

1 Anthony S. Epolite
 2 Tax Counsel IV
 3 Board of Equalization, Legal Department
 4 450 N Street, MIC:85
 5 PO Box 942879
 6 Sacramento, CA 95814
 7 Tel: (916) 323-3134
 8 Fax: (916) 324-2618

9 Attorney for Appeals Division

10 **STATE OF CALIFORNIA**
 11 **BOARD OF EQUALIZATION**

12 In the Matter of the Petition for) **APPEALS DIVISION'S**
 13 Reassessment of the 2011 Unitary Value for:) **HEARING SUMMARY FOR**
 14) **ORAL HEARING ON**
 15) **PROPERTY TAX PETITION**
 16)
 17) **Gill Ranch Storage, LLC (121)**)
 18)
 19)
 20)
 21)
 22)
 23)
 24)
 25)
 26)
 27)
 28)
) Appeal No.: SAU 11-031¹
) Case ID No.: 577341

29 Representing the Parties:

30 For the Petitioner: Joe Molina, Ryan & Co.
 31 Mark LoRusso, Ryan & Co.
 32 For the Respondent: Matthew Burke, Tax Counsel
 33 Attorney for State-Assessed Properties Division
 34 Ken Thompson, Chief
 35 State-Assessed Properties Division
 36 Counsel for Appeals Division: Anthony S. Epolite, Tax Counsel IV

37 **PROPOSED VALUES**

	Value	Penalty	Total
2011 Board-Adopted Unitary Value	\$222,400,000	\$0	\$222,400,000
Petitioner's Requested Unitary Value	\$123,000,000	\$0	\$123,000,000
Respondent's Appeal Recommendation	\$222,400,000	\$0	\$222,400,000
Respondent's Revised Recommendation	\$200,400,000	\$0	\$200,400,000

38 ¹ This matter was originally scheduled for oral hearing at the Board's November 15-16, 2011 meeting. However, the matter was postponed and rescheduled to the December 14-15, 2011 meeting due to a scheduling conflict of petitioner's representative.

1 addition, petitioner asserts that \$50 million of the facility's property costs (Issue 1) reflected
2 superadequacy (\$20 million attributable to compressor costs; \$25 million attributable to the transmission
3 line; and \$5 million attributable to other costs).³ Petitioner states that, because of shale oil discoveries,
4 there is currently no expansion of the facility planned.

5 Petitioner contends that the facility was conceived when natural gas prices were robust.
6 However, natural gas prices have changed dramatically and the spread between winter and summer
7 prices spreads have collapsed, eliminating the demand for storage. Petitioner argues that the cost
8 approach needs to be adjusted for obsolescence because the economic viability of the project is no
9 longer there or that an income approach should have been utilized to value petitioner's property (Issue
10 2). Petitioner asserts an income approach indicates a value of \$62.6 million for the property. In
11 addition, petitioner contends that a 50/50 weighting of the cost approach (the ReproCLD value
12 indicator) and the income approach (Capitalized Earning Ability (CEA) value indicator) should be
13 utilized to value the facility.

14 State-Assessed Properties Division (SAPD) staff discussed the CH2M HILL Study and notes the
15 following, pursuant to the study: (1) petitioner's budget for the project was too low; (2) petitioner did
16 not actually have cost overruns; and (3) a cost of \$284,000,000 was within the budgeted range for the
17 project. Based upon these findings, respondent contends that the Board-adopted value of the facility
18 was within the range of value.

19 ///

20 ///

21 ///

22 ///

23 ///

24 ///

25
26
27 ³ In its discussion of cost overruns, petitioner referred to a study prepared by CH2M HILL (Gill Ranch Storage, Post Project
28 Controls Assessment, dated April 2011) (hereafter, the CH2M HILL Study). It appears that petitioner provided State-
Assessed Properties Division (SAPD) staff with a copy of the study after filing the petition. However, neither SAPD's
counsel nor the Appeals Division received a copy of the study. As such, subsequent to the conference, the Appeals Division
requested, and petitioner submitted, a copy of the CH2M HILL Study so that the study could be incorporated as part of
petitioner's submission.

1 **Appeals Division's Recommendation**⁴

2 The Appeals Division recommends that the Board deny the petition for reassessment because
3 petitioner has not presented evidence to establish its claimed adjustments to the ReproCLD value
4 indicator or to establish that the property, which was placed into service in October 2010, suffers from
5 extraordinary economic obsolescence.

6 **Issue 1**

7 **Whether respondent should exclude claimed construction cost overruns and approximately**
8 **\$50 million of costs in certain infrastructure in calculating petitioner's ReproCLD value indicator.**

9 In its opening brief, petitioner asserted cost overruns of \$19.2 million. However, at the appeals
10 conference, petitioner asserted that the cost overruns relating to the construction of the facility totaled
11 \$31.2 million.

12 **Petitioner's Contentions**

13 Petitioner describes the facility as follows. The facility utilizes depleted reservoirs in a natural
14 gas production field. The facility includes three depleted natural gas reservoirs, twelve wells (including
15 gas injection and withdrawal wells), observation and monitoring wells, a salt water disposal well, a
16 compressor station, dehydration and control equipment, a 115 kilovolt gathering line, an electric
17 substation, a 30-inch diameter natural gas pipeline that extends to the PG&E transmission system, and
18 other related facilities. (Petition, p. 2.)

19 Petitioner also describes the facility as being designed for 20 billion cubic feet of storage
20 capacity and that petitioner's share of the facility is 15 billion cubic feet of that capacity, a capacity
21 which it expects to achieve by the end of 2013. Petitioner asserts, subject to market demand, funding,
22 and plant modifications, that the facility could be expanded for another 20 billion cubic feet of storage
23 capacity. (Petition, p. 2.)

24 Petitioner states that its total cost of construction of the facility was \$205.1 million, excluding the
25

26 ⁴ Unless the Board otherwise holds, the Board shall take official notice of: the property statement filed with the Board,
27 together with any attachments, including without limitation any reports to regulatory agencies such as the U.S. Securities and
28 Exchange Commission and the California Public Utilities Commission, and any annual reports to shareholders; the Appraisal
Data Report (ADR) prepared by the State-Assessed Properties Division (SAPD) together with any workpapers; the Notice of
Unitary Value; and any correspondence between SAPD and petitioner.

1 year-end construction work in progress, materials and supplies, inventory, and land. Petitioner contends
2 that it experienced cost overruns in the construction of the facility and that the facility's budgeted costs
3 were \$185,891,507, or \$19.2 million more than budgeted, due to unfavorable weather conditions and
4 permitting delays. Petitioner asserts that its excess costs of construction is a form of functional
5 obsolescence and that this excess cost should not be included in determining the Replacement Cost New
6 (RCN) before applying all forms of obsolescence in determining the cost value indicator.⁵ (Petition, p.
7 4.)

8 Petitioner also asserts that the initial construction of the facility included \$50 million in costs of
9 additional infrastructure to accommodate a potential expansion of the facility. Petitioner states that, as
10 of January 1, 2011, the facility was fully subscribed. However, petitioner asserts that the potential
11 expansion will not be undertaken due to the decline in the marketplace for stored gas. Petitioner
12 estimates that the \$50 million of additional infrastructure will not be utilized in the foreseeable future.
13 (Petition, pp. 4-5.)

14 **Respondent's Contentions**

15 In response to petitioner's assertions, respondent cites Assessors' Handbook section 501, *Basic*
16 *Appraisal* (January 2002) (AH 501), which provides for the costs that should be included in determining
17 the full economic cost of a property:

18 Costs for appraisal purposes may be thought of as full economic costs. Full economic
19 costs are defined as the payments that must be made to secure the supply of all the
20 necessary agents of production. Costs necessary to construct a property and make it
21 ready for its intended use may be classified as either direct or indirect costs. Direct costs
22 are expenditures for the labor and materials required to construct the property. They
23 include expenditures for permits, materials and labor and contractor's overhead and
24 profit. Indirect costs are expenditures not included in the direct construction of the
25 property. They include expenditures for the developer's administrative expenses,
26 professional fees, construction financing, construction insurance, property taxes during
27 construction, and marketing, sales, and lease-up costs incurred to achieve initial
28 occupancy or sale.

* * *

24 The general principle is that the costs of all functions necessary to place the property in
25 the hands of the consumer are part of the total cost of production. "Necessary" should be
26 emphasized. If a house is painted several times because the owner cannot decide on a
27 color scheme, this would create an unnecessary cost, and only the cost of one painting
28 should be included in the cost estimate. Other costs that do not represent normal costs

⁵ As mentioned above, the property was valued using the Reproduction Cost Less Depreciation (ReproCLD) value indicator.

1 should also be excluded. Abnormal costs include those generated by strikes, lockouts,
2 floods, excessive overtime pay, unforeseen hardships, etc.

3 (AH 501, pp. 75-76.) (Respondent's Opening Brief, pp. 2-3.)

4 As for petitioner's alleged cost overruns (i.e., abnormal costs due to unfavorable weather
5 conditions and delays in permitting), respondent asserts that petitioner has failed to provide any
6 evidence to support its conclusion that its original budgeted costs would have been sufficient to
7 complete the construction of the facility absent such conditions and delays or that the cost overruns were
8 solely attributable to the weather and delays. Respondent argues that not every amount expended over
9 petitioner's budget should be considered an abnormal cost merely because it was a cost overrun and that
10 petitioner's original budget may not have accurately reflected petitioner's actual costs. Furthermore,
11 respondent contends that many cost overruns are normal and are to be expected. Respondent contends
12 that petitioner needs to support its claim by providing comparable cost studies which demonstrate that
13 the budgeted cost of the facility was normal and not under-budgeted. (Respondent's Opening Brief,
14 p. 3.)

15 As for petitioner's \$50 million in costs associated with additional infrastructure, respondent
16 argues that petitioner has failed to provide any extrinsic documentation to support its assertion or to
17 identify the infrastructure at issue. Moreover, respondent contends that the public statements of
18 petitioner's parent company, Northwest Natural Gas Company (Northwest), do not substantiate
19 petitioner's claim as Northwest (1) made no mention of any existing overbuilt assets and (2) did not
20 mention any plants which require a write-down of assets on its December 31, 2010 Form 10-K. Instead,
21 respondent asserts that Northwest stated on the Form 10-K that it expected to continue making
22 expenditures to expand, improve, and operate its distribution and gas storage systems. (Respondent's
23 Opening Brief, p. 4.)

24 **Petitioner's Reply Brief**

25 In response to respondent's position that petitioner had not provided sufficient evidence to
26 support its claimed excess costs, petitioner references the CH2M HILL Study and states that the study
27 identifies numerous instances of poor construction cost management, errors, and hardships encountered
28 during construction. Petitioner asserts that the excess costs of the project totaled nearly \$50 million, of

1 which \$37 million (i.e., 75 percent of this amount) is reflected on petitioner’s balance sheet. Petitioner
2 acknowledges that it originally asserted that there was a \$19.2 million error in the budget versus actual
3 costs. However, petitioner asserts that the actual difference in its budgeted to actual costs (i.e.,
4 comparing “apples to apples” by excluding base gas costs) is \$31 million. (Petitioner’s Reply Brief,
5 p. 1.) Petitioner agrees that unnecessary costs should not be included with full economic costs but
6 argues that, according to AH 501 (AH 501, p. 74), there is no necessary relationship between the
7 concept of cost and actual cost and that typical costs are to be used in the cost approach, such that
8 change orders, poor management, and errors should be excluded. Consequently, petitioner asserts that it
9 is appropriate to reduce petitioner’s actual construction costs. (Petitioner’s Reply Brief, pp. 1-2.)

10 As for the \$50 million cost adjustment for additional infrastructure that petitioner seeks,
11 petitioner states that Property Tax Rule 6 addresses over- and under-improvements of property as forms
12 of obsolescence. Petitioner contends that the excess infrastructure installed for a “Phase 2” capacity
13 expansion of the facility (i.e., the additional 20 billion cubic feet of storage capacity) must be viewed,
14 under current economic conditions, as an over-improvement. Petitioner asserts that, in order for the
15 facility to generate a financial benefit from the \$50 million in additional infrastructure installed, market
16 conditions must justify the expenditure. However, petitioner argues that financial forecasts clearly do
17 not support this expenditure in the foreseeable future. (Petitioner’s Reply Brief, p. 2.)

18 Finally, petitioner contends that respondent has misread the December 31, 2010 10-K from
19 petitioner’s parent company (Northwest). Petitioner states the discussion in the Form 10-K regarding
20 continued expenditures, for the expansion and improvement of gas storage facilities, was a reference to a
21 regulated gas distribution utility that Northwest owns in Oregon. However, with regard to Gill Ranch
22 itself, petitioner argues that Northwest makes no mention of undertaking any capacity expansions at this
23 facility in the foreseeable future, stating the facility would expand subject to “market demand, project
24 execution, available financing, receipt of future permits, and other rights.” Petitioner further asserts that
25 Northwest, in the Form 10-K, states that “[a]lthough stable gas prices provide opportunities to manage
26 costs for our (utility) distribution customers, they present challenges for our gas storage business by
27 lowering the value of, and reducing the demand for, storage services and limiting Gill Ranch’s ability to
28 contract for longer terms at favorable prices.” (Petitioner’s Reply Brief, pp. 2-3.)

Applicable Law and Appraisal Principles

1
2 **Burden of Proof** Assessing officers are presumed to have properly performed their duties. (Evid.
3 Code, § 664.) The Board has promulgated the Rules for Tax Appeals (RTA) to govern the
4 administrative and appellate review processes for all of the tax and fee programs administered by the
5 Board. (Cal. Code Regs., tit. 18, § 5000.) Of relevance here, RTA 5541, subdivision (a), places the
6 burden of proof upon the taxpayer as to all issues of fact except as otherwise specifically provided by
7 law. Courts have long presumed that the Board assesses all property correctly, placing on the taxpayer
8 the burden of proving that an assessment is incorrect. (*Trailer Train Co. v. State Bd. of Equalization*
9 (1986) 180 Cal.App.3d 565, 584.) Therefore, the petitioner bears the burden of showing that the
10 assessment is incorrect or illegal. (*ITT World Communications v. Santa Clara* (1980) 101 Cal.App.3d
11 246.)

12 **The Reproduction Cost Approach to Value** Property Tax Rule 6, subdivision (a), provides, in part,
13 that: “The reproduction or replacement cost approach to value . . . is preferred when neither reliable
14 sales data . . . nor reliable income data are available” In general, the “reproduction cost of a
15 reproducible property may be estimated either by (1) adjusting the property’s original cost for price level
16 changes and for abnormalities, if any, or (2) applying current prices to the property’s labor and material
17 components, with appropriate additions for entrepreneurial services, interest on borrowed or owner-
18 supplied funds, and other costs typically incurred in bringing the property to a finished state.” (Property
19 Tax Rule 6, subd. (b).) The resulting adjusted cost is the reproduction cost new (ReproCN) which is
20 then “reduced by the amount that such cost is estimated to exceed the current value of the reproducible
21 property by reason of physical deterioration, misplacement, over or under improvement, and other forms
22 of depreciation or obsolescence.” (Property Tax Rule 6, subd. (e).)

23 ReproCN is an estimate of the current cost to replace the existing property with a new property
24 that is an exact replica, or virtually so, of the existing property. Data for the derivation of the ReproCN
25 index factors can be obtained either from prices quoted by current vendors of the property or by
26 applying an appropriate index factor to the historical or original acquisition cost of the property. The
27 use of published index factors is the preferred method when performing mass appraisals. Numerous
28 trade publications provide index factors for the conversion of historical cost to ReproCN. The

1 publishers of these index factors generally survey industry participants and equipment manufacturers
2 and compare current prices to a historical cost database. The ratio of price change for a given year
3 period is the ReprCN index factor.

4 The calculation of the ReprCLD indicator is basically a two-step process. First, the
5 reproduction cost new (ReprCN) is calculated by applying an index factor (also known as “trend
6 factors”) to the historical acquisition cost of property, segregated by year of acquisition. Second, the
7 ReprCN is adjusted for normal depreciation by the application of a percent good factor to the
8 ReprCN. The product of this calculation is the ReprCLD value indicator. (*Unitary Valuation*
9 *Methods* (March 2003) p. 11.)

10 For the ReprCLD indicator, depreciation is the difference in value between a new identical
11 substitute property and the existing property. The difference is recognized as the complement to the
12 percent good factors. Respondent conducts service life studies to assist in determining the appropriate
13 percent good factors. The usefulness of the ReprCLD in the appraisal process depends on whether or
14 not the market recognizes an exact replica of the subject property as having adequate utility for the
15 operational needs of a contemporary business. If there are economical substitutes (i.e., a property of
16 lower cost or greater utility for the property being appraised), the ReprCLD indicator may not be a
17 reliable method to determine the fair market value of a subject property.

18 **Costs to Include—Full Economic Costs** Costs, for appraisal purposes, may be thought of as “full
19 economic costs.” In general, full economic costs are the payments that must be made secure the supply
20 of all of the agents necessary for production and consist of all of the expenditures necessary to place the
21 completed property in the hands of the buyer or the ultimate consumer. The costs which are necessary
22 to construct a property and make it ready for its intended use may be classified as either direct or
23 indirect costs. (AH 502, p. 13; AH 501, p. 75.)

24 Direct costs are expenditures for the labor and materials required to construct the
25 property. They include expenditures for permits, materials and labor, and contractor’s
26 overhead and profit. Indirect costs are expenditures not included in the direct
27 construction of the property. They include expenditures for the developer’s
28 administrative expenses, professional fees, construction financing, construction
insurance, property taxes during construction, and marketing, sales, and lease-up costs
incurred to achieve initial occupancy or sale.

(AH 501, p. 75.)

1 Generally, the costs of all of the functions necessary to place a property into the hands of a
2 consumer are part of the total cost of production. However, costs that are not necessary or costs that do
3 not represent normal costs should be excluded from a cost estimate. Abnormal costs include, among
4 others, costs which are generated by strikes, lockouts, floods, excessive overtime pay, and unforeseen
5 hardships. (AH 501, p. 76.)

6 **Future Use Property** The Federal Energy Regulatory Commission (FERC), Natural Gas Uniform
7 System of Accounts, provides basis account descriptions and accounting definitions for information
8 provided on report forms to that agency.⁶ FERC defines a “gas plant held for future use” as: “. . . the
9 original cost of gas plant (except land and land rights) owned and held for future use in gas service
10 under a definite plan for such use, to include: (1) Property acquired (except land and land rights) but
11 never used by the utility in gas service, but held for such service in the future under a definite plan, and
12 (2) property (except land and land rights) previously used by the utility in gas service, but retired from
13 such service and held pending its reuse in the future, under a definite plan, in gas service.”

14 **Appeals Division’s Analysis and Recommendation**

15 Respondent is presumed to have used a proper valuation approach and correctly determined the
16 value of the property at issue, and petitioner bears the burden of proving otherwise. Petitioner claims
17 cost overruns of approximately \$31 million and \$50 million in infrastructure costs (to accommodate a
18 potential expansion of the facility) that it seeks to exclude from its value.

19 As for petitioner’s claimed cost overruns, the Appeals Division reviewed the CH2M HILL Study
20 submitted by petitioner, a study in which the engineering firm provided a post-project “controls
21 assessment” of the Gill Ranch project, with a specific emphasis on cost estimating, cost tracking and
22 forecasting, and cost management. The objective of the controls assessment was to evaluate petitioner’s
23 cost management processes and procedures for the project. CH2M HILL stated that “it was obvious that
24 [petitioner] assembled a quality, dedicated team, but that they were overwhelmed by the size and
25 complexity of the project.” (CH2M HILL Study, pp. 4-5.)

27 ⁶ Staff recognizes that petitioner is a non-regulated facility. Nevertheless this government website provides a generic
28 definition of this term.

See <http://www.ferc.gov/legal/acct-matts/usofa.asp>.

1 CH2M HILL found that, between August 2008 and the completion of the project at the end of
2 2010, “the estimated Gill Ranch Storage total project cost increased from \$234,000,000 to
3 \$284,000,000, an increase of \$49.6MM and 21.2 percent. As a result, as part of the post project controls
4 assessment, CH2M HILL was asked to evaluate the issues below associated with the cost estimating that
5 was performed on the GRS project. . . . the level of design that was completed when the estimate was
6 performed in August of 2008, may have been in the Class 3 range with an expected level of accuracy of
7 -20% to +30% . . . , hence the 21.2% increase would not have been totally un-expected.” (CH2M HILL
8 Study, p. 7 (underlining added).)

9 CH2M HILL determined that “[w]hile the GRS project team⁷ had some experience at NW
10 Natural on smaller individual projects, the project suffered from a lack of a written, well defined
11 estimating process.” (CH2M HILL Study, p. 7.) In addition, CH2M HILL found that:

12 GRS attempted to get the construction contractor selected and on-board before the IFC
13 drawings were completed to provide some construction input into the final design. While
14 this is generally a good idea, several of the GRS team members felt [the general
15 contractor selected] utilized the incomplete drawing to intentionally underbid some of the
16 work to get the contract. The design and construction drawings were completed after the
17 [general contractor] was selected . . . and construction was started in January 2010. In
18 April, 4 months after starting construction, [the general contractor] submitted a \$22.0MM
19 cost increase due to what they termed design changes reflected in the final construction
20 drawings. This is always the risk that a project owner faces when the construction
21 estimate is performed on less than complete construction drawings.

22 (CH2M HILL Study, p. 8 (underlining added).)

23 CH2M HILL also observed the following in reviewing petitioner’s project cost estimating data:
24 (1) petitioner did not utilize a written defined cost estimating process (or use recommended industry
25 standards in the preparation of cost estimates); (2) cost estimates for the project were not performed at
26 specific project milestones (e.g., 30 percent design complete, 60 percent design complete, and 90/100
27 percent design complete); (3) the project managers did not know the basis of the project cost estimates
28 and had little involvement in the development of the cost estimates; and (4) petitioner could not provide
detailed back-up data to support individual project categories. (CH2M HILL Study, pp. 8-9.)

Finally, CH2M HILL also observed that there were several causes for cost increases, including:

⁷ CH2M HILL refers to petitioner as “GRS”.

1 (1) delays in the approval of the compressor package purchases delayed the delivery of compressor
2 vendor drawings and resulted in incomplete drawing packages, which were used for costs estimates and
3 the bidding process, and led to large construction cost increases; (2) options for the disposal of drilling
4 mud were not fully explored early in the project, which added several million dollars more to the
5 project's costs than originally estimated; (3) adverse weather, and problems encountered due to hawk-
6 mating season increased pipeline construction costs by several million dollars; and (4) the underlying
7 causes of cost overruns for the reservoir development program appeared to be the result of the budget
8 estimates being too low. (CH2M HILL Study, p. 9.)

9 As for petitioner's claimed cost overruns, petitioner should be prepared to explain the
10 reasonableness of its budgeting and cost estimates for the construction of the facility when it was
11 petitioner that commissioned CH2M HILL to prepare an analysis reviewing petitioner's cost estimating,
12 cost tracking and forecasting, and cost management of the project. If petitioner disagrees with any of
13 CH2M HILL's findings (such as petitioner's failure to utilize a written defined cost estimating process
14 or the use of recommended industry standards in the preparation of cost estimates), petitioner should be
15 prepared to explain why it disagrees and to provide support for its position. Finally, in its opening brief,
16 petitioner asserted cost overruns of \$19.2 million but, at the appeals conference, asserted cost overruns
17 of \$31.2 million. Petitioner should be prepared to explain the difference and to provide a detailed
18 explanation for the \$31.2 million adjustment. No later than the close of business on Thursday,
19 November 10, 2011, petitioner should submit its budgets and schedules which substantiate its \$31.2
20 million in claimed cost overruns.

21 Petitioner also seeks an adjustment to the ReproCLD value indicator for \$50 million in claimed
22 costs associated with additional infrastructure to accommodate a potential expansion of the property,
23 presumably for an additional 20 billion cubic feet of storage capacity. No later than the close of
24 business on Thursday, November 10, 2011, petitioner should submit asset lists, depreciation schedules,
25 or any other documents which identify the \$50 million in costs at issue. At the hearing, petitioner
26 should be prepared to explain why these costs were incurred and why, shortly after the facility came on
27 line, this \$50 million in additional infrastructure property has no value.

28 For both of the adjustments which petitioner seeks, petitioner should be prepared to explain why

1 its parent company's Form 10-K reporting did not reflect any write-down of assets on its books to reflect
2 these adjustments.

3 Issue 2

4 **Whether respondent should allow petitioner's claimed adjustment for additional external**
5 **obsolescence based upon an income shortfall method calculation.**

6 **Petitioner's Contentions**

7 Petitioner asserts that natural gas storage serves two primary purposes: (1) it helps utilities meet
8 peak gas demand, and (2) it enables utilities and other natural gas users to purchase extra natural gas
9 when prices are relatively low to avoid purchasing natural gas when prices rise. In addition, petitioner
10 contends that storage enhances reliability, moderates seasonal price fluctuations, and sets a soft cap on
11 natural gas prices. Petitioner states that, because of the seasonal pattern on the demand for natural gas,
12 utilities and other natural gas customers tend to inject natural gas into storage facilities during the
13 summer months for withdrawal during the winter peak season. (Petition, pp. 2-3.)

14 Petitioner states that, as recent as 2008, the United States natural gas production capacity was
15 facing a permanent decline. However, due to new technologies and a drilling boom and the discovery of
16 new fields in the United States, petitioner states that the production of natural gas rose 11 percent in
17 2009 and 2010 and has resulted in an excess supply of natural gas and has driven down prices. (Petition,
18 p. 3.)

19 In addition, petitioner states that an April 2008 California Energy Commission report suggested a
20 demand for additional storage capacity in California and that the introduction of competition in the
21 marketplace might reduce the cost of storage for consumers. Petitioner states the report also found that
22 existing storage fields were heavily utilized and that market participants perceived a demand for
23 additional storage capacity. Petitioner notes that, in Northern California, PG&E and three independent
24 gas storage producers serve the area and that PG&E has relied upon Lodi Gas Storage for 1 billion cubic
25 feet of its peak storage capacity. Petitioner also notes that Lodi Gas Storage informed the California
26 Public Utilities Commission (CPUC) that its facilities were being fully utilized and that Southern
27 California Gas Company sold at least 90 percent of its noncore storage capacity inventory in each of the
28 last four years. (Petition, pp. 3-4.)

1 Petitioner states that it operates in a market-based environment and that its strategy is designed to
2 secure sufficient supplies of natural gas to meet the needs of utility customers and to hedge gas prices to
3 effectively manage costs, reduce price volatility, and maintain a competitive advantage. However,
4 petitioner contends that the substantial new supplies of natural gas in the market has contributed to lower
5 and more stable gas prices and, as a result, has presented challenges to gas storage businesses by
6 lowering the value of, and reducing the demand for, storage services and has limited petitioner's ability
7 to contract for longer terms and favorable prices.⁸ (Petition, p. 5.)

8 Petitioner asserts that its discounted cash flow analysis projects a five-year outlook, arriving at
9 an income approach to value of \$62.6 million, compared to the Board-adopted value of \$222.4 million.
10 (Petition, p. 7.) Petitioner states that, although it does not have an earnings history, it provided
11 respondent with its proforma information in order to develop a Capitalized Earnings Approach (CEA)
12 value, in the form of a discounted cash flow. Petitioner asserts that this approach reflects an income
13 shortfall indicating that an obsolescence adjustment to the cost approach to value is warranted.
14 (Petition, p. 10.)

15 Petitioner states that it was in a start-up mode as of January 1, 2011, but that the facility is now
16 fully leased. Petitioner states that it computed a discounted cash flow value for the facility, until the
17 facility reached a stabilized income. Petitioner asserts that it compared the \$8.6 million of projected net
18 operating income in the final year of the projection to the facility's \$206,203,987 replacement cost new,
19 and computed a 4.2 percent rate of return. Petitioner states that it then compared this rate of return to the
20 10.41 percent required rate of return for the industry (from the Board's 2011 Capitalization Rate Study),
21 and computed external obsolescence of 60 percent.⁹ Petitioner asserts that the 60 percent in external
22 obsolescence should be subtracted from the Board's cost approach value indicator (i.e., \$222,390,511 -
23

24 ⁸ Petitioner quotes the following from its parent company's annual report: "Gill Ranch intends to measure their performance
25 and monitor progress on certain metrics including, but not limited to: earnings per share growth; total shareholder return;
26 return on invested capital; utility return on equity; utility customer satisfaction rating; utility margin; utility capital and
27 operations and maintenance expense per customer; and non-utility earnings before interest, taxes, depreciation and
28 amortization (non-utility EBITDA)."

⁹ Petitioner's calculations are as follows:
\$8.6 million ÷ \$206.2 million = a 4.2 percent rate of return.
10.41 percent - 4.2 percent = 6.21 percent.
6.21 percent ÷ 10.41 percent = 60 percent of the standard rate of return.

1 \$133,434,307 = \$88,956,204), resulting in a final cost approach value, after all forms of obsolescence, of
2 \$5,930,414 per billion cubic feet. (Petition, pp. 7-8.)

3 Petitioner states that natural gas storage providers depend upon the spread between winter and
4 summer natural gas pricing to generate the demand for storage and hedging and that, at the time of the
5 facility's construction, petitioner assumed a \$1.20 to \$2.40 spread between the winter and summer
6 natural gas delivery prices per million cubic feet. However, petitioner contends that the dramatic change
7 in the spread between the winter and summer natural gas prices between 2007 and 2010 has caused a
8 drop in its anticipated earnings. (Petition, p. 8.) As of January 1, 2011, petitioner asserts that the
9 winter/summer price spread was only \$0.60 per million cubic feet. (Petition, p. 10.)

10 Petitioner argues that economic conditions are inhibiting the amount of saleable storage,
11 injection rates, and the need for market participants to hedge their holding. As a result, petitioner asserts
12 that its projected earnings indicate an income shortfall for the foreseeable future and that petitioner and
13 the industry as a whole are suffering from these economic conditions. As such, petitioner contends that
14 market indications for the natural gas industry indicate a substantial increase in obsolescence over the
15 past few years and that, when the return on invested capital is less than an investor's required rate of
16 return (i.e., the weighted average cost of capital (WACC)), a discount to the capitalized costs in the cost
17 approach is appropriate in order to achieve a return that is at least equal to the WACC. Petitioner further
18 contends that, due to increasing supplies, price stability, and declining demand, the value of storage
19 facilities are expected to remain low in the near future and such will likely affect the prices that
20 petitioner can attain in its storage contracts. Consequently, petitioner asserts that an obsolescence
21 adjustment of 60 percent is warranted. (Petition, pp. 8-9.)

22 Petitioner concludes that, after adjusting for all forms of obsolescence (including the adjustments
23 discussed in Issue 1 above), a value in the range of \$123,000,000 is indicated. Petitioner contends that
24 this value is based on that of other comparable facilities (see Issue 3 below) and indicates a value of \$8.2
25 million per billion cubic feet. (Petition, p. 11.)

26 **Respondent's Contentions**

27 Respondent states that the Board-adopted value placed an exclusive reliance on the ReproCLD
28 value indicator. Respondent also states that its CEA model assumes that property is being put to its

1 highest and best use and that the property assessed has an established income stream. However,
2 respondent asserts that petitioner's argument, that it has suffered extraordinary economic obsolescence,
3 is based upon an income shortfall analysis, which requires a CEA analysis. Respondent argues that
4 petitioner's position is not persuasive because petitioner's projected income stream is not reliable.
5 Respondent contends that, as of the 2011 lien date, petitioner's facility was in a start-up mode (as the
6 construction of the facility was completed in October 2010). As such, respondent argues that petitioner
7 reported a net operating loss for the year because petitioner's earnings ability had not reached its full
8 potential during the year. Respondent asserts that petitioner's facility has a greater income potential and
9 that, until the facility has established a mature income stream, any measure of obsolescence using an
10 income shortfall method would be inappropriate. (Respondent's Opening Brief, p. 5.)

11 However, subsequent to the appeals conference, respondent reviewed the documentation
12 presented by petitioner. Respondent states that, based upon the current state of the gas storage industry
13 and petitioner's expected income levels over the next several years, an adjustment for economic
14 obsolescence is appropriate. Respondent recommends that the Board-adopted value be reduced by
15 \$22,000,000, resulting in a revised value recommendation of \$200,400,000. Respondent asserts that the
16 proposed reduction in value relates specifically to, and is an adjustment for, economic obsolescence and
17 not for any of the other claimed adjustments sought by petitioner.

18 **Petitioner's Reply Brief**

19 Petitioner asserts that Property Tax Rule 8 does not require an established income stream in
20 order to employ the income approach to value. As such, petitioner contends that, if a real or
21 hypothetical income stream can be attributed to a property, the income approach is then applicable.
22 Petitioner asserts that it had actual contracts in place in 2010 and that additional contracts were executed
23 in 2011, such that there is ample market data specific to its property regarding its income-generating
24 capacity for a full year. Consequently, petitioner submits income projections going forward several
25 years into the future which indicate a significant and verifiable reduction in the facility's earning ability
26 via the income approach or by the income shortfall method as a means of quantifying external
27 obsolescence. (Petitioner's Reply Brief, p. 3.)

28 Petitioner argues that the decline in natural gas spreads has disrupted the financial model for gas

1 storage facilities, such that Gill Ranch as a non-regulated facility is completely subject to market forces.
2 As such, petitioner argues that market realities must be looked at to value the property and to fairly
3 measure its market-based earnings ability. Petitioner asserts that its DCF analysis indicates an enterprise
4 value of \$62.6 million, a value that takes into account Gill Ranch's actual contract revenue from 2010
5 and its best estimate of future earnings for 2011 and beyond based upon its examination of market trends
6 and current contract negotiations. Based upon this, petitioner requests that respondent perform its own
7 CEA analysis using market data and that respondent value petitioner's property based upon an equal
8 weighting (50/50) of the income approach and the cost approach. (Petitioner's Reply Brief, pp. 3-4.)

9 Applicable Law and Appraisal Principles

10 **Burden of Proof** Assessing officers are presumed to have properly performed their duties. (Evid.
11 Code, § 664.) The Board has promulgated the Rules for Tax Appeals (RTA) to govern the
12 administrative and appellate review processes for all of the tax and fee programs administered by the
13 Board. (Cal. Code Regs., tit. 18, § 5000.) Of relevance here, RTA 5541, subdivision (a), places the
14 burden of proof upon the taxpayer as to all issues of fact except as otherwise specifically provided by
15 law. Courts have long presumed that the Board assesses all property correctly, placing on the taxpayer
16 the burden of proving that an assessment is incorrect. (*Trailer Train Co. v. State Bd. of Equalization*
17 (1986) 180 Cal.App.3d 565, 584.) Therefore, the petitioner bears the burden of showing that the
18 assessment is incorrect or illegal. (*ITT World Communications v. Santa Clara* (1980) 101 Cal.App.3d
19 246.)

20 **Value Standard** Property Tax Rule 2, subdivision (a), states that "in addition to the meaning ascribed
21 to them in the Revenue and Taxation Code, the words "full value", "full cash value", "cash value",
22 "actual value" and "fair market value" mean the price at which a property, if exposed for sale in the
23 open market with a reasonable time for the seller to find a purchaser, would transfer for cash or its
24 equivalent under prevailing market conditions between parties who have knowledge of the uses to which
25 the property may be put, both seeking to maximize their gains and neither being in a position to take
26 advantage of the exigencies of the other."

27 **Reconciliation of Value Indicators** Property Tax Rule 3 requires that, in estimating value, the assessor
28 shall consider one or more of the approaches to value "as may be appropriate for the property being

1 appraised,” which includes the comparative sales approach, the replacement or reproduction cost
2 approach (e.g., ReplCLD valuation methodology), or the income approach. The appropriateness of an
3 approach is often related to the type of property being appraised and the available data. (Assessors’
4 Handbook section 502, *Advanced Appraisal* (December 1998) (AH 502), p. 109.) In addition, the
5 validity of a value indicator will depend upon the accuracy of data and adjustments made to the
6 approach. That is, the accuracy of a value indicator depends on the amount of available comparable
7 data, the number and type of adjustments, and the dollar amount of adjustments. Finally, if a large
8 amount of comparable data is available for a given approach, the appraiser may have more confidence in
9 that approach. For example, if income, expense, and capitalization rate data can be obtained from many
10 properties comparable to the subject, the appraiser may attribute significant accuracy to the income
11 approach. The greatest reliance should be placed on that approach or combination of approaches that
12 best measures the type of benefits the subject property yields. The final value estimate reflects the
13 relative weight that the appraiser assigned, either implicitly or explicitly, to each approach. (AH 502,
14 p. 112.)

15 **The Reproduction Cost Approach to Value** Property Tax Rule 6, subdivision (a), provides, in part,
16 that: “The reproduction or replacement cost approach to value . . . is preferred when neither reliable
17 sales data . . . nor reliable income data are available” In general, the “reproduction cost of a
18 reproducible property may be estimated either by (1) adjusting the property’s original cost for price level
19 changes and for abnormalities, if any, or (2) applying current prices to the property’s labor and material
20 components, with appropriate additions for entrepreneurial services, interest on borrowed or owner-
21 supplied funds, and other costs typically incurred in bringing the property to a finished state.” (Property
22 Tax Rule 6, subd. (b).) The resulting adjusted cost is the reproduction cost new (ReproCN) which is
23 then “reduced by the amount that such cost is estimated to exceed the current value of the reproducible
24 property by reason of physical deterioration, misplacement, over or under improvement, and other forms
25 of depreciation or obsolescence.” (Property Tax Rule 6, subd. (e).)

26 ReproCN is an estimate of the current cost to replace the existing property with a new property
27 that is an exact replica, or virtually so, of the existing property. Data for the derivation of the ReproCN
28 index factors can be obtained either from prices quoted by current vendors of the property or by

1 applying an appropriate index factor to the historical or original acquisition cost of the property. The
2 use of published index factors is the preferred method when performing mass appraisals. Numerous
3 trade publications provide index factors for the conversion of historical cost to ReproCN. The
4 publishers of these index factors generally survey industry participants and equipment manufacturers
5 and compare current prices to a historical cost database. The ratio of price change for a given year
6 period is the ReproCN index factor.

7 The calculation of the ReproCLD indicator is basically a two-step process. First, the
8 reproduction cost new (ReproCN) is calculated by applying an index factor (also known as “trend
9 factors”) to the historical acquisition cost of property, segregated by year of acquisition. Second, the
10 ReproCN is adjusted for normal depreciation by the application of a percent good factor to the
11 ReproCN. The product of this calculation is the ReproCLD value indicator. (*Unitary Valuation*
12 *Methods* (March 2003) p. 11.)

13 For the ReproCLD indicator, depreciation is the difference in value between a new identical
14 substitute property and the existing property. The difference is recognized as the complement to the
15 percent good factors. Respondent conducts service life studies to assist in determining the appropriate
16 percent good factors. The usefulness of the ReproCLD in the appraisal process depends on whether or
17 not the market recognizes an exact replica of the subject property as having adequate utility for the
18 operational needs of a contemporary business. If there are economical substitutes (i.e., a property of
19 lower cost or greater utility for the property being appraised), the ReproCLD indicator may not be a
20 reliable method to determine the fair market value of a subject property.

21 **Income Approach to Value** Property Tax Rule 8, subdivision (a), states that “the income approach is
22 used in conjunction with other approaches when the property under appraisal is typically purchased in
23 anticipation of a money income and either has an established income stream or can be attributed a real or
24 hypothetical income stream by comparison with other properties.” Subdivision (b) describes the income
25 approach to value as the valuation method whereby, “an appraiser values an income property by
26 computing the present worth of a future income stream. This present worth depends upon the size,
27 shape, and duration of the estimated stream and upon the capitalization rate at which future income is
28 discounted to its present worth.” Subdivision (c) provides that “the amount to be capitalized is the net

1 return which a reasonably well-informed owner and reasonably well informed buyers may anticipate on
2 the valuation date that the taxable property existing on that date will yield under prudent management
3 and subject to legally enforceable restrictions as such persons may foresee as of that date.”

4 **Appeals Division’s Analysis and Recommendation**

5 Petitioner notes that Lodi Gas Storage has informed the CPUC that its facilities were being fully
6 utilized, that Southern California Gas Company sold at least 90 percent of its storage capacity inventory
7 in each of the last four years, and that, as of January 1, 2011, its facility was fully subscribed (i.e.,
8 leased). Staff notes that petitioner’s facility began operation merely a year ago, in October 2010. In
9 spite of this, petitioner seeks an adjustment for economic obsolescence based upon its income
10 projections of the facility, when the facility has yet to establish an income stream. At the hearing,
11 petitioner should be prepared to explain why its income projections should be considered reliable when
12 petitioner has yet to complete its first full year of operation in 2011 and when the facility does not have
13 an established income stream on which the Board may rely.

14 Petitioner asserts that its value as of the lien date is \$123,000,000, after reflecting all of the
15 adjustments petitioner seeks in this appeal. Also, at the appeals conference, petitioner asserts that a
16 50/50 weighting of the cost approach (the ReproCLD value indicator) and the income approach (the
17 CEA value indicator) should be utilized to value the facility. At the hearing, petitioner should be
18 prepared to explain its method for determining that 50/50 weighting of the cost and income approaches
19 is appropriate here. In addition, petitioner should be prepared to state the amount of the claimed
20 adjustment for economic obsolescence that it seeks and, no later than the close of business on Thursday,
21 November 10, 2011, should submit evidence to substantiate this amount of economic obsolescence.

22 **Issue 3**

23 **Whether respondent should make an adjustment to allow for additional obsolescence based upon**
24 **a comparison of the 2011 Board-adopted unitary values of its competitors.**

25 **Petitioner’s Contentions**

26 Petitioner states (as discussed above) that, although it does not have an earnings history, it
27 provided respondent with its proforma information in order to develop a CEA value, in the form of a
28 discounted cash flow. Petitioner asserts that this approach reflects an income shortfall indicating that an

1 obsolescence adjustment to the cost approach to value is warranted. (Petition, p. 10.) Petitioner
2 compares itself to the other state-assessed storage facilities, and the assessed values of those facilities, to
3 illustrate how market participants would consider its value (Petition, p. 10):

A	B	C	C ÷ B
Entity	Storage Capacity	2011 Assessed Value	Value Per Bcf ¹⁰
Gill Ranch Storage	15 Bcf	\$222,400,000	\$14,826,667
Wild Goose Storage	29 Bcf	\$235,300,000	\$8,113,793
Lodi Gas Storage	34 Bcf	\$274,500,000	\$8,073,529

10 **Respondent's Contentions**

11 Respondent states that petitioner contends that its value, per billion cubic feet, was significantly
12 greater than its competitors and that, as a result, an adjustment for additional obsolescence is warranted.
13 Respondent asserts that petitioner's analysis is flawed because it fails to account for all of the other
14 reasons why differences in value would exist, including differences in location, business operations,
15 customer composition, the estimated depreciation of the facility, and other factors that might influence
16 the assessed value of petitioner's competitors. Respondent argues that Wild Goose's and Lodi Gas's
17 assets are older than petitioner's assets and have experienced depreciation that petitioner's newly-
18 constructed assets have not experienced. Consequently, respondent concludes that no adjustment is
19 warranted. (Respondent's Opening Brief, p. 6.)

20 **Petitioner's Reply Brief**

21 Petitioner compares itself to Wild Goose Storage and Lodi Gas Storage as follows (Petitioner's
22 Reply Brief, p. 4):

- 23 • Location: Petitioner states that all three facilities are within 230 miles of each other in
24 the Central Valley and are in the Northern California storage market.
- 25 • Business: Petitioner states that all three facilities are independent facilities which use
26 underground gas storage fields and are completely subject to market prices.

27
28 ¹⁰ "Bcf" is a reference to billion cubic feet.

- 1 • Customers: Petitioner states that all three facilities compete for the same customer base
2 and have interconnections with PG&E.
- 3 • Depreciation: Petitioner states that Wild Goose Storage was established in 1997 and that
4 Lodi Gas Storage was established in 2002, with additions in 2007 and 2009.

5 Petitioner asserts that it is valued at 1.83 times the value of Wild Goose Storage and at 1.84 times
6 the value of Lodi Gas Storage. Petitioner asserts that the age difference in these facilities is not a
7 reasonable explanation for the lower values of those facilities, as Wild Goose Storage is much older than
8 Lodi Gas Storage but both have very similar values per billion cubic feet of storage capacity. Petitioner
9 instead attributes the value difference to its belief that the earnings ability of those facilities is
10 considered when respondent determines the unitary value of those properties. (Petitioner’s Reply Brief,
11 pp. 4-5.)

12 Applicable Law and Appraisal Principles

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

17 **Value Standard** Property Tax Rule 2, subdivision (a), states that “in addition to the meaning ascribed
18 to them in the Revenue and Taxation Code, the words “full value”, “full cash value”, “cash value”,
19 “actual value” and “fair market value” mean the price at which a property, if exposed for sale in the
20 open market with a reasonable time for the seller to find a purchaser, would transfer for cash or its
21 equivalent under prevailing market conditions between parties who have knowledge of the uses to which
22 the property may be put, both seeking to maximize their gains and neither being in a position to take
23 advantage of the exigencies of the other.”

24 **Reconciliation of Value Indicators** Property Tax Rule 3 requires that, in estimating value, the assessor
25 shall consider one or more of the approaches to value “as may be appropriate for the property being
26 appraised,” which includes the comparative sales approach, the replacement or reproduction cost
27 approach (e.g., ReplCLD valuation methodology), or the income approach. The appropriateness of an
28 approach is often related to the type of property being appraised and the available data. (Assessors’

1 Handbook section 502, *Advanced Appraisal* (December 1998) (AH 502), p. 109.) In addition, the
2 validity of a value indicator will depend upon the accuracy of data and adjustments made to the
3 approach. That is, the accuracy of a value indicator depends on the amount of available comparable
4 data, the number and type of adjustments, and the dollar amount of adjustments. Finally, if a large
5 amount of comparable data is available for a given approach, the appraiser may have more confidence in
6 that approach. For example, if income, expense, and capitalization rate data can be obtained from many
7 properties comparable to the subject, the appraiser may attribute significant accuracy to the income
8 approach. The greatest reliance should be placed on that approach or combination of approaches that
9 best measures the type of benefits the subject property yields. The final value estimate reflects the
10 relative weight that the appraiser assigned, either implicitly or explicitly, to each approach. (AH 502, p.
11 112.)

12 **The Reproduction Cost Approach to Value** Property Tax Rule 6, subdivision (a), provides, in part,
13 that: “The reproduction or replacement cost approach to value . . . is preferred when neither reliable
14 sales data . . . nor reliable income data are available . . .” In general, the “reproduction cost of a
15 reproducible property may be estimated either by (1) adjusting the property’s original cost for price level
16 changes and for abnormalities, if any, or (2) applying current prices to the property’s labor and material
17 components, with appropriate additions for entrepreneurial services, interest on borrowed or owner-
18 supplied funds, and other costs typically incurred in bringing the property to a finished state.” (Property
19 Tax Rule 6, subd. (b).) The resulting adjusted cost is the reproduction cost new (ReproCN) which is
20 then “reduced by the amount that such cost is estimated to exceed the current value of the reproducible
21 property by reason of physical deterioration, misplacement, over or under improvement, and other forms
22 of depreciation or obsolescence.” (Property Tax Rule 6, subd. (e).)

23 ReproCN is an estimate of the current cost to replace the existing property with a new property
24 that is an exact replica, or virtually so, of the existing property. Data for the derivation of the ReproCN
25 index factors can be obtained either from prices quoted by current vendors of the property or by
26 applying an appropriate index factor to the historical or original acquisition cost of the property. The
27 use of published index factors is the preferred method when performing mass appraisals. Numerous
28 trade publications provide index factors for the conversion of historical cost to ReproCN. The

1 publishers of these index factors generally survey industry participants and equipment manufacturers
2 and compare current prices to a historical cost database. The ratio of price change for a given year
3 period is the ReprCN index factor.

4 The calculation of the ReprCLD indicator is basically a two-step process. First, the
5 reproduction cost new (ReprCN) is calculated by applying an index factor (also known as “trend
6 factors”) to the historical acquisition cost of property, segregated by year of acquisition. Second, the
7 ReprCN is adjusted for normal depreciation by the application of a percent good factor to the
8 ReprCN. The product of this calculation is the ReprCLD value indicator. (*Unitary Valuation*
9 *Methods* (March 2003) p. 11.)

10 For the ReprCLD indicator, depreciation is the difference in value between a new identical
11 substitute property and the existing property. The difference is recognized as the complement to the
12 percent good factors. Respondent conducts service life studies to assist in determining the appropriate
13 percent good factors. The usefulness of the ReprCLD in the appraisal process depends on whether or
14 not the market recognizes an exact replica of the subject property as having adequate utility for the
15 operational needs of a contemporary business. If there are economical substitutes (i.e., a property of
16 lower cost or greater utility for the property being appraised), the ReprCLD indicator may not be a
17 reliable method to determine the fair market value of a subject property.

18 **Income Approach to Value** Property Tax Rule 8, subdivision (a), states that “the income approach is
19 used in conjunction with other approaches when the property under appraisal is typically purchased in
20 anticipation of a money income and either has an established income stream or can be attributed a real or
21 hypothetical income stream by comparison with other properties.” Subdivision (b) describes the income
22 approach to value as the valuation method whereby, “an appraiser values an income property by
23 computing the present worth of a future income stream. This present worth depends upon the size,
24 shape, and duration of the estimated stream and upon the capitalization rate at which future income is
25 discounted to its present worth.” Subdivision (c) provides that “the amount to be capitalized is the net
26 return which a reasonably well-informed owner and reasonably well informed buyers may anticipate on
27 the valuation date that the taxable property existing on that date will yield under prudent management
28 and subject to legally enforceable restrictions as such persons may foresee as of that date.”

Appeals Division’s Analysis and Recommendation

Respondent is presumed to have used a proper valuation approach and correctly determined the value of the property at issue, and petitioner bears the burden of proving otherwise. At the hearing, petitioner should be prepared to explain the adjustments that it seeks to its value as discussed in the analysis and recommendation section to Issue 2 above. Respondent should be prepared to present argument and any supporting authority to counter petitioner’s position that its unitary value was significantly higher than its competitors in terms of value per billion cubic feet.

///

///

///

///

///

///

///

///

///

///

///

///

///

///

///

///

///

///

///

///

///

///