State of California

Board of Equalization
Legal Department-MIC: 82

Memorandum

To: Honorable Betty T. Yee, Chairwoman
Honorable Judy Chu, Vice-Chair
Honorable Bill Leonard
Honorable Michelle Steel
Honorable John Chiang

Date: August 2, 2007

From: Kristine Cazadd KC by Robert Lambert
Chief Counsel

Subject: **Proposed Property Tax Rule 474, *Petroleum Refining Properties***
August 14 Board Meeting – Chief Counsel Matters – Item J1- Rulemaking
Request for Board Readoption of Proposed Property Tax Rule 474

The Board staff requests that the Board readopt Proposed Rule 474, *Petroleum Refining Properties,* the text of which is attached hereto, in compliance with OAL's direction. (See attached Proposed Rule 474 and attached Notice of Disapproval of Regulatory Action.) The proposed rule defines "petroleum refining property" and establishes a rebuttable presumption, for purposes of recognizing declines in value, that land, improvements, and fixtures and other machinery and fixtures classified as improvements constitute one appraisal unit, except when measuring declines in value caused by disaster, in which case land constitutes a separate appraisal unit.

Background Information

The proposed rule was originally submitted by the Board to the Office of Administrative Law (OAL) on December 26, 2006. It was subsequently withdrawn by the Board on February 8, 2007, before OAL took any action on the filing. On April 27, 2007, the Board resubmitted the proposed rule to OAL.[1] Subsequently, on June 8, 2007, OAL disapproved the regulatory action on the ground that the Initial Statement of Reasons (ISR) failed to provide the public with the rationale for the Board's determination that the provisions in Proposed Rule 474 are needed to carry out the purpose for which it is proposed. (See attached Notice of Disapproval of Regulatory Action.)

Thereafter, on July 17, 2007, in response to OAL's disapproval of regulatory action on June 8, 2007, the Board referred the ISR to the 15-day file for public comment, recommending that changes be made to the statement to more fully explain the proposed rule's purpose and

[1] This resubmission incorporated the prior rulemaking file by reference and made one minor, nonsubstantive deletion to the reference citations for Proposed Rule 474.

necessity consistent with the OAL decision. At that time, a revised ISR and an underscore-and-strikeout version of revised Proposed Rule 474 was sent to the county assessors, county counsels, and other interested parties and also posted on the Board's Web site. (See attached copies of the 15-day letter to the interested parties; the Amended Initial Statement of Reasons; and Proposed Rule 474.)

Responses to Public Comments

The Board received the following new written comments on Proposed Rule 474 and the revised ISR. The written comments were received during the 15-day public comment period. (See attached written comments, discussed below in the order received.)

Written Comments

Comment 1. Attorney Cris O'Neall of Cahill-Davis & O'Neall

In a letter dated July 23, 2007, Mr. Cris O'Neall of Cahill-Davis & O'Neall wrote in opposition to Proposed Rule 474, stating that there is no evidence supporting the assertion that refineries are always bought and sold as a single unit. As evidence to the contrary, Mr. O'Neall submitted listings and trade articles showing refinery fixtures being sold separately from the land and other improvements.

Staff's Response

While evidence that refineries normally are bought and sold as a single unit are not included in the revised ISR, such evidence is included in the rulemaking record. As stated in the Response 3-1 of the attached Final Statement of Reasons (FSR), Thomas Parker, Deputy County Counsel, Sacramento County; Rick Auerbach, Los Angeles County Assessor and then President of the California Assessors' Association; Lance Howser, Chief Assessor, Solano County; and Robert Quon, Director of Major Appraisals for the Los Angeles County Assessor's office, all testified that refineries are in fact bought, sold, and valued as a single unit. (See attached Final Statement of Reasons.)

Additionally, the evidence submitted by Mr. O'Neall, and similar evidence, was, in part, previously submitted to the Board and is already included as part of the rulemaking record. Such evidence includes listings from companies offering fixtures for sale and descriptions of fixtures that were sold and relocated to other refineries. The Board recognizes that, while individual refinery fixtures (like all fixtures) sometimes depreciate or become obsolete and, thus, periodically may be replaced or upgraded, that does not negate the fact that when refineries transfer as a unit, what is transferred typically consists of the entire operating unit, comprising land, improvements, and fixtures.

Furthermore, Mr. O'Neall does not provide any evidence that, when refineries do sell as a unit, the fixtures typically are sold separately from the land and other improvements, such as in the case where certain tenant improvements commonly are excluded from the sale of a shopping center. Instead, the evidence provided only shows that refinery fixtures are

periodically removed, replaced, or scrapped and that there is a secondary marketplace where these second-hand fixtures may be traded.

Finally, Proposed Rule 474 only creates a presumption that the land, improvements and fixtures are a single appraisal unit. Where there is sufficient evidence to rebut that presumption, the fixtures can be considered a separate appraisal unit for purposes of declines in value.

Comment 2. Rich Auerbach, Assessor, Los Angeles County

In a letter dated July 30, 2007, Mr. Auerbach states his support for the adoption of Proposed Rule 474. Mr. Auerbach states that the proposed rule is consistent with Revenue and Taxation Code section 51(d), Rule 324(b), and Rule 468 (Oil and Gas Properties), Rule 469 (Mining Properties), and Rule 473 (Geothermal Properties).

Staff's Response

The Board's staff generally agrees with Mr. Auerbach's written comments.

Comment 3. Gus Kramer, Assessor, Contra Costa County

In a letter dated July 30, 2007, Mr. Kramer stated that he supports the readoption of Proposed Rule 474. Additionally, Mr. Kramer incorporates, by reference, a memorandum by Mr. Dennis Graves, a retired Deputy County Counsel for Contra Costa County, dated September 1, 2006.

Staff's Response

This letter and its referenced memorandum were previously submitted to the Board and are part of the rulemaking record. The Board staff generally agrees with Mr. Kramer's and Mr. Graves' respective written comments.

Comment 4. Bob Poole, Senior Coordinator, Western States Petroleum Association (WSPA)

In a letter dated July 27, 2007, WSPA objected to adoption of Proposed Rule 474 on the grounds that the proposed rule is not consistent with various authorities and that the revised ISR fails to show reasons or evidence of the necessity for the rule.

Staff's Response

WSPA's current letter is substantially similar in content to a letter dated September 21, 2006 previously submitted by WSPA. The 2006 letter, plus supplemental letters submitted on the same date, are part of the rulemaking record. Since the attached FSR responds to the same or similar issues, those responses are not repeated here. (See attached Final Statement of Reasons.) Furthermore, the revised ISR provides a detailed and thorough statement of necessity for the proposed rule.

Conclusion

As indicated above, the Board Staff requests that the Board readopt Proposed Rule 474, in compliance with OAL's direction.

If you need more information or have any questions, please contact Acting Assistant Chief Counsel Robert Lambert at (916) 324-6593.

KC:jlh
Chief Counsel/Final/Rule 474.8.14.07.doc
Prop/Rules/474.8.14.07.doc

Attachments
1. Proposed Rule 474, with revised references
2. OAL Notice of Disapproval
3. 15-day Letter
4. Amended Initial Statement of Reasons
5. Final Statement of Reasons
6. Public Comments, in the order submitted

Approved: Ramon Hirsig by Robert Lambert
Ramon J. Hirsig
Executive Director

cc: Mr. Ramon Hirsig, MIC: 73
Mr. David Gau, MIC: 63
Mr. Robert Lambert, MIC: 82
Mr. Dean Kinnee, MIC: 64
Mr. Todd Gilman, MIC: 70

bcc: Mr. Alan LoFaso MIC:71
Ms. Sabina Crocette MIC:71
Ms. Mengjun He MIC:71
Mr. Larry Bergkamp MIC:71
Mr. Steve Shea MIC:72
Mr. Reed Schreiter MIC:72
Mr. Mark Ibelle MIC:72
Ms. Barbara Alby MIC:78
Mr. Erik Caldwell MIC:77

Ms. Marcy Jo Mandel, Deputy State Controller
660 South Figueroa Street, Suite 2050
Los Angeles, CA 90017

Proposed Rule 474

RULE 474. PETROLEUM REFINING PROPERTIES.

(a) The provisions of this rule apply to the valuation of the real property, personal property, and fixtures used for the refining of petroleum.

(b) GENERAL.

(1) The unique nature of property used for the refining of petroleum requires the application of specialized appraisal techniques designed to satisfy the requirements of article XIII, section 1, and article XIII A, section 2, of the California Constitution. To this end, petroleum refineries and other real and personal property associated therewith shall be valued pursuant to the principles and procedures set forth in this section.

(2) Notwithstanding any other provision in this section, any appropriate valuation method described in section 3 of title 18 of this code may be applied in the event of a change in ownership in a petroleum refining property.

(c) DEFINITIONS. For the purposes of this section:

(1) "Petroleum refining property" means any industrial plant, including real property, personal property, and fixtures, used for the refining of petroleum, as identified in Standard Industrial Classification (SIC) System Codes 2911 and 2992, or North American Industry Classification System (NAICS) Codes 32411 and 324191.

(2) "Appraisal unit" consists of the real and personal property that persons in the marketplace commonly buy and sell as a unit.

(d) DECLINES IN VALUE. For the purposes of this section:

(1) Declines in value of petroleum refining properties will be determined by comparing the current lien date full value of the appraisal unit to the indexed base year full value of the same unit.

(2) The land, improvements, and fixtures and other machinery and equipment classified as improvements for a petroleum refining property are rebuttably presumed to constitute a single appraisal unit, except when measuring declines in value caused by disaster, in which case land shall constitute a separate unit.

(3) In rebutting this presumption, the assessor may consider evidence that:

(A) The land and improvements including fixtures and other machinery and equipment classified as improvements are not under common ownership or control and do not typically transfer in the marketplace as one economic unit; or,

(B) When the fixtures and other machinery and equipment classified as improvements are not functionally and physically integrated with the realty and do not operate together as one economic unit.

Authority Cited: Section 15606(c), Government Code
Reference: Article XIII, Section 1, and Article XIII A, Section 2, California Constitution
Sections 51 and 110.1, Revenue and Taxation Code

Notice of Disapproval

STATE OF CALIFORNIA

OFFICE OF ADMINISTRATIVE LAW

In re:	**NOTICE OF DISAPPROVAL OF REGULATORY ACTION**
BOARD OF EQUALIZATION	
REGULATORY ACTION:	**Government Code Section 11349.3**
Title 18, California Code of Regulations	**OAL File No. 07-0427-04 SR**
Adopt sections 474	

This regulatory action defines "petroleum refining property" and establishes a rebuttable presumption, for purposes of recognizing declines in value, that land, improvement, and fixtures and other machinery and equipment classified as improvements constitute one appraisal unit, except when measuring declines in value caused by disaster, in which case land constitutes a separate appraisal unit. This regulatory action was originally submitted by the Board of Equalization (BOE) to the Office of Administrative Law (OAL) on December 26, 2006. It was subsequently withdrawn by BOE on February 8, 2007 before OAL took any action on the filing. On April 27, 2007, BOE resubmitted this regulatory action to OAL. This resubmission incorporated the prior rulemaking file by reference and made one minor deletion to the reference citations for section 474.

OAL disapproves this regulatory action for the following reason(s):

The regulatory file does not contain all required documents, and/or required documents included in the file are defective.

Within seven (7) calendar days of the date of this notice, the Office of Administrative Law will send the adopting agency a written decision detailing the reasons for disapproval of the specified sections of this regulatory filing. Government Code Section 11349.3(b).

Enclosed is the agency's copy of the submitted regulations.

DATE: 06/08/07

CRAIG S. TARPENNING
Senior Staff Counsel

for: SUSAN LAPSLEY
Director

Original : Ramon Hirsig, Executive Director

cc : Diane G. Olson

Decision of Disapproval

STATE OF CALIFORNIA
OFFICE OF ADMINISTRATIVE LAW

In re:	)	
BOARD OF EQUALIZATION	)	DECISION OF DISAPPROVAL OF REGULATORY ACTION
	)	(Gov. Code, sec. 11349.3)
REGULATORY ACTION: Title 18, California Code of Regulations	)	OAL File No. 07-0427-04 SR
ADOPT SECTION 474	)	

SUMMARY OF REGULATORY ACTION

This proposed regulatory action seeks to adopt section 474 to title 18 of the California Code of Regulations. Proposed section 474 defines "petroleum refining property" and establishes a rebuttable presumption, for purposes of recognizing declines in value for such property, that land, improvement, and fixtures and other machinery and equipment classified as improvements constitute one appraisal unit, except when measuring declines in value caused by disaster, in which case the land constitutes a separate appraisal unit. This regulatory action was originally submitted by the Board of Equalization to the Office of Administrative Law on December 26, 2006. It was subsequently withdrawn by the Board of Equalization on February 8, 2007 before the Office of Administrative Law took any action on the filing. On April 27, 2007, the Board of Equalization resubmitted this regulatory action to the Office of Administrative Law. This resubmission incorporated the prior rulemaking file by reference. The only change in the resubmission from the prior rulemaking file was one minor deletion from the reference citations for section 474.

DECISION

On June 8, 2007, the Office of Administrative Law disapproved the above referenced regulatory action because the Initial Statement of Reasons failed to provide the public with the rationale for the determination by the agency that the provisions in section 474 are needed to carry out the purpose for which it is proposed.

DISCUSSION

The adoption of regulations by the Board of Equalization ("Board") must satisfy requirements established by the part of the California Administrative Procedure Act ("APA") that governs rulemaking by a state agency. Any rule or regulation adopted by a state agency to implement,

interpret, or make specific the law enforced or administered by it, or to govern its procedure, is subject to the APA unless a statute expressly exempts the regulation from APA coverage. (Gov. Code, sec. 11346.)

Before any rule or regulation subject to the APA may become effective, the rule or regulation is reviewed by the Office of Administrative Law ("OAL") for compliance with the procedural requirements of the APA and for compliance with the standards for administrative regulations in Government Code Section 11349.1. Generally, to satisfy the standards a rule or regulation must be legally valid, supported by an adequate record, and easy to understand. In this review OAL is limited to the rulemaking record and may not substitute its judgment for that of the rulemaking agency with regard to the substantive content of the regulation. This review is an independent check on the exercise of rulemaking powers by executive branch agencies intended to improve the quality of rules and regulations that implement, interpret, and make specific statutory law, and to ensure that the public is provided with a meaningful opportunity to comment on rules and regulations before they become effective. (Gov. Code, sec 11349.1.)

Government Code section 11349.1(a)(1) requires that OAL review all regulations for compliance with the "necessity" standard. Government Code section 11349(a) defines "necessity" to mean ". . . the record of the rulemaking proceeding demonstrates by substantial evidence the need for a regulation to effectuate the purpose of the statute, court decision, or other provision of law that the regulation implements, interprets, or makes specific, taking into account the totality of the record. For purpose of this standard, evidence includes, but is not limited to, facts, studies, and expert opinion."

To further explain the meaning of substantial evidence in the context of the "necessity" standard, subdivision (b) of section 10 of the Title 1 of the California Code of Regulations provides:

> "In order to meet the 'necessity' standard of Government Code section 11349.1, the record of the rulemaking proceeding shall include:
>
> (1) a statement of the specific purpose of each adoption, amendment, or repeal; and
>
> (2) information explaining why each provision of the adopted regulations is required to carry out the described purpose of the provision. Such information shall include, but is not limited to, facts, studies, or expert opinion. When the explanation is based upon policies, conclusions, speculation, or conjecture, the rulemaking record must include, in addition, supporting facts, studies, expert opinion, or other information. An 'expert' within the meaning of this section is a person who possesses special skill or knowledge by reason of study or experience which is relevant to the regulation in question."

In order to provide the public with an opportunity to review and comment upon an agency's perceived need for a regulation, the APA requires that the agency describe the need for the regulation in the Initial Statement of Reasons. (Gov. Code, sec. 11346.2(b).) The Initial Statement of Reasons is the primary document in the rulemaking record that demonstrates that

the adoption, amendment, or repeal satisfies the "necessity" standard. The Initial Statement of Reasons must include a statement of the specific purpose for each adoption, amendment, or repeal, and the rationale for the determination by the agency that each regulation is reasonably necessary to carry out the purpose for which it is proposed or, simply restated, "why" a regulation is needed and "why" the particular provisions contained in this regulation were chosen to fill that need. (Gov. Code, sec. 11346.2(b)(1).) The Initial Statement of Reasons must also identify any technical, theoretical, or empirical study, report, or similar document upon which the agency relies. (Gov. Code, sec. 11346.2(b)(2).)

The Initial Statement of Reasons must be submitted to OAL with the Notice of the Proposed Action and be made available to the public during the public comment period, along with all the information upon which the proposal is based. (Gov. Code, secs. 11346.2(b) and 11346.5(a)(16) and (b).) In this way the public is informed of why the regulation is needed and why the particular provisions contained in the regulation were chosen to fill that need. This information is essential in order to comment knowledgeably. The Initial Statement of Reasons and all data and other factual information, studies or reports upon which the agency is relying in the regulatory action must also be included in the rulemaking file. (Gov. Code, sec. 11347.3(b)(2) and (7).)

The Initial Statement of Reasons provided with this regulatory action is inadequate. It contains just five short paragraphs: the first paragraph describes in one sentence the general purpose of section 474, the second and third paragraphs briefly describe pertinent provisions in Article XIII of the California Constitution and section 51 of the Revenue and Taxation Code, and the last two paragraphs briefly describe the effect of section 474. The Initial Statement of Reasons fails to provide the public with the rationale for the determination by the Board as to why the provisions in section 474 are needed to carry out the purpose for which it is proposed, i.e., why the particular provisions contained in the regulation were chosen. For example, for subsection (d)(2) of section 474, there is no information explaining why fixtures and other machinery and equipment classified as improvements on petroleum refining property should be rebuttably presumed to constitute a single appraisal unit with the land and improvements.

It is vital that this information be made available to the public during the rulemaking process so that the public is informed of the basis of the proposed action and can comment knowledgably during the public comment period. In that the 45-day comment period had already been completed, Board staff were advised by OAL in early February, prior to the withdrawal of the original submission of this rulemaking, that the defect could be remedied by making the information required to be contained in the Initial Statement of Reasons available to the public for a 15-day written comment period pursuant to sections 11346.8(d) and 11347.1 of the Government Code. OAL did not advise Board staff that the public hearing on the proposed regulatory action had to be reopened. Government Code section 11347.1(b) requires that the rulemaking agency mail to persons who commented or requested notification of changes a notice making documents added to the record available for public inspection and written comment for at least 15 days. In the event any comments are received by the agency on the documents during the 15-day comment period, Government Code section 11346.8(a) would require that the comments be considered by the agency prior to adoption.

The Board in this resubmission has elected to resubmit the file to OAL without making this information available to the public for a 15-day written comment period. The only change in the resubmission from the prior rulemaking file was one minor deletion from the reference citations for section 474.

CONCLUSION

For the reasons set forth above, OAL has disapproved this regulatory action.

Date: June 8, 2007

CRAIG S. TARPENNING
Senior Staff Counsel

for: SUSAN LAPSLEY
Director

Original: Ramon Hirsig, Executive Director
cc: Diane Olson

LTA 2007 - 032

STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
450 N STREET, SACRAMENTO, CALIFORNIA
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0080
916-322-9569 • FAX 916-324-3984
www.boe.ca.gov

BETTY T. YEE
First District, San Francisco

BILL LEONARD
Second District, Ontario/Sacramento

MICHELLE STEEL
Third District, Rolling Hills Estates

JUDY CHU
Fourth District, Los Angeles

JOHN CHIANG
State Controller

RAMON J. HIRSIG
Executive Director

July 17, 2007

No. 2007/032
Revised

TO COUNTY ASSESSORS, COUNTY COUNSELS,
AND OTHER INTERESTED PARTIES:

NOTICE OF PROPOSED REGULATORY ACTION
BY THE
STATE BOARD OF EQUALIZATION

PROPOSED ADOPTION OF
PROPERTY TAX RULE 474 -- *PETROLEUM REFINING PROPERTIES*

On September 27, 2006, the State Board of Equalization held a public hearing and adopted proposed Property Tax Rule 474, *Petroleum Refining Properties*. The Office of Administrative Law (OAL) issued its Decision of Disapproval of Regulatory Action dated June 8, 2007, solely based on the finding that "the Initial Statement of Reasons failed to provide the public with the rationale for the determination by the agency that the provisions in section 474 are needed to carry out the purpose for which it is proposed." In response, the Board of Equalization has submitted the initial statement of reasons to the 15-day file, recommending that changes be made to the statement to more fully explain the proposed rule's purpose and necessity consistent with the OAL decision. No substantive changes to the proposed rule have been made; however, a statutory reference to Revenue and Taxation Code section 53.5 was determined to be irrelevant and removed.

Enclosed are the revised versions of the initial statement of reasons and proposed Rule 474.

In accordance with Government Code section 11346.8, subdivisions (c) and (d), and section 11347.1, the revised initial statement of this rule is being placed in the rulemaking file and mailed today to interested parties who commented orally or in writing, or who asked to be informed of such revisions. If you wish to review the rulemaking file, it is available for your inspection at the State Board of Equalization, 450 N Street, Sacramento, California. The proposed rule will be placed on the agenda for the August 14, 2007 Board meeting for the Board's consideration.

Questions regarding the substance of the proposed rule should be directed to: Mr. Robert Lambert, Acting Assistant Chief Counsel, at P.O. Box 942879, 450 N Street, MIC:82, Sacramento, CA 94279-0082; E-mail: Robert.Lambert@boe.ca.gov; Telephone: 916-324-6593; Fax: 916-323-3387.

Requests to present testimony and bring witnesses to the public hearing, and inquiries concerning the proposed administrative action should be directed to: Ms. Diane Olson, Regulations Coordinator, P.O. Box 942879, 450 N Street, MIC:80, Sacramento, CA 94279-0080; E-mail: Diane.Olson@boe.ca.gov; Telephone: 916-322-9569; Fax: 916-324-2597. Written comments must be submitted to Ms. Olson by August 1, 2007.

Sincerely,

Gary Evans, Assistant Chief
Board Proceedings Division

GE:dgo

Enclosure

Initial Statement of Reasons

INITIAL STATEMENT OF REASONS
NON-CONTROLLING SUMMARY

Property Tax Rule 474
Petroleum Refining Properties

~~**Specific Purpose**~~

~~The purpose of the proposed rule is to implement and make specific the requirements for valuation of real property, personal property, and fixtures used to refine petroleum.~~

~~**Factual Basis**~~

~~Section 1 of article XIII of the California Constitution provides that, unless otherwise provided by the California Constitution or the laws of the United States, all property is taxable and all assessed property is taxed in proportion to its full value. Subdivision (b) of section 2 of article XIII A of the California Constitution requires that the base year value of assessed property may not increase annually by more than the inflation factor prescribed in that subdivision.~~

~~Section 51 of the Revenue and Taxation Code implements these provisions by establishing methods for adjusting the base year values of assessed real property. Subdivision (d) of section 51 provides that "real property" means "that appraisal unit that person in the marketplace commonly buy and sell as a unit, or that is normally valued separately."~~

~~The Board of Equalization proposes to adopt Rule 474 to clarify and make specific certain specialized appraisal techniques for the valuation of real property, personal property, and fixtures used to refine petroleum.~~

~~Proposed Rule 474 will (1) define "petroleum refining property;" and (2) establish a rebuttable presumption for purposes of recognizing declines in value that fixtures and machinery and equipment classified as improvements for a petroleum refining property are part of the same appraisal unit as the land and structures. The presumption must be overcome before fixtures are treated as a separate appraisal unit for declines in value, except when measuring declines in value caused by disaster, in which case land constitutes a separate appraisal unit.~~

Proposed Property Tax Rule 474

Proposed Rule 474[1] will (1) define "petroleum refining property;" and (2) establish a rebuttable presumption for purposes of recognizing declines in value that fixtures and machinery and equipment classified as improvements for a petroleum refining property are part of the same appraisal unit as the land and structures. The presumption must be overcome before fixtures are treated as a separate appraisal unit for declines in value, except when measuring declines in value caused by disaster, in which case land constitutes a separate appraisal unit.

Specific Purpose; Necessity; Factual Basis

General purpose. In general, the purpose of the proposed rule is to implement and make specific the requirements for valuation of real property, personal property, and fixtures used to refine petroleum. More specifically, the purpose of the proposed Property Tax Rule 474 is to clarify and implement the requirements under article XIII, section 1, and article XIII A, section 2, of the California Constitution for the valuation of real property, personal property, and fixtures used to refine petroleum. The proposed rule is necessary in order to require that assessors value petroleum refinery property properly for fair market value/decline in value purposes, as explained and for the reasons set forth below:

Summary of Necessity. As explained in more detail below, Rule 461, subdivision (e) provides the general rule that, in appraisals conducted for the purpose of determining whether or not there has been a decline in value in real property upon which improvements, fixtures, and machinery are located, the fixtures and other machinery and equipment classified as improvements constitute a separate appraisal unit. This rule is premised upon the normal market situation, applicable to most types of property, where the land and improvements are most commonly sold separately from the fixtures and machinery. Accordingly, when applied to the appraisal of most types of real property, Rule 461, subdivision (e) will result in accurate fair market valuations of both the land and improvements and the fixtures and machinery.

It has long been recognized, however, that Rule 461, subdivision (e) will not produce accurate fair market valuations in all situations. In some exceptional cases involving special types of properties, the normal market situation involves the sale of land, improvements, fixtures and machinery as a single economic unit. In these types of cases, in order to be consistent with the marketplace, the land, improvements, fixtures, and machinery should be valued as a single appraisal unit to determine whether or not there has been a decline in value. Because petroleum refinery properties sell most commonly as a single economic unit – including land, improvements, fixtures, and machinery, the application of the "general rule" of Rule 461, subdivision (e) to petroleum

[1] All references to proposed Property Tax Rule or proposed Rule are to the rule proposed for inclusion in title 18 of the California Code of Regulations.

refinery properties is inappropriate; and, in fact, will lead to appraisals that are not consistent with fair market value when calculating declines in value for such properties.

In order to address the special characteristics of such properties, Proposed Rule 474: (1) defines the petroleum refining property appraisal unit that normally will be used to determine "full cash value" under article XIII A, section 2; and (2) establishes a rebuttable presumption that fixtures and machinery and equipment classified as improvements, for a petroleum refining property, are part of the same appraisal unit as the land for purposes of recognizing declines in value. This presumption may be overcome by showing that the land and fixtures in a specific petroleum refining property do not operate together as a single economic unit. In the case of declines in value caused by disaster, however, land and fixtures would constitute separate appraisal units. Proposed Rule 474 thereby clarifies how the value of petroleum refining properties should be determined when there has been a decline in value.

Fair market valuation and declines in value. Section 1 of article XIII of the California Constitution states that, unless otherwise provided by the California Constitution or the laws of the United States, all property is taxable and shall be assessed at the same percentage of fair market value. Article XIII A (which contains Proposition 13 as amended by Proposition 8) of the California Constitution requires that all real property be valued at its factored base year value (Proposition 13 value), which is a property's fair market value as of the date of a change in ownership or completion of new construction adjusted annually to reflect an inflation factor of no more than 2 percent, or the property's fair market value at the lien date (Proposition 8 value), whichever is lower. (See Rev. & Tax. Code, § 51, subd. (a).)[2] Proposition 8 amended Proposition 13 to provide a temporary reduction in assessed value where the property has experienced a decline in fair market value to an amount below Proposition 13 value. (*County of Orange v. Renee M Bezaire* (2004) 117 Cal.App.4th 121.)

The determination of whether or not there has been a decline in value of petroleum refining property is currently governed by section 51 and Rule 461, subdivision (e), which provide the general decline in value principles for use in implementing article XIII, section 1 and article XIII A, section 2, of the California Constitution. Under these provisions:

> In determining the extent of a potential decline in value, the assessor must look to the net change in value of the appraisal unit which is commonly bought and sold in the market place, or which is normally valued separately . . . . This means that land and improvements are ordinarily treated as a unit, [footnote omitted] and that a taxpayer cannot claim a net decline in full cash value terms of an improvement due to depreciation [i.e. decline in value], without also including any appreciation in the value of the land. If the building depreciation is offset by the increase in land value, then no reduction in assessment occurs. Fixtures, however, are

[2] All section references are to the Revenue and Taxation Code unless otherwise specified.

> normally appraised separately, thus owners may claim a decline based on depreciation of the fixture without regard to the value of the surrounding land or improvements. (Emphasis added.)[3]

Section 51, subdivision (d) defines an "appraisal unit" alternatively as: (1) that which "persons in the marketplace commonly buy and sell as a unit" or (2) that which is "normally valued separately." The second alternative was adopted in recognition of the fact that fixtures and other machinery and equipment classified as improvements are normally valued separately in the marketplace.

After the passage of Proposition 8, the Board amended Rule 461 to state that fixtures and other machinery and equipment classified as improvements should be treated as a separate appraisal unit. Accordingly, Rule 461, subdivision (e) presently provides that fixtures and other machinery and equipment classified as improvements constitute a separate appraisal unit. The Board adopted the language of Rule 461, subdivision (e) on January 25, 1979, and it has remained unchanged since that time. Given such separate appraisal units, no offsetting of land and improvement value vis-à-vis fixture and machinery value can take place, having the effect of isolating fixture and machinery declines in value from land and improvement increases in value. Under such a rule, any fixture and machinery declines in value (from depreciation or any other cause) are immediately recognized for property tax purposes as Proposition 8 value reductions, despite increases in land and improvement value. While this is entirely appropriate and, in fact, mandatory, where the market indicates the existence of two separate appraisal units – one for land and improvements and one for fixtures and machinery – it is inappropriate where the market indicates that, in fact, the two categories of property commonly sell as a single unit.

The appraisal of property at fair market (or full cash) value means 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 the property may be put…." (Rule 2, subd. (a) (Emphasis added); see also Rev. & Tax. Code, § 110, subd. (a).) Thus, the price at which property would transfer in the open market is the fundamental principle in defining fair market value. Consequently, for property tax purposes, the unit of property that commonly must be appraised is the one normally dealt with in the market. According to the Board's Assessors' Handbook (AH) 501, Basic Appraisal, p. 10-11, "The identification of the property to be appraised is an integral part of the appraisal process. Part of the process of identifying the property is identifying the 'appraisal unit' …. The proper unit to be valued is the unit that people in the market typically buy and sell. For example, single family homes are sold as a combination of land and buildings …. The combination of land and buildings, therefore, comprises the appraisal unit [for single family homes], and the appraisal of this type of property must reflect the value of this unit." Subdivision (b) of Rule 324 similarly provides that, "An

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[3] Implementation of Proposition 13, Volume 1, Property Tax Assessment, Assembly Revenue and Taxation Committee, October 29, 1979, page 13.

appraisal unit of property is a collection of assets that functions together, and that persons in the marketplace commonly buy and sell as a single unit or that is normally valued in the marketplace separately from other property, or that is specifically designated as such by law." (Emphasis added.)

Existing exceptions to Rule 461, subdivision (e). While the general decline in value rule is adequate for properties that can be valued and which sell in the marketplace as separate appraisal units, the Board has adopted special rules for property that, like petroleum refining property, is of a type that is not adequately addressed by the general rule. These types of properties include oil and gas, mining, and geothermal properties, which are governed by Property Tax Rules 468, 469, and 473, respectively. In contrast to present Rule 461, Rules 468, 469, and 473 provide, as an exception to the general rule of decline in value appraisals, that fixtures and other machinery and equipment classified as improvements do not constitute a separate appraisal unit. These rules were promulgated in recognition of the unique nature of these properties, and to provide specialized appraisal techniques required to satisfy the requirements of article XIII, section 1, and article XIII A, section 2, of the California Constitution.

Petroleum refineries. The general decline in value rule set forth in Rule 461, subdivision (e), has been interpreted by some as applying to the valuation of petroleum refinery property. Such application, however, has been criticized as being inconsistent both with market practices and the constitutional requirement of fair market valuation. Unlike the usual case for most other types of property, in the sale and purchase of petroleum refinery property, land, improvements, and fixtures are commonly bought and sold as a single economic unit; in fact, it appears that the sale of refinery property almost always includes all three categories of property. This is because all the parts of the refinery must operate together to produce the finished product. Refineries are different from other heavily fixturized manufacturing industries in that up to 80 percent of their values are contained in the fixtures. In addition, because the land and fixtures are so integrated, it is difficult to physically separate the fixtures from the land. Furthermore, the land and fixtures are so economically integrated that, in an open market transaction, a buyer would not purchase the land or fixtures separately.

Thus, application of the "general rule" set forth in Rule 461, subdivision (e) to refinery property is inconsistent with the constitutional requirement of fair market valuation in that such regulatory provision might be interpreted as mandating two separate appraisal units while the petroleum refinery market evidences a single appraisal unit, one that encompasses land and improvements, as well as fixtures and other machinery and equipment classified as improvements. The general rule would be valid for petroleum refinery property only if persons in the marketplace commonly bought and sold refinery land/improvements, on the one hand, and fixtures/machinery, on the other, as separate units; or if such types of property were normally valued separately.[4] But refinery land, improvements, and fixtures and other machinery and equipment classified

[4] Of course, if two types of property are not bought and sold separately, then generally there is no reason (or basis upon which) to value them separately.

as improvements are commonly bought, sold, and valued as a single unit in the marketplace. Thus, application of the general decline in value rule to petroleum refining property may, under appropriate facts, violate the California Constitution's requirement that property be valued at fair market value. (Cal. Const., art. XIII, § 1 and art. XIII A, § 2.) Proposed Rule 474 corrects this misinterpretation of Rule 461 and section 51.5

Conclusion. In conclusion, Proposed Rule 474 is necessary since the current statutory and regulatory scheme does not adequately address the decline in value of petroleum refining property. Similar to properties governed by Rules 468, 469, and 473, petroleum refineries normally would not separately sell their land apart from their fixtures.

Proposed Rule 474, thus, is necessary with respect to appraising the declines in value of petroleum refineries because the application of the "general rule" in Rule 461, subdivision (e), to such refineries is inappropriate and will lead to inaccurate valuations. Proposed Rule 474: (1) defines the petroleum refining property appraisal unit that normally will be used to determine "full cash value" under article XIII A, section 2; and (2) establishes a rebuttable presumption that fixtures and machinery and equipment classified as improvements, for a petroleum refining property, are part of the same appraisal unit as the land for purposes of recognizing declines in value. This presumption may be overcome by showing that the land and fixtures in a specific petroleum refining property do not operate together as a single economic unit. In the case of declines in value caused by disaster, however, land and fixtures would constitute separate appraisal units. Proposed Rule 474 thereby clarifies how the value of petroleum refining properties should be determined when there has been a decline in value.

Final Statement of Reasons

FINAL STATEMENT OF REASONS
NON-CONTROLLING SUMMARY

Property Tax Rule 474
Petroleum Refining Properties

Specific Purpose

The purpose of the proposed Property Tax Rule[1] 474 is to clarify and implement the requirements under article XIII, section 1, and article XIII A, section 2, of the California Constitution for the valuation of real property, personal property, and fixtures used to refine petroleum.

Legal and Factual Basis

Based on the rulemaking record, proposed Property Tax Rule (Rule) 474 is well-grounded in law and fact, clarifying and advancing the specific application of the general decline in value rules to petroleum refining properties.

Summary. As explained in more detail below, Rule 461, subdivision (e) provides the general rule that, in appraisals conducted for the purpose of determining whether or not there has been a decline in value in real property upon which improvements, fixtures, and machinery are located, the fixtures and other machinery and equipment classified as improvements constitute a separate appraisal unit. This rule is premised upon the normal market situation, applicable to most types of property, where the land and improvements are most commonly sold separately from the fixtures and machinery. Accordingly, when applied to the appraisal of most types of real property, Rule 461, subdivision (e) will result in accurate fair market valuations of both the land and improvements and the fixtures and machinery.

It has long been recognized, however, that Rule 461, subdivision (e) will not produce accurate fair market valuations in all situations. In some exceptional cases involving special types of properties, the normal market situation involves the sale of land, improvements, fixtures and machinery as a single economic unit. In these types of cases, in order to be consistent with the marketplace, the land, improvements, fixtures, and machinery should be valued as a single appraisal unit to determine whether or not there has been a decline in value.

In the past, the Board has adopted regulations for those special types of properties that are not adequately addressed by the general rule set forth in Rule 461, subdivision (e). These types of properties include oil and gas, mining, and geothermal properties, which are governed by Property Tax Rules 468, 469, and 473, respectively. In contrast to present Rule 461, Rules 468, 469, and 473 provide that fixtures and other machinery and equipment classified as improvements do not constitute a separate appraisal unit for

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[1] All references to proposed Property Tax Rule or proposed Rule are to the rule proposed for inclusion in title 18 of the California Code of Regulations.

purposes of determining decline in value. These rules were promulgated in recognition of the unique nature of these properties, and in order to provide the specialized appraisal techniques required to determine their fair market value.

Based upon testimony and evidence submitted to the Board during this rulemaking process, it has been established that petroleum refinery properties also most commonly sell as a single economic unit – including land, improvements, fixtures, and machinery. Thus, as is the case with oil and gas, mining, and geothermal properties, it is inappropriate to apply the "general rule" of Rule 461, subdivision (e) to petroleum refinery properties. In order to address the special characteristics of such properties, Proposed Rule 474 (1) defines the petroleum refining property appraisal unit that normally will be used to determine "full cash value" under article XIII A, section 2; and (2) establishes a rebuttable presumption that fixtures and machinery and equipment classified as improvements, for a petroleum refining property, are part of the same appraisal unit as the land for purposes of recognizing declines in value. This presumption may be overcome by showing that the land and fixtures in a specific petroleum refining property do not operate together as a single economic unit. In the case of declines in value caused by disaster, however, land and fixtures would constitute separate appraisal units. Proposed Rule 474 thereby clarifies how the value of petroleum refining properties should be determined when there has been a decline in value.

Fair market valuation and declines in value. Section 1 of article XIII of the California Constitution states that, unless otherwise provided by the California Constitution or the laws of the United States, all property is taxable and shall be assessed at the same percentage of fair market value. Article XIII A (which contains Proposition 13 as amended by Proposition 8) of the California Constitution requires that all real property be valued at its factored base year value (Proposition 13 value), which is a property's fair market value as of the date of a change in ownership or completion of new construction adjusted annually to reflect an inflation factor of no more than 2 percent, or the property's fair market value at the lien date (Proposition 8 value), whichever is lower. (See Rev. & Tax. Code, § 51, subd. (a).) Proposition 8 amended Proposition 13 to provide a temporary reduction in assessed value where the property has experienced a decline in fair market value to an amount below Proposition 13 value. (*County of Orange v. Renee M Bezaire* (2004) 117 Cal.App.4th 121.)

The determination of whether or not there has been a decline in value of petroleum refining property is currently governed by section[2] 51 and Rule 461, subdivision (e), which provide the general decline in value principles for use in implementing article XIII, section 1 and article XIII A, section 2, of the California Constitution. Under these provisions:

> In determining the extent of a potential decline in value, the assessor must look to the net change in value of the appraisal unit which is commonly bought and sold in the market place, or which is normally valued separately . . . . This means that land and

[2] All section references are to the Revenue and Taxation Code unless otherwise specified.

> improvements are ordinarily treated as a unit, [footnote omitted] and that a taxpayer cannot claim a net decline in full cash value terms of an improvement due to depreciation [i.e. decline in value], without also including any appreciation in the value of the land. If the building depreciation is offset by the increase in land value, then no reduction in assessment occurs. Fixtures, however, are normally appraised separately, thus owners may claim a decline based on depreciation of the fixture without regard to the value of the surrounding land or improvements.[3] (Emphasis added.)

Section 51, subdivision (d) defines an "appraisal unit" alternatively as: (1) that which "persons in the marketplace commonly buy and sell as a unit" or (2) that which is "normally valued separately." The second alternative was adopted in recognition of the fact that fixtures and other machinery and equipment classified as improvements are normally valued separately in the marketplace.

After the passage of Proposition 8, the Board amended Rule 461 to state that fixtures and other machinery and equipment classified as improvements should be treated as a separate appraisal unit. Accordingly, Rule 461, subdivision (e) presently provides that fixtures and other machinery and equipment classified as improvements constitute a separate appraisal unit. The Board adopted the language of Rule 461, subdivision (e) on January 25, 1979, and it has remained unchanged since that time. Given such separate appraisal units, no offsetting of land and improvement value vis-à-vis fixture and machinery value can take place, having the effect of isolating fixture and machinery declines in value from land and improvement increases in value. Under such a rule, any fixture and machinery declines in value (from depreciation or any other cause) are immediately recognized for property tax purposes as Proposition 8 value reductions, despite increases in land and improvement value. While this is entirely appropriate and, in fact, mandatory, where the market indicates the existence of two separate appraisal units – one for land and improvements and one for fixtures and machinery – it is inappropriate where the market indicates that, in fact, the two categories of property commonly sell as a single unit.

The appraisal of property at fair market (or full cash) value means 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 the property may be put…." (Rule 2, subd. (a) (Emphasis added); see also Rev. & Tax. Code, § 110, subd. (a).) Thus, the price at which property would transfer in the open market is the fundamental principle in defining fair market value. Consequently, for property tax purposes, the unit of property that commonly must be appraised is the one normally dealt with in the market. According to the Board's Assessors' Handbook (AH) 501, *Basic Appraisal*, p. 10-11, "The identification of the property to be appraised is an integral part of the appraisal process. Part of the process of identifying the property is identifying the

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[3] *Implementation of Proposition 13,* Volume 1, *Property Tax Assessment*, Assembly Revenue and Taxation Committee, October 29, 1979, page 13.

'appraisal unit' .... The proper unit to be valued is the unit that people in the market typically buy and sell. For example, single family homes are sold as a combination of land and buildings .... The combination of land and buildings, therefore, comprises the appraisal unit [for single family homes], and the appraisal of this type of property must reflect the value of this unit." Subdivision (b) of Rule 324 similarly provides that, "An appraisal unit of property is a collection of assets that functions together, and that persons in the marketplace commonly buy and sell as a single unit or that is normally valued in the marketplace separately from other property, or that is specifically designated as such by law." (Emphasis added.)

Existing exceptions to Rule 461, subdivision (e). While the general decline in value rule is adequate for properties that can be valued and which sell in the marketplace as separate appraisal units, the Board has adopted special rules for property that, like petroleum refining property, is of a type that is not adequately addressed by the general rule. These types of properties include oil and gas, mining, and geothermal properties, which are governed by Property Tax Rules 468, 469, and 473, respectively. In contrast to present Rule 461, Rules 468, 469, and 473 provide, as an exception to the general rule of decline in value appraisals, that fixtures and other machinery and equipment classified as improvements do not constitute a separate appraisal unit. These rules were promulgated in recognition of the unique nature of these properties, and to provide specialized appraisal techniques required to satisfy the requirements of article XIII, section 1, and article XIII A, section 2, of the California Constitution.

Petroleum refineries. The general decline in value rule set forth in Rule 461, subdivision (e), has been interpreted by some as applying to the valuation of petroleum refinery property. Such application, however, has been criticized as being inconsistent both with market practices and the constitutional requirement of fair market valuation. According to the testimony and evidence presented to the Board, unlike the usual case for most other types of property, in the sale and purchase of petroleum refinery property, land, improvements, and fixtures are commonly bought and sold as a single economic unit; in fact, it appears that the sale of refinery property almost always includes all three categories of property.

Thus, given the testimony and evidence supplied to the Board, application of the "general rule" set forth in Rule 461, subdivision (e) to refinery property is inconsistent with the constitutional requirement of fair market valuation in that such regulatory provision might be interpreted as mandating two separate appraisal units while the petroleum refinery market evidences a single appraisal unit, one that encompasses land and improvements, as well as fixtures and other machinery and equipment classified as improvements. The general rule would be valid for petroleum refinery property only if persons in the marketplace commonly bought and sold refinery land/improvements, on the one hand, and fixtures/machinery, on the other, as separate units; or if such types of property were normally valued separately.[4] But, based upon the market evidence, refinery land, improvements, and fixtures and other machinery and equipment classified

[4] Of course, if two types of property are not bought and sold separately, then generally there is no reason (or basis upon which) to value them separately.

as improvements are commonly bought, sold, and valued as a single unit in the marketplace. Thus, application of the general decline in value rule to petroleum refining property may, under appropriate facts, violate the California Constitution's requirement that property be valued at fair market value. (Cal. Const., art. XIII, § 1 and art. XIII A, § 2.) Proposed Rule 474 corrects this misinterpretation of Rule 461 and section 51.[5]

Proposed Rule 474. Rule 474 is necessary since the current statutory and regulatory scheme does not adequately address the decline in value of petroleum refining property. Similar to properties governed by Rules 468, 469, and 473, petroleum refineries normally would not separately sell their land and fixtures. Written and oral comments received regarding proposed Rule 474 indicate that an operating refinery typically is sold as a single operating unit consisting of the land and improvements and fixtures since all the parts of the refinery must operate together to produce the finished product. Comments also indicate that refineries are different from other heavily-fixturized manufacturing industries in that up to 80 percent of their values are contained in the fixtures, and because the land and fixtures are so integrated, it is difficult to physically separate the fixtures from the land. Further, the land and fixtures are so economically integrated that, in an open market transaction, a buyer would not purchase the land or fixtures separately.

Proposed Rule 474 thus specifically addresses the decline in value appraisal of petroleum refineries. It (1) defines the petroleum refining property appraisal unit that normally will be used to determine "full cash value" under article XIII A, section 2; and (2) establishes a rebuttable presumption that fixtures and machinery and equipment classified as improvements, for a petroleum refining property, are part of the same appraisal unit as the land for purposes of recognizing declines in value. This presumption may be overcome by showing that the land and fixtures in a specific petroleum refining property do not operate together as a single economic unit. In the case of declines in value caused by disaster, however, land and fixtures would constitute separate appraisal units. Proposed Rule 474 thereby clarifies how the value of petroleum refining properties should be determined when there has been a decline in value.

Local Mandate Determination

The State Board of Equalization has determined that proposed Rule 474 does not impose a mandate on local agencies or school districts. Further, the Board has determined that the proposed rule will not result in direct or indirect costs or savings to any state agency, any costs to local agencies or school districts that are required to be reimbursed under Part 7 (commencing with Section 17500) of Division 4 of Title 2 of the Government Code, or other non-discretionary costs or savings imposed on local agencies, or cost or savings in federal funding to the State of California.

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[5] Note, however, that the proposed rule only provides a presumption that is rebuttable; thus, assessors may make exceptions where appropriate.

Response to Public Comment

The Board received the following written and oral comments on proposed Rule 474. The written comments were received during the 45-day public comment period which ended September 11, 2006. The oral comments were heard at the September 27, 2006 Board meeting. During that meeting, the Board adopted the proposed Rule as published.

Written Comments

Comment 1. Honorable Gus S. Kramer, Assessor, Contra Costa County.

In a letter dated September 12, 2006, Mr. Kramer wrote in support of the adoption of proposed Rule 474, enclosing a letter dated September 1, 2006, written by Dennis Graves, a legal consultant to the Assessor's Office on refinery matters, explaining the legality of proposed Rule 474.

Mr. Graves states that Propositions 8 and 13, as well as section 51, subdivision (d), and Rule 461, subdivision (e) require the valuation methodology set forth in proposed Rule 474. Since these provisions require that the value of property be determined by comparing the property's factored base year value with the property's fair market value for a unit of property for which a fair market value can be determined in a real-world, open-market, non-exigency sale, the only proper appraisal unit for an open-market, non-exigency sale of a refinery is the entire refinery, including land and fixtures. Thus, section 51, subdivision (d) in defining an "appraisal unit" as that which "persons in the marketplace commonly buy and sell as a unit, or that is normally valued separately" may not be read to allow refinery land and fixtures to be valued separately. Instead, it should be read similarly to Rule 324, subdivision (b), which states that an "appraisal unit" is that which "persons in the marketplace commonly buy and sell as a unit, or that is normally valued in the marketplace separately from other property . . . ." By adding the phrase "in the marketplace," Rule 324, subdivision (b) limits the appraisal unit to those units that could actually be sold apart from other property.

In his letter, Mr. Graves also states that "in the case of a viable operating refinery, the entire refinery is invariably sold as a single operating unit consisting of land, buildings, tanks, machinery and equipment necessary to producing gasoline and other finished products." This is because all of the "parts of the plant must operate together to produce the finished product that is to be sold, and the potential buyers are basing their bids on the present value of the income that can be generated over a holding period by producing and selling gasoline using all parts of the plant operating together." Thus potential buyers normally would not be interested in buying any fixtures separate from the land. While there have been some unusual situations where parts of a refinery have been sold, those sales were exigency sales where the plant is usually being shut down for a major renovation.

Thus Rule 461, subdivision (e) is unconstitutional in its application to refineries if it allows refinery fixtures to be valued as a separate appraisal unit from the land because it would violate the Constitutional requirement to tax based on fair market value.

Response

Legal Department staff generally agrees with Mr. Graves' analysis and conclusions.

Comment 2. David R. Doerr, Chair, Task Force on Property Tax Administration of 1978-79.

In a letter dated August 24, 2006, Mr. David Doerr, Chair of the Task Force on Property Tax Administration of 1978-79, wrote in opposition to proposed Rule 474. Mr. Doerr argued that the provisions of proposed Rule 474 are inconsistent with the recommendations of the Task Force on Property Tax Administration and legislation that enacted section 51.

Response

While the intent of section 51 was to separately value and assess fixtures from land, petroleum refineries present a unique industry warranting a unique valuation method as explained in Comment 1 and Response 3-1. Oil and gas producing properties, mining properties, and geothermal properties are also subject to specialized valuation rules because of the extremely high degree of integration of land and fixtures. Further, Mr. Doerr states that the Task Force decided to determine declines in value based on the appraisal unit commonly sold in the marketplace but does not explain the marketplace for refinery properties or describe how they are sold in the marketplace. Finally, Mr. Doerr does not cite any specific provision in the Tax Force recommendations or legislative history of section 51 that addresses the issue of petroleum refinery valuation.

Comment 3. Honorable Bill Leonard, Member, Board of Equalization, Second District.

In a letter dated September 11, 2006, Board Member Bill Leonard objected to the adoption of proposed Rule 474 stating that the proposed rule failed the "six tests" used to evaluate new regulations found in Government Code section 11349.1. His objections and Board staff's responses to those objections follow:

Objection 1: No Necessity

Proposed Rule 474 is unnecessary because no evidence or allegation of underassessment has been presented.

Response 3-1

Sufficient evidence in the rulemaking record exists to determine that proposed Rule 474 is necessary to obtain assessments more accurately reflecting how petroleum refinery properties would actually trade in the marketplace. In addition to Comment 1, at the June 27, 2006 Property Tax Committee meeting, Thomas Parker, Deputy County Counsel, Sacramento County; Rick Auerbach, Los Angeles County Assessor and President of the California Assessor's Association; Lance Howser, Chief Assessor, Solano County; and Robert Quon, Director of Major Appraisals for the Los Angeles County Assessor's office, all testified that refineries are in fact bought, sold, and valued as a single unit. At the same meeting, Mr. Auerbach testified that refineries are different from other heavily-fixturized manufacturing industries such as breweries, canneries, amusement parks and toy manufacturing. Refineries are unique in that up to 80 percent of their values are contained in the fixtures and because the land and fixtures are so integrated, it is difficult to physically separate the fixtures from the land. Further, the land and fixtures are also so economically integrated that a buyer normally would not, in a fair market transaction, purchase the land separately from the fixtures or the fixtures separately from the land.

Since petroleum refineries are bought and sold as a unit consisting of the land and fixtures, to value the fixtures separate and apart from the land may result in assessed values either below or above fair market value in violation of Propositions 8 and 13.

Objection 2: No Authority

The proposed Rule conflicts with the California Constitution, most notably, Proposition 8 and Proposition 13. Thus, the Board of Equalization has no authority to adopt the proposed Rule.

Response 3-2

The Board of Equalization has the authority pursuant to Government Code section 15606 to adopt rules and regulations to interpret, implement and make specific property tax provisions, including Proposition 8, Proposition 13, and section 51. Proposition 8 modified Proposition 13 to allow temporary reductions in assessed values of real property where the Proposition 13 value exceeds the Proposition 8 value. Section 51 was enacted to implement the provisions of Proposition 8.

Objection 3: Lack of Clarity

The proposed Rule is vague and ambiguous. As an example, assessors would be required to determine whether "fixtures and other machinery and equipment classified as improvements are not functionally and physically integrated with the realty and do not

operate together as one economic unit, and that it is not clear how one might define such a unit." Additionally, "it seems hopeless to expect ordinary taxpayers to understand it and apply it" and "it is not clear how one might define such a unit."

Response 3-3

The assessment issues raised by proposed Rule 474 can be clearly understood and determined by assessors and taxpayers, especially those with experience in the oil refining industry. Functional and physical integration are routinely addressed by assessors and taxpayers in the course of valuing property, and are specifically addressed in Rule 122.5, *Fixtures*, and in Chapter 2 of Assessors' Handbook Section 504, *Assessment of Personal Property and Fixtures*. Further, "appraisal unit" is defined in subdivision (c) (2) of Rule 122.5 and is addressed in detail in Assessors' Handbook Section 501, *Basic Appraisal*, and Assessors' Handbook Section 502, *Advanced Appraisal*. The determination of the correct "appraisal unit" is also routinely addressed by assessors and taxpayers in the course of valuing property.

Similar assessment issues to those in proposed Rule 474 were addressed by the California Court of Appeal in *Exxon Mobil Corp. v. County of Santa Barbara* (2001) 92 Cal.App.4th 1347. In *Exxon*, the court considered the definitions of "appraisal unit" found in Property Tax Rule 324, subdivision (b) and Assessors' Handbook section 502, *Advanced Appraisal* to determine that an off-shore oil production field and an on-shore refining facility connected only by a single pipeline were part of the same "appraisal unit" for property tax valuation purposes. In reaching that conclusion, the court made factual determinations that the facilities could not stand alone, that the value of the refining facility depended on the value of the production field, that the facilities were in a state of "symbiosis," and that due to the facility development plan and permit restrictions, the refining facility could not be sold separately from the production field. (*Exxon Mobil Corp. v. County of Santa Barbara* (2001) 92 Cal.App.4th 1347, 1353-1354.)

Objection 4: Lack of Consistency

The proposed Rule is inconsistent with section 51, subdivision (d) and Property Tax Rule 461. This inconsistency results in the inconsistent treatment of similarly-situated taxpayers, complicates tax administration, confuses taxpayers and assessors, increases errors and appeals, and creates the impression of favoritism and corruption.

Response 3-4

In the specific case of defining the appraisal unit for purposes of determining declines in value of petroleum refinery properties, proposed Rule 474 interprets, clarifies, and advances Rule 461 and section 51.

Currently, there are no rules specifically governing the declines in value of petroleum refining properties. Rule 461 and section 51 provide a general rule for determination of real property value changes and a general definition of "appraisal unit." Since, as explained in Response 3-1, petroleum refining properties present unique valuation issues related to the definition of the appropriate appraisal unit, Rule 461 and section 51 do not adequately address their valuations. Proposed Rule 474 creates a presumption regarding the appraisal unit to be valued and provides a means to rebut the presumption it creates, both of which are applicable to petroleum refining properties only.

Objection 5: No Reference

Although the proposed Rule contains several statutory references, the text of the rule does not advance, clarify, or interpret those references.

Response 3-5

Proposed Rule 474 furthers the referenced constitutional and statutory authorities by providing specific valuation methods for taxable property that result in appropriate assessed values. Proposed Rule 474 references California Constitution article XIII, section 1 and article XIII A, section 2, as well as sections 51, 53.5, and 110.1. As proposed, Rule 474 creates a rebuttable presumption defining the "appraisal unit" to be used in valuing petroleum refining properties and prescribes a specific methodology by which those properties are valued for all purposes, including declines in value.

Specifically, article XIII, section 1 of the California Constitution requires that all property is taxable. Proposed Rule 474 clarifies how a particular type of property (petroleum refining properties) should be taxed. Article XIII A, section 2 of the California Constitution and section 51 prescribe that taxable property shall be valued at the lesser of fair market value or adjusted base year value. Section 53.5 references an example of a statute allowing the use of a different appraisal method for decline in value purposes than that prescribed in section 51, subdivision (d) and Rule 461, subdivision (e). Proposed Rule 474 defines the petroleum refining property appraisal unit that will be used to determine "full cash value" under article XIII A, section 2, and clarifies how the value of petroleum refining properties should be determined when there has been a decline in value.

Objection 6: Duplication

The proposed Rule serves the same purpose as Property Tax Rule 461, and to the extent that taxpayers could rebut the presumption created by the rule, the tax outcome would be the same as if proposed Rule 474 did not exist.

Response 3-6

Currently, there are no other property tax statutes or rules specifically governing the declines in value of petroleum refining properties. Rule 461 provides a general rule for determination of real property value changes and, in subdivision (e), provides a general definition of "appraisal unit." To the extent that petroleum refining properties present unique valuation issues related to the definition of the appropriate appraisal unit, Rule 461 does not adequately address their valuations.

Proposed Rule 474 creates a presumption regarding the appraisal unit to be valued and provides a means to rebut the presumption it creates, both of which are applicable to petroleum refining properties only. To the extent that including fixtures and other machinery and equipment classified as improvements in the same appraisal unit as land and improvements is inappropriate in valuing a specific petroleum refining property, the taxpayer may submit evidence to overcome the presumption. Thus, in the specific case of defining the appraisal unit for purposes of determining declines in value of petroleum refinery properties, proposed Rule 474 would supersede, not duplicate, Rule 461.

Comment 4. Bob Poole, Coastal Coordinator, Western States Petroleum Association.

In a letter dated September 21, 2006, plus supplemental letters filed on the same day, the Western States Petroleum Association (WSPA) objects to the adoption of proposed Rule 474, stating that the proposed Rule does not comply with the California Administrative Procedures Act and the United States and California Constitutions. WSPA objections, followed by the Board staff's responses, are below:

Objection 1: There is No Necessity for Enactment of Proposed Rule 474, and Proposed Rule 474 is Not Reasonably Necessary to Effectuate Section 51, Subdivision (d)

There is no evidence in the rulemaking record supporting the need for proposed Rule 474. WSPA also states that it is not aware of factual circumstance that justifies changing the way petroleum refineries are currently assessed.

Response 4-1

See Response 3-1.

Objection 2: Proposed Rule 474 is Not Consistent With and Contradicts Various Authorities

Proposed Rule 474 contradicts section 51, Proposition 13, Proposition 8, and Property Tax Rules 461 and 324 since those authorities provide for the presumption that fixtures are not part of the same appraisal unit as land and improvements for purposes of

evaluating declines in value in property while proposed Rule 474 provides the opposite presumption.

Response 4-2

See Response 3-4. Rule 324, subdivision (b) states that an assessor's authority, in assessment appeals, to determine the full value of property is not predicated on nor limited by an applicant's request for relief and the assessor may determine the value of the entire "appraisal unit" when it is necessary to a determination of full value. Thus, determination of the relevant appraisal unit is an essential predicate to the determination of full cash value. In defining an appraisal unit, Rule 324 uses language similar to language in section 51, subdivision (d), which includes in the definition of "appraisal unit" "a collection of assets that function together, and that persons in the marketplace commonly buy and sell as a single unit." Accordingly, given that proposed Rule 474 is not inconsistent with section 51, it also is not inconsistent with Rule 324. Furthermore, Rule 324, subdivision (b), also states that an appraisal unit of property includes collections of assets specifically designated as such by the law. Proposed Rule 474 would make such a designation by creating a rebuttable presumption that petroleum refining properties are a single appraisal unit for decline in value purposes.

Objection 3: The Statutory References Cited in Rule 474 Do Not Support its Enactment

Proposed Rule 474 references sections 51, 53.5 and 110.1. None of these statutes referenced support proposed Rule 474's adoption: section 51 because it contains the opposite presumption as the proposed Rule; section 53.5 because it applies to leach pads, tailing facilities, and settling ponds, none of which are owned by petroleum refineries; and section 110.1 because the term "full cash value" is not used in proposed Rule 474.

Response 4-3

See Response 3-5.

Objection 4: Rule 474 Lacks Clarity

Proposed Rule 474 is unclear because it contains unfamiliar and undefined terms, terms which have more than one meaning, and terms which will be confusing to assessors and taxpayers who are directly affected by the rule. Specifically, WSPA contends that the following terms are unclear:

1. "Unique nature of property used for the refining of petroleum"
2. "Application of specialized appraisal techniques"
3. "'Appraisal unit' consists of the real and personal property that persons in the marketplace commonly buy and sell as a unit."

4. "Petroleum refineries and other real and personal property associated therewith"
5. "Fixtures not ... functionally and physically integrated with the realty."
6. "As identified in Standard Industrial Classification (SIC) System Codes 2911 and 2992, or North American Industry Classification System (NAICS) Codes 32411 and 324191."

Response 4-4

Proposed Rule 474 does not use terms so as to make the Rule unclear and unenforceable as Assessors and directly affected taxpayers currently interpret and apply complex appraisal terms.

1. See Response 3-1.
2. See Response 3-1.
3. See Response 3-1. Proposed Rule 474, subdivision (d)(2) clearly defines the components that make up an "appraisal unit" for petroleum refining purposes as "[t]he land, improvements, and fixtures and other machinery and equipment classified as improvements . . . ." Furthermore, defining an "appraisal unit" is a fundamental duty of assessors and appraisers.
4. The determination of real and personal property associated with petroleum refineries can be made through a development of facts by assessors and taxpayers, especially those that are experienced in the oil refining industry.
5. See Response 3-3.
6. The SIC and the NAICS are coding systems used to classify and measure economic activity by industry categories. The NAICS was developed in 1997 to replace the SIC, which was criticized as outmoded and not reflective of the United States economy. The SIC, however, is still in use by some agencies, most notably the Securities and Exchange Commission. Proposed Rule 474 makes reference to both classification systems. Each of the SIC and NAICS codes referred to in proposed Rule 474 properly identifies industries to which the proposed Rule would apply.[6]

---

[6] SIC Code 2911, "Petroleum Refining" is defined as:

> Establishments primarily engaged in producing gasoline, kerosene, distillate fuel oils, residual fuel oils, and lubricants, through fractionation or straight distillation of crude oil, redistillation of unfinished petroleum derivatives, cracking or other processes. Establishments of this industry also produce aliphatic and aromatic chemicals as by-products. Establishments primarily engaged in producing natural gasoline from natural gas are classified in mining industries. Those manufacturing lubricating oils and greases by blending and compounding purchased materials are included in Industry 2992. Establishments primarily re-refining used lubricating oils are classified in Industry 2992. (Occupational Safety and Health Administration, SIC Manual <http://www.osha.gov/pls/imis/sic_manual.display?id=627&tab=description>.)

Objection 5: Proposed Rule 474 Lacks Clarity in the Context of Existing Regulations

The language in Rules 461 and 324 demonstrates that proposed Rule 474 fails to meet the "clarity" standard of Government Code section 11349.1, subdivision (b). The proposed Rule is also inconsistent with Property Tax Rules 468, 469, and 470.

Response 4-5

See Response 3-3. Rule 461 and section 51 govern declines in value for all real property with the exception of oil and gas, mining, and geothermal properties, which are governed by Property Tax Rules 468, 469, and 473, respectively. In contrast to Rule 461, Rules 468, 469, and 473 provide, as an exception to the general rule of decline-in-value appraisal, that fixtures and other machinery and equipment classified as improvements do not constitute a separate appraisal unit. These rules were promulgated in recognition of the unique nature of these properties, and to provide specialized appraisal techniques required to satisfy the requirements of article XIII, section 1, and article XIII A, section 2, of the California Constitution. There is no requirement that special appraisal rules may only be made for depleting asset properties, nor is there any requirement that a property tax rule be "comprehensive" in dealing with all appraisal aspects of a particular industry.

As described in Response 3-1, petroleum refineries would be bought and sold in the marketplace as a single unit because they are heavily-fixturized, with fixtures that are more extensively integrated with the land than other heavily-fixturized manufacturers. Thus, similar to the exception to the general decline in value appraisal method found in Rules 468, 469, and 473, proposed Rule 474 provides an exception for petroleum refineries.

Objection 6: Proposed Rule 474 Violates the "Nonduplication" Standard

The proposed Rule contains provisions which overlap with those set forth in Property Tax Rule 461, subdivision (e).

SIC Code 2992, "Lubricating Oils and Greases," is defined as:

> Establishments primarily engaged in blending, compounding, and re-refining lubricating oils and greases from purchased mineral, animal, and vegetable materials. Petroleum refineries engaged in the production of lubricating oils and greases are classified in Industry 2911. (Occupational Safety and Health Administration, SIC Manual <http://www.osha.gov/pls/imis/sic_manual.display?id=630&tab=description>.)

NAICS Code 32411 refers to the industry group "Petroleum Refineries" which includes the six-digit code 324110 defined in the NAICS Manual as:

> This industry comprises establishments primarily engaged in refining crude petroleum into refined petroleum. Petroleum refining involves one or more of the following activities: (1) fractionation; (2) straight distillation of crude oil; and (3) cracking.

Response 4-6

See Response 3-6.

Objection 7: The Financial Impact of Proposed Rule 474 is Greatly Understated

The cost-impact figure set forth in the Board's August 11, 2006 Notice of Proposed Regulatory Action is too low and the Board should provide the public with the complete basis for its calculation. WSPA states that it believes the cost impact will be at least $5 million, and perhaps as much as $10 million.

Response 4-7

Board staff prepared a Revenue Estimate, Issue # 06-001 (Revenue Estimate), of the impacts of the proposed rule. This is the only dollar-value measure of potential underassessment of petroleum refinery properties that appears in the record to date. As part of the Revenue Estimate, a cost impact of proposed Rule 474 was calculated using WSPA- and County-supplied data. The derivation of this figure is included in the Revenue Estimate. WSPA has not provided data or methodology from which its cost impact estimates can be independently derived.

Objection 8: Proposed Rule 474 Violates Equal Protection Prohibiting Disparate Treatment of Taxpayers

There is no rational basis for proposed Rule 474's disparate treatment of petroleum refineries from other industries with "heavily-fixturized" properties.

Response 4-8

In equal protection challenges to state taxation where no specific federal right apart from equal protection is imperiled, the "States have large leeway in making classifications and drawing lines which in their judgment produce reasonable systems of taxation." (*Amador Valley Joint Union High School District v. State Board of Equalization* (1978) 22 Cal.3d 208, 233-234.) As long as a tax system has a "rational basis" and is not "palpably arbitrary," it will be upheld despite the absence of precise, scientific uniformity of taxation. (*Id.* at 234.) Accordingly, there is a long line of U.S. Supreme Court cases that permit states broad latitude to classify and tax property, including on the basis of: (1) the taxpayer's ability to pay (*Fox v. Standard Oil Company of New Jersey* (1935) 294 U.S. 87, 101); (2) the intangible or tangible nature of the property (*Klein v. Jefferson County Board of Tax Supervisors* (1930) 282 U.S. 19, 23-24); (3) the use of the property (*Clark v. Kansas City* (1900) 176 U.S. 114); (4) the corporate or individual status of the owner (*Lehnhausen v. Lake Shore Auto Parts Co.*

(1973) 410 U.S. 356); or (5) the acquisition date of the property (*Nordlinger v. Hahn* (1992) 505 U.S. 1 (upholding Proposition 13).).

Based on the record, summarized in part in Response 3-1, there is sufficient evidence to determine that a "rational basis" exists for proposed Rule 474, and that it is not "palpably arbitrary."

Objection 9: Proposed Rule 474 Will Produce a Lack of Uniformity in Assessments

A lack of uniformity in assessments will result if proposed Rule 474 is adopted since the proposed Rule will cause petroleum refineries to be assessed differently than other manufacturing and industrial properties, even though there is no palpable distinction between refineries and those other properties.

Response 4-9

Proposed Rule 474 does not violate article XIII, section 1 of the California Constitution which requires that property throughout the state be valued and assessed uniformly. As explained in Response 3-4, specific rules are promulgated for unique industries. As explained in Comment 1 and Response 3-1, evidence exists that petroleum refining properties are unique and qualitatively different from other industrial properties. Accordingly, an exception to the general rule is warranted for petroleum refinery decline in value purposes.

Objection 10: Proposed Rule 474 Violates the Prohibition Against New Property Taxes

The proposed rule effectively imposes a new tax or an increase in taxes on petroleum refineries by making the Proposition 8 protections inapplicable to petroleum refineries.

Response 4-10

Proposed Rule 474 does not violate article XIII A, section 3 of the California Constitution, which states that any changes in State taxes enacted for the purpose of increasing revenues requires a two-thirds legislative approval. The proposed Rule, however, is not being enacted for the purpose of raising revenue. It is being enacted to specify the correct appraisal methodology for a unique industry, where the general appraisal method has been found to be inadequate. Thus, it does not create a new tax, nor does it change the method or rate of tax within the meaning of article XIII A, section 3. It merely sets forth a specific method for the application of Proposition 8 to petroleum refining properties.

Comment 5. Kyla Christoffersen, Legislative Advocate-Taxation, California Chamber of Commerce & Matthew Sutton, Tax Policy Director, California Manufacturers and Technology Association.

In a letter dated September 25, 2006, the California Chamber of Commerce and the California Manufacturers and Technology Association object to the adoption of proposed Rule 474. Those organizations state two objections, summarized below and followed by the Board staff's responses.

Objection 1: The Proposed Rule Would Have Significant Statewide Adverse Economic Impact Since it Sets Precedent to Single Out Particular Industries.

No evidence has been provided in the proposed Rule or throughout the hearing process that refinery fixtures are "unique." Since refinery fixtures simply convert raw petroleum into petroleum suitable for commercial use, there is no distinction between refinery fixtures and fixtures used at other industrial and manufacturing facilities.

Response 5-1

Testimony has been provided that refining fixtures are "unique." See Response 3-1. For economic impact, see Response 4-7.

Objection 2: Proposed Rule 474 Violates Rulemaking Standards Because it Violates the United States and California Constitutions and There is No Statutory Authority or Reference.

The proposed Rule violates constitutional equal protection standards, as well as Propositions 8 and 13, Rule 461, subdivision (e), and section 51, subdivision (d). Thus, there is no authority or reference for the Board of Equalization to adopt proposed Rule 474.

Response 5-2

See Responses 3-2, 3-5, 4-5 and 4-8.

Comment 6. Attorney Cris K. O'Neall of Rodi, Pollock, Pettker, Galbraith & Cahill.

In a letter dated September 25, 2006, Cris O'Neall of the law firm Rodi, Pollock, Pettker, Galbraith & Cahill enclosed a compact disk (CD) containing an audio recording of the June 27, 2006 Board of Equalization Property Tax Committee meeting and requested that the CD to be included in the rulemaking record.

Response

The CD is included as a part of the rulemaking record.

Comment 7. Attorney Cris K. O'Neall of Rodi, Pollock, Pettker, Galbraith & Cahill.

In a letter dated September 26, 2006, Cris O'Neall of the law firm Rodi, Pollock, Pettker, Galbraith & Cahill objects to proposed Rule 474 since Letters to Assessors (LTA) 79/59 and 79/143 affirm that fixtures are separate appraisal units for Proposition 8 purposes.

Response

The above-cited LTAs apply generally to machinery and equipment. To the extent that a new rule such as proposed Rule 474 establishes a different means of calculating declines in value for a specific industry, the cited LTAs would not apply. LTA 79/59 states that the taxable value of machinery and equipment classified as improvements should be the lower of either the factored base year value or the market value, and establishes a new base year value for the machinery or equipment. LTA 79/143 states that LTA 79/59 is incorrect in stating that when the fair market value is lower than the factored base year value a new base year value is established. These LTAs discuss the decline in value rules as they apply generally to fixtures and not specifically to the petroleum refinery industry. Thus, they are of limited value in determining the proper method by which to determine a decline in value of petroleum refinery equipment.

Comment 8. Teresa Casazza, VP-Legislative Director, Cal-Tax.

In a letter dated September 26, 2006, Teresa Casazza stated that Cal-Tax objects to proposed Rule 474 on two grounds. She also offers as an alternative to the adoption of proposed Rule 474, an amendment to Rule 461, subdivision (e).

Objection 1: Violates Government Code 11349.1 "Necessity" Requirement

The Board of Equalization has not demonstrated by substantial evidence the "need for a regulation."

Response 8-1

See Response 3-1.

Objection 2: Violates Government Code 11349.1 "Consistency" Requirement

Proposed Rule 474 conflicts with section 51, subdivision (d)'s presumption that fixtures are a separate appraisal unit by establishing a presumption that fixtures are not presumed to constitute a separate appraisal unit.

Response 8-2

See Response 3-4.

Cal-Tax Alternative: Amendment to Rule 461, Subdivision (e)

The proposed amendment to Rule 461 would create a presumption that fixtures are a separate appraisal unit.

Response 8-3

Rule 461 and section 51, subdivision (d) already presume that fixtures are valued separately for decline in value purposes. However, the amended Rule 461 is inadequate in addressing specific industries, such as the petroleum refining industries, requiring unique valuation methods as described in Comment 1 and Response 3-4. See also Oral Comment 1.

Oral Comments

The following oral comments were made at the September 27, 2006 Board meeting in Sacramento, California.

Comment 1. Rick Auerbach, Assessor, Los Angeles County & President, California Assessors' Association

Mr. Auerbach stated that he supports the adoption of proposed Rule 474. It is consistent with section 51, subdivision (d) since refineries are commonly bought and sold as a unit including the land and structures and fixtures. Mr. Auerbach also stated that homes with fixtures are treated as a single appraisal unit and that if the proposed rule does not pass, it would amount to a break for refineries that is not given to the individual homeowner. Finally, Mr. Auerbach also stated that the Cal-Tax alternative proposal would result in refineries being excluded from appraisal as a single unit since the proposal requires there to be a number of willing buyers and a number of properties for sale at all times.

Response 1

The Board's legal staff generally agrees with Mr. Auerbach's comments.

Comment 2. Gus Kramer, Assessor, Contra Costa County

Mr. Kramer stated that he supports the adoption of proposed Rule 474.

Response 2

None.

Comment 3. Thomas Parker, Deputy County Counsel, Sacramento County

Mr. Parker stated that he supports the adoption of proposed Rule 474.

Response 3

None.

Comment 4. Wayne Lewoczko, ExxonMobil

Mr. Lewoczko stated that there is no difference between oil refineries and other manufacturers. Oil refineries are liquid assembly lines where heat is added to raw materials to create the finished product.

Response 4

See Written Comment 1 and Response 3-1 to the Written Comments above.

Comment 5. Teresa Casazza, California Taxpayers Association

Ms. Casazza expressed two objections: (1) that the enactment of proposed Rule 474 does not meet the consistency and necessity provisions of Government Code section 11342.1; and (2) that the proposed rule conflicts with section 51, subdivision (d). As an alternative, Ms. Casazza submitted a proposed amendment to Rule 461, subdivision (e) creating a presumption that fixtures are a separate appraisal unit for all manufacturers and industries.

Response 5

See Responses 3-1 ,3-4, and 8-3 to the Written Comments above.

Comment 6. Cris O'Neall, Rodi Pollock, representing the Western States Petroleum Association

Mr. O'Neall stated that proposed Rule 474 conflicts with section 51, subdivision (d) and the proposed rule is unnecessary.

Response 6

See Responses 3-1 and 3-4 to the Written Comments above.

Comment 7. Richard Ayoob, Ajalat, Polley & Ayoob

Mr. Ayoob objected to the adoption of proposed Rule 474 because it violates Propositions 8 and 13 without a rational appraisal theory. Other regulations, such as those that deal with the extraction of oil and other minerals, that do not separate fixtures

for decline in value purposes deal with a species of property very different from oil refineries.

Response 7

See Responses 3-2 and 4-8 to the Written Comments above.

Comment 8. Erika Frank, California Chamber of Commerce

Ms. Frank objected to proposed Rule 474 because the proposed rule sets a dangerous precedent of singling out a particular industry, which will add complexity and confusion to the property tax laws.

Response 8

See Responses 3-1 and 4-8 to the Written Comments above.

Comment 9. Matt Sutton, California Manufacturers and Technology Association

Mr. Sutton objected to proposed Rule 474 because the proposed rule sets a dangerous precedent of singling out a particular industry, which may lead to the incremental adoption of similar rules for other industries.

Response 9

See Responses 3-1 and 4-8 to the Written Comments above.

Comment 10. Elizabeth Maeng, ConocoPhillips

Ms. Maeng objected to the adoption of the proposed rule because there is no need to adopt the proposed rule and because adoption of the proposed rule would violate the equal protection clause.

Response 10

See Responses 3-4 and 4-8 to the Written Comments above.

Effect on Business

Pursuant to Government Code section 11346.5, subdivision (a)(8), the Board of Equalization makes an initial determination that the adoption of Rule 474 will not have a significant statewide adverse economic impact directly affecting business because the proposed rule merely interprets and clarifies existing statutory provisions.

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

The rule will not affect small business because the new rule only interprets and clarifies property tax assessment law statutory provisions and does not impose any additional compliance or reporting requirements on taxpayers.

Federal Regulations

Rule 474 has no comparable federal regulation.

Plain English Statement

Rule 474 clarifies the requirements under article XIII, section 1, and article XIII A, section 2, of the California Constitution for the valuation of real property, personal property, and fixtures used to refine petroleum.

Alternatives Considered

The Board has determined that no reasonable alternative considered by it or that has otherwise been identified and brought to its attention would be more effective in carrying out the purpose for which this action is proposed or be as effective as and less burdensome to affected private persons than the proposed action.

Cahill·Davis & O'Neall, LLP
LAWYERS

John D. Cahill
C. Stephen Davis
Cris K. O'Neall
Wade E. Norwood
Andrew W. Bodeau

660 South Figueroa Street • Suite 1650
Los Angeles, California 90017

telephone: 213-622-0600
facsimile: 213-622-9825

www.cahilldavis.com

July 23, 2007

Ms. Diane Olson
Regulations Coordinator
P. O. Box 942879
450 N Street, MIC:80
Sacramento, CA 94279-0080

Re: Proposed Property Tax Rule 474, *Petroleum Refining Properties*
Comments on Revised Initial Statement of Reasons ("Revised ISR")
Hearing Date: August 14, 2007

Dear Ms. Olson:

At the request of the Western States Petroleum Association ("WSPA"), I am submitting the following information and attachments pertaining to Proposed Property Tax Rule 474 for consideration by the State Board of Equalization at the hearing on August 14, 2007.

This information and attachments provide evidence that petroleum refinery process units, which consist of machinery and equipment (and are classified as "fixtures" for property tax purposes), are sold in the marketplace separately from the land on which they are situated and then relocated and installed at other sites.

This evidence contradicts the unsupported assertions in the Revised ISR that refinery land, improvements and fixtures always (or almost always) transfer in the marketplace as a single unit. This evidence undermines the basis for adoption of Proposed Rule 474 as framed by the ISR.[1]

---

[1] Note that WSPA disagrees with way in which the Revised ISR frames the "test" for determining whether refinery fixtures and land should be treated as part of the same unit for property tax purposes. The ISR contends that fixtures and land are part of the same "economic unit" through vague references to refinery sales, and then erroneously concludes that refinery fixtures and land are part of the same "appraisal unit." In fact, the starting reference point is whether refinery fixtures and land are part of the same "appraisal unit," a term that appears in *Revenue and Taxation Code* section 51(d). Section 51(d) defines the "appraisal unit" as either the unit "that persons in the marketplace commonly buy and sell as a unit, *or that is normally valued separately*." The latter italicized phrase applies to refinery fixtures, and establishes the requirement that such fixtures be assessed as a separate appraisal unit. In this context, whether or not refinery fixtures and land are part of the same "economic unit" has little relevance. Nevertheless, the evidence set forth below demonstrates that refinery process units do not always or even commonly sell with the land on which they are situated (*i.e.*, often they are not part of the same "economic unit").

Process Units Are Marketed Separately from Entire Refineries

There is ample evidence available through the Internet that individual process units are marketed separately from entire refineries and separately from the land on which the individual process units are situated. **(SEE EXHIBIT A)**

For example, Ventech Process Equipment, Inc. ("Ventech") is currently offering or has offered a number of process units for sale at the Gaviota, California Gas & Oil plant and at the ChevronTexaco Panama Refinery. In addition, Ventech is currently offering for sale the Hydrogen plant at the Chevron Refinery in El Segundo, California.

Similarly, Total Energy is currently offering for sale process units at a natural gas plant in Pennsylvania, and Cenco Refining Company in Santa Fe Springs, California is offering several units from its refinery for sale. Likewise, Bexar Energy has reported a number of sales and relocations of process units, including the sale and relocation of a process unit from California to Washington.

Process Units Are Sold Separately from Refineries and Relocated to Other Sites.

Information from industry trade journals and from market participants shows that refinery process units offered for sale are frequently sold and relocated, usually to another refinery or chemical plant.

Oil industry trade journals have reported on sales and relocations of refinery process units in recent years. The March 20, 1995 edition of *Oil & Gas Journal* chronicled the sale and transfer of a refinery process unit (vacuum unit) from a refinery in Carson, California to the Tesoro refinery in Kenai, Alaska. The same edition of the *Oil & Gas Journal* reported on the sale and relocation of several process units from a refinery in Freeport, Texas to Philbro Energy USA's refinery in Texas City, Texas. Other process units from the same Freeport, Texas refinery were sold and relocated to a refinery in South Korea. **(SEE EXHIBIT B)**

Ventech has participated in the sale and relocation of dozens of refinery process units in recent years. These projects are reported in Ventech's company literature or on the company's website. The process units that Ventech has sold are significant in size, and include key refinery components such as crude units, vacuum units, fluid catalytic cracking (FCC) units, hydrotreaters and reformers. **(SEE EXHIBIT C)**

Selected Refinery Process Units Sales/Relocations Reported by *O&GJ* and Ventech

Type of Unit	Buyer / Seller	Located from	Located to
Vacuum	Tesoro / Fletcher	Carson, California	Kenai, Alaska
Crude, Hydrotreaters	Philbro / Dow	Freeport, Texas	Texas City, Texas
Sulphur	BP Amoco / Pride	Abilene, Texas	Mandan, No. Dakota
Sulphur	Koch / Unknown	Louisiana	Corpus Christi, Texas
Hydrocracker	Gary / Unknown	Louisiana	Fruita, Colorado
Reformer	Ashland / Ashland	Buffalo, New York	St. Paul, Minnesota

The above, along with the attached documents, demonstrate that refinery process units, which constitute the bulk of the fixtures at any refinery, are often sold separately from the land on which they are situated, and that refinery process units do not always transfer as a single unit.

There is no evidence in the Revised ISR for Proposed Rule 474 that contradicts the information in this latter and the attachments hereto, nor is there any evidence supporting the ISR's assertions that refinery process units (fixtures) always transfer with land and improvements as a single unit.

The assumption underlying the Revised ISR, that refineries are always bought and sold as a single unit, cannot be met and, therefore, Proposed Rule 474 should not be adopted.

Respectfully submitted,

Cris K. O'Neall

Attachments

cc: Honorable Betty Yee, Member, First District (w/Attachments)
Honorable Bill Leonard, Member, Second District (w/Attachments)
Honorable Michelle Steel, Member, Third District (w/Attachments)
Honorable Judy Chu, Member, Fourth District (w/Attachments)
Honorable John Chiang, State Controller, c/o Marcy Jo Mandel, Deputy State Controller (w/Attachments)

z:/

EXHIBIT A

Ventech Process Equipment, Inc.

The Ventech Companies

Ventech Engineers, Inc.

Ventech Engineers Int'l Corp.

Ventech Process Equipment, Inc.

Ventech Appraisal Services, Inc.

1149 Ellsworth
P.O. 4261
Pasadena, Texas 77502
(713) 477-0201 phone
(713) 477-2420 fax

Legal Notice

FOR SALE

(For Relocation Only)

Gaviota Gas & Oil Plant

The Gaviota Gas and Oil Plant is designed to process 100,000 BPD of crude and 60 MMscfd of gas. Click for detailed description.

The Oil Plant produces dry, stabilized crude for shipment via pipeline. The Gas Plant produces sweet sales gas, propane, butane, NGL and elemental sulfur for shipment by truck and pipeline.

Associated utilities and produced water treating systems are also available from this site.

Block Flow Diagram (PDF)

Individual Plants:

- Plant 3 - Oil Stabilization Plant
- Plant 4 - Produced Water Treating Plant
- Plants 10A/10B - Intake Separation, Condensate Stripping and Gas Compression Plants ---> **10B SOLD**
- Plants 11/21 - Acid Gas Removal Plants ---> **SOLD**
- Plants 12/13 - LTS/Deethanizer and Sales Gas Compression
- Plants 14/24 - Selectox Sulfur Plants --->**14 SALE PENDING**
- Plants 15/25 - Tail Gas Treating Plants --->**15 SALE PENDING**
- Plant 16 - Fractionation Plant ---> **SOLD**
- Plant 17 - Liquids Treating Plant
- Plant 72 - VRU and Utilities
- Plants 73A/73B - Sulfur & LPG Loading & Storage -->**73A SOLD**

Detailed Equipment List:

- Air Coolers
- Blowers
- Boilers
- Centrifugal Pumps
- Columns
- Compressors
- Filters
- Heat Exchangers
- Miscellaneous
- Tanks
- Reciprocating Pumps
- Vessels

Ventech Process Equipment, Inc.

The Ventech Companies

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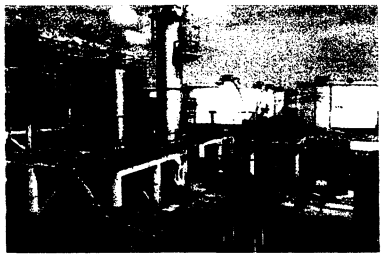
Legal Notice

FOR SALE
(For Relocation Only)

ChevronTexaco Panama Refinery



The Panama Refinery was originally constructed in 1961 and expanded in 1967 to provide LPG, gasoline, jet fuel, diesel fuel and asphalt for Panama's domestic consumption and Bunker C for the Panama Canal's shipping industry. The refinery underwent several modernizations and revamp projects throughout the 1970's and 1980's. Click for detailed description.

From 1993 to 1994 a major project was implemented to increase the size of the Visbreaker Unit through the installation of a new Saturated Gas Plant, Naphtha Splitter Unit, LSRN/LPG Merichem Treaters, and various smaller revamps that converted the refinery to its current configuration. Other smaller projects, equipment and upgrading projects continued until the facility's closure in 2002. Oriente crude from Ecuador, with an average 26 API, 1.1 wt% sulfur, was the last crude slate run when the refinery was closed.

Block Flow Diagram (PDF)

Complete Process Units and approximate operating capacities:

- Crude Distillation Unit 60,000 b/d---> **SOLD**
- Vacuum/Asphalt Unit 11,000 b/d---> **SOLD**
- Visbreaker Unit 27,000 b/d ---> **SALE PENDING**
- Naphtha Splitter Unit 16,500 b/d---> **SOLD**
- Hydrotreater Units
  Naphtha Hydrotreater Unit 11,800 b/d
  Kerosene Hydrotreater Unit 8,500 b/d
  Diesel Hydrotreater Unit 6,500 b/d
- Catalytic Reformer Unit 11,000 b/d
- LPG Stabilization Unit 7,250 b/d
- Merichem Treaters
  LSRN 5,500 b/d
  LPG 2,750 b/d

Equipment Lists:

- Air Coolers
- Blowers
- Centrifugal Pumps
- Columns ---> **SOLD**
- Compressors ---> **SOLD**
- Filters
- Heaters
- Heat Exchangers
- Miscellaneous
- Tanks
- Reciprocating Pumps
- Vessels

Ventech Process Equipment, Inc.

The Ventech Companies

Ventech Engineers, Inc.

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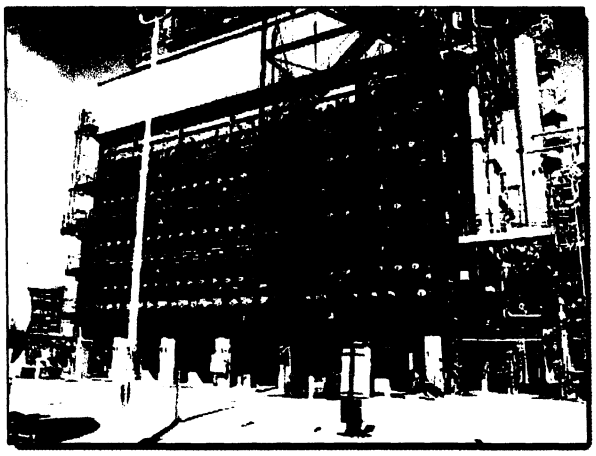
(713) 477-2420 fax

Legal Notice

FOR SALE

(For Relocation Only)

El Segundo Hydrogen SMR



Process Flow Diagram

Detailed Equipment List:

- Compressors
- Heat Exchangers
- Heaters
- Pressure Vessels
- Pumps

Section 100

Section 150

Section 200

Catalytic Rich Gas (CRG)

Section 300

Support Facilities

Synthetic Natural Gas Plant

Philadelphia, PA

Plant Details

The SNG facility was constructed in 1977 but has seen very little operational activity. The SNG Facility employs the British Gas hydro gasification process to convert naptha feedstock into SNG at a design rate of 60,000 decatherms per day, and was constructed by Foster Wheeler Energy Corporation. The principle areas of the plant that are offered for sale are as follows:

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REFINING COMPANY

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PARTS FOR SALE

- Units For Sale
- Pumps For Sale

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Units For Sale

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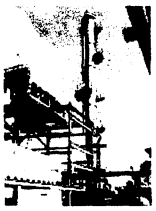
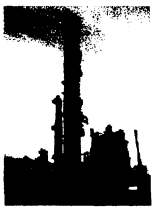


FCC Depentanizer



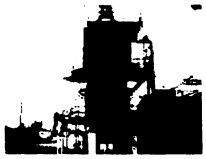
Fractionator Column

Coker Fractionator Column

Vapor Recovery Unit

Boilers

Hydrogen Plant

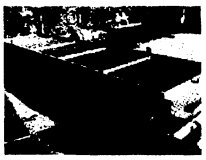


20 MMBTU/hr Natural Gas Fired Heater

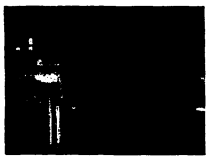
27 MMBTU/hr Natural Gas Fired Heaters

Beckman MV 8000 Process Control System

Heated Blending Tank



Heat Exchangers



Physical Plant Items

New Stainless and Monel Tubing

New Items For Sale

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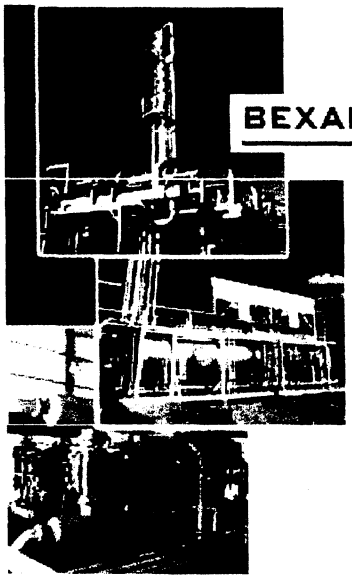
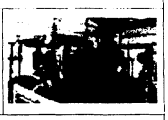
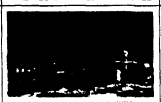
BEXAR



BEXAR ENERGY PROJECT LIST

Equipment Inquiries

BEXAR ENERGY RECENT PROCESS EQUIPMENT SALES			
3 Ea. 3200 Hp Gas Engine Drive Recompressors, Relocated From Louisiana To New Mexico		4 Ea. 3200 Hp Gas Engine Drive Refrigeration Compressors, Relocated From Louisiana To New Mexico	
25 Mmcfd Cryogenic Plant, Relocated Within Texas		225 Gpm Amine Plant, Relocated From Oklahoma To Pakistan	
6000 Bpd Fractionation Plant And Storage Facility, Relocated From California To Nigeria		55 Mmcfd Cryogenic Plant, Relocated From Louisiana To Nigeria	
800 Gpm Amine Unit, Relocated From Louisiana To Texas		800 Gpm Amine Unit, Relocated From Louisiana To Pakistan	
75 Mmcfd Cryogenic Plant, Relocated From Texas To Bolivia		15 Mmcfd Cryogenic Plant, Relocated Within Texas	

300 Gpm Amine Plant, Relocated From California To Washington		1 Ea. 8000 Hp Electric Motor Drive Injection Compressor, Relocated Within Texas	
100 Gpm Amine Plant, Relocated Within Texas		2 Ea. 1100 Hp Gas Engine Drive Recompressors, Relocated Within Texas	
60 Gpm Amine Plant Relocated Within Texas		3 Ea. 600 Hp Gas Engine Drive Feed Gas Compressors, Relocated Within Texas	
2 Ea. 800 Hp Gas Engine Drive Feed Gas Compressors, Relocated Within Texas		40 Gpm Amine Plant, Relocated Within Texas	
25 Gpm Amine Plant, Relocated From Oklahoma To Texas		55 Gpm Amine Plant, Relocated Within Texas	
20 Mmcfd Refrigeration Plant, Relocated From Texas To Louisiana		7 Mmcfd Refrigeration Plant, Relocated Within Texas	
15 Mmcfd Cryogenic Plant, Relocated Within Texas		14 Tpd Sulfur Recovery Unit, Relocated From Oklahoma To Texas	

EXHIBIT B

Alaskan refiner raced against winter to relocate vacuum unit

Lowell Michael Gdula *Tesoro Petroleum Corp. Kenai, Alas.*
James A. Wentworth *Litwin Engineers & Constructors Inc. Houston*

In late November 1994, San Antonio-based Tesoro Petroleum Corp. and Litwin Engineers & Constructors Inc. completed the relocation and refurbishment of a $25 million vacuum unit at Tesoro's 72,000 b/d Kenai, Alas., refinery.

The addition of the vacuum distillation unit is a critical component in Tesoro's market-driven strategy to enhance operating profits by maximizing production of higher-margin products such as gasoline and jet fuel.

With its new vacuum distillation unit, Tesoro has reduced production of lower-value residual fuel oil while recovering more lighter, high-value material. This investment is projected to yield increased operating income of $9-15 million/year, an after-tax internal rate of return of 35%, and a payback period of 2.5 years.

The decision

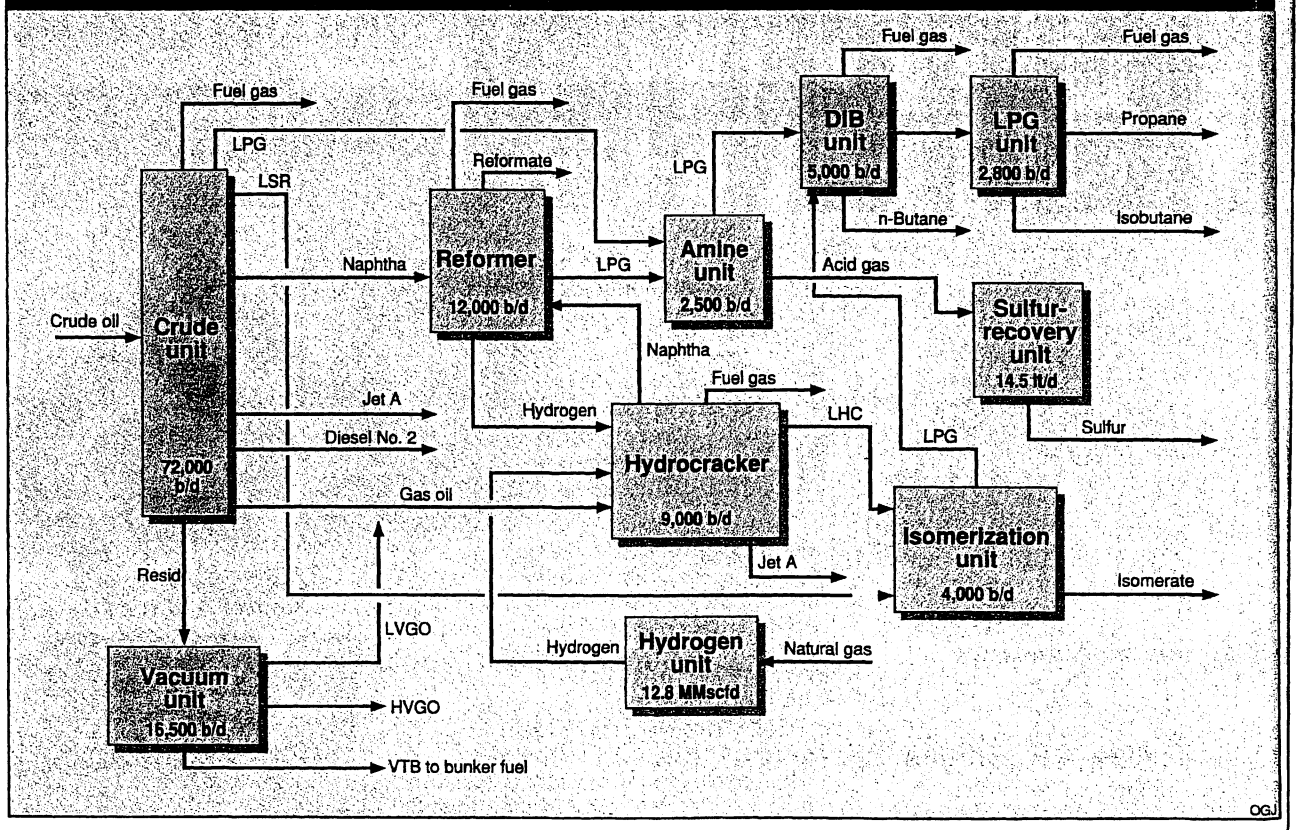
The economic and strategic merits of purchasing and relocating an existing vacuum unit vastly outweighed those of constructing a new unit on site. The cost difference between the two options was estimated to be $3-5 million (overall installed cost).

The vacuum unit was purchased from Fletcher Oil & Refining Co., which owns a shutdown refinery in Carson, Calif. Salvaging all the major equipment from the relatively new unit (commissioned in 1989 and operated for only 18 months) resulted in a majority of the cost savings.

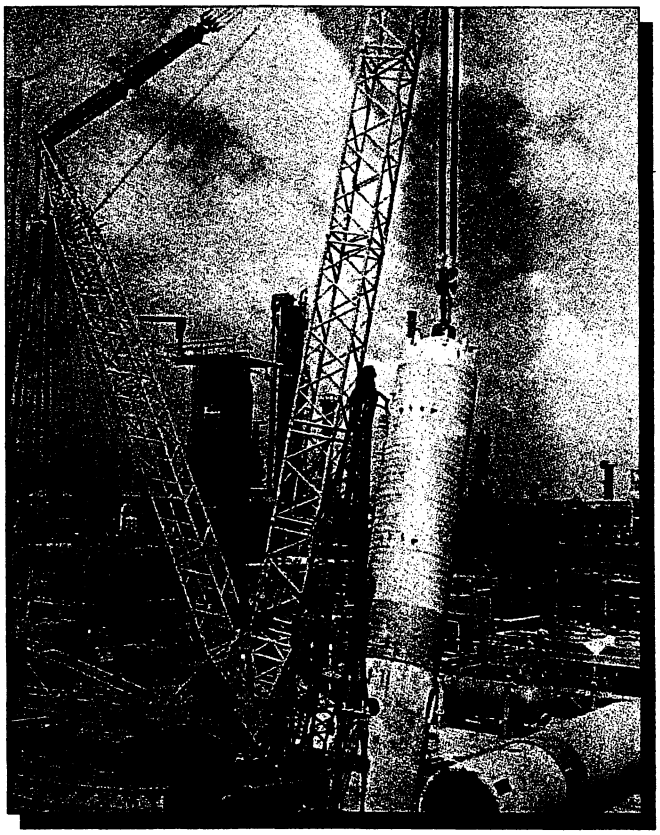
Although the unit required significant modification, the additional time and money necessary to build a grassroots unit ultimately drove the decision toward relocation and refurbishment. Fig. 1 shows a flow diagram of Tesoro's Kenai refinery.

Fig. 1

REFINERY FLOW DIAGRAM



The 63,000 b/cd Residfiner at the former Dow refinery at Oyster Creek, Tex., was moved to Phibro Energy USA Inc.'s Texas City refinery. This photo shows the dismantling of the Residfiner reactors (Fig. 1).



About this report

This year's Refining Report describes four unique projects that are saving refiners bottom-line dollars:

- Equipment from an idle Texas refinery is being relocated and integrated into two separate refinery expansions, one in Texas and the other in South Korea.
- A refiner in Alaska installed an idle vacuum tower, moved from a California site, to reduce resid production.
- An Austrian refiner has increased throughput in its butadiene and methyl tertiary butyl ether units using advanced process control.
- A Canadian refiner was the first to reduce waste disposal costs by using a caustic-free Merox process for treating jet fuel.

Texas refiner optimizes by integrating units from idle plant

Anne K. Rhodes *Refining/Petrochemical Editor*

In 1993, Phibro Energy USA Inc. purchased Dow Chemical Co.'s idle 200,000 b/d refinery at Freeport, Tex. The Dow facility, known as the Oyster Creek refinery, was incapable of producing gasoline, and therefore was somewhat incomplete as a stand-alone refinery.

By relocating and integrating units from the Dow plant with Phibro's 130,700 b/d refinery at Texas City, Tex., and adding a new residual oil solvent extraction (ROSE) unit, Phibro will optimize its Texas refinery operations.

The dismantling, movement, and re-erection phases of the project are all but finished, and installation of piping and new instrumentation for the major relocated units is well under way. When the project is complete, Phibro will drastically reduce fuel oil production at Texas City and increase output of middle distillate.

Resid, which the company now produces in excess, will be converted to a heavy fluid catalytic cracking (FCC) feedstock. Most of this stream will be fed to the oversized FCC unit (FCCU) at Phibro's 71,000 b/d Houston refinery, thus eliminating Phibro's reliance on purchased FCC feed.

Oyster Creek refinery

During the 1970s oil embargo, Dow was in need of naphtha feedstock for its Freeport, Tex., ethylene plant. The company decided to build what Richard Duszynski, Phibro's senior vice-president of planning and business development, calls "half a refinery."

The 200,000 b/d plant comprised: a crude tower, three distillate

Korean refiner buys rest of Dow refinery

THERE IS A GOOD DEAL OF EQUIPMENT AT Dow's Oyster Creek refinery that Phibro does not have use for at its Texas City site—specifically, a 200,000 b/sd crude unit, 32,000 b/sd gas oil hydrotreater, two 24,000 b/cd kerosine hydrotreaters, and a 6,000 b/sd light-ends processing and treating unit. But Phibro's contract with Dow included the requirement that Phibro was to remove all of the refinery equipment from the site.

Subsequent to Phibro's agreement with Dow, the refiner struck a deal for purchase of the unused equipment with Hyundai Oil Refinery Co. Ltd., operator of a 60,000 b/d refinery at Daesan, South Korea.

As part of Phibro's contract with Hyundai, Phibro managed the dismantling and preparation of the equipment for shipment to Seoul.

Phibro also is refurbishing some equipment (including pumps, compressors, motors, and control, relief, and block valves) before it is shipped to Korea. Matrix Engineering Inc. and A&B Constructors Inc. are under contract to Phibro in this effort.

Work on this portion of the relocation project began in April 1994 and was completed in October. For this work, more than 20,000 pieces of equipment were tagged with bar-coded labels.

The largest combination of lifts involved in this project (in fact the two largest lifts ever made in North America) was movement of the 758-ton crude tower, which was 200 ft long and 30 ft in diameter. To make the two lifts required to move this tower, A&B Constructors used 800 and 1,100-ton DeMag SuperLifter Cranes from Italy.

The crude tower was the first shipment to leave the Freeport docks for Korea.

The tower was shipped via the M/V Super Servant 4, a vessel from The Netherlands, on Aug. 24, 1994 (photo).

The unit was lowered onto four self-propelled motor transports owned and operated by The Netherlands' Davenport Mammoet. A Roflo crane was used to load the tower from the barge to the vessel.

The Super Servant 4 vessel holds a crude tower and other equipment bound for Hyundai's refinery in Daesan, South Korea.

Fourteen other large pieces of equipment (crude heaters, reactors, etc.) weighing 3,763 tons were loaded onto barges for movement from the refinery to the transport vessel.

The equipment was then loaded onto the vessel, using the Russian Titan V barge crane.

The second shipment departed during the last week of September. This Bahamas-registered Croatian ship, called the M/V Franine, contained 233 pieces of equipment weighing 7,840 tons. The third and final ship was Africa's M/V PAL Wind, which was loaded with 53 pieces of equipment weighing 1,500 tons.

Other equipment was shipped to the port of Long Beach, Calif., via rail, then to Korea.

More than 400 40-ft containers holding all associated pipe, structural steel, instrumentation, and electrical and other small equipment, have been hauled to Long Beach.

Hyundai plans to use the equipment as a central component in a major expansion of its refinery to 310,000 b/d from its present capacity of 110,000 b/d. In addition to the relocated units, Hyundai will build a 20,000 b/sd naphtha hydrotreater, a 20,000 b/sd Platformer, and a 180 tons/day sulfur recovery unit.

Houston and Texas City refineries will be fed hydrotreated feedstock; whereas today they typically process virgin feedstock. There will be little if any change in FCCU operating parameters, but an increase in conversion and product quality is expected.

Fig. 3 illustrates the integration of Phibro's Texas refineries after completion of the project.

Utilities

The added units will increase electricity requirements at the Texas City refinery from the current level of 35 mw to 62 mw after the expansion. Of this increase, 7 mw will be provided

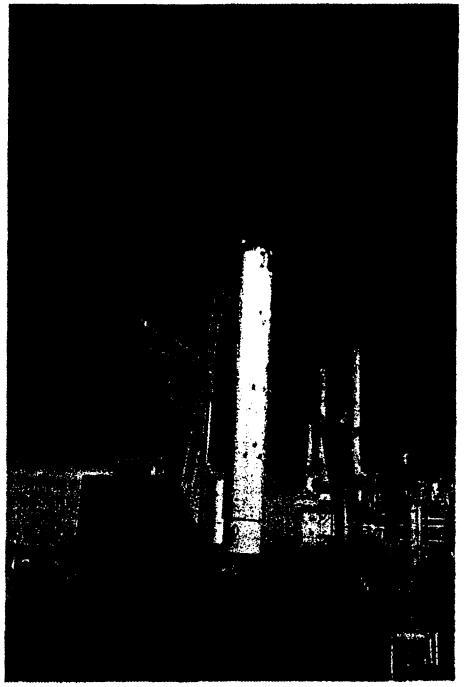
EXHIBIT C

Distillate Desulphurization Unit

A Relocation Project of

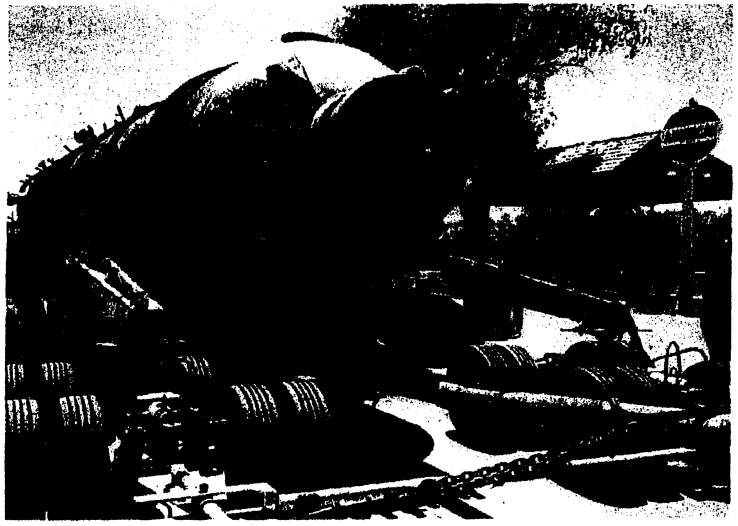
The Ventech Companies

For BP Amoco
Mandan, North Dakota



A Surplus 12,000 BPD Distillate Desulphurization Unit was purchased by Ventech Process Equipment from Pride Refining in Abilene, Texas and relocated for BP Amoco to their Mandan, North Dakota refinery by Ventech Engineers.

Ventech Engineers provided the engineering, procurement, and construction management services to dismantle, refurbish, relocate, and re-erect the unit. The dismantling effort in Abilene began March, 1999, broke ground in Mandan in April, 1999 and was completed in June, 2000 including winter curtailment of 4 months.



VENTECH ENGINEERS, INC.
A VENTECH COMPANY

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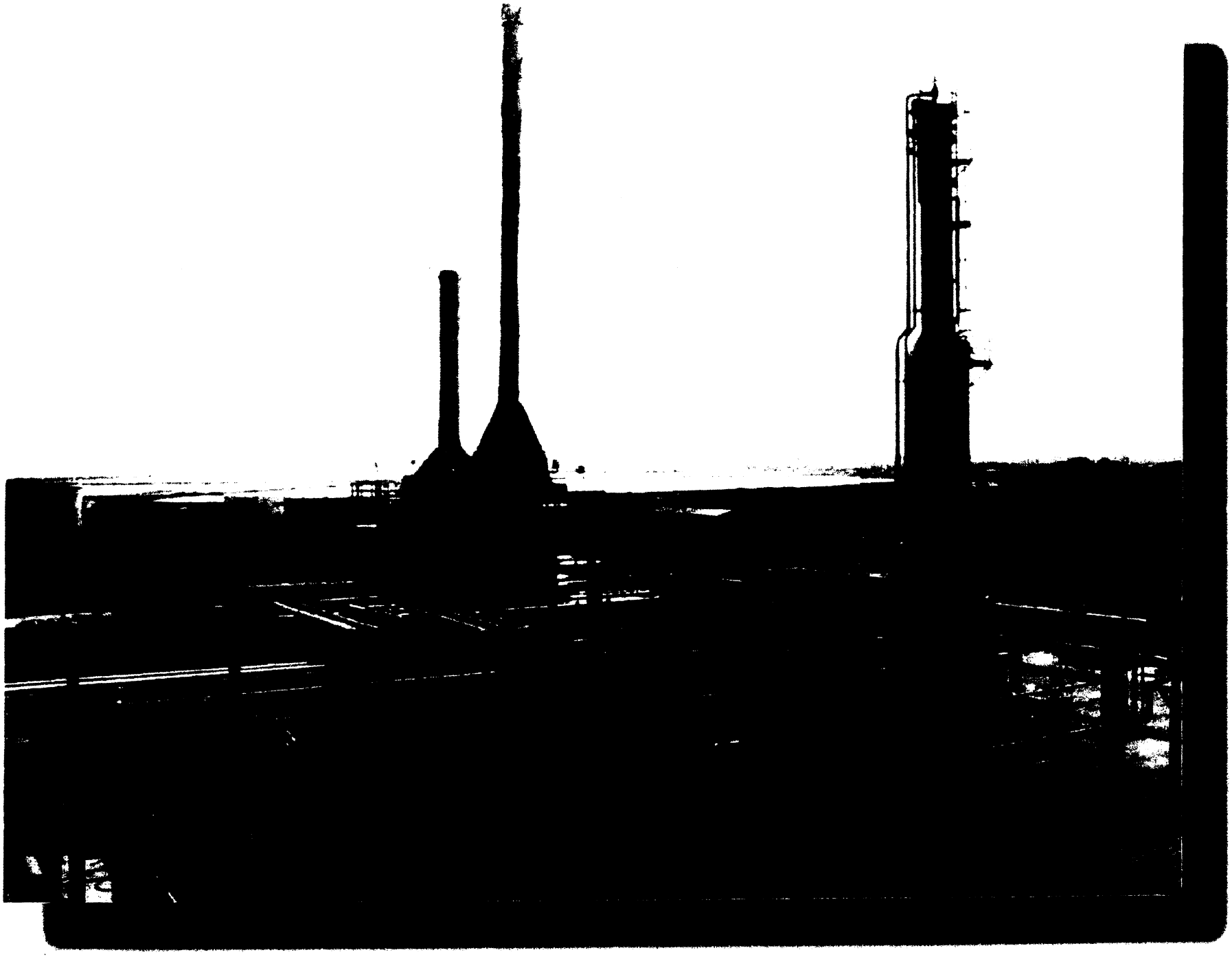
www.ventech-eng.com

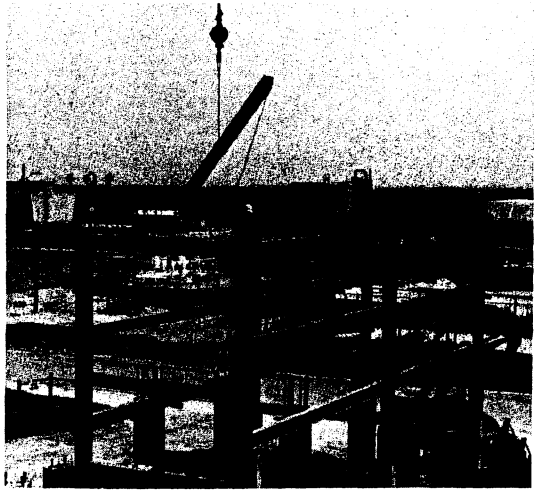


Naphtha Desulfurization Unit

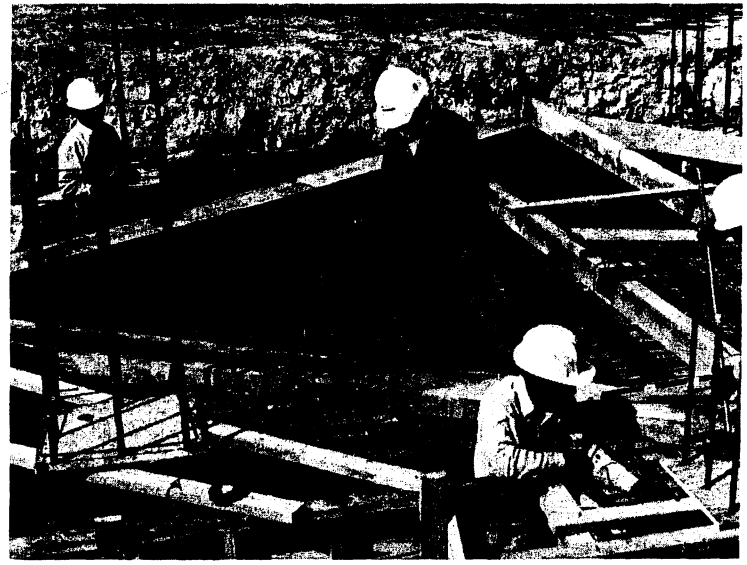
A Relocation Project of
THE VENTECH COMPANIES

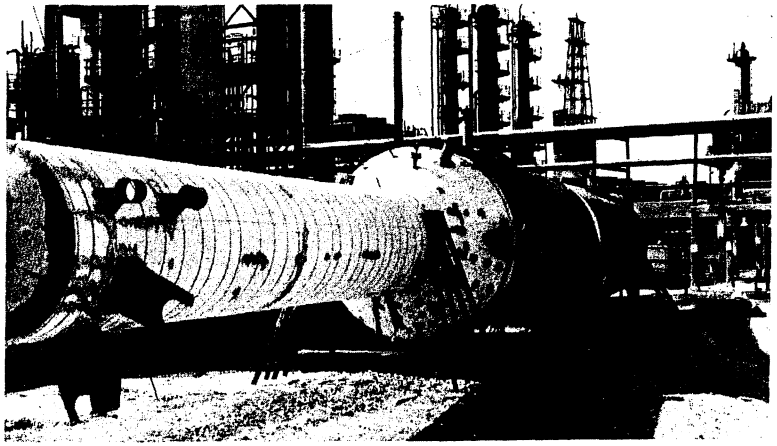
For Koch Refining Company
Corpus Christi, Texas

Koch Refining Company needed a naphtha desulfurizer for their refinery in Corpus Christi, Texas. Ventech supplied a surplus unit and relocated it from Louisiana. Surplus equipment resulted in a capital savings of 30% less than new unit cost. The project required only eight months — five months less than new unit construction.



Ventech upgraded the unit for greater capacity, better efficiency and higher operating pressure to desulfurize a mixture of straight run and coker naphtha. Our turnkey approach started with the feasibility study and finished with the erected plant. Today the unit is processing over 16,000 BPSD.





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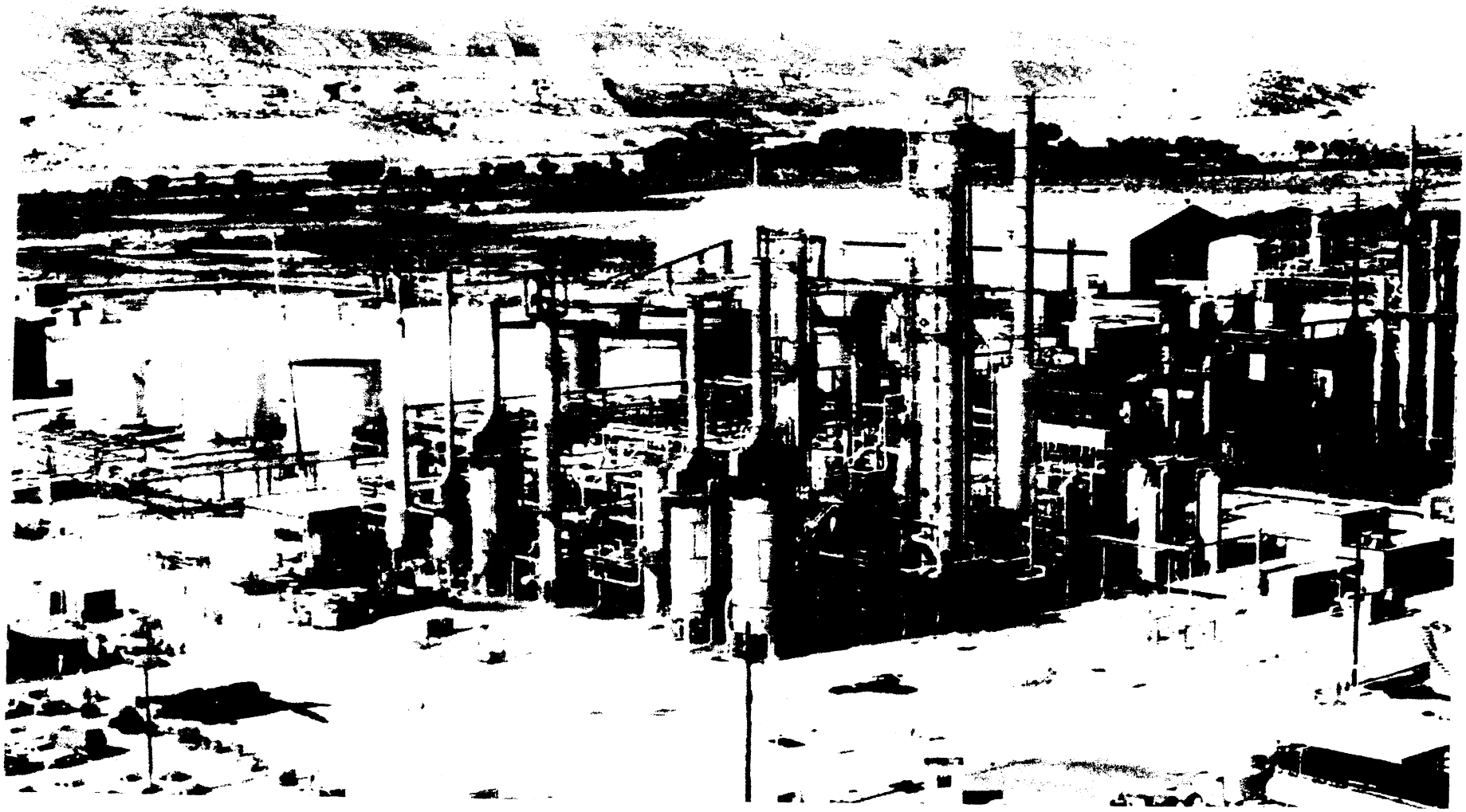
TLX 77-4273

Gary_Complex_small.jpg (JPEG Image, 1692x1354 pixels) - Scaled (70%)

http://www.ventech-eng.com/Gary_Complex_small.jpg



Hydrocracker Complex

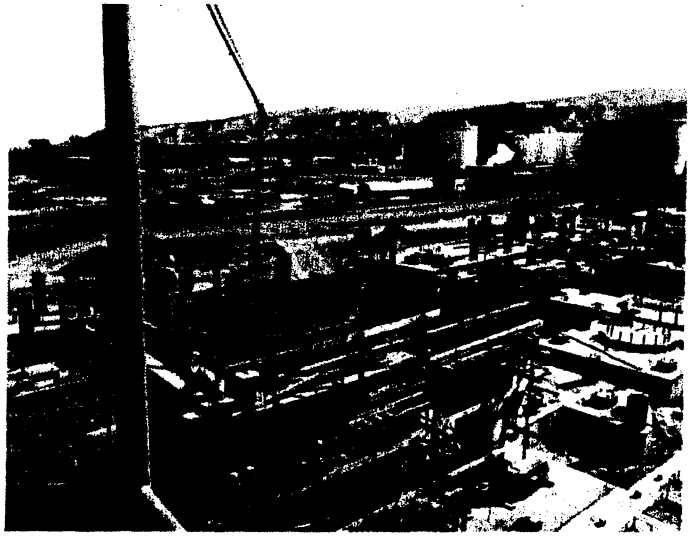
A Relocation Project of
THE VENTECH COMPANIES

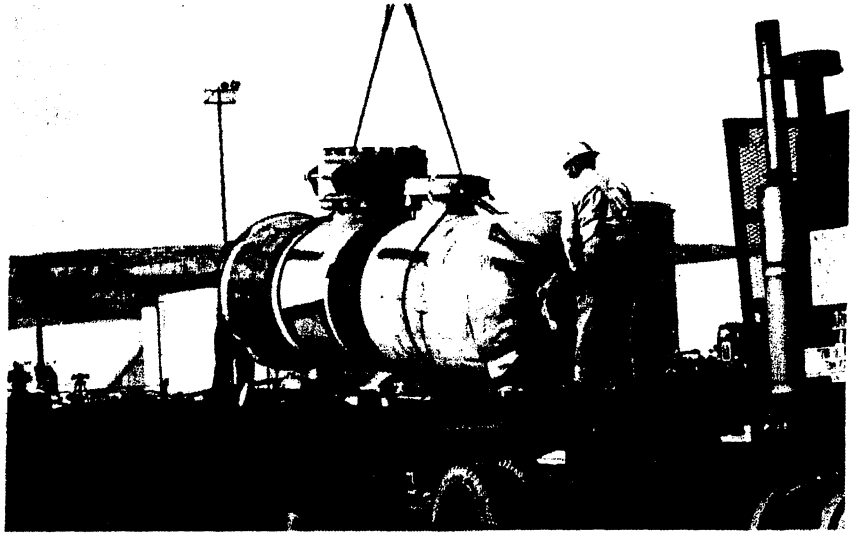
For Gary Refining Company
Fruita, Colorado

Gary Refining asked Ventech to build a refinery in Fruita, Colorado to produce jet fuel and JP4 from feedstock derived from Shale Oil. Ventech delivered it for about 70% of normal new unit cost and had it ready for operation in 13 months.

To accomplish this project, Ventech relocated two existing hydrocrackers with a common fractionating section from Louisiana and modified them for one new service using Union Oil Hydrocracking technology. Ventech also supplied an existing Hydrogen Plant from Puerto Rico, an Amine Unit from Texas and remanufactured valves and instrumentation from our shops.

Ventech's engineering and construction capabilities provided the project management and relocation expertise to get the job done. Start-up was uneventful and current operation better than expected.





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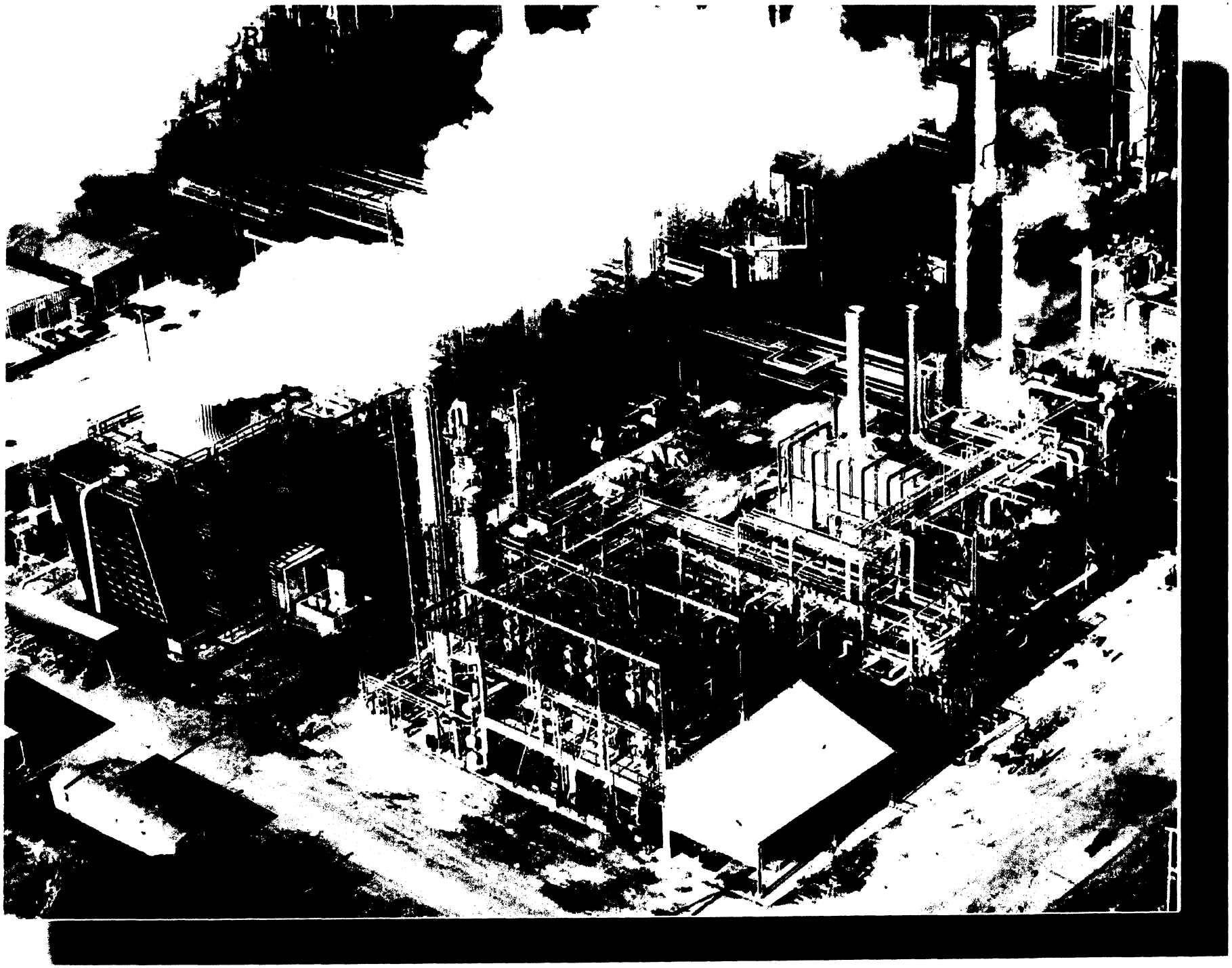
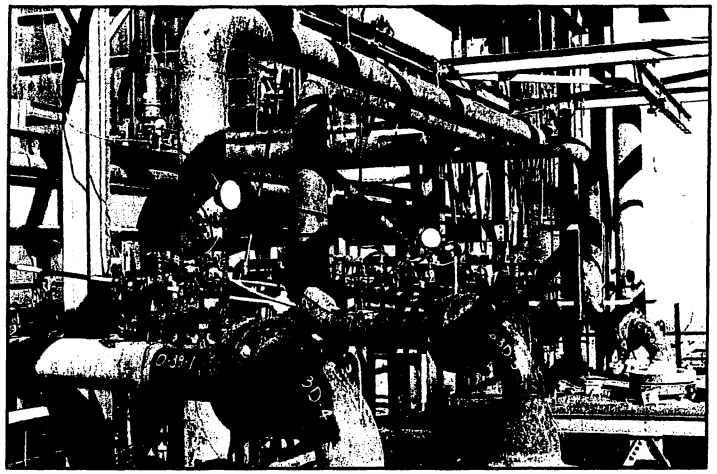


Hydrodesulfurization And Reformer Unit

A Relocation Project of
VENTECH ENGINEERS, INC.

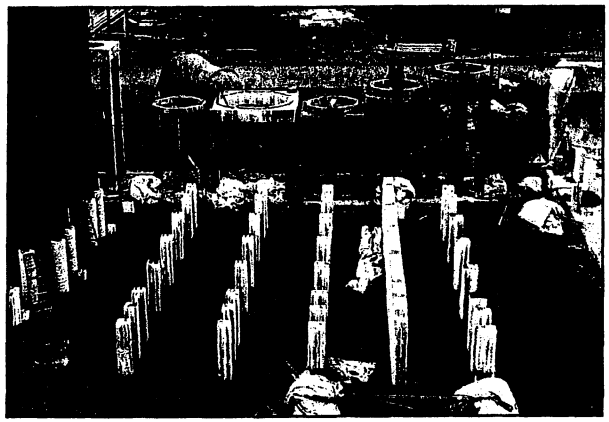
For Ashland Petroleum Corporation
St. Paul Park, Minnesota

Ashland Petroleum Corporation had a 10,000 BPSD HDS-Reformer Unit at their shut down refinery in Buffalo, New York that they wanted relocated to their St. Paul Park, Minnesota refinery. New soil conditions and a change in plot plan required extensive re-engineering. The schedule of the project dictated that field work proceed despite the severe weather conditions in Minnesota. Ventech broke ground in January, 1986 and the units were operating in December, 1986.

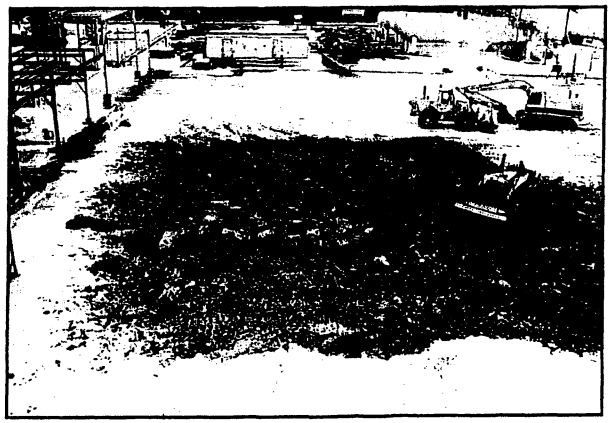


NOVEMBER 1985
The existing unit at Buffalo was dismantled and transported to rebuilding shops and the new site for re-erection.

**The picture on the other side is in December, 1986 with the plant mechanically complete and operating.*



MARCH, 1986
Spring finds most of the concrete is in place and equipment setting is proceeding.



JANUARY 1986
While the unit is being dismantled and re-engineering is being performed, the ground is broken for installation of all foundations. (-17° temp. was common)

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The Ventech Companies

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Ventech Engineers Int'l Corp.

Ventech Process Equipment, Inc.

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Map

Legal Notice

Refinery Process Units

Complete Process Units

Crude Units

- 17,000 b/d Crude Distillation Unit —> **SOLD**
- 35,000 b/d #1 Crude/Vacuum Distillation Unit —> **SOLD**
- 42,000 b/d #2 Crude Distillation Unit/Sour Water Stripper —> **SOLD**
- 42,000 b/d Crude Unit —> **SOLD**
- 50,000 b/d Crude Unit —> **SOLD**

Hydrotreaters

Naphtha

- 4,500 b/d Naphtha Hydrotreater Unit —> **SOLD**
- 9,000 b/d Naphtha Hydrotreater/Platformer & 16,000 b/d Naphtha Splitter Unit —> **SOLD**
- 14,000 b/d Naphtha Hydrotreater —> **SOLD**

Kerosene

- 2,600 b/d Kerosene Hydrotreater Unit —> **SOLD**

Diesel

- 6,800 b/d Distillate Desulfurizing Unit —> **SOLD**
- 16,000 b/d Distillate Desulfurizing Unit —> **SOLD**

Reformers

- 3,600 b/d Catalytic Reformer Unit —> **SOLD**
- 4,000 b/d Naphtha Hydrotreater/Reformer
- 9,000 b/d Naphtha Hydrotreater/Platformer & 16,000 b/d Naphtha Splitter Unit —> **SOLD**
- 14,000 b/d Catalytic Reformer Unit —> **SOLD**

Catalytic Crackers

- 12,000 b/d Fluid Catalytic Cracker & Gas Recovery Unit —> **SOLD**
- 13,000 b/d Fluid Catalytic Cracker Unit —> **SOLD**
- 14,000 b/d Fluid Catalytic Cracker Unit —> **SOLD**

Sulfur Recovery

- 40 t/d Sulfur Recovery Plant ---> **SOLD**
- 43 t/d Sulfur Plant ---> **SOLD**

Product Treaters

LSRN

- 10,000 b/d LSR Merox ---> **SOLD**

Jet/Kero

- 5,500 b/d Jet/Kero Merox ---> **SOLD**
- 6,000 b/d Jet/Kero Merox ---> **SOLD**
- 7,500 b/d Jet/Kero Merox ---> **SOLD**

LPG

- 2,200 b/d LPG Treating Plant ---> **SOLD**
- 3,600 b/d LPG Treating Plant ---> **SOLD**

Vacuum Unit

- 16,500 b/d Vacuum Distillation Unit ---> **SOLD**
- 21,000 b/d Vacuum Distillation Unit ---> **SOLD**
- 26,100 b/d Vacuum Distillation Unit ---> **SOLD**

Miscellaneous Units

Alkylation Unit

- 4,000 b/d Alkylation Unit ---> **SOLD**

Hydrogen Production Unit

- 265 MMSCFD

Inert Gas Generators

- Inert Gas Generators (2)

Isom Unit

- 7,500 b/d Isom Unit ---> **SOLD**

LPG Stabilization

Naphtha Splitter

- 14,000 b/d Naphtha Splitter ---> **SOLD**
- 16,000 b/d Naphtha Splitter Unit ---> **SOLD**

Propane/Propylene Splitter

- 1,500 b/d Propane/Propylene Splitter —> **SOLD**

SWS

- 166 gpm Sour Water Stripper —> **SOLD**

Visbreaker

For more information contact the Sales Dept. at (713) 477-0201 ext. 1609 or e-mail robert@ventech-eng.com.

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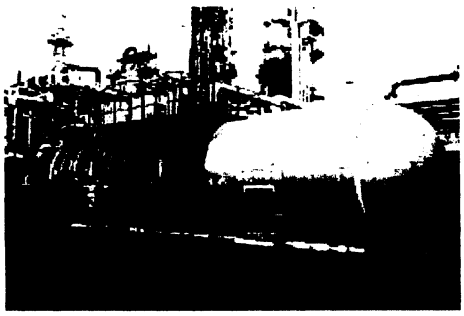
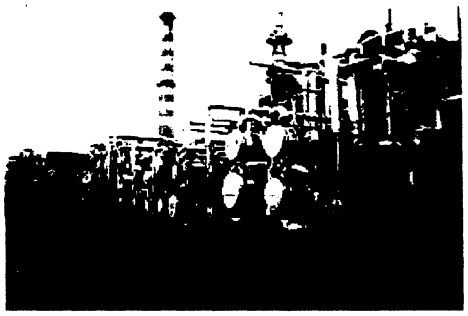
Crude Distillation Unit #1
Vacuum Distillation Unit

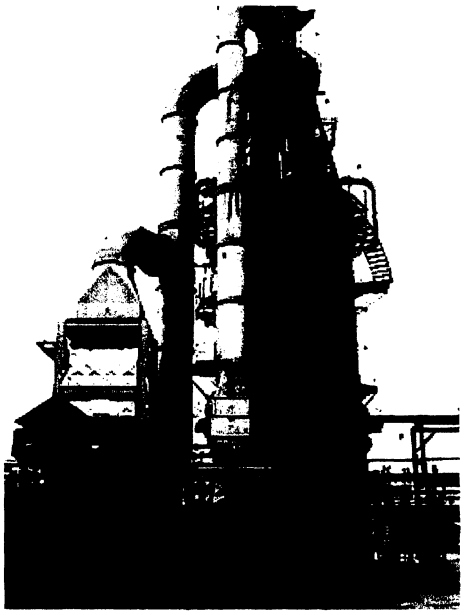
SOLD

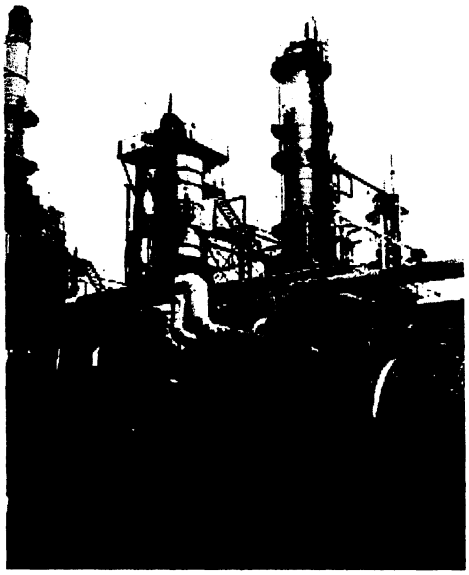
The CDU-1 and VDU were originally designed and constructed in 1954 by Foster Wheeler as a heat integrated unit. The unit was commissioned with a rated capacity of 14,000 bpsd. Over the next twelve (12) years the unit was de-bottlenecked to its current design capacity of 35,000 bpsd. This unit also includes a kerosene rerun tower.

The desalter, rated at 50,000 b/d, was installed in 1973 and the crude charge heater was replaced in 1981. The vacuum charge heater was replaced and the vacuum tower was completely rebuilt in 1988.









Click here for process description

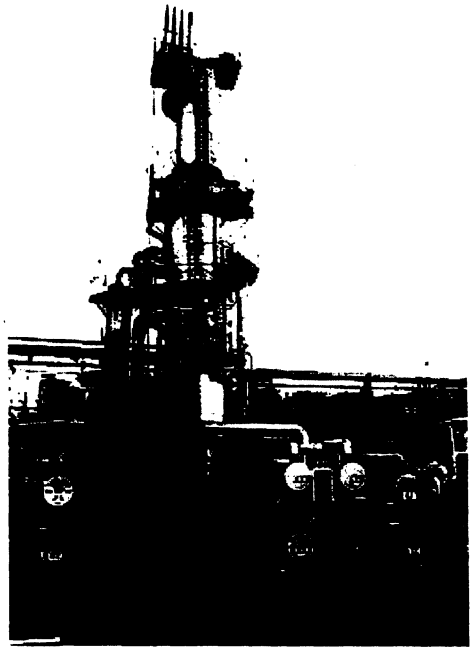
Process Flow Diagram (PDF)

Ventech Process Equipment, Inc.

Crude Distillation Unit #2

SOLD

The CDU-2 was designed and built in 1967 in conjunction with the NHT/Platformer units. CDU-2 is designed to process 42,000 bpsd. The desalter, rated at 50,000 b/d was installed in 1972 to enable the unit to process lower quality crudes. The crude charge heater was replaced in 1991 with a larger heater, which improved distillate capacity of the unit by 4000 b/d. A preflash tower was added to the unit in 1998, which increased the overall distillate capacity of the unit to 27,000 b/d.



The Ventech Companies

Ventech Engineers, Inc.

Ventech Engineers Int'l Corp.

Ventech Process Equipment, Inc.

Ventech Appraisal Services, Inc.

1149 Ellsworth
P.O. 4261
Pasadena, Texas 77502
(713) 477-0201 phone
(713) 477-2420 fax

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The Ventech Companies

Ventech Engineers, Inc.

Ventech Engineers Int'l Corp.

Ventech Process Equipment, Inc.

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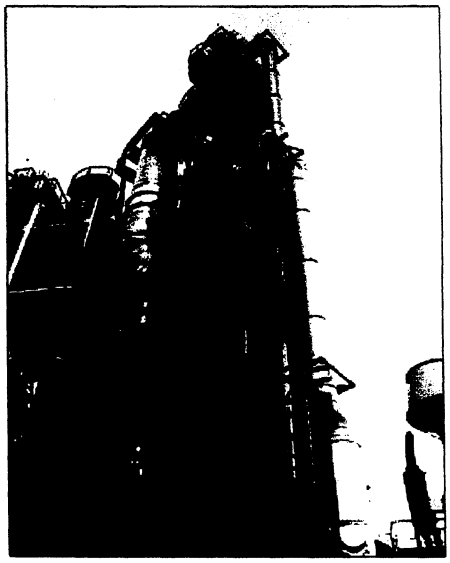
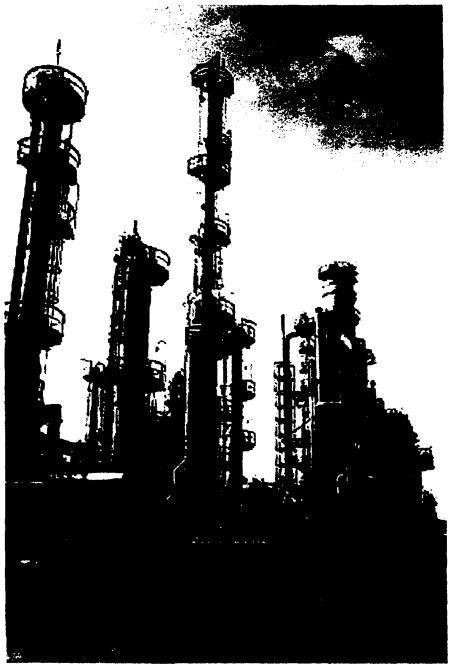
SOLD
#1 Fluid Catalytic Cracking Unit

& Gas Recovery Plant





The #1 Fluid Catalytic Cracking Unit (#1 FCCU), Unit 12, is a UOP stack type configuration unit, and over the years it has been upgraded with the addition of more modern technological designs such as reactor and regenerator internals, riser injection nozzles, etc.

The predominant equipment age is from the initial 1958 installation and the subsequent 1964 revamp. The unit was revamped again in 1995 to allow for processing small percentages of high quality residues with predominant VGO feedstocks. A new riser termination device was added in 2002 as part of low sulfur gasoline modifications. In addition, the main fractionator column, overheads drum, overheads condensers and liquid product pumps were replaced. In the gas recovery plant the Absorber/Deethanizer column was replaced, and other modifications included new Debutanizer tower internals, multiple pump upgrades and an addition of a new heavy cat naphtha recycle system.

The unit has a single motor driven 3600 HP main air blower, installed in 1958. The gas recovery plant wet gas compressors are two original 450 HP two-stage reciprocating machines, which have been supplemented with a newer 900 HP two stage reciprocating machine during a later revamp. The unit capacity is 14,000 BPSD of fresh VGO feedstocks.

The #1 Gas Recovery Plant (#1 GRP), Unit 13, associated with #1 FCCU's designed to process both saturated and unsaturated feeds. The #1 GRP receives feeds from the #1 FCCU, #1 CDU and #1 CRU.

Click here for process description

Process Flow Diagrams:

#1 FCCU Process Flow Diagram

#1 GRP Process Flow Diagram

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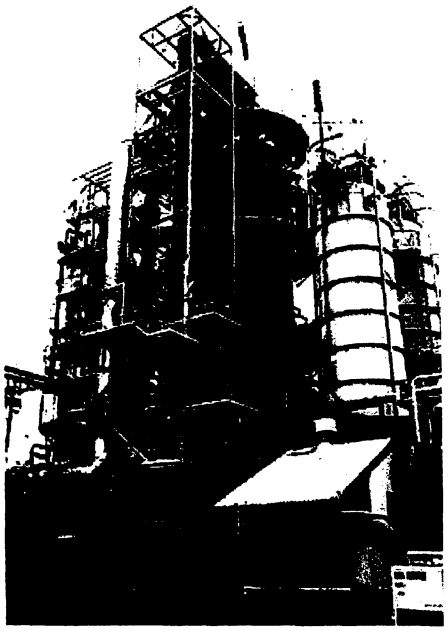
Fluid Catalytic Cracking Unit (FCCU) & Gas Recovery Plant (GRP)

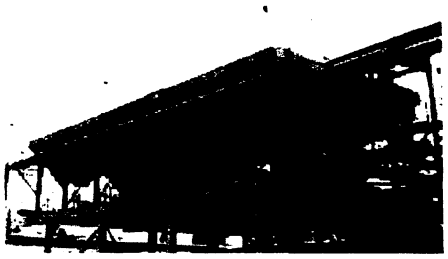
SOLD

The FCCU/GRP complex was originally built in 1954 as an Esso Model IV side-by-side unit. Numerous upgrades and revamps have been performed on this system throughout its operational life. The final capacity of this unit was 12,000 b/d on fresh feed upon closure of the refinery.

Upgrade of the FCCU to current riser technology is prevented by the configuration of the reactor/regenerator and the u-tube design and associated catalyst flow. The reactor was significantly modified in 1993 and currently utilizes single stage cyclones. A CO Boiler was added to the unit in 1973. An automatic catalyst addition system was installed in 2001 for overall yield improvements to the unit. A new stabilizer and Minalk treating unit were installed in the unit in 1994.

The main air blower is a steam turbine driven Demag compressor. The unit has four (4) gas engine driven reciprocating wet gas compressors.





Click here for process description

Process Flow Diagram (PDF)

Equipment List

Ventech Process Equipment, Inc.

Home | Contact Us | Consignment | Equipment | Process Units | Español | English

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Distillate Hydrotreater Unit (DDU)

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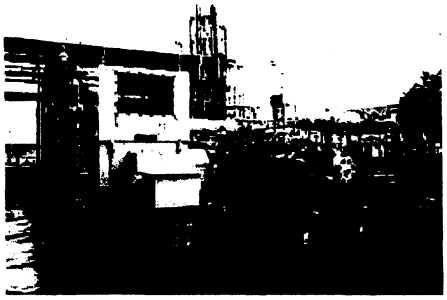
The DDU was designed and constructed in 1973 utilizing UOP's Hydrobon technology. The unit has a capacity of 16,000 b/d and has run as high as 18,000 b/d upon occasion processing mainly straight run distillates as well as a portion of the light cracked gas oil. The unit is designed to process 1.0 wt% sulfur feed into 0.1 wt% sulfur diesel product.

The DDU reactor is 102" diameter by 17'-6" T/T, 765 psig @ 800 F, A204C with 405SS cladding. There are two (2) 60% motor driven reciprocating make-up/recycle gas compressors each rated at 500 hp with a discharge pressure of 784 psig.

Click here for process description

Process Flow Diagram (PDF)

Equipment List



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Naphtha Hydrotreater / Platformer Unit & Naphtha Splitter Unit

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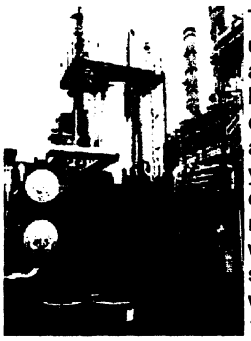
The Naphtha Hydrotreater and Platformer units were originally designed and constructed in 1967 as an integrated system and had a final capacity of 9,000 b/d. The UOP licensed Platformer unit is a three (3) reactor semi regen design.



The Naphtha Splitter unit was designed and constructed in late 2002 and operated approximately one year prior to the closure of the refinery. The unit was constructed as a standalone system with a capacity of 16,000 b/d. It is located adjacent to the Naphtha Hydrotreater / Platformer unit.

The Naphtha Hydrotreater reactor is 84" diameter by 16'-3" T/T, 440 psig @ 750 F and is constructed of SA387C with 347SS cladding. The recycle compressor for this unit is a steam turbine driven centrifugal Demag compressor. The compressor is rated for 1877 hp and has a capacity of 57 MMscfd of hydrogen at a discharge pressure of 490 psig.

Click here for process description

Process Flow Diagrams:

Naphtha Hydrotreater & Naphtha Splitter Unit Process Flow Diagram (PDF)

Platformer Process Flow Diagram (PDF)

Equipment Lists:

Naphtha Hydrotreater & Naphtha Splitter Unit Equipment List

Platformer Equipment List

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ISO-REF Unit

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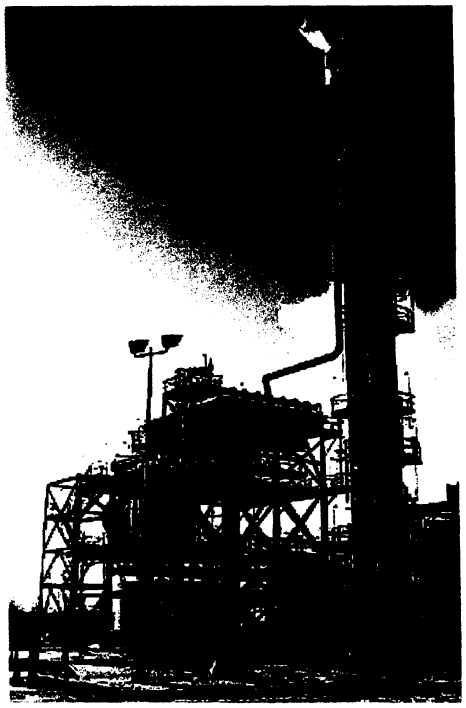
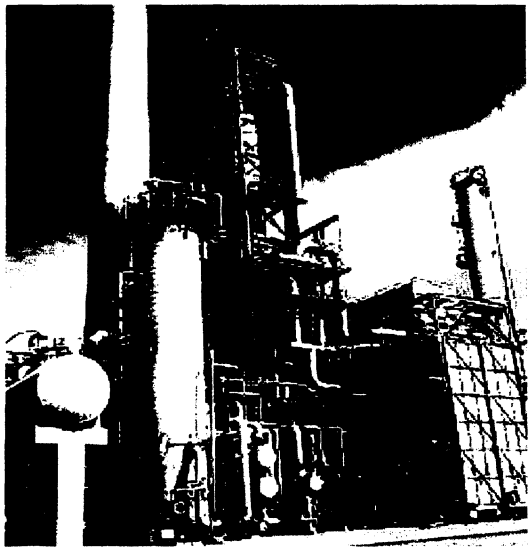
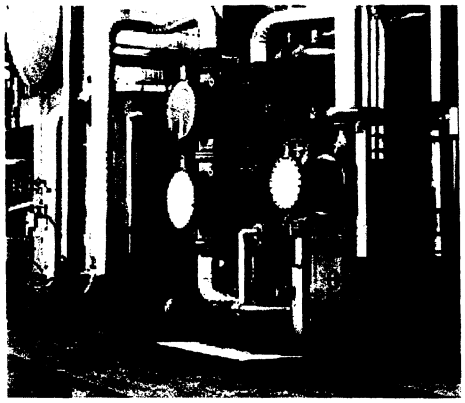
In 1999, a new Naphtha Splitter and C5/C6 Isomerization Unit were integrated with the existing #2 Naphtha Hydrotreater Unit (NHU) and Catalytic Reformer Unit (CRU) to form the current ISO-REF unit.

The light and heavy straight run naphthas (LSRN/HSRN) from the #1 & #2 CDU's are combined into the #2 NHU feed. The #2 NHU is designed to process up to 14,000 BPSD of full range naphtha. The hydrotreated naphtha is then split with the LSRN providing feed to the ISOM unit and the HSRN providing feed to the CRU.

The isomerate and reformate products from these process are recombined and sent to storage for gasoline blending.







Renane Olson

OFFICE OF THE ASSESSOR
COUNTY OF LOS ANGELES
320 Kenneth Hahn Hall of Administration
Los Angeles, California 90012-2770
(213) 974-3101
assessor.lacounty.gov

RICK AUERBACH
ASSESSOR

RECEIVED
BOARD OF EQUALIZATION
BOARD OF ACCOUNTS DIVISION
07 JUL 30 AM 9:17

July 30, 2007

Honorable Betty T. Yee
Chairwoman, State Board of Equalization
450 "N" Street, MIC: 71
Sacramento, CA 95814

Dear Chairwoman Yee:

PROPOSED RULE 474

I would like, once again, to voice my strong support for proposed Rule 474 regarding the appraisal unit when measuring declines in value in the assessment of oil refineries.

It is consistent with Revenue and Taxation Code Section 51(d) which states: "...'real property' means that appraisal unit that persons in the marketplace commonly buy and sell as a unit, or that is normally valued separately." It is also consistent with Rule 324(b), in the context of assessment appeals that states that "an appraisal unit of property is a collection of assets that functions together, and that persons in the marketplace commonly buy and sell as a single unit or that is normally valued in the marketplace separately from other property, or that is specifically designated as such by law."

I also believe that Rule 474 is in harmony with the Board's adoption of Rules 468 (Oil and Gas Producing Properties), 469 (Mining Properties) and 473 (Geothermal Properties). While these three are extractive industries, they also bear similarities to refineries in that they are:

1) Land and fixture intensive, with no or minimal structural improvements. This describes a refinery, but not a cannery or manufacturing plant.

2) Immovable, fixed in place, such as a refinery which cannot easily be moved because of its extensive underground pipeline network. These pipelines carry the crude oil into the refinery (e.g.: in Los Angeles County, from the harbor area or Central California) and they carry the

finished products to their distribution terminals where it is then loaded into tanker trucks. There are also refinery-to-refinery pipelines. Furthermore, the equipment in a refinery is specific for that general location (e.g.: distillation columns are custom built for its ambient air temperature and its specific soil conditions). In addition, they typically have drilled water wells for a relatively inexpensive source of water. This would distinguish a refinery from virtually every other industry. In short, the fixtures are so functionally and physically integrated with the land that they should be considered part of the appraisal unit. As no buyer and seller would separately negotiate a price for a parcel of land and the house which sits on it, no buyer and seller would separately negotiate a price for the refinery fixtures and a separate price for the land on which it sits, meeting the definition of R&T 51(d).

3) Not easily convertible to another use. An abandoned refinery typically cannot be converted to another use, given the prohibitively high cost of demolishing the fixtures (and their extensive underground concrete supports) and cleaning up the contaminated land. This would not be the case with a typical manufacturing plant or an amusement park. Most other properties have fixtures which can be removed, e.g.: a tire manufacturing plant can become a shopping mall.

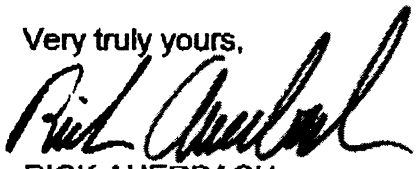
4) Impossible or difficult to duplicate. You cannot create another oil or geothermal property. In the same way, no new refinery has been built in the United States in the last 30 years. Despite the narrow gap in California between supply and demand, as noted by the severe price distortions that take place whenever a single refinery experiences a significant problem or does extensive maintenance, no one has made plans to build another one in this state.

In short, just as no one would buy the land in an oil producing, mining or geothermal property separately from the fixtures which are necessary to operate it, no one who would buy a refinery for only its land or only its fixtures. This is in marked contrast to the vast majority of other types of commercial-industrial fixtures that are sold separately from the land and structures, are normally valued separately and hence, do constitute a separate appraisal unit for property tax assessment purposes.

It should also be emphasized that for those refineries that do not share the above characteristics with Revenue and Taxation Code Section 51(d) or all of the aforementioned rules, the rebuttable presumption portion of Rule 474 is applicable.

For the reasons noted above, I strongly urge your Board to approve resubmitting proposed Rule 474 to the Office of Administrative Law with the revised initial statement of reasons.

Very truly yours,



RICK AUERBACH

RA:f

c: Honorable John Chiang, State Controller
Members, State Board of Equalization
Diane Olson, BOE Regulations Coordinator

Contra Costa County

Contra Costa County

Office of Assessor

2530 Arnold Drive, Suite 400
Martinez, California 94553-4359
FAX: (925) 313-7660
Telephone: (925) 313-7500

Gus S. Kramer
Assessor

Lori Koch
Assistant Assessor
Administration

Walter Busenius
Assistant Assessor
Valuation

July 30, 2007

The Honorable Betty Yee
State Board of Equalization
450 Capitol Mall, Ste. 2340
Sacramento, CA 95814

Re: Support for Rule 474 Re-Adoption – Petroleum Refining Properties

Dear Board Member :

On August 14, 2007, the State Board of Equalization will hold a public hearing to again complete the rulemaking process for proposed Rule 474 – Petroleum Refining Properties. Consistent with the principle of fair and uniform taxation based on fair market values, Rule 474 correctly establishes the presumption that there is a single appraisal unit when determining a refinery's taxable value. As the Assessor of Contra Costa County, I respectfully recommend the Board's re-adoption of Rule 474 in its current form.

The enclosed memorandum explains the appropriateness and legality of Rule 474. This memorandum was prepared by Dennis Graves, a retired Deputy County Counsel for Contra Costa County and a legal consultant to the Assessor's Office on matters pertaining to refinery assessment, who has considerable legal expertise in the area of refinery appraisal and assessment.

Please feel free to contact me at 925-313-7501 if further discussion or information would be helpful relative to the adoption of this rule.

I look forward to attending the August 14, 2007, meeting to re-adopt Rule 474, and I strongly encourage the Board to finalize re-adoption of this fair, equitable and important rule.

Sincerely,

GUS S. KRAMER
Assessor

Enclosure

Dennis C. Graves

Dennis C. Graves
Attorney at Law
1552R Green Street
San Francisco CA 94123
(415) 931-6855
d_graves@pacbell.net
September 1, 2006

The Honorable Gus Kramer
Assessor of Contra Costa County
2530 Arnold Drive, Suite 400
Martinez CA 94553

Re: SBE Rule 461(e) is contrary to the California Constitution and Revenue and Taxation Code when applied to oil refineries; proposed Rule 474 would correct the problem

Dear Mr. Kramer:

State Board of Equalization (SBE) Rule 461(e) provides that fixtures and other machinery and equipment classified as improvements are to be an appraisal unit separate from land and improvements when determining whether property is entitled to taxation at a declined or "Proposition 8" value for a tax year. You have asked for my opinion on the validity of Rule 461(e) as applied to oil refineries and as to the appropriateness of proposed Rule 474, which would except refineries from the Rule 461(e) requirement of two separate appraisal units. After providing some basic background on California property taxation, this memorandum explains that Rule 461(e) is contrary to California law in its application to refineries, because it would not allow a proper appraisal unit consisting of property that actually could be offered for sale in an open market non-exigency transaction and for which a fair market value properly could be determined as required by the California Constitution and Revenue and Taxation Code. The memorandum closes by explaining that proposed Rule 474 would correct the problem.

I. The California Constitution Requires That All Real Property Be Taxed At Its *Fair Market Value* Determined Upon Change of Ownership or New Construction and Annually Adjusted For Inflation (the Proposition 13 Factored Base Year Value) or Its *Fair Market Value* Determined For the Annual Lien Date, If Lower Than the Factored Base Year Value (the Proposition 8 Declined Value)

The California Constitution establishes two basic rules for taxing all non-exempt real property in this State, both of which are founded on the bedrock concept of California property taxation: fair and uniform taxation based on fair market values. All taxable real property must be taxed either at 1) its "base year value" (BYV) determined

under Proposition 13 as the *fair market value* (FMV) upon a change of ownership or new construction, and thereafter annually adjusted or "factored" for inflation (Art. XIIIA, Secs. 1(a), 2(a),(b)) (hereafter a "Proposition 13 value" or "factored base year value") or 2) its *fair market value* determined on the annual lien date (January 1), if the FMV is lower on that date (Art. XIIIA, Sec. 2(b)) (hereafter a "Proposition 8 value" or "declined" value). Notwithstanding the later adoption of Article XIIIA (Proposition 13), the basic Article XIII, Section 1, Constitutional command to tax property based on *fair market values* still survives, requiring the establishment of *fair market values* both when determining a new Proposition 13 value and a declined Proposition 8 value. (*State Board of Equalization v Board of Supervisors of San Diego County* (1980) 105 CA 3d 813, 820-3.) Neither the Legislature, the State Board of Equalization (SBE), nor any assessor or local body can deviate from this fair market value standard without running afoul of the California Constitution. (See *Bauer-Schweitzer Malting v San Francisco* (1973) 8 C3d 942, 946; *ExCello Corp v Alameda* (1973) 32 CA3d 135,140; *Lucas v County of Monterey* (1977) 65 CA3d 947, 954-6; *Nunes Turfgrass v Kern County* (1980) 111 CA3d 855, 862-3, 871; *Forster Shipbuilding v Los Angeles County* (1960) 54 C2d 450, 456-7; *Sea Train Terminals v Alameda County* (1978) 83 CA3rd 69, 81; *State Board of Equalization v Board of Supervisors of San Diego County, supra,* 105 CA 3d 813, 820-3.)[1]

Because the Constitution requires a *fair market valuation* when determining if a property is entitled to taxation at a declined Proposition 8 value for the tax year, the appraisal unit for such a valuation necessarily must consist of property which actually could be sold apart from other property in an open market non-exigency sale and for which a fair market value actually could be determined under the open market non-exigency sale standard specified in the Revenue and Taxation Code Section 110(a) definition of fair market value. As will be seen, when applied to oil refineries Rule 461(e) cannot be squared with this basic Constitutional requirement and Revenue and Taxation Code Section 110(a) because the Rule would result in appraisal units which could not be sold apart from other property in an open market non-exigency sale and for which proper fair market values could not be determined.

II. The FMV Required By the Constitution Can Only Be Determined For a Unit of Property That Could Be Sold Apart From Other Property In An Open Market Non-exigency Transaction

Regardless of whether determining a new Proposition 13 value or a declined Proposition 8 value, California Revenue and Taxation Code Section 110(a) has long established the foundational definition that the fair market values required by the Constitution for California property taxation purposes must reflect the prices that could be obtained in open market, non-exigency sales. Several basic principles of fair market value emerge from this definition and accepted appraisal principles.

---

[1] In a rising property value market, the Proposition 13 value established at FMV on the date of change of ownership or completion of new construction, and annually thereafter factored, typically will be lower than the FMV of the property on a subsequent lien date. Since property is taxed at the lower of its factored BYV or lien date FMV, much property thus is annually taxed at less than its FMV. Notwithstanding, FMV remains the Constitutional standard that applies both for a Proposition 8 taxable value determination and when a new Proposition 13 value is established. (R+TC Secs. 110(a), 110.1(a), 51(a),(d).)

First, the fair market value is to be that established by the highest bid accepted from the market of potential purchasers, rather than the value to the existing owner. (See *Pacific Mutual Life Insurance Company v Orange County* (1985) 187 CA3d 1141, 1148.)

Second, fair market value must reflect the price obtainable for property if exposed for sale in the open market rather than sold in a limited offering environment where there is not sufficient opportunity for competing bids to establish a market value. (SBE Rule 2(a); *Guild Wineries & Distilleries v. County of Fresno* (1975) 51 CA3d 182,186-8.)

Third, fair market value must reflect the price obtainable when property is not subject to some exigency where one party could take advantage of the other. (SBE Rule 2(a); The Appraisal of Real Estate, 11th Ed., The Appraisal Institute, pp. 22-24; The Valuation of Real Estate, 3rd Ed., Ring + Boykin, pp. 10-12.)

Fourth, a very fundamental concept is that the property for which fair market value is established under these principles must consist of a definable unit of property – called an "appraisal unit" – that rationally can be identified, valued and offered for sale. When something is sold in an open market non-exigency transaction, the seller and buyer have to agree on what is to be sold, and the property thus agreed upon is the unit for which the highest acceptable bid establishes fair market value. In order to determine a fair market value, the property inherently must be able to be 1) legally separated from other property and 2) valued separately from other property. If the property in question is not a unit of property that might be valued and offered for sale by a rational seller and purchased by a rational purchaser in an open market non-exigency transaction, no fair market value could be determined for the property.[2]

While some might argue that one could theoretically value and offer *any* portion of any property for sale, that argument is spurious in the context of determining fair market values for California property taxation. Property would never be sold in an open market non-exigency sale and a proper fair market value could not be established if 1) it is impractical to separate out the portion to be sold, 2) people would not buy such a specified portion, 3) such a specified portion would have no utility, 4) separating out the portion offered for sale would result in a significant remainder portion having only scrap value, or 5) such a portion could not be meaningfully valued for sale. Some examples will illustrate.

Example 1:

---

[2] Although property interests that are less than a fee ownership interest are transferred (eg, co-tenant interests), the basic requirements remain for any interest for which FMV is to be established: the interest must be able to be legally separated from other property (eg, the interest of another co-tenant) and separately valued for sale. Like entire fee interests, such partial interests also must be a unit of property that would be valued and offered for sale by a rational seller and purchased by a rational purchaser in an open market non-exigency transaction. Without meeting such criteria, no fair market value could be determined for such interests. Since full fee interests normally are assessed for property tax purposes, assessors seldom are concerned with such partial interests. (See SBE Rule 2(a).)

Assume the following. Seller S offers a used car in good operating condition for sale for $10,000. Buyer B only needs a replacement engine and offers to purchase the engine for $500. If S were to remove the engine and sell it for $500, the balance of the car would have a scrap value of $1000. No rational seller would accept B's offer. Indeed, if any seller would sell an engine separate from the car, the only reason would be that the condition of the car is so bad that it had only scrap value. Were that the case, there would not be an open market non-exigency sale of an operating car, but rather an exigency sale of scrap parts of a non-operating car. Of course, replacement tires or even engines are sold, but they are not be sold off of cars in sound operating condition. Upon sale of a car, all parts of the car (engine, transmission, wheels, brakes, chassis, body, etc.) that work together as an operating unit must be sold as a single unit if the sale is to be an open market non-exigency sale. If a car were taken apart and the engine, wheels, etc. were sold individually, the total brought by all parts would reflect scrap value. Upon such a sale of the parts, the total sum received would doubtless be far less than the FMV of the operating car.

Example 2:

Assume the following. Seller S is a retailer who leases a building in order to conduct his business. S has purchased and installed the counters and display cases necessary in his business. When the lease expires, the lessee decides to move to another location which already has the necessary counters and display cases. There is a market for such counters, and S sells the counters and display cases to another retailer that needs such items. The building owner then leases the premises to another tenant that brings in its own counters. In this example, the counters are trade fixtures which were separable from the building and the land on which the building sits. Such counters are a proper sale unit because they can be valued and sold separate from the land and building in an open market non-exigency sale that can establish FMV.

Example 3:

Assume the following. Seller S owns an oil refinery, consisting of land, buildings and tanks, and the massive cracking towers and other items of heavy machinery and equipment, linked together by the pipes that transfer product from one unit to another during the refining process. The cracking towers and other items of machinery and equipment are affixed to the real estate both by their great weight and being bolted to massive concrete foundations. While any given unit can be replaced, replacement is a significant construction project requiring heavy capacity cranes and special equipment for cutting the units apart so they can be removed. Such a project may require a large workforce and, if the unit being replaced is an essential component of a manufacturing process (often the case), the entire process line typically would be shut down during the project. The replacement unit then would be built at the same site, using the same cranes, welders, etc. Indeed, it usually is easier and less costly to replace a storage building or office building than to replace a major processing unit.

The owner of the refinery can sell it for one billion dollars in an open market, non-exigency sale. The buyers of such a refinery are only willing to offer that price if they can recover their investment and make a profit, and the only way they can do so is to continue to make gasoline from crude oil, using the same machinery, equipment, buildings, tanks and land as the current owner. The potential buyers are not interested in buying a single cracking tower, or the tanks that store crude oil, or the land, or any

other portion separate from the entire refinery.[3] All parts of the plant must operate together to produce the finished product that is to be sold, and the potential buyers are basing their bids on the present value of the income that can be generated over a holding period by producing and selling gasoline using all parts of the plant operating together.

The only proper appraisal unit for an open market non-exigency sale for this real life example of a refinery would be the entire refinery, including land, buildings, tanks, and all machinery and equipment necessary to producing gasoline. If the land, buildings and tanks were to be offered for sale separately from the machinery and equipment, no one would buy them for more than scrap value. If the machinery and equipment were offered for sale without the land, buildings and tanks, which are integral parts of the unit of property necessary to produce gasoline, no one would buy the machinery and equipment for more than scrap value. Requiring a refinery to be broken into the aforenoted two separate appraisal units, as SBE Rule 461(e) purports to require, would be akin to requiring the engine to be a separate appraisal unit from the remainder of the car in example one, above. Unlike the counters in example two, above, which are the type of fixtures that Rule 461(e) contemplates, the machinery and equipment of a refinery would not be sold in real world open market non-exigency transactions separate from the remainder of the refinery property. Much like the scrap value sale of the separate car parts in example one, separate sales of refinery machinery and equipment would result in a total price for all property that would be far less than if the refinery were sold as a single operating unit (assuming that machinery and equipment even could be separated out from the remainder of the refinery). Moreover, as next discussed, an attempt to value machinery and equipment separately from land and improvements could only result in arbitrary values that fail to satisfy the FMV requirements of California law.

III. An Entire Refinery Must Be the Proper Appraisal Unit Because a Proper Fair Market Value Can Only Be Established For Such an Appraisal Unit

We have seen that the California Constitution requires taxation at the FMV determined for a unit of property that logically can be separated from other property and sold in an open market non-exigency sale.

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[3] While there have been unusual situations where parts of a refinery have been sold, or even where an entire refinery has been sold as scrap, those sales are by definition exigency sales where the plant usually is being shut down for a major renovation, or even permanently. Such sales do not represent the fair value of a viable functioning refinery sold in an open market non-exigency sale. If a refinery is a viable operating unit that effectively produces marketable products, as is the case with virtually all plants that have been adequately maintained and improved over time, the highest and best use of the plant is as an integrated operating refinery, and it would be sold as such if the sale is an open market non-exigency sale. This example and this memorandum are not concerned with exigency or scrap sales of outmoded plants. The issues addressed herein concern a viable plant, which could be sold in an open market non-exigency sale, and for which a fair market value could be determined for the highest and best use of a viable operating refinery. In the case of a viable operating refinery, the entire refinery is invariably sold as a single operating unit consisting of the land, buildings, tanks, machinery and equipment necessary to producing gasoline and other finished products.

There are three valuation approaches generally used when valuing property for California property taxation purposes: the sales, cost and income approaches. (See SBE Rules 1-10.) In the real world open market non-exigency transactions that determine FMV, the income approach is used to value refineries. Only rarely do the cost and sales approaches have any validity in such valuations.[4] When valuing refineries, potential purchasers of a refinery calculate the present value of each year's projected net income over (typically) a 10 year holding period, and the sum of those 10 year present values plus a residual value at the end of the holding period is the amount the potential purchaser is willing to bid.

As illustrated in example three of Section II, above, all components of a refinery property, including the land, improvements (buildings and tanks), machinery and equipment (the cracking towers, piping, etc.) must operate together to produce the net income that is discounted to determine value. Each component of the total refinery is essential to producing income, and the income upon which refinery value is based could not be produced without all components of the refinery operating together. No part of the income from the products produced by a refinery can meaningfully be attributed to any component of the refinery. For example, one could not say that the land and improvements generated X amount of income and the machinery and equipment Y amount of income. But to value two separate refinery appraisal units, as Rule 461(e) purports to require, would necessitate attributing a portion of the total net income to each part, which would be inherently arbitrary and thus result in arbitrary values for each appraisal unit. Because only the income approach is used in refinery valuations for real world open market non-exigency transactions and because that approach must value the income from *all* parts of the refinery operating together as a single unit, it would be impossible to determine meaningful values for the two separate appraisal units that Rule 461(e) purports to require. Arbitrarily assigning income to two separate appraisal units would result in arbitrary values that would fail the fundamental requirement of *fair market valuations for valid appraisal units*. The law should not be interpreted to require such a meaningless result as would obtain if the Assessor attempted to follow Rule 461(e) and value a refinery as two separate appraisal units. (See *Wasatch Property Management v Syriah Degrate* (2005) 35 C4th 1111, 1122.)

IV. Revenue and Taxation Code Section 51(d) Must Be Interpreted In a Manner That Results In the Comparison of FBYV and FMV For a Unit of Property For Which a *Fair Market Value* Could Be Determined In a Real World Open Market Non-exigency Sale

Revenue and Taxation Code Section 51(d), part of the implementing legislation for Article XIIIA (Proposition 13), provides that when determining taxable value the

[4] Only in the rarest cases are the cost and sales approaches given any weight at all in California refinery transactions, and even then the value is determined almost entirely on the basis of the income approach. Potential purchasers simply do not care about the cost of building a refinery because in most of California that option is not feasible (eg, due to environmental and permitting constraints and the uncertainty of the time required to build). Further, the sales approach has little validity because there rarely are open market non-exigency sales that are even reasonably comparable, and it rarely is feasible to make adjustments (eg, for location and variances in processing capability) to attain sufficient comparability to make the sales approach meaningful.

assessor is to compare the FBYV and lien date FMV of a proper *appraisal unit,* reflecting what:

> "...persons in the marketplace commonly buy and sell as a unit, ***or*** that is normally valued separately". (R+TC Sec. 51(d), in pertinent part, emphasis added.)

It is the inartful use of the disjunctive "or" that has caused some confusion on this issue. Contrary to Rule 461(e), the proper interpretation of Section 51(d) for refineries is that the disjunctive is not intended to allow a separate valuation of refinery machinery and equipment when determining if a Proposition 8 declined value is appropriate on a lien date. Refinery machinery and equipment would not sell apart from the land and improvements in an open market non-exigency sale and, as already explained, a *fair market value* could not be determined for either appraisal unit if an owner attempted a sale of such separate units.

Rule 324(b) is one of the SBE Rules that implements Revenue and Taxation Code Section 51(d). Rule 324(b) provides that:

> "An appraisal unit of property is a collection of assets that functions together, and that persons in the marketplace commonly buy and sell as a single unit *or* that is normally valued *in the marketplace* separately from other property..." (Rule 324(b), in pertinent part, emphasis added.)

Like Revenue and Taxation Code Section 51(d), Rule 324(b) uses the disjunctive "or". However, the addition of the emphasized words "in the marketplace" helps explain that, consistent with the Constitutional requirement of fair market values, both the Code Section and Rule intend that a proper appraisal unit consists of property that actually could be valued at FMV and sold apart from other property in a non-exigency sale *in the marketplace*. As explained above, a refinery, including land, buildings, tanks, machinery and equipment, is a collection of assets that functions together as a single unit to produce the income stream that is discounted to determine FMV. As also explained, such a property is always valued and sold as a single integrated operating unit in any sale that is an open market non-exigency sale. While the two appraisal units that Rule 461(e) purports to require could not transfer and be valued apart from other property in a non-exigency sale in the marketplace, the entire refinery property could. Thus, the entire refinery must be deemed a single appraisal unit within the meaning of Revenue and Taxation Code Section 51(d) and Rule 324(b).

Rule 324(b) was interpreted in *Exxon Mobil Corporation v County of Santa Barbara* (2001) 92 CA 4th 1347, where Exxon challenged a base year value established upon completion of new construction, as well as the taxable values for the three succeeding years. The property in question included two components: an off-shore oil production field and an on-shore processing facility. Although appearing to be two separate properties, the two components were connected by pipeline, and the on-shore facility was necessary to separate salt water from the crude oil produced from the off-shore field. The Assessor contended the off-shore and on-shore properties should be assessed as separate appraisal units, using the cost approach. Exxon asserted that both on-shore and off-shore components had to be valued as a single integrated appraisal unit valued under the income approach. The Court held for Exxon, emphasizing the Rule 324(b) concept that both on-shore and off-shore components

functioned together to produce the de-watered oil sold to obtain the income which determined the value of both components in the marketplace. The Court agreed that both components would be sold together and had to be valued as the single economic unit that would sell in the marketplace. (*Exxon Mobil Corp. v County of Santa Barbara*, *supra*, 92 CA 4th 1347, 1353-5.) If two such separate properties, connected only by a long pipeline, are a single appraisal unit because they operate together to pump and clean the crude oil upon which the value of the total property depends, certainly all parts of a refinery, closely connected by a myriad of piping, must be a single appraisal unit since all parts necessarily operate together to make the gasoline sold to produce the income upon which the value of a refinery is based.

When drafting Revenue and Taxation Code Section 51(d), the Committee that drafted the implementing legislation likely was thinking of common trade fixtures, like the counters in example two, above, that in fact are often valued and sold separately from the underlying land and improvements. In that hectic period in the wake of Proposition 13, it is highly unlikely that the Committee even contemplated the unusual fixtures central to the functioning of a refinery. Since such refinery fixtures are not valued and sold separately from the land and improvements in the open market non-exigency transactions that determine FMV, it is extremely doubtful that the Committee contemplated a separate valuation or appraisal unit for such property.

If a statute can be interpreted two ways, one which accords with a superior constitutional provision and one which is inconsistent with the constitutional provision, the constitutional interpretation must be chosen. (See *Espinosa v Superior Court* (1975) 50 CA 3d 347, 352-3.) Interpreting R+TC 51(d) to allow separation of refinery machinery and equipment from the remainder of the refinery would violate the fundamental Constitutional requirement that a proper appraisal unit consists of property that actually could be offered for sale in open market non-exigency transactions and for which a true *fair market value* could be determined. As to oil refineries, Section 51(d) must be interpreted to mean the entire refinery, including land, buildings, tanks, machinery and equipment is to be a single appraisal unit.

V. In Its Application To Oil Refineries, SBE Rule 461(e) Is Contrary to the Constitution and Revenue and Taxation Code Because Fair Market Values Could Not Be Determined For Either Appraisal Unit That the Rule Purports To Require

Fundamentally, Rule 461(e) is unconstitutional in its application to refineries because it would not allow the determination of the fair market values required by the Constitution and Revenue and Taxation Code for either appraisal unit the Rule purports to require. As explained in the Section I, above, the California Constitution and Revenue and Taxation Code require that property be valued either 1) at its *fair market value* determined at the time of change of ownership or completion of new construction, and thereafter factored annually for inflation, or 2) at its *fair market value* on an annual lien date. (See Art. XIII, Sec. 1, Art. XIIIA, Secs. 1(a), 2(a),(b); R+TC Secs. 110(a), 110.1(a), 51(a).) As explained in Section II, above, the FMV required by the Constitution must be determinable for a unit of property that could be valued and sold in an open market non-exigency transaction apart from other property. As also explained above, in the case of oil refineries that unit of property must be the entire refinery, including land, buildings, tanks, machinery and equipment. As further explained in Section III, above, a real FMV simply could not be determined for either of the appraisal units Rule 461(e) purports to

require because the income approach is used to value refineries, and it would be impossible to meaningfully allocate income between two appraisal units so as to determine fair market values for each unit. Indeed, any sale of less than all components of a refinery would occur only as an exigency scrap value sale, and the total value for the components of such a sale would be far below the fair market value of the refinery as a whole. Accordingly, Rule 461(e) is contrary to the basic FMV mandate of the California Constitution and Revenue and Taxation Code.

In its application to refineries, SBE Rule 461(e) also is inconsistent with a proper interpretation of Revenue and Taxation Code Section 51(d), which the Rule is supposed to implement. Providing that fixtures and other machinery and equipment classified as improvements are to be an appraisal unit separate from land and improvements, Rule 461(e) is based on the assumption that the fixtures and other machinery and equipment to which it applies in fact are valued and sold separately from land and improvements. (See SBE Issue Paper 06-001, page 3, first and second paragraphs). But we have seen that, as to refineries, this assumption just is not true for transactions that are the open market non-exigency transactions contemplated by Revenue and Taxation Code 110(a). Although Rule 461(e) may be workable for other properties, it is not workable for refineries because refineries invariably are valued and sold in real world open market non-exigency transactions only as a single unit with all parts working together to produce the income discounted to determine value under the income approach. As explained in Section IV, above, if the language of Revenue and Taxation Code Section 51(d) is properly interpreted to define an appraisal unit as property commonly sold together and for which a FMV could be established in a non-exigency transaction in the marketplace, it becomes apparent that Rule 461(e) is inconsistent with Section 51(d) when applied to refineries.

In sum, when applied to refineries, Rule 461(e) would not allow the fair market value required by the Constitution and Revenue and Taxation Code and, as such, is contrary to both the Constitution and Revenue and Taxation Code in its application to refineries.

VI. Proposed Rule 474 Corrects the Improper Results That Would Occur If Rule 461(e) Were Applied to Refineries

Rule 461(e) *generally* may be consistent with Revenue and Taxation Code Section 51(d) and the Constitution.[5] But, as applied to oil refineries, we have seen that

[5] There is a wide spectrum of industrial property that has machinery and equipment affixed to the real estate. While much machinery and equipment of other industries may be readily removable and may not be functionally integrated with the real estate, the machinery and equipment of oil refineries are both functionally and physically integrated with the land, buildings and tanks and extremely difficult and expensive to remove or replace. (See the description in Example 3 of Section II, above.) Indeed, oil refineries may be the most extreme example of machinery and equipment clearly classifiable as real estate (see R+T C Secs. 104(c), 105(a)) and functionally integrated with other real estate. Unlike much other industrial plant and equipment, refinery machinery and equipment are not valued and sold apart from other property of the plant (except in exigency transactions such as scrap sales of a defunct plant). Further, refineries may be the sole type of California industrial property valued only under the income approach and for which separate values could not be determined for the different appraisal units Rule 461(e) purports to require. Although this memorandum only addresses the applicability of Rule 461(e) to oil

the Rule 461(e) requirement of two separate appraisal units is contrary to the California Constitution and Revenue and Taxation Code because refinery land and improvements are not sold separately from machinery and fixtures in open market non-exigency sales and fair market values could not be determined for such separate appraisal units.

Regardless of the propriety of the separate appraisal units *generally* required by Rule 461(e) for other property, proposed Rule 474 addresses the *specific* case of refineries, establishing a presumption that there is to be a single appraisal unit when determining taxable value, which includes land, buildings, tanks, machinery and equipment. The specific refinery rule of proposed Rule 474 thus would correct the problem that would occur were the general rule of Rule 461(e) to be applied to refineries. (See *People v Cockburn* (2003) 109 CA4th 1151, 1158.)

VII. Conclusion

The Rule 461(e) requirement of two separate appraisal units fails the Constitutional test in the case of refineries because refinery land and improvements are not sold separately from machinery and equipment in open market non-exigency sales, and fair market values could not be determined for such separate appraisal units. Proposed Rule 474, however, provides for a single appraisal unit consisting of all parts of the refinery (land, buildings, tanks, machinery and equipment) which operate together to produce the income that is the basis for refinery fair market valuations. Rule 474 is needed to correct the problem created when Rule 461(e) is applied to refineries.

Yours truly,

Dennis C. Graves
Attorney at Law

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refineries, it would appear that the conclusion that Rule 461(e) is contrary to law likely would be limited to its application to oil refineries.

WSPA

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July 27, 2007

Ms. Diane Olson
Regulations Coordinator
P. O. Box 942879
450 N Street, MIC:80
Sacramento, CA 94279-0080

Re: Proposed Property Tax Rule 474, *Petroleum Refining Properties*
WSPA's Comments on Revised Initial Statement of Reasons
Hearing Date: August 14, 2007

Dear Ms. Olson:

The Western States Petroleum Association ("WSPA") submits the following comments on the Revised Initial Statement of Reasons ("Revised ISR" or "ISR") for Proposed Property Tax Rule 474 issued by the State Board of Equalization ("Board") on July 16/17, 2007.[1] WSPA representatives will also be present to testify at the Board hearing on Rule 474 scheduled for August 14, 2007.

1. There Is No Need for Rule 474 Because It Does Not Implement a Statute, Case or Law.

The Revised ISR fails to demonstrate why adoption of Rule 474 is necessary in order to implement or interpret a specific statute, court decision or other provision of law. (*Govt. Code*, sec. 11349.1(a)(1).) Although the ISR refers to the California Constitution and the Revenue & Taxation Code, it does not state that Rule 474 specifically implements those legal provisions. At most, the ISR states that Rule 474 is needed because Property Tax Rule 461(e) allegedly does not apply to refineries. However, an asserted inconsistency with another regulation is not a basis for adopting Rule 474, particularly when Rule 461(e), and the statutory provisions cited in the ISR, have been in existence for many years.[2] There is no necessity for Rule 474 because there is no predicate statute, case or law for Rule 474 to implement or interpret.

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[1] WSPA has previously submitted letters to the Board regarding Proposed Rule 474. Those letters, copies of which are enclosed for the Board's convenience, were submitted to the Board on July 15, 2005, October 10, 2005, November 9, 2005, September 21, 2006 (multiple letters), and September 26, 2006 (Rodi-Pollock). The discussions in these prior letters are incorporated in this letter by reference. In particular, WSPA directs the Board's attention to its letters dated September 21, 2006 which specifically address the issues raised in the Revised ISR.

[2] To address this concern, the better approach would be for the Board to amend Rule 461(e), as suggested in the discussion of alternative courses of action later in this letter.

P.O. Box 21108, Santa Barbara, California 93121
(805) 966-7113 • Fax: (805) 963-0647 • Cell: (805) 252-6778 • bob@wspa.org • www.wspa.org

2. The ISR Provides No Facts to Show Why Adoption of Rule 474 Is Necessary.

The Office of Administrative Law ("OAL") June 8, 2007 Disapproval of Proposed Rule 474 specifically stated on page 2 that the explanation or reasons for adoption of a regulation must be supported by "facts, studies, and expert opinion" (citing Government Code section 11349.1(a)(1)). The Revised ISR makes no reference to any facts, studies or expert opinion that would support adoption of Proposed Rule 474. Although the ISR repeatedly states that refinery land, improvements and fixtures/equipment are "commonly" bought and sold as a unit, no specific evidence supporting that assertion is provided. The ISR does not discuss specific information relating to any refinery transactions. Nor does the ISR provide any evidence for the assertion that the large percentage of fixtures in refineries ("up to 80 percent of their values") is a valid basis for distinguishing refineries from other heavily-fixturized properties such as amusement and theme parks, power plants, breweries, auto assembly plants, television sound stages, and food processing facilities.[3] Moreover, the ISR simply ignores evidence previously provided by WSPA that refinery fixtures and equipment are commonly sold separately from refinery land and improvements for relocation (see further discussion below).

Supporting facts, studies, and expert opinion is also required where the reasons for a regulation are based on policies, conclusions, speculation or conjecture, as is the case with the Revised ISR. The Revised ISR opines that Rule 474 should be enacted in order to prevent refinery properties from be assessed at values that differ from "fair market value." No evidence is given, however, to show that any refinery has, in fact, been assessed at a value other than fair market value. Once again, and under the circumstances in this matter, the Revised ISR fails to provide substantial evidence, *i.e.*, supporting facts, studies, expert opinion, or other information, that is required in order to demonstrate the "necessity" for a proposed regulation.[4]

3. The ISR Ignores the "Normally Valued Separately" Clause in Section 51(d).

The Revised ISR completely fails to address the "normally valued separately" clause in Section 51(d), the statutory provision that implemented Propositions 13 and 8. In so doing, the ISR ignores the two primary reasons for treating fixtures separately from land and improvements for "decline-in-value" assessment purposes. First, fixtures *depreciate* in value. Consequently,

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[3] The Revised ISR states that, in the marketplace, refineries are "unlike the usual case for most other types of property" (ISR, p. 5, 2nd ¶). The ISR provides no evidence to distinguish refineries from the major entertainment and manufacturing properties listed here.

[4] *California Code of Regs.*, tit. 1, sect. 10, subd. (b); *In re Board of Forestry & Fire Protection*, OAL File No. 01-1016-02 S (December 7, 2001), p. 6 [Initial statement of reasons fails to meet substantial evidence element of "Necessity" standard where factual information, studies and reports are not included in rulemaking file].

the assessment of fixtures for "decline-in-value" purposes requires consideration of physical deterioration and obsolescence which cause the value of fixtures to decline. Such is not the case with land, and one of the reasons why fixtures are to be valued separately from land. The foregoing is clearly shown by David Doerr's August 24, 2006 letter attached hereto and discussed below. Second, fixtures are treated separately because of the administrative difficulties that would result from assessing and auditing them as part of a single appraisal unit, particularly for manufacturing facilities. This concern was clearly indicated by Los Angeles County Assessor Alexander Pope in a December 1978 letter to David Doerr (treating fixtures with land "administratively unworkable") and by Contra Costa County Assessor Carl Rush in a January 1979 letter to Janice Masterson at the Board (valuing fixtures with land "an impossible requirement" and "unadministrable"). Both of these letters (as well as the attached letter from David Doerr) recognize and memorialize the pre-Proposition 13/Proposition 8 practice of assessing and auditing fixtures as a separate appraisal unit. Copies of the letters from Assessors Pope and Rush are attached.[5]

4. Refinery Fixtures Do Not "Commonly" Sell as a Unit with Land and Improvements.

The Revised ISR's contention that refinery fixtures and equipment "commonly" sell as an "economic unit" with land and improvements (even assuming this is the correct criteria) is simply untrue.[6] In fact, refinery equipment frequently sells *separately* from land and improvements. Through consultations with market participants such as The Ventech Companies and other research, WSPA has determined that refinery process units consisting of many items of machinery and equipment ("M&E") are frequently sold and relocated (see letter from Cris K.

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[5] It is noteworthy that almost all of the major refineries in California are located in Los Angeles County and Contra Costa County.

[6] The Revised ISR repeatedly and erroneously equates "economic unit" with "appraisal unit" even though these terms have different meanings. While an economic unit is what sells in the marketplace, an economic unit is *not always* the same as an appraisal unit. Section 51(d) establishes that fixtures are to be treated as a separate *appraisal unit*. Section 51(d) does not state that, because refinery fixtures may be sold as part of a "single economic unit" (ISR, p. 5, 2nd ¶), they are also necessarily assessed along with land and improvements as a single appraisal unit.

Proposed Rule 474(d)(3)(B) conflicts with the provisions of Section 51(d) on this particular point by stating that the presumption in the Rule may be overcome with evidence that a refinery's fixtures are not operated as an economic unit along with the land. This test, which wrongly equates "economic unit" with "appraisal unit," could never be satisfied and blatantly disregards the statutory criteria in Section 51(d) for segregating land and fixture assessment where fixtures "normally valued separately."

O'Neall of Cahill, Davis & O'Neall, LLP filed with the Board and dated July 23, 2007). This evidence substantially undermines the ISR's assertion that refinery "land, improvements, and fixtures, and other machinery and equipment classified as improvements are commonly bought, sold and valued as a single [economic] unit in the marketplace" (ISR, p. 5 (2nd ¶), pp. 5-6).

5. <u>The Contention that Rule 461(e) Should Not Apply to Refineries Is Misleading</u>.

One of the primary themes of the Revised ISR is that applying of Property Tax Rule 461(e) to refineries will produce non-market value assessments in violation of the Constitutional requirement to assess properties at fair market value. This assertion is misleading. It fails to comprehend the genesis of Rule 461(e), namely *Revenue and Taxation Code* section 51, which implemented California Propositions 13 and 8. This was explained in the August 24, 2006 letter submitted to the Board by David R. Doerr, Chair of the Task Force on Property Administration which drafted the statutory language implementing Propositions 13 and 8, including Section 51. Mr. Doerr's letter explains that Section 51 and its progeny, Rule 461(e), were both adopted in order to implement the provisions of Propositions 13 and 8 in California's Constitution. Consequently, the contention in the Revised ISR that Rule 461(e) as applied to refineries "is inconsistent with the constitutional requirement of fair market valuation" under Article XIII, section 1 (ISR, p. 5, 3rd ¶) is both misleading and incorrect.

In fact, the true but unacknowledged purpose for Proposed Rule 474 is to undermine Proposition 13 and Proposition 8 protections for refineries by allowing increases in land value at a refinery to offset decreases in value attributable to depreciating fixtures.

6. <u>Property Tax Rules for Extractive/Mineral Properties Are Inapplicable to Refineries</u>.

Refineries are large manufacturing properties that employ fixtures as part of a manufacturing process. Refineries are distinguishable from extractive/mineral properties, which also employ fixtures, because extractive/mineral properties require fixtures in order to exploit the property mineral rights relating to depleting natural resources <u>*at a specific location*</u>. Property Tax Rules 468, 469 and 473 (cited by the ISR as exceptions that justify treating refineries differently) include fixtures within the appraisal unit for extractive/mineral properties for this reason. Such reason does not exist, however, for refineries, the fixtures of which are not used to exploit depleting natural resources and are indistinguishable from other manufacturing properties, such as those listed in Section 2 above. Consequently, Rules 468, 469 and 473 are not precedents that support the adoption of Rule 474.[7]

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[7] In addition, Rules 468, 469 and 473 are comprehensive rules that address all aspects of valuation for oil and gas, mining and geothermal properties. Proposed Rule 474 is not comprehensive, but only pertains to a single aspect of refinery valuation and assessment. This is a significant weakness in Rule 474.

7. The Revised ISR Does Not Eliminate Previously Identified Problems with Rule 474.

WSPA's September 21, 2006 letter to the Board on Proposed Rule 474 identified numerous problems with the Rule, including the following:

a) There is no legal or factual predicate that makes adoption of Rule 474 necessary at this time;

b) Rule 474 contradicts Section 51(d), the statutory provision that the Rule ostensibly effectuates, by establishing a valuation presumption that is inconsistent with the presumption implicit in Section 51(d);

c) The Rule contains unfamiliar and undefined terms in violation of the "Clarity" standard for new regulations, and the Rule is unclear in the light of existing regulations;

d) The provisions of Rule 474 duplicate provisions in existing regulations (Property Tax Rules);

e) Rule 474 discriminates against petroleum refineries by establishing a separate class of taxpayers without any reasonable distinction or rational basis, thereby violating Constitutional equal protection standards;

f) Use of Rule 474 will produce a statewide lack of uniformity in the assessment of and assessed values for industrial and manufacturing properties; and

g) Rule 474 will impose "new taxes" on petroleum refiners, in violation of Article XIIIA, section 3, of the California Constitution, by changing the method by which taxes on petroleum refineries are to be determined.

The Revised ISR does not address or adequately respond to the problems cited above, and each of the grounds listed above is a valid basis for rejection of Proposed Rule 474.

Conclusion.

WSPA opposes Proposed Rule 474 and urges the Board to reject the Rule because its adoption will erode the Proposition 13 and Proposition 8 protections that refinery properties are entitled to receive. There is no evidence establishing a need for Rule 474, and the Revised ISR and Rule contradicts Section 51(d) and the Constitutional provisions implemented by Section 51(d), as well as the Board's long-standing position that fixtures are to be treated as a separate

appraisal unit. Finally, although it is several pages in length and contains more discussion than the original ISR, the Revised ISR still fails to give any solid reasons as to "why" Rule 474 is needed, or provide any evidence that makes adoption of the Rule necessary.

Instead of adopting this the Rule, WSPA would encourage the Board to consider a more comprehensive approach to refinery assessment and valuation issues by developing and adopting an Assessors' Handbook for refinery properties. Alternatively, WSPA would urge the Board to amend Rule 461(e) along the lines suggested by the California Taxpayers' Association in its September 26, 2006 letter to the Board on Rule 474 (copy attached).

Respectfully submitted,

WESTERN STATES PETROLEUM ASSOCIATION

By: Robert W. Poole

Bob Poole
Senior Coordinator
Coastal and Property Tax Issues

Attachments and Enclosures

cc: Honorable Betty Yee, Member, First District (w/Attachments and Enclosures)
Honorable Bill Leonard, Member, Second District (w/Attachments and Enclosures)
Honorable Michelle Steel, Member, Third District (w/Attachments and Enclosures)
Honorable Judy Chu, Member, Fourth District (w/Attachments and Enclosures)
Honorable John Chiang, State Controller, c/o Marcy Jo Mandel,
Deputy State Controller (w/Attachments and Enclosures)

z:/

August 24, 2006

Ms. Diane Olson
Regulations Coordinator
P.O. Box 942879
450 N Street, MIC: 80
Sacramento, CA 94279-0080

Re: Proposal to Adopt Rule 474, Petroleum Refining Properties

At the June meeting of the board's Property Tax Committee, I was both amused and frustrated with comments made by all parties on Proposed Rule 474, relative to legislative intent of Revenue and Taxation Code Section 51, added in 1979. No one who spoke at the meeting was there when this section was being developed and enacted. I was there.

Therefore, I am writing as the Chair of the Tax Force on Property Tax Administration of 1978-79 to try and set the record straight. At that time, I was also Chief Consultant to the Assembly Revenue and Taxation Committee, working directly for the committee chair, Assembly Member Willie Brown, Jr. Mr. Brown was the author of AB 1488 of 1979, which enacted Section 51 into law. I worked on this legislation, provided testimony in legislative committees and discussed amendments with all interested parties. I also prepared a report in October 1979 entitled "Property Tax Assessment" which Mr. Brown approved and was published by the committee. This report describes in detail the new post-Proposition 13 assessment system and the intent of the various bills enacted in 1979 relating to the new assessment system.

The Task Force first met on October 12, 1978 to develop a work plan. On October 26, the Task Force began discussions on how the decline-in-value provisions should be drafted. In subsequent weeks, the language continued to be refined. However, the provisions relating to fixtures were not discussed until December 18.

One of the problems in determining how declines in values were to be assessed was the constitutional provision (Article XIII, Section 13) requiring land and improvements to be separately assessed. The Task Force decided to ignore the constitutional provision and determine declines in value based on the appraisal unit commonly sold in the market place. The key to this provision is the word "market place." To have a "market place," there has to be a number of willing buyers and sellers.

The issue of the treatment of fixtures arose in a December 12 letter to me from Bob Morris, a Task Force member who was an attorney and a member of the State Bar's Committee on Property Taxation. He wrote:

"There is one issue I have not dealt with – the question of the 'unit' of property assessed. There is a hidden issue which the Task Force has not considered, namely, the terrific strain on real property/personal property classification which

would result if decline in the value of fixtures were to be offset by appreciation in land and improvements while 'personal property' of the same nature were recognized (as it would be), without offset.

"Assessors are not equipped to make fine distinctions between 'fixtures' and 'personal property' for every property every year. It would vastly increase their work load if they were forced to make the actual appraisals necessary to do so.

"I personally believe that any property which is valued separately, or by a separate method of valuation, than the remainder of the property assessed (and both things are true of fixtures versus land and buildings) is the only logical and definable property 'unit.' In any case, these considerations should be explored, discussed and voted on at the December 18th meeting."

The Task Force agreed with Mr. Morris and added the language "... or which are normally valued separately," to the proposed Section 51 recommended by the Task Force.

The intent of this language is also made clear in the October committee report on the new assessment provisions. On page 16, the report states:

"Fixtures, however, are normally appraised separately, thus owners may claim a decline based on depreciation of the fixture without regard to the value of the surrounding land or improvements."

There has been no evidence introduced that fixtures were not separate appraisal units prior to the passage of Proposition 13.

It should be noted that the Legislature did not buy, in its entirely, the Task Force's recommendation for Section 51. However, the provisions of Section 51(d) are verbatim from the Task Force recommendation.

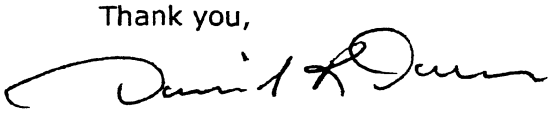
As mentioned earlier, there was concern about ignoring the constitutional provisions requiring separate assessment of land and improvements. Also, it seemed unfair and illogical that if an improvement were removed, by a disaster or by voluntary action, the assessment would stay the same because of an increase in land value. After discussions by me with Mr. Brown, and key staff and members, Mr. Brown gave me the green light to modify the Task Force recommendation on declines in value. In addition to provisions relating to separate appraisal units for fixtures, separate appraisal units were added for land and improvements under certain situations. When the Task Force recommendations were added to AB 156 (Brown) on February 22, 1979, as author's amendments, they contained subsection (c) (which is now subsection (b)) of Section 51 that required separate assessments of land and improvements in certain situations. Currently Section 51(b) requires a separate decline-in-value appraisal for land and for improvements in either of the following: (1) The property is damaged or destroyed by a disaster and the county does not have a Section 170 ordinance, or (2) All or part of the property has been voluntarily removed by the taxpayer.

This also illustrates that the Legislature was concerned about netting all real property into the appraisal unit.

Further evidence about the Legislature's view of fixtures can be seen by the treatment of fixtures on the supplemental roll. When the bill creating the supplemental roll was passed in 1983 (SB 813, Hart), it exempted fixtures. Thus all supplemental roll assessments have an appraisal unit excluding fixtures. After some court challenges, the First District Court of Appeal (in *Shafer v. State Board of Equalization*, 1985, 174 Cal. App. 3d 423) upheld the Legislature's exclusion of fixtures on the supplemental roll.

For the reasons outlined in this letter, I believe the provisions of proposed Rule 474 is inconsistent with the recommendation of the Task Force on Property Tax Administration and legislation authored by Assemblyman Brown that placed Section 51 in the Revenue and Taxation Code.

Thank you,



David R. Doerr
Chair, Task Force on Property Tax Administration
4549 Belcrest Way
Sacramento, CA 95821

cc: The Honorable Board Member John Chiang
The Honorable Board Member Bill Leonard
The Honorable Board Member Claude Parrish
The Honorable Board Member Steve Westly
The Honorable Board Member Betty Yee

Attachments: Letter to David R. Doerr by Bob Morris
Assembly Revenue & Taxation Committee Report, pages 13 & 16

County of Los Angeles
OFFICE OF ASSESSOR
500 WEST TEMPLE STREET
LOS ANGELES, CALIFORNIA 90012
(213) 974-3101

ALEXANDER H. POPE
ASSESSOR

December 4, 1978

RECEIVED
1 1 1978
Division of Assessment Standards

Mr. David R. Doerr
Chief Consultant
Assembly Revenue and
Taxation Committee
State Capitol, Room 2013
Sacramento, California 95814

Dear Dave:

RE: COMMENTS ON TASK FORCE RECOMMENDATIONS

I have reviewed the Task Force recommendations with the members of the Executive Staff of this Department. While we support generally all the proposals with respect to which a consensus has been reached to date, we do want to make a few comments about the following matters.

1. Change of Ownership

We agree with the concept embodied in the new definition of change of ownership because it provides a consistent, overall basis for determining which transfers trigger reappraisal.

Our major concern is with the retroactive application of the definition to the 1975-1978 period. This would require us to review the more than 900,000 documents which are already being processed under a system recently designed to comply with the requirements set forth in S.B. 2212. Such a review would be exceedingly time-consuming and expensive and would require a substantial budget augmentation in this period of limited budgetary resources.

In the alternative, we suggest that the effective date for the new definition be July 1, 1979, when the applicable provisions of S.B. 2212 will cease to be operative. This would allow sufficient lead-time for development of procedures to accommodate to the new approach.

Also, we recommend incorporation into the draft legislation of a provision which would provide for the separate assessment of each unit in community apartments (commonly known as "own-your-owns") and other similar common ownerships. They are presently valued and entered on the roll as a single entity, irrespective of the number of separately owned dwellings within such multi-unit structures. This change in the law would facilitate implementation of the rule that only the unit transferred is subject to reappraisal.

2. Taxpayer Reporting

The procedure recommended for the discovery of unrecorded transfers is acceptable to us as a marked improvement over our present inability to identify such transactions. We are concerned, however, that an ownership statement incorporated into the business property statements and mailed to other commercial and industrial property owners would cost more and, obviously, have less coverage than one enclosed with all tax bills. For this reason, we still prefer the approach originally suggested by us for Task Force approval.

Since that initial discussion, we have modified our proposal by eliminating the requirement that tax collectors not accept any payment of taxes unaccompanied by a completed ownership statement. We have removed another objection of our Tax Collector by requiring the filing of such statements primarily when there are changes in beneficial interests not evidenced by recorded transfer documents.

We would like to have the Task Force reconsider this revised version of the proposed statutory changes (a copy of which is enclosed). If it does not meet with general approval, we may want to consider offering it as a special amendment applicable only to counties with a population in excess of four million.

3. New Construction

We concur with the prevailing view that the definition of new construction contained in S.B.E. Rule 463, as revised by us, should be drafted in statutory form (as we understand the S.B.E. staff is doing).

One remaining concern is that appropriate language be added to deal with shopping center or high-rise office building developments where the construction process often transcends several lien dates. For that purpose, we have amended the draft previously distributed. Under the amended version (copy enclosed), the date of completion of such construction would be deferred until the new construction is ready for occupancy. We decided against any more specific language at this level. Presumably, the Board will spell out the new code section in a more extensive Rule than the current 463.

4. Decline in Value

We agree with the legal analysis which gives a broad interpretation to the words "other factors" as used in Paragraph (b) of Proposition 8. With respect to the question of the appraisal unit to which the Proposition 8 test should be applied, we believe fixtures and personal property should, in accordance with past practice, be treated separately from land and buildings. Anything else would be administratively unworkable at this time.

Equally important is the need to establish the effective date of Proposition 8. Our suggestion is that Paragraph (a) is simply declarative of the intent of Proposition 13 (the pre-existing Board rules are much broader as we discussed) and should be applied for all purposes under Section XIII-A; but that Paragraph (b) is clearly a change which should be applied prospectively only, starting with the 1979-80 lien year.

I am taking the liberty of sending copies of this letter to other members of the Task Force. Hopefully, it will be received by some in time to be given a moment's thought before the next meeting on December 7.

Sincerely yours,

Alexander H. Pope

ALEXANDER H. POPE
Assessor

AHP:wh
Encls.
cc: All Task Force Members
Gerald D. Cochran, Assessor, Del Norte County
Ernest L. Comalli, Assessor, Sonoma County
Bradley L. Jacobs, Assessor, Orange County
William C. Lynch, Assessor, Sacramento County
Frank C. Seeley, Assessor, Riverside County
Eldon C. Williams, Assessor, San Diego County

County Assessor

834 Court Street
Martinez, California 94553
(415) 372-2257
E.F. Wanaka
Assessor
XXXXXXXX
XXXXXXXXXXXXX

Contra
Costa
County

Information
372-2252
Tax Exemptions
372-2292
Property Valuation
372-2265
Richmond Office
256 24th Street
94804
233-7060

n/a

January 9, 1979

Board Hearing
1-23-79

Janice Masterton
Calendar Clerk
State Board of Equalization
P. O. Box 1799
Sacramento, CA 95808

Dear Ms. Masterton:

We are enclosing comments received from staff in reference to proposed rule changes 460, et al.

An apparent conflict exists between Rule 460 and Rule 324 regarding the unit of appraisal.

In addition, please note the attached comments regarding SBE letters and examples. They are confusing as noted.

Thank you for your consideration.

Very truly yours,

Carl S. Rush

CARL S. RUSH
County Assessor

CSR:ni

Enclosures

1/2 Board Members Bell, Rigby, Senini, Watton

Office of
CONTRA COSTA COUNTY ASSESSOR
834 Court Street
Martinez, California 94553

January 3, 1979

TO: Carl Rush

FROM: A. Lagorio

RECEIVED
JAN 4 1979
CONTRA COSTA
COUNTY ASSESSOR

SUBJECT: Proposed Amendments - Rules 460, et al.

RULE 461 (d)

Proposed amendment is acceptable as written. Exclusion of machinery and equipment from improvements constituting an appraisal unit was recommended by the Business Property Sub-Committee.

The Sub-Committee concurred that "additional computation of market values, and annually reviewing all fixtures with land and structural appraisals to compare total 'unit' market values versus Prop. 13 values create an impossible requirement. Of the counties present at the meeting, NONE were of the opinion that they could comply with such a procedure and consider it unadministrable" (BPSC minutes 11/78).

RULE 467 Amend.

Proposed amended wording is ambiguous and should be rewritten.

September 26, 2006

Ms. Diane Olson
Regulations Coordinator
State Board of Equalization
450 N Street, MIC:80
Sacramento, CA 95814

Re: Proposal to Adopt Property Tax Rule 474, *Petroleum Refining Properties*

Dear Ms. Olson:

The California Taxpayers' Association ("Cal-Tax") represents taxpayers in various legislative contexts on issues relating to tax policy. Members of Cal-Tax come from nearly every industry in California.

Cal-Tax opposes the State Board of Equalization's ("BOE's) adoption of Property Tax Rule 474 on two specific grounds, both of which are described below. Instead of adopting Rule 474, Cal-Tax proposes that the BOE amend existing Property Tax Rule 461(e). We have enclosed a proposed amendment to Rule 461(e) for the BOE's consideration at its meeting on September 27, 2006.

Objections to Rule 474

Cal-Tax's first objection to Rule 474 is based on the absence of any need for such a rule. *Government Code* sections 11349.1 and 11349, which are part of the California Administrative Procedures Act ("APA"), require the BOE to demonstrate by substantial evidence the "need for a regulation" in order to carry out the purpose of a statute, court decision or other provision of law. Cal-Tax has carefully examined the BOE's Initial Statement of Reasons ("ISR") for Rule 474 as well as the context from which Rule 474 arose. Neither the ISR nor the prior history create any need for a rule of this type.

Moreover, there is no predicate statute, court decision or law which Rule 474 appears to effectuate and, for that reason, the Rule does not fulfill the "Necessity" requirement of the APA.

In addition, Cal-Tax objects to Rule 474 because it is not consistent with the law which it seeks to effectuate as required by the APA. (*Gov. Code*, §§ 11349.1, 11349(d).) Specifically, Rule 474 conflicts with *Revenue and Taxation Code* section 51, subparagraph (d). Section 51(d) was enacted

CALIFORNIA TAXPAYERS' ASSOCIATION
1215 K Street, Suite 1250 • Sacramento, CA 95814 • (916) 441-0490 fax (916) 441-1619 • http://www.caltax.org

by the California Legislature based on the work of the Task Force that was commissioned to implement Propositions 13 and 8 in 1978. The language of Section 51(d) was recommended by the Proposition 13 Task Force and adopted by the Legislature. As explained in the Task Force's January 22, 1979 Report and in the Assembly Revenue and Taxation Committee's October 29, 1979 Report, implicit in that language is the presumption that fixtures are a separate appraisal unit for "decline-in-value" purposes because fixtures had been separately valued prior to the adoption of Propositions 13 and 8. Rule 474 turns this arrangement "on its head" by establishing the opposite presumption for petroleum refineries, namely, that fixtures are not presumed to constitute a separate appraisal unit. The Rule's position directly contradicts Section 51(d), the basis cited for the Rule, and also undermines twenty-five years of consistent BOE practice on this issue.

For the reasons stated above, Cal-Tax firmly believes that the BOE should reject Rule 474.

Alternative to Rule 474

Government Code section 11346.5(a)(13) requires the SBE to consider reasonable alternatives to Rule 474 prior to its adoption. Such alternative(s) should be either "more effective in carrying out the purpose for which the action is proposed or . . . as effective and less burdensome to affected private persons than the proposed action."

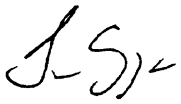
As an alternative to Rule 474, Cal-Tax proposes that the BOE amend Property Tax Rule 461, subparagraph (e), to elaborate and explain the basis and methods for valuing fixtures as a separate appraisal unit in the "decline-in-value" context. To that end, you will find enclosed a proposed comprehensive amendment to Rule 461(e). This amendment preserves the language of Rule 461(e) but also incorporates key provisions from *Revenue and Taxation Code* section 51. The suggested revision includes the correct appraisal unit presumption, *i.e.*, that fixtures are presumed to be a separate appraisal unit, and provides the historical context for that presumption (as was discussed in the 1979 Proposition 13 Task Force Report and the 1979 Assembly Revenue and Taxation Committee Proposition 13 Implementation Report).

Cal-Tax believes that the proposed amendment to Rule 461(e) is a statement of existing law and long-standing BOE practice, and that the suggested language will apply to all types of industrial and manufacturing properties throughout California. Cal-Tax also believes that the proposed amendment provides instruction to California assessors as to how to make "decline-in-value" analyses for fixtures. Finally, the suggested alternative is more effective in carrying out the provisions of Section 51(d).

Conclusion

To reiterate, Cal-Tax urges the BOE to turn down Rule 474. There is no necessity for adoption of the Rule, and the Rule clearly conflicts with Section 51(d), the statute it supposedly seeks to effectuate. Instead, Cal-Tax asks that the BOE seriously consider amending Rule 461, subparagraph (e), along the lines set forth in the enclosed document, as an effective alternative to Rule 474.

Respectfully submitted,



Teresa Casazza
Vice President/Legislative Director

Enclosure

PROPOSED AMENDMENT TO CALIF. PROPERTY TAX RULE 461(e)

(e) The following provisions govern the identification and measurement of declines in value for real property under Section 51 of the Revenue and Taxation Code.

(1) The current lien date full value of real property shall be determined by taking into account reductions in value due to damage, destruction, depreciation, obsolescence, removal of property, or other factors causing a decline in value. Declines in value will be determined by comparing the current lien date full value of the appraisal unit to the indexed base year full value of the same unit for the current lien date.

(2) For purposes of this subdivision, real property means that appraisal unit that persons in the marketplace commonly buy and sell as a unit, or that is normally valued separately.

(3) If the real property was damaged or destroyed by disaster, misfortune, or calamity and the board of supervisors of the county in which the real property is located has not adopted an ordinance pursuant to Section 170, or any portion of the real property has been removed by voluntary action by the taxpayer, the taxable value of the property shall be the sum of the following:

(a) The lesser of the indexed base year full value of land or the current lien date full value of land.

(b) The lesser of the indexed base year full value of improvements or the current lien date full value of improvements.

In applying this subdivision, the base year value of the subject real property does not include that portion of the previous base year value of that property that was attributable to any portion of the property that has been destroyed or removed. The sum determined under this subdivision shall then become the base year value of the real property until that property is restored, repaired, or reconstructed or other provisions of law require establishment of a new base year value.

(4) If the real property was damaged or destroyed by disaster, misfortune or calamity and the board of supervisors in the county in which the real property is located has adopted an ordinance pursuant to Section 170, the taxable value of the real property shall be its assessed value as computed pursuant to Section 170.

(5) For purposes of this subsection fixtures and other machinery and equipment classified as improvements are rebuttably presumed to constitute a separate appraisal unit when determining the current lien date full value for any assessment after July 1, 1978. This presumption may be rebutted by presenting evidence that land and improvements, including fixtures and other machinery and equipment classified as improvements, are the unit that commonly sold in the marketplace, or were commonly valued as a unit, prior to July 1, 1978. As

used in this subsection, marketplace means there are a number of properties for sale at all times and a number of willing buyers.

(6) Because fixtures and other machinery and equipment classified as improvements are presumed to constitute a separate appraisal unit for decline in value purposes, their current lien date full value shall be determined by applying the valuation method or methods used to value fixtures and other machinery and equipment classified as improvements prior to July 1, 1978. Where fixtures and other machinery and equipment classified as improvements constitute a separate appraisal unit, but the method or methods used to value such property prior to July 1, 1978 are not known, such property shall be valued using the method or methods that permit the separate valuation of fixtures and other machinery and equipment classified as improvements. If the presumption in the prior subparagraph is rebutted through the presentation of adequate evidence as required in that subparagraph, then fixtures and machinery and equipment classified as improvements may be valued using any of the valuation methods set forth in Section 3 of Title 18 of this code, and such property need not be separately valued.

SOURCES:

Paragraph (e):	New
Subparagraph (1):	1st sentence: R&TC § 51(a)(2) 2nd sentence: Existing Rule 461(e)
Subparagraph (2):	R&TC § 51(d)
Subparagraph (3):	R&TC § 51(b) [Subsections (a) and (b) terminology adjusted to follow nomenclature in second sentence of revised Subparagraph (1) above]
Subparagraph (4):	R&TC § 51(c)
Subparagraph (5):	1st sentence: Existing Rule 461(e) and New (underscored) Balance of Subparagraph: New
Subparagraph (6):	New

[Note: "New" language is based on January 22, 1979 Prop. 13 Task Force Report and October 29, 1979 Assembly Revenue and Taxation Committee Report]

WSPA
Western States Petroleum Association
Credible Solutions • Responsive Service • Since 1907

Letters Submitted To State Board Of Equalization
Regarding Proposed Property Tax Rule 474

Tab No.	Letter
1	July 15, 2005 letter from Bob Poole, Western States Petroleum Association to David Yeung, State Board of Equalization
2	October 10, 2005 letter from Bob Poole, Western States Petroleum Association to David Yeung, State Board of Equalization
3	November 9, 2005 letter from Bob Poole, Western States Petroleum Association to David Yeung, State Board of Equalization
4	September 21, 2006 letter from Bob Poole, Western States Petroleum Association to Diane Olson, State Board of Equalization
5	September 21, 2006 supplemental letter from Bob Poole, Western States Petroleum Association to Diane Olson, State Board of Equalization
6	September 26, 2006 letter from Cris K. O'Neall, Rodi, Pollock, Pettker, Galbraith & Cahill to Diane Olson, State Board of Equalization

P.O. Box 21108, Santa Barbara, California 93121
(805) 966-7113 • Fax: (805) 963-0647 • Cell: (805) 252-6778 • bob@wspa.org • www.wspa.org

Tab No. 1

Tab No. 1

WSPA
Western States Petroleum Association
Credible Solutions • Responsive Service • Since 1907

7-15-05

Attn: Mr. David Yeung
State Board of Equalization
Assessment Policy and Standards
450 "N" Street
PO Box 942879
Sacramento, California 94279-0064

david.yeung@boe.ca.gov

WSPA letter #1

RE: Proposed Property Tax Rule 474, *Petroleum Refining Properties*

David,

The Western States Petroleum Association (WSPA) is a non-profit trade association that represents approximately 30 companies that account for the bulk of petroleum exploration, production, refining, transportation and marketing in the six western states of Arizona, California, Hawaii, Nevada, Oregon and Washington. Founded in 1907, WSPA is the oldest petroleum trade association in the United States.

As you know most refiners and WSPA have opposed the amendments to Rule 461which,in essence, gave the Assessor the discretion to remove Proposition 13 protection from land and Proposition 8 protection from fixtures for any properties the Assessor deemed to be in a single appraisal unit. The proposals ignored the history of the statutes implementing Proposition 13 and were wisely withdrawn by the Assessor's Association. In fact, the proposals were withdrawn in part because "it has always been the CAA's position that Rules should not be written or modified when there is pending litigation on the subject, we believe that further action on modifying Rule 461(e) should be postponed pending the outcome of the litigation." (CAA letter dated December 10, 2004 to the Honorable Claude Parrish Chairman, Property Tax Committee)

The Assessors now support proposed Rule 474 that seeks to *automatically* remove that protection for all refineries on the theory that they are special properties and should be accorded special treatment with respect to appraisal unit theory as has been done for oil and gas producing properties and mineral producing properties. That proposal ignores that extractive processes are completely different from manufacturing and are possessory rights where the right to extract is taxed, not the minerals themselves. In such a case, any fixture attendant to such a possessory right is logically within the same appraisal unit as that possessory right.

To the contrary, a refinery is no different than any manufacturing assembly line and should not be treated differently in appraisal unit theory. Fixtures are purchased separately and applied to refinery property in exactly the same manner, as is the case with every other manufacturing facility. The SBE specifically wanted to protect the declines in value for affixed machinery and equipment in enacting Rule 461 and that protection should not be undone piecemeal in a setting given to advocacy rather than one driven by overall assessment policy. In fact, in an interested parties meeting on Rule 461, an assessor admitted that the change was designed to increase revenues. If Rule 474 passes in its current form, no other manufacturing property could be logically distinguished and the system would be out of balance. Further, the Assessors would be forced to consider the impact of land contamination in

relation to the positive values on machinery and equipment under the concept of the appraisal unit advanced under Rule 474.

If refinery properties are truly unique as the Assessors' Association purports, then they should embrace a comprehensive rule to cover all aspects of such properties similar to the scope of Rules 468 and 469, which they cite as authority for their current proposal. *None of the other rules narrowly tackle a single aspect of a special property.*

Some of the topics of concern to taxpayers that must be addressed in any rule are as follows:

Income Approach

- Discount rates which do not reflect the risk of owning a single refinery asset
- Product pricing based on assets not present at the refinery (i.e. rack vs. spot prices)
- Removal of intangible business enterprise values
- Proper calculation of working capital

Cost Approach

- Capital expenditures for sustaining items (maintenance, environmental compliance, etc.) are added to the value conclusion when only strategic capital adds value
- Equipment lives in calculating depreciation
- Calculation of economic obsolescence

Sales Comparison Approach

- Assessors failure to consider sales of comparable property
- Units of comparison

These are only a few of the concerns that must be addressed in any rule purporting to establish guidelines for assessing refineries. We would be happy to discuss specific examples of these issues and other points during the interested parties' process. We would insist that such items be considered otherwise the rulemaking process becomes nothing more than advocacy outside the judicial arena.

As you know, from time to time WSPA has proposed an Assessor's Handbook on refineries. If Rule 474 is necessary as the Assessors say, then a comprehensive Handbook should be developed prior to the adoption of this rule

Thank you for the opportunity to provide comments on this issue. We look forward to participating on behalf of our members in the upcoming Interested Parties process, and at the subsequent SBE's Property Tax Committee hearing on Proposed Rule 474.

Respectfully

Bob Poole
Coastal Coordinator

P.O. Box 21108, Santa Barbara, California 93121
(805) 966-7113 • Fax: (805) 963-0647 • Cell: (805) 252-6778 • bob@wspa.org • www.wspa.org

Tab No. 2

Tab No. 2

WSPA letter #2

October 10, 2005

BY E-MAIL (david.yeung@boe.ca.gov) AND U.S. MAIL

Mr. David Yeung
State Board of Equalization
Assessment Policy and Standards Division
P.O. Box 942879
Sacramento, CA 94279-0064

Re: **Proposed Property Tax Rule 474**
Alternative Industry Language Submitted
by Western States Petroleum Association

Dear David:

The Western States Petroleum Association (WSPA) submits the enclosed alternative language to Proposed Property Tax Rule 474. This alternative language is being submitted in accordance with instructions from Sherrie Kinkle which were provided to all interested parties by e-mail on September 1, 2005.

WSPA's alternative language broadens the scope of Proposed Rule 474 to include all manufacturing and industrial properties, as well as other "heavily-fixturized" properties. WSPA believes that if the concept within the proposed rule is to be adopted, it must be applied to all manufacturing and industrial properties and not just to petroleum refineries. As WSPA representatives pointed out during the interested parties meeting on August 23, 2005, there is no material difference between a refinery and any other type of manufacturing or industrial processing facility. Auto assembly factories, food processing facilities and power plants, to name a few, are indistinguishable in terms of valuation and assessment. In fact, even motion picture studios and amusement parks can be valued and assessed in a manner similar to that used for petroleum refineries.

There is a sound legal basis for broadening the scope of Proposed Rule 474 to include all manufacturing and industrial facilities. As currently written, the proposed rule singles out petroleum refineries for special treatment without providing any reason for doing so. The law requires more than the bald assertion in the proposed rule that petroleum refineries are

"unique" in nature.[1] In fact, the U.S. Constitution prohibits taxing authorities from discriminating against a specific class of taxpayers by taxing their property differently from other taxpayers unless the taxing authority's practice is founded upon a "reasonable distinction," "is supported by a rational basis," and "is not palpably arbitrary." (*Amador Valley Joint Union High School Dist. v. State Bd. of Equalization* (1978) 22 Cal.3d 208, 234; *Haman v. County of Humboldt* (1973) 8 Cal.3d 922, 926-27.) A taxing scheme which offends these requirements violates the Equal Protection Clause of the U.S. Constitution. WSPA contends that Proposed Rule 474 is being arbitrarily imposed on petroleum refineries without any reasonable distinction or rational basis and that, if approved, the proposed rule will violate the Equal Protection Clause. WSPA's proposed alternative language, if adopted, would reduce the likelihood of an equal protection challenge because the alternative language treats all manufacturing and industrial properties, including petroleum refineries, in the same way.

There is another valid reason for broadening the scope of Proposed Rule 474. Article 13, section 1 of the California Constitution requires that all properties be valued and assessed uniformly throughout the state. That requirement is codified in Government Code section 15606(c) and (e) under which the State Board of Equalization (SBE) is charged with the duty of prescribing rules and regulations governing assessment practices throughout the state "in order to insure uniformity in appraisal practices." (*Xerox Corp. v. County of Orange* (1977) 66 Cal.App.3d 746, 753.) If Rule 474 is adopted as originally proposed, the assessment practices of county assessors with regard to petroleum refineries will vary considerably from those used for other manufacturing and industrial properties, even though there is no palpable distinction between refineries and manufacturing/industrial properties. Once again, by broadening Proposed Rule 474 as WSPA suggests to include all manufacturing and industrial properties, the proposed rule is less likely to run afoul of the uniformity requirement in the California Constitution.

Please note that this letter does not supersede or replace WSPA's July 15, 2005 letter to you. As stated in that letter, it is WSPA's position that Rule 474, as originally proposed, is too narrowly focused. If the SBE intends to promulgate a rule pertaining to petroleum refineries, such rule should be comprehensive in scope, covering all aspects of refinery valuation and assessment, just as Property Tax Rules 468, 469 and 473 do for oil and gas producing properties, mining properties and geothermal properties. In addition, or alternatively, the SBE should undertake preparation and publication of a comprehensive handbook on the subject of refinery valuation and assessment.

---

[1] The same could be said for breweries, power plants and amusement parks.

WSPA requests that the alternative language which accompanies this letter be included in the Issue Paper which the Board's staff prepares in conjunction with Proposed Rule 474.

Respectfully submitted,

WESTERN STATES PETROLEUM ASSOCIATION

By:_____
Bob Poole, Coastal Coordinator

Enclosure (Industry Proposed Draft Rule 474)

295351.1

RULE 474. MANUFACTURING AND INDUSTRIAL PROPERTIES.

Authority Cited: Section 15606(c), Government Code
Reference: Article XIII, Section 1, and Article XIII A, Section 2, California Constitution
Sections 51, 53.5, and 110.1, Revenue and Taxation Code

(a) The provisions of this rule apply to the valuation of the real property, including personal property and fixtures located at the real property, used for manufacturing and industrial purposes and to facilities in which fixtures constitute a significant percentage of the property located at the facility.

(b) GENERAL.

(1) The unique nature of manufacturing and industrial properties as well as facilities in which fixtures constitute a significant percentage of the property located at the facility requires the application of specialized appraisal techniques designed to satisfy the requirements of article XIII, section 1, and article XIII A, section 2, of the California Constitution. To this end, manufacturing and industrial properties as well as facilities in which fixtures constitute a significant percentage of the property located at the facility shall be valued pursuant to the principles and procedures set forth in this rule.

(2) Notwithstanding any other provision in this rule, any appropriate valuation method described in section 3 of title 18 of this code may be applied in the event of a change in ownership for any property which falls within the category of properties referred to in paragraph (a) above.

(c) DEFINITIONS. For the purposes of this section:

(1) "Manufacturing and industrial properties" means any facility, including real property, personal property, and fixtures, used for manufacturing or industrial purposes, as identified in 2002 North American Industry Classification System (NAICS) Codes 31 through 339999 (Manufacturing).

(2) "Facilities in which fixtures constitute a significant percentage of the property located at the facility" means any facility in which the full value of the fixtures located at such facility constitute at least forty percent (40%) of the full value for all real and personal property and fixtures located at that facility.

(3) "Appraisal unit" consists of the real and personal property and fixtures that persons in the marketplace commonly buy and sell as a unit.

(d) DECLINES IN VALUE. For the purposes of this section:

(1) Declines in value of manufacturing and industrial properties or facilities in which fixtures constitute a significant percentage of the property located at the facility will be determined by comparing the current lien date full value of the appraisal unit to the indexed base year full value of the same unit.

(2) The land, improvements, and fixtures and other machinery and equipment classified as improvements for a manufacturing property, industrial property, or a facility in which fixtures constitute a significant percentage of the property located at the facility are rebuttably presumed to constitute a single appraisal unit, except when measuring declines in value caused by disaster, in which case land shall constitute a separate unit.

(3) In rebutting this presumption, the assessor may consider evidence that:

(A) The land and improvements including fixtures and other machinery and equipment classified as improvements are not under common ownership or control and do not typically transfer in the marketplace as one economic unit; or,

(B) When the fixtures and other machinery and equipment classified as improvements are not functionally and physically integrated with the realty and do not operate together as one economic unit.

October 10, 2005

295328.1

Tab No. 3

Tab No. 3

WSPA

Western States Petroleum Association
Credible Solutions • Responsive Service • Since 1907

November 9, 2005

WSPA letter #3

BY E-MAIL (david.yeung@boe.ca.gov) AND U.S. MAIL

Mr. David Yeung
State Board of Equalization
Assessment Policy and Standards Division
P.O. Box 942879
Sacramento, CA 94279-0064

Re: **Proposed Property Tax Rule 474**
Additional Comments by
Western States Petroleum Association

Dear David:

The Western States Petroleum Association (WSPA) submits the following additional comments in connection with Proposed Property Tax Rule 474.

As you know, Proposed Rule 474, paragraph (c)(2), defines an "appraisal unit" as the "property that persons in the marketplace commonly buy and sell as a unit." This definition, as applied to petroleum refining properties, is premised on the assumption that refineries are always sold or transferred as a single unit.

In fact, that is not the case. There are numerous instances in which large items of refinery equipment, known as "process units," are sold or transferred separately from the land on which they are situated and the other improvements, machinery and equipment at a refinery.

I have set forth below several Internet websites and Internet links for companies, which relocate refinery process units, or broker the sales of individual units, including Ventech and ConneXsys:

http://www.ventech-eng.com/PastProjects.htm

http://www.ventech-eng.com/RelocatedRefineries.htm

http://www.ventechequipment.com/surplus.htm (click "El Segundo" and "Gaviota")

http://www.connexsysinc.com/html/diesel_hydrotreater_project.html

http://www.cencorefining.com/units_for_sale.htm

Ventech's website lists the refinery process units which Ventech has moved from one location to another for Koch Refining, Gary Refining and Ashland Petroleum. The website also sets forth the refinery process units which are currently for sale, including several units in southern California (printouts from the website are attached to this letter). ConneXsys' website

describes a process unit which was moved from a refinery in New Jersey to Chevron's refinery in Richmond, California (printout also attached). Also attached is a printout from CENCO refining's website listing the process units for sale at CENCO's refinery in Santa Fe Springs, California.

There are a number of California refineries using process units that were obtained from other locations, including out-of-state locations. In addition to the unit that was moved to Chevron's Richmond, California refinery from New Jersey, ConocoPhillips' has a hydrotreater process unit that was moved from a location in western Colorado and installed at ConocoPhillips' Los Angeles Refinery during the 1990s.

WSPA believes there is significant information demonstrating that petroleum refining properties ***do <u>not</u> always sell or transfer as a single appraisal unit***. That being the case, it would be inappropriate to adopt Proposed Rule 474, because that rule is based on an incorrect and unsupportable assumption.

For the reasons set forth above, as well as in WSPA's July 15th and October 10th letters to the State Board of Equalization, WSPA urges the Board and its Staff to reject Proposed Property Tax Rule 474.

Respectfully submitted,

WESTERN STATES PETROLEUM ASSOCIATION

By:_____
Bob Poole, Coastal Coordinator

Attachments

P.O. Box 21108, Santa Barbara, California 93121
(805) 966-7113 • Fax: (805) 963-0647 • Cell: (805) 252-6778 • bob@wspa.org • www.wspa.org

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Respectfully submitted,

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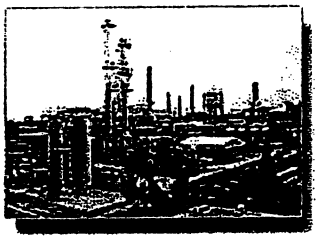
Thursday, **November 03, 2005**

The Ventech Companies

Past Projects

Modular Refineries

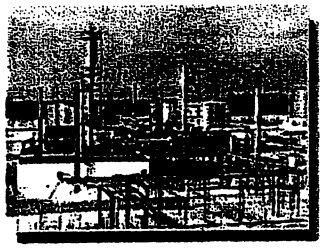


PT Humpuss Pengolahan Minyak

A new 10,000 BPSD crude unit with a 4,000 BPSD hydrotreater and reformer were constructed for PT Humpuss Pengolahan Minyak on the Eastern end of Java. Ventech Engineers began with a crude assay and executed the purchasing, engineering, shipping, construction, and operator training for the facility, all within an eight-month period.

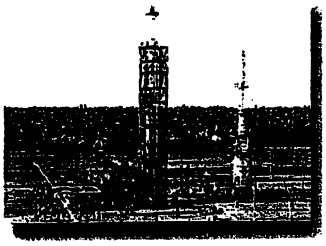
Kogalymnefegaz, (Division of Lukoil)

Ventech Engineers designed, fabricated, assembled and shipped in early 2001 a 126,000 MTA Distillate Hydrotreater and a 33,000 MTA Catalytic Reformer for Kogalymneftegaz. This facility was designed to meet Russian codes and standards, modularized for quick installation and winterized for operations down to -56°C temperatures in Siberia.



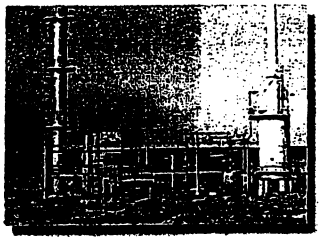
Uraineftegaz (Division of Lukoil)

Ventech Engineers designed and supplied a 2,000 BPSD crude topping unit along with a 650 BPSD Hydrotreater and Reformer for Lukoil operations located in Western Siberia. This facility was designed to meet Russian codes and standards, modularized for quick installation and winterized for operations down to -56°C temperatures in Siberia.



ONGC

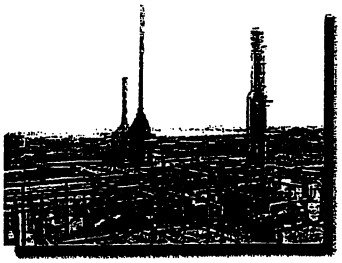
Ventech Engineers partnered with an Indian Contractor to provide a 2,000 BPSD Modular Crude Unit to ONGC (Oil and Natural Gas Corporation of India) that was started up in early 2001. Ventech provided the front end engineering, some detailed engineering, and commissioning and start-up assistance.



Azov

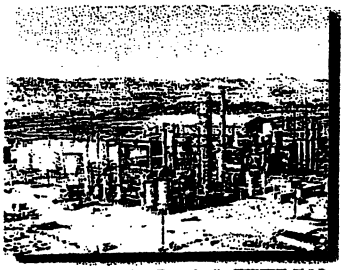
Ventech Engineers engineered, assembled and shipped to the Ukraine a 6000 BPSD Modular Crude unit and associated utilities to the Azov Oil Company. This unit was shipped in early 2001.

Relocated Refineries



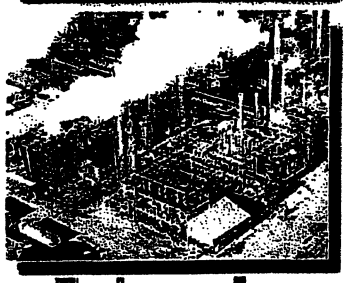
Koch Refining Company

Koch Refining Company needed a naphtha desulfurizer for their refinery in Corpus Christi, Texas. Ventech supplied a surplus unit and relocated it from Louisiana. Surplus equipment resulted in a capital savings of 30% less than new unit cost. The project required only eight months - five months less than new unit construction.



Gary Refining

Gary Refining asked Ventech to build a refinery in Fruita, Colorado, to produce jet fuel and JP4 from feedstock derived from Shale Oil. Ventech delivered it for about 70% of normal new unit cost and had it ready for operation in 13 months. To accomplish this project, Ventech relocated two existing hydrocrackers with a common fractionating section from Louisiana and modified them for one new service using Union Oil Hydrocracking technology.



Ashland Petroleum Corporation

Ashland Petroleum Corporation had a 10,000 BPSD HDS Reformer Unit at their shut down refinery in Buffalo, New York that they wanted relocated to their St. Paul, Minnesota refinery. New soil conditions and a change in plot plan required extensive re-engineering. Despite severe weather conditions, Ventech completed the entire project within the course of a year.

Ark City Refinery

Ventech Engineers oversaw the dismantling, match marking, loading, and transportation of a 30,000 BPSD Crude and Vacuum Unit in Arkansas City for relocation to the Ukraine. The unit is currently stored at Ventech's Fabrication Facilities in Pasadena, Texas.

Thursday, November 03, 2005

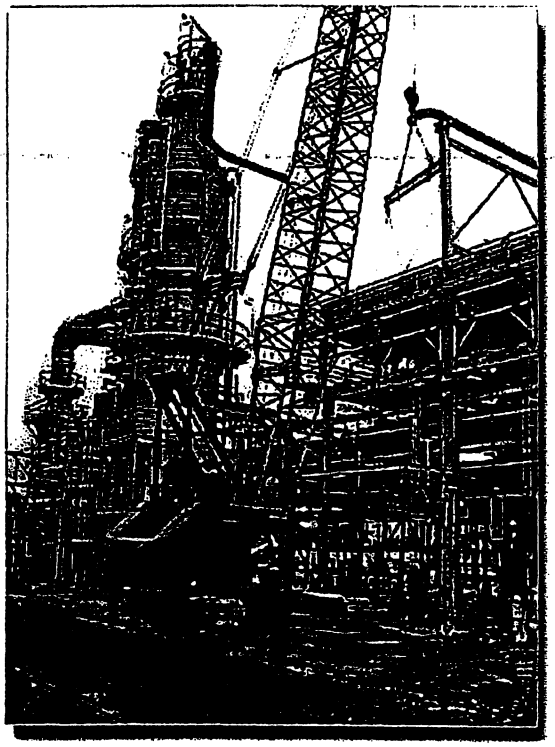
The Ventech Companies

Plant Relocations

Ventech is known worldwide as the leader in plant relocations.

Ventech is the internationally recognized leader for plant relocations, having moved more refineries (often from one continent to another) than any other company in the world. Our engineering, surplus equipment and construction divisions are experienced in match marking, dismantling, loading, and shipping complete process units. We will re-engineer, refurbish, and re-erect the facilities for new operations, using both new and surplus equipment.

Advantages of Refinery Relocation



- **Re-engineering efforts may be done faster than original design.** This saves tremendously on working man-hours, allowing time and money ordinarily spent in design and development to be re-allocated, resulting in lower construction costs.

- **Site preparation and civil/foundation construction design is released for construction much earlier.** Foundations re-design incorporates different geotechnical constraints. The equipment footprints remain identical to the original design.

- **Major equipment and materials can be available on site at a much earlier date.** Since the majority of the process equipment is already fabricated, there is a dramatic decrease in the time usually allotted to new equipment deliveries, thus plant erection can begin at a much earlier date.

- **Bulk materials and equipment can be ordered earlier and available on site with major equipment.** Materials such as structural steel, conduit, and piping can be ordered much earlier, resulting in a faster project schedule.

- **Overall project plan is reduced and the plant can be in operation months earlier.** Operating revenue from early startup represents the largest cost savings advantage of refinery relocation. Financing costs are also reduced.

Ventech Process Equipment, Inc.

The Ventech Companies

Ventech Engineers, Inc.

Ventech Engineers Int'l Corp.

Ventech Process Equipment, Inc.

Ventech Appraisal Services, Inc.

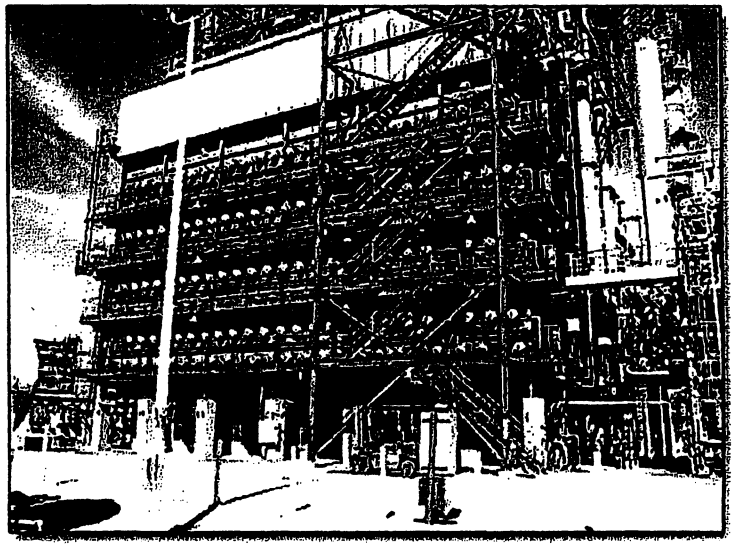
1149 Ellsworth
P.O. 4261
Pasadena, Texas 77502
(713) 477-0201 phone
(713) 477-2420 fax

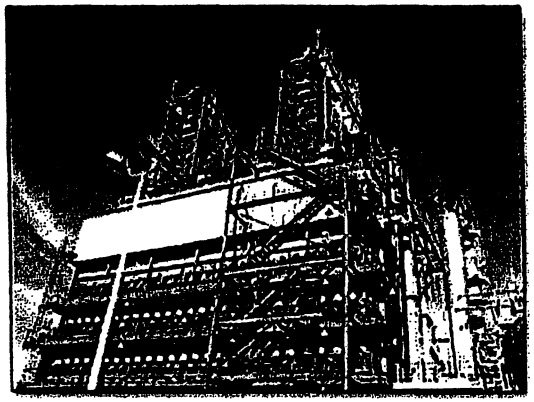
Legal Notice

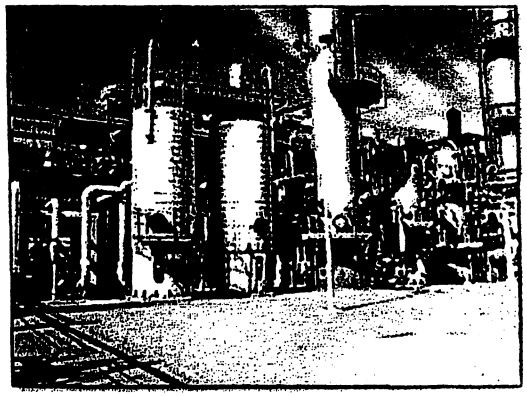
FOR SALE

(For Relocation Only)

El Segundo Hydrogen SMR







Process Flow Diagram

Detailed Equipment List:

- Compressors
- Heat Exchangers
- Heaters
- Pressure Vessels
- Pumps
- Tanks
- Miscellaneous & Utilities

For more information contact the Sales Dept. at (713) 477-0201 ext. 1609
or e-mail robert@ventech-eng.com.

Ventech Process Equipment, Inc.

FOR SALE

(For Relocation Only)

Gaviota Gas & Oil Plant

The Ventech Companies

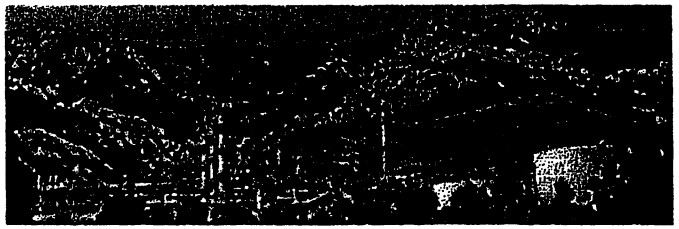
Ventech Engineers, Inc.

Ventech Engineers Int'l Corp.

Ventech Process Equipment, Inc.

Ventech Appraisal Services, Inc.

1149 Ellsworth
P.O. 4261
Pasadena, Texas 77502
(713) 477-0201 phone
(713) 477-2420 fax



The Gaviota Gas and Oil Plant is designed to process 100,000 BPD of crude and 60 MMscfd of gas. Click for detailed description.

The Oil Plant produces dry, stabilized crude for shipment via pipeline. The Gas Plant produces sweet sales gas, propane, butane, NGL and elemental sulfur for shipment by truck and pipeline.

Associated utilities and produced water treating systems are also available from this site.

Block Flow Diagram (PDF)

Legal Notice

Individual Plants:

- Plant 3 - Oil Stabilization Plant

- Plant 4 - Produced Water Treating Plant
- Plants 10A/10B - Intake Separation, Condensate Stripping and Gas Compression Plants ---> **10B SOLD**
- Plants 11/21 - Acid Gas Removal Plants ---> **21 SOLD**
- Plants 12/13 - LTS/Deethanizer and Sales Gas Compression
- Plants 14/24 - Selectox Sulfur Plants
- Plants 15/25 - Tail Gas Treating Plants
- Plant 16 - Fractionation Plant ---> **SOLD**
- Plant 17 - Liquids Treating Plant
- Plant 72 - VRU and Utilities
- Plants 73A/73B - Sulfur & LPG Loading & Storage -->**73A SOLD**

Detailed Equipment List:

- Air Coolers
- Blowers
- Boilers
- Centrifugal Pumps
- Columns
- Compressors
- Filters
- Heat Exchangers
- Miscellaneous
- Tanks
- Reciprocating Pumps
- Vessels

For more information contact the Sales Dept. at (713) 477-0201 ext. 1609 or e-mail robert@ventech-eng.com.

Tab No. 4

Tab No. 4

WSPA

Western States Petroleum Association
Credible Solutions • Responsive Service • Since 1907

September 21, 2006

WSPA letter #4

BY FEDEX

Ms. Diane Olson
Regulations Coordinator
State Board of Equalization
450 N Street, MIC:80
Sacramento, CA 94279-0080

Re: Proposal to Adopt Property Tax Rule 474, *Petroleum Refining Properties*
Western States Petroleum Association's Objections to Proposed Rule 474

Dear Ms. Olson:

The Western States Petroleum Association ("WSPA") respectfully submits the following opposing comments and objections to proposed Property Tax Rule 474 ("Rule 474"). Rule 474 is scheduled to be heard by the State Board of Equalization ("SBE") on Wednesday, September 27, 2006. This letter should be included in the SBE's official rulemaking file for Rule 474.

WSPA is a long-standing trade association comprised of energy companies that own and operate properties and facilities in the petroleum industry, including petroleum refineries. WSPA opposes Rule 474 on the following grounds:

(1) There is no legal or factual predicate that makes enactment of Rule 474 necessary at this time;

(2) Rule 474 contradicts *Revenue and Taxation Code* section 51(d), the statutory provision that the Rule ostensibly effectuates, by establishing a valuation presumption that is inconsistent with the presumption implicit in Section 51(d);

(3) Certain references upon which Rule 474 is based are incorrect;

(4) The Rule contains unfamiliar and undefined terms in violation of the "Clarity" standard for new regulations, and the Rule is unclear in the light of existing regulations;

(5) The provisions of Rule 474 duplicate provisions in existing regulations;

P.O. Box 21108, Santa Barbara, California 93121
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(6) Rule 474 discriminates against petroleum refineries by establishing a separate class of taxpayers without any reasonable distinction or rational basis, thereby violating Constitutional equal protection standards;

(7) Use of Rule 474 will produce a statewide lack of uniformity in the assessment of and assessed values for industrial and manufacturing properties; and

(8) Rule 474 will impose "new taxes" on petroleum refiners, in violation of Article XIII A, section 3, of the California Constitution, by changing the method by which taxes on petroleum refineries are to be determined.

Each of these grounds is discussed below. Based on the above and the discussion that follows, WSPA urges the SBE to reject Rule 474 in its entirety.

BACKGROUND

HISTORY OF FIXTURES AS A SEPARATE APPRAISAL UNIT

Proposition 8 "Declines-in-Value" and the Enactment of *Revenue and Taxation Code* section 51

Proposed Rule 474 establishes a rebuttable presumption that the class of property known as "fixtures" be subsumed into all property comprising a petroleum refinery when measuring a refinery's market value, that is, whether a refinery has experienced a "decline-in-value." The requirement to track "declines-in-value" resulted from the passage of California's Proposition 13 ("Prop. 13") in 1978 and the subsequent approval of Proposition 8 ("Prop. 8"), the complement to Prop. 13, later in the same year. In brief, Prop. 13 puts a cap on increases in property assessments and taxes, while Prop. 8 requires assessment at market value when a property's value declines below the Prop. 13 cap. Hence, the term "decline-in-value," which is synonymous with the concept of market value in property tax assessment circles. The California Legislature implemented Prop. 8 by enacting *Revenue and Taxation Code* section 51 in 1979.[1]

[1] A summary of activities leading up to the implementation of Prop. 13 and Prop. 8 is appended to another letter which WSPA is submitting concurrently with this letter (the "Prop. 13 / Prop. 8 Implementation – *Rev. & Tax. Code* Section 51" Letter).

Fixture Valuation and Assessment Prior to Prop. 13 / Prop. 8

Prior to passage of Prop. 13 and Prop. 8, fixtures were normally appraised and assessed separately from other forms of real property, namely land and improvements.[2] In fact, before Prop. 13 and Prop. 8 were approved by the electorate, fixtures were usually assessed using a cost approach to value because that valuation method allowed assessors to separately depreciate and value fixtures. This is corroborated in submittals by assessor's offices to the SBE both at the time Prop. 8 was being implemented through Section 51[3] and in later administrative proceedings before the SBE to amend Property Tax Rule 461,[4] a portion of which deals with treatment of fixtures for "decline-in-value" purposes.

Use of the "Appraisal Unit" Concept in Implementing Prop. 13 and Prop. 8

The implementation of Prop. 13 and Prop. 8 required the Legislature to consider the different methods by which land, improvements and fixtures were normally valued. The valuation methods in use at that time for these classes of property differed, with fixtures typically being valued using a cost approach, and land and improvements normally being valued by a sales comparison approach or income approach.

The Task Force on Property Administration discussed the implementation of Prop. 13 and Prop. 8 in its January 22, 1979 Report to the California Assembly Committee on Revenue and Taxation ("Task Force Report"). The Task Force, which had been tasked with developing ways of implementing Prop. 13 and Prop. 8, specifically addressed Prop. 8's "decline-in-value" aspect and recommended use of the "appraisal unit" concept in its Report:

---

[2] Common examples of fixtures include large pieces of machinery and equipment, such as the process units found in a petroleum refinery. Improvements generally includes buildings, although the statutory definition of "improvements" in *Revenue and Taxation Code* section 105 encompasses fixtures.

[3] *See, e.g.*, December 4, 1978 letter from Los Angeles County Assessor Alexander H. Pope to David R. Doerr (Consultant to the Assembly Revenue and Taxation Committee and Chairman of the Prop. 13 Implementation Task Force) at page 3 (stating that fixtures be treated as a separate appraisal unit "in accordance with past practice") [copy attached hereto under Tab 1]. Reference should also be made to WSPA's "Prop.13 / Prop. 8 Implementation – *Rev. & Tax. Code* Section 51" Letter for further information regarding the treatment of fixtures.

[4] *Cal. Code Regs.*, tit. 18, § 461.

> The Task Force recommends that the assessed value of real property be the lesser of the Prop. 13 base value compounded annually by 2%, or full cash value [market or Prop. 8 value]. These changes will be measured by *that appraisal unit which is commonly bought and sold in the market, or which is normally valued separately.*[5] (Emphasis added.)

The Task Force Report went on to explain: "The purpose of the 'appraisal unit' concept is to ensure that these increases or declines in value be measured in the same manner as such property was appraised prior to Prop. 13."[6] The language from the Task Force Report's recommendation on the "appraisal unit" was subsequently adopted by the Legislature and is currently set forth in subparagraph (d) of *Revenue and Taxation Code* section 51:

> (d) For purposes of this section, 'real property' means *that appraisal unit that persons in the marketplace commonly buy and sell as a unit, or that is normally valued separately.* (Emphasis added.)

Following the enactment of Section 51 in the summer of 1979 (AB 1488, Brown), the Assembly Revenue and Taxation Committee issued a report entitled "Implementation of Proposition 13 – Property Tax Assessment" dated October 29, 1979 ("Assembly Report"). The Assembly Report provided further explanation of the Prop. 8 "decline-in-value" provisions and also elaborated on the "appraisal unit" concept:

> In determining the extent of a potential decline in value, the assessor must look to the net change in value of the appraisal unit which is commonly bought and sold in the market place, or which is normally valued separately (section 51(c), 2d paragraph [now section 51(d)]). This means that land and improvements are ordinarily treated as a unit, and that a taxpayer cannot claim a net decline in full cash value terms of an improvement due to depreciation, without also including any appreciation in the value of the land. If the building depreciation is offset by the increase in

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[5] Task Force Report, p. 29. This page and other pertinent pages from the Task Force Report are attached to WSPA's "Prop.13 / Prop. 8 Implementation – *Rev. & Tax. Code* Section 51" Letter.

[6] Task Force Report, p. 31.

> land value, then no reduction in assessment occurs. *Fixtures, however, are normally appraised separately, thus owners may claim a decline based on depreciation of the fixture without regard to the value of the surrounding land or improvements.*[7] (Emphasis added.)

Fixtures Presumed to Be "Normally Appraised and Valued Separately"

Careful review of the excerpts from the Task Force Report, the Assembly Report and Section 51(d) set forth above reveals that, for land and improvements, the "appraisal unit" is intended to be that property which commonly bought and sold in the marketplace, while for fixtures the "appraisal unit" is constituted of that property *normally appraised and valued separately*. Key to this definition is knowing what the practice for valuing properties was *at that time*. As described above, as of 1979, fixtures were normally appraised separately using a cost approach. It follows, therefore, that the Section 51(d) definition of the appraisal unit as real property "that is normally valued separately" refers to fixtures and that, consistent with assessment practice when Section 51 was adopted in 1979, fixtures were *presumed* to be a separate appraisal unit for property tax assessment purposes.[8]

SBE and Courts Support Fixtures as a "Separate Appraisal Unit"

In 1978, at the same time that Section 51 was being enacted, the SBE was adopting regulations to implement Prop. 13 and Prop. 8 (and to implement Section 51). The "fixtures as a separate appraisal unit" concept in the "decline-in-value" context was set forth in Property Tax Rule 461 and currently appears in subparagraph (e) of Rule 461:

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[7] Assembly Report, pp. 13, 16. The Assembly Report refers to land, improvements and fixtures. All of these items fall under the definition of real property (*see Rev. & Tax. Code*, §§ 104, 105) and would be included in the term "real property" set forth in Section 51(d). Pertinent pages from the Assembly Report are attached to WSPA's "Prop.13 / Prop. 8 Implementation – *Rev. & Tax. Code* Section 51" Letter.

[8] As explained below, the "fixtures as a separate appraisal unit" concept embodied in Section 51(d) is undermined by Rule 474, which presumes that fixtures in a petroleum refining property are not a separate appraisal unit but, rather, part of a larger "appraisal unit" that includes land and improvements.

> (e) Declines in value will be determined by comparing the current lien date value full value [Prop. 8 value] of the appraisal unit to the indexed base year full value [Prop. 13 value] of the same unit for the current lien date. Land and improvements constitute an appraisal unit except when measuring declines in value caused by disaster, in which case land shall constitute a separate appraisal unit. *For purposes of this subsection fixtures and other machinery and equipment classified as improvements constitute a separate appraisal unit.* (Emphasis added.)

This language, which first appeared in Rule 461 starting in 1979, has been consistently followed by the SBE over the years. For example, in 1979, the SBE issued Letter to Assessors ("LTA") No. 79/39 which explicitly stated in response to Question 9 on Page 2 that fixtures were a separate appraisal unit and that value changes in land and improvements could not be offset against value changes in fixtures. In 1996, the SBE also issued legal opinions supporting the separate assessment of fixtures (SBE Annotation Nos. 850.0016 [January 30, 1996] and 848.0005 [November 7, 1996]). In 1998, the SBE published *Assessors' Handbook* Section 502 entitled "Advanced Appraisal," the fifth page of which repeated the requirement that fixtures are a separate appraisal unit for "decline-in-value" purposes. Four years later, in 2002, the SBE published Section 504 of the *Assessors' Handbook* entitled "Assessment of Personal Property and Fixtures." Pages 17, 95-96 and 101-102 of that publication contain an extensive discussion of "decline-in-value" assessment of fixtures, including the requirement to consider fixtures as a separate appraisal unit. In fact, as recently as November 2005, the SBE issued a legal opinion stating that fixtures constitute a separate appraisal unit for "decline-in-value" purposes and that offsetting appreciation in land and building improvements values against declines in value due to depreciation of fixtures (which would occur if land, improvements and fixtures are all included in the same appraisal unit) was prohibited (SBE Annotation 180.0073 [November 23, 2005], p. 3).[9]

California's courts have also supported Rule 461(e)'s separate appraisal unit requirement. In *BP West Coast Products, LLC v. County of Los Angeles*, Los Angeles County Superior Court Case No. BC269200, the court reviewed the substance and background of Rule 461(e) and found that the Los Angeles County Assessment Appeals Board failed to follow Rule 461(e)'s mandate to "treat fixtures as a separate appraisal unit."[10] Treating fixtures as a separate appraisal unit for

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[9] Copies of the SBE authorities cited in this paragraph are attached hereto [Tab 2].

[10] *See* May 26, 2004 Statement of Decision in *BP West Coast Products, LLC v. County of Los Angeles*, Los Angeles County Superior Court Case No. BC269200, at p. 3 (lines 12-15), a (footnote continued)

"decline-in-value" purposes has also been accepted by the California Court of Appeal. In *County of Orange v. Orange County Assessment Appeals Bd. No. 1*, the appellate court cited Rule 461 in support of its finding that it was appropriate to value fixtures separately.[11]

The Ongoing Controversy over Fixtures as a Separate Appraisal Unit

Although up until the advent of Rule 474, the SBE had consistently held fixtures to be a separate appraisal unit for Prop. 8 "decline-in-value" purposes, that position has been challenged by assessors in recent years. Most recently, in 2003, the California Assessor's Association ("CAA") asked the SBE to amend paragraph (e) of Rule 461 by inserting the word "may" into the last sentence of the rule. This change would have made the treatment of fixtures as a separate appraisal unit permissive rather than mandatory. The CAA withdrew that request to amend Rule 461(e) in December 2004. The SBE's current effort relating to Rule 474 is the latest chapter in the CAA's ongoing attempts to weaken subparagraph (e) of Rule 461 as it pertains to assessment of fixtures at large industrial facilities such as refineries.[12]

RULE 474 PROCEDURAL HISTORY

Rule 474 was initially proposed in early 2005 by SBE Member Claude Parrish. Upon its introduction, the SBE's Property Tax Committee voted to submit the Rule to an "interested parties process," which is an informal information-gathering and consensus-building process used by the SBE prior to taking specific action under the authority granted to the SBE by *Government Code* section 15606. Following meetings among assessors, representatives from industry (including WSPA) and the SBE's Staff, the Property Tax Committee took up the question of whether to press forward with a rulemaking procedure for Rule 474 at the Committee's December 2005 meeting. At that time, there were insufficient votes to place the Rule into the rulemaking process. Thereafter, Member Parrish put consideration of Rule 474 on the Committee's June 2006 agenda, at which time the Committee and then the SBE voted to proceed with the formal rulemaking process. Information regarding the initial introduction of

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copy of which is attached hereto [Tab 3]. Although a Judgment was issued based on this Statement of Decision, that Judgment was vacated in the settlement of a subsequent appeal.

[11] *County of Orange v. Orange County Assessment Appeals Bd. No. 1* (1993) 13 Cal.App.4th 524, at pp. 531-32.

[12] A summary of prior administrative activity relating to Rule 461, and subparagraph (e) in particular, is set forth in a separate letter titled "Enactment and Other State Board of Equalization Activities Re: Rule 461(e)" submitted to the SBE concurrently with this letter.

Rule 474 and the "interested parties process" leading up to the June 2006 vote to commence the rulemaking process is set forth in a letter which WSPA has filed concurrently with this letter (WSPA's "Rule 474 Interested Parties Process" Letter).

OBJECTIONS TO RULE 474

ADMINISTRATIVE PROCEDURES ACT

Government Code section 15606 authorizes the SBE to prescribe rules and regulations regarding the assessment of property by county assessors. Such rules and regulations must be adopted in accordance with the Administrative Procedures Act ("APA").[13] The APA sets forth both procedural and substantive standards which must be satisfied for the adoption of a new regulation. The California Office of Administrative Law ("OAL") is responsible for reviewing all regulations adopted by the SBE for compliance with procedural requirements as well as insuring that new regulations meet standards for (1) Necessity, (2) Authority, (3) Consistency, (4) Clarity, (5) Reference, and (6) Nonduplication.[14]

WSPA submits that Rule 474 does not comply with the requirements of the APA for the reasons set forth below.

Objection # 1: There Is No Necessity for Enactment of Rule 474, and Rule 474 Is Not Reasonably Necessary to Effectuate *Revenue and Taxation Code* Section 51.

Government Code section 11349.1(a)(1) requires all regulations to meet the requirement for "Necessity" in order to be valid. Furthermore, *Government Code* section 11342.2 states that "no regulation adopted is valid or effective . . . unless *reasonably necessary to effectuate* the purpose of the statute." (Emphasis added.) In implementing the "Necessity" standard, the reasonableness of a regulation is tested solely by the answer to the question of whether there is *any reasonable basis in fact* to support the legislative determination of the regulation's wisdom and necessity.[15]

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[13] *Gov. Code*, § 11340, et seq.

[14] *Gov. Code*, §§ 11349, 11349.1.

[15] *Consolidated Rock Products Co. v. City of Los Angeles* (1962) 57 Cal.2d 515, 522; *see also Slocum v. State Bd. of Equalization* (2005) 134 Cal.App.4th 969, 975-76 (invalidating (footnote continued)

In this vein, *Government Code* section 11349(a) defines "Necessity" to mean:

> . . . the record of the rulemaking proceeding demonstrates by substantial evidence the need for a regulation to effectuate the purpose of the statute, court decision, or other provision of law that the regulation implements, interprets or makes specific, taking into account the totality of the record. For purposes of this standard, evidence includes, but is not limited to, facts, studies, and expert opinion.

Section 10, subdivision (b) of Title 1 of the *California Code of Regulations* provides that in order to meet the "necessity standard" [of *Government Code* section 11349.1] the rulemaking record must include:

> (1) A statement of the specific purpose of each adoption, amendment, or repeal; and
>
> (2) information explaining why each provision of the adopted regulation is required to carry out the described purpose of the provision. Such information shall include, but is not limited to, facts, studies, or expert opinion. When the explanation is based upon policies, conclusions, speculation, or conjecture, the rulemaking record must include, in addition, supporting facts, studies, expert opinion, or other information. An 'expert' within the meaning of this section is a person who possesses special skill or knowledge by reason of study or experience which is relevant to the regulation in question.

Compliance with the "Necessity" standard requires more than a general discussion of the need for a regulatory action as a whole or simply a description of the regulatory action. It

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Property Tax Rule 139 on grounds that it was inconsistent with *Revenue and Taxation Code Code* section 170, and holding that *Government Code* section 15606 does not authorize the SBE to promulgate an unnecessary rule that conflicts with a statute that is within the SBE's enforcement purview); *accord Canteen Corp. v. State Bd. of Equalization* (1985) 174 Cal.App.3d 952, 961-62 (invalidating sales tax rule on grounds that it was inconsistent with statute, and stating that new regulation must be consistent and not in conflict with statute, and that regulation must be reasonably necessary to effectuate statute's purpose).

requires substantial evidence supporting an explanation as to "why" each provision of the proposed regulation is required to carry out its described purpose.[16]

Rule 474 does not meet the APA's "Necessity" standard. The SBE's Initial Statement of Reasons ("ISOR") purports to set forth a "Specific Purpose" and "Factual Basis" for Rule 474's enactment. Examination of the "Factual Basis" in the ISOR shows that there is no valid or substantial evidence for adoption of the Rule.

The "Factual Basis" in the ISOR consists of four (4) paragraphs. The first and second paragraphs of the ISOR summarize the provisions of California Constitution, article XIII, section 1 and article XIII A, section 2, subparagraph (b), and *Revenue and Taxation Code* section 51, subdivision (d). The summarization of these constitutional provisions and Section 51's provisions is not a factual basis, and certainly not substantial evidence, for the adoption of Rule 474.

The third and fourth paragraphs of the ISOR summarize the provisions of Rule 474 by stating what the Rule will do. Once again, a basic summarization of the provisions in Rule 474 is not a valid factual basis and does not constitute substantial evidence.[17]

The "Factual Basis" in the ISOR does not explain "why" Rule 474 is needed and "how" the Rule fills the need or "Specific Purpose" in the ISOR. Nor has the SBE provided or included within the rulemaking file any studies or expert opinions as to why Rule 474 is needed.[18] *Government Code* section 11346.2(b)(1) requires the SBE to set forth the "rationale" for its determination that adoption of Rule 474 to accomplish the "Specific Purpose" in the ISOR. And *Government Code* section 11349(a) requires the SBE to do so by a showing of "substantial evidence." The SBE's Rule 474 ISOR completely fails to satisfy these requirements and, therefore, Rule 474 fails to meet the "Necessity" standard.

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[16] *In Re Board of Equalization*, OAL File No. 03-0317-01 S (May 6, 2003), pp. 1-2; *In Re Contractors State License Board*, OAL File No. 00-1127-03 S (January 17, 2001), pp. 9-10.

[17] *In Re Office of Emergency Services*, OAL File No. 02-0731-03 C (September 19, 2002), pp. 11-12 [statement of reasons that only recites what regulation does without giving reasons does not meet substantial evidence requirement]; *In Re Acupuncture Board*, OAL File No. 06-0608-01 S (July 27, 2006), pp. 7-8 ["Necessity" requirement not satisfied by simply describing what regulations will do].

[18] *In Re Board of Forestry & Fire Protection*, OAL File No. 01-1016-02 S (December 7, 2001), p. 6 [ISOR fails to meet substantial evidence element of "Necessity" standard where factual information, studies and reports are not included in rulemaking file].

Rule 474 is not reasonably necessary to effectuate the purpose of Section 51. WSPA is not aware of any factual circumstance which justifies enactment of Rule 474 at this point in time. There is no new statute or change in any statute, no court decision, and no other change in the law which justifies changing the way in which petroleum refineries are assessed. Nor has there been any change in the nature of refineries, or the component parts of refineries, including machinery and equipment (fixtures) used at refineries, that supports enactment of Rule 474 at this time. Furthermore, as discussed below, it is clear that Rule 474 does not effectuate the purpose of *Revenue and Taxation Code* section 51 (*Gov. Code*, § 11342.2); in fact, the Rule explicitly contradicts the "fixtures as a separate appraisal unit" presumption in that statute. All of these factors militate against adoption of Rule 474.

Objection # 2: Rule 474 Is Not Consistent with and Contradicts Various Authorities.

In order to be valid, a regulation must also comply with the "Consistency" standard set forth in *Government Code* section 11349.1(4) and *Government Code* section 11342.2: "[N]o regulation is adopted is valid or effective unless consistent and not in conflict with the statute." *Government Code* section 11349, subdivision (d), defines "consistency" to mean "being in harmony with, and not in conflict with or contradictory to, existing statutes, court decisions, or other provisions of law." Administrative regulations that alter or amend a statute, or that enlarge or impair a statute's scope, are void.[19] This prohibition extends to SBE rules that are inconsistent with statutory or constitutional provisions.[20]

Rule 474 Contradicts Section 51 and the Constitutional Provisions Section 51 Implemented (Prop. 13 and Prop. 8). Rule 474 references California Constitution, article XIII, section 1, California Constitution, article XIII A, section 2, subparagraph (b), and *Revenue and Taxation Code* section 51 as the statutes which support its adoption.[21] WSPA contends that Rule 474 contradicts and is inconsistent with Section 51 and the Constitutional provisions it references and that the Rule is therefore void.

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[19] *Rosas v. Montgomery* (1970) 10 Cal.App.3d 77.

[20] *Slocum v. State Bd. of Equalization* (2005) 134 Cal.App.4th 969, 975-76; *Canteen Corp. v. State Bd. of Equalization* (1985) 174 Cal.App.3d 952, 961-62.

[21] Article XIII A, section 2, subparagraph (b) sets forth the value-limiting provision of Prop. 13 and the "decline-in-value" provision of Prop. 8. As mentioned above, and discussed in an attachment to WSPA's "Prop.13 / Prop. 8 Implementation – *Rev. & Tax. Code* Section 51" Letter, these constitutional provisions were implemented and codified in *Revenue and Taxation Code* section 51.

As discussed at the outset of this letter, Rule 474 seeks to establish a "rebuttable presumption" that fixtures (*i.e.*, machinery and equipment) located at a petroleum refinery should be valued and assessed as part of a single "appraisal unit" that also includes land and improvements. Rule 474's presumption, however, is directly contrary to the presumption incorporated into *Revenue and Taxation Code* section 51(d), as explained by legislative history.[22] The presumption in Section 51(d) is that fixtures are *not* part of the same appraisal unit as land and improvements for purposes of evaluating "declines-in-value" of property. ***Stated another way, existing law (Section 51) mandates a presumption that fixtures are a separate appraisal unit, while Rule 474 states just the opposite, i.e., that fixtures are not a separate appraisal unit.*** Because Section 51(d) is a statute of general application to all types of properties, including fixtures at petroleum refineries, Rule 474 necessarily contradicts and is in conflict with Section 51, particularly subdivision (d) of Section 51.[23] Consequently, Rule 474 does not meet the "Consistency" standard of the APA and the regulation is void.

Rule 474 Contradicts the Presumption Implicit in Property Tax Rules 461 and 324. It should be mentioned at this point that Rule 474's presumption is also inconsistent with the provisions of Property Tax Rules 461 and 324,[24] both of which have been in existence since the 1970s. Rule 461 addresses real property value changes, and Rule 324 describes the jurisdiction of local boards of equalization and local assessment appeals boards in adjudicating property tax

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[22] *See* Letter from David R. Doerr, Chair, Task Force on Property Tax Administration, to Diane Olson, dated August 24, 2006, a copy of which is attached hereto [Tab 4].

[23] It follows that Rule 474 is also in conflict with Prop. 13 and Prop. 8 (*Cal. Const.*, art. XIII A, § 2(b)) which were implemented through passage of Section 51.

Note that Rule 474 also impairs or restricts the scope of Section 51(d), a statute of general application, by making Section 51(d) inapplicable to petroleum refineries.

By artificially combining all real property (*i.e.*, land, improvements and fixtures) at refineries into a single appraisal unit, Rule 474 also undermines Prop. 13 / Prop. 8 tax increase protections to a significant extent. Application of the Rule will "water down" the Prop. 13 cap on land and building improvements when fixtures at the same location decline in value as a result of depreciation and obsolescence. In other words, using the single appraisal unit for "decline-in-value" analysis will cause declines in fixture values to offset increases in land and building improvement values. The SBE has consistently opposed the use of valuation practices which permit such offsetting to occur. *See, e.g.*, LTA No. 79/39, p. 2 [Question 9]; *Assessors' Handbook* Section 502, "Advanced Appraisal" (December 1998), p. 5; Annotation 180.0073 [November 23, 2005], p. 3 (copies attached hereto under Tab 2).

[24] *Cal. Code Regs.*, tit. 18, §§ 461 and 324, copies attached hereto [Tab 5].

appeals. Subdivision (e) in Rule 461 (set forth previously) specifically states that fixtures are a separate appraisal unit for "decline-in-value" purposes. The fourth paragraph in subdivision (b) of Rule 324, which tracks the language of Section 51(d), contains the same presumption:

> An appraisal unit of property is a collection of assets that functions together, and that persons in the marketplace commonly buy and sell as a single unit or *that is normally valued in the marketplace separately* from other property, or that is specifically designated as such by law. (Emphasis added)

As the italics show, Rule 324(b) contains the same "normally valued separately" presumption that appears in Section 51(d) and Rule 461(e). The "appraisal unit" presumption embedded in Rules 461 and 324 conflicts directly with the "appraisal unit" presumption in Rule 474, which is a further ground for rejecting the Rule.

Objection # 3: Some References Cited in Rule 474 Do Not Support Its Enactment.

Every regulation adopted by a state agency pursuant to the APA must also comply with the "Reference" standard. "'Reference" means the statute, court decision, or other provision of law which the agency implements, interprets, or makes specific by adopting, amending, or repealing a regulation."[25]

The reference statutes for Rule 474 do not support the Rule's enactment. Rule 474 cites as "Reference" statutes Sections 51, 53.5 and 110.1 of the Revenue and Taxation Code (in addition to constitutional provisions). None of the referenced statutes support Rule 474's adoption.

First, as explained above, Section 51(d) contains a presumption (*i.e.*, "fixtures are a separate appraisal unit for decline in value purposes") that is diametrically opposed to the presumption set forth in Rule 474. Therefore, it is not possible to say that Rule 474 in any way implements, interprets, or makes specific the provisions of Section 51(d).

In addition, Section 53.5, Rule 474's second reference statute, pertains to the valuation of leach pads, tailing facilities and settling ponds in mining and mineral properties. Rule 474 is only directed towards petroleum refineries, which do not have leach pads, tailing facilities or

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[25] *Gov. Code*, § 11349(e).

settling ponds. Such facilities are only found in mines and similar properties. The reference to Section 53.5 is clearly misplaced.

Finally, the reference to Section 110.1 is also misplaced. Section 110.1 defines "full cash value" under Article XIII A of the California Constitution (Prop. 13 and Prop. 8). However, Rule 474 does not use the term "full cash value" in any of its provisions. The Rule does refer to "full value" in subdivision (d), paragraph (1). "Full value" is defined in *Revenue and Taxation Code* section 110.5. As with Section 53.5, the reference to Section 110.1 is also misplaced.

Objection # 4: Rule 474 Lacks Clarity.

To be valid, a proposed regulation must meet the APA's "Clarity" standard.[26] *Government Code* section 11349, subdivision (c), defines "Clarity" to mean "written or displayed so that the meaning of regulations will be easily understood by those persons directly affected by them."

The "Clarity" standard is further defined in section 16 of title 1 of the *California Code of Regulations* which provides the following:

> In examining a regulation for compliance with the 'clarity' requirement of *Government Code* section 11349.1, OAL shall apply the following standards and presumptions:
>
> (a) A regulation shall be presumed not to comply with the 'clarity' standard if any of the following conditions exists:
>
> (1) the regulation can, on its face, be reasonably and logically interpreted to have more than one meaning; or
>
> (2) the language of the regulation conflicts with the agency's description of the effect of the regulation; or
>
> (3) the regulation uses terms which do not have meanings generally familiar to those 'directly affected' by the regulation, and those terms are defined neither in the regulation nor in the governing statute; or

[26] *Gov. Code*, § 11349.1(3).

(4) the regulation uses language incorrectly. This includes, but is not limited to, incorrect spelling, grammar or punctuation; or

(5) the regulation presents information in a format that is not readily understandable by persons 'directly affected;' or

(6) the regulation does not use citation styles which clearly identify published material cited in the regulation.

(b) Persons shall be presumed to be 'directly affected' if they:

(1) are legally required to comply with the regulation; or

(2) are legally required to enforce the regulation; or

(3) derive from the enforcement of the regulation a benefit that is not common to the public in general; or

(4) incur from the enforcement of the regulation a detriment that is not common to the public in general.

Rule 474 is unclear because it contains unfamiliar and undefined terms, terms which have more than one meaning, and terms which will be confusing to assessors and taxpayers who are directly affected by the Rule. The following is a summary of the offending terms in Rule 474 and the problems created by their usage in the Rule.

(i) "Unique nature of property used for the refining of petroleum" [Rule 474(b)(1)]. Rule 474 provides no explanation of what aspect of a petroleum refining property is "unique" in nature. Refineries employ land and buildings as part of their operations. There is nothing "unique" about land and buildings. Refineries also employ a large amount of machinery and equipment (usually classified as fixtures), including pumps, motors, compressors, heaters/boilers and vessels. Once again, there is nothing "unique" about these items of equipment which are commonly found in all types of industrial facilities. In order to satisfy the "Clarity" standard, Rule 474 must define and explain its use of the term "unique nature."

(ii) "Application of specialized appraisal techniques" [Rule 474(b)(1)]. The term "specialized appraisal techniques" is not defined in any part of Rule 474, nor does the Rule set forth or describe any "specialized appraisal techniques." In addition, there is no reference to another statute or regulation (*i.e.*, Property Tax Rule) which defines "specialized appraisal

techniques." A further concern is the reference to the "application" of appraisal techniques (subsection (d), the operative part of Rule 474, does not address appraisal "techniques"). Even if the term "specialized appraisal techniques" were defined, Rule 474 provides no guidance as to the "application" of such techniques. Rule 474 must define the term "specialized appraisal techniques" and describe the "application" of such techniques in order to meet the "Clarity" standard.

(iii) "'Appraisal unit' consists of the real and personal property that persons in the marketplace commonly buy and sell as a unit" [Rule 474(c)(2)]. In this provision, "appraisal unit" is defined to include "real and personal property." *Revenue and Taxation Code* sections 104 and 105 incorporate land, improvements and fixtures in the definition of "real property." In subparagraph (d)(2) of Rule 474, however, the "appraisal unit" *only includes* land, improvements and fixtures and *excludes* personal property. Rule 474's provisions create confusion as to what property is included in the "appraisal unit." Consequently, the Rule fails to meet the "Clarity" standard on this ground as well.

In addition, to the above concerns, subparagraph (c)(2) of Rule 474 contains a noticeable omission from the statute it seeks to implement, namely *Revenue and Taxation Code* section 51. Subparagraph (d) of Section 51 defines "appraisal unit" alternatively as the unit "that persons in the marketplace commonly buy and sell as a unit, ***or*** *that is normally valued separately*." This italicized phrase is clearly missing from the definition used in Rule 474(c)(2). Because of this omission, Rule 474's use of the term "appraisal unit" does not have the meaning that is "generally familiar" to persons who are directly affected by the regulation.

(iv) "Petroleum refineries and other real and personal property associated therewith" [Rule 474(b)(1)]. Rule 474 is directed to petroleum refining properties. The inclusion of the term "and other real and personal property associated therewith" creates considerable confusion as to what is meant, including the possibility that non-petroleum refining properties are also brought under the Rule's jurisdiction. For example, would a hydrogen manufacturing plant owned by a third party but located on a refinery's premises and which provides hydrogen to a refinery be evaluated under Rule 474? Likewise, would a cogeneration facility adjacent to and serving a refinery be assessed using Rule 474's presumption? The reference to "other real and personal property associated therewith" causes confusion in the application of Rule 474 and is another example of why the Rule does not satisfy the "Clarity" standard.

(v) "Fixtures not . . . functionally and physically integrated with the realty" [Rule 474(d)(3)(B)]. This provision contains undefined terms. Specifically, the terms "functionally and physically integrated" and "realty" are not defined in Rule 474 or by reference to any other statute or regulation, which makes it impossible for assessors and taxpayers to know what is meant by these terms when they seek to provide evidence that rebuts Rule 474's presumption.

The lack of any definition for the referenced terms prevents Rule 474 from meeting the APA's "Clarity" standard.

(vi) "As identified in Standard Industrial Classification (SIC) System Codes 2911 and 2992, or North American Industry Classification System (NAICS) Codes 32411 and 324191" [Rule 474(c)(2)]. The SIC System Codes and the NAICS Codes are not referenced or used in the governing statutes. Furthermore, the SIC System Codes and the NAICS Codes are not used in any of the Property Tax Rules promulgated by the SBE, which makes definitions of these codes not "generally familiar" to assessors and property taxpayers. Finally, NAICS Code 32411 referenced in Rule 474 is incomplete, as all NAICS Codes are comprised of six (6) digits. For these reasons, and the reasons set forth in preceding paragraphs, Rule 474 does not meet the "Clarity" standard in the APA.

Objection # 5: Rule 474 also Lacks Clarity in the Context of Existing Related Regulations.

Government Code section 11349.1(b) requires that a proposed regulation's compliance with the APA's "Clarity" standard[27] be reviewed "in the context of related regulations already in existence."

The language in existing Property Tax Rules demonstrates that Rule 474 fails to meet the "Clarity" standard. In particular, Rule 474 contains language which does not fit the context of Property Tax Rule 461, subparagraph (e), and Property Tax Rule 324, subparagraph (b). Rules 461(e) defines fixtures as a separate appraisal unit for "decline-in-value" purposes and Rule 324(b) identifies the appraisal unit using the "normally valued separately" language found in *Revenue and Taxation Code* section 51(d). As explained at the outset of this letter, the "normally valued separately" phrase, which is noticeably absent from Rule 474(c)(2), incorporates the concept of separate valuation of fixtures in the "decline-in-value" context. Because Property Tax Rules (or regulations) 461 and 324 treat fixtures as a separate appraisal unit for "decline-in-value" purposes and employ the "normally valued separately" language (which implies a "decline-in-value" context), these existing regulations have established a context which differs from that of Rule 474. Rule 474 will cause confusion among persons who are "directly affected" by the Rule's provisions because the Rule's context differs from existing regulations and, for that reason, Rule 474 does not meet the APA's "Clarity" standard.[28]

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[27] *Gov. Code*, §§ 11349.1(3), 11349(c).

[28] Rule 324(b) is directed at local boards of equalization and local assessment appeals boards in carrying out their responsibility to adjudicate assessment appeal applications. The first paragraph in subdivision (b) of Rule 324 calls for these local boards "to determine the full value (footnote continued)

On a related note, it may be asserted that Rule 474 is consistent with Property Tax Rules 468, 469 and 470[29] relating to valuation and assessment of petroleum producing properties, mining properties and geothermal properties. All three of those Rules include fixtures within the appraisal unit for "decline-in-value" analysis purposes. The provisions of these Rules are inapplicable to Rule 474 because Rules 468, 469 and 473 all deal with valuation of depleting natural resources – oil and gas, minerals, and geothermal energy (steam) – and the Rules are comprehensive in nature. It is sensible to include fixtures in the appraisal unit for the property types covered by these Rules because it not possible to exploit depleting assets without the fixtures needed for their exploitation. Note also that the depreciable lives of such production fixtures are tied to the duration of the depleting assets (oil, gas, minerals, steam) produced by means of such fixtures.

Rule 474, however, arises in an entirely different context, namely the valuation of manufacturing or industrial properties. There are no depleting assets in a refinery, which is much more closely related to a power plant, steel mill, brewery or auto manufacturing plant, and the lifetime of refinery fixtures (for depreciation purposes) is unrelated to the amount of depleting assets that have not yet been exploited. Moreover, Rule 474 is not comprehensive, but only pertains to a single aspect of refinery assessment and valuation.

Rules 468, 469 and 473 relate to properties of a completely different nature and are comprehensive in their scope. Those Rules have no relevance to the question of whether Rule 474 is a valid regulation for the valuation and assessment of petroleum refineries.[30]

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of the entire appraisal unit." Full value is defined in *Revenue and Taxation Code* section 110.5 as "fair market value," which is also the basis for Prop. 8 "decline-in-value" analyses. (*Rev. & Tax. Code* § 51(a)(2) [basis for decline-in-value is "full cash value" in *Rev. & Tax. Code* section 110; Section 110 equates "full cash value" with "fair market value"].) Consequently, a local board adjudicating a Prop. 8 "decline-in-value" assessment appeal will face the dilemma of determining whether to apply the definition of "appraisal unit" found in the last paragraph of Rule 324(b) or the "appraisal unit" definition set forth in Rule 474.

[29] *Cal. Code Regs.*, tit. 18, §§ 468, 469 and 473.

[30] *See* March 23, 1988 SBE Memorandum from Eric F. Eisenlauer to Verne Walton, a copy of which is attached hereto [Tab 6], explaining why Rule 461(d) [now Rule 461(e)] does not apply to oil and gas properties (covered by Rule 468) or mining properties (covered Rule 469). The reasoning in Mr. Eisenlauer's Memorandum also extends to geothermal properties (Rule 473).

Objection # 6: Rule 474 Violates the "Nonduplication" Standard.

The APA also requires new regulations to meet the "Nonduplication" standard.[31] "Nonduplication" is defined in *Government Code* section 11349(f) to mean:

> That a regulation does not serve the same purpose as a state or federal or another regulation. This standard requires that an agency proposing to amend or adopt a regulation must identify any state or federal state or regulation which is overlapped or duplicated by the proposed regulation and justify any overlap or duplication.

As mentioned previously, Rule 474 contains provisions which overlap with those set forth in Property Tax Rule 461(e). Rule 461(e) sets forth provisions which are applicable to all properties generally. The SBE's August 11, 2006 Notice of Proposed Regulatory Action for Rule 474 contains no reference to Rule 461(e), and no mention that Rule 461(e) also defines the appraisal unit for petroleum refineries in the "decline-in-value" context. Consequently, the SBE has not provided any information about the applicability of Rule 461(e). In view of this, Rule 474 fails to meet the APA's "Nonduplication" standard.

Objection # 7: The Financial Impact of Rule 474 Is Greatly Understated.

WSPA questions the "Cost Impact" figure set forth on page 2 of the SBE's August 11, 2006 Notice of Proposed Regulatory Action. The $1.4 million figure significantly understates the cost impact that Rule 474 will have on California refineries. WSPA believes that the direct cost impact of Rule 474, in terms of additional taxes on California refineries, will be at least $5 million, and perhaps as much as $10 million or more. The SBE should provide the public with the complete basis for its calculation of the $1.4 million figure.

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[31] *Gov. Code*, § 11349.1(6).

U.S. AND CALIFORNIA CONSTITUTIONS

Rule 474 also runs afoul of several provisions in the U.S. and the California Constitutions. The specific provisions which the Rule violates are discussed below.

Objection # 8: Rule 474 Violates Equal Protection Standards Prohibiting Disparate Treatment Of Taxpayers.

Rule 474 violates the Equal Protection Clauses of the U.S. Constitution and the California Constitution.

The Fourteenth Amendment to the U.S. Constitution provides that no state shall "deny to any person within its jurisdiction the equal protection of the laws." The federal Equal Protection Clause requires equality in the tax treatment of property owners and prohibits discrimination against property owners within the same class who are similarly situated.[32]

Similarly, Article I, section 7(a) of the California Constitution expressly prohibits the denial of equal protection of the laws. In addition, the California Constitution contains a number of provisions requiring uniformity in legislation. The California provisions go further than the Fourteenth Amendment, particularly in invalidating legislation where the basis for classification is wholly unreasonable. These additional provisions are Article I, section 7(b), which prevents the granting of special privileges or immunities to particular citizens or classes of citizens which are not granted to all, Article IV, section 16, requiring uniform operation of general laws, and Article IV, section 16(b) which bars local or special laws.

Under any of the foregoing provisions, the effect of both the U.S. and California Constitutions, and the standards for testing constitutional violations, are the same. "The test for determining the validity of a statute where a claim is made that it unlawfully discriminates against any class is substantially the same under the state prohibitions against special legislation and the equal protection clause of the federal constitution."[33] In fact, the U.S. Constitution prohibits taxing authorities from discriminating against a specific class of taxpayers by taxing their property differently from other taxpayers unless the taxing authority's practice is founded upon a "reasonable distinction," "is supported by a rational basis," and "is not palpably

---

[32] *Allegheny Pittsburgh Coal v. County Com. of Webster County* (1989) 488 U.S. 336, 345, 102 L.Ed. 2d 688, 698; *Nordlinger v. Lynch* (1990) 225 Cal.App.3d 1259, 1276-79.

[33] *Los Angeles v. Southern California Tel. Co.* (1948) 32 Cal.2d 378, 389.

arbitrary."[34] If there is no basis given for the disparate treatment, the taxing provision is deemed "arbitrary" and violates the constitutional equal protection standard.

Rule 474's disparate treatment of fixture assessments for petroleum refining properties and other "heavily-fixturized" properties raises fundamental constitutional questions. There is no rational basis for treating petroleum refineries differently from other manufacturing and heavily-fixturized properties such as auto assembly plants, food processing facilities, power plants and amusement parks. A refinery is no different than any manufacturing assembly line, and is not treated differently for appraisal purposes. Rule 474 should not be approved unless credible reasons for treating petroleum refineries differently from other manufacturing properties are provided. Absent such a showing, all California manufacturers and heavily-fixturized properties should be assessed on the same basis.

Objection # 9: Rule 474 Will Produce a Lack of Uniformity in Assessments.

Article XIII, section 1 of the California Constitution requires that all properties be valued and assessed uniformly throughout the state. That requirement is codified in *Government Code* section 15606(c) and (e) under which the SBE is charged with the duty of prescribing rules and regulations governing assessment practices throughout the state "in order to insure uniformity in appraisal practices."[35] Rule 474's adoption will cause the assessment practices of county assessors with regard to petroleum refineries to vary considerably from those used for other manufacturing and industrial properties, even though there is no palpable distinction between refineries and other manufacturing/industrial properties. The result will be lack of uniformity in the assessment of industrial properties.

Currently, some assessors are treating refinery land, improvements and fixtures as a single appraisal unit (contrary to the requirements of Property Tax Rule 461(e)) for purposes of Prop. 8 "decline-in-value" analysis. This is done by valuing refineries using an income approach, allocating a portion of the resulting income approach value to the trended base-year value for land and improvements, and placing the remainder of the value (residual value) on fixtures (stated another way, total value over and above the land and improvements' Prop. 13 value is assigned to fixtures). This practice is illegal because it uses Prop. 8 to inflate fixture

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[34] *Amador Valley Joint Union High School Dist. v. State Bd. of Equalization* (1978) 22 Cal.3d 208, 234; *Haman v. County of Humboldt* (1973) 8 Cal.3d 922, 926-27.

[35] *Xerox Corp. v. County of Orange* (1977) 66 Cal.App.3d 746, 753.

value, equates that inflated value to the Prop. 13 value, and thereby deprives refiners of a meaningful and accurate comparison of Prop. 13 and Prop. 8 values as required by *Revenue and Taxation Code* section 51(a). This practice results in excessive assessed values for some of California's petroleum refineries, and has created a lack of uniformity between northern California and southern California refinery assessments.

Objection # 10: Rule 474 Violates the Prohibition Against New Property Taxes.

Article XIII A, section 3 of the California Constitution states that "no new ad valorem [property] taxes on real property . . . may be imposed." The same provision requires two-thirds legislative approval for changes in the rate or method of calculating taxes. Rule 474 runs afoul of this prohibition by making the Prop. 8 "decline-in-value" protections set forth in *Revenue and Taxation Code* section 51 and Property Tax Rule 461(e) inapplicable to petroleum refining fixtures. The changes caused by Rule 474 will permit assessors to circumvent Prop. 13 / Prop. 8 so that increases in land values beyond Prop. 13's annual cap of 2% will offset declines in the value of fixtures at refineries. The result will constitute a new tax or an increase in tax due to the method by which assessed values are determined, and will violate the restrictions imposed by article XIII A, section 3, absent approval by two-thirds of the legislature.

CONCLUSION

As demonstrated above, Rule 474 contains numerous and significant flaws. There is no reason or need for Rule 474, and the Rule directly contradicts the statutory provision it is supposed to effectuate. Moreover, there are a number of technical flaws in the Rule as proposed, and many portions of the rule are unclear and confusing. Finally, the Rule runs afoul of Constitutional provisions prohibiting discrimination against a specific group of taxpayers without any sound rationale, and it will produce a statewide lack of uniformity in the assessment of industrial and manufacturing properties.

For all of the reasons discussed above, and in order to support existing law and the SBE's previous long-standing position on the "fixtures as a separate appraisal unit" issue, WSPA urges the SBE to reject Rule 474 in its entirety.

Respectfully submitted,

WESTERN STATES PETROLEUM ASSOCIATION

By: _____
Bob Poole, Coastal Coordinator

Attachments

cc: Honorable Betty Yee, Member, First District (w/Attachments)
Honorable Bill Leonard, Member, Second District (w/Attachments)
Honorable Claude Parrish, Member, Third District (w/Attachments)
Honorable John Chiang, Member, Fourth District (w/Attachments)
Honorable Steve Westly, State Controller, c/o Marcy Jo Mandel, Deputy State Controller (w/Attachments)

310550.1

Tab No. 5

Tab No. 5

WSPA

Western States Petroleum Association
Credible Solutions • Responsive Service • Since 1907

September 21, 2006

WSPA letter #5

BY FEDEX

Ms. Diane Olson
Regulations Coordinator
State Board of Equalization
450 N Street, MIC:80
Sacramento, CA 94279-0080

Re: Proposal to Adopt Property Tax Rule 474, *Petroleum Refining Properties*
WSPA Supplemental Letter # 1
Prop. 13 / Prop. 8 Implementation – *Rev. & Tax. Code* Section 51

Dear Ms. Olson:

This letter supplements the comments submitted by the Western States Petroleum Association ("WSPA") by letter of this same date regarding proposed Property Tax Rule 474. This letter, and the attachments hereto, pertain to "Prop. 13 / Prop. 8 Implementation – *Rev. & Tax. Code* Section 51."

A list of the attachments to this letter is appended at the end of this letter. For convenience of the reader, WSPA sets forth below the following excerpts of key language from the attached documents.

Tab 7 – Task Force Report:

Page 4: (Summary of Major Task Force Recommendations) "Declines in Value . . . B. Increases or declines in real property shall be measured by the appraisal unit which is commonly bought or sold in the market place, or which is normally value separately."

Page 31: "The purpose of the 'appraisal unit' concept is to ensure that these increases or declines in value be measured in the same manner as such property was appraised prior to Prop. 13."

Tab 10 – Letter from Robert H. Morris to David R. Doerr

Page 2: "I personally believe that any property which is valued separately, or by a separate method of valuation, than [sic] the remainder of the property assessed (and both things are true of fixtures versus land and buildings) is the only logical and definable property 'unit'."

P.O. Box 21108, Santa Barbara, California 93121
(805) 966-7113 • Fax: (805) 963-0647 • Cell: (805) 252-6778 • bob@wspa.org • www.wspa.org

Tab 12 – July 1979 Assembly Revenue and Taxation Committee Report

Page 2: (Summary of Provisions) "Assessment Procedures B. Increases or declines in real property shall be measured by the appraisal unit which is commonly bought or sold in the market place, or which is normally valued separately. (Sec. 51(c), 2d paragraph, R&TC)"

Tab 13 – October 1979 Assembly Revenue and Taxation Committee Report

Page 16: "Fixtures, however, are normally appraised separately, thus owners may claim a decline based on depreciation of the fixture without regard to the value of the surrounding land or improvements."

Page 75: (Implementation of Article XIII A – R&TC 51) "For purposes of this section, "real property" means that appraisal unit which persons in the market place commonly buy and sell as a unit, or which are normally valued separately."

Page 109: (Property Tax Rule 461, August 1979, subparagraph (d) ["Declines in value"], last sentence) "For purposes of this subsection fixtures and other machinery and equipment classified as improvements constitute a separate appraisal unit."

This letter and its attachments (Tabs 7 through 13) should be included in the proposed Property Tax Rule 474 rulemaking file for consideration by the State Board of Equalization.

Respectfully submitted,

WESTERN STATES PETROLEUM ASSOCIATION

By: Robert W. Poole

Bob Poole, Coastal Coordinator

Attachments

310743.1

Tab No. 6

WSPA

Western States Petroleum Association
Credible Solutions • Responsive Service • Since 1907

September 21, 2006

WSPA letter #6

Ms. Diane Olson **BY FEDEX**
Regulations Coordinator
State Board of Equalization
450 N Street, MIC:80
Sacramento, CA 94279-0080

Re: Proposal to Adopt Property Tax Rule 474, *Petroleum Refining Properties*
WSPA Supplemental Letter # 2
Enactment and Other State Board of Equalization Activities Re: Rule 461(e)

Dear Ms. Olson:

This letter supplements the comments submitted by the Western States Petroleum Association ("WSPA") by letter of this same date regarding proposed Property Tax Rule 474. This letter, and the attachments hereto, pertain to "Enactment and Other State Board of Equalization Activities Re: Rule 461(e)."

A list of the attachments to this letter is appended at the end of this letter. For convenience of the reader, WSPA sets forth below the following excerpts of key language from the attached documents.

Tab 14 – 1979 Enactment of Rule 461, Subdivision (d) [now (e)]:

Page 2: (January 1979 Memo from Contra Costa County Assessor [for CAA]) "Rule 461 (d) ¶ Proposed amendment is acceptable as written. Exclusion of machinery and equipment from improvements constituting an appraisal unit was recommended by the Business Property Sub-Committee. ¶ The Sub-Committee concurred that 'additional computation of market values, and annually reviewing all fixtures with land and structural appraisals to compare total "unit" market value versus Prop. 13 values create an impossible requirement. Of the counties present at the meeting, NONE were of the opinion that they could comply with such a procedure and consider it unadministrable'" (BPSC minutes 11/78)

Tab 19 – Rule 461(e) – 2004 CAA Request to Amend

Page 3: (SBE Interested Parties Meeting Minutes) "Counties concede that the vast majority of fixtures are a separate appraisal unit. However, they believe that Section 51(d) provides for those instances when fixtures are part of the large appraisal unit, and that the rule should be amended to reflect the

P.O. Box 21108, Santa Barbara, California 93121
(805) 966-7113 • Fax: (805) 963-0647 • Cell: (805) 252-6778 • bob@wspa.org • www.wspa.org

statutory provisions. They want to change their original petition language from "may" to "normally" to reflect the language in both Section 51(d) and the Task Force Report."

Tab 23 – Rule 461(e) – 2004 CAA Request to Amend

Page 1: (California Assessors' Association Letter) "At the conclusion of the Interested Parties meeting on June 25, 2004, Board staff requested that we work on some alternative language for the purpose of providing a 'bright line test' that would make the rule clear. In August, Board staff proposed the following language: '*For purposes of this subsection, fixtures and other machinery and equipment classified as improvements are rebuttably presumed to constitute a separate appraisal unit.*' On September 13, 2004, Assessors met with Board staff and agreed to the alternative language with the addition of language to clearly define what factors were needed to overcome the presumption."

Tab 31 – SBE Correspondence Re Rule 461

Page 3: (SBE Annotation No. 850.0016) "By letter of January 9, 1979 (attached) the Honorable Carl S. Rush, Assessor of Contra Costa County, submitted comments of Mr. Al Lagorio of his staff (who was also secretary of the Business Property Subcommittee of the Assessor's Association) which noted approval of the proposed and still current language of Rule 461(d) [now 461(e)]. Also attached is the letter of January 19, 1979 from the Honorable William H. Cook, Assessor of Santa Barbara County, at the time President of the California Assessors Association, which notes the approval of Rule 461(d) by the Association's Executive and Standards Committees."

This letter and its attachments (Tabs 14 through 33) should be included in the proposed Property Tax Rule 474 rulemaking file for consideration by the State Board of Equalization.

Respectfully submitted,

WESTERN STATES PETROLEUM ASSOCIATION

By: Bob Poole, Coastal Coordinator

Attachments

310744.1

Rodi-Pollock

RODI·POLLOCK

JOHN D. CAHILL
JOHN D. PETTKER
WILLIAM R. CHRISTIAN
HENRY P. PRAMOV, JR.
ALLAN E. CERAN
CRIS K. O'NEALL
THOMAS CURTISS, JR.
ALFRED KLEIN
PATRICK J. CAIN
ELIZABETH B. BLAKELY
WADE E. NORWOOD
WALTER T. KILLMER, JR.
KENNETH A. FRANKLIN
ANDREW W. BODEAU
JEAN M. BEASLEY
BRADLEY R. MARSH
RICHARD W. PETTY

RODI, POLLOCK, PETTKER, GALBRAITH & CAHILL
A LAW CORPORATION

444 SOUTH FLOWER STREET
SUITE 1700
LOS ANGELES, CALIFORNIA 90071-2901
TEL: (213) 895-4900

KARL B. RODI (1908-1982)
DANIEL C. BOND (1942-1977)
PAUL E. SCHWAB (1896-1973)

OF COUNSEL
JOHN P. POLLOCK
ROBERT A. YAHIRO
C. STEPHEN DAVIS

TELECOPIERS
(213) 895-4921
(213) 895-4922
(213) 895-4750

September 26, 2006

OUR FILE NUMBER

06351-70005

BY FACSIMILE (916-324-2597) AND E-MAIL (Diane.Olson@boe.ca.gov)

Ms. Diane Olson
Regulations Coordinator
State Board of Equalization
450 N Street, MIC: 80
Sacramento, CA 94279-0080

Re: Proposal to Adopt Property Tax Rule 474, *Petroleum Refining Properties*
Comments Regarding Proposed Property Tax Rule 474 – BOE LTAs

Dear Ms. Olson:

In connection with Proposed Property Tax Rule 474, I would like to bring the State Board of Equalization's ("BOE's") attention to Letters to Assessors ("LTAs") Nos. 79/59 and 79/143.

Both of these LTAs deal with the application of Proposition 8 "decline-in-value" concepts to fixtures (machinery and equipment) classified as improvements.

LTA 79/~~49~~ 59 specifically states:

> For the 1979-80 and subsequent tax years, the taxable value of machinery and equipment classified as improvements should be the lower of either the full cash value base or the full value.
>
> Unit of Appraisal
>
> The unit of appraisal is the total of all property that qualifies as an improvement and is reportable on Schedule "C" of the business property statement.

* * * * * *

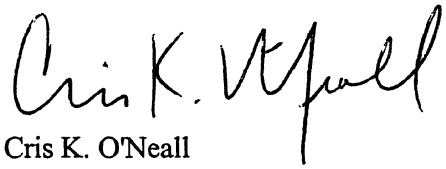
> [T]he unit consists of all fixed machinery and equipment and applicable fixtures assessed to the taxpayer at a particular plant site.

LTA 79/143 confirms the provisions of LTA 79/59 as they pertain to the "appraisal unit."

These two LTAs set forth the position that the BOE has taken on the proper appraisal unit for "fixtures classified as improvements" since the time of *Revenue and Taxation Code* Section 51's enactment and the BOE's adoption of Property Tax Rule 461.

The LTAs affirm that fixtures classified as improvements are a "separate appraisal unit" for Proposition 8 "decline-in-value" purposes.

Very truly yours,



Cris K. O'Neall

Enclosures (BOE LTAs 79/59 and 79/143)

311074.1

STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
[illegible]00 N STREET, SACRAMENTO, CALIFORNIA
([illegible].O. BOX 1799, SACRAMENTO, CALIFORNIA 95808)
(916) 445-4982

GEORGE R. REILLY
First District, San Francisco
IRIS SANKEY
Second District, San Diego
WILLIAM M. BENNETT
Third District, San Rafael
RICHARD NEVINS
Fourth District, Pasadena
KENNETH CORY
Controller, Sacramento
DOUGLAS D. BELL
Executive Secretary

March 20, 1979

No. 79/59

TO COUNTY ASSESSORS:

EFFECT OF PROPOSITION 8 UPON
MACHINERY AND EQUIPMENT VALUATION

For the 1979-80 and subsequent tax years, the taxable value of machinery and equipment classified as improvements should be the lower of either the full cash value base or the full value.

Unit of Appraisal

The unit of appraisal is the total of all property that qualifies as an improvement and is reportable on Schedule "C" of the business property statement. This would include the improvement portion of the machinery and equipment category; the office furniture and equipment category; the tools, molds, dies, and jigs category; and the "other" equipment category. The unit would also consist of fixed machinery and equipment reported as construction in progress. The unit would also include fixed equipment leased to and assessed to the taxpayer. The equipment of an industrial plant located on two or more adjacent parcels would all be considered a unit for estimating the full cash value base and the full value.

Fixtures reported on Schedule "B" of the business property statement will be considered as part of either the land and structure unit or the fixed machinery and equipment unit depending upon the category the fixtures are most compatible with.

Taxable Values

The taxable value calculations may be made as follows:

(1) Apply the full cash value base factors to the reported acquisition costs of each property category containing improvements. Then multiply each category's total by its respective improvement percentage. The combined totals of the improvement portions will be the full cash value base.

(2) Where the cost approach is used in estimating the full value, you should apply the full value factors (combined trend/percent good factors) to the reported acquisition costs of each property category containing improvements. Again multiply each category's total by its respective improvement percentage. The combined results yield the full value. Of course, you may estimate the full value by use of the income or other acceptable approaches. Additional obsolescence not accounted for in the full value factors should be considered in determining the full value.

After establishing the full cash value base and the full value of the unit, the lower of the two is the taxable value for enrollment.

File Identification

Enrollment of the full value creates a new base year value. Thus, it will be necessary each year to identify and review each taxpayer's file containing machinery and equipment classified as improvements in order to determine the proper base year value that was established the previous year.

Example

The enclosed three sheets reflect the calculation of the full cash value base factors, the full value factors, and their application to reported costs on Schedule "C." The example only covers machinery and equipment, but, as indicated earlier, if the other categories contained improvements, they would also be considered in determining the total unit value, together with the applicable fixtures.

Change to Assessors' Letter 79/39

We previously indicated in Assessors' letter 79/39 under question and answer A-11 that each year's acquisitions of machinery and equipment would be considered the unit and valued separately. Also, in question and answer A-10 we indicated that fixtures on Schedule B would be a separate unit for appraisal purposes. We have changed our position on these subjects and, as you can see, now hold that the unit consists of all fixed machinery and equipment and applicable fixtures assessed to the taxpayer at a particular plant site.

Sincerely,

Verne Walton

Verne Walton, Chief
Assessment Standards Division

VW:pb
Enclosures

SCHEDULE COST DETAIL: EQUIPMENT Include equipment expensed & fully depreciated items. Include sales or use tax, freight & installation costs. Attach schedules as needed.

LINE NO	Calendar Year of Acquis.	1. MACHINERY AND EQUIPMENT FOR INDUSTRY, PROFESSION, OR TRADE					2. OFFICE FURNITURE AND EQUIPMENT		3. TOOLS, MOLDS, DIES, JIGS		4. OTHER EQUIPMENT (Describe)	
		COST	ASSESSOR'S USE ONLY (1)		ASSESSOR'S USE ONLY (2)		COST	ASSESSOR'S USE ONLY	COST	ASSESSOR'S USE ONLY	COST	ASSESSOR'S USE ONLY
68	1979	10,000	100.0	10,000	100	10,000						
69	1978	90,000	100.0	90,000	96	86,400						
70	1977	110,000	102.0	112,200	99	108,900						
71	1976	40,000	104.04	41,616	100	40,000						
72	1975	60,000	106.12	63,672	100	60,000						
73	1974	175,000	102.82	179,935	109	190,750						
74	1973	180,000	110.4	198,720	119	214,200						
75	1972	240,000	109.32	262,368	115	276,000						
76	1971	120,000	102.83	123,396	107	128,400						
77	1970	30,000	98.50	29,550	102	30,600						
78	1969	30,000	97.42	29,226	96	28,800						
79	1968	35,000	92.00	32,200	89	31,150						
80	1967	40,000	85.51	34,204	82	32,800						
81	1966	80,000	81.18	64,944	74	59,200						
82	1965	60,000	73.60	44,160	65	39,000						
83	1964	50,000	66.03	33,015	57	28,500						
84	1963	25,000	58.45	14,612	49	12,250						
85	1962	20,000	49.79	9,958	42	8,400						
86	1961	20,000	43.30	8,660	35	7,000						
87	1960	15,000	36.80	5,520	30	4,500						
88	1959	15,000	31.39	4,709	23	3,450						
89	PRIOR	30,000	27.06	8,118	19	5,700						
90	TOTAL	1,475,000		1,400,783		1,406,000						
91	Add totals on Line 90 and any supplemental schedules								ENTER HERE AND ON LINE 3, PART II			

(1) Full cash value base computation.
(2) Full value computation

Assume an AH 581 Group 4 trend factor, 15-year life, and 80 percent of the machinery and equipment is classified as improvements.

REMARKS:		
20% Personal	<280,157>	<281,200>
Improvement	1,120,626	1,124,800
Additional Obsolescence	-	<20,000> - Allowed on a machine acquired in 1972.
	1,120,626	1,104,800

ASSESSOR'S USE ONLY

CLASSIFICATION	COL.	FIXTURES FULL VALUE	PERSONAL PROPERTY RCLND	ADJUSTMENTS	PERSONAL PROPERTY FULL VALUE
Machinery & Equipment	1	1,104,800	281,200		
Office Furniture & Equipment	2				
Tools, Molds, Dies & Jigs	3				
Other Equipment	4				
Attached Schedules	–				
TOTALS					

SCHEDULE COST DETAIL: BUILDINGS, BUILDING IMPROVEMENTS, AND/OR LEASEHOLD IMPROVEMENTS, LAND IMPROVEMENTS, LAND AND LAND DEVELOPMENT

LINE NO.	Calendar Year of Acquis.	BUILDINGS, BUILDING IMPROVEMENTS, AND/OR LEASEHOLD IMPROVEMENTS: 1. STRUCTURE ITEMS ONLY (See Instructions)			2. FIXTURE ITEMS ONLY (See Instructions)			3. LAND IMPROVEMENTS (e.g., blacktop, curbs, fences)			4. LAND AND LAND DEVELOPMENT (e.g., fill, grading)		
		COST	ASSESSOR'S USE ONLY		COST	ASSESSOR'S USE ONLY		COST	ASSESSOR'S USE ONLY		COST	ASSESSOR'S USE ONLY	
44	1979												
45	1978												
46	1977												
47	1976												
48	1975												
49	1974												
50	1973												
51	1972												
52	1971												
53	1970												
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57	1966												
58	1965												
59	1964												
60	1963												
61	1962												
62	1961												
63	1960												
64	1959												
65	Prior												
66	Total												
67	Add totals on Line 66 and any supplemental schedules.							ENTER HERE AND ON LINE 5, PART II					

TO AVOID DUPLICATE AND OVER ASSESSMENT, explain in detail additions and retirements from March 1, 1978, to February 28, 1979. (See Instructions)
(ATTACH SCHEDULES AS NEEDED)

CATEGORY	ADDITIONS – DETAIL	MO./YR. ACQD.	COST	CATEGORY	RETIREMENTS – DETAIL	YEAR ACQD.	COST
1. Structures				1. Structures			
2. Fixtures				2. Fixtures			
3. Land Imps.				3. Land Imps.			
4. Land				4. Land			

Assume an AH 581 Group 4 Industry
and a 15-Year Economic Life

Computation of the 1979 Full Cash Value Base Factors:

Year	Trend Factor AH 581 Industry Group 4		AH 581 15-Year Percent Good Factor		Combined Factor		Inflation Factor	1979 Full Cash Value Base Factor
1979	100		100		100		100.00	100.00
1978	100		100		100		100.00	100.00
1977	100	1/	100	1/	100	1/	102.00	102.00
1976	100		100		100		104.04	104.04
1975	100		100		100		106.12	106.12
1974	100	2/	95	2/	95	2/	108.24	102.82
1973	115		89		102		108.24	110.40
1972	120		84		101		108.24	109.32
1971	122		78		95		108.24	102.83
1970	127		72		91		108.24	98.50
1969	134		67		90		108.24	97.42
1968	139		61		85		108.24	92.00
1967	144		55		79		108.24	85.51
1966	150		50		75		108.24	81.18
1965	155		44		68		108.24	73.60
1964	157		39		61		108.24	66.03
1963	159		34		54		108.24	58.45
1962	160		29		46		108.24	49.79
1961	161		25		40		108.24	43.30
1960	160		21		34		108.24	36.80
1959	162		18		29		108.24	31.39
1958	165		15		25		108.24	27.06

1/ Assumed to be the value at time of purchase.
2/ From the 1975 Assessors' Handbook Section 581, Equipment Index Factors and Inventory Ratios.

Computation of the 1979 Combined Trend—Percent Good Factors (Full Value Factors):

Year	Trend Factor AH 581 Industry Group 4	AH 581 15-Year Percent Good Factor	Combined Trend/ Percent Good Factor (Full Value Factor)
1979	100	100	100
1978	100	96	96
1977	109	91	99
1976	116	86	100
1975	123	81	100
1974	143	76	109
1973	167	71	119
1972	174	66	115
1971	178	60	107
1970	185	55	102
1969	195	49	96
1968	202	44	89
1967	210	39	82
1966	218	34	74
1965	225	29	65
1964	229	25	57
1963	231	21	49
1962	233	18	42
1961	234	15	35
1960	234	13	30
1959	234	10	23
1958	234	8	19

STATE OF CALIFORNIA
STATE BOARD OF EQUALIZATION
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Executive Secretary

August 28, 1979

No. 79/143

TO COUNTY ASSESSORS:

EFFECT OF ASSEMBLY BILL 1488 UPON FIXTURES AND MACHINERY AND EQUIPMENT CLASSIFIED AS IMPROVEMENTS

In assessors' letter number 79/59 we stated that the lower of either the factored base year value or the market value for a combined unit of fixtures and fixed machinery and equipment would be the taxable value to enroll. We then indicated that this value created a new base year value for subsequent years. That advice is no longer correct. Under the guidelines of Assembly Bill 1488 and revised Board Rules 460 and 461, the enrollment of a taxable value that is less than the trended base year value does not establish a new base year value when the decline in value is attributable to economic conditions. The annual comparison will now be made between the original base year value, adjusted for additions and deletions, and properly trended to the current lien date, and the current market value. You then enroll the lower of the two. The following year you would again compare the adjusted and trended original base year value to the current market value and enroll the lower amount.

For example: Assume a taxpayer had a machine that qualified as an improvement. Its base year was 1975 with a market value at that time of $50,000. For 1979 the trended base year value would be $54,120 ($50,000 x 1.0824). You estimate the market value to be $45,000. The lower of the two—$45,000—is then enrolled as the 1979 taxable value. For 1980 the trended base year value is $55,200 ($50,000 x 1.104) but you estimate the market value to be $60,000. The lower of the two—$55,200—is enrolled as the 1980 taxable value.

The other concepts expressed in assessors' letter number 79/59 remain unchanged.

Any questions should be directed to Bud Florence of this division.

Sincerely,

Verne Walton

Verne Walton, Chief
Assessment Standards Division

VW:sk