HdL Coren & Cone

Memo

To: HdL Coren & Cone Clients

From: HdL Coren &Cone

COVID-19 AND POTENTIAL IMPACT TO PROPERTY TAX REVENUES

As cities are confronting making difficult decisions in response to the impacts of the COVID-19 virus, we at HdL Coren & Cone (HdLCC) have been receiving questions from our clients on the possible impact this growing crisis may have on current year revenues and on forecasts of property tax revenues for 2020-21 and subsequent years. Federal, State, and local governments are working to limit the spread of COVID-19 and orders to limit meeting sizes, practice social distancing, and to stay home if possible has already caused closure of businesses and limits on access to retail and service industries. This has and will continue to have impacts on the economy. This pandemic event is not something we have seen before and, until very recently, was not on anyone's radar as the potential reason for the economic changes we are seeing. Whether these economic conditions will be short or long term is not yet evident.

The assessed values and tax bills for the current year, 2019-20, are out and will, for the most part, be paid within the next month. We see no reason to expect that property tax revenues for this fiscal year will be impacted to any significant degree. The most we might anticipate would be a minor reduction in supplemental revenues if transfers of ownership or new construction is reduced between now and August. The mid-year property tax budget adjustments you may have made should still be valid.

The 2020-21 forecast tools that we provided our clients last month are still valid. The values that will be enrolled for 2020-21 were initially established as of the January 1, 2020 lien date. That date is when the 2% growth per Proposition 13 is added and the events such as sale transactions, new development and construction additions that occurred in 2019 are reflected on the tax roll for the 2020-21 fiscal year. The tax roll values are processed by the Assessor between January and June before their transfer to the Auditor-Controller and then to the Tax Collector for property tax collection. While we had already begun to see a leveling of sale prices throughout the State, and in some counties a small decline in median sale prices based on reported sales in 2018 and 2019, the real impact of sales occurring in the 2020 calendar year will impact the 2021-22 property tax forecast. In counties where declining sale prices in 2019 were experienced, the forecast we prepared for 2020-21 included less growth as a result of those transactions. In some cities the potential recovery of value within the Proposition 8 pool of properties were reduced within our forecast in line with declines in market value.

If there is a recession, it is unlikely to be something that can be modeled identically using one of the past three (3) downturns we have seen in the 30 years we have been providing property tax services for California cities. If there are significant, long term job losses, individuals may have difficulty paying their mortgages and ultimately, we might see an uptick in foreclosures and the banks repossessing properties. If we use a model based on the recession of 10 years ago, the impact of this would be a drag on the median sale prices especially if individuals decide to sell their homes to meet other obligations. When this has happened in prior recessions, our modeling shows that asking prices are lowered and median sale prices will dip. When sale prices decline, DTT receipts are lower because they are tied to sale prices and numbers of sale transactions and, we also see negative supplemental allocations which are distributed based on countywide receipts per AB-8. If, however, the impacts of this virus are, relatively, short-term as expected, any impacts on property values may also be short-term as well.

If this crisis continues through the summer, we may expect that revenues for 2020-21 may be reduced due to some level of delinquency and Assessor value reductions to reflect market values. The potential for such reductions will only become evident as time passes. Because the nature of this crisis is far different from the circumstances 10 years ago, it is not likely that the impact of this crisis will be as deep or as long lasting as the last recession. The impacts, large or small, of this crisis on assessed values will start to be seen in calendar year 2020 and would be reflected in the 2021-22 fiscal year.

To review, the assessed values for 2020-21 are based on what happened in 2019 and are already in the process of being finalized. The negative impacts will be the result of what happens during the rest of 2020 and in 2021 based on assessment appeals, lower valued sales and the resulting reductions in supplemental assessment and/or DTT revenue declines, and potential Prop 8 value reductions. We are not economists and don't know yet how this pandemic may play out or how economic programs instituted at the Federal, State or local levels may mitigate the long-term impacts of this challenge. For now, we all must wait and see. Fortunately, the nature of property tax revenues as a lagging indicator is such that we will be able to see the impacts coming.

Once HdLCC starts to prepare the 2021-22 forecasting tools near the end of 2020, we will be able to see what has happened to the full year of sale transactions for 2020 and Assessors will be indicating if they are reviewing properties in anticipation of value reductions per Prop 8. We will also be able to look at the number of building permits approved and sales tax numbers will give us an indication about business property and the health of businesses in general. With this data we will be able to provide a more reliable forecast for 2020-21 mid-year adjustments and for 2021-22 budgets.

In the meantime, please contact us if you have questions about your specific situation or if you need specific information. Phone: (714) 879-5000

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