September 16, 2015

From: Sherrie Kinkle
Tax Administrator II
County-Assessed Properties Division

To: Interested Parties

The following table summarizes the proposed "final" language for the issues that were outstanding at the close of the interested parties meeting held on September 9. Please note:

- The language for Matrix items 18 & 19 has been further revised.
- The rewrites for Matrix items 43, 44, 61, and 62 have been added.
- Three additional items have been added to accommodate the *Elk Hills* and *Sprint* cases.

Please provide me with any concerns that you may have with either the below items or any other items in the draft of the *State Assessment Manual* by October 2, 2015. The draft is posted on the project webpage at www.boe.ca.gov/proptaxes/sam_timeline.htm.

Thank you for your participation in this project.

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Matrix Number	***Comment***
18 & 19	**Additional Language Submitted by Doug Mo:** Subdivision (e) states: "Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the property to beneficial or productive use." ~~Appellate courts have distinguished between "assuming the presence" of tangibles and adding a value component for such intangible assets or rights.~~ However, sections 110(e) and 212(c) do not authorize adding an increment to the value of taxable property to reflect the value of intangible assets." [Fn] [Fn] *Elk Hills Power, LLC v. Board of Equalization* (2013) 57 Cal.4th 593, 616 (quoting the Bd. of Equalization Assessors' Handbook Section 502, *Advanced Appraisal*, (Dec 1998), ch. 6, p. 152.
25	**Additional Language Submitted by Ken Thompson:** Thus, from a theoretical perspective, the principle of unit valuation holds that the unit of property appropriate for the estimation of a market value should include all property items that are *functionally related* and with *common ownership* or control (such as leased property or a possessory interest).

43	**Section revised by Ken Thompson:** Section 100.95, effective beginning with the 2007-2008 fiscal year, requires the county auditor to allocate property tax revenue from qualified public utility owned property newly constructed after January 1, 2007 ~~to those governmental agencies and school entities in the tax-rate area where the property is located~~ in a prescribed manner rather than distributing in the same manner as the countywide tax-rate area. ~~The county, school entities in the county, and certain special districts are to receive the same proportion of the revenues as was received from the countywide unitary allocation in the previous fiscal year in the same manner as other unitary property. The remaining revenue is allocated to the city or county as determined by the tax-rate area where the property is located and is excluded from the countywide distribution directed by section 100.~~
44	**No further revisions made to this section:** As with section 100.95, this law requires that the portion of ~~value~~ revenue allocated ~~to~~ from the qualified property be assigned to the ~~specific tax rate area~~ City of Oakley and the East Contra Costa County Fire Protection District where the property is located, rather than ~~assigning it to~~ distributing in the same manner as the countywide tax-rate area.
61	**Section to by Richard Moon:** *Cardinal Health v. County of Orange* (2008) 167 Cal.App.4th 219 The issue in this case was whether application software was ~~not~~ subject to property taxation if it came ~~"~~bundled~~" or "embedded"~~ with taxable computer hardware. The Court of Appeal held that bundling by itself is not dispositive of whether application software is taxable under Revenue and Taxation Code sections 995 and 995.2, as basic operational programming. Rather, pursuant to Property Tax Rule 152, subdivision (f), when application software is bundled into the sale or lease price of computer equipment, the burden is on the taxpayer to segregate the value of nontaxable application software from the otherwise taxable value of the computer and basic operational programs. ~~The assessment appeals board and the trial court agreed with the assessor that because the application software was bundled or embedded with taxable computer hardware, the assessor could ignore the taxpayer's evidence of the value of its nontaxable application software and assess the total amount charged for the software and hardware bundle. The Court of Appeal reversed the decision of the trial court, and held that the fact that the nontaxable application software was bundled or embedded with taxable computer hardware did not excuse the assessor from his duty to make an informed judgment as to the value of taxable and nontaxable components of the bundled software and hardware.~~
62	**Section to be revised by Richard Moon:** *Elk Hills Power, LLC v. Board of Equalization* (2013) 57 Cal.4th 593. The issue in this case was whether the Board properly applied (as opposed to "banked") emission reduction credits (ERCs) in determining the unitary value of Elk Hills' state-assessed electric power plant for purposes of property taxation under both the replacement cost less depreciation approach (RCLD) and the income approach. The Supreme Court concluded that "the Board directly and improperly taxed the power company's ERCs when it added their replacement cost to the power plant's taxable value." The Supreme Court, however, clarified that "[w]here the taxpayer does not proffer evidence that the Board included the fair market value of an intangible right or asset in the unit whole, the Board would

	not have to make a deduction prior to assessment." With respect to the income approach, the Court distinguished between two lines of cases. "In the first line of cases, as in this case, courts have upheld income-based assessments that properly assumed the presence of intangible assets necessary to the productive use of taxable property without deducting a value for intangible assets…The second line of cases 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." The Court concluded that "the Board was not required to deduct a value attributable to the ERCs under an income approach" because "[t]here was no credible showing that there is a separate stream of income related to enterprise activity." Accordingly, the Court determined that the Board correctly "estimated the amount of income the property is expected to yield over its life and determined the present value of that amount."
New issue Page 13, Line 21	**Text revised to reflect *Elk Hills* language:** Subdivisions (d), (e), and (f) of section 110 address the treatment of intangible assets and rights. Subdivision (d) provides that: (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, 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; and (3) the exclusive nature of a concession, franchise, or similar agreement is an intangible asset that shall not enhance the value of taxable property, including real property. [19] ~~However, in~~ In applying ~~the above principles, the Legislature stated at the beginning of subdivision (d) that its provisions are expressly subject to the language in subdivision (e). Subdivision (e) states: "Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the property to beneficial or productive use."~~ a replacement cost valuation approach, assuming the presence of intangible assets or rights "do(es) not authorize adding an increment to the value of table property to reflect the value of intangible assets." [20] In applying a capitalized income approach, 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. [21] [19] For additional discussion of the market value concept, see Assessors' Handbook Section 501, *Basic Appraisal*, and Assessors' Handbook Section 502, *Advanced Appraisal*. [20] *Elk Hills Power, LLC v. Board of Equalization* (2013) 57 Cal.4th 593, 616 citing Assessors' Handbook Section 502, *Advanced Appraisal* (Dec. 1998) p. 152. [21] *Elk Hills Power, LLC v. Board of Equalization* (2013) 57 Cal.4th 593, 619.

New issue Matrix Item 57	**Revise footnote:** If the Board denies the petition and, hence, the claim, then upon payment of tax to the county or counties, the assessee may proceed directly to file an action in superior court for a refund of the tax. [Fn] [Fn] ~~*Sprint Telephone v. State Board of Equalization*~~ *Sprint Telephony PCS, L.P. v. State Bd. of Equalization* (2015) 238 Cal.App.4th 871, 882-83, as modified on denial of reh'g (Aug. 14, 2015), review filed (Aug. 24, 2015).
New issue Handbook page 80	**Add case summary:** *Sprint Telephony PCS, L.P. v. State Bd. of Equalization* (2015) 238 Cal. App. 4th 871, as modified on denial of reh'g (Aug. 14, 2015), review filed (Aug. 24, 2015). The appellate court noted that the plain language of Revenue and Taxation Code section 5148, subdivisions (f) and (g) requires that a telephone company wanting to preserve its right to file a judicial tax-refund action must state that its reassessment petition is also to serve as a claim for refund. The court then concluded that Sprint's failure to designate its petition for reassessment as also a claim for refund, by either checking a box on the reassessment petition or otherwise indicating its intent that the petition serve as a claim, barred Sprint's property tax refund action under section 5148. The court noted that although the company argued that the notice requirement was an unfair technicality and that the counties where it owned property were not prejudiced by its failure to comply, the trial court did not err when it relied on the principle requiring strict compliance with tax statutes in accordance with the constitutional limitation in California Constitution article XIII, section 32, vesting the Legislature with plenary control over the manner in which tax refunds could be obtained.