

SANTA CRUZ COUNTY ASSESSMENT PRACTICES SURVEY

JULY 2007

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July 31, 2007

TO COUNTY ASSESSORS:

RAMON J. HIRSIG
Executive Director

No. 2007/033

SANTA CRUZ COUNTY
ASSESSMENT PRACTICES SURVEY

A copy of the [Santa Cruz County Assessment Practices Survey Report](#) is enclosed for your information. The Board of Equalization (BOE) completed this survey in fulfillment of the provisions of sections 15640-15646 of the Government Code. These code sections provide that the BOE shall make surveys in each county and city and county to determine that the practices and procedures used by the county assessor in the valuation of properties are in conformity with all provisions of law.

The Honorable Gary E. Hazelton, Santa Cruz County Assessor-Recorder, was provided a draft of this report and given an opportunity to file a written response to the findings and recommendations contained therein. The report, including the assessor's response, constitutes the final survey report which is distributed to the Governor, the Attorney General, and the State Legislature; and to the Santa Cruz County Board of Supervisors, Grand Jury, and Assessment Appeals Board.

Fieldwork for this survey was performed by the BOE's County-Assessed Properties Division from September 2005 through February 2006. The report does not reflect changes implemented by the assessor after the fieldwork was completed.

Mr. Hazelton and his staff gave their complete cooperation during the survey. We gratefully acknowledge their patience and courtesy during the interruption of their normal work routine.

These survey reports give government officials in California charged with property tax administration the opportunity to exchange ideas for the mutual benefit of all participants and stakeholders. We encourage you to share with us your questions, comments, and suggestions for improvement.

Sincerely,

/s/Lynn Bartolo for

David J. Gau
Deputy Director
Property and Special Taxes Department

DJG:ps
Enclosure

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INTRODUCTION

Although county government has the primary responsibility for local property tax assessment, the State has both a public policy interest and a financial interest in promoting fair and equitable assessments throughout California. The public policy interest arises from the impact of property taxes on taxpayers and the inherently subjective nature of the assessment process. The financial interest comes from the fact that more than one-half of all property tax revenue is used to fund public schools and the State is required to backfill any shortfalls from that property tax funding.

The assessment practices survey program is one of the State's major efforts to address these interests and to promote uniformity, fairness, equity, and integrity in the property tax assessment process. Under this program, the State Board of Equalization (BOE) periodically reviews the practices and procedures of (surveys) every county assessor's office. This report reflects the BOE's findings in its current survey of the Santa Cruz County Assessor's Office.

The assessor is required to file with the board of supervisors a response that states the manner in which the assessor has implemented, intends to implement, or the reasons for not implementing the recommendations contained in this report. Copies of the response are to be sent to the Governor, the Attorney General, the BOE, the Senate and Assembly, and the Santa Cruz County Board of Supervisors, Grand Jury and Assessment Appeals Board. That response is to be filed within one year of the date the report is issued and annually thereafter until all issues are resolved. The Honorable Gary E. Hazelton, Santa Cruz County Assessor-Recorder,¹ elected to file his initial response prior to the publication of our survey; it is included in this report following the Appendixes.

While typical management audit reports emphasize problem areas, they say little about operations that are performed correctly. Assessment practices survey reports also tend to emphasize problem areas, but they also contain information required by law (see *Scope of Assessment Practices Surveys*) and information that may be useful to other assessors. The latter information is provided in the hope that the report will promote uniform, effective, and efficient assessment practices throughout California.

¹ This report covers only the assessment functions of his office.

SCOPE OF ASSESSMENT PRACTICES SURVEYS

Government Code sections 15640 and 15642 define the scope of an assessment practices survey. As directed by those statutes, our survey addresses the adequacy of the procedures and practices employed by the assessor in the valuation of property, the volume of assessing work as measured by property type, and the performance of other duties enjoined upon the assessor.

In addition, pursuant to Revenue and Taxation Code² section 75.60, the BOE determines through the survey program whether a county assessment roll meets the standards for purposes of certifying the eligibility of the county to continue to recover costs associated with administering supplemental assessments. Such certification is obtained either by satisfactory statistical result from a sampling of the county's assessment roll, or by a determination by the survey team—based on objective standards defined in regulation—that there are no significant assessment problems in the county. The statutory and regulatory requirements pertaining to the assessment practices survey program are detailed in Appendix C.

Our survey of the Santa Cruz County Assessor's Office included reviews of the assessor's records, interviews with the assessor and his staff, and contacts with officials in other public agencies in Santa Cruz County who provided information relevant to the property tax assessment program. This survey also included an assessment sample of the 2005 assessment roll to determine the average level (ratio) of assessment for all properties and the disparity among assessments within the sample. The ideal assessment ratio is 100 percent, and the minimum acceptable ratio is 95 percent. Disparity among assessments is measured by the sum of absolute differences found in the sample; the ideal sum of absolute differences is 0 percent and the maximum acceptable number is 7.5 percent. If the assessment roll meets the minimum standards for ratio and disparity, the county is eligible to continue to recover the administrative cost of processing supplemental assessments. The sampling program is described in detail in Appendix B.

This report offers recommendations to help the assessor correct assessment problems identified by the survey team. The survey team makes recommendations when assessment practices in a given area are not in accordance with property tax law or generally accepted appraisal practices. An assessment practices survey is not a comprehensive audit of the assessor's entire operation. The survey team does not examine internal fiscal controls or the internal management of an assessor's office outside those areas related to assessment. In terms of current auditing practices, an assessment practices survey resembles a compliance audit—the survey team's primary objective is to determine whether assessments are being made in accordance with property tax law.

² Unless otherwise stated, all statutory references are to the California Revenue and Taxation Code.

EXECUTIVE SUMMARY

As stated in the Introduction, this report emphasizes problem areas we found in the operations of the Santa Cruz County Assessor's office. However, it also identifies program elements that we found particularly effective and describes areas of improvement since our last assessment practices survey.

More specifically, this survey reports on the current procedures and practices of the assessor and addresses problems discovered in our 2002 survey, in which we made 18 recommendations for improvement. The assessor has fully implemented 11 of those recommendations. Statutory changes have rendered inapplicable two of the remaining six recommendations. The remaining recommendations that were not implemented, or were implemented only in part, are repeated in this report.

This report enumerates and explains our recommendations for improvement in the assessor's operation; in general, we do not emphasize the positive aspects of his program. Thus, it is important to note at the outset that we found the assessor's overall operation to be sound. The assessor has an effective administration program, the major portions of his real property assessment program are well managed, and he has made major improvements to his business property program.

Our recommendations concern portions of programs that are currently effective but need additional improvement. In many instances, the assessor is already aware of the need for improvement and is considering changes as time and resources permit.

The assessor is effectively managing the major portions of the administration program, including appraiser training and certification, assessment appeals, and low-value property exemptions. However, in other areas there are procedures that should be revised.

The issue of most significance is that the assessor does not annually review all welfare exemption claim forms filed by existing claimants. Often these filings will disclose uses of the claimed property that would disqualify the property for the welfare exemption, either in whole or in part. Alternatively, such filings may disclose uses by other exempt organizations who have not filed as operators of the subject properties.

Under either of these circumstances, the assessor should not simply continue granting the exemption. We urge the assessor to investigate information reported on the annually filed claim forms to ensure that only qualifying uses by qualifying exempt organizations receive the welfare exemption.

In the area of real property assessment, we found that the assessor effectively manages the major portions of the program, change in ownership and new construction. There are, however, procedures for assessing special use properties that should be revised. Our primary concern is the assessment of taxable possessory interests.

The assessor often does not identify the essential factors applicable to the valuation of each taxable possessory interest. Without this information, the assessor may be unable to either (1) properly establish the base year value of a taxable possessory interest, or (2) if the base year value is properly established, monitor the value in subsequent years. We also noted that the assessor does not recognize the special statutory requirements applicable to taxable possessory interests in property owned by redevelopment agencies.

Overall, the business property division is well managed, and the audit and statement processing programs have improved substantially since our last survey. However, we are making a few recommendations regarding the valuation of business property; the most significant of these deal with the assessment of vessels.

Specifically, the assessor does not properly capture information about high-cost or documented vessels because he does not use the BOE-prescribed forms designed for these vessels. In addition, the assessor's valuation methodology systematically misstates the market value of vessels because the assessor (1) omits a sales tax allowance from values based upon vessel publications and (2) applies a fixed annual depreciation percentage to all vessels, without conducting a study of market activity to confirm the appropriateness of this fixed percentage. Because so many of the vessel assessments are affected by these shortcomings, we consider this a significant issue.

The Santa Cruz County assessment roll meets the requirements for assessment quality established by section 75.60. Our sample of the 2005-06 assessment roll indicated an average assessment ratio of 99.29 percent, and the sum of the absolute differences from the required assessment level was 1.28 percent. Accordingly, the BOE certifies that Santa Cruz County is eligible to receive reimbursement of costs associated with administering supplemental assessments.

Here is a list of the formal recommendations contained in this report, arrayed in the order that they appear in the text.

RECOMMENDATION 1: Revise the calamity reassessment notice to reflect the requirements of section 170(c).14

RECOMMENDATION 2: Improve the processing of assessment roll changes by: (1) correctly identifying penalties for prior rolls on the current roll as required by Rule 261, and (2) correctly notifying the assessee that an escape assessment has been enrolled as required by section 534.....16

RECOMMENDATION 3: Revise welfare exemption procedures by: (1) verifying that exempted property is exclusively used for qualifying purposes, and (2) limit exemption amounts for late-filed claims in accordance with section 270.....20

RECOMMENDATION 4: Revise assessment forms procedures by: (1) using only approved assessment forms, (2) using only BOE-prescribed forms, and (3) timely submitting the final prints of all assessment forms to the BOE.22

RECOMMENDATION 5: Use an appropriate income stream when valuing restricted vineyards and orchards.33

RECOMMENDATION 6: Assess taxable government-owned properties at the lowest of current fair market value, factored base year value, or restricted value.....34

RECOMMENDATION 7: Send annual questionnaires to owners of TPZ land requesting information on compatible uses.35

RECOMMENDATION 8: Improve the taxable possessory interest assessment program by: (1) assessing month-to-month taxable possessory interests in compliance with section 61(b)(2); (2) recognizing lessor expenses when valuing taxable possessory interests by the income approach; (3) obtaining copies of all lease agreements that create taxable possessory interests; and (4) assessing property in a redevelopment project in compliance with Health and Safety Code section 33673.37

RECOMMENDATION 9: Improve the assessment of water company properties by: (1) ensuring that mutual water system property is not double assessed, and (2) identifying and properly assessing all regulated water companies.40

RECOMMENDATION 10: Offset tax liabilities for escape assessments against refunds due for reductions in value only within the same tax year.45

RECOMMENDATION 11: Improve the assessment of manufactured homes by: (1) enrolling manufactured homes as personal property, and (2) enrolling the lesser of the factored base year value or the full cash value as of the lien date.50

RECOMMENDATION 12: Revise vessel procedures by: (1) ensuring that a certified auditor-appraiser reviews vessel values, (2) including sales tax as a component of a vessel's value, (3) assessing all vessels at market value, and (4) requiring vessel owners to file annual vessel property statements for boats costing \$100,000 or more.52

RESULTS OF 2002 SURVEY

Assessment Roll Changes

We recommended the assessor identify penalty and escape assessments on the current assessment roll. Amendments to section 533 have eliminated the requirement to identify escape assessments on the roll. However, the assessor is still not identifying penalties for prior rolls on the current roll; accordingly, we repeat this portion of the prior recommendation.

Disaster Relief

We recommended the assessor revise filing deadlines in the calamity brochure and the cover letter mailed with disaster relief applications so that they conform to the county's disaster relief ordinance. The assessor has fully complied with this recommendation.

Supplemental Assessments

We recommended the assessor enroll all supplemental assessments. The assessor has fully complied with this recommendation.

Change in Ownership

We recommended the assessor use the BOE-prescribed *Change of Ownership Statement*, Form BOE-502-AH, instead of his locally-developed form. This problem still exists; we repeat the prior recommendation.

We recommended the assessor include all of the information required by section 408.1 on the public transfer list. Our review indicated that the assessor included the recording date on the transfer list, but not the date posted on the grant deed. We now conclude that this omission is insignificant, since in most cases in Santa Cruz County the recording date and the date posted on the grant deed are the same. The result is that the assessor's transfer list substantially complies with section 408.1. Therefore, we do not repeat our earlier recommendation.

We also recommended that the assessor grant the parent-child exclusion from reassessment only upon receipt of a completed application, and that he report to the BOE on a quarterly basis all approved claims for base year value transfer under section 69.5. The assessor has fully implemented these two recommendations.

Declines in Value

We recommended the assessor provide an explanation of the stipulation procedure when notifying taxpayers of a value change as required by section 619. We now find his *Notification Of Assessment* in compliance with our previous recommendation and section 619.

Taxable Possessory Interests

We recommended the assessor review all private uses at the fairgrounds to determine whether taxable possessory interests existed. We also recommended that, unless otherwise provided by law, the assessor assess taxable possessory interests only in real property. The assessor has implemented our recommendations.

Low Value Property

We recommended the assessor enroll all taxable possessory interests that have a value greater than \$2,000. The assessor has implemented this recommendation.

California Land Conservation Property (CLCA)

We recommended the assessor use a basic 1 percent risk rate when valuing CLCA properties and conduct studies to establish rates that reflect the risks for the various types of CLCA land and living improvements. The assessor has partially implemented this recommendation by using a 1 percent risk rate for all CLCA properties, but has not conducted any studies to establish risk rates that recognize differences in property type or uses. Because there is no readily available data to quantitatively distinguish increments of risk for various crops, we do not repeat the prior recommendation in this report.

Audit Program

We recommended the assessor complete all mandatory audits as required by section 469 and obtain a signed waiver of the statute of limitations when a mandatory audit will not be completed on time. The assessor has complied with these recommendations.

Vessels

We recommended the assessor value vessels using data derived from the market, rather than using the same annual depreciation factor for all pleasure vessels. The assessor has not changed his practice. Therefore, we repeat the prior recommendation.

We also recommended the assessor use the BOE-prescribed forms for obtaining information for vessels eligible for the 4 percent assessment. The assessor currently uses a prototype of Form BOE-576-E, *Affidavit For 4 Percent Assessment of Certain Vessels*. However, the assessor printed a *Supplemental 4 percent Assessment Questionnaire* on the reverse side, thus altering the form without BOE approval. Therefore, we repeat the prior recommendation in the forms section of this report.

Manufactured Homes

We recommended the assessor enroll manufactured homes as personal property and establish a new base year value for any site, located within a resident-owned mobilehome park that received the section 62.1 exclusion, that has subsequently changed ownership. The assessor has implemented the second part of our recommendation.

However, he continues to enroll manufactured homes as real property. Accordingly, we repeat the first part of our recommendation.

OVERVIEW OF SANTA CRUZ COUNTY

Santa Cruz County is located at the northern tip of Monterey Bay, 65 miles south of San Francisco, 35 miles north of Monterey, and 35 miles southwest of the Silicon Valley. It is one of California's original 27 counties, created in 1850 by the State Legislature. The county has a population of approximately 260,000 inhabitants, most of whom live in the population centers of Santa Cruz, Watsonville, Scotts Valley, and Capitola. Santa Cruz County encompasses approximately 440 square miles. Major industries are technology, agriculture, and tourism. Santa Cruz County is bordered on the west by the Pacific Ocean, to the east by Santa Clara County, to the north by San Mateo County, and to the south by San Benito and Monterey Counties.

The following table displays information pertinent to the 2005-06 assessment roll as provided by the assessor:

	PROPERTY TYPE	ENROLLED VALUE
Secured Roll	Land	\$14,563,324,914
	Improvements	\$13,448,223,112
	Personal Property	\$173,745,664
	Total Gross Secured	\$28,185,293,690
	Less Exemptions	(\$610,984,919)
	Total Net Secured	\$27,574,308,771
Unsecured Roll	Personal Property & Fixtures	\$792,922,366
	Total Assessment Roll	\$28,367,231,137

The next table illustrates the growth in assessed values for recent years as reported in the BOE's annual reports:

ROLL YEAR	TOTAL ROLL VALUE	INCREASE	STATEWIDE INCREASE
2005-06	\$28,367,103,000	9.8%	11.1%
2004-05	\$25,844,411,000	6.9%	8.3%
2003-04	\$24,165,854,000	6.7%	7.3%
2002-03	\$22,643,706,000	6.1%	7.3%
2001-02	\$21,335,180,000	N/A	N/A

ADMINISTRATION

This section of the survey report focuses on administrative policies and procedures of the assessor's office that affect both the real property and business property assessment programs. Subjects addressed include the assessor's budget and staffing, the State-County Property Tax Administration Program (PTAP), appraiser certification, assessment appeals, disaster relief, assessment roll changes, exemptions, and assessment forms.

Budget and Staffing

Budget

As shown in the following table, the assessor's office has benefited from increased funding levels over recent years. PTAP funds are included in the assessor's official budget.

BUDGET YEAR	GROSS BUDGET	PERCENT CHANGE	PERMANENT STAFF	PTAP FUNDS RECEIVED	PTAP STAFF
2005-06	\$3,446,612	-0.00%	31	\$565,328	7
2004-05	\$3,448,323	11.81%	31	\$565,328	7
2003-04	\$3,084,029	5.40%	31	\$565,328	7
2002-03	\$2,925,984	10.42%	31	\$565,328	7
2001-02	\$2,649,789	N/A	31	\$565,328	7

Staffing

The assessor's office has 38 budgeted full-time positions, including the assessor. The following table shows the staff positions and the number of employees in each classification.

CLASSIFICATION	NO.	CLASSIFICATION	NO.
Assessor	1	Auditor-Appraiser II	3
Chief Deputy Assessor Administration	1	Department DP Coordinator	1
Chief Deputy Assessor Valuation	1	GIS Analyst	1
Chief Assessment Standards	1	GIS Technician	2
Chief Auditor-Appraiser	1	Assessment Technician	4
Senior Appraiser	3	Assessment Clerk	5
Clerical Supervisor	1	Assessor Aide	3
Appraiser	8	Receptionist	1
Auditor-Appraiser III	1		

Staff Property Procedures

We reviewed property records to determine if the assessor has proper procedures in place to ensure that staff do not value their own properties for property taxation purposes. We found that a senior appraiser makes the initial valuation on an employee's property, which is then reviewed by the chief deputy assessor-valuation. We did not find any instance where an appraiser made his or her assessment on any property that the appraiser owned or in which he/she had an interest.

State-County Property Tax Administration Program

In 1995, the Legislature established the State-County Property Tax Administration Program (PTAP). This program, which was later entitled the State-County Property Tax Administration Loan Program, provided state-funded loans to eligible counties for the improvement of property tax administration.³ This program expired June 30, 2001, and was replaced with the Property Tax Administration Grant Program, which is available to counties for fiscal years 2002-03 through 2006-07.⁴ The grant program operates in essentially the same manner as the loan program except that if a county does not meet its contractual performance criteria, the county will not be obligated to repay the grant but will be ineligible to continue to receive a grant.

If an eligible county elected to participate, the county and the State Department of Finance entered into a written contract as described in section 95.31. The contract provides that the county must agree to maintain a base funding and staffing level in the assessor's office equal to

³ Chapter 914, Statutes of 1995, in effect October 16, 1995. The Property Tax Administration Loan Program expired June 30, 2001.

⁴ The PTAP funding has been suspended for two years, beginning with the 2005-06 California Budget.

the funding and staffing levels for the 1994-95 fiscal year. This requirement prevents a county from using PTAP funds to supplant the assessor's existing funding.

For most counties, the contract provides that verification of performance is provided to the State Department of Finance by the county auditor-controller.

Santa Cruz County has participated in the PTAP since the inception of the program. For contract year 2004-05, the assessor received a grant of \$565,328. The county's required base funding and staffing levels for the assessor's office are \$1,789,692 and 31 positions, respectively. The Santa Cruz County Auditor-Controller has certified to the State Department of Finance that the county met the contractual requirements for loan repayment for every year under contract.

The assessor has effectively used PTAP funds for mandatory and nonmandatory audits, the timely completion of assessment appeals, enrolling transfers, new construction, and administering new business accounts. Funds have also been used to purchase new information technology hardware and software. All expenditures are designed to increase the long-term productivity of the assessor's office and other county units that are part of the property tax system.

Appraiser Certification

Section 670 provides that no person shall perform the duties of an appraiser for property tax purposes as an employee of any county or city and county unless he or she is the holder of a valid appraiser's or advanced appraiser's certificate issued by the BOE. Additionally, section 671 provides that, in order to retain a valid appraiser's certificate, every year each holder shall complete at least 24 hours of training (12 hours in the case of a holder of an advanced certificate) conducted or approved by the BOE.

There are 20 certified appraisers in the Santa Cruz County Assessor's Office, of whom 9, including the assessor, hold advanced certificates. Additionally, the auditor-appraisers performing mandatory audits meet the requirements referenced in section 670(d). The assessor does not use contract appraisers. All staff, including the assessor, are appropriately certified and are current in their training hours.

Assessment Appeals

The assessment appeals function is prescribed by article XIII, section 16 of the California Constitution. Sections 1601 through 1641.5 are the statutory provisions governing the assessment appeals process, including the conduct and procedures of assessment appeals boards and the manner of their creation. As authorized by Government Code section 15606, the BOE has adopted Rules 301 through 326⁵ to regulate the assessment appeal process.

⁵ All references to rules, refer to California Code of Regulations Title 18, Public Revenues.

The following table illustrates the assessment appeals workload for the period 2000-2004:

Fiscal Year	Total Appeals	Held over	Withdrawn	Stipulated	Not Timely	Appeals Board Decisions		
						Reduced	Upheld	No show
2004-05	105	29	52	19	0	0	5	0
2003-04	231	6	161	45	1	2	9	7
2002-03	186	0	70	73	3	2	20	18
2001-02	207	0	80	94	11	1	17	4
2000-01	85	0	44	27	0	10	3	1

Santa Cruz County has one assessment appeals board; it consists of three members appointed by the board of supervisors. All assessment appeals board members have attended the BOE assessment appeals training class. The assessor efficiently manages his appeals and coordinates scheduling of appeals hearings with the assessment appeals board.

Copies of applications for changed assessment are sent from the clerk of the board to the assessor, where the appeals are tracked in a computer database. Then, the appeals are forwarded to appropriate team supervisors for review and assignment to appraisers for their review. Many applications for changed assessment are withdrawn by the property owners upon receiving and reviewing the assessor's evidence of value.

We reviewed both real property and business property appeal hearing files. All comparable sales used in appeal hearing appraisals for real property were in accord with the requirement under Rule 324(d) that such sales occur no more than 90 days after the date for which the value was being estimated.

In accordance with section 1604(c)(1), taxpayers and the assessment appeals board have mutually signed extensions for all appeals not resolved within two years of the timely filing of the application for changed assessment.

The assessment appeals process is in compliance with all applicable statutes and rules. In each instance, the appeal was filed timely, and the assessor's opinions and value conclusions were reasonable and well documented.

Disaster Relief

Section 170 permits a county board of supervisors to adopt an ordinance that allows immediate property tax relief on qualifying property damaged or destroyed by misfortune or calamity. The property tax relief is available to the owner of any taxable property whose property suffers damage exceeding \$10,000 (without his or her fault) in a misfortune or calamity. In addition, section 170 provides procedures for calculating value reductions and restorations of value for the affected property.

To obtain relief under section 170, assessees must make a written application to the assessor requesting reassessment. Alternatively, if the assessor is aware of any property that has suffered damage by misfortune or calamity, the assessor must provide the last known assessee with an application for reassessment.

Upon receipt of a properly completed application, the assessor shall reassess the property for tax relief purposes. If the sum of the full cash values of the land, improvements, and personal property before the damage or destruction exceeds the sum of the values after the damage by \$10,000 or more, the assessor shall then determine the percentage reductions in current market value and reduce the assessed values by those percentages.

The Santa Cruz County Board of Supervisors adopted a disaster relief ordinance in 1975. The ordinance was subsequently modified in 1980, 1981, and 2002.

We found that the assessor's disaster relief program reflects the current provisions of section 170. The assessor discovers instances of disaster or calamity by reviewing newspaper articles and building permits, field canvassing, and taxpayer-initiated contacts. Upon discovery, the assessor mails an application to the property owner. Returned applications are logged in, analyzed, and processed if accepted. If denied, property owners are notified by telephone or letter. The following table lists the number of claims processed in recent years:

ROLL YEAR	CALAMITY APPLICATIONS PROCESSED
2004-05	20
2003-04	10
2002-03	17
2001-02	18
2000-01	23

We found that the assessor reassessed property for disaster relief purposes only upon receipt of a properly completed, timely filed application in full compliance with section 170(d). In the 2002 survey, we recommended that the assessor revise the filing deadlines in the calamity brochure and the cover letter mailed with the disaster relief applications to conform to the county's disaster relief ordinance. The assessor has fully complied with this recommendation. However, the assessor's notification to the taxpayer following a value reduction does not meet statutory requirements.

RECOMMENDATION 1: Revise the calamity reassessment notice to reflect the requirements of section 170(c).

We found that after the assessor adjusts the property value due to a calamity he notifies the taxpayer of this reassessment by mailing a *NOTICE OF SUPPLEMENTAL ASSESSMENT*. There is no mention in this notification of the appeal filing deadline specific to this type of reassessment, as required by section 170(c).

Section 170(c) provides that the assessor's notice shall state that the applicant may appeal the proposed reassessment within six months following the date the notice was mailed. By omitting this language from his notice, the assessor could mislead a taxpayer who might be interested in appealing a reassessment due to a calamity. The assessor should clearly notify the taxpayer of the filing deadline specific to this type of reassessment as required by section 170(c).

Assessment Roll Changes

Each year the assessor must complete the local assessment roll and deliver it to the auditor by July 1. Once the roll is delivered to the auditor, any correction that would decrease the amount of the unpaid taxes requires the consent of the board of supervisors. All changes to the roll are authorized by specific statutes, and any roll change must be accompanied by the appropriate statutory reference.

Assessment roll changes fall under two general categories: escape assessments and corrections. An escape assessment is an assessment of property that was not assessed or was underassessed, for any reason, on the original roll. A correction is any type of authorized change to an existing assessment except for an underassessment caused by an error or omission of the assessee.

The following table shows the number of roll changes, both real and business property, processed in Santa Cruz County for recent years:

ROLL YEAR	ROLL CHANGES
2004-05	2,058
2003-04	1,588
2002-03	2,110
2001-02	2,624
1999-00	2,052

In our 2002 survey, we recommended that escape assessments and penalties be correctly identified on the current assessment roll. We are not repeating that portion of the recommendation concerning escape assessments; amendments to section 533 have eliminated this requirement. However, we are repeating the portion of the recommendation concerning penalties on the assessment roll. In addition, we recommend that the assessor properly notify assesses of escape assessments.

RECOMMENDATION 2: Improve the processing of assessment roll changes by:
(1) correctly identifying penalties for prior rolls on the current roll as required by Rule 261, and (2) correctly notifying the assessee that an escape assessment has been enrolled as required by section 534.

Correctly identify penalties for prior rolls on the current roll as required by Rule 261.

Currently, the assessor identifies penalty assessments on a worksheet and for assessments for the current roll, but does not identify penalty information for prior rolls on the current assessment roll.

Rule 261(a) provides that a penalty imposed under sections 463, 503, or 504 of the Revenue and Taxation Code shall be entered on the roll in one of three methods:

- (1) By adding 10 percent or 25 percent or the percentage or maximum allowable dollar amount prescribed by statute, as the case may be, to the assessed value of each class of property to which the penalty is applicable and referencing the values so increased to footnotes or entries in the comment field which reads: "Includes ___% penalty or the maximum allowable dollar amount penalty added pursuant to Sec._____, R & T Code," or words substantially to this effect.
- (2) By inserting the amount to be added to the assessed value of each class of property and identifying the penalty by an entry which reads: "Penalty added pursuant to Sec. _____, R & T Code," or words substantially to this effect.
- (3) By entering the amount to be added to the assessed value of each class of property in another part of the roll, together with the name and address of the assessee, the tax rate area code, the words "Penalty added pursuant to Sec. _____, R & T Code" or words substantially to this effect, and a cross reference to the place on the roll at which the assessed values are entered. When this manner of enrolling penalties is chosen, the assessed value entries shall be cross-referenced to the penalty entries.

Because the assessor does not include the appropriate statutory provisions identifying the penalty for prior rolls on the current roll, the assessor's practice does not meet regulatory requirements.

Correctly notify the assessee that an escape assessment has been enrolled as required by section 534.

The assessor sends a correct *NOTICE OF PROPOSED ESCAPE ASSESSMENT* for real property escapes as required by section 531.8. For business property accounts that have been audited, the assessor sends a letter detailing the findings of the audit and informing the assessee of changes in taxable value for the fiscal year(s) affected. This letter contains all the information required by section 531.8. However, the assessor does not send a subsequent *NOTICE OF ENROLLED*

ESCAPE ASSESSMENT as required by section 534, subdivisions (c) and (d). The assessor's practice is to have the property tax bill serve as this notice.

Effective January 1, 2006, section 534(c)(3) provides that tax bills may be used instead of formal notices of enrollment of escape assessment, but only in Los Angeles County and counties whose boards of supervisors have adopted resolutions authorizing an alternate assessment appeal filing date. In addition, the tax bill must provide specific information regarding appeal rights.

The property tax bill sent out by the Santa Cruz County Tax Collector does not contain all the necessary elements specified in section 534(c)(2); it lacks language advising the taxpayer that an appeal shall be filed within 60 days of the date of mailing printed on the notice or the postmarked date thereof, whichever is later. The assessor's practice is contrary to law and does not provide proper notice to taxpayers regarding appeals of escape assessments.

Low-Value Property Exemption

Section 155.20 authorizes a county board of supervisors to exempt all real property with a base year value, and personal property with a full value, so low that the total taxes, special assessments, and applicable subventions on the property would be less than the assessment and collection costs if the property were not exempt.

Section 155.20(b)(1) provides that a county board of supervisors shall not exempt property with a total base year value or full value of more than \$5,000, or more than \$50,000 in the case of certain taxable possessory interests. A board of supervisors must adopt a low-value property exemption before the lien date for the fiscal year to which the exemption is to apply. At the option of the board of supervisors, the exemption may continue in effect for succeeding fiscal years.

Santa Cruz County adopted Resolution No. 480-99 on December 14, 1999, authorizing the exemption of all personal property with a full value of \$5,000 or less and all real property with a base year value of \$2,000 or less. Additionally, Ordinance No. 4736 delegates authority to the treasurer-tax collector and assessor to cancel taxes or supplemental and escaped assessments when the taxes do not exceed \$50.

The assessor's computer program automatically identifies real estate values that meet the low value exemption threshold, generates an exemption amount equal to the total value, and creates a zero net value that is used to cancel the assessment. We reviewed the 2005-06 secured roll and found that the exemption had been consistently applied to all eligible properties. Below is a table summarizing secured parcels exempted for low value.

ROLL YEAR	SECURED PROPERTIES	EXEMPTED VALUE
2005-06	6,150	\$4,824,082
2004-05	6,197	\$4,789,151

Unlike the secured roll, a low value exemption on the unsecured roll is created manually. When the business property statements are returned and values are estimated, accounts that have a

value less than \$5,001 are given a special code and the value is entered as \$0. We reviewed the 2005-06 unsecured roll and found no accounts with values less than \$5,001 that had been assessed.

The low-value property exemption is well managed; we have no recommendations in this area.

Exemptions

Church and Religious Exemptions

The church exemption is authorized by article XIII, section 3(f) of the California Constitution. This constitutional provision, implemented by section 206 of the Revenue and Taxation Code, exempts buildings, the land on which they are situated, and equipment used exclusively for religious worship, when such property is owned or leased by a church. Property that is reasonably and necessarily required for church parking is also exempt under article XIII, section 4(d), provided that the property is not used for commercial purposes. The church parking exemption is available for owned or leased property meeting the requirements of section 206.1.

Article XIII, section 4(b) authorizes the Legislature to exempt property used exclusively for religious, hospital or charitable purposes and owned or held in trust by a corporation or other entity. The corporation or entity, however, must meet the following requirements: (1) it must be organized and operated for those purposes; (2) it must be non-profit; and (3) no part of its net earnings can inure to the benefit of any private shareholder or individual. The Legislature has implemented this constitutional authorization in section 207 of the Revenue and Taxation Code, which exempts property owned by a church and used exclusively for religious worship and school purposes.

County assessors administer the church and religious exemptions. The church exemption and the church parking exemption require an annual filing of the exemption claim. The religious exemption requires a one-time filing by the claimant. Once granted, this exemption remains in effect until terminated or until the property is no longer eligible for the exemption.

In Santa Cruz County, institutional exemption claims are processed by the chief deputy assessor for administration and an auditor-appraiser aide. The assessor has no formal written procedures for processing exemptions, although staff refer to BOE guidance in the form of advisory letters and Assessors' Handbook Section 267, *Church, Religious, and Welfare Exemptions*, as well as information received in BOE and California Assessors' Association exemption workshops.

The deputy assessor personally makes field inspections of all real property for which a church, religious, or welfare exemption is claimed. For inspections of the larger, more complex properties, she is accompanied by the appraiser assigned to the area where the claimed property is located. For new claims involving only unsecured business property, the deputy assessor relies on telephone contacts to confirm the location and actual operation of the exempt activity.

In 1998 and 1999, the assessor sent appraisal staff into the field to inventory all real property granted a church, religious, or welfare exemption. The staff updated the building records, noted changed uses, and, in some cases, adjusted the percentage of the property eligible for exemption. To obtain updated information on uses of exempted property by other organizations, the assessor includes a *Property Use Report* with annual claim forms sent to church and welfare exemption claimants.

The following table presents the number of properties and the amount of assessed value exempted under the church and religious exemptions for recent roll years:

ROLL YEAR	CHURCH EXEMPTIONS	EXEMPTED VALUE	RELIGIOUS EXEMPTIONS	EXEMPTED VALUE
2005-06	27	\$16,143,729	125	\$50,363,044
2004-05	26	\$15,716,028	127	\$49,601,205
2003-04	28	\$13,876,753	128	\$48,861,520
2002-03	28	\$14,091,298	131	\$51,644,381
2001-02	21	\$10,468,440	124	\$48,957,974

If a claimant for the religious exemption fails to return the annual religious exemption termination notice, the assessor sends the claimant a letter. If there is no response to the letter, an aide makes contact by telephone to verify continued eligibility for the religious exemption. Occasionally, she will request that the area appraiser review the property in the field.

The assessor properly requires claimants to annually file an affidavit for the church exemption, correctly penalizes late-filed claims, and generally maintains an effective program for administering both church and religious exemptions. We have no recommendations for improvement in this area.

Welfare Exemption

The welfare exemption from local property taxation is available for property owned and used exclusively for qualifying religious, hospital, scientific, or charitable purposes by organizations formed and operated exclusively for those purposes. Both the organizational and property use requirements must be met for the exemption to be granted.

The welfare exemption is co-administered by the BOE and county assessors. Effective January 1, 2004, the BOE became responsible for determining whether an organization itself is eligible for the welfare exemption and for issuing *Organizational Clearance Certificates (OCCs)* to qualified nonprofit organizations. Additionally, the assessor became responsible for determining whether the use of a qualifying organization's property is eligible for exemption and for approving or denying exemption claims.

The assessor may not grant a welfare exemption on an organization's property unless the organization holds a valid OCC issued by the BOE. The assessor may, however, deny an exemption claim, based on non-qualifying use of the property, notwithstanding the claimant's possession of a valid BOE-issued OCC.

The following table summarizes the welfare exemptions granted on the local assessment roll for recent years:

ROLL YEAR	WELFARE EXEMPTIONS	EXEMPTED VALUE
2005-06	558	\$508,840,694
2004-05	598	\$510,742,498
2003-04	570	\$461,654,788
2002-03	502	\$445,521,836
2001-02	432	\$318,536,976

We reviewed a variety of welfare exemption claims on file at the assessor's office. The claims involved such diverse uses as a religious school, a museum, youth organizations, a senior citizens' center, a summer camp, churches, low-income rental housing, a religious retreat, and a residential drug treatment center. We found that the assessor requires an OCC from each claimant, consistently applies late-filing penalties, and correctly allocates exempt and taxable areas of properties receiving partial exemptions.

We found two incorrect practices in the assessor's welfare exemption program.

RECOMMENDATION 3: Revise welfare exemption procedures by: (1) verifying that exempted property is exclusively used for qualifying purposes, and (2) limit exemption amounts for late-filed claims in accordance with section 270.

Verify that exempted property is exclusively used for qualifying purposes.

We noted several annual claims approved for the 2005-06 roll in which the claimant either did not submit required supplemental affidavits or reported apparently disqualifying uses of the exempt property by the claimant or other groups.

Some of these uses would disqualify a portion of the land and buildings for the welfare exemption because they render the claimed property not exclusively used for religious, scientific, or charitable purposes by a qualifying organization. Others may be within the scope of the welfare exemption, but the exemption may not be granted unless the owner provides the necessary documentation for these uses or, in the case of other groups using the exempted property, unless a qualifying operator also files a proper claim for exemption and meets all the requirements of section 214. Assessors' Handbook Section 267, *Church, Religious, and Welfare Exemptions*, specifies that both qualifying ownership and qualifying use, both by the owner and by any other users of the property, are essential elements of the welfare exemption.

The assessor should carefully review all annual filings for the welfare exemption and investigate any reports that the owner uses the property for commercial purposes or staff housing or leases the property to any other groups. Neglecting to do so could lead to unwarranted exemption of taxable property.

Limit exemption amounts for late-filed claims in accordance with section 270.

When a claimant for the welfare exemption files after the annual February deadline, the assessor allows only a percentage exemption of 85 or 90 percent, depending upon when the claim form is filed. The assessor applies this reduced exemption amount to each parcel of real property or unsecured business property account for which the qualifying organization has claimed the exemption. The effect is that the late-filing penalty enrolled in some cases exceeds \$250 in total, and in other cases exceeds \$250 per parcel or account.

Section 270(a) provides that late-filed claims for the welfare exemption (and several other types of exemptions) may be allowed at 90 percent of the full exemption if the claim is filed after February 15 but before the following January 1 lien date, and 85 percent if the claim is filed after the following lien date. Section 270(b) limits the total penalty in taxes for late filing to a maximum of \$250.

This penalty is to be applied to the exempt organization as a whole, not to each property included in the welfare exemption claim. Assessors' Handbook Section 267, *Church, Religious, and Welfare Exemptions* (October 2004), provides on page 110 of Part I: "The \$250 should not be based on each parcel in a claim, or on each claim if there is more than one claim, but on the claimant's total property that is exempt in the county."

By not limiting the late-filing penalty to a maximum of \$250 in taxes, whether the claim involves a single location or multiple locations, the assessor is not properly applying the penalty limitations of section 270.

Assessment Forms

Government Code section 15606 requires the BOE to prescribe the use of all forms for the assessment of property for taxation.⁶ For the 2005 lien date, the BOE prescribed 79 forms for use by county assessors and one form for use by county assessment appeals boards. Generally, the assessor may not change, add to, or delete the specific wording in a prescribed form. The assessor may, however, rearrange information on a form, provided that the assessor submits such form to the BOE for review and approval. Assessors may also use locally-developed forms to assist them in their assessment duties. However, such forms may not be used as substitutes for BOE-prescribed forms that are required to be used, and no penalty may be imposed upon a property owner for failure to file such form or questionnaire.

To enforce the use of prescribed forms the BOE annually requires assessors to specify in writing the forms they will use in the succeeding assessment year. Assessors are also required to submit to the BOE copies of the final prints of all prescribed forms they intend to use.

⁶ Also sections 480(b), 480.2(b), 480.4, and rules 101 and 171.

A review of the forms used by the Santa Cruz County Assessor's Office for the year 2005-06 revealed the following:

- Of the 79 BOE-prescribed forms, the assessor used 57.
- Of those 57 forms used, the assessor rearranged 9 forms, but either did not submit them for BOE approval or submitted them after the regulatory deadline.
- The final prints of the property statements were not submitted to the BOE in a timely manner.
- Five property statement final prints were returned to the assessor for correction, but the assessor failed to correct and return them to the BOE.

We also reviewed locally-developed forms, letters, questionnaires, and notices. The following changes would improve the program.

RECOMMENDATION 4: Revise assessment forms procedures by: (1) using only approved assessment forms, (2) using only BOE-prescribed forms, and (3) timely submitting the final prints of all assessment forms to the BOE.

Use only approved assessment forms.

The assessor uses eight unapproved, rearranged BOE-prescribed forms. The assessor combined Forms BOE-266-CD, (*Claim for Homeowners' Property Tax Exemption*), and BOE-266-SCD, (*Spanish Version, Claim for Homeowners' Exemption*) into one form, and did not return corrected Forms BOE-260, (*Certificated and Affidavit for Exemption of Work of Art*), BOE-260-A, (*Certificate and Affidavit for Exemption of Certain Aircraft*), BOE-260-B, (*Claim for Exemption from Property Taxes of Aircraft of Historical Significance*), BOE-267-A, (*Claim for Welfare Exemption*) and BOE-269-AH (*Claim for Veterans' Organization Exemption*) for final approval.

In addition, Forms BOE-571-L, *Business Property Statement*, and BOE-571-D, *Supplemental Schedule of Monthly Acquisitions and Disposals*, were rearranged but not indicated as such on the required forms checklist; Form BOE-571-A, *Agricultural Property Statement*, includes unapproved additional instructions, and the assessor printed a supplemental questionnaire on the reverse side of Form BOE-576-E.

Rule 171(a) provides that the assessor may rearrange BOE-prescribed forms, but he or she may not add to or delete any part of the form. Rule 171 also provides that the assessor must notify the BOE annually of those BOE-prescribed forms he or she will use and that a copy must be submitted to the BOE for approval.

Use only BOE-prescribed forms.

The assessor developed alternative forms which are not approved by the BOE. For example, the assessor uses a Property Transfer Questionnaire (PTQ) in lieu of Form BOE-502-AH, *Change of Ownership Statement* (COS). This form differs in several areas:

- The title is *PROPERTY TRANSFER QUESTIONNAIRE*.
- The addition of internal tracking and processing data fields.
- The application of a penalty for noncompliance with their PTQ.

Section 480 requires a transferee to file a COS with the assessor whenever a change in ownership of real property occurs. The format is prescribed and cannot be altered without BOE approval.

The assessor's practice is contrary to specific statutory requirements in section 480. This form is not the BOE-prescribed form referred to in that section. Also, the form contains penalty language for failure to file the PTQ. Penalties may not be applied through the use of any forms that are not BOE-prescribed.

Also, section 452 provides that the BOE shall prescribe the content of property statements for assessors' use. Where the BOE has developed and prescribed specific property statements for use in reporting information about various types of property, the assessor must use these forms, not locally-developed versions.

Timely submit the final prints of all assessment forms to the BOE.

The assessor was late in submitting the final prints of the 2005 property statements to the BOE. Our review of the forms for the years 2002 and 2004 revealed that the assessor also submitted these forms late, and, in the case of the year 2003, the assessor did not submit the final prints at all.

Government Code section 15606(d) provides the BOE prescribe forms to be used by assessors for property taxation purposes. As a result, the BOE instituted procedures for the approval of assessment forms. These procedures are intended to standardize assessment forms for the benefit of taxpayers statewide. The assessor's participation and compliance are mandatory.

ASSESSMENT OF REAL PROPERTY

The assessor's program for assessing real property includes the following principal elements:

- Revaluation of properties that have changed ownership.
- Valuation of new construction.
- Annual review of properties that have experienced declines in value.
- Annual revaluations of certain properties subject to special assessment procedures, such as property subject to California Land Conservation Act contracts, taxable government-owned property, and property in Timberland Production Zones.

Article XIII A of the California Constitution provides that, absent post-1975 new construction or changes in ownership, the taxable value of real property shall not exceed its 1975 full cash value, adjusted annually for inflation by a factor not to exceed 2 percent.

Change in Ownership

Section 60 defines change in ownership as a transfer of a present interest in real property, including the beneficial use thereof, the value of which is substantially equal to the value of the fee simple interest. Sections 61 through 69.5 further clarify what is considered a change in ownership and what is excluded from change in ownership for property tax purposes. Section 50 requires the assessor to establish a base year value for real property upon a change in ownership; a property's base year value is its fair market value on the date of change in ownership.

Discovery and Document Processing

The assessor's primary means of discovering properties that have changed ownership is the review of deeds and other documents recorded with the county recorders' office. Pursuant to section 480.3, the recorder's office requires that Form BOE-502-A, *Preliminary Change of Ownership Report* (PCOR), accompany documents that evidence a transfer of ownership of real property. A \$20 fee is added to the recording fee when a PCOR does not accompany such a document.

All deeds are electronically scanned into the recorder's database by legal document examiners. PCORs are batched daily and forwarded to the assessor's office, where an assessment clerk scans and indexes them.

Because the assessor is also the recorder, cooperation between the two offices is excellent. The assessor's interface program retrieves deeds, PCORs, and other transfer-related documents from the recorder's system. An assessment technician selects a recording date and processes all documents retrieved by the program. The technician then analyzes the recorded document to determine the percentage of ownership transferred, if any, and whether the document represents a reappraisable event.

When a document is received without a PCOR, the technician electronically flags the file. The system sends Form BOE-502-AH, *Change of Ownership Statement (COS)*, on a weekly basis to those buyers of the property. A COS is also sent when there is insufficient or incomplete information on the PCOR.

We reviewed the files for several properties recently valued by the assessor for changes in ownership and found that the assessor establishes the correct base year, adheres to the presumption in Rule 2 that the sale price reflects the full cash value of the property, and uses reasonable appraisal techniques. He also correctly values partial interest transfers, applies the annual inflation adjustment, and enrolls supplemental assessments.

Document Processing

The assessor received 18,055 recorded deeds pertaining to 20,541 parcels transferred for the 2004 calendar year. Generally, the time period for processing documents is about six to eight weeks, with an additional six weeks for transfers needing additional documentation.

The number of recorded deeds reviewed during the period 2000-04 is as follows:

CALENDAR YEAR	RECORDED DEEDS
2004	18,055
2003	20,495
2002	17,567
2001	15,127
2000	14,639

Homeowners' exemptions are automatically removed following a change in ownership. Partial transfer deeds for properties with this exemption are directed to the exemptions staff to determine if the exemption should be retained. When a valuation notice is sent to a new homeowner, a homeowners' exemption claim is included in the mailing.

Section 63.1 Exclusion

Section 63.1 excludes from the definition of change in ownership the purchase or transfer of principal residences and the first \$1 million of other real property between parents and children. Certain transfers between grandparents and grandchildren are also excluded.

Information and claim forms regarding section 63.1 are available both at the assessor's public counter and on the assessor's website. The transfer staff submits the quarterly reports as requested by the BOE. In calendar year 2005, the assessor processed 1,081 claims; in 2004 there were 757; and in 2003 there were 776.

We found that section 63.1 applications are properly processed and that this program fully complies with the provisions of section 63.1.

Section 69.5 Base Year Value Transfers

Section 69.5 generally allows for the transfer of the base year value of a principal residence to a replacement residence of equal or lesser value, provided the property owner is at least 55 years of age, files a timely claim, and the properties are within the same county. The transfer staff submits the quarterly reports to the BOE as required by section 69.5(b)(7). The following table shows the number of section 69.5 claims processed for the period 2002-05. The 2005 count is incomplete as some claims were still in process at the time of our field work.

CALENDAR YEAR	SECTION 69.5 CLAIMS
2005	47
2004	98
2003	56
2002	47

We found that section 69.5 claims are properly processed and that this program fully complies with section 69.5.

Section 408.1 Transfer Lists

Section 408.1 requires the assessor to maintain a list, available to the public, showing property transfers that have occurred within the preceding two years. The list must be divided into geographical areas and must include the transferor and transferee, if available, assessor's parcel number, address of the transferred property, date of transfer, date of recording and recording reference number, and the consideration paid if known by the assessor.

In Santa Cruz County, the assessor updates the transfer list at the end of every month. This list, which is indexed by assessor's parcel number and shows transfers for the last three years, properly excludes information taken from change of ownership statements. It is available at the public counter during business hours. The assessor's transfer list meets all the requirements of section 408.1.

Legal Entity Ownership Program (LEOP)

Section 64 provides that certain transfers of ownership interests in a legal entity constitute a change in ownership of all real property owned by the entity and its subsidiaries. Rule 462.180 interprets and clarifies section 64, providing examples of transactions that either do or do not constitute a change in entity control and hence either do or do not constitute a corresponding change in ownership of the real property owned by the entity. Discovery of these types of changes in ownership is difficult for assessors because ordinarily there is no recorded notice of the real property transfer.

To help assessors, the BOE's LEOP unit investigates and verifies changes in entity control and ownership reported by legal entities, transmitting to each county a listing, with corresponding property schedules, of legal entities that have reported a change in control under section 64(c) or

section 64(d). However, many of the acquiring entities do not provide information sufficient to identify the real property. Because of the limited data provided by many entities, assessors should independently research each entity's property holdings to determine whether all affected parcels have been identified and properly reappraised.

We reviewed the assessment of properties owned by eight legal entities reported to the assessor as having experienced a change in control. We found that the assessor took appropriate action in reviewing and reappraising the real property parcels acquired by these entities, and that the staff processes LEOP transfers in a timely manner.

Direct Enrollment Program

Direct enrollment is a program used by many assessors to streamline the processing of simple transfers of residential properties. In Santa Cruz County, the assessor's direct enrollment program is used only to enroll qualifying single-family residences and condominiums. For the 2004 calendar year, approximately 1,953 transfers were enrolled through this program. Direct enrollment involves computer analysis of any residential transfers that have been entered by the appraisal staff for confirmed sales that conform to specific criteria. Among the parameters that a property must meet to qualify for direct enrollment are:

- The transfer must involve a 100 percent interest,
- The deed must show a documentary transfer tax based on the full sale price, and
- The PCOR-reported sale price must be within \$5,000 of the sale price indicated by the documentary transfer tax.

If a transferred property is not eligible for direct enrollment, it is assigned for review as part of the appraisal workload.

We reviewed a number of transfers in three different subdivisions and found the processing for these assessments consistent with parameters of the assessor's direct enrollment program and statutory provisions.

Improvement Bonds

Improvement bonds are instruments used to finance construction of public improvements that generally enhance the land value of privately owned real property. Improvements often financed using improvement bonds include sewers, sidewalks, lighting, and water lines. Land directly benefiting from such improvements is pledged as security for repayment of the construction loan. The improvement bond is a lien that runs with the land and binds the owner and all successors in interest in accordance with 1911, 1913, or 1915 Bond Acts.

Section 110(b) provides a rebuttable presumption that the value of improvements financed by bonds is reflected in the purchase price paid for a property exclusive of the bond amount. The assessor can overcome this presumption by a preponderance of evidence.

The assessor has determined that there is no evidence in the marketplace to justify the addition of bond amounts to sale prices and consequently does not add unpaid bond balances to nominal selling prices. This is consistent with the requirements of section 110(b).

Resident-Owned Mobilehome Parks (ROP)

Sections 62.1 and 62.2 exclude certain transfers of mobilehome parks from change in ownership if the park is ultimately purchased by at least 51 percent of the tenants renting the individual spaces in the park. Conversion to resident ownership under these provisions permits the residents of the park to retain the base year value of the previous park owner, rather than triggering a reassessment of the park to current market value. In some instances, prior to a transfer to the residents directly or to an entity owned by the residents, there is an interim transfer of the park to a non-resident-owned entity. This entity helps facilitate the purchase and conversion to an ROP.

In Santa Cruz County, there are currently four ROPs where each owner has a separate legal parcel for his or her residence and owns shared amenities in common. In addition, there are 15 non-parcelized ROPs, where residents own the fee simple interests in their individual spaces and undivided interests in the park's common areas.

Sections 62.1 and 62.2 create three change in ownership exclusions with respect to transfers of parks:

- Transfers to resident-owned entities.
- Transfers of rental spaces to the residents.
- Transfers to non-resident-owned entities.

To qualify for the exclusion from reassessment for transfer from landlord to tenant ownership, residents are required to acquire 51 percent ownership participation within a specified time. Three of the 15 non-parcelized ROPs predate the 1985 legislation providing for the exclusion. The remaining ROPs in Santa Cruz County met or exceeded the participation level in advance of the required deadline.

Since the non-parcelized ROPs with undivided interests do not use recorded deeds to transfer ownership interests, the assessor annually acquires a list of all recent changes in ownership of spaces from park management, including the information required by section 62.1.

Assessors' Handbook Section 511, *Assessment of Manufactured Homes and Parks* (AH 511), contains a section describing the change in ownership assessment procedure for residents' interests in individual spaces in ROPs. AH 511 recommends that if the purchase price was negotiated in the open market at arm's length, then the assessor should enroll the entire amount in the combined assessments of the manufactured home and the space in the ROP. The most reasonable way of allocating the value between the two assessments would be to extract from the purchase price the value of the manufactured home (using a recognized value guide) and then assign the residual amount to the space. This method of allocation will ensure that the market value attributable to the location of the space being transferred within the park is recognized.

In addition, Letter To Assessors 99/87, dated December 31, 1999, recommends that the value of a resident's ownership share of the park should be derived by subtracting the market value of the manufactured home from the combined price paid for the manufactured home and the share or interest in the park. This residual value would be the share value that should be enrolled, not an equalized or average value of the shares or interests transferred that year. The assessor values residents' interests in mobilehome parks by (1) deducting from the sale price the market value of the manufactured home, and (2) allocating the residual amount to the land and the prorata share of common park interests. We found that the assessor correctly values transfers in ROPs.

New Construction

Section 70 defines newly constructed property, or new construction, as (1) any addition to real property since the last lien date; or (2) any alteration of land or improvements since the last lien date that constitutes a major rehabilitation of the property or converts the property to a different use. Further, section 70 establishes that any rehabilitation, renovation, or modernization that converts an improvement to the substantial equivalent of a new improvement, constitutes a major rehabilitation of the improvement. Section 71 requires the assessor to determine the full cash value of newly constructed real property on each lien date while construction is in progress and on its date of completion, and provides that the full cash value of completed new construction becomes the new base year value of the newly constructed property.

Rules 463 and 463.500 clarify the statutory provisions of sections 70 and 71, and Assessors' Handbook Section 502, *Advanced Appraisal*, Chapter 6, provides guidance for the assessment of new construction.

There are several statutory exclusions from what constitutes new construction; section 70(c), (d), and (e), and sections 73 through 74.7 address these exclusions.

Building Permits

Building permits are the assessor's primary means of discovering assessable new construction. Currently, the assessor electronically receives all permits issued from five permit-issuing agencies: the Santa Cruz County Planning Department and the cities of Santa Cruz, Watsonville, Scotts Valley, and Capitola. The permit-issuing agencies code the building permits according to the nature of the work being done, allowing the assessor to quickly cull permits that do not represent assessable new construction. The assessor also disregards permits representing low-valued items that do not add measurable value.

The assessor also discovers new construction during field canvassing by appraisers in their assigned areas, through a review of business property statements, and during reviews of changes in ownership. Any new construction reported on Form BOE-571-L, *Business Property Statement*, is also reported to the real property division for review.

The following is a table indicating the number of permits reported to the assessor by each permit-issuing agency in recent years.

Calendar Year	County of Santa Cruz	City of Santa Cruz	Capitola	Scotts Valley	Watsonville	Total
2005	2,373	1,020	233	251	530	4,407
2004	3,546	1,548	421	389	1,001	6,905
2003	2,115	1,583	336	413	1,074	5,521
2002	n/a	982	316	357	694	2,349
2001	n/a	1,615	385	414	n/a	2,414

The assessor appraises construction in progress as of the lien date, appraises completed new construction as of the date of completion, and applies the appropriate supplemental assessments.

Valuation

While the assessor's office uses all appropriate methods of valuation to estimate the fair market value of new construction, the cost approach is the primary approach used. The assessor sends a construction cost questionnaire for new construction deemed to be assessable new construction. When the replacement cost method is utilized to estimate new construction value, the assessor considers the impact on the remaining economic life of the entire property.

All newly constructed buildings are sketched using Apex software. Either the area appraiser or an appraisal technician is responsible for preparing the sketch and attaching it to the property record.

The base year and base year value are maintained on the property record for each item of new construction. Entrepreneurial profit is added, where appropriate, in the cost approach, but the amount is the responsibility of the individual appraiser to estimate and support.

Declines in Value

Section 51 requires the assessor to enroll on the lien date an assessment that is the lesser of a property's factored base year value or its current full cash value, as defined in section 110. Thus, if a property's full cash value falls below its factored base year value on any given lien date, the assessor must enroll that lower value. If, on a subsequent lien date, a property's full cash value rises above its factored base year value, then the assessor must enroll the factored base year value.

Similar to many other California counties, Santa Cruz County has experienced notable increases in property values in recent years. Consequently, the assessor has removed many properties from decline-in-value status. There are about 160 properties assessed on the 2005-06 roll at values below their factored base year levels.

The assessor has no formal program for discovering declines in value. He depends on taxpayer requests for appraisal review and the appraisers' knowledge of their assigned areas. On occasion, a decline in value may be discovered during a reappraisal of real property that has changed ownership.

When taxpayers question the valuation of their property, the assessor provides a *Request for Reappraisal* form for the taxpayers to complete. This form and an associated pamphlet are available at the public counter or from the assessor's website. In addition, where an appraiser determines, while examining sales, that downward value adjustments are warranted for other properties in the neighborhood, such adjustments can be made without requiring the taxpayers to file the *Request for Reappraisal*.

When returning a property either in whole or in part to its factored base year value under article XIII A of the California Constitution, the assessor's notice to the property owner includes the property's factored base year value, its current market value, and information about assessment appeal procedures. The assessor's notice provides all the information required by section 619.

The assessor annually reviews the assessment of all decline-in-value properties. Properties currently in decline-in-value status are tracked on the assessor's system, allowing staff to print a list of properties needing annual review. Upon review, the appraiser may add value to land only, to improvements only, or to both, depending on the appraiser's judgment of the property's market potential. To determine current market values for comparison purposes, the assessor relies primarily on the income approach for commercial properties and the comparative sales approach for residential properties.

The assessor's decline-in-value program meets all provisions of law, including the treatment of fixtures as separate appraisal units when determining declines in value of business properties.

California Land Conservation Act Property

Pursuant to the California Land Conservation Act (CLCA) of 1965, agricultural preserves may be established by a city or county for the purpose of identifying areas within which the city or county will enter into agricultural preserve contracts with property owners.

Property owners who place their lands under contract agree to restrict the use of such lands to agriculture and other compatible uses; in exchange, the lands are assessed at a restricted value. Lands under contract are valued for property tax purposes by a method that is based upon agricultural income-producing ability (including income derived from compatible uses, e.g., hunting rights and communications facilities). Although such lands must be assessed at the lowest of the restricted value, current market value, or factored base year value, the restricted value typically is the lowest.

Sections 421 through 430.5 prescribe the method of assessment for land subject to agricultural preserve contracts. Assessors' Handbook Section 521, *Assessment of Agricultural and Open-Space Properties*, October 2003 (AH 521), provides guidance for the appraisal of these properties.

On the 2005-06 tax roll, the assessor enrolled 355 parcels encumbered by CLCA and Open Space Easement (OSE) contracts (land designated for nonbuilding uses). There are eight parcels currently in nonrenewal status. The total assessed value for CLCA/OSE properties for 2005-06 was \$133,302,409.

Homesites

Section 428 provides that the restricted valuation standard for CLCA land does not apply to residences or the site of a residence. AH 521 on page II-51 provides that even though it might be highly unlikely or impossible to actually be bought and sold in the marketplace, the homesite must be valued as though they were a separate appraisal unit and traded in that manner. In other words, the homesite must be valued at the lesser of the factored base year value or the fair market value of a comparable homesite. We found that this is the assessor's policy and practice.

Income and Expenses

The income to be capitalized is the economic net income attributable to the land determined, whenever possible, by the analysis of rents received in the area for similar lands in similar use. To determine net income, the appraiser must estimate the future gross income the land can be expected to produce and subtract the allowable cash expenses (except property taxes) necessary to maintain this income. The gross income is primarily from agricultural production, but it also includes income from any compatible uses actually occurring, such as lease payments for oil or gas exploration rights, communication facility sites, and recreational uses such as hunting or fishing. There are no limits placed upon the income to be capitalized unless the contract contains a provision establishing a minimum annual income per acre.

Since the income to be capitalized in the valuation of open-space properties is the net income attributable to the land, the expenses necessary to maintain this income and the portion of the income attributable to improvements must be subtracted from the expected gross income prior to capitalization. The type of expenses deducted, and to some extent the amount of the deductions, will depend upon the composition of the gross income. For example, a gross income derived from cash rents will generally require fewer adjustments than a gross income derived from share rents, and, while a management charge is generally applicable to both income streams, this charge will normally be less in cash rental analysis. In addition to the expenses that are incurred for the creation and maintenance of the income, the property owner is entitled to a fair return on the value of the improvements that are necessary to produce the income and the return of (recapture) the value of such improvements.

Capitalization Rates

Section 423(b) prescribes the composition of the capitalization rate to be used in determining CLCA-restricted land values. It requires that the capitalization rate shall be the sum of the following components:

- An interest component annually determined and announced by the BOE;

- A risk component based on the location and characteristics of the land, the crops to be grown thereon and the provisions of any lease or rental agreement to which the land is subject;
- A component for property taxes; and
- A component for amortization of any investment in perennials over their estimated economic life when the total income from land and perennials other than timber exceeds the yield from other typical crops grown in the area.

In our 2002 survey, we recommended the assessor use a basic 1 percent risk rate and conduct studies to establish rates that reflect the risks for the various types of CLCA land and living improvements. The assessor has partially implemented this recommendation by using a 1 percent risk rate for all CLCA properties, but has not conducted any studies to establish risk rates that recognize differences in property type or uses.

The valuation of CLCA property in Santa Cruz County is the responsibility of one real property appraiser. The appraiser mails CLCA questionnaires annually to the taxpayers and compiles the collected information into a spreadsheet for valuation of CLCA properties.

We noted one weakness in the assessor's CLCA program.

RECOMMENDATION 5: Use an appropriate income stream when valuing restricted vineyards and orchards.

We found that the assessor uses a straight-line declining income premise when appraising vineyards and orchards in all stages of production.

The AH 521 on pages II-38 through II-43 describes the procedure for capitalizing income from trees and vines. The appropriate method depends primarily on the shape of the anticipated income stream. For most vineyard and orchards, the shape of the income stream includes the following three stages: (1) a period of development, when production (income stream) initiates and rises; (2) a period of maturity, when production remains relatively stable; and (3) a period of decline, when production drops as the improvements near the end of their economic lives.

The assessor has no support or documentation for using the straight-line declining income stream over the typical three-stage income stream. Not recognizing the shape of the income stream may result in the undervaluation of trees and vines in early- to mid-life.

Taxable Government-Owned Property

Article XIII, section 3 of the California Constitution exempts from property taxation any property owned by local governments, except as provided in article XIII, section 11. Section 11 provides that land, and improvements thereon, located outside a local government's or local government agency's boundaries are taxable at a restricted value if the property was taxable at the time of acquisition. Improvements that were constructed to replace improvements that were taxable when acquired are also taxable. These lands and taxable improvements are commonly referred to as taxable government-owned properties.

There are 106 taxable government-owned properties assessed in Santa Cruz County on the 2005-06 roll, including parcels owned by various cities and municipal utilities. The total assessed value of taxable government-owned properties on the 2005-06 assessment roll was \$4,253,015.

To verify that all taxable government-owned properties were being assessed, we randomly reviewed properties with a zero roll value to confirm that the properties were either located within that agency's boundaries or were already exempt when acquired by the agency. We found no instances where such properties were unassessed. We did find one problem, however, in the assessor's treatment of taxable government-owned properties.

RECOMMENDATION 6: Assess taxable government-owned properties at the lowest of current fair market value, factored base year value, or restricted value.

The assessor has correctly established the base year value of newly acquired taxable government-owned properties at the lowest of the market value or the restricted value (1967 assessed value times the BOE-announced factor) at the time of acquisition. In each case, the restricted value was lower than the market value at the time of acquisition. However, in years subsequent to the initial enrollment the assessor does not perform a comparison to determine if the factored base year value, current market value, or restricted value is lowest. Instead, each year after acquisition the assessor simply calculates and enrolls the restricted value.

In Letter To Assessors 2000/37, dated June 23, 2000, we advised assessors that taxable government-owned properties are subject to the value limitations of article XIII A of the California Constitution and that therefore it is necessary to annually compare current market value, factored base year value, and restricted value and enroll the lowest indicator. By failing to make this comparison, the assessor risks improper values for taxable government-owned properties.

Timberland Production Zone Property

Lands zoned "Timberland Production Zone" (TPZ) are valued in accordance with special TPZ site classifications; the valuation of such lands excludes the value of any standing timber. The annual value of a TPZ property is determined by its appropriate per-acre site value (section 434.5) plus the lower of the current market value or the factored base year value of any compatible, nonexclusive uses of the property (section 435). Assuming that TPZ lands are not also under CLCA contract, the annual taxable value of TPZ lands is the lowest of (1) the TPZ value, (2) the current market value, or (3) the factored base year value.

The special valuation methods for TPZ lands do not apply to structures on TPZ lands or to reasonable sites for such structures. In other words, structures and the sites directly related to those structures are assessed as all other real property.

As of the 2005-06 lien date, there were 491 parcels zoned TPZ in Santa Cruz County with a total assessed value of nearly \$76 million.

We note one shortcoming in the assessor's TPZ procedures.

RECOMMENDATION 7: Send annual questionnaires to owners of TPZ land requesting information on compatible uses.

Although the assessor correctly assesses exclusive compatible uses such as homesites, residences, and outbuildings, he makes no attempt to systematically canvass TPZ properties to obtain information regarding other compatible uses. During our review of these properties, we found evidence of compatible uses that were not assessed.

Section 435(a) requires the assessor to value TPZ property according to the site value schedules expressed in section 434.5, plus the value of any compatible, nonexclusive uses of land. These uses may include grazing, hunting, camping, mining, and others. The taxable value of these compatible uses must be determined annually and added to the site class values of the TPZ property (see the BOE's *Timber and Timberland Values Manual*, November 2005, pages 32-34).

Once land is zoned TPZ and enrolled as such by the assessor, there is usually very little contact between the assessor and owners of TPZ lands. This creates a discovery problem if there is income to the property from subsequent compatible uses. The assessor could easily remedy this situation by sending out a questionnaire requesting information on compatible uses to the participating TPZ landowners. The assessment of these additional compatible uses will enable the assessor to be in full compliance with section 435(a).

Taxable Possessory Interests

A taxable possessory interest results from the possession, a right to possession, or a claim to a right to possession of publicly owned real property, in which the possession provides a private benefit to the possessor and is independent, durable, and exclusive of rights held by others. The assessment of a taxable possessory interest in tax-exempt publicly-owned property is based on the value of the rights held by the possessor; the value of the rights retained by the public owner is almost always tax exempt.

In Santa Cruz County, there are more than 1,300 taxable possessory interests on the 2005-06 assessment roll. Marina slips at the Santa Cruz Harbor and hangars at the Watsonville Airport that are rented on a month-to-month basis comprise about 80 percent of those interests.

The following table shows a distribution of the taxable possessory interests on the 2005-06 assessment roll.

TYPE	ASSESSMENTS	ASSESSED VALUES
CA Department of Forestry	9	\$217,125
CA Department of Parks and Recreation	63	\$2,194,986
CA Department of Youth Authority	1	\$14,998
Santa Cruz County Fair	4	\$381,774
Soquel Creek Water District	1	\$35,910
Santa Cruz County Parks	6	\$165,800
Santa Cruz County Public Works	18	\$13,305,253
Santa Cruz Port District (including slips)	836	\$16,605,921
City of Capitola	34	\$310,508
City of Santa Cruz	46	\$20,648,135
City of Scotts Valley	4	\$2,823,151
City of Watsonville (including hangars)	250	\$10,342,796
Santa Cruz County Redevelopment Agency	16	\$516,560
Santa Cruz Metropolitan Transit District	11	\$414,526
La Selva Beach Recreation District	1	\$11,400
University of California, Santa Cruz	5	\$113,955
United States Navy	2	\$4,018,725
Pajaro Valley Unified School District	2	\$36,224
Soquel Union School District	1	\$44,104
TOTAL	1,310	\$72,201,851

Two appraisers are responsible for the discovery and assessment of the taxable possessory interests in Santa Cruz County. Annually, the appraisers contact about 20 public agencies with existing taxable possessory interests requesting updated listings of tenants and lease terms.

Our review of the assessor's property files and assessment procedures found areas in the assessor's taxable possessory interest program that should be improved. They are addressed in the following recommendation.

RECOMMENDATION 8: Improve the taxable possessory interest assessment program by: (1) assessing month-to-month taxable possessory interests in compliance with section 61(b)(2); (2) recognizing lessor expenses when valuing taxable possessory interests by the income approach; (3) obtaining copies of all lease agreements that create taxable possessory interests; and (4) assessing property in a redevelopment project in compliance with Health and Safety Code section 33673.

Assess month-to-month taxable possessory interests in compliance with section 61(b)(2).

We found that the assessor revalues month-to-month taxable possessory interests on an annual basis rather than at the end of the reasonably anticipated term of possession used to establish the value. For these interests, the assessor updates the income to current economic rent each year and uses a three- or four-year term of possession.

Section 61(b)(2) provides that a renewal of a taxable possessory interest during the reasonably anticipated term of possession used by the assessor to value that interest does not cause a change in ownership until the end of that term. By revaluing month-to-month taxable possessory interests annually, the assessor has revalued property that has not undergone a statutory change in ownership. The result is that increases in the assessed values for these interests may exceed the 2 percent annual maximum allowed by article XIII A of the California Constitution.

Recognize lessor expenses when valuing taxable possessory interests by the income approach.

When utilizing the income approach to value taxable possessory interests, the assessor capitalizes the estimated economic rent without making any deductions for management or other operating expenses incurred by the public lessor.

Rule 21(e)(3)(A) prescribes how the direct income approach is to be applied when valuing taxable possessory interests. In the direct income approach, the amount to be capitalized is the future net income that the taxable possessory interest is capable of generating under typical management during the anticipated term of possession. Rule 8(c) provides that it is appropriate to reduce a lessor's rental income for typical management and other operating expenses incurred by the lessor. The written agreement creating the taxable possessory interest should be reviewed to determine which specific expenses pertain, while typical expenses such as management charges should also be recognized.

The assessor does not recognize any operating expenses incurred by the public owner. Failing to recognize appropriate lessor expenses may result in an overstatement of the full cash value of a taxable possessory interest.

Obtain copies of all lease agreements that create taxable possessory interests.

We found that the assessor does not obtain copies of contracts for taxable possessory interests where the rights to use of the public property were conveyed through written contract. We

discovered contract terms that were not considered in the valuation of the rights conveyed by the contracts. Following are a few such terms:

- The rent was based on the gross income from the premises in excess of the sum of the tenant's operating costs, loan amortization, and return on the tenant's equity investment; thus, the annual rent for the preceding year reported by the public agency was not reflective of market rent.
- All four renewal option periods were included in the term of possession used to value the taxable possessory interest, but the contract included limiting conditions that probably would have been considered of sufficient impact so as to negate inclusion of all four renewal periods.
- In a ground lease, the tenant was responsible for construction of the improvements, but the improvements were considered to be owned by the landlord upon expiration or termination of the contract.
- The landlord was responsible for a portion of the building maintenance including the exterior walls, roof, as well as some plumbing and sewage services to the building.
- The landlord and tenant agreed to share the cost of the replacement of the heating and ventilation system.

Rule 21 describes the various approaches to value and how to determine the term of possession for the valuation of taxable possessory interests. For example, subsection (d) explains that the stated term of possession is deemed the reasonably anticipated term of possession except in certain situations, and subsection (e)(3)(C) explains how to determine the net operating income for capitalization purposes. These steps in the valuation process cannot be completed with any validity if the contract conveying the taxable possessory interest is not reviewed.

The reports submitted annually to the assessor by government agencies that lease property to others provide some information, but they are not adequate substitutes for the actual leases. Unconfirmed data provided in summary reports may be inaccurate or incomplete and lead to incorrect assessments. All contracts and subsequent amendments should be reviewed by the assessor to ascertain all terms that affect the valuation of the rights conveyed by the lease.

Assess property in a redevelopment project in compliance with Health and Safety Code section 33673.

The assessor values only the right of the lessee (namely, the restricted rights) when assessing taxable possessory interests in property owned by a city redevelopment agency that has been redeveloped through a joint venture between the lessor and a tenant. As discussed below, this property should be assessed as other fee-owned property. (See Assessors' Handbook Section 510, *Assessment of Taxable Possessory Interests*, December 2002, pages 75-76.)

Section 33673 of the Health and Safety Code provides that, whenever property in any redevelopment project has been redeveloped and is leased by the redevelopment agency to any person or persons or is leased to a party for redevelopment, the property shall be assessed and

taxed in the same manner as privately-owned property. The assessor's practice has resulted in underassessments.

Leasehold Improvements

Leasehold improvements are all improvements or additions to leased property that have been made by the tenant or lessee. Such improvements can be secured to the real property or assessed to the lessee on the unsecured roll.

Commercial, industrial, and other types of income-producing properties require regular monitoring by the assessor because, as tenants change over a period of time, they may add and remove improvements that may result in a changed use of the property. These changes must, by law, be reflected in the property's assessment if they qualify as new construction.

When real property is reported on Form BOE-571-L, *Business Property Statement*, coordination between the real property and business property divisions of the assessor's office is important. The reported cost should be examined by both an appraiser in the real property division and an auditor-appraiser in the business property division. The divisions should determine the proper classification of the property to ensure appropriate assessment by each division and avoid escapes and double assessments.

The Santa Cruz County Assessor's Office does not have written procedures for the assessment of leasehold improvements. However, there is an established procedure for sharing information between the real property and business property divisions. Under this procedure, which is in place to prevent double assessments and escaped assessments, the real property division uses a *Structural Improvement Memo* (STIM) to alert the business property division when a new permit is reviewed and action is taken. Additionally, the business property division sends copies of Forms BOE-571-L and BOE-571-D to the real property division when these property statements show expenditures for structural leasehold improvements that should be assessed on the secured account.

The real property division determines whether the reported items are real or personal property. If it is a real property item, then it determines whether the costs (1) are already included in the improvement value, (2) are an expense item and therefore should not be included, or (3) should be assessed as new construction. If it is a personal property item, the real property division sends a STIM to the business property division.

The business property division is responsible for assessing unsecured leasehold improvements classified as fixtures.

Discovery

The primary discovery tools for leasehold improvements are Form BOE-571-L, building permits, field checks, and bulk transfer notices. All costs reported on the BOE-571-L and BOE-571-D are investigated when the audit is conducted.

Valuation

Structural items are classified as real estate and assessed at the lower of their factored base year value or current market value. Leasehold improvements are assessed to the lessee except when there exists a documented agreement between lessor and lessee to do otherwise. When leasehold improvements are abandoned, the business property division deactivates the account and notifies the real property division, which determines whether the leasehold improvements should be added to the lessor's secured account. Supplemental assessments are applied to structural leasehold improvements on both the secured and unsecured rolls.

We found no problems with the assessment of leasehold improvements.

Water Company Property

Taxable water company property may include the property of private water companies, mutual water companies, and some property of government-owned water systems. Each type of water company property presents different assessment issues.

We obtained lists of all water supply sources from three public agencies: the California State Department of Health Services' Branch of Drinking Water Field Operations, the California Public Utilities Commission (CPUC), and the County of Santa Cruz Health Services Agency. The table below is a list of the types of water companies assessed by the assessor's office:

TYPE	WATER COMPANIES	ASSESSED VALUES
CPUC Regulated	2	\$626,136
Mutual	28	\$178,595
Municipal (section 11)	2	\$38,207
Unregulated private	42	\$11,633,822

Our review of the assessor's property files and assessments found areas in the assessor's program that should be improved.

RECOMMENDATION 9: Improve the assessment of water company properties by: (1) ensuring that mutual water system property is not double assessed, and (2) identifying and properly assessing all regulated water companies.

Ensure that mutual water system property is not double assessed.

Our search of properties coded as mutual water companies revealed several parcels that were incorrectly assessed. The assessor's procedures instruct appraisers to consider the value of water system improvements to be reflected in the land value of the parcels served by the water company, but they neglect to mention the same for land owned by the water company. Assessors' Handbook Section 542, *Assessment of Water Companies and Water Rights* (AH 542), on page 18

provides that appraisers must recognize that the value of the mutual water company is included in the value of the land that it serves.

We found some situations where the assessor enrolled assessments for land owned by the mutual water company. If the assessor assesses land owned by the mutual water company and enrolls the sales price of the properties served by the mutual water company, double assessments may result.

Identify and properly assess all regulated water companies.

We found one CPUC-regulated water company that was not assessed by the assessor. In addition, we found that the assessor does not develop a historical cost less depreciation (HCLD) indicator as recommended by AH 542. Finally, we noted that the assessor does not enroll the lowest of the HCLD, the factored base year value, or the current market value of regulated water companies. These erroneous practices could result in incorrect assessments.

ASSESSMENT OF PERSONAL PROPERTY AND FIXTURES

The assessor's program for assessing personal property and fixtures includes the following major elements:

- Discovery and classification of taxable personal property and fixtures.
- Mailing and processing of annual property statements and questionnaires.
- Annual revaluation of taxable personal property and fixtures.
- Auditing taxpayers whose assessments are based on information provided in property statements.

In this section of the survey report, we review the assessor's audit, business property statement processing, business equipment valuation, leased equipment discovery and assessment programs, and the assessment of manufactured homes, aircraft, and vessels.

Audit Program

A comprehensive audit program is essential to the successful administration of any tax program that relies on information supplied by taxpayers. A good audit program discourages deliberate underreporting, educates those property owners who unintentionally misreport, and provides the assessor with additional information to make fair and accurate assessments.

The following table shows the total number of audits completed for recent years:

FISCAL YEAR	2004-05	2003-04	2002-03	2001-02	2000-01
Audits Workload Per Year:					
Mandatory	52	65	43	46	53
Nonmandatory	22	32	46	42	43
Total Audits Scheduled	74	97	89	88	96
Audits Carried Over from Prior Year	20	21	33	29	29
Total Audit Workload	94	118	122	117	125
Audits Completed:					
Mandatory	72	67	68	45	53
Nonmandatory	22	31	33	39	43
Total Audit Completed	94	98	101	84	96
Audits Carried Forward					
Mandatory	0	20	21	33	29
Nonmandatory	0	0	0	0	0
Total Audits Carried Forward	0	20	21	33	29

The following table categorizes the results of mandatory audits completed during recent years:

FISCAL YEAR	ESCAPES	REFUNDS	NO CHANGE	TOTAL
2004-05	21	15	36	72
2003-04	19	19	29	67
2002-03	21	12	35	68
2001-02	11	15	19	45
2000-01	18	12	23	53

The following table categorizes the results of nonmandatory audits completed during recent years:

FISCAL YEAR	ESCAPES	REFUNDS	NO CHANGE	TOTAL
2004-05	12	4	6	22
2003-04	14	7	10	31
2002-03	13	10	10	33
2001-02	22	5	12	39
2000-01	16	15	12	43

Mandatory Audits

Pursuant to section 469, audits are mandatory for taxpayers reporting business tangible personal property and trade fixtures valued at \$400,000 or more.

We reviewed the audit procedures and the forms used for audits and found that they are acceptable.

In our 2002 survey report, we recommended that the assessor complete all mandatory audits as required by section 469. Our review of the mandatory audit program indicated that all mandatory audits due for fiscal year 2004-05 were completed. There were 72 mandatory audits completed in fiscal year 2004-05 and 233 mandatory audits completed during the preceding four years. The assessor has an effective mandatory audit program.

Nonmandatory Audits

A nonmandatory audit program serves several purposes in the assessment of personal property. Besides helping to mitigate taxpayer reporting errors, a nonmandatory program also allows for the investigation and resolution of special problems uncovered during the processing of property statements.

The assessor completed 22 nonmandatory audits in fiscal year 2004-05 and 146 audits during the preceding four years.

Statute of Limitations

Section 532 provides that when the assessor discovers through an audit that property has escaped assessment, an assessment of such property must be enrolled within four years after July 1 of the assessment year during which the property escaped assessment. If the assessor cannot complete an audit within the prescribed time, the assessor may request, pursuant to section 532.1, a waiver of the statute of limitations from the taxpayer to extend the time for making an assessment.

In our 2002 survey report, we recommended that the assessor obtain a signed waiver of the statute of limitations when a mandatory audit will not be completed on time. Our current review of the audit program indicated that all scheduled audits were timely completed. Additionally, the

assessor has changed his procedures so that if an audit cannot be completed timely, he requests a waiver from the taxpayer.

Audit Quality

An audit should follow a standard format so that the auditor-appraiser may easily determine whether the property owner has correctly reported all taxable property. Audit narratives and summaries should include adequate documentation, full value calculations, reconciliation of the fixed assets totals to the general ledger and financial statements, review of asset invoices, reconciliation between reported and audit amounts, an analysis of expense accounts, and an analysis of depreciation and obsolescence factors that may affect the value of the business property.

We found that the assessor performs change in control (ownership) reviews, verifies leased equipment ownership, enrolls construction in progress, accounts for supplies, and properly classifies equipment, among other things. In all cases, both mandatory and nonmandatory audits were supported by an audit checklist defining the areas of investigation. However, we found a problem with the way the assessor handles offsets of value differences across audit years.

RECOMMENDATION 10: Offset tax liabilities for escape assessments against refunds due for reductions in value only within the same tax year.

We found that the assessor offsets an escape assessment of one year of an audit against reductions in value for other years in the same audit period.

Section 533 provides that tax liabilities for escape assessments for one assessment year should be offset only against refunds in taxes for the same year. The assessor has no authority to offset escaped assessments in one year with reduced assessments in another year. In addition, section 506 provides that the tax rate applicable shall be that tax rate to which the property would have been subject if it appeared upon the affected roll year. By offsetting the assessments before the application of the tax rate for each year, the net tax liability for the entire audit period is incorrect.

Business Property Statement Program

Section 441 requires each person owning taxable personal property (other than a manufactured home) having an aggregate cost of \$100,000 or more to annually file a property statement with the assessor; other persons must file a property statement if requested by the assessor. Property statements form the backbone of the business property assessment program. Several variants of the property statement address a variety of property types, including commercial, industrial, and agricultural property, vessels, and certificated aircraft.

Auditor-appraisers process all business property statements. They carry out all statement processing functions under the direct control of the chief auditor-appraiser. Only certified staff determine the correct input of reported costs from business property statements. Additionally, certified auditor-appraisers check for full disclosures of property based on a taxpayer's prior year's statement and reconcile any differences during processing. Statements with fixtures

reported on Schedule B of the business property statement are forwarded to the real property section, when appropriate.

The following table displays the assessor's workload of property statements for businesses, leased equipment, and other property types for the 2004-05 assessment roll.

CATEGORY	TOTAL COUNT	SECURED VALUE	UNSECURED VALUE	TOTAL VALUE
Agriculture	156	\$3,464,409	\$9,465,140	\$12,929,549
Apartments	727	\$5,001,439	\$36,800	\$5,038,239
Financial	79	\$510,710	\$9,297,969	\$9,808,679
Gen. Business	6,070	\$269,570,121	\$558,317,254	\$827,887,375
Leased Equip.	823	0	\$56,172,956	\$56,172,956
Service Stations	81	\$7,469,692	\$5,080,760	\$12,550,452
Other	3,600	0	\$157,601,517	\$157,601,517
Total	11,536	\$286,016,371	\$795,972,396	\$1,081,988,767

We noted a problem with the assessor's use of incorrect forms. The issue of using incorrect forms is discussed in more detail under the Assessment Forms topic.

Discovery

The assessor has an efficient discovery program. Taxpayer self-reporting and annual canvassing are the principal means of discovering assessable property. Other means of discovery include reviewing fictitious business name filings, newspaper articles and advertisements, city and county business licenses, referrals from other counties, and BOE notifications. Our survey indicates that the assessor's office employs effective methods to discover taxable business property.

Direct Billing

Many California assessors utilize an assessment procedure called "direct billing" or "direct assessment." It is a method of assessing lower-value business property accounts without the annual filing of a business property statement. The assessor establishes an initial value and continues it for several years. Property statement filings or field reviews are periodically required. Examples of businesses suitable for direct billing include apartments, barber shops, beauty parlors, coin-operated laundrettes, small cafes and restaurants, and professional firms with small equipment holdings.

The direct billing program is beneficial to the taxpayer and the assessor. It results in a reduction of paperwork for taxpayers and fewer business property statements that must be processed annually by the assessor's staff, increasing time available for the auditor-appraisers to perform other required duties.

The Santa Cruz County Assessor utilizes such a program. The accounts that are direct-billed are generally stable and less than \$30,000 in full cash value of reportable business property. Every four years the assessor sends a business property statement to direct-billed taxpayers to determine if there have been any substantial changes of business property, including increased equipment, decreased equipment, sale of the business, any change in ownership, or a change in location.

The assessor then decides whether the account is still suitable for direct billing. If not, he converts the account back to a regular account and resumes yearly business property statement mailings. For fiscal year 2005-06, the assessor direct billed 4,489 accounts.

Business Equipment Valuation

Commercial, Industrial, and Agricultural Equipment

Assessors value most machinery and equipment using business property value factors. Value factors are derived by combining price index factors (trend factors) with percent-good factors. A value indicator is obtained by multiplying a property's historical (acquisition) cost by an appropriate value factor.

Section 401.5 provides that the BOE shall issue information that promotes uniformity in appraisal practices and assessed values. Pursuant to that mandate, the BOE annually publishes Assessors' Handbook Section 581, *Equipment Index and Percent Good Factors* (AH 581).

The proper selection and application of valuation factors applied to historical cost produces an estimate of market value. The BOE annually publishes equipment index factors and percent good factors in the AH 581. This handbook is useful to the assessor in the valuation of business property and trade fixtures. The equipment index factors measure the annual trended values of equipment with normal service lives. The percent good factors reflect the average loss in value that commercial or industrial equipment will suffer over its service life.

The assessor codes the business property accounts using Business Classification Codes. We reviewed the written procedures dealing with business property valuation and found them to be in order.

The following table displays the assessor's current secured and unsecured business property assessments assessed on the 2005-06 assessment roll:

2005-06 Assessment Roll						
CATEGORY	SEC.	ASSESSED VALUE	UNSEC.	ASSESSED VALUE	TOTAL	ASSESSED VALUE
Commercial	1,192	\$282,551,962	6,588	\$628,905,739	7,780	\$911,457,701
Agricultural	65	\$3,416,548	91	\$9,513,001	156	\$12,929,549
Vessels	0	0	1,876	\$40,287,521	1,876	\$40,287,521
4% Vessels	0	0	32	\$979,774	32	\$979,774
General Aircraft	0	0	311	\$38,639,109	311	\$38,639,109
TOTAL	1,257	\$285,968,510	8,898	\$718,325,144	10,155	\$1,004,293,654

The Santa Cruz County Assessor adopted the price indices and percent good factors recommended by the California Assessors' Association (CAA). The price indices generally parallel the indices published in AH 581.

Computer Valuation

Pursuant to section 401.5, the BOE also issues valuation factors for computer equipment (see AH 581, Table 7: Computer Valuation Factors).

We found the assessor has adopted the CAA percent good factor tables except for the minimum percent good on certain life tables. The CAA factors for computer equipment agree with those found in AH 581. Except for older equipment, the assessor's percent good factors are similar to the factors found in the AH 581.

Leased Equipment

The business property division is responsible for the discovery, valuation, and assessment of leased equipment. This type of property is one of the more difficult to assess correctly. Common problems include difficulty in establishing taxability and taxable situs, reporting errors by lessees and lessors, valuation (whether the value of the equipment should be the lessor's cost or the cost for the consumer to purchase), and double assessments or escape assessments resulting from lessor and lessee reporting. These issues are discussed in detail in Assessors' Handbook Section 504, *Assessment of Personal Property and Fixtures*.

The assessor has the responsibility to discover and assess all taxable leased equipment located within his county. Lessees of leased equipment are required to report all leased equipment, that is, taxable property in their possession but belonging to others, on the annually filed business property statement. On the statement, the assessor requests the name and address of the owner, the month and year of property acquisition, the acquisition cost, the location, and other relevant information.

When the lessee reports leased equipment on the business property statement, the assessor updates the lessor's property file to identify the lessee. This ensures that the lessor and lessee account files are properly cross-referenced, the business property is correctly assessed, and the proper assessee is identified.

When the assessor receives business property statements from leasing companies and other known lessors in the county, he verifies whether any items have gone off-lease and may be escaping assessment for the current year. He accomplishes this by comparing lessee and lessor business property statements for common equipment in the current and previous years and searching all business property reporting categories on the lessee's statement for the off-lease equipment.

Off-lease equipment is often purchased by the former lessee and, as such, must be reported by the former lessee. The assessor is diligent in accounting for all leased and previously leased equipment.

Manufactured Homes

A "manufactured home" is defined in Health and Safety Code sections 18007 and 18008, and statutes prescribing the method of assessing manufactured homes are contained in sections 5800 through 5842. A manufactured home is subject to local property taxation if sold new on or after July 1, 1980, or if its owner requests conversion from the vehicle license fee to local property taxation. Manufactured homes should be classified as personal property and enrolled on the secured roll.

Until recently in Santa Cruz County, zoning regulations prohibited manufactured homes from being installed on land outside mobilehome parks. For this reason, almost all of the manufactured homes are situated in the approximately 75 mobilehome parks in the county. Nineteen of these are resident-owned parks. A few statistics on manufactured homes on the 2005-06 assessment roll follow:

TYPE OF PARK	ASSESSMENTS	TOTAL ASSESSMENTS
Resident-owned	407	\$45,708,888
Non resident-owned	1,599	\$88,548,439
TOTAL	2,006	\$134,257,327

The valuation of manufactured homes is the responsibility of the appraiser assigned to the geographical area in which the home is located. The primary method of discovering manufactured homes is through the State Department of Housing and Community Development's listing of transfers, voluntary conversions, and new registrations. This method is augmented by manufactured home dealer reports of sales, Form BOE-502-A, *Preliminary Change of Ownership Report*, and building permits.

BOE unit cost factors are the primary source of data for valuing manufactured homes. Using this source ensures that the significant value attributable to the in-park location in Santa Cruz County

will not be included in the assessment of the manufactured home. When applicable, supplemental assessments are processed.

In our 2002 survey report, we recommended the assessor enroll manufactured homes as personal property and establish a new base year value for any site within a resident-owned mobilehome park that received the section 62.1 exclusion upon a change in ownership. We found that the assessor implemented the second recommendation, but did not implement the first.

Therefore, we repeat the recommendation for the enrollment of manufactured homes as personal property. We also found that the assessor does not conduct any annual or periodic review of manufactured home assessments.

RECOMMENDATION 11: Improve the assessment of manufactured homes by:
(1) enrolling manufactured homes as personal property, and
(2) enrolling the lesser of the factored base year value or the full cash value as of the lien date.

Enroll manufactured homes as personal property.

We found that the assessor continues to enroll manufactured homes as improvements. Section 5801(b)(2) provides that manufactured homes shall not be classified as real property for taxation purposes. This is explained in detail in Letter To Assessors 92/57, dated August 31, 1992, and in Assessors' Handbook Section 511, *Assessment of Manufactured Homes and Parks*.

If special assessments are levied, improper classification of manufactured homes can affect the amount of taxes due. Special assessments are levies upon real property in a district for the purpose of paying for improvements. The amount of the levy is based upon the benefits accruing to the property as a result of the improvements. Special assessments are not typically imposed on items of personal property. Thus, classification of manufactured homes may result in the inappropriate application of special assessments.

Enroll the lesser of the factored base year value or the full cash value as of the lien date.

After the initial enrollment, the assessor factors the base year value on an annual basis with no review for declines in value. We found cases where the base year value was factored for as long as nine years. We found instances where the full cash value of a manufactured home was from 17 to 30 percent lower than the factored base year value.

Section 5813 provides that the taxable value of a manufactured home should be the lesser of (1) its factored base year value; (2) its full cash value as of the lien date, considering reductions in value due to damage, destruction, depreciation, obsolescence, or other factors causing a decline in value; or (3) if the manufactured home is damaged or destroyed by a disaster, misfortune, or calamity, its full cash value in its damaged condition. The assessor's practice of not ensuring that the lowest of these values is enrolled has resulted in overassessments.

Aircraft

General Aircraft

General aircraft are privately owned aircraft that are used for pleasure or business but that are not authorized to carry passengers, mail, or freight on a commercial basis. Section 5363 requires the assessor to determine the market value of all aircraft according to standards and guidelines prescribed by the BOE. Section 5364 requires the BOE to establish such standards. On January 10, 1997, the BOE approved the *Aircraft Bluebook-Price Digest (Bluebook)* as the primary guide for valuing aircraft, with the *Vref Aircraft Value Reference (Vref)* as an alternative guide for aircraft not listed in the *Bluebook*.

The following table illustrates the number of aircraft assessed in Santa Cruz County for recent roll years:

ROLL YEAR	GENERAL	HISTORICAL	ASSESSED VALUE
2005-06	305	6	\$38,368,549
2004-05	279	5	\$30,760,090
2003-04	203	7	\$26,324,700
2002-03	295	7	\$30,232,430
2001-02	301	9	\$30,225,510

The assessor primarily uses the *Bluebook* for appraising general aircraft. This value guide provides for adjustments due to engine hours, extra equipment, and general aircraft condition, all of which are required to be disclosed by aircraft owners on the aircraft property statement. Additional information is gathered from other counties, aircraft brokers, airport operators' tenant lists, Federal Aviation Administration reports, and websites such as www.trade-a-plane.com.

The assessor's general aircraft valuations comply with statutory requirements. We found no problems with this program.

Historical Aircraft

Aircraft of historical significance can be exempted from taxation if they meet certain requirements. Section 220.5 defines "aircraft of historical significance" as (1) an aircraft that is an original, restored, or replica of a heavier than air powered aircraft 35 years or older; or (2) any aircraft of a type or model of which there are fewer than five such aircraft known to exist worldwide.

The historical aircraft exemption is not automatic. Each year, the owner of a historical aircraft must submit an affidavit on or before 5:00 p.m., February 15, paying a filing fee of \$35 upon the initial application for exemption. Along with these requirements, aircraft of historical significance are exempt only if the following conditions are met: (1) the assessee is an individual owner who does not hold the aircraft primarily for purposes of sale; (2) the assessee does not use

the aircraft for commercial purposes or general transportation; and, (3) the aircraft was available for display to the public at least 12 days during the 12-month period immediately preceding the lien date for the year for which exemption is claimed.

There were six historical aircraft assessed on the 2005-06 roll in Santa Cruz County with a total value of more than \$270,000. The assessor has properly obtained signed affidavits for the historical aircraft exemption pursuant to section 220.5(c). We found the assessor to be in full compliance with the historical aircraft filing procedures.

Vessels

Assessors must annually appraise all vessels at market value. The primary sources used for the discovery of assessable vessels include State Department of Motor Vehicles (DMV) reports, referrals from other counties, and information provided by the vessel owners themselves.

For the 2004-05 roll year, the assessor enrolled 1,908 vessels with a total assessed value of \$41,267,295.

The following table shows the vessels assessed in Santa Cruz for recent years:

ROLL YEAR	PLEASURE	ASSESSED VALUE	DOCUMENTED	ASSESSED VALUE
2004-05	1,875	\$40,281,821	33	\$985,474
2003-04	1,822	\$38,269,722	37	\$1,237,137
2002-03	1,787	\$37,440,806	39	\$1,263,611
2001-02	1,729	\$35,493,699	47	\$1,627,749
2000-01	1,643	\$32,534,579	50	\$1,849,619

The vessels are discovered through property statements, certificates of documentation issued by the United States Coast Guard, harbormasters' marina reports, field canvassing, referrals from other counties, and DMV reports.

We found several areas that need improvement.

RECOMMENDATION 12: Revise vessel procedures by: (1) ensuring that a certified auditor-appraiser reviews vessel values, (2) including sales tax as a component of a vessel's value, (3) assessing all vessels at market value, and (4) requiring vessel owners to file annual vessel property statements for boats costing \$100,000 or more.

Ensure that a certified auditor-appraiser reviews vessel values.

An auditor-appraiser aide makes the initial appraisal of all vessels using the *BUC Used Boat Price Guide* (BUC) and, secondarily, the *National Automobile Dealers Association Small and*

Large Boat Appraisal Guide (NADA). Although it is the assessor's policy that complex vessel appraisals be reviewed and approved by a certified appraiser, there is no evidence that the vessel appraisals are actually reviewed.

Section 670 provides that no person shall perform the duties or exercise the authority of an appraiser for property tax purposes as an employee of the state, any county, or city and county, unless they hold a valid appraiser's or advanced appraiser's certificate issued by the BOE. By allowing an uncertified staff member to value property, the assessor is allowing an unqualified staff member to exercise the authority of an appraiser.

Include sales tax as a component of a vessel's value.

The assessor fails to add sales tax to the indicated values from the BUC or NADA value guides when computing the vessel's assessed value.

Generally, when determining market value where cost is the basis of that value, sales or use tax, freight, and installation costs are elements of the value as stated in Assessors' Handbook Section 576, *Assessment of Vessels*. Without all of the elements of the cost included, appraised values are understated.

Assess all vessels at market value.

This recommendation is repeated from our 2002 survey report. In Santa Cruz County, vessels are initially assessed at market value using the BUC or NADA value guides, the cost code assigned by the DMV, or the purchase price reported by the boat owner. Once the initial value is set, the assessor reduces subsequent assessments annually by 5 percent overall. This practice is not supported by any study.

The law requires the assessor to assess all taxable property in proportion to its value unless there is specific statutory provision for another manner of assessment. Pleasure vessels are subject to assessment at market value. The assessor's practice of using a fixed depreciation factor results in some vessels being assessed at greater than market value and others being assessed at less than market value.

Require vessel owners to file annual property statements for boats costing \$100,000 or more.

We found that the assessor does not send Form BOE-576-D, *Vessel Property Statement*, to the owners of vessels costing over \$100,000.

Section 441 requires each person owning taxable personal property, other than a manufactured home, having an aggregate cost of \$100,000 or more for any assessment year, to file a signed annual property statement with the assessor. This provision applies to all vessels, including noncommercial vessels. Having this information will provide the assessor with current and accurate data regarding replacement engines and new accessories.

Failing to require owners of qualifying vessels to file a property statement increases the risk of inaccurate assessments based on insufficient information.

APPENDIXES

A. County-Assessed Properties Division Survey Group

Santa Cruz County

Chief

Dean Kinnee

Survey Program Director:

Arnold Fong

Principal Property Appraiser

Survey Team Supervisor:

Sally Boeck

Supervising Property Appraiser

Peter Gaffney

Supervising Property Appraiser

Survey Team Leader:

Dale Peterson

Senior Specialist Property Auditor-Appraiser

Survey Team:

Glenn Danley

Senior Specialist Property Appraiser

Lloyd Allred

Associate Property Auditor-Appraiser

Ancil Aydelott

Associate Property Auditor-Appraiser

Dave Barbeiro

Associate Property Auditor-Appraiser

Larry Gee

Associate Property Auditor-Appraiser

Bob Marr

Associate Property Appraiser

Jay Price

Associate Property Appraiser

Erica Fisher

Office Technician

Kristina Valdez

Tax Technician I

B. Assessment Sampling Program

The need for compliance with the laws, rules, and regulations governing the property tax system and related assessing⁷ activities is very important in today's fiscally stringent times. The importance of compliance is twofold. First, the statewide maximum tax rate is set at one percent of taxable value. Therefore, a reduction of local revenues occurs in direct proportion to any undervaluation of property. (It is not legally allowable to raise the tax rate to compensate for increased revenue needs.) Secondly, with a major portion of every property tax dollar statewide going to public schools, a reduction in available local property tax revenues has a direct impact on the State's General Fund, which must backfill any property tax shortfall.

The BOE, in order to meet its constitutional and statutory obligations, focuses the assessment sampling program on a determination of the full value of locally taxable property and eventually its assessment level. The purpose of the BOE's assessment sampling program is to review a representative sampling of the assessments making up the local assessment rolls, both secured and unsecured, to determine how effectively the assessor is identifying those properties subject to revaluation and how well he/she is performing the valuation function.

The BOE's County-Assessed Properties Division (CAPD) conducts the assessment sampling program on a five-year cycle for the 11 largest counties and cities and counties and on either a random or as needed basis for the other 47 counties. This sampling program is described as follows:

A representative random sampling is drawn from both the secured and unsecured local assessment rolls for the counties to be surveyed.

These assessments are stratified into 18 value strata (nine secured and nine unsecured.)⁸

From each stratum a random sampling is drawn for field investigation, sufficient in size to reflect the assessment level within the county.

For purposes of analysis, after the sample is drawn, the items are identified and placed into one of the five categories listed below:

Base year properties. Those properties the county assessor has not reappraised for either an ownership change or new construction during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling.

⁷ The term "assessing" as used here includes the actions of local assessment appeals boards, the boards of supervisors when acting as boards of equalization, and local officials who are directed by law to provide assessment-related information.

⁸ The nine value strata are \$1 to \$99,999; \$100,000 to \$199,999; \$200,000 to \$499,999; \$500,000 to \$999,999; \$1,000,000 to \$1,999,999; \$2,000,000 to \$19,999,999; \$20,000,000 to \$99,999,999; \$100,000,000 to \$249,999,999; and \$250,000,000 and over.

Transferred properties. Those properties last reappraised because of an ownership change that occurred during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling.

New construction. Those properties last reappraised to reflect new construction that occurred during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling.

Non-Proposition 13 properties. Those properties not subject to the value restrictions of article XIII A, or those properties that have a unique treatment. Such properties include mineral-producing property, open-space property, timber preserve property, and taxable government-owned property.

Unsecured properties. Those properties on the unsecured roll.

From the assessment universe in each of these 18 value strata (nine strata on both secured and unsecured local rolls), a simple random sampling is drawn for field investigation that is sufficient in size to reflect the assessment practices within the county. A simple nonstratified random sampling would cause the sample items to be concentrated in those areas with the largest number of properties and might not adequately represent all assessments of various types and values. Because a separate sample is drawn from each stratum, the number of sample items from each category is not in the same proportion to the number of assessments in each category. This method of sample selection causes the raw sample, i.e., the "unexpanded" sample, to overrepresent some assessment types and underrepresent others. "Expanding" the sample data eliminates this apparent distortion in the raw sampling; that is, the sample data in each stratum are multiplied by the ratio of the number of assessments in the particular stratum to the number of sample items selected from the stratum. Once the raw sampling data are expanded, the findings are proportional to the actual assessments on the assessment roll. Without this adjustment, the raw sampling would represent a distorted picture of the assessment practices. This expansion further converts the sampling results into a magnitude representative of the total assessed value in the county.

The field investigation objectives are somewhat different in each category, for example:

Base year properties -- for those properties not reappraised during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling: was the value properly factored forward (for the allowed inflation adjustment) to the roll being sampled? was there a change in ownership? was there new construction? or was there a decline in value?

Transferred properties -- for those properties where a change in ownership was the most recent assessment activity during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling: do we concur that a reappraisal was needed? do we concur with the county assessor's new value? was the base year value trended forward (for the allowed inflation adjustment)? was there a subsequent ownership change? was there subsequent new construction? was there a decline in value?

New construction -- for those properties where the most recent assessment activity was new construction added during the period between the lien date five years prior to the roll currently being sampled and the lien date of the current sampling: do we concur that the construction caused a reappraisal? do we concur with the value enrolled? was the base year amount trended forward properly (for the allowed inflation adjustment)? was there subsequent new construction? or was there a decline in value?

Non-Prop 13 properties -- for properties not covered by the value restrictions of article XIII A, or those properties that have a unique treatment do we concur with the amount enrolled?

Unsecured properties -- for assessments enrolled on the unsecured roll, do we concur with the amount enrolled?

The results of the field investigations are reported to the county assessor, and conferences are held to review individual sample items whenever the county assessor disagrees with the conclusions.

The results of the sample are then expanded as described above. The expanded results are summarized according to the five assessment categories and by property type and are incorporated into the published assessment practices survey report.

The primary use of the assessment sampling is to determine an assessor's eligibility for the cost reimbursement authorized by section 75.60. During the course of the sampling activity, the assessment practices survey team may also discover recurring causes for the differences in the opinion of taxable value that arise between the assessor and the County-Assessed Properties Division. These discoveries may lead to recommendations in the survey report that would not have otherwise been made.

C. Relevant Statutes and Regulations

Government Code

15640. Survey by board of county assessment procedures.

- (a) The State Board of Equalization shall make surveys in each county and city and county to determine the adequacy of the procedures and practices employed by the county assessor in the valuation of property for the purposes of taxation and in the performance generally of the duties enjoined upon him or her.
- (b) The surveys shall include a review of the practices of the assessor with respect to uniformity of treatment of all classes of property to ensure that all classes are treated equitably, and that no class receives a systematic overvaluation or undervaluation as compared to other classes of property in the county or city and county.
- (c) The surveys may include a sampling of assessments from the local assessment rolls. Any sampling conducted pursuant to subdivision (b) of Section 15643 shall be sufficient in size and dispersion to insure an adequate representation therein of the several classes of property throughout the county.
- (d) In addition, the board may periodically conduct statewide surveys limited in scope to specific topics, issues, or problems requiring immediate attention.
- (e) The board's duly authorized representatives shall, for purposes of these surveys, have access to, and may make copies of, all records, public or otherwise, maintained in the office of any county assessor.
- (f) The board shall develop procedures to carry out its duties under this section after consultation with the California Assessors' Association. The board shall also provide a right to each county assessor to appeal to the board appraisals made within his or her county where differences have not been resolved before completion of a field review and shall adopt procedures to implement the appeal process.

15641. Audit of Records; Appraisal Data Not Public.

In order to verify the information furnished to the assessor of the county, the board may audit the original books of account, wherever located, of any person owning, claiming, possessing or controlling property included in a survey conducted pursuant to this chapter when the property is of a type for which accounting records are useful sources of appraisal data.

No appraisal data relating to individual properties obtained for the purposes of any survey under this chapter shall be made public, and no state or local officer or employee thereof gaining knowledge thereof in any action taken under this chapter shall make any disclosure with respect thereto except as that may be required for the purposes of this chapter. Except as specifically provided herein, any appraisal data may be disclosed by the board to any assessor, or by the board or the assessor to the assessee of the property to which the data relate.

The board shall permit an assessee of property to inspect, at the appropriate office of the board, any information and records relating to an appraisal of his or her property, including "market data" as defined in Section 408. However, no information or records, other than "market data," which relate to the property or business affairs of a person other than the assessee shall be disclosed.

Nothing in this section shall be construed as preventing examination of that data by law enforcement agencies, grand juries, boards of supervisors, or their duly authorized agents, employees, or representatives conducting an investigation of an assessor's office pursuant to Section 25303, and other duly authorized legislative or administrative bodies of the state pursuant to their authorization to examine that data.

15642. Research by board employees.

The board shall send members of its staff to the several counties and cities and counties of the state for the purpose of conducting that research it deems essential for the completion of a survey report pursuant to Section 15640 with respect to each county and city and county. The survey report shall show the volume of assessing work to be done as measured by the various types of property to be assessed and the number of individual assessments to be made, the responsibilities devolving upon the county assessor, and the extent to which assessment practices are consistent with or differ from state law and regulations. The report may also show the county assessor's requirements for maps, records, and other equipment and supplies essential to the adequate performance of his or her duties, the number and classification of personnel needed by him or her for the adequate conduct of his or her office, and the fiscal outlay required to secure for that office sufficient funds to ensure the proper performance of its duties.

15643. When surveys to be made.

- (a) The board shall proceed with the surveys of the assessment procedures and practices in the several counties and cities and counties as rapidly as feasible, and shall repeat or supplement each survey at least once in five years.
- (b) The surveys of the 10 largest counties and cities and counties shall include a sampling of assessments on the local assessment rolls as described in Section 15640. In addition, the board shall each year, in accordance with procedures established by the board by regulation, select at random at least three of the remaining counties or cities and counties, and conduct a sample of assessments on the local assessment roll in those counties. If the board finds that a county or city and county has "significant assessment problems," as provided in Section 75.60 of the Revenue and Taxation Code, a sample of assessments will be conducted in that county or city and county in lieu of a county or city and county selected at random. The 10 largest counties and cities and counties shall be determined based upon the total value of locally assessed property located in the counties and cities and counties on the lien date that falls within the calendar year of 1995 and every fifth calendar year thereafter.
- (c) The statewide surveys which are limited in scope to specific topics, issues, or problems may be conducted whenever the board determines that a need exists to conduct a survey.
- (d) When requested by the legislative body or the assessor of any county or city and county to perform a survey not otherwise scheduled, the board may enter into a contract with the requesting local agency to conduct that survey. The contract may provide for a board sampling of assessments on the local roll. The amount of the contracts shall not be less than the cost to the board, and shall be subject to regulations approved by the Director of General Services.

15644. Recommendations by board.

The surveys shall incorporate reviews of existing assessment procedures and practices as well as recommendations for their improvement in conformity with the information developed in the surveys as to what is required to afford the most efficient assessment of property for tax purposes in the counties or cities and counties concerned.

15645. Survey report; final survey report; assessor's report.

- (a) Upon completion of a survey of the procedures and practices of a county assessor, the board shall prepare a written survey report setting forth its findings and recommendations and transmit a copy to the

assessor. In addition the board may file with the assessor a confidential report containing matters relating to personnel. Before preparing its written survey report, the board shall meet with the assessor to discuss and confer on those matters which may be included in the written survey report.

(b) Within 30 days after receiving a copy of the survey report, the assessor may file with the board a written response to the findings and recommendations in the survey report.

The board may, for good cause, extend the period for filing the response.

(c) The survey report, together with the assessor's response, if any, and the board's comments, if any, shall constitute the final survey report. The final survey report shall be issued by the board within two years after the date the board began the survey. Within a year after receiving a copy of the final survey report, and annually thereafter, no later than the date on which the initial report was issued by the board and until all issues are resolved, the assessor shall file with the board of supervisors a report, indicating the manner in which the assessor has implemented, intends to implement, or the reasons for not implementing the recommendations of the survey report, with copies of that response being sent to the Governor, the Attorney General, the State Board of Equalization, the Senate and Assembly and to the grand juries and assessment appeals boards of the counties to which they relate.

15646. Copies of final survey reports to be filed with local officials.

Copies of final survey reports shall be filed with the Governor, Attorney General, and with the assessors, the boards of supervisors, the grand juries and assessment appeals boards of the counties to which they relate, and to other assessors of the counties unless one of these assessors notifies the State Board of Equalization to the contrary and, on the opening day of each regular session, with the Senate and Assembly.

Revenue and Taxation Code**75.60. Allocation for administration.**

(a) Notwithstanding any other provision of law, the board of supervisors of an eligible county or city and county, upon the adoption of a method identifying the actual administrative costs associated with the supplemental assessment roll, may direct the county auditor to allocate to the county or city and county, prior to the allocation of property tax revenues pursuant to Chapter 6 (commencing with Section 95) and prior to the allocation made pursuant to Section 75.70, an amount equal to the actual administrative costs, but not to exceed 5 percent of the revenues that have been collected on or after January 1, 1987, due to the assessments under this chapter. Those revenues shall be used solely for the purpose of administration of this chapter, regardless of the date those costs are incurred.

(b) For purposes of this section:

- (1) "Actual administrative costs" includes only those direct costs for administration, data processing, collection, and appeal that are incurred by county auditors, assessors, and tax collectors. "Actual administrative costs" also includes those indirect costs for administration, data processing, collections, and appeal that are incurred by county auditors, assessors, and tax collectors and are allowed by state and federal audit standards pursuant to the A-87 Cost Allocation Program.
- (2) "Eligible county or city and county" means a county or city and county that has been certified by the State Board of Equalization as an eligible county or city and county. The State Board of Equalization shall certify a county or city and county as an eligible county or city and county only if both of the following are determined to exist:
 - (A) The average assessment level in the county or city and county is at least 95 percent of the assessment level required by statute, as determined by the board's most recent survey of that county or city and county performed pursuant to Section 15640 of the Government Code.
 - (B) For any survey of a county assessment roll for the 1996-97 fiscal year and each fiscal year thereafter, the sum of the absolute values of the differences from the statutorily required assessment level described in subparagraph (A) does not exceed 7.5 percent of the total amount of the county's or city and county's statutorily required assessed value, as determined pursuant to the board's survey described in subparagraph (A).
- (3) Each certification of a county or city and county shall be valid only until the next survey made by the board. If a county or city and county has been certified following a survey that includes a sampling of assessments, the board may continue to certify that county or city and county following a survey that does not include sampling if the board finds in the survey conducted without sampling that there are no significant assessment problems in the county or city and county. The board shall, by regulation, define "significant assessment problems" for purposes of this section, and that definition shall include objective standards to measure performance. If the board finds in the survey conducted without sampling that significant assessment problems exist, the board shall conduct a sampling of assessments in that county or city and county to determine if it is an eligible county or city and county. If a county or city and county is not certified by the board, it may request a new survey in advance of the regularly scheduled survey, provided that it agrees to pay for the cost of the survey.

Title 18, California Code of Regulations

Rule 370. Random selection of counties for representative sampling.

(a) **SURVEY CYCLE.** The board shall select at random at least three counties from among all except the 10 largest counties and cities and counties for a representative sampling of assessments in accordance with the procedures contained herein. Counties eligible for random selection will be distributed as equally as possible in a five-year rotation commencing with the local assessment roll for the 1997–98 fiscal year.

(b) **RANDOM SELECTION FOR ASSESSMENT SAMPLING.** The three counties selected at random will be drawn from the group of counties scheduled in that year for surveys of assessment practices. The scheduled counties will be ranked according to the size of their local assessment rolls for the year prior to the sampling.

(1) If no county has been selected for an assessment sampling on the basis of significant assessment problems as provided in subdivision (c), the counties eligible in that year for random selection will be divided into three groups (small, medium, and large), such that each county has an equal chance of being selected. One county will be selected at random by the board from each of these groups. The board may randomly select an additional county or counties to be included in any survey cycle year. The selection will be done by lot, with a representative of the California Assessors' Association witnessing the selection process.

(2) If one or more counties are scheduled for an assessment sampling in that year because they were found to have significant assessment problems, the counties eligible for random selection will be divided into the same number of groups as there are counties to be randomly selected, such that each county has an equal chance of being selected. For example, if one county is to be sampled because it was found to have significant assessment problems, only two counties will then be randomly selected and the pool of eligible counties will be divided into two groups. If two counties are to be sampled because they were found to have significant assessment problems, only one county will be randomly selected and all counties eligible in that year for random selection will be pooled into one group.

(3) Once random selection has been made, neither the counties selected for an assessment sampling nor the remaining counties in the group for that fiscal year shall again become eligible for random selection until the next fiscal year in which such counties are scheduled for an assessment practices survey, as determined by the five-year rotation. At that time, both the counties selected and the remaining counties in that group shall again be eligible for random selection.

(c) **ASSESSMENT SAMPLING OF COUNTIES WITH SIGNIFICANT ASSESSMENT PROBLEMS.** If the board finds during the course of an assessment practices survey that a county has significant assessment problems as defined in Rule 371, the board shall conduct a sampling of assessments in that county in lieu of conducting a sampling in a county selected at random.

(d) **ADDITIONAL SURVEYS.** This regulation shall not be construed to prohibit the Board from conducting additional surveys, samples, or other investigations of any county assessor's office.

Rule 371. Significant assessment problems.

(a) For purposes of Revenue and Taxation Code Section 75.60 and Government Code Section 15643, "significant assessment problems" means procedure(s) in one or more areas of an assessor's assessment

operation, which alone or in combination, have been found by the Board to indicate a reasonable probability that either:

- (1) the average assessment level in the county is less than 95 percent of the assessment level required by statute; or
- (2) the sum of all the differences between the board's appraisals and the assessor's values (without regard to whether the differences are underassessments or overassessments), expanded statistically over the assessor's entire roll, exceeds 7.5 percent of the assessment level required by statute.

(b) For purposes of this regulation, "areas of an assessor's assessment operation" means, but is not limited to, an assessor's programs for:

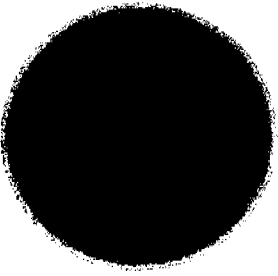
- (1) Uniformity of treatment for all classes of property.
- (2) Discovering and assessing newly constructed property.
- (3) Discovering and assessing real property that has undergone a change in ownership.
- (4) Conducting mandatory audits in accordance with Revenue and Taxation Code Section 469 and Property Tax Rule 192.
- (5) Assessing open-space land subject to enforceable restriction, in accordance with Revenue and Taxation Code Sections 421 et. seq.
- (6) Discovering and assessing taxable possessory interests in accordance with Revenue and Taxation Code Sections 107 et. seq.
- (7) Discovering and assessing mineral-producing properties in accordance with Property Tax Rule 469.
- (8) Discovering and assessing property that has suffered a decline in value.
- (9) Reviewing, adjusting, and, if appropriate, defending assessments for which taxpayers have filed applications for reduction with the local assessment appeals board.

(c) A finding of "significant assessment problems," as defined in this regulation, would be limited to the purposes of Revenue and Taxation Code Section 75.60 and Government Code Section 15643, and shall not be construed as a generalized conclusion about an assessor's practices.

ASSESSOR'S RESPONSE TO BOE'S FINDINGS

Section 15645 of the Government Code provides that the assessor may file with the BOE a response to the findings and recommendation in the survey report. The survey report, the assessor's response, and the BOE's comments on the assessor's response, if any, constitute the final survey report.

The Santa Cruz County Assessor's response begins on the next page. The BOE has no comments on the response.



County of Santa Cruz

GARY E. HAZELTON, ASSESSOR-RECORDER

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Jessie Mudgett
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Chief Deputy-Valuation
Carol D. Sutherland
Chief Deputy-Recorder

May 10, 2007

David J. Gau, Deputy Director
Property and Special Taxes Department
State Board of Equalization
P.O. Box 942879
Sacramento, CA. 94279-0063

RECEIVED

MAY 14 2007

DEPARTMENT OF REVENUE
PROPERTY AND SPECIAL TAXES

Dear Mr. Gau:

Pursuant to Section 15645 of the California Government Code, I am providing a written response to the findings and recommendations contained in the *April 2007 Santa Cruz County Assessment Practices Survey*. Please include my response in your final report.

I wish to express my appreciation to the entire Board of Equalization survey team for the professional and courteous manner in which they performed the survey. I do regard the survey as an important tool for the continuing dialogue between the State Board of Equalization and local Assessors.

I would also like to express my gratitude to the employees of the Santa Cruz County Assessor's Office for their hard work, expertise, dedication and commitment to public service. They are a great staff and their commitment to excellence is unequalled.

Sincerely,

Gary E. Hazelton
Santa Cruz County Assessor-Recorder

Santa Cruz County Assessor
Responses to State Board of Equalization
Assessment Practices Survey Report
April 2007

- Recommendation 1: We concur. We have created a notice to be included with the supplemental assessment notice for calamities.
- Recommendation 2: (1) The Assessor properly notes the penalty on the roll change document. The roll change is processed by the Auditor's Office and a penalty flag is keyed to represent the penalty aspect of the assessment. The Tax Collector's Office has been notified of this problem and they are working with the IT Department for resolution of this problem.
- (2) Notification language advising the taxpayer of his rights to appeal is listed on the reverse side of the unsecured tax bill under the heading of "If you disagree with the assessed value as shown on the tax bill". This admonition, together with the penalty phrase from section (1), will fulfill the requirements.
- Recommendation 3: (1) We concur. Recommendation has been implemented.
- (2) We concur. Recommendation was implemented for 2006-07.
- Recommendation 4: (1) We concur. We will comply beginning with the 2007-08 year.
- (2) We concur. However programming to make the change is prohibitive at this time. The problem will be addressed in our new system currently under development.
- (3) We concur. We will submit forms for review timely.
- Recommendation 5: We concur. We will request our IT Department to revise our vineyard and orchard program to allow for a modified income stream.
- Recommendation 6: We concur. The eight (8) properties affected have been corrected.
- Recommendation 7: We concur. Recommendation has been implemented.

- Recommendation 8: (1) This recommendation will require extensive mainframe programming to implement. It will be included in our new system currently being developed.
- (2) Recommendation implemented
- (3) Recommendation will be implemented.
- (4) Recommendation implemented on the one property identified in the survey.

Recommendation 9: We concur. The recommendation has been implemented.

Recommendation 10: The Assessor has reduced, but not eliminated, the practice of netting audit escapes and refunds. The practice, when carefully applied, increases efficiency, is more economical, and is more understandable to the taxpayer. No change in procedure is contemplated using our current computer system. We expect that our new system currently under development will be more flexible in this area.

- Recommendation 11: (1) We concur. We have always treated manufactured homes as personal property as reflected in the fact that no special levies or charges are applied to these accounts. Our current computer system does not allow manufactured homes to be shown on the tax bill as personal property.
- (2) Limited staff will not allow us to review all manufactured homes annually. We will begin a review as time and staffing becomes available.

- Recommendation 12: (1) We disagree. The Chief Deputy Assessor-Valuation reviews all vessel assessments before they are enrolled.
- (2) Recommendation will be implemented.
- (3) Limited staff will not allow us to review all vessel assessments annually. We currently review 20% of the vessels each year. Others are depreciated at a rate of 5%.
- (4) We will implement the program for the 2007-08 assessment year. In the past, the program has had a very low rate of return and not cost effective.