



BOARD OF EQUALIZATION

PROPERTY TAX COMMITTEE MEETING MINUTES

HONORABLE DEAN F. ANDAL, COMMITTEE CHAIR

450 N STREET, SACRAMENTO

NOVEMBER 17, 1998

ACTION ITEMS

Agenda Item: Approval of Wording for Draft Assessors' Handbook 502, *Advanced Appraisal* (AH 502)

Issue 1

Are fixtures always a separate appraisal unit for the purpose of measuring declines in value? (Is the language in rule 461(e) in conflict with section 51(d)?)

Committee Discussion

Board staff, representatives of the California Assessors' Association (CAA), and Committee Members presented their views on the above issue. Staff recommended that fixtures are *always* a separate appraisal unit for the purpose of measuring declines in value as required by rule 461(e). The staff position has been supported by industry. The CAA view was that the language in rule 461(e) is in conflict with section 51(d). CAA believed the appraisal unit is determined in the marketplace. Therefore, fixtures *may be* a separate appraisal unit for the purpose of measuring declines in value. Staff reported that a rule change would be needed for the handbook to reflect the CAA's view.

Committee Action/Recommendation

The Committee recommends that the Board approve staff's existing language in the November 1998 draft AH 502 addressing this issue.

Issue 2

Does new construction include a portion of an existing structure or other improvement for the purpose of establishing a new base year value for that portion? (Is the language in rules 463 and 463.5 in conflict with section 70?)

Committee Discussion

Board staff, industry representative, and Committee Members presented their views on the above issue. Staff gave its position that new construction includes a portion of an existing structure or other improvement for the purpose of establishing a new base year value for that portion. The staff position has been supported by CAA. Industry has disagreed with the staff's position, and contended that new construction requires the entire property. The discussion centered on remodeling, particularly on what constitutes new construction. Staff reported that no new construction would result if remodeling is a replacement due to repair and maintenance.

Committee Action/Recommendation

The Committee directs that the staff add a paragraph to elaborate the discussion of replacement related to "a portion thereof" and bring the language to the Board for consideration at its December 7, 1998 meeting.

Issue 3

Should a discussion of historical cost approach be included in Assessors' Handbook Section 502, *Advanced Appraisal*?

Committee Discussion

Board staff, a representative of CAA, and a representative from industry presented their views on the above issue. Staff recommended that the existing discussion relating to the historical cost approach be retained in AH 502. The staff view has been supported by the industry. CAA recommended that the historical cost approach discussion be excluded from AH 502 due to the limited application for locally assessed properties.

Committee Action/Recommendation

The Committee recommends that the Board adopt the staff's position to retain the existing discussion relating to the historical cost approach as reflected in the November 1998 draft AH 502.

Issue 4

Should a discussion describing methods for deriving discount rates using data from the capital market be included in Assessors' Handbook Section 502, *Advanced Appraisal?* ("CAPM" issue)

Committee Discussion

Board staff, a representative of CAA, and a representative from industry presented their views on the "CAPM" (Capital Asset Pricing Model) issue. Staff recommended that the existing discussion describing methods for deriving discount rates using data from capital market be retained in AH 502. The staff position has been supported by industry. CAA recommended that such discussion be excluded from AH 502 because such methods using data from capital markets are traditionally not employed in the appraisal of the majority of locally assessed properties. The State Controller's representative stated that the Controller has some concerns with the CAPM methods and requested further consideration of the CAPM issue.

Committee Action/Recommendation

The Committee recommends that the Board adopt the staff's position to retain the existing discussion describing methods for deriving discount rates using data from capital market as reflected in the November 1998 draft of AH 502.

Issue 5

Which version of the section relating to the treatment of intangible assets and rights should the Board adopt for inclusion in AH 502, *Advanced Appraisal?*

Committee Discussion

Board staff reported that there are two versions (staff's version and industry's version) of the proposed language for the section relating to treatment of intangible assets and

rights before the Committee. Staff recommended that the Board adopt the staff's version in AH 502. Staff presented its view that the language of the staff version on treatment of intangible assets and rights is consistent with current law. CAA was supportive of the staff version. Industry recommended that the Board adopt the industry version because its version captures all developments relating to the intangible issue.

Board staff, representatives of CAA and representatives from industry presented their views on the section relating to the treatment of intangible assets and rights. Representatives from the CAA expressed concerns on implementation problems with the industry version. The Committee Chairman reiterated that Assessors' Handbooks are not law and are not binding on Board Members in carrying out their constitutional duties but merely provide guidance for appraisers.

Committee Action/Recommendation

The Committee voted to direct staff to develop, and bring back to the Board for consideration at its December 7, 1998 meeting, a Board version that makes the following amendments and revisions to the industry version of the draft on treatment of intangible assets and rights (Attachment A):

1. Incorporate the staff language for following topics not included in the industry version:
 - Government Permits (Staff Version, Page 2-Attachment B)
 - Private Contract Rights (Staff version, Page 2-Attachment B)
 - Principle of Unit Valuation (First Paragraph Only of Staff version, Page 5-Attachment B)
 - Components of a Going Concern
 - ◇ Possible inclusion of "Going Concern Value" definition. (Staff version, Page 4-Attachment B)
 - ◇ Monetary Assets (Staff version, Page 6-Attachment B)
 - ◇ Real Property (Staff version, Page 6-Attachment B)
 - ◇ Tangible Personal Property (Staff version, Page 6-Attachment B)
 - ◇ Intangible Assets and Rights (Industry version) [Included for consistency purposes]
2. Without changing the fundamental meaning, redraft the industry version for style, grammar, redundancies, tone, and organization.
3. Add the following specific language regarding the cost approach:

There may be circumstances when the cost approach may be unreliable and inappropriate: (1) cost data not available; (2) taxpayer's refusal to provide

information; and (3) extensive depreciation, including physical deterioration, functional obsolescence, and economic obsolescence.

4. Delete from industry version the following:

- Last sentence of the first paragraph on Page 6 of 24 of the industry version (Attachment A).

Under appraisal theory, the fair market value of any taxable property cannot be more than cost to procure a reasonable substitute.

- Last sentence of the paragraph in the middle of the Page 13 of 24 of the industry version (Attachment A).

The appraiser must also be mindful of the principle of substitution, which holds that no one would pay more for the subject property than the cost to procure a reasonable substitute without undue delay, sets a ceiling on the appraiser's determination of fair market value.

5. Add the staff language for the topic of "Introduction" (Staff version Page 1- Attachment B) with the following changes:

- Delete "many" in the first sentence of the third paragraph.
- Replace "taxable" with "tangible" for all occurrences in the third paragraph.
- Delete "which are not an integral part of the bundle of rights (e.g., use, employment, and possession) conveyed with the ownership of real and personal property" from the second sentence of the second paragraph for consistency purposes.

6. Modify for the purposes of accurately quoting the law without editorializing.

Issue 6

Approval of wording on the November Draft Assessors' Handbook 502, *Advanced Appraisal*, with the exception of changes resulting from today's (November 17, 1998) Committee meeting.

Committee Discussion

The staff reported that there were three consent items (Items 6a, 6b, and 6c) before the Committee, in addition to the 5 issues (Issues 1 through 5). The State Controller's representative requested that the Committee pull Items 6a and 6c for discussion. Board staff, a representative from industry, and a representative from CAA presented their views regarding Item 6a and Item 6c.

The issue for Item 6a was whether initial leasing costs to achieve stabilized occupancy are valid components of cost in the cost approach [Staff November 1998 draft, p.13, last bulleted item]. Industry contended that initial leasing costs to achieve stabilized occupancy are not valid component of cost in the cost approach.

The issue for Item 6c was whether a footnote citing a recent court case [*Texaco Producing, Inc. v. County of Kern (1988) 66 Cal.App.4th 1029*] involving the Capital Asset Pricing Model (CAPM) should be included in the manual [Staff November 1998 Draft, p. 183, footnote 151]. Staff and CAA recommended that the footnote be included. Industry recommended that the footnote be deleted.

Committee Action/Recommendation

The Committee recommends that the Board:

- Tentatively adopt industry position on Item 6a and delete the staff's wording that initial leasing costs to achieve stabilized occupancy are valid component of cost in the cost approach. Direct staff to resubmit to the Committee additional language for reconsideration at its December 7, 1998 meeting.
- Approve Consent Item 6b.
- Accept staff recommendation on Item 6c to include a footnote citing the recent court case involving CAPM.
- Approve wording on the November 1998 Draft Assessors' Handbook 502, *Advanced Appraisal*, as submitted by the staff with the exception of changes and amendments directed by the Committee as stated in today's (November 17, 1998) Committee minutes.

Approved: _____



Dean F. Andal, Committee Chair



E. L. Sorensen, Jr., Executive Director

BOARD APPROVED

at the 11-19-98 Board Meeting



Janice Masterton, Chief

Board Proceedings Division