STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION
PROPERTY AND SPECIAL TAXES DEPARTMENT
ASSESSMENT POLICY AND STANDARDS DIVISION
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

September 20, 2002

TO INTERESTED PARTIES:

ASSESSORS' HANDBOOK SECTION 510,
ASSESSMENT OF POSSESSORY INTERESTS

Under cover of a letter dated May 10, 2002, staff distributed to interested parties a draft revision to Assessors' Handbook Section 510, *Assessment of Possessory Interests* (AH 510). Interested parties were asked to submit proposed changes to the draft by July 12, 2002. The changes submitted are compiled in the enclosed matrix, which also shows staff's responses to the submissions.

On October 8, 2002, staff will meet with interested parties to discuss the matrix. The meeting will begin at 9:30 a.m. at the Board's headquarters at 450 N Street in Sacramento, Room 122.

After the October 8 meeting, any unresolved issues will be detailed in an issue paper prepared by staff. The issue paper will be discussed at the Board's Property Tax Committee meeting on December 18, 2002.

If you have questions or comments regarding the matrix, please contact Mr. Paul Lane at (916) 324-5828, paul.lane@boe.ca.gov. This letter and all future letters regarding this project will be posted on the Board's Web site and can be accessed by way of the following links: 1) Property Taxes, 2) Property Tax Committee Work Plans, and 3) Property Tax Committee Work Plans 2002.

Sincerely,

/s/ Dean R. Kinnee

Dean R. Kinnee, Chief
Assessment Policy and Standards Division
Property and Special Taxes Department

DRK:mn
Enclosure

ASSESSORS' HANDBOOK SECTION 510
ASSESSMENT OF TAXABLE POSSESSORY INTERESTS
ALTERNATIVE LANGUAGE

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
1.	1	31	California Assessors' Association (CAA)	**Revise as follows:** "Property~~,~~", as defined in~~s~~ sections 103 and… **Comment:** Comma should appear outside single word quotation. "Is" should be "in".	Accepted in part. Comma outside of single word quotation is not accepted. Grammatical correction of "is" to "in" is accepted.
2.	3	27	Ajalat, Polley & Ayoob	**Comment:** *People v. Shearer* to the extent that it suggests that a naked trespasser can have a taxable possessory interest in land appears to have been implicitly overruled in *Kaiser v. Reid* and its progeny. See your discussion on page 5. A trespasser does not have an "ascertainable period." How can a trespasser have an interest that is independent, durable, or exclusive. A trespasser does not have any on those attributes. Valuation looks forward. At the valuation date, a trespasser has nothing. How can a trespasser have "the ability to exclude from possession by means of legal process others who may interfere with that enjoyment?" AH 501, page 8, lines 8-9	The discussion is part of the legal background leading to *Kaiser v. Reid*. *People v. Shearer* illustrates the evolution of the primary criteria used to determine if a taxable possessory interest exists. The language is not intended to reflect current law.
3.	3	31	California Taxpayer's Association (Cal-Tax)	**Comment:** To the extent that *Shearer* suggests that a naked trespasser can have a taxable PI in land appears to have been implicitly overruled by *Kaiser v. Reid*. Some reference to that fact should be made or this discussion simply eliminated. How can a trespasser have an interest that is either independent, durable, or exclusive? A trespasser seems not to have any of these attributes. If the trespasser has no rights to the land, what is being valued? How can a trespasser have "the ability to exclude from possession by means of legal process other who may interfere with that enjoyment." See AH 501, Page 8, Lines 8-9.	See staff comment at #2 above.
4.	6	5	CAA	**Revise as follows:** **Rule 20.** Rule 20 begins by defining a "possessory interest" as… **Comment:** Rule 20 should have a separate title line and be in bold print to emphasize that the following sections are an explanation of this rule.	Not accepted. Inconsistent with general formatting.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
5.	7	1-5	CAA	**Revise as follows:** ~~Thus, possession means something qualitatively different than a possessor's receipt of a mere economic benefit from the use of publicly owned real property that the possessor does not occupy or have the right to occupy. Similarly, t~~The rule further defines "a right to the possession" or... **Comment:** This issue is dealt with in the subsequent discussion on exclusivity. As stated, the paragraph is confusing by raising issues not fully developed, and out of context.	Staff proposes the following language (derived from Property Tax Rule 20(c)(2)): Thus, possession requires more than incidental benefit from the public property; it requires actual physical occupation of the property pursuant to rights not granted to the general public. The rule further defines a "right to the possession" ….
6.	7	8	Cal-Tax CAA	**Revise as follows:** In other words, if the possessor acts as an agent of the public owner, the public owner's immunity or exemption from taxation extends to the possessor's activities, and there is no taxable possessory interest.	Accepted. Grammar/style.
7.	7	18-22	CAA	**Revise as follows:** ~~Example: The control of an airport runway or taxiway by the Federal Aviation Administration (FAA) or another governmental agency or its agent is so complete that it precludes the airlines from exercising sufficient authority and control over the management or operation of the runways or taxiway and does not constitute sufficient "independence" to support a possessory interest.~~ **Comment:** Delete example. Rule 20 is inconsistent with R&T Code Section 107.9, as well as with *United Airlines v. San Diego County 1* Cal.App.4th 152. The example is not an accurate depiction of the law.	Not accepted. Example is quoted directly from Property Tax Rule 20.
8.	8	26	Ajalat, Polley & Ayoob	**Comment:** The example implies that the short-term user does not have a taxable possessory interest. We see no reason why the short-term user could not have a taxable possessory interest.	Not accepted. Example is quoted directly from Property Tax Rule 20.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
9.	14	Chart	CAA	**Revise as follows:** Airport ~~office and~~ car rental counter space and leased areas **Comment:** Change represents the accurate representation of rights involved.	Accepted in concept. Revise as follows: Airport car rental counter space and other leased areas of car rental companies.
10.	16	4-5	CAA	**Revise as follows:** …discussion of a few general concepts related to valuation of taxable possessory interests ~~in general~~ and then discusses each of the specific taxable possessory interest valuation approaches. **Comment:** Redundant and unnecessary use of the word "general" within the same sentence.	Accepted. Grammar/style.
11.	16	6-7	CAA	**Revise as follows:** The valuation of taxable possessory interests is primarily addressed in ~~rule, not statute, with~~ Rule 21 ~~as the primary rule that addresses valuation~~. **Comment:** Deletion adds clarity to the reading of the section.	Accepted.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
12.	17	6	Ajalat, Polley & Ayoob Cal-Tax	**Add the following:** <u>The value of a possessory interest is typically best seen as the amount that a buyer would be willing to pay to the public owner of the real property for the income stream that the public owner will receive from the possessory interest taking into account all expenses the public owner incurs in connection with the receipt of such income stream.</u> **Comment:** There is often confusion as to what is being valued. A statement that what is being valued is the **net** value to the public owner will eliminate much of the current confusion. It will also provide guidance as to proper adjustments for each method of valuation. For example, whether using rental income or operational income, the public owner's expenses incurred in connection with such income must be taken into account. The above insertion provides the analytical basis for why that is true. If the appraiser uses comparable sales of the **possessor's** rights, several adjustments have to be made. One adjustment is the addition of any obligations assumed under the lease (such as the obligation to pay rent). Another adjustment is the deduction of any benefit received under the lease (including expenses incurred by the public owner).	Not accepted. This section addresses the standard of value, not valuation methods. Moreover, the proposed language expresses a general preference for a single approach.
13.	17	8-9	CAA	**Revise as follows:** … and best use. In brief, the highest and best use is the use that produces the greatest long-term economic return to the ~~property's owner~~ <u>land</u>. **Comment:** The property owner's economic return may be construed to relate to business enterprise, and not the assessable possessory interest. Greatest economic return to land is consistent with the classic definition of highest and best use.	Accepted in concept. See staff comment at item #14.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
14.	17	7-9	Cal-Tax	**Revise as follows: Market value and highest and best use.** A property's fair market value ~~is premised on~~ presumes the property being put to its highest and best use. ~~In brief, the highest and best use that produces the greatest long-term economic return to the property's owner.~~ The highest and best use is that use, among the possible alternative uses, that is physically practical, legally permissible, market supportable, and most economically feasible. This use, which is determined by market forces, is referred to as the property's "highest and best use." **Comment:** While this is not the place to have an extended discussion of "highest and best use" (which is described at length in AH 501, it is important that the description not be so short as to imply an improper definition. The amendment proposed is intended to clarify that the "highest and best use" is not simply a use that produces the greatest long term economic return, but a use, itself (regardless of alternative uses) that the market will support.	Staff proposes the following language to replace the draft language at page 17, lines 7 through 22: **Market value and highest and best use.** When estimating a property's fair market value, the appraiser generally presumes that the property is put to its highest and best use. The highest and best use is that use, among possible alternative uses, that is physically possible, legally permissible, financially feasible, and maximally profitable. The highest and best use produces the greatest long-term economic return to the land. When estimating the fair market value of a taxable possessory interest, the appraiser should presume that the possessory interest will be put to its permitted use—that is, the use allowed by the public owner. The permitted use defines the rights held by the possessor, which, for a taxable possessory interest, are the only taxable rights in the property. Hence, in effect, the highest and best use of a taxable possessory interest is always its permitted use.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
15.	17	9-11	Cal-Tax	**Add the following footnote:** Among alternative uses that are physically practicable, legally permitted, and economically feasible (i.e., that produce a positive net return), the highest and best use is the use that produces the highest net return.[Footnote] [Footnote] This definition of "highest and best use" should not be interpreted to allow the assessment of intangible assets that may generate part of the operating income produced by the possessory interest. See AH 502.	Not accepted. The proposed language is unclear. Intangible assets and rights are nontaxable. But property may be valued assuming the presence of intangible assets and rights necessary to put the property to beneficial and productive use. Beneficial and productive use means highest and best use (AH502, Chapter 6).
16.	17	20-22	Cal-Tax	**Revise as follows:** ~~Occasionally, the conditions of a taxable possessory interest preclude the highest and best, but in most cases the permitted use under the taxable possessory interest and the highest and best use of the property coincide.~~ Consequently, the highest and best use can never presume a use precluded by enforceable restrictions on the real property nor precluded by enforceable restrictions placed by the public owner on the possessor's possession and use of the property. **Comment:** Highest and best use can never exceed permissible uses. Any enforceable restriction must be factored into the determination of what the highest and best use is.	See staff's proposed language at item #14.
17.	17	21-22	CAA	**Revise as follows:** …best use, but in most cases the permitted use under the taxable possessory interest and the highest and best use of the property coincide. **Comment:** Corrects omission of full phrase "highest and best use."	See staff's proposed language at item #14.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
18.	17	22	CAA	**Revise as follows:** …best use of the property coincide. <u>However, the possessory interest assessment is always based upon and limited to the permitted uses which may or may not equal the highest and best use.</u> **Comment:** This section is overly complex for a general instruction manual. The section at least needs a simple summary.	See staff's proposed language at item #14.
19.	17-19		CAA	**Comment:** Delete the entire section titled "Review of Property Interests" and replace with text in Attachment A.	Not accepted. The proposed text is more difficult to understand than the draft text.
20.	17	35	Cal-Tax	**Revise as follows:** As briefly discussed in ~~the~~ Chapter 1, when a possessory interest is created, the bundle of rights that constitute the fee simple interest is divided into a possessory interest (or interests) and a nonpossessory interest (or interests).	Accepted. Grammar/style.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
21.	18	26-32	Cal-Tax	**Revise as follows:** 1. The present value of the future market (economic) rents for the rights possessed minus allowable expenses over the remaining term of the lease ~~at the market rental rate~~. 2. The present value of the future contract rents for the rights possessed minus allowable expenses over the remaining term of the lease plus what we have called the positive or negative "equity value of the leasehold interest" 3. The value of the fee simple interest for the rights possessed minus the present value of the reversionary interest (i.e., the estimated present value of the land and improvements at the termination of the lease). **Comment:** The PI is always restricted to the rights possessed. Rule 21 recognizes that economic rent can be adjusted by certain allowable expenses.	Accepted with minor rephrasing. Would read as follows: 1. The present value of the future market (economic) rents (reduced by any allowed expenses paid from the market rent by the public owner) for the rights possessed over the remaining term of the lease. 2. The present value of the future contract rents (reduced by any allowed expenses paid from the contract rent by the public owner) for the rights possessed over the remaining term of the lease, plus what we have called the positive or negative "equity value of the leasehold interest" 3. The value of the fee simple interest for the rights possessed minus the present value of the reversionary interest (i.e., the estimated present value of the land and improvements at the termination of the lease).

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
22.	18	34	Ajalat, Polley & Ayoob Cal-Tax	**Add the following:** "Full value of the leasehold interest" as defined above does not equal the fair market value of the taxable possessory interest. It is only the beginning of the analysis. Other adjustments must be made to arrive at the fair market value of the taxable possessory interest. For example, with respect to items 1 and 2, deductions for the public owner's expenses must be made. With respect to item 3, deductions for all restrictions imposed by the lease must be made.	Not accepted. See staff's proposed language at item #21.
23.	20	19-22	Ajalat, Polley & Ayoob (APA) Cal-Tax	**Revise as follows:** Thus, the *De Luz* method captures the full value of the leasehold interest. For example, it is the amount a prospective lessee might pay for the subject leasehold interest ~~if he or she prepaid the future rents at the market (economic) rental rate, with deductions from the rent for only~~ as if all future rents had been prepaid and assuming that there were no "necessary expenditures" by the public owner. ~~and recognition of the time value of money on a risk adjusted basis.~~ If the rents had not been prepaid, their present value would have to be added. If the public owner incurs expenses with respect to the taxable possessory interest, their present value would have to be deducted. **Comment (APA):** We are not sure what the staff is trying to say. It seems to us that the text confused rental income with operational income. De Luz is talking about operational income. We do not know what is meant by prepaying economic rent. The purchase price would already include economic rent. The only thing that needs to be added is contract rent. **Comment (Cal-Tax):** De Luz was talking about operational income, not rental income. The sentence as drafted seemed to confuse the two. How does one pre-pay economic rent?	See staff's proposed language below: Thus, the *De Luz* method captures the full value of the leasehold interest, whereas the *Blinn* method captured only the lessee's equity, or bonus, value in the leasehold. In other words, the value under *De Luz* is equal to the present value of the future market rents under the leasehold (reduced by any allowed expenses of the public owner paid from the market rent).
24.	21	21	Cal-Tax	**Revise as follows:** The "term of possession" is the measure of a taxable possessory interest's ~~future~~ duration. **Comment:** Future duration? Duration is by definition a period of time or existence.	Accepted.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
25.	21	22-23	CAA	**Revise as follows:** ~~It is impossible t~~To value a taxable possessory interest, a term of possession should always be considered. ~~without assuming or postulating a term of possession—t~~This variable appears in each of the taxable possessory interest valuation methods. **Comment:** Possessory interest assessments based on sales price (e.g. some boat moorings), and prepaid rent interests (e.g. housing authority low-income single family residences and condominiums) are examples where a possessory interest can be valued without the need to assume or postulate a term of possession.	Staff proposes the following language: When valuing a taxable possessory interest, the appraiser must determine a term of possession for the interest. Directly or indirectly, a term of possession is required in each of the methods for valuing a taxable possessory interest.
26.	21	22-23	Cal-Tax	**Revise as follows:** It is impossible to value a taxable possessory interest without ~~assuming or postulating a~~ establishing the term of possession—this variable appears in each of the taxable possessory interest valuation methods. **Comment:** Using the words assuming and postulating seems to infer arbitrariness or that it involves the exercise of judgment, when it normally is simply a matter of fact. There is method to setting the term of possession, otherwise, the valuation of the PI is itself arbitrary.	See staff comment item #25.
27.	21	22-23	Ajalat, Polley & Ayoob	**Revise as follows:** It is impossible to value a taxable possessory interest without ~~assuming or postulating~~ determining ~~a~~ the term of possession—this variable appears in each of the taxable possessory interest valuation methods.	See staff comment item #25.
28.	21	24	Cal-Tax	**Revise as follows:** ~~The term of possession also significantly affects the valuation.~~ **Comment:** This sentence is confusing. In the prior two sentences it is established that the term of possession is an element in valuation. Ipso facto, the, it affects valuation.	See proposed staff language below. This would replace lines 24 to 27. The term of possession also affects the value of a taxable possessory interest. All else being equal, the longer the term of possession, the higher the value of the possessory interest.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
29.	21	24-27	Cal-Tax	**Revise as follows:** A one-year term of possession means that the taxable possessory interest will be valued at only a small fraction of the value of the fee simple interest; whereas a 35~~25~~-year term of possession means that the value of the taxable possessory interest will approach the value of the fee simple interest. It should also be noted that as each year of a term of possession expires, the value of the possessory interest will be negatively affected as well. **Comment:** 25 years is way too short for the period of ownership to approximate fee simple values.	See staff comment item #28.
30.	21	28-29	Ajalat, Polley & Ayoob	**Revise as follows: Reasonably anticipated term of possession.** Rule 21 defines the term of possession through a standard called the "reasonably anticipated term of possession~~."~~ The reasonably anticipated term will generally be the stated term of possession as set forth in the agreement between the possessor and the public owner.	Not accepted. See staff comment at item #31.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
31.	21- 22	28-36 1-5	Cal-Tax	**Revise as follows: Reasonably anticipated term of possession.** Rule 21 defines the "term of possession ~~through a standard called~~ for valuation purposes" as the "reasonably anticipated term of possession." The reasonably~~-~~anticipated standard applies to all taxable possessory interests regardless of the type of real property or form of tenancy (e.g., month-to-month, long-term, or some other type of relationship). As stated in subsection (d)(1)~~(2)~~ of the rule, ~~the reasonably anticipated term of possession is "demonstrated by intent of the public owner and the private possessor, and similarly situated parties," through criteria such as the following:~~ "[t]he stated term of possession shall be deemed the reasonably anticipated term of possession unless it is demonstrated by clear and convincing evidence that the public owner and the private possessor have reached a mutual understanding or agreement, whether or not in writing, such that the reasonably anticipated term of possession is shorter or longer than the state term of possession." ~~1. The sales prices of the subject and comparable taxable possessory interests~~ ~~2. The rules, policies and customs of the public owner and other similarly situated public owners~~ ~~3. The customs and practices of the private possessor and similarly situated private possessors~~ ~~4. The history of the public owner and the private possessor and similarly situated public owners and private possessors~~ ~~5. The actions of the public owner and the private possessor, such as investments in improvements by the public owner or the private possessor~~ **Comment:** Rule 21 clearly sets the stated term of possession as the default. The draft begins with the exception to the rule. Only if there is no stated term, or the assessor establishes by clear and convincing evidence that the parties have established and intend a different term of possession does the assessor look to the demonstrated intent.	Not accepted. The draft begins with a description of the reasonably anticipated standard, followed by a discussion of how the standard is applied in cases where there is or is not a stated term of possession. This presents the material in a more logical order.

NO.	PAGE/LINE REFERENCE		SOURCE	PROPOSED LANGUAGE	SBE STAFF POSITION
32.	21-22	31	Ajalat, Polley & Ayoob	Page 21, line 31 through page 22 line 5, move text beginning with "As stated" to page 23, after line 17. **Comment:** Most of the time the term of possession need not be assumed or postulated. It merely needs to be looked up. The Staff draft misleads the reader to think that typically the reasonably anticipated term is a matter of judgment, when it typically is a given fact. The AH starts out with the exception to the rule and not the rule. This also misleads the reader to think that he should apply the factors to determine the reasonably anticipated term. The AH should start with the general rule, the stated term. The factors should come at the end after the appraiser has determined that he can prove a mutual agreement contrary to the stated term by clear and convincing evidence.	Not accepted. See staff comment item 31.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
33.	21- 22	35-36 1-5	CAA	**Revise as follows:** ~~1. The sales prices of the subject and comparable taxable possessory interests~~ ~~2. The rules, policies and customs of the public owner and other similarly situated public owners~~ ~~3. The customs and practices of the private possessor and similarly situated private possessors~~ ~~4. The history of the public owner and the private possessor and similarly situated public owners and private possessors~~ 5. ~~The actions of the public owner and the private possessor, such as investments in improvements by the public owner or the private possessor~~ 1. The sales price of the subject taxable possessory interest and the sales prices of comparable taxable possessory interests. Sales of existing possessory interests indicate anticipated terms of considerable length since both buyer and seller consider the subject property rights valuable enough to transfer. 2. The rules, policies, and customs of the public owner and of similarly situated public owners. Examples of such policies include the practice of writing leases for certain types of property rights to include terms of a particular length. 3. The history of the subject taxable possessory interest's use and the histories of the uses of comparable taxable possessory interests. Such histories may indicate a typical length of term practiced by the majority of the typical lessees or permittees. 4. The history of the relationship of the parties to the subject taxable possessory interest and the histories of the relationships of similarly situated parties. Such histories may include a particular lessee's history of leasing the property for a consecutive series of two or more separate periods for a particular length of possession. 5. The actions of the parties to the subject taxable possessory interest, including any amounts invested in improvements by the public owner or the possessor. Actions such as investment outlays by the lessee may indicate an intention of the parties to continue the agreement. Other actions taken by the public owner, such as an agreement to not renew, clearly demonstrate that. **Comment:** The factors of a reasonably anticipated term in the staff proposed version could be more instructive and provide direct examples.	Not accepted. The added language does not significantly clarify the draft language.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
34.	22	6	Cal-Tax	**Revise as follows:** Rule 21 defines the "stated term of possession" of a taxable possessory interest as the remaining period of possession on the valuation date as specified in the lease or other legal instrument that created, renewed, or extended the taxable possessory interest (including any option periods if it is reasonable to assume that the option or options will be exercised).[30] Also under the rule, however, certain taxable possessory interests are deemed to not have a stated term of possession, such as those created by month-to-month leases or agreements. The presumption regarding stated term of possession is not applicable to these taxable possessory interests. ~~Under Rule 21, the stated term of possession is presumptively the reasonably anticipated term of possession unless there is "clear and convincing" evidence that demonstrates that the possessor and the public owner have reached a mutual understanding or agreement, oral or written, such that the reasonably anticipated term of possession is shorter or longer than the stated term of possession. Also under the rule, however, certain taxable possessory interests are deemed to not have a stated term of possession, such as those created by month-to-month leases or agreements. The presumption regarding stated term of possession is not applicable to these taxable possessory interests.~~ ~~Section 115 of the California Evidence Code defines burden of proof as "the obligation of a party to establish by evidence a requisite degree of belief concerning a fact in the mind of the trier of fact or the court." The party with the burden of proof is required to establish the existence or nonexistence of a fact by producing evidence that satisfies a required standard. It is the assessor's burden to prove that the reasonably anticipated term of possession differs from the stated term of possession. In general, this means that the assessor must present evidence that the private possessor and the public owner have reached an understanding in regard to future possession of the property that differs from the stated term of possession (i.e., remaining term under the existing agreement).~~ ~~Unless otherwise provided by law, the required civil burden of proof in California is proof by a preponderance of the evidence.~~[31] ~~A preponderance of the evidence is usually defined "in terms of probability of truth" and as evidence which, when weighed against evidence offered in opposition to it, "has more convincing force and the greater probability of truth."~~[32] **Comment:** This lengthy discussion of the "preponderance standard" is superfluous and confusing. The standard is clear and convincing and should not be muddled with a lengthy discussion of what a preponderance standard is.	Accepted in concept. See staff's proposed language below (this replaces the text from page 22, line 6 through page 23, line 17):

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
			Staff	<u>Rule 21 defines the "stated term of possession" of a taxable possessory interest as the remaining period of possession on the valuation date as specified in the lease or other legal instrument that created, renewed, or extended the taxable possessory interest (including any option periods if it is reasonable to assume that the option or options will be exercised).</u> <u>Under Rule 21, the stated term of possession is presumed to be the reasonably anticipated term of possession unless there is "clear and convincing" evidence that demonstrates that the possessor and the public owner have reached a mutual understanding or agreement, oral or written, such that the reasonably anticipated term of possession is shorter or longer than the stated term of possession.</u> <u>If the assessor successfully demonstrates by clear and convincing evidence that the public owner and the possessor have reached a mutual understanding or agreement such that the reasonably anticipated term of possession differs from the stated term of possession, the term of possession for valuation purposes is the stated term of possession as modified by the terms of the mutual understanding or agreement. Such a mutual understanding or agreement may be proved by evidence relating to the conduct of one or both parties. The conduct must prove by clear and convincing evidence that there is a mutual understanding or agreement between the parties. For example, if the possessor makes substantial improvements in anticipation that the term will be extended, the reasonably anticipated term will not include the extended period until there is an actual mutual understanding or agreement that the term will be extended. The reasonably anticipated term of possession so demonstrated may be longer or shorter than the stated term of possession.</u> <u>Also under Rule 21, certain taxable possessory interests are deemed to not have a stated term of possession, such as those created by month-to-month leases or agreements. The presumption regarding stated term of possession does not apply to these taxable possessory interests. Examples of such taxable possessory interests include taxable possessory interests than run from month-to-month, taxable possessory interests without a fixed term, and taxable possessory interests of otherwise unspecified duration.</u> <u>For a taxable possessory interests that are without stated terms of possession, the assessor should determine a term of possession on each valuation date using the criteria for the reasonably anticipated term of possession listed above together with other relevant criteria.</u>	
35.	22	13	CAA	**Revise as follows:** …possession. <u>Examples of such evidence are enumerated above.</u> Also under the rule however, certain taxable possessory interests are deemed to not… **Comment:** The paragraph needs to provide guidance to the factors to be considered in the "clear and convincing" evidence standard.	Not accepted. See staff comment item #33.
36.	22	30-32	Cal-Tax	**Revise as follows:** In order to overcome the presumption that the stated term of possession is the reasonably anticipated term of possession~~, however,~~ the required burden of proof is clear and convincing evidence.	Accepted in concept. See staff's revised language at item #34

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
37.	22-23	All	CAA	**Comment:** All references to "clear and convincing evidence" should be stricken and replaced with "preponderance of evidence" as the appropriate standard. The CAA is of the opinion that the "clear and convincing evidence" standard is not appropriate and has no legal basis. The CAA is considering a Section 538 action challenging this provision.	Not accepted. "Clear and convincing evidence" is the standard prescribed in Rule 21.
38.	23	1-2	Cal-Tax	**Revise as follows:** …other words, a preponderance calls for ~~probability~~ <u>merely or more likely than not</u> while "clear and convincing proof demands a high probability."[34] **Comment:** Technically, everything is probable. While we typically use probably to mean more likely than not, it is not its actual, technical meaning.	Not accepted. See staff's proposed language at item #34 (removes all language at left).
39.	23	1-2	Ajalat, Polley & Ayoob	**Revise as follows:** …other words, a preponderance calls for <u>merely a more likely than not</u> probability while "clear and convincing proof demands a higher probability." **Comment:** Technically, everything is probable. It may have a 1 in 10,000 probability or a 99 in 100 probability. In common language we use probable to mean more likely than not, but that is not it's technical meaning.	Not accepted. See staff's proposed language at item #34 (removes all language at left).

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
40.	23	3-9	Cal-Tax	**Revise as follows:** If the assessor successfully demonstrates by clear and convincing evidence that the public owner and the possessor have reached a mutual understanding or agreement such that the reasonably anticipated term of possession differs from the stated term of possession, the term of possession for valuation purposes is the stated term of possession as modified by the terms of the mutual understanding or agreement. Such a mutual understanding or agreement may be proved by evidence relating to the conduct of ~~one or both~~ the parties. The conduct must prove by clear and convincing evidence that there is a mutual understanding or agreement between the parties. The conduct of one or both parties which evidences that one or both of them anticipate that the term will be other than the stated term by itself is not evidence of an agreement or understanding. For example, if the possessor makes substantial improvements in anticipation that the term will be extended, the reasonably anticipated term will not include the extended period until there is an actual mutual understanding or agreement that the term will be extended. The reasonably anticipated term of possession so demonstrated may be longer or shorter than the stated term of possession. **Comment:** If the assessor ignores the stated term, the evidence must reflect the MUTUAL understanding of the parties. One person's intent does not an agreement or understanding make.	Accepted in part. See staff's proposed language at item #34.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
41.	23	8	Ajalat, Polley & Ayoob	**Add the following:** The conduct must prove by clear and convincing evidence that there is a mutual understanding or agreement between the parties. The conduct of one or both parties which evidences that one or both of them anticipate that the term will be other than the stated term by itself is not evidence of a mutual agreement or understanding. For example, it the possessor makes substantial improvements in anticipation that the term will be extended, the reasonably anticipated term will not include the extended period until there is an actual mutual understanding or agreement that the assessor can prove by clear and convincing evidence. **Comment:** Add the above text after the word "parties."	Accepted in part. See staff's proposed language at item #34.
42.	23	10-12	Cal-Tax	**Revise as follows:** As noted above, ~~for taxable possessory interests without a stated term of possession,~~ the presumption that the stated term of possession is the reasonably anticipated term of possession is not applicable in certain circumstances. **Comment:** This is just confusing. The Rule says, that although there is a stated term (i.e., month-to-month) the presumption doesn't apply. It doesn't say there is no stated term. As drafted it is a non-sequitor.	Not accepted. If there is a stated term of possession, the presumption applies. If there is not a stated term of possession, the presumption does not apply. Rule 21 specifically designates month-to-month tenancies as not of a stated term. See also item #34.
43.	23	13	CAA	**Revise as follows:** …tha~~n~~t run from month to month, taxable possessory interests without a fixed term, and taxable… **Comment:** grammar/typographical error	Accepted. Grammar/style.
44.	23	14-17	Cal-Tax	**Delete the following:** ~~For a taxable possessory interest that is without a stated term of possession, the assessor should determine a term of possession on each valuation date using the criteria for the reasonably anticipated term of possession listed above together with other relevant criteria.~~	Not accepted. The draft language provides guidance concerning the treatment of interests without a stated term of possession. This is appropriate. See also item #34.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
45.	23	16	Ajalat, Polley & Ayoob	**Revise as follows:** …valuation date using the criteria for the reasonably anticipated term of possession listed ~~above~~ below together with other relevant criteria.	Not accepted. See staff comment item #31.
46.	23	17	Cal-Tax	**Revise as follows:** If there is no stated term of possession or the presumption in favor of the stated term is prohibited by the Rule, the reasonably anticipated term of possession can be established by demonstrating the intent of the public owner and the private possessor, as well as by establishing the intent of similarly situated parties through criteria such as the following: 1. The sales prices of the subject and comparable taxable possessory interests 2. The rules, policies and customs of the public owner and other similarly situated public owners 3. The customs and practices of the private possessor and similarly situated private possessors 4. The history of the public owner and the private possessor and similarly situated public owners and private possessors **5.** The actions of the public owner and the private possessor, such as investments in improvements by the public owner or the private possessor	Not accepted. See staff comment item #31.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
47.	23- 24	18-31 1-4	Cal-Tax	**Delete the following:** ~~**Recurring taxable possessory interests.** A taxable possessory interest may recur from year to year without the possession, right to possession, or claim to a right to the possession inherent in the interest being continuous in time. That is, the possession, right to possession, or claim to a right to possession may apply to a recurring annual time period that is less than the entire year.[36]~~ ~~If the contract term of an annually recurring taxable possessory interest begins each year after January 1 but ends before January 1 of the succeeding year, then it could be argued that the taxable possessory interest does not exist on the January 1 lien date of any given year and that, as a consequence, the annually recurring taxable possessory interests are subject only to annual supplemental assessments. In other words, each year a new taxable possessory interest would be created with a reasonably anticipated term of possession of less than one year, causing annual changes in ownership with resulting annual supplemental assessments.~~ ~~Under *Dressler v. County of Alpine*, however, a history of annually recurring taxable possessory interests with contract terms of less than one year ending on or before December 31 of each year may nevertheless, under appropriate facts, establish the existence of an actual or constructive possession, right to possession, or claim to a right to Possession that extends to each January 1 lien date.[37] Pursuant to this authority, under appropriate facts, assessors may make annual lien date assessments of such recurring taxable possessory interests provided that their reasonably anticipated terms of possession are at least one year in length.[38]~~ **Comment:** This discussion on recurring use is at best in an inappropriate place as it has little to do with Term of Possession under Rule 21. Moreover, Dressler was addressing the existence of a PI, in particular the question of durability, not term of possession. On the issue of valuation, Dressler concerned itself with the comparable sales approach.	Accepted in part. Staff proposes the following: Delete draft language at page 23, lines 22 through 28. Move language at page 23, line 18 through page 24, line 4 (excluding deleted part above) and place at page 13, line 25 under its own heading.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
48.	23	22-28	CAA	**Revise as follows:** ~~If the contract term of an annually recurring taxable possessory interest begins each year after January 1 but ends before January 1 of the succeeding year, then it could be argued that the taxable possessory interest does not exist on the January 1 lien date of any given year and that, as a consequence, the annually recurring taxable possessory interests are subject only to annual supplemental assessments. In other words, each year a new taxable possessory interest would be created with a reasonably anticipated term of possession of less than one year, causing annual changes in ownership with resulting annual supplemental assessments.~~ **Comment:** This paragraph is inconsistent with the paragraph that follows. The supposition on line 22 that the term is "an annually, recurring taxable possessory interest" makes it subject to *Dressler* cited as authority for annual lien date assessments. Reference should be made to *Carlson v. City of San Jose* 57 Cal.App.4th 1348.	Accepted. See staff comment item #47.
49.	23	29	Ajalat, Polley & Ayoob	**Comment:** Dressler was addressing whether there existed something that could be taxed. This section is dealing with term of possession. This section seems to imply that the rules discussed above about stated term and reasonably anticipated term do not apply here. This implication is incorrect and should be eliminated. Footnote 36 states the using a long term will generally result in a somewhat lower assessment than if the interest's shorter reasonably anticipated term of possession is used. We do no know how that is possible.	Not accepted. See also staff comment item #47. Re footnote 36: In this context, the alternative terms of possession are one year or a period less than one year, and there is a single payment. An amount X, discounted for 1 year, will be less than the same amount X discounted for a period less than 1 year.
50.	23	29	CAA	**Revise as follows:** Under *Dressler v. County of Alpine*, ~~however,~~ a history of annually recurring taxable possessory… **Comment:** Harmonizing grammatically with previous recommendation.	Accepted. See also staff comment item #47.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
51.	24	3-4	CAA	**Revise as follows:** …date assessments of such recurring taxable possessory interests, provided that the appraised term of possession is one year ~~their reasonably anticipated terms of possession are at least one year in length~~. **Comment:** Paragraph should be logically consonant with Section 61(b)(2).	Not accepted. Draft language is accurate ("appraised term of possession" must be the reasonably anticipated term of possession).
52.	24	5-10	Cal-Tax	**Delete the following:** ~~**"Terminating" taxable possessory interests.** A special case exists when the evidence establishes that at a certain future date the public owner of the real property will no longer make the real property available for private possession. This situation is sometimes called a "terminating taxable possessory interest." If the evidence establishes the existence of a terminating taxable possessory interest, the term of possession on each valuation date should be the anticipated remaining period that the real property will be available for private possession.~~ **Comment:** Moved "Terminating taxable PI" to Page 50.	Not accepted. This discussion relates to term of possession and therefore is appropriately placed.
53.	24	10	Ajalat, Polley & Ayoob	**Revise as follows:** …that the real property will be available for private possession or the stated term, whichever is shorter.	Accept in concept. Staff proposes the following language: …that the real property will be available for private possession or the reasonably anticipated term of possession, whichever is shorter.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
54.	24	15-17	Cal-Tax	**Revise as follows:** However, the conventional approaches must be modified to accommodate the finite duration of a taxable possessory interest and the corresponding fact that the portion of the fee simple interest retained by the public owner, the reversionary interest, and other retained interests, are ~~is~~ nontaxable and that other portions of the fee simple interest may have been granted to others.[39]	Not accepted. The meaning of the proposed language is unclear. However, see staff's proposed language below. However, the conventional approaches must be modified to accommodate the finite duration of a taxable possessory interest and the corresponding fact that a portion of the fee simple interest relating to a taxable possessory interest, the reversionary interest, is retained by the public owner and is nontaxable.
55.	24	17	Ajalat, Polley & Ayoob	**Revise as follows:** …retained by the public owner, the reversionary interest and other retained interest, is nontaxable and that other portions of the fee simple interest may have been granted to others.	Not accepted. See staff comment item #54.
56.	24	18-26	Ajalat, Polley & Ayoob	**Revise as follows:** A taxable possessory interest may be valued using the "direct methods or "indirect methods." With the direct methods, the appraiser directly estimates the present value of the rights held by the possessor over the ~~reasonably anticipated~~ term of possession. With the indirect methods, the appraiser estimates the value of the rights in the taxable possessory interest as if it were owned in perpetuity (i.e., as if it were owned in fee simple and subtracts the estimated present value of the nontaxable reversionary right and other rights retained by the public owner or granted to others, leaving a remainder equal to the value of the taxable possessory interest. The indirect methods thus require estimates of at least two values: the as-if-owned-in-fee value and the present value of the nontaxable, publicly owned reversion and other rights retained by the public owner or granted to others. [40]	Not accepted. The proposed language is not accurate because the as-if-in-fee value of the taxable possessory interest relates only to the rights held by the possessor.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
57.	24	18-26	Cal-Tax	**Revise as follows:** A taxable possessory interest may be valued using the "direct methods or "indirect methods." With the direct methods, the appraiser directly estimates the present value of the rights held by the possessor over the ~~reasonably anticipated~~ term of possession. With the indirect methods, the appraiser estimates the value of the rights in the taxable possessory interest as if it were owned in perpetuity (i.e., as if it were owned in fee simple and subtracts the estimated present value of the nontaxable reversionary right <u>and other rights</u> retained by the public owner <u>or granted to others</u>, leaving a remainder equal to the value of the taxable possessory interest. The indirect methods thus require estimates of <u>at least</u> two values: the as-if-owned-in-fee value and the present value of the nontaxable, publicly owned reversion <u>and other rights retained by the public owner</u>. [40]	Not accepted. See item #56.
58.	25	18	Ajalat, Polley & Ayoob Cal-Tax	**Add the following:** <u>The value of a possessory interest is typically best seen as the amount that a buyer would be willing to pay to the public owner of the real property for the income stream that the public owner will receive from the possessory interest taking into account all expenses the public owner incurs in connection with the receipt of such income stream.</u> **Comment:** There is often confusion as to what is being valued. A statement that what is being valued is the **net** value to the public owner will eliminate much of the current confusion. It will also provide guidance as to proper adjustments for each method of valuation. For example, whether using rental income or operational income, the public owner's expenses incurred in connection with such income must be taken into account. The above insertion provides the theoretical basis for why that is true. If the appraiser uses comparable sales of the possessor's rights, several adjustments would have to be made. One adjustment would be to add any obligations assumed under the lease (such as the obligation to pay rent). Another adjustment would be to deduct any benefit received under the lease (such as expenses incurred by the public owner).	Not accepted. The proposed language states a general preference for a single approach.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
59.	25	26-31	Ajalat, Polley & Ayoob	**Revise as follows:** 2. Add the present value on the sale date of the unpaid contract rent for the ~~reasonably anticipated~~ term of possession (in ~~some~~ <u>most</u> cases, this will be based on the stated term of possession; in others, it will be based on the criteria in Rule 21). The contract rent should be reduced by any expenditure <u>by the public owner</u> necessary to maintain the income from the taxable possessory interest during the possessor's ~~reasonably anticipated~~ term of possession, including any element of "gross outgo" as defined in subsection (c) of Rule 8.	Accepted in part. See staff comment at item #60.
60.	25	26-31	Cal-Tax	**Revise as follows:** 2. Add the present value on the sale date of the unpaid contract rent for the ~~reasonably anticipated~~ term of possession (~~in some cases,~~ this will be based on the stated term of possession~~; in~~ <u>or</u> ~~others, it will be based~~ on the <u>other</u> criteria in Rule 21). The contract rent should be reduced by any expenditure <u>by the public owner</u> necessary to maintain the income from the taxable possessory interest during the possessor's reasonably anticipated term of possession, including any element of "gross outgo" as defined in subsection (c) of Rule 8. <u>Examples of allowable expenses ("gross outgo") include but are not limited to, security services, maintenance, administration, trash removal, facility improvements, utility fees, advertising and promotional services, etc.</u>	Accepted in part. Staff proposes the following language: 2. <u>Add the present value on the sale date of the unpaid contract rent for the reasonably anticipated term of possession (based on the stated term of possession or the stated criteria in Rule 21, as applicable). The contract rent should be reduced by any expenditure by the public owner necessary to maintain the income from the taxable possessory interest during the possessor's reasonably anticipated term of possession, including any element of "gross outgo" as defined in subsection (c) of Rule 8.</u>

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
61.	26	5-8	CAA	**Delete the following:** ~~5. Subtract the present value on the sale date of any future contractually entitled cash receipts that the buyer will receive associated with the possession of the property (the salvage value of, or the reimbursement value for, any possessor-constructed improvements at the termination of the taxable possessory interest).~~ **Comment:** Confusing, contradictory and ambiguous. Unable to determine factual situation associated with this guideline.	Not accepted. But see proposed staff language below, which comes directly from Rule 21(e)(1)(A). 5. Subtract the present value on the sale date of any future contractually entitled cash receipts that the buyer will receive associated with the possession of the property (e.g., the salvage value of, or the reimbursement value for, improvements existing at the end of the term of possession.
62.	26	18-22	Cal-Tax	**Revise as follows:** If the future contract rents are not prepaid (the typical case), the sale price is only an indicator of the equity value of the leasehold. To arrive at the consideration paid for the taxable possessory interest (i.e., the "full value of the leasehold interest"), the appraiser must add the present value of the unpaid future contract rents and subtract allowable expenses for the reasonably anticipated term of possession from ~~to~~ the cash equivalent equity sale price.	Accepted in concept. Would revise slightly as follows: … the appraiser must add the present value of the unpaid future contract rents (reduced by any allowed expenses paid by the public owner) for the reasonably anticipated term of possession to the cash equivalent equity sale price.
63.	26	32	Cal-Tax	**Add the following:** Such obligated costs do not include allowable expenses that the public owner pays in order to continue the production of income from the property. For example, janitorial services, security services, advertising and promotion expenses, maintenance and repair, management and administrative expenses would not be included.	Not accepted. The draft language refers to obligated costs of the buyer of a taxable possessory interest, which is not related to expenses paid by the public owner.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
64.	27	3	Cal-Tax	**Revise as follows:** **EXAMPLE 3.1** **USING THE COMPARATIVE SALES APPROACH-DIRECT METHOD** **TO VALUE TAXABLE POSSESSORY INTEREST** Subject taxable possessory interest: the right to possess a cabin in a national forest. PERTINENT INFORMATION: • Purchase price: $76,000 (cash) • Reasonably anticipated term of possession: 20 years • Annual contract land rent: $1,200 • Allowable Expenses: 3% management, $50 per year road and tree maintenance; total allowable expenses: $86 per year. • Assume that the sale of the subject cabin occurred 2 years ago; market values of comparable cabins have increased about 10% per year since the sale date of the subject cabin; thus, use $15,000 as market conditions adjustment. • Capitalization (discount) rate used to discount future contract rent, exclusive of property taxes: 12% (It is not necessary to add a property tax component to the discount rate because the possessor will pay the possessory interest taxes.) The sale price of the subject property itself is used to derive the value indicator: thus, no Adjustment for comparability is required. Accordingly, the only required adjustments are for market conditions and the present value of unpaid future contract rent. If this sale were used as a comparable in the valuation of another subject property, the adjustment for market conditions might be different, and an additional adjustments for property attributes (i.e., the comparable vis-a-vis the subject property) also might be necessary. Equity Sale Price of Subject $76,000 Market Conditions Adjustment 15,000 Add Present Value of the Contract Rent ($1,200 less $86 = $1114/yr for 20 yrs. @ 12%) PV$1PP (annual)/20 yrs./12% = 9.13 $1,114 ~~$1,200~~ x 9.13 10,170~~10,956~~ Adjusted Sale Price $101,170~~101,956~~ Indicated Value of Subject $101,170~~101,956~~ Say, $101,000~~101,500~~ * Although…	Accepted. Will designate as "Allowed expenses paid by the public owner"

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
65.	27	3	CAA	**Comment:** Unable to suggest alternative example, given unclear objective of original. The reason for doing the appraisal should be stated at the beginning of the example. It is not apparent why we are valuing the property two years after the sale. Also, since this is a sales approach, shouldn't the example provide a more traditional and common sales comparable format, and not attempt to address other issues with the main problem?	The purpose of the example is to illustrate issues specific to the valuation of taxable possessory interests. Therefore, providing "a more traditional and common sales comparable format" was not necessary. Also, the reason for valuing the property two years after the sale does not affect the example.
66.	27	3	CAA	**Revise as follows:** PV$1PP (annual)/20yrs./12% = ~~9.13~~ 7.47 **Comment:** The indicated factor for PW1PP/20 yrs./12% is not 9.13. Also, following computations would obviously require correction.	Accepted.
67.	27	3	CAA	**Delete Portion of Footnote As Follows:** ~~Also, the present value of any contractually entitled benefits received by the buyer (in addition to the right to possession) should be subtracted from the equity sale price. The part of the purchase price paid for such benefits is not part of the consideration paid for the right to possession.~~ **Comment:** The footnote adjustments for contractual entitled benefits received by the buyer should be excluded for the same reasons enumerated on page 26 lines 5-8. Again, it is unclear what is being adjusted. Also, since the footnote has no attribution to the body of the example, it is difficult to see how it would be handled in the methodology.	Accepted. Footnote is not relevant to the example as presented.
68.	28	2-5	CAA	**Revise as follows:** In the comparative sales approach-indirect comparison method, the taxable possessory interest value is derived ~~the appraiser derives a value indicator using the estimated value of the subject taxable possessory interest as if it were owned in fee and the estimated value of the nontaxable publicly owned reversion. This method involves the following steps:~~ by employing the two following steps: **Comment:** The preamble is redundant to the body of the text and adds no additional emphasis to the procedure.	Not accepted. Although somewhat redundant, this intro parallels that of the comparative sales approach-direct method.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
69.	28- 29	31-34 1-8	CAA	**Delete the following:** ~~1. If the reasonably anticipated term of possession on the valuation date is relatively lengthy (e.g., greater than 15 years), assume that the estimated as-if-in-fee value of the subject taxable possessory interest will increase at something approaching the long-term inflation rate (e.g., 3-4 percent per year) and use this amount as the estimated value of the reversion. Then, discount this value at an "appropriate" discount rate to arrive at the estimated present value of the reversion.~~ ~~2. If the reasonably anticipated term of possession is intermediate in length (i.e., 6 to 15 years), and a growth rate different from the long-term rate is expected, use this rate to estimate the value of the reversion. Discount this value to its present value as in No. 1.~~ ~~3. If the reasonably anticipated term of possession is relatively short (5 years or less), do as in No. 2 or simply use the estimated as-if-in-fee value as the present value of the reversion.~~ **Comment:** The example is not specific as to the components of the discount rate. The long term inflation rate is not distinguished from the real growth rate.	Accepted in concept. Delete page 28, line 31 through page 29, line 7 (passage at left). Revise page 28., lines 27 through 30, as follows: **Present value of the reversion.** An estimate of the present value of the reversionary interest is required in both the comparative sales approach-indirect method and the income approach-indirect method (discussed below). Estimating the present value of the reversion first requires an estimate of its future value (i.e., the value of the reversionary interest at the end of the reasonably anticipated term of possession); this estimated future value is then discounted to its present value.
70.	30	3	CAA	**Comment:** Delete entire example (i.e., Example 3.2), pending correction of imprecise terminology and methodology. The four percent growth rate does not relate to the inflation rate, and stands outside real life experience. If the four percent is an inflation rate, it should be built into the discount rate.	Accepted. See staff comment item #69.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
71.	31	7	Cal-Tax	**Revise as follows:** …either (1) the estimated <u>net</u> market (economic) rent attributable to the taxable possessory interest or…	Staff proposes the following: 1) replace draft language at page 31, lines 4 through 10, with the language below; 2) retitle heading at page 31, line 11 as Estimating the Market (Economic) Rent"; and 3) delete draft language at page 31, lines 24 through 36 (becomes part of proposed new language); and delete draft language at page 32, lines 18 through 35 (becomes part of proposed new language).

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
			Staff	**General.** The income to be capitalized when valuing a taxable possessory interest is the "net return" attributable to the taxable possessory interest, which is “gross return” less “gross outgo.” As defined in subsection (c) of Rule 8, gross return means any money or money’s worth that the taxable property will produce. Gross outgo means any outlay of money or money’s worth required to develop and maintain the estimated income. Gross outgo is also referred to herein as allowed expenses. Elements of gross outgo, or allowed expenses, include the following, as applicable: cost of goods sold, typical operating expenses, typical management expense, an allowance for a return on working capital, and an allowance for a return on and a return of the value of any nontaxable property that contributes to the gross operating income. Typical operating expenses may include expenses for the rental of personal property, for the provision of security services, and for advertising and promotional services, provided such expenses are necessary for the production of the gross income from the subject taxable possessory interest. Typical operating and management expenses include expenses that an owner/operator typically would bear to maintain the property and to continue the production of income from the property but which, in the case of the subject taxable possessory interest, are borne by the public owner. Gross outgo, or allowed expenses, does not include the following: amortization, depreciation, depletion charges, debt retirement, interest on funds invested in the taxable possessory interest, the contract rent for the taxable possessory interest, property taxes on the taxable possessory interest, income taxes, or state franchise taxes measured by income. The income to be capitalized may be based on either rental or operating income. The rental income should reflect the estimated market (economic) rent for the subject taxable possessory interest. Rental income is preferred because operating income may be influenced by managerial skill or derived, in part, from nontaxable property. **With Rental Income.** When estimating the income to be capitalized, or net return, from rental income, elements of gross outgo, or allowed expenses, paid by the public owner must be subtracted from the rental income. The amount and type of allowed expenses to be subtracted depends on the structure of the lease or agreement related to the taxable possessory interest. In a gross lease, all operating expenses, including property taxes, are included in the stated, or contract, rent, and the landlord/public owner pays these expenses from the stated, or contract, rent. Thus, all allowed expenses must be subtracted from a gross rent. In a net lease, most operating expenses, including property taxes, are excluded from the stated, or contract rent, and these expenses are paid by the tenant/private possessor in addition to the stated, or contract, rent. Thus, few expenses must be subtracted from a net rent. Some lease structures are hybrids of these pure forms, with the landlord/public possessor paying specified expenses and the tenant/possessor paying others. In these cases, the amount and type of expenses that must be subtracted from the rental income will vary. Even with a net lease, however, it may be necessary to subtract some expenses from the net rent. The landlord/public owner must manage and administer the taxable possessory interest and may incur other allowed expenses related to the taxable possessory interest that are not paid by the tenant/possessor and must be paid out of the net rent. The use of comparable rental data based on a lease structure (i.e., gross vs. net) similar to that of subject taxable possessory interest is preferred. Otherwise, the appraiser must adjust the comparable rental data to reflect the lease structure of the subject property. **With Operating Income.** When estimating the income to be capitalized, or net return, from operating income, all elements of gross outgo, or allowed expenses, whether paid by the landlord/public owner or by the tenant/possessor, must be subtracted from the gross return. “Gross operating income” and “net operating income” are defined consistent with "gross return" and "net return," respectively, in subsection (c) of Rule 8.	

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
72.	31	10	Cal-Tax	**Add the following:** <u>The "net return" that is to be capitalized is the net return to the public owner. When computing the net return from rent, expenses of the public owner that are necessary to continue the production of income from the property must be subtracted. When computing the net return from operating income, both operating expenses of the possessor and expenses of the pubic owner must be subtracted.</u>	Accepted in concept. See proposed staff language at item #71.
73.	31	24-36	Cal-Tax	**Delete the following:** ~~The structure of a lease can vary in terms of how operating expenses are paid. In a gross lease, all operating expenses, including property taxes, are included in the stated, or contract, rent, and the landlord pays these expenses from the stated, or contract, rent. In a net lease, all operating expenses, including property taxes, are excluded from the stated, or contract rent, and these expenses are paid by the tenant in addition to the stated, or contract, rent. Some lease structures are hybrids of these pure forms, with the landlord paying some types of expenses and the tenant paying others.~~ ~~When using contract rents from comparable properties as an indicator of the market (economic) rent for the subject taxable possessory interest, a contract rent with the same lease structure as the subject taxable possessory interest with regard to the payment of operating expenses is preferred. In doing so, the appraiser avoids the necessity of adjusting the contract rent such that it reflects a lease structure, with regard to the payment of operating expenses, that is comparable to that of the subject taxable possessory interest.~~	See proposed staff language at item #71.
74.	31	28	CAA	**Revise as follows:** …expenses are paid by the tenant in addition to the stated, or contract~~,~~ rent. **Comment:** Punctuation error.	Accepted. But see proposed staff language at item #71.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
75.	32	17	Cal-Tax	**Add the following: <u>Allowable Expenses-Rental Income</u>** <u>All the necessary expenses of the public owner must be subtracted from the gross rent to compute the net return to the public owner. Allowable expenses that need to be subtracted are expenses that are necessary to continue the production of income from the property but are borne by the public owner, such as maintenance and repair, security services, general clean up and janitorial services, marketing and advertisement, management/administration, etc.</u> <u>The amount of expenses that must be subtracted will depend on the structure of the lease or agreement. In a gross lease, all operating expenses, including property taxes, are included in the stated, or contract, rent, and the landlord (the public owner in the case of a possessory interest) pays these expenses from the stated, or contract, rent. In a net lease, most operating expenses, including property taxes, are excluded from the stated, or contract rent, and these expenses are paid by the tenant in addition to the stated, or contract, rent. Some lease structures are hybrids of these pure forms, with the landlord paying some types of expenses and the tenant paying others. Even with a net lease some expenses must be subtracted. The public owner must spend time managing the property and ensuring the area is maintained (much like an owner of a true triple-net lease in a retail center has management expense, insurance expense, and possibly some maintenance and repair.) An example of the public owner's management expense is the Request for Proposal that is required to contract with a carnival at a county fair.</u> <u>When using contract rents from comparable properties as an indicator of the market (economic) rent for the subject taxable possessory interest, a contract rent with the same lease structure as the subject taxable possessory interest with regard to the payment of operating expenses is preferred. In doing so, the appraiser avoids the necessity of adjusting the contract rent such that it reflects a lease structure, with regard to the payment of operating expenses, that is comparable to that of the subject taxable possessory interest.</u>	Accepted in concept. See proposed staff language at item #71.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
76.	32	18-35	Cal-Tax	**Revise as follows: Operating Income.** If operating income is used, the income to be capitalized is the net return from operating income to the public owner. The net return~~Net operating income~~ is gross operating income less allowed expenses, including a reasonable estimate of profit, of the pubic owner and the operating expenses of the possessor. Gross operating income, allowed expenses, and net operating income are defined consistent with "gross return," "gross outgo," and "net return," respectively, in subsection (c) of Rule 8. Allowed expenses of the public owner may include the following, as applicable: maintenance and repair, security services, general clean up and janitorial services, marketing and advertisement, management and administration, etc. Allowed expenses are any expenses necessary to continue the production of income from the property borne by the public owner. Typical operating expenses may include expenses for the rental of personal property, cost of goods sold, typical operating expenses, typical management expense, an allowance for a return on working capital, and an allowance for a return on and a return of the value of any nontaxable property that contributes to the gross operating income (such as a return on investment and the cost of inventory). ~~Allowed~~ Operating expenses do not include the following: amortization, depreciation, depletion charges, debt retirement, interest on funds invested in the taxable possessory interest, the contract rent for the taxable possessory interest, property taxes on the taxable possessory interest, income taxes, or state franchise taxes measured by income. ~~Typical operating expenses may include expenses for the rental of personal property, for the provision of security services, and for advertising and promotional services, provided such expenses are necessary for the production of the gross income from the subject taxable possessory interest. Typical operating and management expenses include expenses that an owner/operator typically would bear to maintain the property and to continue the production of income from the property but which, in the case of the subject taxable possessory interest, are borne by the public owner.~~ The use of operating income may be influenced by managerial skills and may arise in part from nontaxable property or other sources (rule 8 (e)). Other sources are the need for the business owner (possessor of a taxable possessory interest) to make a profit. In theory, the net operating income would equal the net market (economic) rent for a property. Therefore, some level of profit must be removed from the gross operating income in order for net operating income to equal the theoretical net market rent. No rational business owner would rent a property for the operating income not adjusted for some profit. If the operating income were not adjusted for profit, the business owner would be paying all the remaining income after expenses as rent to the property. If the income to be capitalized is a percentage of operating income, the income needs to be adjusted to a net return to the public owner ensuring the removal of income from intangible assets, if any, and a reasonable profit in addition to an adjustment for underpaid or unpaid management. As mentioned above, after adjusting the operating income for these operating expenses, the income must be adjusted for the allowable expenses the public owner pays.	See proposed staff language at item #71. Language regarding profit not accepted. More generally, the income to be capitalized is the income attributable to the taxable property, which has already been said. A percentage rent is rental income, therefore, no adjustment is necessary for intangible assets or rights. As with other rental income, there should be deduction for expenses paid by the public owner.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
77.	32	18	Ajalat, Polley & Ayoob	**Revise as follows: Operating Income**. If operating income is used, the income to be capitalized is some portion of the net operating income. The net operating income as computed below is the amount available for the payment of rent. A portion of the net income will be the profit necessary for the continuance of the enterprise. Reasonable estimates of that profit must be deducted from net operating income. The remaining net operating income is available for the payment of rent. From the deemed rent, the public owner's expenses necessary to continue the income stream must be deducted.	Not accepted. But see staff's proposed language at item #71.
78.	32	24	CAA	**Revise as follows:** …allowance for a return on ~~and a return of~~ the value of any nontaxable property that contributes to the gross operating income. **Comment:** A return **of** a non-wasting asset is inappropriate. There is no necessity for recapture in a capital charge for items that have no physical, economic, or functional depreciation. This is recounted in the CAA Position Paper 99-003 Addendum to AH502, page 165, which when addressing adjustments to arrive at income attributable to the taxable property, cites only a "return on" component.	Not accepted. An allowance for the return on and return of the value of nontaxable property that contributes to the gross operating income is appropriate in order to avoid capitalizing income attributable to the nontaxable property. Nontaxable property may have a finite life.
79.	33	8-10	CAA	**Delete the following:** ~~1. By comparing the anticipated net incomes from comparable taxable possessory interests with their sales prices stated in cash or its equivalent and adjusted as described in subsection (e)(1)(A)~~ **Comment:** The only manner in which this method is accurate would be if the land were transferred. This rarely occurs. Otherwise, the land component is missing from the indicated rate.	Not accepted. The method is valid and may be used in certain situations.
80.	33	35	Cal-Tax	**Add the following:** …price divided by the comparable property's expected annual net income). Extreme caution should be taken when using direct capitalization. Direct capitalization typically values property in fee because the income stream is expected to continue into perpetuity for land. This method is only appropriate if the direct capitalization rate is derived from comparable sales of possessory interests where the income stream is very similar and for essentially the same term of possession. In yield capitalization,…	Not accepted. The requirement for comparability is stated.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
81.	34	11-14	CAA	**Delete the following:** …rate. ~~The valuation of a taxable possessory interest always involves, in one form or another, depending on the particular approach, a discounting of multiple net incomes. Thus, taxable possessory interest valuation always involves yield, or annuity, capitalization and the use of a yield rate.~~ **Comment:** The statement would exclude other approaches to value, especially the indirect income approach. Therefore, taxable possessory interest valuation does not always involve yield, or annuity capitalization and the use of a yield rate.	Accepted. (Also, combine remaining text of paragraph with the following paragraph for continuity.)
82.	34	15-19	CAA	**Revise as follows:** ~~In order~~ One way to derive a yield rate from sales data (i.e., "the market-derived" way), requires the appraiser ~~requires~~ to know the buyer's expected annual net incomes (including the expected income that results from the reversionary value) over the buyer's expected holding period. This data is very difficult to obtain for sales of fee simple interests and ~~almost impossible to obtain~~ equally so for sales of taxable possessory interests. **Comment:** This methodology is not the only manner to derive a yield rate from sales data as the language of the passage would imply.	Not accepted. Draft language is accurate.
83.	34	20-21	CAA	**Revise as follows:** ~~This often leaves the band of investment technique as the only practical means by which the appraiser can arrive at a discount rate.~~ In the band of investment, the estimate of the debt return... **Comment:** The admitted inherent difficulties with deriving the equity rate of return does not make this the "often only practical means by which the appraiser can arrive at a discount rate." As in all appraisal endeavors, the quality, quantity, and reliability of data dictates the basis upon which the appraiser bases his/her opinions.	Accepted.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
84.	34	21-25	Cal-Tax	**Revise as follows:** …appraiser can arrive at a discount rate. In the band of investment, the estimate of the debt return component is relatively straightforward if loans are made on the property type (residential properties in state parks and hotels on tax exempt land); the appraiser may have access to lender data involving comparable taxable possessory interests, and he or she will almost certainly have access to market loan rates for comparable fee-owed property. However, if loans are not made on similar property types (leases of land for short terms or leases in privately owned sports arenas), then the equity rate is likely to equal the yield rate used in yield capitalization. It also is not difficult to estimate a typical loan-to-value ratio assuming loans are made on the property type. The difficult part in the band of investment technique is the estimate of the equity rate…	Not accepted. Staff language is accurate—appraiser will use most comparable data available. Do not understand "… then the equity rate is likely to equal the yield rate used in yield capitalization."
85.	34	26	CAA	**Revise as follows:** …of return, about which only limited data is available from fee-owned comparables and practically no data is available from taxable possessory interests. **Comment:** Typographical omission.	Accepted. Grammar/style.
86.	35	3-9	Cal-Tax	**Revise as follows:** 3. In yet another approach, an equity rate of return can be estimated by applying a simple equity-over-debt premium. The expected equity rate of return will always be higher than the related debt rate because the equity return is residual to the ~~equity~~ debt return and is more volatile (i.e., riskier) due to financial leverage. The difficulty here, of course, is estimating exactly what the equity-over-debt premium should be; nevertheless, an ~~small~~ equity-over-debt premium arguably is supportable on theory alone (i.e., the higher required rate of return on equity vis-a-vis the debt rate, given the equity position's greater risk). If debt rates don't exist for the subject property type, this method is not applicable. For example, the appraiser might be able to determine a debt rate for land sales, but a short-term lease of land is not a comparable property type.	Do not accept added sentence—the appraiser will use the most comparable data available. Accept corrections.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
87.	35	3-10	CAA	**Delete the following:** ~~3. In yet another approach, an equity rate of return can be estimated by applying a simple equity-over-debt premium. The expected equity rate of return will always be higher than the related debt rate because the equity return is residual to the equity return and is more volatile (i.e., riskier) due to financial leverage. The difficulty here, of course, is estimating exactly what the equity-over-debt premium should be; nevertheless, a "small" equity-over-debt premium arguably is supportable on theory alone (i.e., the higher required rate of return on equity vis-a-vis the debt rate, given the equity position's greater risk).~~ ~~4. Finally, the appraiser could consider the following relationship: 10~~ ~~$r_o = k_o - g$ or~~ ~~$k_o = r_o + g$,~~ **Comment:** This passage is too simplistic. Because many significant assumptions are inherently necessary in this approach, the passage demands extensive attention to the complexities not addressed.	Not accepted. Provides another alternatives for estimating a yield, or discount, rate.
88.	35	10	Cal-Tax	**Comment:** Shouldn't this example be the same as the Basic Yield Capitalization Formula in AH 502 (page 89)?	Formula is correct.
89.	36	18	CAA	**Revise as follows:** …value of the reversion. <u>The reversion reflects the value of the property after the lease term expires and possession of the property reverts to the tax exempt or immune governmental entity.</u> **Comment:** The addition completes the sequence of events and rationale.	Accepted in concept. See staff's proposed language below: <u>The reversion reflects the value of the property at the end of the term of possession, when the right to possession will revert back to the public entity.</u>

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
90.	37	2-8	Cal-Tax	**Revise as follows:** In the income approach-direct method, the appraiser estimates the value of the subject taxable possessory interest by discounting either the estimated net market rent or the estimated ~~expected~~ future net operating income attributable to the subject taxable possessory interest for the reasonably anticipated term of possession using a discount rate that reflects the risk associated with the receipt of the expected future net operating income. The direct income method is ~~probably~~ the most widely used method in the valuation of taxable possessory interests because of the quantity and quality of data available relating to market (economic) rents.	Accepted in concept. Will say "… estimated market rent (less allowed expenses paid by the public owner)"
91.	38	3 Ex. 3.3	CAA	**Revise as follows:** Present value factor: (PV$1PP (annual)/10 yrs./~~12~~ 13% = ~~5.65~~ 5.43) **Comment:** Present worth factor is incorrect based on the facts of the example. Resultant indicated value would thereby change as well.	Accepted.
92.	38	3 Ex. 3.3	Ajalat, Polley & Ayoob	**Comment:** Some expenses of the public owner should be added so that appraisers are not misled. We suggest that actual out of operational expenses be used such as maintaining fencing, in addition to some managerial expenses.	Accepted in concept. Staff will place a footnote within the example stating this idea.

<table>
<tr><th>No.</th><th colspan="2">Page/Line Reference</th><th>Source</th><th>Proposed Language</th><th>SBE Staff Position</th></tr>
<tr><td>93.</td><td>38</td><td>Ex. 3.3</td><td>Cal-Tax</td><td>
Delete draft example and replace with the following example:
Subject taxable possessory interest: Carnival Agreement at the county fair grounds.
PERTINENT INFORMATION:

Second year of a three year agreement with District Agricultural Association to provide the carnival at the county fair each year for one week.
Reasonably anticipated term of possession: 2 years
Market Rent: Flat rate payment of $68,000 plus 30 % of advanced ticket sales (rent is typical for county fairs of this size) Annual Estimate $78,500
Allowable Expenses (paid by public owner and are necessary for the continued production of income to the possessory interest: Advertising and Promotion $18,000; Maintenance, Administration, Trash removal, Utility fees $16,000; Security Operations $8,500; Attractions and Entertainment $16,000; Total $58,500
Capitalization (discount) rate, exclusive of property taxes: 15%
Added component for property taxes (general rate): 0%

In this approach, the appraiser capitalizes (discounts) the estimated market (economic) rent over the reasonably anticipated term of possession.
Although often the contract rent is a valid indicator of the market (economic) rent, the appraiser should not uncritically accept it as the market (economic) rent.
In this example, it was not necessary to add a property tax component to the discount rate because property taxes are not part of the income to be capitalized.
~~Estimated annual market rent: (200 AUM @ $10/AUM) $2,000~~
~~x~~
~~Present value factor: (PV$1PP (annual)/10 yrs/12% = 5.65) 5.65~~
~~Indicated Value $11,300~~
Forecast Potential Gross Income $78,500
Minus Allowable Expenses $58,500
Net Income $20,000
Present value factor: (PV$1PP (annual)/2 yrs/15% = 1.63) 1.63
Indicated Value $32,600
</td><td>Not accepted. This essentially recasts the entire example.</td></tr>
</table>

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
94.	39	11-16	Ajalat, Polley & Ayoob Cal-Tax	**Revise as follows:** 2. The appraiser subtracts the value of all other interests held be others, the value of all of the interests retained by the public owner, and the estimated present value of the nontaxable reversionary interest retained by the public owner from the as-if-fee value estimated in No. 1 above. The estimated present value of the reversion can be estimated using the methods described in the discussion of the comparative sales approach-indirect method. ~~As also stated earlier, the estimated present value of the reversion should be based on the same rights as those contained in the subject taxable possessory interest.~~ **Comment (APA):** The last sentence makes no sense to us. Paragraph 1 determined the fee value. Therefore, in addition to the reversion all other interests held by third parties and all other interests retained by the public owner must be valued and deducted. **Comment (Cal-Tax):** This last sentence didn't appear to make any sense. Paragraph 1 determined the value of the fee. Thus, in addition to the reversion, all other interests held by third parties and all other interests held by the public owner must be valued and deducted.	Not accepted. The "as-if-in-fee" value of the subject taxable possessory interest should reflect only the rights held by the possessor. This is how it is stated in Rule 21 and the draft manual. Therefore, the reversionary value that is subtracted should also reflect the value of those same rights.
95.	39	12	CAA	**Revise as follows:** …retained by the public owner from the as-if-in-fee value estimated in the discussion of the comparative sales approach-indirect method. **Comment:** Typographical omission.	Accepted.
96.	40	2 Ex. 3.4	CAA	**Comment:** Delete the entire example. The example shows land and improvement reversion having appreciated at the same rate. Improvements are wasting assets. Land is not. The example should show separate calculations for land and building reversion. The example also does not demonstrate how the fee value was derived, which is the major component of the approach. Additionally, the example assumes a level income premise, and yet fails to include the inflation rate into the discount rate.	Not accepted. 1) separate estimates for land and improvements are not required; 2) estimating the fee value is not the main point in this context; 3) the inflation rate is part of the assumed discount rate.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
97.	40	2 Ex. 3.4	Cal-Tax	**Revise as follows:** PERTINENT INFORMATION: • Estimated value of taxable possessory interest as if owned in fee simple: $1,125,000. • ~~Typically, t~~ The appraiser would estimate this value using direct or yield capitalization~~, that is, by capitalizing the subject property's expected net operating income for the upcoming year using an overall capitalization rate derived from comparable sales.~~ • The appraisal unit comprises land and improvements; ~~this is always the case in the indirect methods (assuming of course, that the property is improved).~~ • Reasonably anticipated …	Accepted in concept; would read as follows: PERTINENT INFORMATION: • Estimated value of taxable possessory interest as if owned in fee simple: $1,125,000. • The appraiser would estimate this value using direct or yield capitalization. • The appraisal unit consists of land and improvements (assuming an improved property). • Reasonably anticipated …
98.	41	16-21	Ajalat, Polley & Ayoob Cal-Tax	**Revise as follows:** 4. Finally, the appraiser subtracts the value of the interests held by others, the value of all of the interests retained by the public owner including the estimated present value of the nontaxable reversionary improvements, if any, from the amount in No. 3 above. As in No. 1 above, the estimated reversionary value of the improvements typically is estimated as the replacement cost new less depreciation of the improvements at the end of the reasonably anticipated term of possession. Again, as of the valuation date, such improvements will be nontaxable because their ownership will have reverted back to the public owner.[47]	Accepted in concept. See staff's proposed language at item #99.
99.	41	21	Ajalat, Polley & Ayoob	**Add the following:** The difficulty with the cost approach is that it includes all interests and makes no adjustment for any of the restrictions imposed in the lease agreement. When using the cost approach, in some leases there may be 100 or more restrictions that have to be separately valued and deducted. In a properly applied income approach many of these restrictions are automatically taken into account.	Accepted in concept. See staff's proposed language below, which would replace page 41, lines 2 through 35, and page 42, lines 1 through 4 (most of this rewrite simply removes redundancy, but see, in particular, last two paragraphs).

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
			Staff	In the cost approach, as applied to taxable possessory interests, the estimated value of the subject taxable possessory interest in land is added to the estimated value of the subject improvements, and this sum is reduced by the estimated present value, if any, of the subject improvements upon reversion to the public owner. The cost approach is often used when improvements are constructed by the possessor. The cost approach thus involves the following steps: 1. Estimate the value of the subject improvements based on their estimated cost new less the depreciation. Typically, depreciation is estimated using a standard depreciation schedule. 2. Estimate the value of the taxable possessory interest in land. This value may be estimated using one or more of the previously discussed methods—that is, the comparative sales approach (direct or indirect method) or the income approach (direct or indirect method). 3. Add the estimated value of the subject improvements to the estimated value of the taxable possessory interest in land. As in the "conventional" cost approach, land and improvements are valued separately and summed. 4. Finally, subtract the estimated present value, if any, of the nontaxable reversionary improvements from the amount in No. 3 above. If the estimated remaining economic life of the subject improvements exceeds the reasonably anticipated term of possession, there will be a reversionary improvement value. As in No. 1 above, typically, the reversionary value of the improvements is estimated based on their estimated cost new less depreciation at the end of the reasonably anticipated term of possession. The estimated value of the improvements must be consistent with the permitted use under the taxable possessory interest. If the permitted use does not correspond to the use for which the subject improvements were originally designed and constructed, the cost new less depreciation of the subject improvements may not be a reliable indicator of the value of the taxable possessory interest in the improvements. If the possessor's use of the property is limited to specified time periods or is shared with other possessors, the final value indicator from the cost approach must be allocated to the subject taxable possessory interest in a manner that reflects the proportionate value of the subject taxable possessory interest.	

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
100.	41	21	Cal-Tax	**Add the following:** The difficulty with the cost approach is that it includes all interests and makes no adjustment for all of the restrictions imposed in the lease agreement. When using the cost approach, in some leases there may be 100 or more restrictions that have to be separately valued and deducted. In a properly applied income approach many of these restrictions are automatically taken into account.	Accepted in concept. See proposed staff language at item #99.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
101.	42	Ex. 3.5	Cal-Tax	**Revise as follows:** PERTINENT INFORMATION: • The possessor groundleases 1.50 acres of land (65,340 square feet) from the airport authority and constructs a 45,000 square foot aircraft maintenance building. The market ground rent is $0.10 per square foot per month, or $78,408 per year. The market rent is constant over the reasonably anticipated term of possession. • Allowable Expenses: Management and administration – 5%, and road and access repairs - $1,000 annually. • The reasonably anticipated term of possession is 30 years, based on the stated term of possession (the remaining term of the ground lease on the valuation date). There are no factors that indicate that the reasonably anticipated term of possession is other than 30 years. • The capitalization (discount) rate is 12%. The capitalization rate could be developed by any of the described methods. In the example, it is not necessary to add a property tax component to the discount rate because the possessor will pay the possessory interest taxes in addition to the ground rent. A. Computation of possessory interest value in land: The appraiser estimates the value of the taxable possessory interest in land using the income approach direct method, that is, by discounting the estimated market rent over the reasonably anticipated term of possession ($78,408 - $3920 - $1000 = $73,488 x 8.055 [PV$1PP, 30 yrs/12%] = $~~631,576~~591,946, rounded to $~~631,500~~591,500). The appraiser could estimate the value of the taxable possessory interest in land using this method or any of three other methods—the comparative sales approach-direct method, the comparative sales approach-indirect method, or the income approach-indirect method—with the selected method(s) determined by the quantity and quality of the data. The estimated market value of the taxable possessory interest in land is $~~631,500~~591,500. B. Computation of possessory interest value in improvements: Typically, the appraiser will estimate the value of the improvement using the possessor's reported costs, an independent cost estimate based on cost service data, or both. The objective is an estimate of the replacement cost new less depreciation of the improvements that includes all components of full economic cost. Next, the appraiser must decide whether to attribute a reversionary value to the improvements. In the example, we assumed that the improvements will be valueless at the end of the reasonably anticipated term of possession; thus, it is not necessary to adjust the improvement value for a reversionary value. On subsequent valuation dates, the appraiser also would estimate the value of the improvements based on replacement cost new less depreciation, probably by adopting a standard depreciation schedule, for example, straight-line depreciation. The estimated market value of the taxable possessory interest in improvements is $1,000,000. Estimated market value of the taxable possessory interest in land $~~631,576~~591,946 say $~~631,500~~591,500 Estimated market value of the taxable possessory interest in improvements $1,000,000 Estimated market value of the entire subject taxable possessory interest $~~1,631,500~~1,591,500	Not accepted, but will place footnote at bottom of example stating the idea.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
102.	44	2	CAA	**Revise as follows:** ~~Subtract Present value of possessor's contractually entitled benefits, if any.~~ **Comment:** As in the objection on page 26, the nature of "contractually entitled benefits" without definition leaves an ambiguity over how this item should be considered.	Not accepted. See staff comment at item #61.
103.	44	2	Cal-Tax	**Add the following:** Equity sale price (subject or comparable) Adjust for (+ or -) Cash equivalence Adjust for (+ or -) Market conditions Adjust for (+ or -) Comparability Add Present value of contract rents for reasonably anticipated term of possession. Subtract Allowable Expenses when computing present worth of contract payments. Add Present value of possessor's contractually obligated future costs, if any. Subtract Present value of possessor's contractually entitled benefits, if any. Equals Indicated value of subject taxable possessory interest	Accepted in concept. Would read: "Add the present value of the contract rent (less any allowed expenses paid from the contract rent by the public owner) for the reasonably anticipated term of possession."
104.	44	6	Cal-Tax	**Revise as follows:** Estimate Expected net market (economic) rent (rent adjusted for allowable expenses) of the rights of possession under the subject taxable possessory interest over the reasonably anticipated term of possession. Calculate Present value of the future expected market rents. Equals Indicated value of subject taxable possessory interest.	Accepted in concept. See staff comment at item #90.
105.	45	14	CAA	**Revise as follows:** As with post-*De Luz* taxable possessory interests, there are five methods… **Comment:** Typographical omission.	Accepted.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
106.	47	7	Cal-Tax	**Revise as follows:** Read together, Rules 4, 6, and 8 provide ~~an~~ the general order of preference for the applicability of the valuation approaches. When reliable comparative sales data are available, the preferred valuation approach is the comparative sales approach. When market sales data are not available, but an income for the subject property can be reliably estimated, the income approach is next preferred. Finally, when neither reliable sales nor income data are available, the cost approach is preferred.[Footnote] [Footnote] This order of preference is intended as a generalization. The sales approach is favored by statute whereas the choice among income and cost approaches is not absolute and dependent on factors and circumstances beyond the scope of this discussion. See Rules 4, 6, and 8 for more detail.	Not accepted. The draft language accurately summarizes the language of Rules 4, 6, and 8 relating to the application of the approaches.
107.	47	10	CAA	**Revise as follows:** …income for the subject property can be reliably estimated, the income approach is the next preferred approach. **Comment:** Suggestion establishes an otherwise uncertain order of preference.	Accepted.
108.	47	12	Cal-Tax	**Revise as follows:** The same general order of preference applies to the valuation approaches for taxable possessory interests.	Not accepted. See staff comment at item #106.
109.	47	12	CAA	**Revise as follows:** The same order of preference applies to the valuation approaches for taxable possessory interests, with some exceptions (e.g. Section 107.7 cable television and Section 107.9 airport landing rights).	Not accepted. The cited statutes specify conditions under which the assessor's presumption of correctness is retained. The statutes do not address the application of the approaches to value.
110.	47	19	CAA	**Revise as follows:** …data may be available (e.g., resort cabins, long term residential leases on Indian land, and boat slips).	Not accepted. The added example adds little.
111.	47	20-21	Cal-Tax	**Revise as follows:** 2. Because quality rental data is often readily available, the income approach-direct method is ~~probably~~ the most widely used valuation method for taxable possessory interests. This is …	Accepted. (It's an assertion, but probably a correct one.)

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
112.	49	17-19	Cal-Tax	**Revise as follows:** As with other real property and as provided in section 110.1, a taxable possessory interest in existence on March 1, 1975, received a base year ~~based on~~ value equal to its fair market value as of that date, with that value indexed by the inflation factor to the 1978 lien date. A taxable possessory…	Accepted.
113.	49	17	CAA	**Revise as follows:** As with other real property and as provided in section 110.1, a taxable possessory interest in existence on… **Comment:** Typographical omission.	Accepted. See item 111.
114.	49	18	CAA	**Revise as follows:** …March 1, 1975, received a base year value ~~based~~ on its fair market value as of that date, with that value indexed by the inflation factor to the 1978 lien date. **Comment:** Avoids repetition.	Accepted in concept. But see staff comment at item #112.
115.	50	4-7	Ajalat, Polley & Ayoob	**Comment:** We are not sure what these lines intended. Some clarification would be helpful.	Replace draft language at page 50, lines 1 through 14, with the following: Among the factors that may cause a decline in value of a taxable possessory interest is a reduction in the reasonably anticipated term of possession used to value the interest. As discussed in Chapter 3, if the reasonably anticipated term of possession is based on the stated term of possession, the term of possession will decline on each lien date. Other market factors, however, may counteract the effect of a declining term of possession such that the market value of the taxable possessory interest does not decline.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
116.	50	11	CAA	**Revise as follows:** …(i.e., the remaining term under the lease or agreement, or the reasonably anticipated term of possession) as of the lien date.	See staff comment at item #115.
117.	50	14	Cal-Tax	**Add the following: "Terminating" taxable possessory interests.** A special case exists when the evidence establishes that at a certain future date the public owner of the real property will no longer make the real property available for private possession. This situation is sometimes called a "terminating taxable possessory interest." If the evidence establishes the existence of a terminating taxable possessory interest, the term of possession on each valuation date should be the anticipated remaining period that the real property will be available for private possession or the stated term, whichever is shorter.	Not accepted. This concept is presented in the draft at page 24, lines 5 through 10. It is appropriately and adequately addressed there.
118.	50	14	CAA	**Revise as follows:** …purposes. Under market conditions, where rents are increasing, a declining term may not be sufficient to cause a value decline. It should also be noted that under section 51(e), the assessor is not required to make an annual reappraisal of all assessable property. Only assessments that have been lowered require an annual appraisal comparison. **Comment:** The proposal puts into more complete context the appraisal problem associated with decline in value analyses.	Accepted in part. See staff comment at item 115.
119.	51	23	Cal-Tax	**Revise as follows:** • The termination of a sublease of a taxable possessory interest with an original term (including renewal options) that exceeds half the length of the remaining term of the master taxable possessory interest (including renewal options) when the sublease was entered into. (Section 61, subdivision (d)(1).)	Accepted.
120.	53	2	Cal-Tax	**Revise as follows (1st Column, 4th Row):** The termination of a sublease of a taxable possessory interest with an original contract term (including any renewal options) that exceeds half the length of the remaining contract term (including any renewal options) of the master taxable possessory interest when the sublease was entered into. [Section 61, subdivision (d)(1).]	Accepted.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
121.	54	2	CAA	**Revise as follows:** Most of the above provisions pertain to the ~~change-in-ownership~~ change in ownership implications of a sublease of a … **Comment:** Hyphens in phrase "change in ownership" are not common usage.	Accepted.
122.	55	1	CAA	**Comment:** The example would be more instructional if values could be calculated for the remaining master lease assignment and the sublease value.	Not accepted. The example addresses the change in ownership of taxable possessory interests, not their valuation.
123.	55- 56	6-14 1-4	CAA	**Revise as follows:** ~~1. Do any leasehold interests that exist on the acquisition date become taxable possessory interests on that date?~~ ~~2. If so, is there a change in ownership of such interests on the acquisition date?~~ ~~The answer to the first question is that, assuming they satisfy the legal criteria for constituting a taxable possessory interest, the leasehold interests become separately assessable taxable possessory interests on the date of acquisition by the public entity. The answer to the second question, however, is that the acquisition does not constitute a change in ownership of the leasehold interests for the purposes of section 61(b). The tenant's leasehold interests have not changed ownership. Such interests should be valued as if they had been taxable possessory interests when the leases commenced. In other words, they should receive a base year value, in retrospect, as of the date the leases commenced. If the interests are subsequently renewed, extended, or assigned, of course, a change in ownership under section 61(b) occurs, and they should be reassessed and new base year values established.51~~ **Comment:** The proposal does not appear to rely or cite any statutory authority. It can just as easily be argued that the governmental acquisition creates a new possessory interest assessment, as well as a new appraisal event. The section is also not instructive as to tenant owned or built improvements, which should be not subject to any reappraisal, and enjoy their prior Article XIIIA assessed values.	Not accepted. Section 61(b) defines "change in ownership" as "[t]he creation, renewal, sublease, or assignment of the taxable possessory interest in tax exempt real property." When a public entity acquires privately owned real property subject to a lease, there has been a change in ownership of the leased fee. There has not been, however, a change in ownership of the taxable possessory interest pursuant to section 61(b). Thus, the proposed discussion is accurate and supported by section 61.
124.	57	32-36	Cal-Tax	**Comment:** We are somewhat confused by this discussion and not entirely convinced it is accurate. The explanation appears to argue the two pieces to a single pie create two whole pies.	The discussion is based on longstanding Board opinion as stated in LTA 86/12.

NO.	PAGE/LINE REFERENCE		SOURCE	PROPOSED LANGUAGE	SBE STAFF POSITION
125.	58	14	CAA	**Add the following:** Possessory interest assessments are unsecured assessments. As such, they are not subject to proration upon termination. Prior to Proposition 13 and supplemental assessments, this was not a significant issue since values were assessed from lien date to lien date. The untaxed time gained by the assessee on the front end of the possessory interest tended to offset the time lost upon termination. With the introduction of supplemental assessments on the front end taking affect as of the actual start date of the possessory interest, the front end cushion was removed but no relief was given for terminations, which were still based on the lien date. With no provision for proration upon possessory interest termination, the lessee is still responsible for the entire following fiscal year's taxes if the possessory interest existed on the lien date. **Comment:** Addresses a common and frequent problem raised by possessory interest assessees.	Not accepted. The issue is adequately addressed in staff's language.
126.	58	14	Staff	Staff is drafting language that addresses the assessment of short-term, recurring taxable possessory interests vis-à-vis the supplemental and regular rolls. Staff will provide language at the interested parties meeting, or earlier.	In progress.
127.	59	1 Ex. 4.2	CAA	**Revise as follows (3rd and 4th lines of 3rd paragraph):** …of $100,000 would have been subtracted from the new base year value of $120,000. **Comment:** Typographical omission.	Accepted.
128.	59	4	CAA	**Revise as follows:** Under the provisions of section 155.20, a county board of supervisors may exempt from taxation, by local ordinance or resolution … **Comment:** Correction provides the complete provisions of Section 155.20.	Accepted.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
129.	62	21	CAA	**Revise as follows:** …exception, that is, the entity only has to indicate any changes to the prior year's report. <u>Some counties are taking advantage of the internet and making their possessory interest databases interactive. Each governmental agency can thereby locate their account and make changes on-line for immediate access by the assessor.</u> **Comment:** This addition provides a more current picture of how reporting is accomplished.	Accepted in concept. Add the following sentence to the draft text: <u>Some assessors have implemented this or a similar approach through the electronic exchange of information with public agencies</u>.
130.	63	2	CAA	**Revise as follows:** … must be entered on the secured roll. <u>However, the tax thereon is unpaid when any installment of taxes on the secured roll becomes delinquent, the tax collector may use the procedures which are applicable to the collection of taxes on the unsecured roll.</u> **Comment:** This suggested addition presents a more complete picture of assessment and collection procedures that may ensue.	Not accepted. Proposed language refers to tax collection, not assessment or enrollment.
131.	63-65	All	CAA	**Revise as follows:** Delete all references to "unit of real property", "unit of taxable government-owned real property", "government owned real property", "taxable replacement improvements", "taxable improvements", "taxable government owned real property", appraisal unit of taxable government owned property. **Comment:** Section 11 assessments and its dictates relate only to land. Improvements continue to enjoy Article XIIIA protections. The entire section continually references "unit of real property" and improvements erroneously.	Not accepted. References to terms used in Property Tax Rule 29 are necessary for explaining the regulation.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
132.	66	Ex. 5.1	CAA	**Revise as follows:** Delete example. Replace with Attachment 2. **Comment:** Practical examples, utilizing actual "real world" calculations would be far more helpful for an instructional manual. There are many complexities regarding Section 11/Rule 29 assessments. The worst problem seems to call for the taxable improvements to be included in the calculation of the possessory interest limitation amount. The improvements are not assessed under Article XIII, but are under Article XIIIA. Improvements should have no bearing on the possessory interest limitation amount, yet Rule 29 calls for the property (land and improvements) to be included in the calculation.	Not accepted. The proposed examples are inconsistent with Property Tax Rule 29. Section 11 provides an exemption for extraterritorial improvements that replace improvements that were taxable when acquired. The proposed examples do not recognize that section 11(f) provides that a taxable possessory interest exists in these replacement improvements.
133.	69	36	CAA	**Revise as follows:** …employees retirement system <u>outside its political boundaries,</u> is not removed from the roll; rather, it is taxable under the provisions of article XIII, section 11. **Comment:** The requirement, as stated, falls short of that which qualifies for the purview of Section 11.	Accepted in concept. Proposed staff language as follows: <u>…employees retirement system that is outside the system's boundaries is not removed from the roll; rather, it is taxable under the provisions of article XIII, section 11.</u>
134.	75	12	CAA	**Revise as follows:** …includes, but is not limited to intangible assets or rights, the assessment also loses it<u>s</u> presumption of correctness. **Comment:** Grammatical correction.	Accepted. Grammar/style.
135.	76	30	CAA	**Revise as follows:** …defined in the statute with their initial values established using ~~on~~ data from 1996 assessments… **Comment:** Grammatical correction.	Accepted. Grammar/style.
136.	80	16	CAA	**Revise as follows:** ~~In this regard,~~ <u>The deduction for rent was</u> subsequently reversed in *De Luz Homes, Inc. v. San Diego County.* **Comment:** More specific attribution necessary to avoid confusion regarding what was overturned.	Accepted.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
137.	81	9-11	Cal-Tax	**Revise as follows:** *County of Los Angeles v. County of Los Angeles AAB No. 1* (1993) 13 Cal.App.4th 102. ~~A nonexclusive right to use public property that is merely in common with, and coequal to, the general public's does not constitute a taxable possessory interest.~~ The possession or use which grounds possessory interests means and requires not just some benefit from the public property, but physical possession or use of it. Thus, the county assessment appeals board was correct in limiting taxable possessory interest assessments of several car rental firms at county airports to their counters and reserved parking lots rather than on their "use" of the airports as a whole. A nonexclusive right to use public property that is merely in common with, and coequal to, the general public's does not constitute a taxable possessory interest. Further rights granted by the airports, to do business at the airports and their environs, were not possessory interests but were intangibles not subject to property tax. **Comment:** This case was discussed twice (once here once on Page 83). Simply combined the discussions.	Accepted in concept. Staff will cite the case once and include both annotations. But replace first annotation (strikeout at left) with the following rewrite: Taxable possessory interests in public property are grounded on physical possession or use of it; not just some benefit from public property.
138.	81	32-34	CAA	**Revise as follows:** ...use is limited by the other party's right to use the property at the same time. ~~And p~~Possible interference with use affects value, but not the existence of a possessory right. ~~Possible interference with use affects value, but not existence of a possessory right.~~ **Comment:** Sentence structure correction and deletion of repeated sentence.	Accepted.
139.	83	3-10	Cal-Tax	**Delete the following:** ~~*Los Angeles County v. Los Angeles County Assessment Appeals Board No. 1* (1993) 13 Cal.App.4th 102. The possession or use which grounds possessory interests means and requires not just some benefit from the public property, but physical possession or use of it. Thus, the county assessment appeals board was correct in limiting taxable possessory interest assessments of several car rental firms at county airports to their counters and reserved parking lots rather than on their "use" of the airports as a whole. Further rights granted by the airports, to do business at the airports and their environs, were not possessory interests but were intangibles not subject to property tax.~~	See staff comment item #136.

No.	Page/Line Reference		Source	Proposed Language	SBE Staff Position
140.	85	29	CAA	**Revise as follows:** *Seegmiller v. Nevada County* 53 Cal.App.4th 1397 provides authority for not canceling or prorating possessory interest taxes for termination of lease after the lien date.	Not accepted. *Seegmiller v. Nevada County* addresses personal property and business fixtures rather than possessory interests.
141.	91		Cal-Tax	**Revise as follows: Highest and best use** ~~The most profitable use of a property at the time of the appraisal; that available use and program of future utilization that produces the highest present land value; must be legal, physically possible, financially feasible, and maximally profitable; see text for the distinction between highest and best use as though vacant and highest and best use as improved~~That use, among the possible alternative uses, that is physically practical, legally permissible, market supportable, and most economically feasible.	Not accepted. The definition was recently authorized by the Board in Assessors' Handbook section 501, *Basic Appraisal* and is also contained in AH 502, *Advanced Appraisal*

Attachments to AH 510 Matrix
September 20, 2002

Attachment A – CAA proposed language for item 19

Attachment B – CAA proposed language for item 131

Attachment A (CAA-proposed language re matrix item #19)

REVIEW OF PROPERTY INTERESTS

In general, the taxable value of a possessory interest is "the sum of the value of all property rights in land and improvements held by the possessor. This value is not diminished by any obligation to pay rent or to retire debt secured by the possessory interest. In other terms, the taxable value of a possessory interest is the full cash value of the fee simple estate reduced by the value of any rights, except security interests, held by the public owner (other than the right to receive rent) or granted by the public owner to other persons." Table 1 shows the relationships of the various rights involved in a taxable possessory interest.

Table 1

PW of Rent Advantage	PW of Contract Rent	PW of Reversion
LEASEHOLD	LEASED FEE	
FEE SIMPLE (FREEHOLD)		
POSSESSORY INTEREST		Reversion
PW OF ECONOMIC RENT		PW OF REVERSION

In Table 1 each row represents the full cash value for a typical real property owned by a public owner. It is comprised of the leasehold and the leased fee. The possessory interest is shown to encompass the entire leasehold plus a portion of the leased fee. The value of the possessory interest is the present worth of the economic rent for the rights allowed by the lease during the reasonable anticipated term of possession. The PW of the reversion is thus excluded from the value of the possessory interest.

The reversion is excluded since the public owner of the property is exempt. By leasing the property to a private party the public owner has relinquished its present interests in the real property for the right to receive rents. This present interest is taxable and assessable to the private party. However when the property reverts back to the public owner, at the end of the reasonably anticipated term, the property is again exempted or immune from taxation. The value of this exemption is called the PW of Reversion and must not be assessed.

The "value of the leased fee interest" is the sum of the present value of the contract rents over the remaining term of possession under the lease and the present value of the reversionary interest at lease termination. Restated, it is the present value of the right to possess and control the property when the lease terminates. The value of the leased fee interest generally is not relevant to possessory interest valuation.

As mentioned above, taxable possessory interests are usually valued for property tax purposes by determining the present worth of the economic rent for the rights allowed by the lease during the reasonable anticipated term of possession. For every holder of real property involving a particular estate, each owner has separate and distinct rights associated with their estate interest. These relationships are represented in Table 2 below.

Table 2

ESTATE **(INTEREST)**	**FEE SIMPLE** **FREEHOLD**	**LEASED FEE**	**LEASEHOLD**	**POSSESSORY INTEREST**
HOLDER	Fee Title Owner	Landlord/ Lessor	Tenant/lessee	Tenant/lessee
RIGHTS	Absolute ownership unencumbered by any other interest	1. To receive contract rent. 2. The reversion	Economic productivity of the property subject to the leased terms	Full rights allowed by lease
VALUE	Full Cash Value 1. leased fee plus leasehold 2. Possessory interest plus PW of reversion	PW of contract rent + PW of reversion	PW of (economic rent - contract rent) rental advantage	PW of economic rent during reasonably anticipated term of possession

These relationships form the conceptual basis for the various taxable possessory interest valuation approaches that will be mentioned later in this chapter. To simplify further discussion of taxable possessory interests we will refer to them as "full value of the leasehold interest."

Although a taxable possessory interest created by a lease—that is, a leasehold interest—is a common form of taxable possessory interest, a taxable possessory interest can be created in many ways that do not require the execution of a lease, or, for that matter, any written agreement. The concepts and terms used above in the context of a lease can be generalized to refer to other types of property relations that also constitute taxable possessory interests.

The basis for valuing taxable possessory interests is the full cash value standard as mentioned by the California Supreme Court in *De Luz Homes, Inc. v. County of San Diego* and described earlier in this chapter. The Court, to fit non-fee situations, adapted this full cash value standard. This linked the full cash value standard to all aspects of taxable possessory interest valuations. The standard requires that taxable possessory interests be valued by estimating what the property rights conferred under the lease would command in an open market by not the present lessee, but a typical prospective one. This requires the assessor to determine not only the economic rent for the allowed uses, but also the reasonably anticipated term. These are valuation issues that the assessor must prove through market evidence to support his opinion of value.

Rule 29 CALCULATIONS

Scenario 1 (PI is less than PI limitation amount)

Land						
67 value		**2000 Philips factor**	**2000 Section 11 Land**		**Comments**
$	285	29.1006	$	8,294	Not enrolled
Sect 11 BV		**CPI**	**Trended BY Value**		
$	5,000	1.59525	$	7,976	Enrolled
Current Market			$	220,000	Not enrolled
PI BY Land Value					
$	46,000	1.32162	$	60,795	Partially or fully enrolled(see taxable PI land)

PI Limitation Amount		
$	220,000	Cur Fair Mkt Value
$	(8,294)	Sect 11 LV
$	211,706	PI Limitation Amt

Taxable PI Land			Comments
$	211,706	PI Limitation Amt	The total trended base year value of the land for the PI is enrolled since it is below PI Limitation Amount
$	60,795	PI trended land value	
$	**60,795**	PI land value enrolled	

Improvement				
Not taxable when acquired (tenant owned)				
$	300,000	1.32162	**$**	**396,486**
Total taxable PI value			**$**	**457,281**

Rule 29 SAMPLE CALCULATIONS
Scenario 2 Land Only (PI Land exceeds PI limitation amount)

Land						
67 value		**2000 Philips factor**	**2000 Section 11 Land**		**Comments**
$	285	29.1006	$	8,294	Not enrolled
Sect 11 Base Value		**CPI**	**Trended BY Value**		
$	5,000	1.59525	$	7,976	Enrolled
Current Fair Market Value			$	350,000	Not enrolled
PI BY Land Value					
$	300,000	1.02	$	306,000	Partially or fully enrolled (see taxable PI Land)

PI Limitation Amount		
Current Fair Mkt Val	$	350,000
Sect 11 LV	$	(8,294)
PI Limitation Amt	$	341,706

Taxable PI Land			
$	341,706	PI Limitation Amt	The total trended base year value of the land for the PI is not enrolled, but is reduced to equal the PI Limitation amount.
$	306,000	PI trended Land Value	
$	**306,000**	PI Land Value Enrolled	

Improvement				
Not taxable when acquired (tenant owned)				
$	162,000	1.02	**$**	**165,240**
Total taxable PI value			**$**	**471,240**

Rule 29 SAMPLE CALCULATIONS
Scenario 3 Taxable Land and Improvements Involved in Calculating PI Limitation Amount

Land					
67 value		**2000 Philips factor**	**2000 Section 11 Land**		**Comments**
$	285	29.1006	$	8,294	Not enrolled
Sect 11 Base Value		**CPI**	**Trended BY Value**		
$	2,000	1.59525	$	3,191	Enrolled
Current Fair Market Value			$	350,000	Not enrolled
Improvement					
1975 BY Imp Value					
$	50,000	1.59525	$	79,763	Enrolled
2000 Fair market value			$	200,000	Not enrolled
Maximum assessable value			$	79,763	
Totals (entire unit)					
Fair Market Value			$	550,000	
Factored Base Year Value			$	82,954	
Article XIII, Section 11(land only)			$	8,294	
Total Article XIII value (entire unit)			$	88,057	
Assessed 2000 roll value			$	82,954	
PI BY Land Value					
$	300,000	1.02	$	306,000	Partially or fully enrolled (see taxable PI Land)
PI BY Imp					
$	162,000	1.02	$	165,240	
Total PI			$	471,240	
PI Limitation Amount					
Current Fair Mkt Val		$ 550,000			
Sect 11 LV		$ 88,057			
PI Limitation Amt		$ 461,943			
Taxable PI Land					The total trended base year value
$	461,943	PI Limitation Amt			for the PI is not enrolled
$	471,240	PI valuation			
$	**(9,297)**	amount to deduct from PI			