



STATE BOARD OF EQUALIZATION

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Executive Director
No. 2000/002

January 7, 2000

TO COUNTY ASSESSORS,
COUNTY COUNSELS,
ASSESSMENT APPEALS BOARDS,
AND OTHER INTERESTED PARTIES:

**NOTICE OF PROPOSED REGULATORY ACTION
BY THE
STATE BOARD OF EQUALIZATION**

AMEND PROPERTY TAX 10 –TRADE LEVEL FOR TANGIBLE PERSONAL PROPERTY

PUBLIC HEARING: WEDNESDAY, FEBRUARY 23, 2000 AT 1:30 P.M.

NOTICE IS HEREBY GIVEN:

The State Board of Equalization, pursuant to the authority vested in the Board by section 15606, subd. (c) of the Government Code, proposes to amend Rule 10, Trade Level For Tangible Personal Property, in Title 18, Division 1 of the California Code of Regulations. A public hearing on the proposed regulation will be held in Room 121, 450 N Street, Sacramento, at 1:30 p.m., or as soon thereafter as the matter may be heard, on February 23, 2000. Any person interested may present statements or arguments orally at that time and place. Written statements or arguments will be considered by the Board if received by February 23, 2000.

INFORMATIVE DIGEST/PLAIN ENGLISH OVERVIEW

The State Board of Equalization proposes to amend Rule 10 to delete provisions that provide guidance on the valuation of business inventory for property tax assessment purposes to reflect a change in existing law. In 1980, the Legislature repealed former section 219 of the Revenue and Taxation Code, which provided a partial exemption from taxation for business inventory from 1970 through 1980, and enacted the current section 219 to provide a full exemption for business inventory. (Stats. 1980, Ch. 411, in effect July 11, 1980).

The proposed amendments to Rule 10 clarify and make specific Revenue and Taxation Code Sections 110 and 401, and Article XIII, section 1(a) of the California Constitution. Rule 10 specifies that tangible personal property shall be valued at the proper level of trade, based on its location and use on the lien date. The trade level concept is consistent with Constitutional and

statutory mandates that property shall be valued at fair market value. The Constitution requires that all taxable property must be assessed at fair market value. (Cal. Const. Art. XIII, § 1(a).) Section 110, subd. (a) of the Revenue and Taxation Code defines fair market value or full cash value as the amount of cash or its equivalent which property would bring if exposed for sale in the open market under conditions which neither buyer or seller could take advantage of the exigencies of the other. The fair market value mandate of Section 110 requires assessment uniformity.

The trade level concept is that property normally increases in value as it progresses through production and distribution channels to the consumer, whether or not the cost or value added is booked in accounting records. The trade level concept is applicable when book cost does not provide adequate information for making a fair market appraisal and is most frequently applied to leased equipment and self-constructed equipment. Trade level adjustments ensure assessment uniformity for similar property that may be acquired through different means including self constructed, leased, or purchased by a consumer. The proposed amendment of Rule 10 provides guidance on the valuation of property to ensure assessment uniformity and valuation of personal property at fair market value.

The express terms of the proposed action, written in plain English, are available from the agency contact person named in this notice.

COST TO LOCAL AGENCIES AND SCHOOL DISTRICTS

The State Board of Equalization has determined that the proposed amendment of Rule 10 does not impose a mandate on local agencies or school districts. Further, the Board has determined that the amended rule will result in no additional direct or indirect costs to any State agency or any local agency or school district that is required to be reimbursed under Part 7 (commencing with Section 17500) of Division 4 of Title 2 of the Government Code, and that there are no other non-discretionary costs or savings imposed on local agencies, or cost or savings in Federal funding to the State of California.

EFFECT ON BUSINESS

Pursuant to Government Code Section 11346.53(c), the Board of Equalization finds that the amendment of Rule 10 will not have a significant adverse economic impact on business, because the proposed changes only clarify existing constitutional and statutory interpretations.

The amendment of Rule 10 will neither create nor eliminate jobs in the State of California nor result in the elimination of existing businesses nor create or expand business in the State of California.

The amendment of the rule as proposed will not be detrimental to California businesses in competing with businesses in other states.

The proposed amendment of the rule will not affect small business because the rule only clarifies existing statutory interpretations.

ADVERSE ECONOMIC IMPACT ON PRIVATE PERSONS/BUSINESSES

No impact.

SIGNIFICANT EFFECT ON HOUSING COSTS

No significant effect.

FEDERAL REGULATIONS

Rule 10 has no comparable Federal regulations.

PLAIN ENGLISH STATEMENT

Preparation of the proposed amendment to Rule 10 included consideration of the “plain English” requirement. Any technical terms that may be unfamiliar to the intended users and are not industry-recognized are defined or explained.

AUTHORITY

Government Code section 15606, subdivision (c).

REFERENCES

California Constitution, article XIII, section 1(a); Revenue and Taxation Code sections 110 and 401.

CONTACT

Questions regarding the content of the proposed regulation should be directed to: Ms. Mary Ann Alonzo, Tax Counsel, at P.O. Box 942879, 450 N Street, MIC:82, Sacramento, CA 94279-0082. Telephone: (916) 324-1392; FAX (916) 323-3387.

Written comments for the Board’s consideration or requests to present testimony and bring witnesses to the public hearing should be directed to Ms. Mary Ann Stumpf, Regulations Coordinator, (916) 322-9569, and P. O. Box 942879, 450 N Street, MIC:80, Sacramento, CA 94279-0080.

ALTERNATIVES CONSIDERED

The Board must determine that no alternative considered would be more effective in carrying out the purpose for which this action is proposed or be as effective and less burdensome to affected private persons than the proposed action.

AVAILABILITY OF STATEMENT OF REASONS AND OF TEXT OF PROPOSED REGULATIONS

The Board has prepared a statement of reasons and underscore version of the proposed rule. Those documents and all information on which the proposed regulation is based are available to the public upon request. The Rulemaking file is available for public inspection at 450 N Street, Sacramento, California. Requests for copies should be addressed to Ms. Mary Ann Stumpf, Regulations Coordinator, (916) 322-9569, at P. O. Box 942879, 450 N Street, MIC:80, Sacramento, CA 94279-0080. The express terms of the proposed rule are available on the internet at the Board's web site, <http://www.boe.ca.gov>.

ADDITIONAL COMMENTS

Following the hearing, the State Board of Equalization may in accordance with law, adopt the amended rule if the text remains substantially the same as described in the text originally made available to the public. If the State Board of Equalization makes modifications which are substantially related to the originally proposed text, the Board will make the modified text, with the changes clearly indicated, available to the public for fifteen days before adoption of the regulation. The text of any modified rule will be mailed to those interested parties who commented on the proposed regulatory action orally or in writing or who asked to be informed of such changes. The modified rule will be available to the public from Ms. Stumpf. The State Board of Equalization will consider written comments on the modified rule for fifteen days after the date on which the modified rule is made available to the public.

Dated: December 20, 1999

STATE BOARD OF EQUALIZATION

/s/ Janice Masterton

Janice Masterton, Chief
Board Proceedings Division

Rule 10 TRADE LEVEL FOR TANGIBLE PERSONAL PROPERTY

(a) In appraising tangible personal property, the assessor shall give recognition to the trade level at which the property is situated and to the principle that property normally increases in value as it progresses through production and distribution channels. Such property normally attains its maximum value as it reaches the consumer level. Accordingly, tangible personal property shall be valued by procedures that are consistent with the general policies set forth herein.

~~(b) Tangible personal property in the hands of a primary producer which is produce of the soil and for which there are regular markets established by the buyers of the property, such as petroleum and other minerals, logs, livestock, and other farm products, shall be valued at the price offered by the buyers less the unincurred cost of preparing the property for market and of moving the property to the market place at which such price is applicable, or plus the cost of moving the goods from that market place to the place at which they are to be processed if the latter location is the tax situs.~~

(b) Except as provided by the following subdivisions, tangible personal property held by a consumer shall be valued at the amount of cash or its equivalent for which the property would transfer to a consumer of like property at the same trade level if exposed for sale on the open market. This value shall be estimated in accordance with regulations 4, 6, and 8. If a cost approach is employed, the cost shall include the full economic cost of placing the property in service. Full economic cost (i.e., replacement or reproduction cost), includes costs typically incurred in bringing the property to a finished state, including labor and materials, freight or shipping cost, installation costs, sales or use taxes, and additions for market supported entrepreneurial services (with appropriate allowances for trade, quantity, or cash discounts).—Full economic cost does not include extended service plans or extended warranties, supplies, or other assets or business services that may have been included in a purchase contract.

~~(c) Tangible personal property in the hands of a manufacturer who holds it for processing or for sale shall be valued at the amount for which it would transfer to other manufacturers of like property. This value shall be estimated (1) by reference to the cost of the property in its condition on the lien date or (2) by reference to the cash price at which the manufacturer is expected to sell the property less costs yet to be incurred and experienced gross profits. When the cost approach is used, there shall be added to the cost of raw materials all other direct costs and manufacturing burden, including depreciation and property taxes, but excluding selling and general administrative costs. Unprocessed raw material cost is the cost of replacement on the lien date as evidenced by recent purchases by the assessee or other recent market transactions.~~

(c) Tangible personal property leased, rented, or loaned for a period of six months or less, having a tax situs at the place where the lessor normally keeps the property as provided in regulation 204, shall be valued at the amount of cash or its equivalent for which it would transfer to other lessors or retailers of like property. The value may be estimated by reference to the price at which the lessor could be expected to sell the property at fair market value to other lessors or retailers of like property. If that price is unknown, then the value may be estimated by reference to one or more of the following indicators of value: (1) the lessor's full economic cost of the

property with a reasonable allowance for depreciation; (2) the cost indicated in subdivision (e) if the lessor is also the manufacturer; or (3) in accordance with subdivision (b).

~~(d) Tangible personal property in the hands of a retail merchant who holds it for sale, lease, or rental shall be valued at the amount for which it would transfer to other retailers of like property; and tangible personal property in the hands of a wholesale merchant who holds it for sale, lease, or rental shall be valued at the amount for which it would transfer to other wholesalers of like property. This value shall be estimated (1) by reference to the property's cost to the merchant, including freight in and deducting trade, quantity, and cash discounts, with reasonable allowance based on proper substantiation for damaged, shopworn, out-of-style, used, or overage stock, or (2) by reference to the price at which the merchant is expected to sell the property less his experienced gross profit.~~

(d) Tangible personal property leased, rented, or loaned for an extended but unspecified period or leased for a term of more than six months, having tax situs at the lessee's situs as provided in regulation 204, shall be valued by estimating the cash price or its equivalent for which the property could be sold at fair market value to an outside customer operating at the same level of trade as the lessee. If that price is unknown, then the value may be estimated by reference to one or more of the following indicators of value: (1) the lessee's full economic cost of the property with a reasonable allowance for depreciation, or (2) in accordance with subdivision (b).

~~(e) Tangible personal property in the hands of a person who holds it for consumption shall be valued in accordance with sections 4, 6, and 8 of this subchapter. When, however, such property is leased or rented for a period of less than six months so that its tax situs, as provided in section 204 of this chapter is at the place where the lessor normally keeps the property, it shall be valued in accordance with the last sentence of subdivision (d).~~

(e) Tangible personal property acquired from internal sources for self-consumption or use, shall be valued by estimating the cash price or its equivalent for which the property could be sold at fair market value to an outside customer using the property at the same trade level, (with appropriate allowances for trade, quantity, or cash discounts). If that price is unknown, then the value may be estimated by reference to one or more of the following indicators of value: (1) the cost of the property in its condition and location on the lien date, had it been acquired at fair market value from an outside supplier (including labor, materials, overhead, interdivisional and/or intercompany profits, interest on borrowed or owner supplied funds, sales or use tax, installation, and other costs incurred in bringing the property to a finished state, with appropriate allowances for trade, quantity, or cash discounts, and depreciation), or (2) in accordance with subdivision (b). The cost of the property in its condition and location on the lien date, had it been acquired at fair market value from an outside supplier, does not include extended service plans or extended warranties, supplies, other assets or business services. The quantity discount allowed a manufacturer, when it is its own largest customer, should be at least as large as that allowed its largest wholesale or retail customer.

~~(f) When tangible personal property is in the hands of a person engaged in two or more of the functions of producer, manufacturer or processor, wholesaler, retailer, or consumer, the level of trade at which the property is held shall be determined by reference to its form, location,~~

~~quantity, acquisition source, and probable purchasers or lessees. A person is operating at two or more levels when the property consists of raw materials, semi-manufacturers, or finished goods which were acquired from sources within a business entity (other than component parts meeting the tests of the following sentence) and the property is held (1) for consumption by the business entity or (2) for processing and/or marketing in competition with similar products marketed by other business entities that have purchased like raw materials, semi-manufacturers, or finished goods at the same stage of production from external sources. Component parts held at the manufacturing-processing level, however, shall not be considered to be at a higher level than that at which they are manufactured when they have been manufactured by a business entity specifically and exclusively for (1) incorporation by the entity in its finished product, (2) marketing as replacement parts for its finished product, or (3) both.~~

~~When it is concluded that the person holding tangible personal property is operating at more than one trade level, property at the higher trade level or levels acquired from internal sources shall be valued (1) by estimating what the property, in its condition and location on the lien date, would have cost had it been acquired in an arm's length transaction from an outside supplier, (2) by reference to the cash price at which the property could be sold in an arm's length transaction to an outside customer less a reasonable gross profit, or (3) if held at the consumer level, in accordance with subdivision (e).~~

~~(g) Storage of tangible personal property in a warehouse, in and of itself, does not alter the trade level. The trade level of such property will be determined in accordance with subdivision (f).~~

(f) Tangible personal property in the hands of a person engaged in the function of a manufacturer, wholesaler, or retailer and a consumer shall be valued by estimating the cash price or its equivalent for which the property could be sold at fair market value to an outside customer operating at the same level of trade. The property shall be valued based on how it is situated or used on the lien date pursuant to subdivisions (b), (c), (d), and (e).

Authority: Government Code Section 15606(c).

References: Chapter 147, Statutes of 1966, First Extraordinary Session.
Sections 110, 401, Revenue and Taxation Code.