CALIFONIA STATE BOARD OF EQUALIZATION

SUMMARY DECISION UNDER REVENUE AND TAXATION CODE SECTION 40

In the Matter of the Petition for Reassessment of the 2023 Unitary Value for: **LIBERTY UTILITIES (CALPECO ELECTRIC), LLC (0163)** Petitioner	Appeal No. SAU 23-018 Nonappearance Hearing Date: December 12, 2023[1]

Representing the Parties:

For the Petitioner:	Daniel Tobias, Authorized Agent Tobias & Associates, Inc. Christopher Tobias, Authorized Agent Tobias & Associates, Inc.
For the Respondent:	Richard Moon, Attorney V Attorney for State-Assessed Properties Division Michelle Cruz, Principal Property Appraiser State-Assessed Properties Division
Appeals Attorney:	Sarah J. Wilkman, Attorney III

VALUES AT ISSUE

	Value	Penalty	Total
2023 Board-Adopted Unitary Value	$266,600,000	$0	$266,600,000
Petitioner's Requested Unitary Value	$172,913,950	$0	$172,913,950
Respondent's Appeal Recommendation	$266,600,000	$0	$266,600,000
Respondent's Revised Recommendation	$262,500,000	$0	$262,500,000
Board Determined Value	$262,500,000	$0	$262,500,000

[1] At the nonappearance hearing, the Board partially granted the petition as to Issue 6 and denied the petition as to all other issues, by a unanimous vote of the Members present, with Chair Vazquez, Vice-Chair Lieber, Member Schaefer, Member Gaines, and Controller Cohen voting aye.

Factual Background

Liberty Utilities (Calpeco Electric), LLC (Liberty or Petitioner) provides regulated electricity, water, and natural gas utility services to over 1 million customer connections, primarily in North America. Its California service areas include Coleville, Floriston, Loyalton, Markleeville, North Lake Tahoe, Portola, South Lake Tahoe, Topaz Lake, Truckee, Verdi, Walker, and Woodfords.

The 2023 Board-adopted unitary value for Petitioner of $266,600,000 was based upon 75 percent reliance on the Historic Cost New Less Depreciation (HCLD) value indicator and 25 percent reliance on the Capitalized Earning Ability (CEA) value indicator.

On appeal, Petitioner contends that their 2023 Board-adopted unitary value is overstated and requests a revised unitary value of $172,913,950. Throughout the appeals process, Petitioner and the State-Assessed Properties Division (SAPD or Respondent) each submitted briefing, evidence, and argument throughout the appeals process, including at the appeals conference[2], to support their positions on the six issues raised in this petition.

After a review of Petitioner's submitted evidence and argument in response to an information exchange after the Appeals Conference, Respondent revised its recommended unitary value, supporting a reduction of $4,100,000 (described in greater detail in issue 6).

Legal Issues 1 and 2: Whether Petitioner Has Shown that Respondent Improperly Placed 75 Percent Reliance on the Historical Cost Less Depreciation (HCLD) Value Indicator and 25 Percent Reliance on the Capitalized Earning Ability (CEA) Value Indicator, and, If So, Whether Petitioner Has Shown Additional Reliance on the CEA Value Indicator is Appropriate.

Findings of Fact and Related Contentions

Petitioner asserts Respondent's 75 percent HCLD reliance and 25 percent CEA reliance reflects a weighted average that does not reflect industry and market conditions and asserts that the value indicator reflects non-recoverable costs in the general rate case. Specifically, Petitioner asserts that Respondent's assignment of 25 percent to the CEA approach is incorrect as the subject property's

---

[2] The appeals conference was held on November 8, 2023.

taxable CEA income has decreased by 5.86 percent and the Petitioner's 2023 Board-adopted unitary value increasing by 23.65 percent when compared to the 2022 value indicates that Respondent has not reconciled the overall differences in the two approaches. Petitioner further argues that the difference between the two value indicators may signify obsolescence or that other problems exist in the property, and in this instance its HCLD value indicator is 46.5744 percent greater than its CEA value indicator. Accordingly, Petitioner asserts that this shows that the CEA value approach should be given more weight. Based on the foregoing rationales, Petitioner requests that the Board instead utilize 100 percent reliance on the income approach instead of Respondent's 75 percent reliance on the HCLD approach and 25 percent reliance on the income approach.

Respondent has conducted its appraisal by calculating and reconciling the HCLD and CEA value indicators, consistent with relevant law and appraisal guidance.[3] Respondent notes significant differences in the two value approaches can and may occur, as stated in Assessors' Handbook, section 501 (AH 501) *Basic Appraisal,* without compromising the validity of the underlying value approach, quoting:

> The reconciliation of value indicators from the separate approaches to value and the resulting final value estimate is the next step in the appraisal process. Theoretically, the approaches to value should produce identical value indicators. In practice, however, this is rarely the case, and significant differences may occur. To produce a final value estimate, the appraiser reconciles the indicators from each approach utilized. Value indicators should be reconciled considering: (1) the appropriateness of the approach given the purpose of the appraisal; and (2) the adequacy and reliability of the data available to perform the appraisal. The appraiser should examine and reconcile all value indicators.

(AH 501, p. 62.) Specifically, Respondent notes that when analyzing and reconciling value indicators to arrive at a final value estimate, the criteria described in AH 502, *Advanced Appraisal,* should be considered:

> The final value estimate is an appraiser's opinion of value. There is no mathematical formula or statistical technique to which the appraiser can ultimately refer in order to reach the final value estimate. It is an opinion that should be based on the appraiser's application of generally accepted appraisal methods and procedures.
>
> It is generally inappropriate to use the arithmetic mean of the value indicators as the final value estimate. Simply calculating an average implies that all the value indicators have equal validity.

[3] Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.)

> While this may occur in certain instances, it is usually not the case. Appraisers must follow Rule[4] 3, noted above, and consider the appropriateness of the value approaches, the relative accuracy of the value indicators, and the quantity and quality of the data available when reconciling value indicators to reach the final value estimate.

(AH 502, p. 111.)

Respondent notes the HCLD approach is a reliable indicator of market value for closely regulated public utilities, like Petitioner, as HCLD, with some modification, approximates the rate base that regulators use in establishing revenue requirements. (*Unitary Valuation Methods* (*UVM*) (2003), p. 1.) HCLD reflects the market value contribution of all taxable property including the depreciated historical cost of plant in service, possessory interests, construction work in progress, and materials and supplies, and is:

> A generally accepted method for valuing property interests of rate base regulated utilities, whether centrally or locally assessed, is by use of the historical cost approach. Certain industries have been and continue to be subject to rate base regulation, as a result of which authorized earnings, or rates of return, are set by regulators and measured by rate base. Under Rule 3(d), the assessing agency shall consider as relevant to value the amount actually invested in the property or the amount invested less depreciation, if the income from the property is regulated by law and the regulatory agency uses historical cost, historical cost less depreciation (HCLD), or trended original cost as a rate base. Thus, the historical cost approach is considered relevant for estimating the market value of public utility properties depending upon regulatory influences.

(AH 502, p. 146.) Further, HCLD is,

> one of the more important indicators of value for closely regulated public utilities. The general practice of the California Public Utilities Commission (CPUC) and most other regulatory agencies is to use historical or original cost less depreciation (with various adjustments) as the rate base. The regulatory agencies establish a rate base and a rate of return; utilities are permitted to earn at this established rate on the rate base.

(*UVM,* p. 1.)

Respondent also notes that Property Tax Rule 8, subdivision (a), indicates the CEA value indicator is appropriate to use when the property has "an established income stream…," and here, Petitioner has an established income stream.

Respondent states that consistent with the relevant HCLD and CEA value indicator authorities and considerations, and Petitioner being a utility, rate regulated by the CPUC, Respondent considered

---

[4] All references to Property Tax Rule or Rules are to sections of title 18 of the California Code of Regulations.

HCLD to be the most reliable indicator of value, placing 75 percent reliance on the indicator. Respondent notes that due to Petitioner's significant growth in actual and planned capital expenditures to replace and expand distribution and transmission infrastructure, and to construct and replace generation assets, Petitioner is experiencing "regulatory lag" and the relative reliance on the indicators corresponds accordingly.[5] As such, Respondent's maintains it is appropriate to weight the CEA value indicator 25 percent.

Applicable Law and Appraisal Principles

Burden of Proof

Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.) Therefore, Petitioner has the burden of showing that the assessment is incorrect or illegal. (*ITT World Communications v. Santa Clara* (1980) 101 Cal.App.3d 246; see also Cal. Code Regs., tit. 18, § 5541, subd. (a).)

Value Standard

Revenue and Taxation Code section 110, subdivisions (a) and (b) define "full cash value" or "fair market value" for California property tax assessment purposes.

HCLD Approach to Value

Property Tax Rule 3, subdivision (d) provides the HCLD approach to value shall be considered "[i]f the income from the property is regulated by law and the regulatory agency uses historical cost or historical cost less deprecation as the rate base, the amount invested in the property or the amount invested less depreciation computed by the method employed by the regulatory agency." HCLD, with some modification, approximates the rate base that regulators use in establishing revenue requirements. (See *UVM*, p. 1.) HCLD reflects the market value contribution of all taxable property including the depreciated historical cost of plant in service, possessory interests, construction work in progress, and materials and supplies. (AH 502, p. 146.) HCLD is,

> one of the more important indicators of value for closely regulated public utilities. The general practice of the California Public Utilities Commission (CPUC) and most other regulatory agencies is to use historical or original cost less depreciation (with various adjustments) as the

---

[5] Regulatory lag is the time delay between a utility's costs and any adjustment CPUC may make to the rate base to account for these costs. This process creates a lag between the time the assets are placed in service and the time the company begins to get a recover of and recovery on the assets.

> rate base. The regulatory agencies establish a rate base and a rate of return; utilities are permitted to earn at this established rate on the rate base.

(UVM (2003), p. 1.)

Further, Board guidance states,

> Appraisal depreciation in the form of obsolescence may be present in utility property and deducted from HCLD. Such deductions may be proper when the utility's economic income has been impaired and the rate or tariff-setting regulators have recognized such impairment.

(UVM, p. 1.)

<u>Income Approach to Value</u>

Property Tax Rule 8, subdivision (a), states that "the income approach is used in conjunction with other approaches when the property under appraisal is typically purchased in anticipation of a money income and either has an established income stream or can be attributed a real or hypothetical income stream by comparison with other properties." Subdivision (b) describes the income approach to value as the valuation method whereby, "an appraiser values an income property by computing the present worth of a future income stream. This present worth depends upon the size, shape, and duration of the estimated stream and upon the capitalization rate at which future income is discounted to its present worth." Subdivision (c) provides that "the amount to be capitalized is the net return which a reasonably well-informed owner and reasonably well-informed buyers may anticipate on the valuation date that the taxable property existing on that date will yield under prudent management and subject to legally enforceable restrictions as such persons may foresee as of that date."

<u>Reconciliation of Value Indicators</u>

Property Tax Rule 3 requires that, in estimating value, the assessor shall consider one or more of the approaches to value "as may be appropriate for the property being appraised," which includes the comparative sales approach, the cost approach (e.g., HCLD valuation methodology), or the income approach (CEA valuation methodology). The appropriateness of an approach is often related to the type of property being appraised and the available data. (AH 502, p. 109.) In addition, the validity of a value indicator will depend upon the accuracy of data and adjustments made to the approach. That is, the accuracy of a value indicator depends on the amount of available comparable data, the number and type of adjustments, and the dollar amount of adjustments. Finally, if a large amount of comparable data is available for a given approach, the appraiser may have more confidence in that approach. For example, if income, expense, and capitalization rate data can be obtained from many properties comparable to the subject, the appraiser may attribute significant accuracy to the income approach. The greatest reliance should be placed on that approach or combination of approaches that best measures the type of benefits the subject property yields. The final value estimate reflects the relative weight that the appraiser assigned, either implicitly or explicitly, to each approach. (AH 502, p. 112.)

Analysis and Disposition

Respondent is presumed to have correctly determined the value of the property at issue, and Petitioner bears the burden of proving otherwise. Here, Petitioner contends that because Respondent's calculated HCLD value indicator exceeds the CEA value indicator by 46.5744 percent, Respondent's 2023 Board-adopted unitary value is flawed, as the various approaches to value must yield approximately the same results, and differences of such a magnitude indicate that the value indicators were not reconciled or do not otherwise reflect market conditions. However, as Board guidance and Respondent note, significant differences may occur in validly calculated indicators. While Petitioner advances various arguments, Respondent contends, in light of all available evidence, it was reasonable and appropriate to place 75 percent reliance on the HCLD value indicator, which reflects the consideration of many factors, including: that the HCLD value indicator is a reliable indicator of value for closely regulated public utilities like Petitioner, because HCLD, with some modification, approximates the rate base that regulators use in establishing revenue requirements; Petitioner's "regulatory lag"; Petitioner's established income stream; and consistency with Property Tax Rules 3, 6, and 8, as well as relevant Board guidance.

We concur with the Respondent and find no error with the reconciliation of Petitioner's 2023 unitary value. Further, based on the evidence and arguments submitted to the record, we find that Petitioner has not shown specific evidence or argument to prove that its HCLD indicator is impaired, nor has Petitioner shown that its CEA value indicator must be granted additional weight. We note Petitioner's assertion that the difference in the HCLD and CEA value indicators being attributed to obsolescence is unsupported. Similarly, Petitioner's assertion that Respondent's appraisal judgement and valuation approach is flawed, without providing any specific evidence, is similarly unsupported. We find

Respondent's appraisal judgment to place 75 percent reliance on the HCLD value indicator and 25 percent reliance on the CEA value indicator was appropriate and reflects the consideration of a variety of factors. Accordingly, we find no error or illegality within Petitioner's 2023 unitary value as to these issues and we further find that Petitioner has not met their burden of proof as to these issues.

Legal Issue 3: Whether Respondent Must Adjust the CEA Value Indicator to Account for Intangible Assets, such as its Trained and Experienced Workforce in Place and Management Expenses.

Findings of Fact and Related Contentions

Petitioner claims that deductions from the CEA value indicator must be made for its intangible assets and rights, such as its trained and experienced workforce and management expenses and other self-created intangible assets. Petitioner argues that its operations workforce saves operating cost, downtime, and outages, as well as other transitional issues and difficulties in other investor-owned utility sales. With respect to management fees, Petitioner cites to AH 502 and *SCH Half Moon Bay v. San Mateo County* (Hereinafter *SCH Half Moon Bay*), (2014) 226 Cal.App.4th, 471, for the proposition that they must be deducted from operating income prior to capitalization. Petitioner asserts these intangible assets have value that are not captured within its financials, and must be deducted, citing to *SCH Half Moon Bay*.

Respondent notes Property Tax Rule 8 does not require a deduction be made for a business with only prudent management and a reasonably skillful workforce, since those levels of expertise must be assumed for the necessary and productive use of the property. Respondent further points out that no authorities, including those cited by the Petitioner –Assessors Handbook section 502, Advanced Appraisal, (AH 502), pp. 162-163 and *SHC Half Moon Bay*– are to the contrary. Under relevant guidance, Respondent notes that for the requested deduction to be proper, Petitioner must show that its "trained and experienced workforce" and "management fees" produced an income superior to that which would have been produced with an ordinary workforce and management. Respondent further notes that it would be difficult for Petitioner to make such a showing because Petitioner's income is rate-regulated

STATE BOARD OF EQUALIZATION
PROPERTY TAX APPEAL

and already assumes prudent management. Ultimately, Respondent contends that Petitioner has made no such factual showing to support the requested deduction.

Applicable Law and Appraisal Principles

Burden of Proof

See Issues 1 & 2, Applicable Law, p. 5.

Value Standard

Revenue and Taxation Code section 110, subdivisions (a) and (b) define "full cash value" or "fair market value" for California property tax assessment purposes. Subdivisions (d) and (e) set forth the limitations on taxation of intangible value and provide in part that:

> (d) Except as provided in subdivision (e), for purposes of determining the "full cash value" or "fair market value" of any taxable property, all of the following shall apply:
> (1) The value of intangible assets and rights relating to the going concern value of a business using taxable property shall not enhance or be reflected in the value of the taxable property.
> (2) If the principle of unit valuation is used to value properties that are operated as a unit and the unit includes intangible assets and rights, then the fair market value of the taxable property contained within the unit shall be determined by removing from the value of the unit the fair market value of the intangible assets and rights contained within the unit.
> * * *
> (e) Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use.

Revenue and Taxation Code section 212, subdivision (c) additionally states:

> (c) Intangible assets and rights are exempt from taxation and, except as otherwise provided in the following sentence, the value of intangible assets and rights shall not enhance or be reflected in the value of taxable property. Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use.

Further, Property Tax Rule 2, subdivision (a) states that "in addition to the meaning ascribed to them in the Revenue and Taxation Code, the words "full value", "full cash value", "cash value", "actual value" and "fair market value" mean the price at which a property, if exposed for sale in the open market with a reasonable time for the seller to find a purchaser, would transfer for cash or its equivalent under prevailing market conditions between parties who have knowledge of the uses to which the property may be put, both seeking to maximize their gains and neither being a position to take advantage of the exigencies of the other."

<u>Income Approach to Value</u>

See Issues 1 & 2, Applicable Law, p. 6.

Additionally, subdivision (c) of Rule 8 provides:

> The amount to be capitalized is the net return which a reasonably well informed owner and reasonably well informed buyers may anticipate on the valuation date that the taxable property existing on that date *will yield under prudent management* and subject to such legally enforceable restrictions as such persons may foresee as of that date.

(Property Tax Rule § 8, subd. (c), italics added.)

Further, subdivision (e) of Rule 8 states, in part, that:

> When income from operating a property is used, sufficient income shall be excluded to provide a return on working capital and other nontaxable operating assets and to compensate unpaid or underpaid management.

(Property Tax Rule § 8, subd. (e).)

***<u>Elk Hills Power LLC v. State Board of Equalization</u>* <u>(2013) 57 Cal.4th 593 (*Elk Hills*)</u>**

In *Elk Hills*, the California Supreme Court held that the Board directly assessed intangible value by assessing the value of the taxpayer's emission reduction credits (ERCs) in violation of Revenue and Taxation Code section 110 when it added the replacement cost of the ERCs to the power plant's taxable value. In that case, the Court examined the property taxation of intangible assets under the cost and income approaches to value. The cost approach is not at issue here.

In its analysis, the Court explained:

> [Revenue and Taxation Code] [s]ections 212(c) and 110(d) prohibit the direct taxation of certain intangible assets and rights .... However, in assessing taxable property under section 110(e), the Board may "assum[e] the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use."

With respect to the income approach to value, the Court states the taxpayer must articulate "a basis for attributing to the [proffered intangible rights or assets] a separate stream of income related to an enterprise activity," in order to impute to the income stream "some independent value that would be deducted from the total income generated by the taxable property." (*Id*. at p. 619.) This is because, "under an income stream approach, not all intangible rights have a quantifiable fair market value that must be deducted." (*Id.* at p. 617.)

To illustrate the analysis that must occur in each case, the Court acknowledged that there are two distinct lines of cases relating to intangibles where an operating property is being valued by use of the

CEA approach. (*Ibid.*) In the first line of cases, "courts have upheld income-based assessments that properly assumed the presence of intangible assets necessary to the productive use of taxable property without deducting value for intangible assets." (*Id.* at p. 618.) In the second line of cases, courts "disapproved assessments that failed to attribute a portion of a business's income stream to the enterprise activity that was directly attributable to the value of intangible assets and deduct that value prior to assessment." (*Ibid.*) As summarized by the Court:

> These cases illustrate the principle that although assessors may assume the presence of intangibles when considering the income stream derived from taxable property that is put to beneficial or productive use, the value of intangibles that directly enhance that income stream cannot be subsumed in the valuation of taxable property, and must be deducted from the unit prior to assessment.

(*Ibid.*)

Thus, the Court differentiated indirect intangibles (intangible assets that indirectly enhance the value of tangible property and the income stream produced by the tangible property by authorizing the beneficial and productive use of the tangible property) from direct intangibles (intangible business or enterprise assets that directly enhance the business income stream but are not necessary to the beneficial and productive use of the tangible property). (*Id.* at pp. 617-618.) In short, the cases indicate no deduction from the income stream should be made for indirect intangibles, while a deduction from the income stream for direct intangibles may occur when the taxpayer proves that the direct intangibles have created a separate stream of income or has enhanced the income stream above that which ordinarily would be reasonably expected from the property operating at highest and best use under normally prudent management. (See Property Tax Rule 8, subd. (c).)

Accordingly, the *Elk Hills* Court determined that if a quantifiable value of intangibles that *directly enhance* an income stream exist, the attributable value cannot be subsumed in the valuation of taxable property and must be deducted from the unit prior to assessment. Rule 8 sets forth how to determine when an income stream has been enhanced. Therefore, to properly determine the fair market value of operating real property using the income method, a direct intangible asset may only reduce net operating income for property tax assessment purposes if it is demonstrated that the income stream produced with the intangible asset is greater than the income stream produced when the property operates at its highest and best use under normally prudent management.

Specifically, the Court found that as “[t]here was no credible showing that there is a separate stream of income related to enterprise activity or even a separate stream of income at all that is attributable to the ERCs” in the evidence proffered by *Elk Hills*, “the Board was not required to deduct a value attributable to the ERCs under an income approach.” (*Elk Hills, supra,* 57 Cal.4th at p. 602.)

Analysis and Disposition

Respondent is presumed to have correctly determined the value of the property at issue, and Petitioner bears the burden of proving otherwise. The issue here is whether Petitioner has shown that Respondent erred by disallowing Petitioner’s requested deduction from the CEA value indicator for its trained and experienced workforce in place and management expenses.

Consistent with Rule 8 and *Elk Hills,* we note there is no deduction from the income stream for intangibles that indirectly enhance the value of the tangible property; further, we note while there may be a deduction for intangibles that directly enhance the income stream if the taxpayer shows that such intangibles have created a separate stream of income or an enhanced income stream to an extent greater than would be reasonably expected from the property at its highest and best use under prudent management pursuant to Property Tax Rule 8, here, Petitioner has made no such showing.

Here, Petitioner’s argument rests upon an argument that Respondent improperly included *direct* intangible assets (i.e., its trained/experienced workforce and management). However, as Respondent points out, for this requested deduction to be proper, Petitioner must show that its “trained and experienced workforce” and “management fees” produced an income for Petitioner superior to that which would have been produced with an ordinary workforce and management, as presumed by Rule 8 and the CEA approach. However, we note Petitioner has not put forth any specific argument or evidence to support that their workforce and management were both underpaid and overproducing of income, such that it was superior to that which would have been produced with an ordinary prudent workforce and management. Accordingly, we find that Petitioner has not met its burden of proof as to this issue.

/

/

Legal Issue 4: Whether Respondent Failed to Include a Replacement Allowance in the CEA Approach.

<u>Factual Findings and Contentions</u>

Petitioner asserts that Respondent has made no allowance for replacement and/or reserve costs. Petitioner provides no new or specific factual evidence to support the requested adjustment.

Respondent notes Petitioner's 2023 Board-adopted unitary value already includes a $11,287,288 capital replacement allowance for lien date 2023. Accordingly, Respondent contends it properly treated replacement costs.

<u>Applicable Law and Appraisal Principles</u>

<u>Burden of Proof</u>

See Issues 1 & 2, Applicable Law, p. 5.

<u>Value Standard</u>

See Issues 1 & 2, Applicable Law, p. 5.

<u>Income Approach</u>

See Issues 1 & 2, Applicable Law, p.6.

<u>Replacement Allowance in the CEA Approach</u>

"A replacement allowance (also called reserve for replacement) is an expense to replace components of an improvement that must be replaced at least once, and often several times, during the improvement's economic life." (AH 502, p. 73.)

<u>Analysis and Disposition</u>

Respondent is presumed to have correctly determined the value of the property at issue, and Petitioner bears the burden of proving otherwise. The issue here is whether Petitioner has shown that Respondent erred by failing to include a replacement allowance in the CEA value indicator.

We note that consistent with relevant appraisal guidance (AH 502), Respondent has utilized a capital replacement allowance of $11,287,288 in Petitioner's 2023 Board-adopted unitary value. While Petitioner appears to claim it was not included, Petitioner has not put forth any specific argument or evidence to support its claim or to support any further adjustment as to this issue. Accordingly, we find that Petitioner has not met its burden of proof as to this issue.

Legal Issue 5: Whether Respondent Erred by Including $63 Million of Wildfire Mitigation Capital Expenditures in the HCLD Value Indicator or Otherwise Failed to Capture Obsolescence.

Factual Findings and Contentions

Petitioner requests that $63 million in capital purchases made during calendar year 2022 be removed from the HCLD value indicator because these expenditures were made to satisfy CPUC-issued wildfire mandates[6] and would not otherwise have been purchased. (Petition, Exhibit 2021 v. 2022 Balance Sheet.) Petitioner notes to comply with the mandate, it responded with a plan to replace all lines, poles, conduits, and towers with a heavier, more fire retardant suppression material. As the lines are heavier, Petitioner asserts it requires new poles, conduits, and towers to support the replacement. Petitioner asserts that the replacement of old lines, poles, conduits, and towers, mean the old materials suffer from significant functional and economic obsolescence, and this should be acknowledged, as Board guidance recommends. Petitioner requests that the Board remove the entire $63 million in capital expenditures from its valuation to acknowledge the asserted additional obsolescence.

Further, Petitioner asserts that because of the legally mandated capital purchases, the old property suffers from obsolescence and that "the replacements are not eligible for rate base relief or recovery in the general rate case. The entire economic and financial burden falls on Liberty with no compensation or relief from the ratepayers."

Respondent contends no adjustment for obsolescence is appropriate for a number of reasons. First, it is unclear why a replacement of old property results in that property suffering from obsolescence, as such property is properly retired and removed from the books and, thus, the HCLD value indicator. Second, Respondent contends that even if obsolescence existed in the old property, it is unreasonable that such obsolescence would be exactly equal to the value of the new property purchased. Third, Petitioner has provided no evidence that its $63 million capital expenditure was all due to the CPUC-issued mandate (as opposed to, for example, regular replacement of aged property or planned wildfire mitigation). Respondent notes that such detail is particularly important since Petitioner's 2023 Wildfire Mitigation Plan reports that its actual 2022 spending was approximately $50 million[7] and its

---

[6] Petitioner cites to OIR Rulemaking 18-10-007, dated 10/25/18. (Petition, p. 7.)

[7] Liberty 2023 Wildfire Mitigation Plan, p. 30 < https://california.libertyutilities.com/uploads/2023-05-

Amended 2022 Risk Spending Accountability Report (RSAR)[8] suggests that its spending on safety, reliability, and maintenance was approximately $67 million, which was not all for the purposes of wildfire mitigation. Finally, Respondent notes that Petitioner has not provided evidence that the new property is not eligible for rate base inclusion. (Citing to Petitioner's General Rate Case decision[9] as well as its RSAR[10], which indicate that its capital expenditures were authorized).

Additionally, Respondent points out that importantly, even if the new property is not rate base eligible, this does not automatically mean the property has no value for property tax purposes. Respondent notes that whether property is or is not included in the rate base of a regulated utility is not solely determinative of whether it must or must not be included in HCLD, referencing AH 502. Further, Respondent points out that if these costs are mandated, without having purchased those assets, Petitioner (or any potential purchaser) would not be compliant with the mandate.

Applicable Law and Appraisal Principles

Burden of Proof

See Issues 1 & 2, Applicable Law, p. 5.

Value Standard

See Issues 1 & 2, Applicable Law, p. 5.

HCLD Approach to Value

See Issues 1 & 2, Applicable Law, p. 6.

Depreciation and the Cost Approach

In general, the cost approach recognizes three types of depreciation: physical deterioration, functional obsolescence, and external, or economic, obsolescence, through the application of the Board's replacement cost new trend factors and "percent" good factors. Obsolescence may occur when property is outmoded (functional obsolescence) or when some event has substantially diminished the future earning power of the property (economic obsolescence). (See Assessors' Handbook section 501, *Basic*

19_Liberty_2023_WMP_R1.pdf> [as of November 30, 2023].

[8] Amended 2022 Risk Spending Accountability Report (RSAR), p. 4, <https://docs.cpuc.ca.gov/PublishedDocs/Efile/G000/M508/K422/508422802.PDF> [as of November 30, 2023].

[9] Decision 23-04-043, p. 22-23, <https://docs.cpuc.ca.gov/PublishedDocs/Published/G000/M507/K581/507581365.PDF> [as of November 30, 2023].

[10] See ftn. 7, Liberty 2023 Wildfire Mitigation Plan at p. 4.

Appraisal (January 2002), pp. 80-83.) Functional obsolescence is the loss of value in a property caused by the property's loss of capacity to perform the function for which it was intended. (*Id*. at p. 81.) Economic obsolescence is the diminished utility of a property due to adverse factors external to the property being appraised and is incurable by the property owner. (*Id*. at p. 82.) The existence of any additional or extraordinary obsolescence must be supported with verifiable documentation and evidence, consistent with Board Guidelines. (See Property Tax Rule 6, subds. (d) & (e); Assessors' Handbook section 502, *Advanced Appraisal* (Reprinted January 2015) (AH 502), pp. 20-21; *Unitary Valuation Methods*, (2003), p. 30; and Cal. Bd. of Equalization, *Guidelines for Substantiating Additional Obsolescence*, at p. 1.)

<u>Analysis and Disposition</u>

Respondent is presumed to have correctly determined the value of the property at issue, and Petitioner bears the burden of proving otherwise. The issue here is whether Petitioner has shown that Respondent erred by including $63 million in capital expenditures for wildfire mitigation, or otherwise erred by not capturing obsolescence to its property.

We note that while Petitioner claims it should not be assessed on its $63 million of capital expenditures for lien date 2023, Petitioner has provided no legal or appraisal authority to support its requested treatment. Further, the Board notes that consistent with relevant appraisal guidance and Board Guidelines, the existence of any additional or extraordinary obsolescence must be supported with verifiable documentation and evidence. Here, Petitioner has not put forth any specific argument or evidence to support its claims of uncaptured obsolescence. Accordingly, based on the evidence and arguments submitted to the record, we find that Petitioner has not met its burden of proof as to this issue.

Legal Issue 6: Whether Respondent Removed Petitioner's Retired Assets from the HCLD Approach

<u>Factual Summary of the Issue, Analysis, and Conclusions</u>

At the Appeals Conference, Petitioner asserted that the value of retired assets being replaced with its capital expenditures were still included in the Respondent calculated HCLD value indicator.

Respondent indicated that if true, such asset costs were appropriately removable in the HCLD value indicator, but that Respondent needed verifiable assessee data to support such an adjustment.

After the Appeals Conference, the appeals attorney facilitated an information exchange. Petitioner submitted data on November 15, 2023. Respondent reviewed the submission and engaged in clarifications thereafter. On November 28, 2023, Respondent confirmed that Petitioner's HCLD value indicator should be adjusted by $5,393,173 to remove the value of assets that were removed physically from Petitioner's infrastructure and were disposed of but had not been removed yet from the HCLD. (Respondent Email Nov. 28, 2023.) Respondent notes that this recommended adjustment results in a reduction to the Petitioner's 2023 Board-adopted unitary value of $4,100,000. (*Ibid*.)

Accordingly, based on the evidence and arguments submitted, we find that Petitioner has met its burden of proof as to this issue, and that Respondent's recommended adjustment is supported by relevant law and appraisal principles applied to the evidence submitted in this petition.

DECISION

Accordingly, the 2023 petition for reassessment is granted in part, reducing Liberty Utilities, LLC's 2023 unitary value by $4,100,000 due to the verifiable evidence submitted in response to issue 6, and denied as to all other issues.*

Antonio Vazquez, Chair

Sally J. Lieber, Vice Chair

Ted Gaines, Member

Mike Schaefer, Member

Malia M. Cohen, Controller

*This decision was rendered in Sacramento, California on December 12, 2023. The summary decision document memorializing this decision was approved on February 21, 2024, in Sacramento, California.