State of California

Memorandum

630.0045

To : Mr. Jon Sperring
Office of Hon. Dean F. Andal

Date: April 19, 1999

From : Timothy W. Boyer
Chief Counsel

Subject: M Ranch -- The Inclusion of Sales Tax in the Calculation of Cost-Based Value Indicators for Personal Property Held at the Consumer Level

This is in response to your fax of March 25, 1999 to Larry Augusta, regarding the letter from Senator Dick Monteith that addressed the inclusion of sales tax in the value of certain personal property for property tax purposes. In particular, you ask to be advised of the "viability of regulatory action" with respect to this matter. The genesis of the issue is a letter from Mr. of M Ranch, Inc., which states that the County Assessor advised Mr. M that "when reporting the purchase price of ... equipment, [he] must also include the sales tax on said purchase."

As set forth below, it is the opinion of the legal staff that including sales tax in cost-based indicators used to value personal property held at the consumer level for property tax purposes is supported by case law, and violates neither the prohibition against double taxation, nor general principles of valuation and appraisal. In fact, the inclusion of sales tax in cost-based value indicators is both required under appraisal theory and consistent with generally accepted accounting principles. Because this appraisal practice is supported by case law, we are of the opinion that an attempt to change this practice by Board Rule or interpretation would not be legally supportable. Thus, instead of seeking regulatory action by the Board, we recommend that the taxpayer seek Legislative relief.

Law and Analysis

It appears that Mr. M 's concern about the inclusion of sales tax in the fair market value of his farming equipment for property tax purposes is twofold: (i) it constitutes double-taxation; and (ii) it is bad appraisal practice since sales tax should not be part of fair market value. The two issues are addressed below.

Double Taxation

There is no double taxation from a legal standpoint under the facts presented. The essence of the taxpayer's complaint is this: while the taxpayer has already paid a sales tax on purchase of the equipment, when computing a cost-based indicator of fair market value for such equipment for property tax purposes, the assessor added the sales tax amount to the retail purchase price in determining the value

The courts have held that double taxation occurs only when "two taxes of the same character are imposed on the same property, for the same purpose, by the same taxing authority within the same jurisdiction during the same taxing period." (*Russ Building Partnership v. San Francisco* (1988) 199 Cal.App.3d 1496, 1509.) Under the facts set forth by the taxpayer, the two taxes -- sales and ad valorem -- are not "of the same character," are not being assessed by the "same taxing authority" – and are likely not being assessed for the "same taxing period." Thus, there is no double taxation from a strictly legal viewpoint.

The Inclusion of Sales Tax in the Cost Indicator for Determination of the Fair Market Value of Personal Property Held at the Consumer Level

While it is true that the trade level principles for the valuation of personal property are incorporated into a Board rule -- namely, Rule 10 -- the inclusion of sales tax in the fair market value of personal property held at the consumer trade level is not purely a matter of Board regulatory action. Not only is such inclusion a matter of consensus as far as appraisal theory and generally accepted accounting principles, the California courts have recognized that, in using a cost-based indicator of value:

> ...The addition of taxes and freight charges to the list price of such equipment is consistent with an appraisal approach that gives consideration to the consumer's cost in arriving at market value. It is in accord with general accounting principles. The cost of an asset includes purchase price, brokerage commission, duties, transportation and all costs of placing the asset in a condition for use. (*Xerox Corp. v. County of Orange* (1977) 66 Cal.App.3d 746, 760; 1 Accountant's Encyclopedia (1962) pp. 168-169, *Lockheed Aircraft Corp. v. County of Los Angeles* (1962) 207 Cal.App.2d 119, 129-130.)

The above is true even if the equipment being appraised is leased rather than purchased. The form of the transaction is irrelevant where value is being determined at the consumer trade level. The fair market value of the property is the same whether the ultimate consumer owns it or leases it. (*Ex-Cello-O Corp. v. County of Alameda* (1973) 32 Cal.App.3d 135, 141.)[1]

Thus, in the opinion of the Legal Division, any attempt to exclude sales tax from the taxable value by regulation would not be found valid if challenged in court. We believe, therefore, that Mr. M should pursue relief through the Legislature.

If you have any questions, please call Robert Lambert at (916) 324-6593.

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cc: Ms. Marcy Jo Mandel
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[1]The trade level theory produces equity between taxpayers by assuring that the taxpayer consumer who owns the equipment will pay the same tax on identical equipment as the taxpayer who leases the equipment to the ultimate consumer. The market value of the equipment is the same if the property is held by the ultimate consumer regardless of who pays the tax. (*Xerox Corp. v. County of Orange, supra,* 66 Cal.App.3d 746, 755.)