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Senate Bill 357 (Hall)
Date: Introduced
Program: Property Tax
Sponsor: Board of Equalization
RTC Sections 11206, 11292, 11293, and 11294
Effective January 1, 2016

Summary: Changes the method of measuring railcar presence in California from car days to mileage for purposes of imposing the Private Railroad Car Tax.

Purpose: To establish a simplified procedure for assessing privately owned railroad cars (PRRCs) that is appropriate and fair, that allocates value among states in a consistent manner, and reduces the administrative burden on both taxpayers and the Board of Equalization (BOE).

Fiscal Impact Summary: Annual revenue loss of $506,000.

Existing Law: California law imposes a property tax on privately owned railroad cars (PRRCs) operating on the state's railroads.[1] The law specifies the methodology to value PRRCs.

Valuation. The BOE determines value based on acquisition cost less depreciation for each railroad car class in the owner's fleet. The law allows additional deductions in the form of depreciation for cars purchased used and newly installed improvements (i.e., betterments) to existing cars.

Apportionment. Because PRRCs are involved in interstate travel, the value must be apportioned among the states. PRRCs are taxed on a pro rata basis consistent with actual presence in California. The law requires presence to be measured by the number of "car-days" each car class spent in the state during the preceding calendar year.

Proposed Law:

Valuation. This bill changes the way PRRCs purchased used are valued. It also changes how to value improvements made to existing railroad cars. Specifically:

- **Used Cars.** The bill eliminates the additional depreciation given to the purchase of used PRRCs by deleting the phrase "minus the age at acquisition."
- **Improvements.** The bill eliminates the additional depreciation given to improvements made to PRRCs by deleting subdivision (g) of Section 11292, the provision that states the new improvements are based on the PRRC's remaining depreciable life.

For valuation purposes, the bill continues to calculate depreciation for all cars based on a 22- or 25-year life, depending on car class.

Apportionment. This bill changes the way physical presence is measured from the number of days each car class spends in California to the pro rata number of miles the owner's PRRC fleet traveled in California. This eliminates the need to distinguish cars by class (data which is not actually maintained).

In General: The PRRC tax is in lieu of all other state and local ad valorem property taxes on PRRCs. Unlike other property taxes, the taxes are state general fund revenues.

Generally, companies that own PRRCs haul their own products or lease their cars to shippers. The PRRC tax does not apply to railroad companies.

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[1] Part 6 of Division 2 of the Revenue and Taxation Code (commencing with Section 11201).

Background:

The **car-day count software program** the BOE uses to measure presence is near the end of its useful life. Switching to a mileage-based system would avoid the cost to replace this software, which BOE staff estimates would cost at least $500,000.

The car-day count system measures the presence of PRRCs within California. Each month, five railroad car companies report border crossing data (movements in and out of California) to the BOE. The BOE's computer program processes this data and determines the number of days each car was physically present in California during the calendar year immediately preceding each lien date. The results are converted to an equivalent number of cars, for a specific car class based on the American Association of Railroads Alpha designation, as explained below.

Applying the car-day method, the car's value is multiplied by the number of days per year that each car was present in California. For example, if the aggregate number of days a company's tank cars were physically present in California was 730 days, the equivalent number of tank cars would be 2 (730 days / 365 days). If the tank car's value is $50,000, calculated using the statutorily required method, then this value is multiplied by 2 to arrive at a $100,000 taxable value of this class of PRRCs ($50,000 x 2).[2] The company's liability is therefore the tax imposed on an assessed value of $100,000.

Legislation. Last year, Assembly Bill 2262 (Frazier) contained a nearly identical proposal that was held in the Senate Appropriations Committee.

Commentary:

1. **Conformity.** A mileage based system conforms to the way other states that impose a PRRC tax measure presence. In addition, railroad companies use mileage to bill PRRC owners for traveling on their systems. Thus, mileage data is readily available since it's already captured for other state's tax systems and railroad billing.

2. **Reduces Taxpayer Compliance Burden**. Switching to mileage reduces the compliance burden on PRRC owners and railroads to comply with California's unique car-day system. Using the same mileage system as other states also reduces compliance costs for PRRC owners and railroads.

3. **Increases Efficiency and Reduces Administrative Complexity.** Measuring presence with a mileage based system is less complex and less costly to administer. Making the tax easier to administer would allow the BOE to re-direct senior staff to other activities and allow junior staff to assume these duties.

4. **Avoids Need to Replace Aged Software Program.** The car-day count software program the BOE uses to measure presence is near the end of its useful life. Switching to a mileage-based system avoids the cost to replace the software, which BOE staff estimates would cost at least $500,000. The current program uses obsolete programming language that is no longer supported and thus increasingly difficult to maintain.

5. **Valuation changes.** The valuation changes (1) eliminate additional depreciation given to cars purchased used and (2) eliminate additional depreciation given to new additions and betterments to existing cars. Depreciation will continue to be calculated for all cars based on a 22- or 25-year life. These valuation changes reduce the bill's overall revenue impact, and simplify tax reporting and administration. Using acquisition cost, with adjustments for betterments and depreciation, produces values that are reasonably within fair market value range.

6. **Improves Accuracy.** The mileage data is more accurate than car days because the BOE must rely on 2nd and 3rd party data (from Rail Inc.) for verification of car days reported by railroads (these sources provide information on movements into and out of California). Under the mileage based system,

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[2] In addition, to comply with the Federal Railroad Revitalization and Regulatory Reform Act (the 4-R Act), the BOE must assess rail transportation property, including PRRCs, at a percentage of full value. For 2014-15, the percentage was 76.38% of market value.

the BOE could obtain mileage data directly from the source (private car owners). Car day counts have not always been accurate.

7. **More Predictable and Stable Revenue Stream.** A review of mileage data from 2010-14 indicated that moving to mileage-based assessments will result in a more predictable and more stable PPRC revenue stream than car-day-based assessments.

Administrative Costs: The BOE would save some costs by (1) canceling an annual $13,000 car registration subscription and (2) avoiding the estimated $500,000 minimum cost to replace the aging car-day counting software.

Revenue Impact:

Background, Methodology, and Assumptions. The state retains the revenue from the PRRC tax. In 2014, the tax revenue from 221 PRRC companies was $8,921,960.[3] Annual tax revenues vary with the level of new car investments and California economic activity. For 2009 to 2014, total assessed values and tax revenues are as follows:

Year	Total Full Value	Total Assessed Value	Tax Rate	Amount of Tax
2009	$922,188,463	$535,934,266	1.097%	$5,879,199
2010	$865,148,570	$564,386,221	1.102%	$6,219,536
2011	$901,214,873	$732,007,910	1.107%	$8,103,328
2012	$879,655,573	$720,268,858	1.108%	$7,980,579
2013	$932,432,014	$753,819,189	1.108%	$8,352,317
2014	$1,055,786,235	$806,687,203	1.106%	$8,921,960

Mileage-based assessments could result in increased or decreased tax liability for individual companies depending on their specific business operation. Thus, the changes don't impact all companies uniformly. Most companies would have reduced taxes from the proposed changes, but some would see taxes increase.

The revenue impact of switching to a mileage based system is difficult to predict with certainty because railcar activity in California and elsewhere depends upon economic conditions, investment choices, labor relations, and political practicalities. In addition, the revenue impact depends on two variables that change each year: the tax rate and the 4R Act Assessment ratio.

BOE staff collected mileage data for years 2010-2014 from large companies that comprise 59% to 65% of total taxes imposed for those years. Staff then applied the proposed valuation changes and presence calculations for those companies and compared taxes actually imposed for those periods to taxes that would be imposed under this bill. The results vary. For the 2010 and 2012 assessment years, taxes would have been higher, but over the entire period total taxes were lower. Staff then applied the sample results to the remainder of the Private Railroad Car Tax Roll. This indicated an average annual reduction of $507,000 in tax over this period.

Summary. Comparing mileage and car-day data from the last five years, staff estimates that the mileage based system switch and other valuation changes would result in a revenue loss of $507,000 annually.

Qualifying remarks. This loss would be offset in the first year by canceling an annual $13,000 car

[3] 2014 Private Railroad Car Assessment Value Recommendations
Private Railroad Car Tax Historical Data 1938 to present (BOE Statistical Table 17B)
Private Railroad Companies (BOE Statistical Table 17A)

registration subscription and avoiding the one-time $500,000 cost to replace the aging car-day counting software.

BOE estimates also conclude that moving to mileage-based assessments will result in a more predictable and more stable revenue stream.

This revenue estimate does not account for any changes in economic activity that may or may not result from enactment of the proposed law.