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## Finance Committee

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### HB 1040

**Brief Description:** Concerning rental income received by people eligible for certain property tax exemption programs.

**Sponsors:** Representatives Doglio, Parshley, Ryu, Ramel, Klicker, Richards, Reed, Alvarado, Shavers, Peterson, Paul, Wylie, Fey, Kloba, Lekanoff, Fosse and Reeves.

Brief Summary of Bill
<ul style="list-style-type: none"><li>• Adds limited income from renting living space in the primary residence as a deduction from the combined disposable income calculation for the senior citizens, disabled individuals, and qualifying veterans tax exemption program.</li></ul>



**Hearing Date:** 2/4/25

**Staff:** Rachelle Harris (786-7137).

#### Background:

##### Property Tax.

All real and personal property is subject to a tax each year based on the highest and best use, unless a specific exemption is provided by law. The annual growth of all regular property tax levy revenue is limited as follows:

- For jurisdictions with a population of less than 10,000, revenue growth is limited to 1 percent.
- For jurisdictions with a population of 10,000 or more, revenue growth is limited to the lesser of inflation or 1 percent plus the value of new construction.

The state collects two regular property tax levies for common schools. The revenue growth limit

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applies to both levies. Participants in the senior citizens, disabled individuals, and qualifying veterans property tax exemption (SPTE) program receive a partial exemption from the original state levy and a full exemption from the additional state levy.

The Washington Constitution limits regular levies to a maximum of 1 percent of the property's value (\$10 per \$1,000 of assessed value). There are individual district rate maximums and aggregate rate maximums to keep the total tax rate for regular property taxes within the constitutional limit.

#### Property Tax—Senior Citizens, Disabled Individuals, and Qualifying Veterans Tax Relief.

Authorized by a constitutional amendment, qualifying senior citizens, persons retired due to disability, and qualifying veterans are entitled to property tax relief on their principal residence.

To qualify for the SPTE, a person must be:

- at least 61 years old;
- at least 57 years old and the surviving spouse or domestic partner of a person who was an exemption participant at the time of their death;
- retired from employment because of disability; or
- a disabled veteran with a service-connected evaluation of at least 80 percent or receiving compensation from the US Department of Veterans Affairs at the 100 percent rate for a service-connected disability.

The home must be owned by and be the primary residence of the applicant, or be a detached accessory dwelling unit. An applicant's combined disposable income must be under the county's income threshold to qualify. Eligible individuals may qualify for a partial property tax exemption and a valuation freeze.

*Partial Tax Exemption:* The partial property tax exemption for the SPTE is provided according to various income thresholds. The income thresholds and associated partial exemptions are as follows:

- "Income threshold one" is the greater of income threshold one for the previous year or 50 percent of the county's median household income. Applicants qualifying under this income threshold receive an exemption from all excess levies, the additional state levy, and regular levies on the greater of \$60,000 or 60 percent of the assessed valuation.
- "Income threshold two" is the greater of income threshold two for the previous year or 60 percent of the county's median household income. Applicants qualifying under this income threshold but above income threshold one receive an exemption from all excess levies, the additional state levy, and regular levies on the greater of \$50,000 or 35 percent of assessed valuation (with a \$70,000 maximum).
- "Income threshold three" is the greater of income threshold three for the previous year or 70 percent of the county's median household income. Applicants qualifying under this income threshold but above income threshold two receive an exemption from all excess levies and the additional state levy.

The income thresholds are adjusted every three years to reflect the most recent year of estimated

county median household incomes as published by the Office of Financial Management. For every adjustment made, if an income threshold in a county is not adjusted based on percentage of county median income, then the income threshold must be adjusted based on the growth of the seasonally adjusted consumer price index for all urban consumers for the prior 12-month period as published by the US Bureau of Labor Statistics, with a limit of 1 percent.

*Valuation Freeze:* In addition to the partial exemptions listed above, the valuation of the residence of an eligible individual is frozen, for the purpose of calculating property tax liability, at the assessed value of the residence on the later of January 1, 1995, or January 1 of the assessment year in which the person first qualifies for the program. To be eligible, the person must have a disposable income of less than income threshold three.

*Deferral:* In addition to the SPTE, individuals who meet the requirements, except for the income and age requirements, are permitted to defer their property taxes if their combined disposable income is less than the deferral threshold and they are 60 years or older. The income threshold for the deferral program is the greater of 75 percent of the county median household income or \$45,000.

Taxes that are deferred become a lien against the property and accrue interest at 5 percent per year. If deferred taxes are not repaid within three years after the eligible person ceases to own and live in the residence, the lien will be foreclosed and the residence sold to recover taxes.

*Combined Disposable Income:* For property tax relief programs, combined disposable income is defined as the sum of federally defined adjusted gross income plus the following, if not already included:

- capital gains;
- deductions for losses;
- depreciation;
- pensions and annuities;
- military pay and benefits;
- veteran's benefits except attendant-care and medical-aid payments;
- Social Security and federal railroad retirement benefits;
- dividends; and
- interest income on state and municipal bonds.

The following are deducted when determining combined disposable income:

- payments for the care of either spouse received in the home, in a boarding home, in an adult family home, or in a nursing home;
- prescription drugs and disposable devices to deliver them;
- Medicare health care insurance premiums;
- supplemental Medicare policies;
- durable medical equipment;
- long term care insurance;
- nebulizers;

- ostomic items;
- insulin;
- kidney dialysis devices; and
- naturopathic medicines.

#### Tax Preference Performance Statement.

State law provides for a range of tax preferences that confer reduced tax liability upon a designated class of taxpayer. Tax preferences include tax exclusions, deductions, exemptions, preferential tax rates, deferrals, and credits. Currently, Washington has over 700 tax preferences, including a variety of sales and use tax exemptions. Legislation that establishes or expands a tax preference must include a Tax Preference Performance Statement (TPPS) that identifies the public policy objective of the preference, as well as specific metrics that the Joint Legislative Audit and Review Committee (JLARC) can use to evaluate the effectiveness of the preference. All new tax preferences automatically expire after 10 years unless an alternative expiration date is provided.

#### **Summary of Bill:**

When calculating combined disposable income for the SPTE and related programs, up to \$6,000 of annual income received from the rental of living space in the primary residence is deducted. Income received from short-term rentals may not be deducted and must still be counted as income.

The requirements for a TPPS and 10-year expiration do not apply to the act, and the bill identifies the legislative intent to keep the tax preference and its expansion permanent.

The bill applies to property taxes levied for collection in 2027 and thereafter.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill takes effect 90 days after adjournment of the session in which the bill is passed.