

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 SUMMARY DECISION UNDER REVENUE AND TAXATION CODE SECTION 40

3 In the Matter of the Petition for)
4 Reassessment of the 2019 Unitary Value for:)
5)
6 FRONTIER CALIFORNIA, INC. (0201))
7 Petitioner)
8)
9)

Appeal No.: SAU 19-009

Case ID No.: 1063284

Nonappearance Hearing Date:
December 17, 2019¹

10 Representing the Parties:

11 For the Petitioner: Peter Michaels, Attorney at Law

12 For the Respondent: Sonya Yim, Tax Counsel III
13 Attorney for the State-Assessed Properties Division

14 Mike Harris, Acting Chief
15 State-Assessed Properties Division

16 Appeals Attorney: Julia Himovitz, Tax Counsel III

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18 **VALUES AT ISSUE**

	Value	Penalty	Total
20 2019 Board-Adopted Unitary Value	\$2,270,200,000	\$0	\$2,270,200,000
21 Petitioner's Requested Unitary Value	\$2,049,600,000	\$0	\$2,049,600,000
22 Respondent's Appeal Recommendation	\$2,256,000,000	\$0	\$2,256,000,000
23 Respondent's Revised Appeal Recommendation	\$2,232,900,000	\$0	\$2,232,900,000

24 **Factual Background**

25 Frontier California, Inc. (Petitioner), formerly Verizon California, Inc., is a wholly owned
26 subsidiary of Frontier Communications Corporation and the second largest incumbent local exchange
27

28 ¹ The Board voted unanimously to grant the petition for reassessment, in part, and reduce affirm the 2019 Board-adopted unitary value of \$2,232,900,000.

1 carrier in the State of California. Petitioner is regulated by the California Public Utilities Commission
2 (CPUC), and like other state-assessed incumbent local telephone companies, is designated as a
3 telephone service provider of last resort (POLR).

4 After Petitioner's purchase of Verizon wireline assets in California, Florida, and Texas in 2016, a
5 purchase price allocation (PPA) was performed for the property acquired in the transaction². A PPA is
6 the process whereby a company, when purchasing another company, allocates the purchase price to
7 various assets and liabilities accounts. It is typically conducted for financial and tax reporting
8 requirements when mergers and acquisitions occur. A PPA for property plant and equipment (PP&E)
9 attempts to determine the assets' fair market value at the time of the transaction. In this case, pursuant to
10 the PPA the fair market value for Petitioner's PP&E specific to California was \$3.4 billion as of April 1,
11 2016.

12 For the 2019 unitary valuation appraisal, Petitioner provided Respondent with a lien date 2019
13 Fair Market Value Appraisal prepared by Duff & Phelps (D&P study) on March 21, 2019. The study
14 develops the Replacement Cost New (RCN) value indicator for the taxable property, then subtracts
15 depreciation and extraordinary obsolescence, and adds the value of real property to determine the total
16 value of Petitioner's unitary property.

17 Respondent utilized the same appraisal methodology for Petitioner's 2019 unitary valuation as
18 was used for the 2018 unitary valuation. Respondent relied on the 2016 PPA as the starting point,
19 adjusted for purchases and asset retirements since the 2016 PPA date, applied appropriate trend and
20 percent good factors to all the taxable costs according to their acquisition years, estimated remaining
21 economic lives for various asset categories, and then adjusted for functional and economic
22 obsolescence, to arrive at the Replacement Cost New Less Depreciation (ReplCLD) value indicator.
23 The 2019 Board-adopted unitary value was based on 100 percent reliance on the ReplCLD value
24 indicator.
25
26
27
28

² In accordance with Financial Accounting Standards Board Accounting Standards Codification 805 (ASC 805).

1 **Legal Issue 1: Whether Petitioner has shown that Respondent’s appraised value for buildings in**
2 **the 2019 unitary valuation was inappropriate.**

3 **Findings of Fact and Related Contentions**

4 Petitioner asserts that its replacement square footage is “significantly smaller than existing
5 square footage. Telephone central office buildings, which were generally constructed decades ago, are
6 exponentially larger than necessary for equipment currently housed inside...An inutility adjustment for
7 buildings should be made, in the amount of \$94.0 million.” (Petition, p. 1.)

8 To further support this contention, Petitioner asserts that they have “identified office building
9 superadequacy that takes into consideration property type, the effective age of the property, current
10 costs, and location. Frontier’s inutility adjustment calculation excludes land and assets under
11 construction; recognizes necessary additional site improvement costs, as well as central office square
12 footage for administrative functions; does not include additional depreciation or obsolescence; and, does
13 not make any superadequacy adjustments for non-central office buildings.” (Petitioner’s Response, p. 3-
14 4)

15 Petitioner states that “At the outset, it must be observed that, as a matter of law, Petitioner’s legal
16 burden of proof is to demonstrate that the Board’s 2019 cost indicator is, in part, methodologically
17 erroneous. If Frontier establishes that the Board’s cost model is partially invalid, Petitioner has met its
18 burden of proof. The Company’s threshold legal burden does not extend to proving the actual value of
19 erroneously assessed central office buildings. (*DFS Group, L.P. v. County of San Mateo* (2019) 31
20 Cal.App.5th 1059, 1074-1074.)

21 “Historically, the Board has recognized excess square footage in central office buildings now
22 owned by Frontier. Those central office buildings were formerly owned by Verizon California
23 (“Verizon”).” (Petitioner’s Response, p. 1-2)

24 Respondent asserts that its valuation for Petitioner’s buildings was based on the 2016 PPA.
25 Subsequent to filing its initial brief on October 4 (SAPD Analysis), Respondent received additional
26 information from Petitioner with regard to the appropriateness of the trend factors as specifically
27 applied to its buildings. Based on a review of the building category, Respondent determined that the
28 trend factor for buildings specific to the PPA year should be adjusted. Respondent therefore applied the

1 adjusted trend factor for the buildings to the appropriate Replacement Cost New (RCN) value indicator,
2 to derive a revised ReplCLD value indicator, resulting in a net reduction to Petitioner's unitary value of
3 \$23.1 million. Respondent contends no further adjustments are warranted.

4 Applicable Law and Appraisal Principles

5 Burden of Proof

6 Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.)
7 The Board has promulgated the Rules for Tax Appeals (RTA) to govern the administrative and
8 appellate review processes for all of the tax and fee programs administered by the Board. (Cal. Code
9 Regs., tit. 18, § 5000.) Of relevance here, RTA 5541, subdivision (a), places the burden of proof upon
10 the taxpayer as to all issues of fact except as otherwise specifically provided by law. Courts have long
11 presumed that the Board assesses all property correctly, placing on the taxpayer the burden of proving
12 that an assessment is incorrect. (*Trailer Train Co. v. State Bd. of Equalization* (1986) 180 Cal.App.3d
13 565, 584.) Therefore, petitioner bears the burden of showing that the assessment is illegal.
14 (*ITT World Communications v. Santa Clara County* (1980) 101 Cal.App.3d 246.)

15 ReplCLD Value Indicator

16 Property Tax Rule 6, subdivision (a) provides, in part: "The reproduction or replacement cost
17 approach to value . . . is preferred when neither reliable sales data . . . nor reliable income data are
18 available . . ." In general, the ReplCLD valuation methodology is estimated by applying trend factors -
19 price level changes, including the application of "current prices to the labor and material components of
20 a substitute property capable of yielding the same services and amenities, with appropriate additions as
21 specified . . ." (Property Tax Rule 6, subd. (d).) Then, the resulting adjusted cost amount is "reduced
22 by the amount that such cost is estimated to exceed the current value of the reproducible property by
23 reason of physical deterioration, misplacement, over- or under-improvement, and other forms of
24 depreciation or obsolescence. The percentage that the remainder represents of the reproduction or
25 replacement cost is the property's percent good." (Property Tax Rule 6, subd. (e); State Board of
26 Equalization, *Unitary Valuation Methods* (March 2003), pp. 23-24.)

Analysis and Disposition

Respondent is presumed to have correctly determined the value of the property at issue, and Petitioner bears the burden of proving otherwise. Here, Petitioner asserts that the square footage it would require to replace its buildings is significantly less than its existing square footage and that a \$94.0 million inutility adjustment should be made. Respondent states that obsolescence for superadequacy would be reflected in the PPA and in Petitioner's unitary value. However, based on additional information provided by Petitioner, Respondent determined that the trend factor for buildings specific to the PPA year should be adjusted and therefore applied the adjusted trend factor for the buildings to the appropriate RCN value indicator, to derive a revised ReplCLD value indicator. For this reason, we note Respondent recommended an additional adjustment of \$23.1 million. Despite Respondent's adjustment, Petitioner still asserts that it is erroneous and believes that a further adjustment should be made. However, Petitioner has not presented additional evidence or arguments to show error or illegality in this adjustment. Accordingly, Petitioner has not presented any evidence or argument to show error in Respondent's adjustment and the reduction is presumed correct. Further, the Appeals Attorney concludes that Petitioner has failed to meet its burden of proving that Respondent incorrectly over-assessed Petitioner when it calculated the 2019 Board-adopted value.

Legal Issue 2: Whether Petitioner has shown that Respondent should reclassify the labor costs for station connections to the electronic account rather the fiber account.

Findings of Fact and Related Contentions

Petitioner claims "that the life of the Optical Network Terminal ("ONT") electronics should be consistent with the life of labor costs (station connect) underlying installation of customer premise equipment ("CPE"). On that basis, Frontier contends that a fiber account reclassification adjustment must be made for labor costs incurred to install CPE." (Petition, p. 2.) Petitioner claims that the company had historically "capitalized costs to install CPE assets into outside plant subaccounts 2423.4 (buried cable) and 2421.4 (aerial cable). As of the 2019 lien date, those capitalized CPE costs were reclassified, to subaccounts 2423.2 and 2421.2, because CPE is shorter lived than fiber, and should not be depreciated on a fiber schedule." (Petitioner, p. 2.) Petitioner contends that a fiber account reclassification adjustment

1 assets. Petitioner has not presented any evidence or argument to show Respondent made an error. For
2 these reasons the Appeals Attorney recommends that no adjustment be made for this issue.

3
4 **Legal Issue 3: Whether Petitioner has shown that Respondent’s excess capital adjustment for the**
5 **rural footprint reflected in the 2019 unitary value was inappropriate.**

6 **Findings of Fact and Related Contentions**

7 Petitioner has two primary contentions as it relates to this issue: conduit and pole removal.

8 Petitioner states that its network “serves many rural areas that are uneconomical... [and] believes
9 that an additional capital cost adjustment for those areas is necessary, specifically for conduit. Frontier
10 estimates the value adjustment associated with proper removal of excess capital costs related to conduit
11 in the Company’s rural footprint is approximately \$73.4 million.” (Petition, p. 2.)

12 Petitioner stated that the Board made an excess capital adjustment for joint-owned poles in the rural
13 footprint, using a pole removal-to-value ratio that is inconsistent with data in Board staff’s appraisal
14 workpapers. (Petitioner, p. 2.) On that basis, Petitioner also believes that an additional downward value
15 adjustment should be made in the amount of \$14.2 million.

16 Respondent states that Petitioner provided the D&P study performed for lien date 2019, which
17 included a \$189 million value adjustment for excess capital to account for the difference in ReplCLD
18 value indicator between building an all fiber network rather than a fixed wireless network for a very
19 rural part of Petitioner’s service area.

20 Respondent states that it agreed with Petitioner that a downward value adjustment was warranted
21 for excess capital since Petitioner was planning to push out fixed wireless services in the same rural
22 area. However, Respondent further asserts that it found deficiencies in Petitioner’s excess capital
23 calculation and thus, made several modifications to address the deficiencies. After Respondent’s
24 modifications, the 2019 ReplCLD value indicator reflects a \$69.2 million downward value adjustment
25 for excess capital.

26 Respondent also contends that Petitioner has not provided any information to show how
27 Respondent’s value adjustment in the original appraisal was inappropriate or insufficient. Furthermore,
28

1 Respondent argues that Petitioner failed to provide documentation to support the \$73.4 million
2 adjustment Petitioner made in excess of the adjustment made by Respondent, thus failing to provide any
3 support or evidence showing how Petitioner’s value adjustment for this issue was appropriate and the
4 value adjustment Respondent had already allowed was inappropriate. Respondent states that Petitioner’s
5 17.5 percent adjustment factor for conduit was derived from general market data and was not specific to
6 Petitioner. Thus, Respondent recommended no adjustment specifically for the conduit portion.
7 Respondent has reviewed the information provided by Petitioner for the excess capital adjustment for
8 joint-owned poles in the rural footprint. Respondent agrees that an additional downward adjustment of
9 \$14.2 should be allowed for this issue.

10 Applicable Law and Appraisal Principles

11 Burden of Proof

12 Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.)
13 Therefore, Petitioner has the burden of showing that the assessment is incorrect or illegal. (*ITT World*
14 *Communications v. Santa Clara* (1980) 101 Cal.App.3d 246; see also Cal. Code Regs., tit. 18, § 5541,
15 subd. (a).)

17 ReplCLD Value Indicator

18 Property Tax Rule 6, subdivision (a), provides, in part: “The reproduction or replacement cost
19 approach to value . . . is preferred when neither reliable sales data . . . nor reliable income data are
20 available . . .” In general, the ReplCLD valuation methodology is estimated by applying trend
21 factors—price level changes, including the application of “current prices to the labor and material
22 components of a substitute property capable of yielding the same services and amenities, with
23 appropriate additions as specified . . .” (Property Tax Rule 6, subd. (d).) Then, the resulting adjusted
24 cost amount is “reduced by the amount that such cost is estimated to exceed the current value of the
25 reproducible property by reason of physical deterioration, misplacement, over- or underimprovement,
26 and other forms of depreciation or obsolescence. The percentage that the remainder represents of the
27 reproduction or replacement cost is the property’s percent good.” (Property Tax Rule 6, subd. (e).)

28

1 **Analysis and Disposition**

2 Respondent is presumed to have correctly determined the value of the property at issue, and
3 Petitioner bears the burden of proving otherwise. Here, Petitioner states that its network serves many
4 rural areas that are uneconomical, believes a capital cost adjustment is appropriate, and that its
5 requested adjustment is conservative. Respondent agrees with Petitioner that a downward adjustment
6 for excess capital is appropriate and has thus made a \$14.2 million downward adjustment. However,
7 Petitioner has not provided additional documentation to support its claim for an additional adjustment
8 of \$73.4 million for excess capital. Therefore, the Appeals Attorney finds that Petitioner has not met its
9 burden of proving that Respondent's excess capital adjustment for the rural footprint reflected in the
10 2019 unitary value was inappropriate and does not recommend any further adjustments for this issue.
11

12 **Legal Issue 4: Whether Petitioner has shown that Respondent's economic obsolescence**
13 **adjustment reflected in the 2019 unitary valuation was inappropriate.**

14 **Findings of Fact and Related Contentions**

15 Petitioner asserts that "Historically, the Board has measured economic obsolescence by using
16 forward-looking calculations based on projected customer counts. Petitioner maintains that the Board's
17 method for estimating future obsolescence is flawed in several critical respects, including calculation of
18 net present value. Frontier contends that an additional adjustment for economic obsolescence should be
19 made in the amount of \$19.0 million, as demonstrated in Exhibit 4." (Petition, p. 3, Ex. 4.)

20 Petitioner claims that Respondent's economic obsolescence calculation was incorrect because
21 Respondent included actual counts of past customer losses in addition to anticipating future losses,
22 rather than relying only on a projected, anticipated loss of customers in future calendar years.
23 Respondent asserts that it relied on the 2016 PPA as a starting point for the ReplCLD value indicator,
24 and that the PPA represents the fair market value of the property at the time of the transaction.
25 Respondent further asserts that including the actual number of customer losses since the PPA date in its
26 economic obsolescence calculation provides more accurate information as to Petitioner's actual
27 operations and value in relation to the actual purchase at fair market value. Respondent states that its
28 calculations resulted in a \$484 million adjustment for economic obsolescence in Petitioner's 2019

1 ReplCLD value indicator. Finally, Respondent asserts that Petitioner has not provided information to
2 explain how Respondent’s inclusion of actual customer losses in the economic obsolescence calculation
3 was inappropriate, nor has Petitioner provided documentation to support its claim for \$19 million in
4 additional adjustments for economic obsolescence. Additionally, Respondent contends that Petitioner’s
5 calculation does not account for the adjustment to Tier 1 of the economic obsolescence worksheet,
6 which Respondent had already calculated an appropriate adjustment for economic obsolescence. For
7 these reasons, Respondent recommends that no adjustment be made for this issue.

8 Applicable Law and Appraisal Principles

9 Burden of Proof

10 Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.)
11 Therefore, the petitioner has the burden of showing that the assessment is incorrect or illegal. (*ITT*
12 *World Communications v. Santa Clara* (1980) 101 Cal.App.3d 246; see also Cal. Code Regs., tit. 18,
13 § 5080 subd. (a).)

14 ReplCLD Value Indicator

15 Property Tax Rule 6, subdivision (a), provides, in part: “The reproduction or replacement cost
16 approach to value . . . is preferred when neither reliable sales data . . . nor reliable income data are
17 available . . .” In general, the ReplCLD valuation methodology is estimated by applying trend
18 factors—price level changes, including the application of “current prices to the labor and material
19 components of a substitute property capable of yielding the same services and amenities, with
20 appropriate additions as specified . . .” (Property Tax Rule 6, subd. (d).) Then, the resulting adjusted
21 cost amount is “reduced by the amount that such cost is estimated to exceed the current value of the
22 reproducible property by reason of physical deterioration, misplacement, over- or underimprovement,
23 and other forms of depreciation or obsolescence. The percentage that the remainder represents of the
24 reproduction or replacement cost is the property’s percent good.” (Property Tax Rule 6, subd. (e).)

25 Analysis and Disposition

26 Respondent is presumed to have correctly determined the value of the property at issue, and
27 Petitioner bears the burden of proving otherwise. Here, while Petitioner asserts that Respondent should
28 not have included actual customer counts in its calculations for economic obsolescence, Petitioner has

1 not provided information to explain how Respondent’s inclusion of actual customer losses in the
2 economic obsolescence calculation was inappropriate, nor has Petitioner provided documentation to
3 support its claim for \$19 million in additional adjustments for economic obsolescence. Therefore, the
4 Appeals Attorney finds that Petitioner has not met its burden of proving that Respondent’s adjustment
5 for economic obsolescence in the 2019 unitary valuation was inappropriate and recommends that no
6 further adjustment be made for this issue.

7
8 **Decision**

9 Accordingly, the petition for reassessment is granted in part, reducing the 2019 Board-adopted
10 unitary value from \$2,270,200,000 to \$2,232,900,000.*

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12 Antonio Vasquez, Chairman

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14 Malia Cohen, Member

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16 Ted Gaines, Member

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18 Betty Yee, Controller

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21 * The decision was rendered in Sacramento, California on December 17, 2019. This summary decision
22 document was approved on January 28, 2020, in Sacramento, California.

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