



STATE BOARD OF EQUALIZATION  
PROPERTY TAXES DEPARTMENT  
450 N STREET, MIC: 64, SACRAMENTO, CALIFORNIA  
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0064  
TELEPHONE (916) 445-4982  
FAX (916) 323-8765  
www.boe.ca.gov

JOHAN KLEHS  
First District, Hayward

DEAN ANDAL  
Second District, Stockton

CLAUDE PARRISH  
Third District, Torrance

JOHN CHIANG  
Fourth District, Los Angeles

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State Controller, Sacramento

September 14, 2001

JAMES E. SPEED  
Executive Director

TO INTERESTED PARTIES:

ASSESSORS' HANDBOOK SECTION 581,  
EQUIPMENT INDEX AND PERCENT GOOD FACTORS

Letter To Assessors 2001/056 announced a meeting between staff and interested parties to discuss Assessors' Handbook Section 581, *Equipment Index and Percent Good Factors* (AH 581). This is to inform you that the meeting with interested parties has been rescheduled for September 25, 2001. The meeting will start at 10:00 a.m. in Room 122, Board of Equalization, 450 N Street, Sacramento.

The purpose of the meeting is to (1) discuss averaging the separate classes of equipment index factors currently listed in Table 1 and Table 2 of AH 581 and (2) discuss whether the use of factors contained in AH 581 results in current replacement or reproduction costs. In regard to this second matter, Board staff has contacted representatives from the publications used to derive the index factors in AH 581 (Marshall and Swift Publication Company and the U. S. Bureau of Labor Statistics) in an effort to determine whether their application will yield reproduction or replacement cost. The information we have received leads us to conclude that application of the index factors in AH 581 to historical cost results in reproduction cost new.

The enclosed attachment shows wording changes proposed by Board staff for Chapter 1 of AH 581 which discusses whether the use of the index factors result in replacement cost or reproduction cost new. In addition to these wording changes, "reproduction cost" will be substituted for "replacement cost" throughout the text. The attachment does not address the wording changes required if the indexes are averaged.

If you have any questions or comments, please contact Mr. Gordon Ferguson at (916) 322-3815; gordon.ferguson@boe.ca.gov. Please submit any suggested wording changes prior to the September 25 meeting.

Sincerely,

Richard C. Johnson  
Deputy Director  
Property Taxes Department

RCJ:gf  
Enclosure

# CHAPTER 1: USE OF EQUIPMENT INDEX FACTORS

The index factor tables found in Chapter 4 of this section of the handbook (Tables 1, 2, and 3) may be used to estimate current replacement costs for various groups of equipment. Equipment index factors are developed for use in mass appraisals and are generally reliable and practical for converting historical or original cost to estimates of reproduction cost or replacement cost new. The index factors recommended by the Board, updated and distributed annually, include three separate index factor tables: Table 1, commercial equipment; Table 2, industrial equipment; and Table 3, agricultural and construction equipment. When an acquisition cost is multiplied by the index factor for the year of acquisition, the product approximates ~~the~~ current reproduction cost new in most instances. In situations where equipment has undergone minimal technological change, reproduction cost and replacement cost are likely to be similar. In industries where the equipment used is undergoing rapid change in technology, further adjustments may be needed to arrive at replacement cost. There may be situations where market evidence supports the need to make adjustments to reproduction cost to account for functional obsolescence before the percent good factors from Table 4 can be applied to arrive at market value.

## PRICE CHANGES

Price changes are usually an increasing factor (inflation) of 100 percent or greater. During those periods of time when the cost of raw material and/or labor actually declines, price changes may be a decreasing factor (deflation).

### Effects of Technological Progress

Technological progress may have a reducing effect on the cost of equipment. If technological progress has occurred since the acquisition date of an asset, the cost of performing the identical functions may now be lower. High technology equipment frequently suffers systematic functional obsolescence due to technological progress.

The tables (and factors) rely on indexes published by the U. S. Government Bureau of Labor Statistics (BLS) and on information published by Marshall & Swift Publication Company. These indexes adjust a property's historical cost for price level changes since the property was acquired.

## COMMERCIAL EQUIPMENT INDEX FACTORS

Indexes for 12 classes of equipment are supplied in Chapter 4, Table 1, Commercial Equipment Index Factors. If the index factors do not reasonably represent changes in equipment costs for a particular industry, additional research should be done to find a more appropriate method of estimating replacement cost new.

The following example demonstrates how to use the index factors to estimate ~~replacement~~ reproduction cost new.