tax and Fee Division

AO:rsw

Enclosures

cc: (all with enclosures)
Mr. Nicolas Maduros (MIC 104)
Ms. Trista Gonzalez (MIC 104)
Mr. Robert Tucker (MIC 83)
Ms. Susanne Buehler (MIC 43)
Ms. Michele Pielsticker Linton (MIC 105)
Mr. Jason Mallet (MIC 25)
Mr. Robert Colivas (MIC 47)
Mr. Bill Hain (MIC 70)
Mr. James Dahlen (MIC 57)
Mr. Jason Parker (MIC 49)
Mr. Steven Mercer (MIC 25)
Ms. Ester Cabrera (MIC 23)
Mr. Jeff Vest (MIC 85)
Mr. Mike Loretta (MIC 42)
Ms. Pamela Bergin (MIC 82)
Mr. Bradley Heller (MIC 82)
Mr. David Levine (MIC 85)
Ms. Dana Brown (MIC 85)
Ms. Casey Tichy (MIC 85)
Ms. Elaine Chu Redman (MIC 82)
Ms. Mari Guzman (MIC 82)
Ms. Lynn Whitaker (MIC 50)
Mr. Chris Davis (MIC 40)
Ms. Valerie Yagen (MIC 40)
Mr. Gentian Droboniku (MIC 67)
Mr. Tom Trach (MIC 67)
Ms. Christine Castillo (MIC 104)
Mr. Marc Alviso (MIC 104)
Ms. Claudette Yang (MIC 104)
Ms. Karina Magana (MIC 47)
Mr. Bradley Miller (MIC 92)
Ms. Jo Trillo (MIC 40)
Ms. Hardeep Heer (MIC 40)
Mr. Robert Prasad (MIC 50)
Mr. Robert Wilke (MIC 50)

DISCUSSION PAPER
Proposed Regulation 35401, *Registration, Reporting, and Reimbursement*

Issue

The California Department of Tax and Fee Administration (Department) proposes to adopt Regulation 35401, *Registration, Reporting, and Reimbursement*, to implement, interpret, and make specific section 2.3 of article XIII A of the California Constitution.

Overview

The Background section provides relevant background information regarding inter-county base year value transfers, the parent-child and grandparent-grandchild transfer exclusions, and the changes to state law made by Assembly Constitutional Amendment No. 11 (2019-2020 Reg. Sess.) (ACA 11), the Home Protection for Seniors, Severely Disabled, Families, and Victims of Wildfire or Natural Disasters Act, which was placed on the ballot as Proposition 19, approved by the voters at the November 3, 2020, Statewide General Election, and added sections 2.1, 2.2, and 2.3 to article XIII A of the California Constitution effective December 16, 2020. Then, the Discussion section discusses the proposed regulation, which:

- Requires each county to register with the Department to report the gains it is required to annually determine for the county and each local agency in the county under subdivision (a) of section 2.3;
- Clarifies the determination periods for which each county shall annually determine the gains;
- Specifies the dates by which each county shall annually determine the gains;
- Requires each county to report its gains to the Department by specified reporting due dates every three years; and
- Clarifies how the Department will use the gains reported by the counties to determine each county's and local agency's aggregate gain every three years and provide reimbursement to each county and local agency with an aggregate negative gain from the money in the County Revenue Protection Fund under subdivision (c) of section 2.3.

Background

Base Year Value

Section 1 of article XIII A of the California Constitution[1] generally limits the maximum amount of ad valorem taxes on real property to one percent of the full cash value of that property, and requires this tax to be collected by the counties and apportioned according to law to the districts within the counties. Section 2 generally defines full cash value as the appraised value of the real property when purchased, newly constructed, or a change in ownership has occurred. It authorizes the full cash value base to be adjusted by an annual inflationary rate not to exceed two percent. It also authorizes the full cash value to be reduced to reflect substantial damage, destruction, or other factors causing a decline in value.

[1] All further section references are to sections in article XIII A of the California Constitution, unless otherwise indicated.

For purposes of section 2, Revenue and Taxation Code (RTC) section 110.1, subdivisions (a) and (b), generally provide that the base year value for real property is the "full cash value" or fair market value of the property as determined pursuant to RTC section 110 on the 1975 lien date or, after the 1975 lien date, the date of the most recent change in ownership of the property or the date of completion of new construction. RTC section 110.1, subdivision (f), requires the base year value of real property to be adjusted by an inflation factor for each lien date[2] after the lien date in which the base year value is determined, and that adjusted value is known as the adjusted base year value. Also, RTC section 51 prohibits the inflation factor from exceeding two percent of the prior year's value. RTC section 51 further provides, for purposes of section 2, that for each lien date after the lien date in which the base year value is determined, the taxable value of real property is generally the lesser of: (1) the adjusted base year value or (2) its full cash value, as defined in RTC section 110, as of the lien date, taking into account reductions in value due to damage, destruction, depreciation, obsolescence, removal of property, or other factors causing a decline in value.

Base Year Value Transfers

Section 2, subdivision (a), authorizes the Legislature to enact legislation that allows a person over 55 years of age or any severely and permanently disabled person residing in property eligible for the homeowner's exemption under article XIII, section 3, subdivision (k), to transfer the property's adjusted base year value to a replacement dwelling of equal or lesser value located in the same county or another county that has adopted an ordinance allowing in-bound base year value transfers from other counties.[3] Pursuant to that constitutional authorization, the Legislature enacted RTC section 69.5 to allow those base year value transfers when certain conditions are met and a claimant files a timely claim with the county assessor that provides specified information, including the address and, if known, the assessor's parcel number of the original property (RTC, § 69.5, subd. (f)). RTC section 69.5 requires the replacement property to be acquired or newly constructed as the principal residence of the person within two years after the sale of the original property. It requires the replacement property's full cash value to be equal to or less than:

- 100 percent of the original property's full cash value if purchased or newly constructed prior to the sale of the original property;
- 105 percent of the original property's full cash value if purchased or newly constructed within one year following the sale of the original property; and
- 110 percent of the original property's full cash value if purchased or newly constructed within the second year following the sale of the original property.

Additionally, RTC section 69.5 only allows a person to make one base year value transfer unless the person was granted relief as a person over 55 years of age and subsequently became severely and permanently disabled.

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[2] RTC section 2192 provides, except as otherwise specified, all tax liens attach annually as of 12:01 a.m. on the first day of January preceding the fiscal year for which the taxes are levied.

[3] According to the State Board of Equalization's (BOE's) website, as of November 7, 2018, the following 10 counties have ordinances enabling the intercounty base year value transfers: Alameda, Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Mateo, Santa Clara, Tuolumne, and Ventura. (www.boe.ca.gov/proptaxes/prop60-90_55over.htm.)

Section 2, subdivision (e), requires the Legislature to enact legislation that allows the base year value of property that is substantially damaged or destroyed by a disaster, as declared by the Governor, to be transferred to comparable property within the same county that is acquired or newly constructed as a replacement for the substantially damaged or destroyed property. Section 2, subdivision (e), also authorizes the Legislature to enact legislation authorizing counties to adopt ordinances allowing similar in-bound base year value transfers if the replacement property is of equal or less value and acquired or newly constructed within three years of the substantial damage or destruction to the original property.[4] The Legislature enacted RTC sections 69 and 69.3 to allow these intra-county and inter-county base year value transfers, respectively.

RTC section 69.3 requires the replacement property for inter-county transfers to be acquired or newly constructed within three years after the damage or destruction of the original property. RTC section 69.3 provides for the transfer of the damaged or destroyed property's adjusted base year value to the replacement property if a claim for relief is filed by the owner with the assessor of the county in which the replacement property is located within three years after the replacement property is acquired or newly constructed (RTC, § 69.3, subd. (e)). RTC section 69.3 also requires the replacement property's full cash value to be equal to or less than:

- 105 percent of the original property's full cash value if purchased or newly constructed within the first year following the damage or destruction of the original property;
- 110 percent of the original property's full cash value if purchased or newly constructed within the second year following the damage or destruction of the original property; and
- 115 percent of the original property's full cash value if purchased or newly constructed within the third year following the damage or destruction to the original property.

Parent-Child and Grandparent-Grandchild Transfer Exclusions

Section 2, subdivision (h), provides that the purchase or transfer of the principal residence, and the first one million dollars of the full cash value of other real property, of a transferor in the case of a transfer between parents and their children, or between grandparents and their grandchildren if all the parents of those grandchildren are deceased, is not a "purchase" or "change in ownership" for purposes of determining the "full cash value" of property under section 2. The Legislature enacted RTC section 63.1 to implement the parent-child and grandparent-grandchild transfer exclusions from reassessment and it generally provides that the full cash value of other real property is its adjusted base year value immediately prior to the date of its purchase or transfer (RTC, § 63.1, subd. (c)). RTC section 63.1 generally allows the exclusions as of the date of transfer if a claim is filed with the county assessor for the exclusion (1) within three years after the date of the purchase or transfer of real property for which the claim is filed or prior to the transfer of the real property to a third party, whichever is earlier, or (2) within six months after the date of mailing of a notice of supplemental or escape assessment that is issued as a result of the purchase or transfer of real property for which the claim is filed. (RTC, § 63.1, subd. (e).) RTC section 63.1 also authorizes county assessors to quarterly report all purchases or transfers, other than purchases or transfers

[4] According to the BOE's website, as of May 6, 2021, the following 14 counties had adopted such ordinances: Contra Costa, Glenn, Los Angeles, Modoc, Orange, San Diego, San Francisco, Santa Clara, Solano, Sonoma, Sutter, Ventura, Yolo, and Yuba. (www.boe.ca.gov/proptaxes/disaster-relief.htm#FAQs.)

involving a principal residence, for which a claim for exclusion is made to the BOE to allow the BOE to monitor the one-million-dollar limitation.

<u>Assembly Constitutional Amendment No. 11 (ACA 11)</u>

New Base Year Value Transfer Provisions

As relevant here, section 2.1, subdivision (b), expands base year value transfers by authorizing, beginning on and after April 1, 2021, an owner of a primary residence who is over fifty-five years of age, severely disabled, or a victim of a wildfire or natural disaster to transfer the taxable value, defined as the base year value plus inflation adjustments, of their primary residence to a replacement primary residence located anywhere in the state, regardless of the location or value of the replacement primary residence, that is purchased or newly constructed as that person's principal residence within two years of the sale of the original primary residence. Section 2.1, subdivision (b), limits a person who is over fifty-five years of age or severely disabled to three transfers under these provisions. Section 2.1, subdivision (b), requires a person seeking to transfer the taxable value of their primary residence to file an application with the assessor of the county in which the replacement primary residence is located that includes, at minimum, information comparable to that submitted with a base year value transfer claim under RTC section 69.5. Section 2.1, subdivision (b), also requires the taxable value of the replacement primary residence to be determined based on the value of the original primary residence as follows:

- For any transfer of taxable value to a replacement primary residence of equal or lesser value than the original primary residence, the taxable value of the replacement primary residence is deemed the taxable value of the original primary residence.
- For any transfer of taxable value to a replacement primary residence of greater value than the original primary residence, the taxable value of the replacement primary residence is calculated by adding the difference between the full cash value of the original primary residence and the full cash value of the replacement primary residence to the taxable value of the original primary residence.

Nothing in ACA 11 expressly supersedes the base year value transfer provisions in section 2 as implemented by RTC sections 69, 69.3, or 69.5 (discussed above) and those base year value transfer provisions may continue to apply on and after April 1, 2021.

New Limitations on the Parent-Child and Grandparent-Grandchild Transfer Exclusions

Section 2.1, subdivision (d), makes the parent-child and grandparent-grandchild transfer exclusions under section 2, subdivision (h), and implemented by RTC section 63.1, as discussed above, inoperative as to any purchase or transfer occurring on or after February 16, 2021. Section 2.1, subdivision (c), provides new parent-child and grandparent-grandchild transfer exclusions that apply to purchases and transfers on and after February 16, 2021. The exclusions provided by section 2.1, subdivision (c), only apply to purchases or transfers of a family home or family farm between parents and their children, or between grandparents and their grandchildren if all the parents of those grandchildren are deceased, and require the property to continue as the family home or family farm of the transferee. "Family home" has the same meaning as "principal residence." (Section 2.1, subd. (e)(3).) Section 2.1, subdivision (c), provides that the new taxable value of the family home or family farm is the sum of the taxable value of that property, subject to adjustment as authorized by section 2, determined as of the date immediately prior to the date of the purchase by, or transfer to, the transferee ("prior taxable value") and the following applicable amount:

- If the assessed value of the family home or family farm upon purchase by, or transfer to, the transferee is less than the sum of the prior taxable value plus one million dollars, then zero dollars.
- If the assessed value of the family home or family farm upon purchase by, or transfer to, the transferee is equal to or more than the sum of the prior taxable value plus one million dollars, an amount equal to the assessed value of the family home or family farm upon purchase by, or transfer to, the transferee, minus the sum of the prior taxable value and one million dollars.[5]

To be allowed the exclusion for the purchase or transfer of a family home, the transferee is required to claim the homeowner's exemption provided by article XIII, section 3, subdivision (k), or the disabled veteran's exemption authorized by article XIII, section 4, subdivision (a), on the property within one year of the purchase or transfer. (Section 2.1, subd. (c)(5).) The BOE has advised in a letter to assessors that a transferee will also be required to file a claim with the county assessor by the time frames specified in RTC section 63.1 (described above) for the exclusion to be allowed as of the date of transfer. (BOE Letter to County Assessors No. 2021/008, Proposition 19 Intergenerational Transfer Exclusion Guidance Questions and Answers (Feb. 16, 2021), p. 3.)

Due to section 2.1, subdivision (c), partial parent-child and grandparent-grandchild transfer exclusions may only be allowed on the purchase or transfer of family homes or family farms with an assessed value of over one million dollars,[6] and there is no longer a parent-child or grandparent-grandchild transfer exclusion that applies to the sale or transfer of real property that is not a family home or family farm.

New California Fire Response Fund and County Revenue Protection Fund

Section 2.2 creates the California Fire Response (CFR) Fund and the County Revenue Protection (CRP) Fund in the State Treasury. Section 2.2 requires the Director of Finance to calculate the additional revenues and savings that accrued to the state from the implementation of section 2.1 during the prior fiscal year, on or before September 1, 2022, and each subsequent September 1 thereafter. Section 2.2 also requires the Controller to transfer 75 percent and 15 percent of the amount calculated by the Director of Finance from the General Fund to the CFR Fund and CRP Fund, respectively, by September 15, 2022, and each subsequent September 15 thereafter. Section 2.2, subdivision (b), continuously appropriates moneys in the CRP Fund for the purposes of reimbursing counties and local agencies that incur a negative gain and paying the Department's administrative costs, in accordance with section 2.3 (discussed below).

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[5] Section 2.1 requires the BOE, beginning on February 16, 2023, and every other February 16 thereafter, to adjust the one million dollar amount 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.

[6] See the BOE's website for an example of a partial exclusion due to the taxable value calculation required by section 2.1. (www.boe.ca.gov/prop19/#FAQs.)

Reimbursing Counties and Local Agencies with a Negative Gain

Section 2.3 provides as follows:

> (a) Each county shall annually, no later than the date specified by the California Department of Tax and Fee Administration by regulations adopted pursuant to this section, determine the gain for the county and for each local agency in the county resulting from implementation of Section 2.1 by adding the following amounts:
>
> (1) The revenue increase resulting from the sale and reassessment of original primary residences for outbound intercounty transfers pursuant to subdivision (b) of Section 2.1.
>
> (2) The revenue decrease, which shall be expressed as a negative number, resulting from the transfer of taxable values of original primary residences located in other counties to replacement primary residences located within the county for inbound intercounty transfers pursuant to subdivision (b) of Section 2.1.
>
> (3) The revenue increase resulting from subdivision (c) of Section 2.1.
>
> (b) A county or any local agency in the county that has a positive gain determined pursuant to subdivision (a) shall not be eligible to receive reimbursement from the County Revenue Protection Fund. A county or any local agency in the county that has a negative gain determined pursuant to subdivision (a) shall be deemed to be an eligible local agency entitled to a reimbursement from the County Revenue Protection Fund.
>
> (c) The California Department of Tax and Fee Administration shall determine each eligible local agency's aggregate gain every three years, based on the amounts determined pursuant to subdivision (a) for each of those three years, and provide reimbursement to each eligible local agency with a negative gain from the moneys in the County Revenue Protection Fund equal to that amount. If there are insufficient moneys in that fund to cover the total amount of reimbursements under this section, the California Department of Tax and Fee Administration shall allocate a pro rata share of the moneys in the fund to each eligible local agency based on the amount of the eligible local agency's reimbursement relative to the total amount of reimbursements under this section.
>
> (d) At the end of each three-year period described in subdivision (c), after the California Department of Tax and Fee Administration has reimbursed each eligible local agency that has experienced a negative gain during that three-year period, the Controller shall transfer the remaining balance, if any, in the County Revenue Protection Fund to the General Fund, to be available for appropriation for any purpose.
>
> (e) The California Department of Tax and Fee Administration shall promulgate regulations to implement this section pursuant to the rulemaking provisions of the Administrative Procedure Act (Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code), as may be amended from time to time by the Legislature, or any successor to those provisions.

> (f) For purposes of this section and Section 2.2, an "eligible local agency" is a county, a city, a city and county, a special district, or a school district as determined pursuant to subdivision (o) of Section 42238.02 of the Education Code as it read on January 8, 2020, that has a negative gain as determined pursuant to this section.

As relevant here, section 2.3, subdivision (a), requires each county to annually determine the gain for the county and for each local agency in the county resulting from adding the revenue increases and decreases from out-bound and in-bound base year value transfers under section 2.1, subdivision (b), and the revenue increases from the limitations on the parent-child and grandparent-grandchild transfer exclusions provided by section 2.1, subdivision (c). Subdivision (a) also refers to that total amount as a gain regardless of whether the amount is a positive or negative number.

Section 2.3, subdivision (b), makes a county or local agency in the county that has a positive gain for a determination period, as determined pursuant to subdivision (a), ineligible to receive reimbursement from the CRP Fund for that period. Subdivision (b) also deems a county or any local agency that has a negative gain for a determination period, as determined pursuant to subdivision (a), eligible to receive reimbursement from the CRP Fund for that period.

Section 2.3, subdivision (c), requires the Department to determine each county's and local agency's aggregate gain every three years ("aggregation period") if the county or local agency was deemed eligible to receive reimbursement for any period in the aggregation period, based on the amounts determined by the counties, and to provide reimbursement to each county and local agency with an aggregate negative gain from the CRP Fund. If there is insufficient money in the CRP Fund to cover the total amount of reimbursements, the Department is required to allocate a pro rata share of the money in the fund to each county and local agency based on the amount it is eligible to be reimbursed relative to the total amount all the counties and local agencies are eligible to be reimbursed for the aggregation period.

Section 2.3, subdivision (d), requires the Controller to transfer any remaining balance in the CRP Fund to the General Fund after the Department has reimbursed each county and local agency that has experienced a negative gain during an aggregation period to be available for appropriation for any purpose. Section 2.3, subdivision (a), requires the Department to adopt a regulation to specify the deadline for the counties' annual determinations and section 2.3, subdivision (e), requires the Department to adopt regulations to implement section 2.3 pursuant to the rulemaking provisions in the Administrative Procedure Act (APA) (Gov. Code § 11340 et seq.).

Discussion

Under the provisions of subdivision (a) of section 2.3, the Department has the responsibility to specify the date by which each county must annually determine the gain for the county and for each local agency in the county resulting from the implementation of section 2.1. Under subdivision (c) of section 2.3, the Department has the responsibility to determine each eligible county's and local agency's aggregate gain every three years, based on the gains determined by the counties, and provide reimbursement to each county or local agency with an aggregate negative gain from the CRP Fund. Also, under subdivision (e) of section 2.3, the Department is required to adopt regulations to implement section 2.3 pursuant to the rulemaking provisions in the APA.

As further explained below, we drafted proposed Regulation 35401, *Registration, Reporting, and Reimbursement* (Exhibit 1), to:

- Require each county to register with the Department to report the gains it is required to annually determine for the county and each local agency in the county under subdivision (a) of section 2.3;
- Clarify the determination periods for which each county shall annually determine the gains;
- Specify the dates by which each county shall annually determine the gains;
- Require each county to report its gains to the Department by specified reporting due dates every three years; and
- Clarify how the Department will use the gains reported by the counties to determine each county's and local agency's aggregate gain every three years and provide reimbursement to each county and local agency with an aggregate negative gain from the money in the CRP Fund under subdivision (c) of section 2.3.

We also recognize that the counties have questions about how to calculate the revenue increases and decreases specified in subdivision (a) of section 2.3 for the county and local agencies in the county. The Department held a separate interested parties meeting on May 26, 2021, and conducted a survey with the counties so the Department could answer the initial questions the Department received based on the general consensus drawn from the counties' survey responses, and the Department may hold additional meetings or conduct additional surveys if needed to address new questions. Information regarding that interested parties meeting, the survey, the guidance already provided, how to sign-up to receive notice of future meetings, and how to submit new questions is available in the Department's Proposition 19 Guide.

Definitions

Subdivision (a) of the proposed regulation defines important terms used in the regulation, including "contact information," "county," "County Revenue Protection Fund Account," "Department," "fiscal year," "gain," "identifying information," "local agency," "negative gain," and "representative information." Subdivision (a) clarifies that the term "county," as used in the proposed regulation, is limited to a county in this state because counties in this state are the only counties required to calculate gains under subdivision (a) of section 2.3, and that the term "county" includes a "city and county," as provided in Government Code section 19 to avoid confusion. Subdivision (a) clarifies that the term "fiscal year," as used in the proposed regulation, means a one-year period beginning on July 1 and ending on June 30 because fiscal years can begin and end on different dates for different purposes and that is the fiscal year for property tax purposes (RTC, § 75.6). Subdivision (a) also clarifies that the term "gain," as used in the proposed regulation means the amount determined by adding the revenue increases and decreases specified in subdivision (a) of section 2.3, rounded to the nearest whole dollar, and that the term "negative gain," as used in the proposed regulation means a gain that is less than zero.

Annual Determinations

Subdivision (b) of the proposed regulation incorporates the requirement that each county annually determine the gain for the county and each local agency in the county from subdivision (a) of section 2.3. It also clarifies that a negative gain shall be expressed as a negative number.

Registration

We determined that it is necessary for each county to register with the Department for a County Revenue Protection Fund Account, as defined in subdivision (a), to report the gains it determines under subdivision (a) of section 2.3, so that the Department can use the gains to determine each county's and local agency's aggregate gain, as required by subdivision (c) of section 2.3. We determined that, as part of the registration process, it is necessary for each county to provide the information the Department needs to specifically identify the county and each local agency in the county, identify and communicate with each county's authorized representatives, and send reimbursement to the counties and local agencies with aggregate negative gains. We also determined it would be more effective and efficient for the counties to register through the Department's online services portal. Therefore, subdivision (c) of the proposed regulation requires each county to electronically register through the Department's online services portal, and provide its "contact information" as defined in subdivision (a), which includes the information the Department needs to identify and communicate with the county's authorized representatives, and the counties "identifying information," as defined in subdivision (a), which includes the information the Department needs to specifically identify and reimburse the county and each local agency in the county. Subdivision (c) also requires each county to update their registration information in a reasonable and timely manner.

Determination Periods

There are no provisions in ACA 11 that specify which periods' revenue should be included in the counties' annual determinations. However, subdivision (a) of section 2.3 requires each county to include the revenue increases from the limitations on the parent-child and grandparent-grandchild transfer exclusions provided by subdivision (c) of section 2.1, in its annual determinations. Therefore, we think that the counties' initial determination period should begin on February 16, 2021, because that was when section 2.1, subdivision (c), became operative.

Also, we understand that property tax is assessed on a fiscal-year basis, counties determine their property tax revenue using a fiscal year that begins on July 1 and ends on June 30, and a substantial majority of the counties that responded to the Department's survey would prefer that their annual determinations be made using the same fiscal year periods. We also recognize that the intent of sections 2.2 and 2.3, when read together, was for the Department to issue its first reimbursements to the eligible counties and local agencies after the Director of Finance has calculated the additional revenues and savings that accrued to the state from the implementation of section 2.1 for three consecutive fiscal years, beginning with the fiscal year ending on June 30, 2022, and the Controller has transferred 15 percent of that money into the CRP fund. We further recognize that the intent was for the first reimbursements to compensate the counties and local agencies with aggregate negative gains for their revenue losses from the implementation of section 2.1 for the same fiscal years. Therefore, subdivision (d)(1) of the proposed regulation clarifies that the initial determination period is the period beginning on February 16, 2021, and ending on June 30, 2022, as suggested in a response to the Department's survey, and each subsequent determination period is a fiscal year beginning July 1 and ending on June 30, commencing with the fiscal year beginning on July 1, 2022, and ending on June 30, 2023.

<u>Determination Date</u>

Subdivision (a) of section 2.3 provides that each county shall annually determine the gain for the county and for each local agency in the county resulting from implementation of section 2.1, no later than the date specified by the Department by regulations. The Department's survey asked the counties when the due date should be for them to determine the gain for the county and each local agency in the county for the prior fiscal year ending June 30 so we could identify a reasonable due date that would be the least burdensome for all the counties. The counties' responses indicated that it would be feasible for them to make their determinations for the prior fiscal year ending on June 30 by the following January 31, if not sooner. Therefore, we believe an annual determination date of January 31 is reasonable and would provide the counties sufficient time to obtain the necessary data to make their determinations for the determination period ending on the preceding June 30. Subdivision (d)(2) of the proposed regulation specifies that, on or before January 31, 2023, each county shall determine the gain for the county and each local agency in the county for the initial determination period ending on June 30, 2022. Also, subdivision (d)(2) specifies that, on or before January 31, 2024, and each subsequent January 31 each county shall determine the gain for the county and each local agency in the county for the determination period ending on the preceding June 30.

<u>Correcting and Updating Gains</u>

We understand that subdivision (a) of section 2.3 requires the counties to make their annual determinations based upon the data available on or before each determination date. We also understand that there may be situations where a county wants to correct errors in or otherwise update the gain determined for a county or local agency before it is reported to the Department and used to calculate the county's or local agency's aggregate gain. For example, a county may identify base year value transfers or parent-child transfers that impact previously determined gains. Therefore, subdivision (e) of the proposed regulation permits a county to correct errors in or update any gain timely determined under subdivision (d)(2) based on more accurate or current information at any time before the gain is required to be reported to the Department.

<u>Reporting Due Date</u>

The Department's survey also asked the counties when the due date should be for them to report the gain for the county and each local agency in the county for the prior fiscal year ending June 30 so we could identify a reasonable reporting due date that would be the least burdensome for all the counties. The counties' responses indicated that it would also be feasible for them to report the gains for the prior fiscal year ending on June 30 by the following January 31, if not sooner. However, we recognize that the Department only needs the counties to report their gains after the end of each aggregation period so that the Department can use them to calculate each county's and local agency's aggregate gain. We also believe it is less burdensome for the counties to report their gains for the same aggregation period at one time and allowing them to do so gives the counties additional time to correct or update the gains for the first two determination periods in each aggregation period before they are required to be reported to the Department. Therefore, subdivision (f)(1) of the proposed regulation generally requires each county to report the gains for the county and each local agency in the county for each of the three preceding determination periods, through the Department's online services portal, on or before January 31, 2025, and every third January 31 thereafter, beginning with January 31, 2028. Subdivision (f)(1) includes an example to illustrate the reporting dues dates. Also, subdivision (f)(2) of the proposed regulation clarifies that the Department will not accept any gain, unless it is reported through the Department's online services portal before the expiration of any extensions of the reporting due granted by the Department.

<u>Extensions</u>

There are provisions that allow the Department to grant extensions for good cause in many of the tax and fee laws administered by the Department, including RTC section 6459 in the Sales and Use Law. Also, the Department's Compliance Policy and Procedures Manual, section 535.050, specifies that "Because of unavoidable delays in obtaining signatures in approval of claims and issuance of warrants by various boards and public officers, a general one-month extension, pursuant to RTC section 6459, is granted to all municipalities, school districts and other political subdivisions of this state, similar to that granted to departments of the state government."

We recognize that reporting gains to the Department is a new requirement for the counties and the process for doing so may be subject to unavoidable delays. Therefore, to be consistent with Department's existing policies, subdivision (g)(1) of the proposed regulation automatically grants each county a one-month extension of the reporting due date specified in subdivision (f)(1).

We also recognize that there may be states of emergency due to disasters that could potentially prevent an affected county from reporting the gains for an aggregation period by the reporting deadline, as automatically extended for one month by subdivision (g)(1). Therefore, subdivision (g)(2) of the proposed regulation further provides that in the case of a state of emergency due to a disaster, as proclaimed by the Governor, the Department may grant the county an extension of the reporting due date specified in subdivision (f)(1) to the following April 30. It also provides that the extension shall be granted at any time provided a request therefor is electronically filed with the Department on or before the April 30 following the reporting due date specified in subdivision (f)(1). Subdivision (g)(3) of the proposed regulation also lists common types of disasters to further clarify the extensions provided for under subdivision (f)(2).

In the event that a county is granted each of the extensions explained above for the same reporting due date, our intent is for the extensions to run concurrently to allow sufficient time for the Department to determine the aggregate gain for the county and each local agency in the county after their gains are reported. In other words, the total time for the extensions would not be greater than three months.

We encourage the counties to report their gains on or before the reporting due dates specified in subdivision (f)(1), rather than wait to report them by the extended due dates under subdivision (g), and the Department intends to have its online reporting system available on the December 1 prior to each reporting due date under subdivision (f)(1) to facilitate timely reporting.

<u>Determining Aggregate Gains and Reimbursing Counties and Local Agencies</u>

Aggregation Date

We recognize that the general intent of sections 2.2 and 2.3 was for the Controller to make three annual transfers from the general fund to the CRP fund before the Department uses the money in the CRP fund to reimburse the counties and local agencies with an aggregate negative gain for an aggregation period. In addition, the Controller is to return any money in the CRP fund to the general fund after the Department has reimbursed the counties and local agencies with an aggregate negative gain for the first aggregation period. And, the whole process will start over with new annual transfers into the fund for purposes of reimbursing the counties and local agencies with an aggregate negative gain for the next aggregation period.

We also recognize that on September 15, 2024, and each September 15 every three years thereafter, all the money available for the Department to provide reimbursement or proportional reimbursement to the counties and local agencies with an aggregate negative gain for the preceding aggregation period should be in the CRP Fund. Therefore, the Department should determine each county's and local agency's aggregate gain for each aggregation period as soon as practical after all the counties are required to report their gains for that period taking into account the potential for some counties to be granted a three month extension of the reporting due date, so that some gains might not be reported until April 30, 2025, and each April 30 every three years thereafter.

Therefore, subdivision (h)(1) of the proposed regulation provides that on May 1, 2025, and on each May 1 every three years thereafter, the Department shall determine each county's and each local agency's aggregate gain, by combining the gains determined by each county and timely reported to the Department for the county and each local agency in the county for each of the three preceding determination periods. It also clarifies that each county and local agency with an aggregate negative gain shall be eligible to be reimbursed an amount equal to its aggregate negative gain expressed as a positive number for that three-year aggregation period. For example, if a local agency's aggregate gain was negative one hundred dollars (-$100) for an aggregation period, then the local agency would be eligible to be reimbursed up to one hundred dollars ($100) for that period.

Reimbursement

We also recognize that the reimbursement process under subdivision (c) of section 2.3 is based upon whether there is money in the CRP Fund at the time the Department determines the counties' and local agencies' aggregate gains for an aggregation period, and whether the money is sufficient to cover the full amount each county and local agency is eligible to be reimbursed. Therefore, subdivision (h)(2) of the proposed regulation provides that on May 1, 2025, and on each May 1 every three years thereafter, the Department shall also determine if there is money in the CRP Fund and whether it is sufficient to provide each county and local agency the full amount it is eligible to be reimbursed for the current aggregation period under subdivision (h)(1). Subdivision (h)(3) of the proposed regulation clarifies that if there is sufficient money in the CRP Fund on May 1, 2025, or any May 1 every three years thereafter, the Department shall begin the process to provide each county and local agency with the full amount it is eligible to be reimbursed for the current aggregation period under subdivision (h)(1). And, subdivision (h)(4) of the proposed regulation further clarifies that if there is money in the CRP Fund on May 1, 2025, or any May 1 every three years thereafter, but not sufficient money to provide each county and local agency the full amount it is eligible to be reimbursed for the current aggregation period under subdivision (h)(1), the Department shall begin the process to provide a pro rata share of the money in the fund to each county and local agency based on the amount the county or local agency is eligible to be reimbursed relative to the total amount all the counties and local agencies are eligible to be reimbursed for the current aggregation period under subdivision (h)(1). For example, if a county is eligible to be reimbursed one percent (1%) of the total amount all the counties and local agencies are eligible to be reimbursed for the current aggregation period, then the Department would provide one percent (1%) of the money in the fund to that county for that period. We believe the due dates and procedures in subdivision (h) will allow the Department to disburse the necessary funds in a timely manner.

<u>Failure to Report</u>

The Department cannot determine a county's or local agency's aggregate gain for any aggregation period unless all of its gains for that period were reported to the Department. Also, the Department cannot reimburse a county or local agency for any aggregation period, unless it can determine that it has an aggregate negative gain for that period. Therefore, subdivision (g) of the proposed regulation provides that if a county fails to report a gain for the county or a local agency in the county for any determination period within an aggregation period before the expiration of the extensions of the reporting due date granted under subdivision (g), the Department will conclusively presume that the county or local agency does not have an aggregate negative gain for the aggregation period and thus is not eligible to be reimbursed from the CRP Fund for that period. We believe it is reasonable for the Department to establish such a presumption under such circumstances and we believe the presumption must be conclusive at some point because the appropriation in section 2.2 is limited to the money in the CRP Fund and the Department will have no money left in the fund to make additional reimbursements for a aggregation period after it completes the reimbursement process for that period and the Controller transfers any money left in the CRP Fund to the General Fund.

Summary

As discussed above, sections 2.2 and 2.3 are intended to provide reimbursement to counties and local agencies that have a negative aggregate gain for an aggregation period. The most reasonable way to effectuate that purpose is to provide the reimbursements as soon as practical after the end of each aggregation period. We believe proposed Regulation 35401 provides a reasonable timeline for the counties to make their annual determinations and report their gains to the Department for each aggregation period, so that the Department can determine each county's and local agency's aggregate gain and provide the necessary reimbursements in a timely manner.

We welcome any comments, suggestions, and input from interested parties regarding proposed Regulation 35401. We also invite interested parties to participate in the September 8, 2021, interested parties meeting regarding the proposed regulation. The deadline for interested parties to provide their written submissions regarding this discussion paper will be September 24, 2021.

Prepared by the Tax Policy Bureau, Business Tax and Fee Division
Current as of 08/23/21

Proposed Text of

California Code of Regulations, Title 18, Division 5,

Chapter 5, *County Revenue Protection Fund Regulations*, and

Section 35401, *Registration, Reporting, and Reimbursement*

(New chapter and regulation to be added to division 5 of title 18 of the California Code of Regulations)

Chapter 5. County Revenue Protection Fund Regulations.

Regulation 35401. Registration, Reporting, and Reimbursement.

(a) Definitions. For purposes of this regulation, the following terms have the following meanings:

(1) “Contact information” means information the Department deems necessary to contact and communicate with the county registering for a County Revenue Protection Fund Account and with that county’s authorized representative(s). Such information includes, but is not limited to, the county’s current mailing address and the representative information for each of its representatives.

(2) “County” means a county in this state and “county” includes a city and county.

(3) “County Revenue Protection Fund Account” means an account issued and maintained by the Department to uniquely identify a county and each local agency in the county for purposes of reimbursement under subdivision (h).

(4) “Department” means the California Department of Tax and Fee Administration.

(5) “Fiscal year” means the one-year period beginning on July 1 and ending on June 30.

(6) “Gain” means the amount determined by adding the revenue increases and decreases specified in subdivision (a) of section 2.3 of article XIII A of the California Constitution, rounded to the nearest whole dollar.

(7) “Identifying information” means information the Department deems necessary to specifically identify the county and each local agency in the county. Such information includes, but is not limited to, the name and federal Taxpayer Identification Number of the county and each local agency in the county, and the mailing addresses to send reimbursement to the county and each local agency in the county.

(8) “Local agency” means a city, a special district, or a school district as determined pursuant to subdivision (o) of section 42238.02 of the Education Code as that subdivision read on January 8, 2020.

(9) “Negative gain” means a gain that is less than zero.

(10) “Representative information” means information the Department deems necessary to verify that an individual is authorized to represent a county and submit an application for registration under subdivision (c), report gains under subdivision (f), or request an extension under subdivision (g)(2) on behalf of the county. Such information includes, but is not limited to, the individual’s first and last name, title, email address, and phone number.

(b) Annual Determinations. Each county is required to annually determine the gain for the county and each local agency in the county. If a county or local agency has a negative gain it shall be expressed as a negative number.

(c) Registration.

(1) Each county shall register with the Department for a County Revenue Protection Fund Account for the purpose of electronically reporting the gains it annually determines pursuant to subdivision (b) to the Department by completing an application for registration through the Department’s online services portal via its website at www.cdtfa.ca.gov.

(2) Every application for registration for a County Revenue Protection Fund Account shall provide the county’s contact information and identifying information.

Each county shall ensure that its contact information and identifying information is updated in a reasonable and timely manner.

(d) Determination Periods and Annual Determination Date.

(1) The initial determination period is the period beginning on February 16, 2021, and ending on June 30, 2022. Each subsequent determination period is a fiscal year, commencing with the fiscal year beginning on July 1, 2022, and ending on June 30, 2023.

(2) On or before January 31, 2023, each county shall determine the gain for the county and each local agency in the county for the initial determination period. On or before January 31, 2024, and each January 31 thereafter, each county shall determine the gain for the county and each local agency in the county for the determination period ending on the preceding June 30. For example, on January 31, 2024, each county shall determine the gain for the county and each local agency in the county for the fiscal year ending on June 30, 2023.

(e) Correcting and Updating Gains. A county may correct errors in or update any gain timely determined under subdivision (d)(2) based on more accurate or current information at any time before the gain is required to be reported to the Department, including during any extension of the reporting due date granted under subdivision (g).

(f) Reporting Due Date.

(1) Except as provided in subdivision (g), each county shall electronically report the gains for the county and each local agency in the county for each of the three preceding determination periods through the Department's online services portal via its website at www.cdtfa.ca.gov on or before January 31, 2025, and every third January 31 thereafter, beginning with January 31, 2028.

For example, each county shall electronically report the gains it determines for the determination periods February 16, 2021, through June 30, 2022, July 1, 2022, through June 30, 2023, and July 1, 2023, through June 30, 2024, on or before January 31, 2025. Each county shall electronically report the gains it determines for the determination periods July 1, 2024, through June 30, 2025, July 1, 2025, through June 30, 2026, and July 1, 2026, through June 30, 2027, on or before January 31, 2028.

(2) The Department will not accept any gain, unless it is reported through the Department's online services portal before the expiration of any extensions of the reporting due date granted under subdivision (g).

(g) Extension of Reporting Due Date.

(1) The Department shall automatically grant an extension of the reporting due date specified in subdivision (f)(1) to the following February 29 in leap years and the following February 28 in years that are not leap years.

(2) In the case of a state of emergency due to a disaster in any county, as proclaimed by the Governor pursuant to section 8625 of the Government Code, the Department may grant the county an extension of the reporting due date specified in subdivision (f)(1) to the following April 30. The extension shall be granted provided a request therefor is electronically filed with the Department on or before the April 30 following the reporting due date specified in subdivision (f)(1).

(3) For purposes of this subdivision, "disaster" includes, but is not limited to, fire, flood, storm, tidal wave, earthquake, epidemic, or similar public calamity, whether or not resulting from natural causes.

(h) Determining Aggregate Gains and Reimbursement.

(1) On May 1, 2025, and on each May 1 every three years thereafter, the Department shall determine each county's and each local agency's aggregate gain, by combining the gains determined by each county and timely reported to the Department for the county and each local agency in the county for each of the three preceding determination periods, and each county and local agency with an aggregate negative gain shall be eligible to be reimbursed an amount equal to its aggregate negative gain expressed as a positive number for that aggregation period. For example, if a local agency's aggregate gain was negative one

hundred dollars (-$100) for an aggregation period, then the local agency would be eligible to be reimbursed up to one hundred dollars ($100) for that period.

(2) On May 1, 2025, and on each May 1 every three years thereafter, the Department shall also determine if there is money in the County Revenue Protection Fund and whether it is sufficient to provide each county and local agency the full amount it is eligible to be reimbursed for the current aggregation period under subdivision (h)(1).

(3) If there is sufficient money in the County Revenue Protection Fund on May 1, 2025, or any May 1 every three years thereafter, the Department shall begin the process to provide each county and local agency with the full amount it is eligible to be reimbursed for the current aggregation period under subdivision (h)(1).

(4) If there is money in the County Revenue Protection Fund on May 1, 2025, or any May 1 every three years thereafter, but not sufficient money to provide each county and local agency the full amount it is eligible to be reimbursed for the current aggregation period under subdivision (h)(1), the Department shall begin the process to provide a pro rata share of the money in the fund to each county and local agency based on the amount the county or local agency is eligible to be reimbursed relative to the total amount all the counties and local agencies are eligible to be reimbursed for the current aggregation period under subdivision (h)(1). For example, if a county is eligible to be reimbursed one percent (1%) of the total amount all the counties and local agencies are eligible to be reimbursed for the current aggregation period, then the Department will provide one percent (1%) of the money in the fund to that county for that period.

(i) Failure to Report. If a county fails to report a gain for the county or a local agency in the county for any determination period within an aggregation period before the expiration of the extensions of the reporting due date granted under subdivision (g), the Department will conclusively presume that the county or local agency does not have an aggregate negative gain for the aggregation period and thus is not eligible to be reimbursed from the County Revenue Protection Fund for that period.

Note: Authority cited: Article XIII A, Section 2.3, California Constitution. Reference: Article XIIIA, Section 2.3, California Constitution.