

Issue Paper Number 00-040



BOARD OF EQUALIZATION
KEY AGENCY ISSUE

- Board Meeting
- Business Taxes Committee
- Customer Services and Administrative Efficiency Committee
- Legislative Committee
- Property Tax Committee
- Other

PENDING LITIGATION PROPERTY TAX RULE 305.3

I. Issue

Should the rulemaking process for Property Tax Rule 305.3 be delayed until the court of appeal decides *Heavenly Valley v. El Dorado County Board of Equalization* due to the fact that the court may decide an issue or issues addressed by Rule 305.3?

II. Staff Recommendation

Staff recommends that the rulemaking process continue even though the *Heavenly Valley* case has not been decided.

III. Other Alternative(s) Considered

The Board could suspend the rulemaking process until a decision is reached. (El Dorado County Counsel)

Issue Paper Number 00-040

IV. Background

Under Government Code section 15606, subdivision (c), the Board is given the power and duty to prescribe rules and regulations to govern local boards of equalization and assessment appeals boards when equalizing and county assessors when assessing. Pursuant to that authority, the Board directed staff to draft a new section 305.3 of Title 18 of the California Code of Regulations, Subchapter 3, Local Equalization Property Tax Rules, to interpret provisions of Revenue and Taxation Code section 469 relating to assessment appeal rights and appeals boards' jurisdiction to equalize escape assessments resulting from audits performed pursuant to that section.

Revenue and Taxation Code section 469 requires that a county assessor audit at least once each four years the assessable trade fixtures and business tangible personal property with a full value of \$400,000 or more owned, claimed, possessed or controlled by a taxpayer engaged in a profession, trade, or business. Section 469 further provides in the fourth paragraph:

If the result of an audit for any year discloses property subject to an escape assessment, then the original assessment of all property of the assessee at the location of the profession, trade, or business for that year shall be subject to review, equalization and adjustment by the county board of equalization or assessment appeals board pursuant to Chapter 1 (commencing with Section 1601) of Part 3 of this division, except in those instances when the property had previously been equalized for the year in question.

The paragraph was added by 1978 legislation amending section 469. Prior to the amendment, a taxpayer could only appeal escape assessments following an audit. In a letter to Governor Edmund G. Brown, Jr., dated August 31, 1978, the sponsors of the amendment (the Taxation Section of the California State Bar) expressed the intent of the legislation as follows:

The bill would allow a business taxpayer of property tax to have his entire assessment for a particular year at a business premises to be reviewed and equalized when the assessor by reason of an audit proposes an escape assessment. The bill is needed because many taxpayers do not protest assessments when the overall assessment at a business premises seems fair, even though some components are over-assessed and some under-assessed. Then, years later the assessor by reason of audit, proposes an escape assessment for the under-assessed component. Under the present law, the taxpayer has no redress for the over-assessed component at the late date of the proposed escape assessment.

Thus, the amendment was intended to address situations where:

- A taxpayer was satisfied with an overall property assessment, even while recognizing that he/she was not in agreement with the assessor's allocation to various parts of the overall assessment.
- Subsequently, the assessor conducted an audit that resulted in an escape assessment, thereby increasing the overall assessment for the property for a particular year.
- Following the audit, the taxpayer could only challenge the escape assessment even though the taxpayer had previously recognized that the assessment allocations were incorrect.

A difference of opinion over the application of the foregoing provision has led to the proposal for a new Property Tax Rule to interpret and to make specific its language. Property Taxes Department staff and Legal Division staff drafted proposed Property Tax Rule 305.3 after receiving input from the California

FORMAL ISSUE PAPER

Association of Clerks and Election Officials, California Assessors' Association, County Councils' Association of California, California Taxpayers' Association, and industry representatives.

On February 25, 2000, staff held a meeting in Sacramento with interested parties for discussions in an effort to reach agreement on as many issues as possible. Staff and interested parties were unable to reach agreement on several key issues and, therefore, it was decided that the rule writing process would be accomplished in two stages.

First, each unresolved issue and the parties' positions on each issue would be presented to the Property Tax Committee for decision. Second, the rule would be redrafted in accordance with the Board's positions taken on the issues, and then resubmitted to interested parties for review and comment. The redrafted Property Tax Rule would then be presented to the Property Tax Committee for approval of the language.

At the Property Tax Committee meeting on April 5, 2000, the Board was asked to decide five major unresolved issues. However, at the request of some interested parties, the Members decided at the April 5 meeting to delay the rulemaking process until November 1, 2000 because the case of *Heavenly Valley v. El Dorado County Board of Equalization* is currently pending before the court of appeal. At issue in the case is the proper interpretation of some aspects of the equalization provisions of Revenue and Taxation Code section 469. The oral arguments in the *Heavenly Valley* case are now set for hearing on November 13, 2000.

As instructed at the April 5 Property Tax Committee meeting, staff now requests direction on five major issues surrounding the equalization provisions of section 469 of the Revenue and Taxation Code which will be presented in this issue paper and four other issue papers.

V. Staff Recommendation

The rulemaking process should continue despite pending litigation that may decide some of the issues.

A. Description of the Staff Recommendation

Staff recommends that the rulemaking process continue notwithstanding the pending litigation. Although staff is aware of three pending court cases, including the *Heavenly Valley* case, in which interpretation of equalization provisions of section 469 is at issue, there is no certainty that the disposition of any of these cases will result in a published opinion that would establish a binding interpretation of the issues presented to the Board. The purpose of the rule is to interpret those provisions and the issues before the Board in order to avoid or minimize the need for future litigation.

Moreover, a court decision is predicated on the specific facts and circumstances of the case. As such, the statutory interpretation may be quite limited in scope and, therefore, have little application to the matters addressed by the proposed rule. The issues addressed by the proposed rule and before the Board are as follows:

1. Whether the equalization provisions apply only to mandatory audits.
2. The meaning of the phrase "the result of the audit discloses property subject to escape assessment" for the purpose of equalization.
3. Whether "property of the assessee" for the purpose of appeal includes only property assessed to the audited taxpayer.
4. The definition of "location" of the property for the purpose of equalization.

FORMAL ISSUE PAPER

The *Heavenly Valley* case addresses only the second issue of whether "property subject to escape assessment" means that such assessment must actually be enrolled before a taxpayer may appeal the over-assessment of other property at the location. The other two cases which are pending in superior court involve none of the issues to be addressed by the rule. In view of the limited scope of the issues before these courts, a published decision in any of these cases would have little or no effect on the issues to be decided by the Board. Therefore, the proposed rule will provide a more comprehensive interpretation of the equalization provisions of section 469 than will the decisions to be made in the pending court cases.

B. Pros of the Staff Recommendation

Adoption of a Property Tax Rule interpreting the equalization provisions of section 469 will:

- Provide clarity by interpreting provisions not at issue in the pending court cases.
- Promote uniformity in enrollment procedures and within the assessment appeals process throughout California.
- Reduce the number of court actions by providing a settled interpretation of the most contentious provisions.
- Encourage consistent treatment of taxpayers in each county when they seek to challenge their property tax assessments following audits conducted pursuant to section 469.

C. Cons of the Staff Recommendation

The promulgation of formal rules is a process that involves the time and resources of the Board and other public agencies and officers. If the rulemaking process continues and the rule is adopted while litigation is pending, it is possible that it would be necessary to amend the rule later because of a contrary judicial interpretation of some provision of section 469. Such an amendment would involve an expenditure of time and resources of the Board and Board staff, which could be avoided by delaying the process.

D. Statutory or Regulatory Change

Action by the Board to adopt a Property Tax Rule interpreting the equalization provisions of section 469 will add section 305.3 to Title 18 of the California Code of Regulations, Subchapter 3.

E. Administrative Impact

None

F. Fiscal Impact

1. Cost Impact

None

2. Revenue Impact

None

G. Taxpayer/Customer Impact

Adoption of a Property Tax Rule interpreting the equalization provisions of section 469 will affect administrative procedures for the assessment appeals process at the county level and the functions of the clerks of the appeals boards, appeals board members, county assessors, county counsels, and each taxpayer seeking a reduction in assessment of his or her property's value following an audit conducted pursuant to section 469.

H. Critical Time Frames

There is no critical time frame for adoption of a Property Tax Rule interpreting section 469 since a county assessor conducts audits pursuant to section 469 on an ongoing basis. The 60-day period for filing an application appealing the result of an audit disclosing property subject to an escape assessment commences on receipt of the proper notice of the escape assessment. Consequently, the equalization provisions of section 469 provide for the filing of an application for an equalization hearing before a local board of equalization or county assessment appeals board throughout the year.

VI. Alternative 1

A. Description of the Alternative (El Dorado County Counsel's proposal)

The Board could decide to suspend the rulemaking process until the court of appeal issues a decision in the *Heavenly Valley v. El Dorado County Board of Equalization* case. The El Dorado County Counsel's Office provided the following information on the status of the case in a writing dated September 21, 2000:

The Third Appellate District has set a firm hearing date of November 13, 2000 for the Heavenly Valley appeal and a written decision can be expected shortly thereafter. El Dorado County Counsel, on behalf of the El Dorado County Assessment Appeals Board, respectfully submits that a further continuance of this rulemaking process for all of the previously stated reasons is appropriate, especially in light of the firm hearing date now established, so close in time to the State Board's hearing date of November 1, 2000, and the fact that the State Board was willing to grant a continuance in April of 2000 when there was no set hearing date. The County AAB counsel also notes that El Dorado County did not request or join the continuance request of Heavenly Valley, and only agreed not to object out of courtesy to opposing counsel who had unavoidable scheduling conflicts.

El Dorado County understands that a further continuance will not be opposed by any of the interested parties. El Dorado County Counsel, on behalf of its AAB, respectfully requests a further continuance in order that any rule promulgated by the State Board has the benefit of the latest appellate legal developments in matters directly relevant to the proposed rule.

B. Pros of the Alternative

Delaying the rulemaking process until disposition of the *Heavenly Valley* case would avoid a situation in which the Board would later need to amend the rule because of a contrary judicial interpretation of some provision of section 469.

C. Cons of the Alternative

Delaying the rulemaking process until disposition of the *Heavenly Valley* case would be of little benefit because that case does not involve most of the issues that will be addressed by the proposed rule. Moreover, there is no certainty that the court will publish its opinion and, thereby, establish a binding interpretation of any issues that are addressed by the proposed rule.

D. Statutory or Regulatory Change

Action by the Board to adopt a Property Tax Rule interpreting the equalization provisions of section 469 will add section 305.3 to Title 18 of the California Code of Regulations, Subchapter 3.

E. Administrative Impact

None

F. Fiscal Impact

None

1. Cost Impact

None

2. Revenue Impact

None

G. Taxpayer/Customer Impact

Adoption of a Property Tax Rule interpreting the equalization provisions of section 469 will affect administrative procedures for the assessment appeals process at the county level and the functions of the clerks of the appeals boards, appeals board members, county assessors, county counsels, and each taxpayer seeking a reduction in assessment of his or her property's value following an audit conducted pursuant to section 469.

H. Critical Time Frames

There is no critical time frame for adoption of a Property Tax Rule interpreting section 469 since a county assessor conducts audits pursuant to section 469 on an ongoing basis. The 60-day period for filing an application appealing the result of an audit disclosing property subject to an escape assessment commences on receipt of the proper notice of the escape assessment. Consequently, the equalization provisions of section 469 provide for the filing of an application for an equalization hearing before a local board of equalization or county assessment appeals board throughout the year.

Prepared by: Property Taxes Department; Policy, Planning, and Standards Division
Legal Division; Property Taxes Section

Current as of: October 12, 2000