STATE OF CALIFORNIA

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Executive Director

February 25, 1999

No. 99/17

TO COUNTY ASSESSORS AND INTERESTED PARTIES:

PROPERTY TAX RULE 10

The Board's Property Taxes Department and Legal Division are proposing to update Property Tax Rule 10, Trade Level for Tangible Personal Property, for purposes of conforming the rule to current law. An initial draft of Rule 10 with proposed revisions, tentatively scheduled to be heard by the Property Tax Committee in August 1999, is enclosed for your review. The proposed draft deletes reference to business inventory eligible for exemption under section 219, and reflects the requirements of the Revenue and Taxation Code.

Attachment A is a "clean" version of staff's proposed Rule 10, while Attachment B shows the proposed additions and deletions in strike-out and underline format. Interested parties are encouraged to submit proposed revisions in the form of alternative text for review and possible inclusion in this draft. Proposed revisions should reference the page and line number of enclosed Attachment A, and must be received by staff no later than April 12, 1999.

Thereafter, staff will develop a matrix summarizing issues raised and revise the proposed rule as appropriate based on comments received. The matrix and a second draft of the rule will be distributed to interested parties by June 7, 1999. An interested parties meeting, tentatively scheduled for June 22, 1999, will be held at Board headquarters to discuss the issues raised and summarized in the matrix.

If you have any questions regarding the revision of this rule, please contact Gordon Ferguson at (916) 322-6815 or Ladeena Ford/Mara Determan at (916) 324-5839.

Sincerely,

/s/ Richard C. Johnson

Richard C. Johnson
Deputy Director
Property Taxes Department

RCJ:md/lf
Enclosures

**ATTACHMENT A**
**STAFF DRAFT OF RULE 10**

# 1ST DRAFT

**Rule 10 TRADE LEVEL FOR TANGIBLE PERSONAL PROPERTY**

*References:* Chapter 147, Statutes of 1966, First Extraordinary Session.

Sections 110, 401, Revenue and Taxation Code.

(a) In appraising tangible personal property, the assessor shall give recognition to the trade level at which the property is situated and to the principle that property normally increases in value as it progresses through production and distribution channels. Such property normally attains its maximum value as it reaches the consumer level. Accordingly, tangible personal property shall be valued by procedures that are consistent with the general policies set forth herein. Trade level recognition shall also be given to fixtures assessed similar to personal property.

(b) Except as provided by the following subdivisions, tangible personal property held by a consumer at a given trade level shall be valued at the amount of cash or its equivalent for which the property would transfer to a consumer of like property at the same trade level. This value shall be estimated in accordance with regulations 4, 6, and 8. If the cost approach is employed, the cost (the replacement or reproduction cost new prior to allowance for depreciation) shall include the full economic cost of placing the property in service. Full economic cost may include, but is not limited to, the typical retail selling price of the property, freight, sales or use tax, and installation, less typical trade, quantity, and/or cash discounts.

(c) Tangible personal property leased, rented, or loaned for a period of less than six months, having a tax situs at the place where the lessor normally keeps the property as provided in regulation 204, shall be valued at the amount of cash or its equivalent for which it would transfer to other lessors or retailers of like property at the same trade level. The value shall be estimated by reference to (1) the lessor's cost to replace the property including freight, less trade, quantity, and cash discounts and a reasonable allowance for depreciation; (2) the cost indicated in subdivision (e) if the lessor is also the manufacturer; or (3) the price at which the lessor could be expected to sell the property.

(d) Tangible personal property leased, rented, or loaned for an extended but unspecified period or leased for a term of more than six months, having tax situs at the lessee's situs as provided in regulation 204, shall be valued by estimating the lessee's cost to replace the property including sales tax, freight, installation charges, less trade, quantity, and cash discounts and a reasonable allowance for depreciation.

# 1ST DRAFT

(e) Tangible personal property acquired from internal sources, for self consumption or use, shall be valued by estimating (1) the cost of the property, in its condition and location on the lien date, had it been acquired in an arm's-length transaction from an outside supplier (including labor, materials, overhead, interest on borrowed or owner supplied funds, and other costs incurred in bringing the property to a finished state), and/or (2) by reference to the cash price or its equivalent for which the property could be sold in an arm's-length transaction to an outside customer, and in accordance with subdivision (b).

(f) Tangible personal property in the hands of a person engaged in two or more trade level functions (i.e., that of a manufacturer, wholesaler, retailer, lessor, or consumer) shall be valued by estimating (1) the cost of the property, in its condition and location on the lien date, had it been acquired in an arms-length transaction from an outside supplier (including labor, materials, overhead, interest on borrowed or owner supplied funds, and other costs incurred in bringing the property to a finished state), and/or (2) the cash price or its equivalent for which the property could be sold in an arm's-length transaction to an outside customer and in accordance with subdivision (b).

*History:* Adopted June 21, 1967, effective July 23, 1967.
Amended February 18, 1970, effective March 26, 1970.
Amended January 6, 1971, effective February 18, 1971.
Amended April 19, 1971, effective May 22, 1971.

**ATTACHMENT B**
**PROPOSED REVISIONS TO CURRENT RULE 10**

# 1st DRAFT

**Rule 10 TRADE LEVEL FOR TANGIBLE PERSONAL PROPERTY**

*References:* Chapter 147, Statutes of 1966, First Extraordinary Session.

Sections 110, 401, Revenue and Taxation Code.

(a) In appraising tangible personal property, the assessor shall give recognition to the trade level at which the property is situated and to the principle that property normally increases in value as it progresses through production and distribution channels. Such property normally attains its maximum value as it reaches the consumer level. Accordingly, tangible personal property shall be valued by procedures that are consistent with the general policies set forth herein. Trade level recognition shall also be given to fixtures assessed similar to personal property.

~~(b) Tangible personal property in the hands of a primary producer which is produce of the soil and for which there are regular markets established by the buyers of the property, such as petroleum and other minerals, logs, livestock, and other farm products, shall be valued at the price offered by the buyers less the unincurred cost of preparing the property for market and of moving the property to the market place at which such price is applicable, or plus the cost of moving the goods from that market place to the place at which they are to be processed if the latter location is the tax situs.~~

(b) Except as provided by the following subdivisions, tangible personal property held by a consumer at a given trade level shall be valued at the amount of cash or its equivalent for which the property would transfer to a consumer of like property at the same trade level. This value shall be estimated in accordance with regulations 4, 6, and 8. If the cost approach is employed, the cost (the replacement or reproduction cost new prior to allowance for depreciation) shall include the full economic cost of placing the property in service. Full economic cost may include, but is not limited to, the typical retail selling price of the property, freight, sales or use tax, and installation, less typical trade, quantity, and/or cash discounts.

~~(c) Tangible personal property in the hands of a manufacturer who holds it for processing or for sale shall be valued at the amount for which it would transfer to other manufacturers of like property. This value shall be estimated (1) by reference to the cost of the property in its condition on the lien date or (2) by reference to the cash price at which the manufacturer is expected to sell the property less costs yet to be incurred and experienced gross profits. When the cost approach is used, there shall be added to the cost of raw materials all other direct costs and manufacturing burden, including depreciation and property taxes, but excluding selling and general administrative costs.~~

# 1st DRAFT

~~Unprocessed raw material cost is the cost of replacement on the lien date as evidenced by recent purchases by the assessee or other recent market transactions.~~

(c) Tangible personal property leased, rented, or loaned for a period of less than six months, having a tax situs at the place where the lessor normally keeps the property as provided in regulation 204, shall be valued at the amount of cash or its equivalent for which it would transfer to other lessors or retailers of like property at the same trade level. The value shall be estimated by reference to (1) the lessor's cost to replace the property including freight, less trade, quantity, and cash discounts and a reasonable allowance for depreciation; (2) the cost indicated in subdivision (e) if the lessor is also the manufacturer; or (3) the price at which the lessor could be expected to sell the property.

(d) Tangible personal property in the hands of a retail merchant who holds it for sale, lease, or rental shall be valued at the amount for which it would transfer to other retailers of like property; and tangible personal property in the hands of a wholesale merchant who holds it for sale, lease, or rental shall be valued at the amount for which it would transfer to other wholesalers of like property. This value shall be estimated (1) by reference to the property's cost to the merchant, including freight-in and deducting trade, quantity, and cash discounts, with reasonable allowance based on proper substantiation for damaged, shopworn, out-of-style, used, or overage stock, or (2) by reference to the price at which the merchant is expected to sell the property less his experienced gross profit.

(d) Tangible personal property leased, rented, or loaned for an extended but unspecified period or leased for a term of more than six months, having tax situs at the lessee's situs, as provided in regulation 204, shall be valued by estimating the lessee's cost to replace the property, including sales tax, freight, installation charges, less trade, quantity, and cash discounts and a reasonable allowance for depreciation.

~~(e) Tangible personal property in the hands of a person who holds it for consumption shall be valued in accordance with sections 4, 6, and 8 of this subchapter. When, however, such property is leased or rented for a period of less than six months so that its tax situs, as provided in section 204 of this chapter is at the place where the lessor normally keeps the property, it shall be valued in accordance with the last sentence of subdivision (d).~~

(e) Tangible personal property acquired from internal sources, for self consumption or use, shall be valued by estimating (1) the cost of the property, in its condition and location on the lien date, had it been acquired in an arm's-length transaction from an outside supplier (including labor, materials, overhead, interest on borrowed or owner supplied funds, and other costs incurred in bringing the property to a finished state), and/or (2) by reference to the cash price or its equivalent for which the property could be sold in an arm's-length transaction to an outside customer, and in accordance with subdivision (b).

**ATTACHMENT B**
**PROPOSED REVISIONS TO CURRENT RULE 10**

# 1st DRAFT

(f) ~~When t~~Tangible personal property is in the hands of a person engaged in two or more trade level ~~of the~~ functions (i.e., that of ~~producer~~ a manufacturer ~~or processor~~, wholesaler, retailer, lessor, or consumer) shall be valued by estimating (1) the cost of the property, in its condition and location on the lien date, had it been acquired in an arms-length transaction from an outside supplier (including labor, materials, overhead, interest on borrowed or owner supplied funds, and other costs incurred in bringing the property to a finished state), and/or (2) the cash price or its equivalent for which the property could be sold in an arm's-length transaction to an outside customer and in accordance with subdivision (b). ~~the level of trade at which the property is held shall be determined by reference to its form, location, quantity, acquisition source, and probably purchasers or lessees. A person is operating at two or more levels when the property consists of raw materials, semi-manufacture, or finished goods which were acquired from sources within a business entity (other than component parts meeting the tests of the following sentence) and the property is held (1) for consumption by the business entity or (2) for processing and/or marketing in competition with similar products marketed by other business entities that have purchased like raw materials, semi-manufacturers, or finished goods at the same stage of production from external sources. Component parts held at the manufacturing processing level, however, shall not be considered to be at a higher level than that at which they are manufactured when they have been manufactured by a business entity specifically and exclusively for (1) incorporation by the entity in its finished product, (2) marketing as replacement parts for its finished product, or (3) both.~~

~~When it is concluded that the person holding tangible personal property is operating at more than one trade level, property. at the higher trade level or levels acquired from internal sources shall be valued (1) by estimating what the property, in its condition and location on the lien date, would have cost had it been acquired in an arm's length transaction from an outside supplier, (2) by reference to the cash price at which the property could be sold in an arm's length transaction to an outside customer less a reasonable gross profit, or (3) if held at the consumer level, in accordance with subdivision (e).~~

~~(g) Storage of tangible personal property in a warehouse, in and of itself, does not alter the trade level. The trade level of such property will be determined in accordance with subdivision (f).~~

*History:* Adopted June 21, 1967, effective July 23, 1967.
Amended February 18, 1970, effective March 26, 1970.
Amended January 6, 1971, effective February 18, 1971.
Amended April 19, 1971, effective May 22, 1971.