

Issue Paper Number 01-016



- Board Meeting
- Business Taxes Committee
- Customer Services and Administrative Efficiency Committee
- Legislative Committee
- Property Tax Committee
- Other

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## PROPERTY TAX RULE 305.3, APPLICATION FOR EQUALIZATION UNDER REVENUE AND TAXATION CODE SECTION 469

### I. Issue

Should the Board authorize publication of proposed new Property Tax Rule 305.3, *Application for Equalization Under Revenue and Taxation Code Section 469*, and what should the rule include with respect to the definition of *result of an audit*, *assessee*, and *property previously equalized*?

### II. Staff Recommendation

Staff recommends that the language for Property Tax Rule 305.3 in Attachment 1 be authorized for publication.

### III. Other Alternative(s) Considered

1. The Board could specify that the definition of *result of an audit* in the attached proposed Property Tax Rule 305.3 be altered as proposed in Attachment 2.
2. The Board could specify that a definition of *assessee* be added to the attached proposed Property Tax Rule 305.3 as proposed in Attachment 3.
3. The Board could specify that the definition of *property previously equalized* in the attached proposed Property Tax Rule 305.3 be altered as proposed in Attachment 4.

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#### **IV. Background**

The Board directed staff to draft a new Rule 305.3 to interpret provisions of Revenue and Taxation Code section 469 relating to assessment appeal rights and appeals boards' jurisdiction to equalize the value of property at the location of a business subject to an audit performed pursuant to that section.

Revenue and Taxation Code section 469 requires that a county assessor audit at least once each four years the books and records of a taxpayer engaged in a profession, trade, or business who owns, claims, possesses or controls assessable trade fixtures and business tangible personal property with a full value of \$400,000 or more. Section 469 further provides in the fourth paragraph:

If the result of an audit for any year discloses property subject to an escape assessment, then the original assessment of all property of the assessee at the location of the profession, trade, or business for that year shall be subject to review, equalization and adjustment by the county board of equalization or assessment appeals board pursuant to Chapter 1 (commencing with Section 1601) of Part 3 of this division, except in those instances when the property had previously been equalized for the year in question.

The paragraph was added by 1978 legislation amending section 469. Prior to the amendment, a taxpayer could only appeal the value of property that was the subject of an enrolled escape assessment following an audit, and could not appeal the original assessment of any other property at the location. In a letter to Governor Edmund G. Brown, Jr., dated August 31, 1978, the sponsors of the amendment (the Taxation Section of the California State Bar) expressed the intent of the legislation as follows:

The bill would allow a business taxpayer of property tax to have his entire assessment for a particular year at a business premises to be reviewed and equalized when the assessor by reason of an audit proposes an escape assessment. The bill is needed because many taxpayers do not protest assessments when the overall assessment at a business premises seems fair, even though some components are over-assessed and some under-assessed. Then, years later the assessor by reason of audit, proposes an escape assessment for the under-assessed component. Under the present law, the taxpayer has no redress for the over-assessed component at the late date of the proposed escape assessment.

Thus, the amendment was intended to address situations where:

- A taxpayer was satisfied with an overall property assessment, even while recognizing that he/she was not in agreement with the assessor's allocation to various parts of the overall assessment.
- Subsequently, the assessor conducted an audit that resulted in an escape assessment, thereby increasing the overall assessment for the property for a particular year.
- Following the audit, the taxpayer could only challenge the escape assessment even though the taxpayer had previously recognized that the assessment allocations were incorrect.

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A difference of opinion over the application of the foregoing provision has led to the proposal for a new Property Tax Rule to interpret and to make specific its language. Property Taxes Department staff and Legal Division staff drafted proposed Property Tax Rule 305.3 after receiving input from the California Association of Clerks and Election Officials, California Assessors' Association, County Counsels' Association of California, California Taxpayers' Association, and industry representatives.

On April 20, 2001, staff held a meeting in Sacramento with interested parties for discussions in an effort to reach agreement on rule language. Staff and interested parties were unable to resolve disagreements over rule language on three issues. The redrafted Property Tax Rule is to be presented to the Property Tax Committee for its recommendation of Board action at its meeting on May 30, 2001.

The staff now requests direction on three issues concerning language for proposed Rule 305.3 which are presented in this issue paper:

1. How should the phrase *result of an audit* be defined?
2. Should a definition of *assessee* be included in the rule?
3. How should the phrase *property previously equalized* be defined?

## V. Staff Recommendation on Issue 1: Definition of phrase *result of an audit*

*Result of an audit* should be defined as "the final conclusions reached by the assessor during the audit process as described in Rule 191 and shall include a description of any property subject to escape assessment."

### A. Description of the Staff Recommendation

Staff's recommendation defines the "result of an audit" in terms of three elements:

- (1) The result is the final conclusions reached by the assessor based on findings made during the audit process.
  - (2) The audit is the process described in Property Tax Rule 191.
  - (3) The result, i.e. final conclusions, shall include a description of any property subject to escape assessment.
1. The equalization provisions of section 469 are triggered if "the *result* of the audit discloses any property subject to escape assessment." Thus, based on grammatical construction it is clear that property subject to escape assessment must be disclosed by the *result* and not merely by the audit process. Moreover, it is generally understood that an audit is the process of gathering, evaluating, and analyzing data and the result is the culmination of that process as the final conclusion or conclusions determined by the auditor. An *audit* is defined as "a formal examination of an organization's or individual's accounts or financial situation" and as "the final report of an audit." Therefore, in the context of the equalization provisions of section 469, the phrase the *result of the audit* means the final conclusion or conclusions reached by examination of a taxpayer's accounts and records.

Staff's recommended language specifies that the final conclusions are made by the assessor because, under California law, the assessor determines the result of an audit conducted pursuant to section 469. The California Constitution requires that all property subject to taxation shall be assessed at its full cash value. The duty to do this lies with the assessor. (*Bauer-Schweitzer Malting Co. v. City and County of San Francisco* (1973) 8 Cal.3d 942.) Consistent with this constitutional duty, Revenue and Taxation Code section 4986 provides in subdivision (a)(7) for cancellation of taxes "[o]n that portion of an assessment in excess of the value of the property *as determined by the assessor pursuant to Section 469.*" Section 5096 provides in subdivision (g) that one condition for refund of taxes includes taxes "[p]aid on an assessment in excess of the value of the property *as determined by the assessor pursuant to Section 469.*" Section 4831.5 provides for roll corrections under certain conditions "[w]hen it can be *ascertained by the assessor* from an audit of an assessee's books of account or other papers that there has been a defect of description or clerical error of the assessee in his property statement or in other information or records furnished to the assessor." (Italics added.) Thus, the statutory scheme for property tax audits contemplates that the assessor shall determine the result of those audits.

2. Rule 191 is the regulation that interprets, implements, and makes specific the audit provisions of section 469. Thus, staff's recommendation references the rule because the relevant audit provisions for purposes of the equalization provisions of section 469 are set forth in Rule 191.
3. The final conclusions shall include a description of any "property subject to escape assessment" which is a finding that property escaped assessment regardless of whether an escape assessment

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was actually enrolled. Such a finding is necessary because "property subject to escape assessment" triggers the assessee's appeal rights, the purpose of the equalization provisions.

**B. Pros of the Staff Recommendation on Issue No. 1**

The staff recommendation is consistent with both the specific language and the intent of section 469. It affirms the right of an assessee to equalization of the original assessment of all property at the location when the result of the audit discloses property subject to escape assessment. It makes clear, consistent with the statute and Rule 191, that it is the assessor who has the responsibility to conduct the audit and to reach the final conclusions as to value of the property indicated by the audit findings. It also prevents the assessor from unilaterally denying a taxpayer the right of appeal by not enrolling an escape assessment. The latter point was made by the court of appeal in *Heavenly Valley v. El Dorado County Bd. of Equalization* (2000) 84 Cal.App.4th 1323.

**C. Cons of the Staff Recommendation on Issue No. 1**

Opponents of staff's recommendation argue that the staff view requires adding words to the statute and rearranging existing words. Opponents argue that result of the audit is the "consequence" of conducting an audit, not the conclusions of the audit. If the consequence of conducting an audit discloses property subject to escape assessment, then appeal rights should be triggered. The consequence of the audit may be the working papers, documents submitted by the taxpayer, or the conclusions of the assessor. Opponents argue that the statute establishes an objective standard by which the appeal rights are triggered if the consequence of an inspection or review of the taxpayer's books and records is the uncovering of property subject to escape, then an application for review and equalization may be filed.

Opponents argue that staff's language allows the assessor to determine whether or not property subject to escape assessment is discovered during an audit and, thereby, allows the assessor the determinative control over whether the assessee will be given a right to a section 469 appeal. Thus, they argue, if assessor's personnel discover an escape assessment and an overassessment of equal value for a particular tax year, they could prevent the taxpayer from obtaining section 469 relief by issuing a "no change" letter or notice as the final conclusion of the audit, or by making a decision not to complete the audit.

**D. Statutory or Regulatory Change**

Action by the Board to adopt a Property Tax Rule interpreting the equalization provisions of section 469 will add section 305.3 to Title 18 of the California Code of Regulations, Subchapter 3.

**E. Administrative Impact**

None

## **F. Fiscal Impact**

### **1. Cost Impact**

No additional costs.

### **2. Revenue Impact**

None

## **G. Taxpayer/Customer Impact**

Adoption of a Property Tax Rule interpreting the equalization provisions of section 469 will affect administrative procedures for the assessment appeals process at the county level and the functions of the clerks of the appeals boards, appeals board members, county assessors, county counsels, and each taxpayer seeking a reduction in assessment of his or her property's value following an audit conducted pursuant to section 469.

## **H. Critical Time Frames**

There is no critical time frame for adoption of a Property Tax Rule interpreting section 469 since a county assessor conducts audits pursuant to section 469 on an ongoing basis. The 60-day period for filing an application appealing the result of an audit disclosing property subject to an escape assessment commences on receipt of the proper notice of the escape assessment. Consequently, the equalization provisions of section 469 provide for the filing of an application for an equalization hearing before a local board of equalization or county assessment appeals board throughout the year.

## **VI. Alternative to Staff Recommendation on Issue No. 1**

### **A. Description of the Alternative (Cal Tax proposal)**

Cal Tax proposes that the phrase *result of an audit* should be defined as "information obtained from the taxpayer or other sources or conclusions reached by the assessor during the audit process." Under this alternative, the "result" means the "consequence" of conducting an audit, not the conclusions reached. "Disclose" means to expose or uncover. The audit is the object of the verb "discloses," not "audit results" which doesn't exist in the statute. Consequently, whether it is the working papers, documents submitted by the taxpayer, the conclusions of the assessor, or otherwise, it is the consequence of the audit that discloses property, not just the conclusions of the assessor.

### **B. Pros of the Alternative**

Proponents of this alternative argue that it is consistent with the intent of section 469 to provide the taxpayer with the right of appeal coextensive with the assessor's right to audit. Without this objective standard, a taxpayer's right of appeal may be extinguished either by a "no change" audit or by the assessor's decision not to complete the audit in midstream.

### **C. Cons of the Alternative**

Staff believes the alternative is inconsistent with the language of section 469. This alternative proposes that a determination of property subject to escape assessment may be made based upon a partial or incomplete audit. An audit is a process that necessarily involves the examination and analysis of all information relating to the taxpayer's financial books and records. Only when all the

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taxpayer's information has been examined and analyzed and when findings and conclusions have been made can it be determined whether there exists property subject to escape assessment or property that has been overassessed. This alternative suggests that any raw information, such as a single invoice, may be the basis of an audit determination. It would be contrary to generally accepted audit practices for an assessor to make such determinations based on incomplete findings which have not been subjected to review and analysis.

This alternative suggests that, contrary to statutory law, in some instances the assessee rather than the assessor determines whether property is subject to escape assessment. However, the statutory scheme for property tax audits provides that the assessor makes the audit determinations. Revenue and Taxation Code sections 4986 and 5096 provide, respectively, for cancellation of taxes and refund of taxes paid when the amount of the original assessment is in excess of "the value of the property *as determined by the assessor* pursuant to section 469." Revenue and Taxation Code section 4831.5 provides for roll corrections under certain conditions "[w]hen it can be *ascertained by the assessor* from an audit of an assessee's books of account or other papers that there has been a defect of description or clerical error of the assessee in his property statement or in other information or records furnished to the assessor." Moreover, the court of appeal in *Heavenly Valley v. County of El Dorado* (2000) 84 Cal.App.4th 1323, 1331 implicitly recognized that the assessor's auditor makes the audit result determination when it concluded in footnote 9 that "the *auditor's finding* of underassessed property triggered the taxpayer's right to administrative review." (Italics added.)

Furthermore, staff's recommendation would not allow a taxpayer's right of appeal to be extinguished either by a "no change" audit or by the assessor's decision not to complete the audit in midstream. In the case of a "no change" audit, staff's language would still require that the final conclusions describe any property subject to escape assessment, even when an escape assessment is not ultimately enrolled. With respect to the concern that the assessor will fail to complete an audit, the assessor has a statutory duty to complete an audit conducted pursuant to section 469, and there are judicial remedies available to compel an assessor to fulfill that duty (Code of Civil Procedure section 1085; *Connolly v. County of Orange* (1992) 1 Cal.4<sup>th</sup> 1105).

**D. Statutory or Regulatory Change**

Action by the Board to adopt a Property Tax Rule interpreting the equalization provisions of section 469 will add section 305.3 to Title 18 of the California Code of Regulations, Subchapter 3.

**E. Administrative Impact**

None

**F. Fiscal Impact****1. Cost Impact**

No additional costs.

**2. Revenue Impact**

None

### **G. Taxpayer/Customer Impact**

Adoption of a Property Tax Rule interpreting the equalization provisions of section 469 will affect administrative procedures for the assessment appeals process at the county level and the functions of the clerks of the appeals boards, appeals board members, county assessors, county counsels, and each taxpayer seeking a reduction in assessment of his or her property's value following an audit conducted pursuant to section 469.

### **H. Critical Time Frames**

There is no critical time frame for adoption of a Property Tax Rule interpreting section 469 since a county assessor conducts audits pursuant to section 469 on an ongoing basis. The 60-day period for filing an application appealing the result of an audit disclosing property subject to an escape assessment commences on receipt of the proper notice of the escape assessment. Consequently, the equalization provisions of section 469 provide for the filing of an application for an equalization hearing before a local board of equalization or county assessment appeals board throughout the year.

## V. Staff Recommendation on Issue No. 2: Should a definition of *assessee* be included in the rule?

Staff recommends that Property Tax Rule 305.3 not include a definition of *assessee* since the term is already defined by Revenue and Taxation Code section 23 as "the person to whom property or a tax is assessed."

### A. Description of the Staff Recommendation

The fourth paragraph of section 469 provides in relevant part:

If the result of an audit for any year discloses property subject to escape assessment, then the original assessment of all property of the *assessee* at the location of the profession, trade or business for that year shall be subject to review, equalization and adjustment by the county board of equalization or assessment appeals board . . . (Italics added.)

Staff recommends that the rule not include a definition of "assessee" for purposes of applying the equalization provisions of section 469. Staff's recommendation is based on the plain language meaning of "assessee" as defined by the Revenue and Taxation Code. Revenue and Taxation Code section 23 defines an *assessee* as "the person to whom the property or a tax is assessed."

The equalization provisions of section 469 afford an audited assessee the opportunity to appeal the original assessment of his or her property not subject to escape assessment to ensure that the assessed value of the entire property is correctly allocated and equalized. The definition of "assessee" should not be expanded beyond its plain language meaning to allow the audited assessee to seek equalization of property which has not been assessed to that person and, thus, was not part of the original assessment. Furthermore, "assessee" should not include other separate legal entities or individuals affiliated with an assessee where the audited property is not assessed to such other legal entities or individuals, and they are not liable for payment of the property taxes on the assessment.

### B. Pros of the Staff Recommendation on Issue No. 2

The recommendation conforms the plain language of section 469 to the statutory definition of *assessee*. Applying the term "assessee" in a manner consistent with existing law ensures that the purpose of the original legislation is fulfilled, but not expanded. The objective of statutory interpretation is to ascertain and effectuate legislative intent. *Burden v. Snowden* (1992) 2 Cal.4<sup>th</sup> 556, 562. In determining intent, one must look first to the language of the statute, giving effect to its plain meaning. *Ibid.* Where the words of the statute are clear, they may not be added to or altered to accomplish a purpose that does not appear on the face of the statute or from its legislative history. *Ibid.*; Code Civ. Proc. § 1858. Statutes are properly interpreted by consulting "the words themselves, giving them their usual and ordinary meaning." *DaFonte v. Up-Right, Inc.* (1992) 2 Cal.4<sup>th</sup> 593, 601.

By using the term "assessee," the Legislature is presumed to have intended the specific definition of Revenue and Taxation Code section 23.

The original legislation that added the equalization provisions to section 469 was intended to provide an assessee and local assessment appeals boards and boards of equalization with a mechanism to ensure that all of the property in the audited assessee's original assessment could be equalized following the discovery of an escape assessment. To accomplish that purpose, the "assessee" for

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purposes of appealing an escape assessment and the original assessment of all property must be the person to whom the property has been assessed. Thus, property in the taxpayer's original assessment may not include property leased by the audited taxpayer and assessed to a third party or property owned, claimed, or possessed by and assessed to a related entity or individual.

**C. Cons of the Staff Recommendation on Issue No. 2**

Staff's recommendation fails to account for the situation in which the assessor combines the value of property owned by related legal entities to determine if that amount exceeds the threshold amount of personal property and fixtures that requires that assessor to conduct an audit pursuant to section 469. In that event, the original assessment of all the property owned by each of the legal entities should be subject to review, equalization and adjustment by the county board of equalization.

**D. Statutory or Regulatory Change**

Action by the Board to adopt a Property Tax Rule interpreting the equalization provisions of section 469 will add section 305.3 to Title 18 of the California Code of Regulations, Subchapter 3.

**E. Administrative Impact**

None

**F. Fiscal Impact****1. Cost Impact**

No additional costs.

**2. Revenue Impact**

None

**G. Taxpayer/Customer Impact**

Adoption of a Property Tax Rule interpreting the equalization provisions of section 469 will affect administrative procedures for the assessment appeals process at the county level and the functions of the clerks of the appeals boards, appeals board members, county assessors, county counsels, and each taxpayer seeking a reduction in assessment of his or her property's value following an audit conducted pursuant to section 469.

**H. Critical Time Frames**

There is no critical time frame for adoption of a Property Tax Rule interpreting section 469 since a county assessor conducts audits pursuant to section 469 on an ongoing basis. The 60-day period for filing an application appealing the result of an audit disclosing property subject to an escape assessment commences on receipt of the proper notice of the escape assessment. Consequently, the equalization provisions of section 469 provide for the filing of an application for an equalization hearing before a local board of equalization or county assessment appeals board throughout the year.

## VI. Alternative to Staff Recommendation on Issue No. 2

### A. Description of the Alternative (Cal Tax proposal)

*Assessee* should be defined as "a firm with common ownership which includes all the legal entities or individuals that (a) together own and conduct a trade or business within the county and (b) own, claim, or possess property which the assessor combines to determine whether the full value of the locally assessable trade fixtures and business tangible personal property owned, claimed, or possessed by the firm in the county meets the minimum criteria of paragraph one of section 469."

Section 23 defines "assessee" as "the person to whom property or a tax is assessed." Section 19 provides that "person includes any person [or] firm . . ." Although the terms "taxpayer" and "firm" are not clearly defined by the California Code, both appear to mean an operating business including all of the subentities that have common ownership and combine to function as one trade or business.

In view of that definition, the "taxpayer" the assessor defines as the aggregate entity for audit purposes in paragraph one of section 469 is the owner of a "firm" as defined in section 19 for assessment purposes which includes all the subsidiary and related entities that combine to operate as the trade or business in the county. Thus, an assessment issued to any commonly owned unique entity within that firm (the "assessee" of section 23) becomes an assessment to all commonly owned entities of the firm. As a result, subject to all of the rest of the qualifications and limitations (location, year, etc.), the firm can appeal the assessment of all of its property at any location in a year where there is property of the firm that is subject to an escape assessment.

### B. Pros of the Alternative

This alternative ensures equal treatment for all taxpayers by affording related legal entities appeal rights when the assessor has aggregated the value of business personal property and fixtures owned by related legal entities to determine if this amount exceeds the threshold value of business personal property and fixtures for conducting an audit pursuant to section 469.

### C. Cons of the Alternative

This alternative would improperly enlarge the meaning of the plain language of the statute by allowing parties other than the person to whom the property has been assessed to invoke the equalization provisions of section 469 with respect to that property.

While it may be desirable for an assessor to audit two or more related entities at the same time, the value of the business personal property and fixtures owned by each legal entity is viewed separately for purposes of determining whether the assessor is mandated to perform an audit pursuant to section 469. The proposed alternative language sets up a two-part test to define an *assessee*, and the second part of the test assumes that the assessor has aggregated the value of property owned by two or more related entities when conducting an audit pursuant to section 469. However, since assessors do not aggregate the value of related entities for purposes of determining whether the assessor is mandated to perform an audit pursuant to section 469, the second part of the test is never met. Thus, this alternative would add language describing a circumstance that does not exist.

### D. Statutory or Regulatory Change

Action by the Board to adopt a Property Tax Rule interpreting the equalization provisions of section 469 will add section 305.3 to Title 18 of the California Code of Regulations, Subchapter 3.

**E. Administrative Impact**

None

**F. Fiscal Impact**

**1. Cost Impact**

No additional costs.

**2. Revenue Impact**

None

**G. Taxpayer/Customer Impact**

Adoption of a Property Tax Rule interpreting the equalization provisions of section 469 will affect administrative procedures for the assessment appeals process at the county level and the functions of the clerks of the appeals boards, appeals board members, county assessors, county counsels, and each taxpayer seeking a reduction in assessment of his or her property's value following an audit conducted pursuant to section 469.

**H. Critical Time Frames**

There is no critical time frame for adoption of a Property Tax Rule interpreting section 469 since a county assessor conducts audits pursuant to section 469 on an ongoing basis. The 60-day period for filing an application appealing the result of an audit disclosing property subject to an escape assessment commences on receipt of the proper notice of the escape assessment. Consequently, the equalization provisions of section 469 provide for the filing of an application for an equalization hearing before a local board of equalization or county assessment appeals board throughout the year.

**V. Staff Recommendation on Issue No. 3: The definition of the phrase *property that has been previously equalized for the year in question***

Staff recommends that Property Tax Rule 305.3 define the phrase *property that has been previously equalized for the year in question* to mean that "the board has previously made a final determination of full value for property that was the subject of an appeals hearing or a stipulated agreement approved by the board. Property shall be deemed to have been previously equalized unless a hearing decision or stipulated agreement for the year in question specifically excludes that property as the subject of the hearing or stipulated agreement."

**A. Description of the Staff Recommendation**

When an application for review is filed and the local appeals board considers the application, the board must address all issues that are properly before it. Consequently, whatever property is identified on the application is assumed to be the subject of the hearing and equalized by the board unless otherwise excluded. Pursuant to Rule 324, the value determinations made by an appeals board decision or agreed upon by stipulation is presumed to equalize the value of all property that was the subject of the hearing or of the agreement.

Staff's recommendation describes the function of an appeals board, which is to make a final determination of the full value of property by conducting an appeals hearing or by approval of a stipulated agreement between the parties. However, Rule 324 also makes clear that an appeals board has jurisdiction to determine the scope of the hearing to include other issues and value determinations. In recognition of that discretion, the second sentence of staff's recommendation provides that the appeals board may specify that some property which was originally the subject of the hearing has been excluded from the board's value determination.

**B. Pros of the Staff Recommendation on Issue No. 3**

By recognizing the constitutional authority of an appeals board to determine the full value of property that is the subject of the hearing, staff's recommendation is consistent with and fulfills the intent of section 469 that any property which has been previously equalized is not subject to review, equalization and adjustment. The law presumes that an appeals board properly performs its constitutional duties to determine value for all property that is the subject of the hearing (Evidence Code section 664). Thus, an appeals board decision carries a presumption that the board has equalized the value of all property that was the subject of the hearing. Therefore, the property that is the subject of the hearing is "presumed" or "deemed" to be equalized unless otherwise specifically excluded.

Contrary to the assertions of those who disagree with staff's recommendation, the language does not "attempt to rewrite the statute in a manner obviously not intended by the Legislature." Cal Tax reasons that "if the Legislature had wanted to create some type of "presumption" or "deeming" that property had been previously equalized, it would have said so." However, the reasoning is circular: the Legislature didn't say it so they didn't intend it and the Legislature didn't intend it because they didn't say it. By making this circular argument (which could be made anytime rule language differed from statutory language), the opponents ignore the obvious fact that the rule is being adopted to interpret the statute and that the purpose of interpretation is to elaborate on and define concepts that are not defined by the statute. Simply put, if the Legislature had defined every term, then there would be no reason to interpret the statute.

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The specificity provided by the "specifically excluded" language will provide all parties with needed clarity and will prevent "gaming" the appeal process. It will also assist the clerk in ensuring that county boards do not inadvertently default on their statutory obligation to hear and decide appeals within two years of timely filing, pursuant to Revenue and Taxation Code section 1604, subdivision (c).

**C. Cons of the Staff Recommendation on Issue No. 3**

Cal Tax contends that "deemed equalized" language is contrary to the statute, which requires that the assessor be permitted to audit and the taxpayer be permitted to seek equalization except for "that portion of the assessment that was the subject of the prior equalization hearing." The concept is very akin to *res judicata*, i.e., that which was decided before need not be addressed again. But the preclusive effect of the prior decision relates only to the portion of the property which was actually the subject of the prior hearing. If the property was not valued in the prior hearing, the assessor should be able to audit such property, and the taxpayer should be able to seek section 469 relief as to the same.

The new "deemed to have been previously equalized" language attempts to rewrite the statute in a manner obviously not intended by the Legislature. If the Legislature had wanted to create some type of "presumption" or "deeming" that property had been previously equalized, it would have said so. Instead, the words of the statute are quite clear. As to the portion of the property which was the subject of the prior hearing, it need not be re-audited. All other portions of the property may be the subject of a subsequent audit and escape assessment.

Thus, it violates the statutory language to deem property which was not the subject of the hearing to instead have been the subject of such hearing. Stated differently, if the property was never part of a hearing, how can it be presumed to be the subject of a hearing simply because the parties did not say it was not "the subject of a hearing"?

As a practical matter, it is very important that the taxpayer and the assessor have the ability to define exactly what a stipulation is intended to cover. Otherwise, some taxpayers might be tempted to file protective applications every year to obtain virtual immunity from the audit process by using a "deemed equalized" or "presumed to be equalized" interpretation of section 469.

**D. Statutory or Regulatory Change**

Action by the Board to adopt a Property Tax Rule interpreting the equalization provisions of section 469 will add section 305.3 to Title 18 of the California Code of Regulations, Subchapter 3.

**E. Administrative Impact**

None

**F. Fiscal Impact****1. Cost Impact**

No additional costs.

**2. Revenue Impact**

None

### **G. Taxpayer/Customer Impact**

Adoption of a Property Tax Rule interpreting the equalization provisions of section 469 will affect administrative procedures for the assessment appeals process at the county level and the functions of the clerks of the appeals boards, appeals board members, county assessors, county counsels, and each taxpayer seeking a reduction in assessment of his or her property's value following an audit conducted pursuant to section 469.

### **H. Critical Time Frames**

There is no critical time frame for adoption of a Property Tax Rule interpreting section 469 since a county assessor conducts audits pursuant to section 469 on an ongoing basis. The 60-day period for filing an application appealing the result of an audit disclosing property subject to an escape assessment commences on receipt of the proper notice of the escape assessment. Consequently, the equalization provisions of section 469 provide for the filing of an application for an equalization hearing before a local board of equalization or county assessment appeals board throughout the year.

## **VI. Alternative to Staff Recommendation on Issue No. 3**

### **A. Description of the Alternative (Cal Tax proposal)**

*Property has been previously equalized for the year in question* "means that the board has previously made a final determination of full value for that item, category, or class of property that was the subject of an assessment appeal hearing or was the subject of a stipulated agreement approved by the board. An item, category, or class of property, or portion thereof, shall be deemed to have been the subject of a hearing or of a stipulated agreement only to the extent the board's decision or the stipulated agreement specifically identify the value of such item, category, or class, or portion thereof, as a value contested and resolved by the board hearing or stipulated agreement."

### **B. Pros of the Alternative**

Only the property specifically identified by the board's decision or stipulated agreement as the subject of a hearing can be presumed to be equalized. A strong practical reason for using the "specifically identified" language is that many stipulations and some board decisions will use "from" and "to" values to inform the collector's office of the change in total assessment values. In each county there may be only one or two categories of personal property showing in the tax bills. Therefore, in order to minimize confusion in changing the roll, the board will notify the collector of changes in those one or two overall numbers by using the "from" and "to" schedules. But that may give little or no indication of what property was the actual subject of the valuation hearing.

For example, there may be \$100,000,000 of personal property shown as a single line item on the tax bill. The taxpayer may file an application in September to object to the trending table on office equipment, which may represent \$2,000,000 of that \$100,000,000 value total. If the board hears the value of the office equipment and determines a \$500,000 reduction in the office equipment, they will reduce the overall personal property value "from" \$100,000,000 "to" \$99,500,000. That does not mean, however, that all of the rest of the personal property was the subject of the equalization hearing.

Under the staff's language, the entire \$100,000,000 would be deemed to have been valued. However, the statute clearly envisions that only the office equipment issue before the board be

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treated as already equalized and that the assessor is permitted to audit all of the rest of the property in that situation.

Finally, it is very important that the taxpayer and the assessor have the ability to define exactly what the stipulation is intended to cover. Otherwise, some taxpayers might be tempted to file protective applications every year to obtain virtual immunity from the audit process by using a "deemed equalized" or "presumed to be equalized" interpretation of section 469.

**C. Cons of the Alternative**

The appeals board is vested with the authority to decide the scope of the hearing including the property on which it makes a value determination. Thus, the board is required to address all issues raised in the application. Therefore, a board's decision or a stipulated agreement approved by the board is presumed to equalize all property that is the subject of the application.

In addition, this alternative would impact the current practice whereby assessors and taxpayers frequently use the stipulation process to resolve disputes. In fiscal year 1998-99, over 18,000 stipulations were submitted to and approved by appeals boards to resolve applications before them. In most instances, the stipulations submitted to the boards equalized all properties that were the subject of the application. From a workload position, it would be onerous to make it necessary for the assessor to specifically identify every item of property. Therefore, it is most feasible that in those few instances where the stipulations are not intended to equalize all property that is the subject of the application, that those stipulations should specify what property is being excluded from equalization.

Further, this alternative would lead to subsequent disputes over which property has been equalized by the decision or stipulation. Under staff's recommendation, the decision or stipulation would specify only that property which has not been equalized.

Finally, the statutory scheme precludes a taxpayer from filing a "protective application each year to obtain virtual immunity" as contended by Cal Tax. Paragraph 3 of section 469 specifically states that "equalization of the property . . . shall not preclude a subsequent audit and shall not preclude the assessor from levying an escape assessment in appropriate instances. . ." Sections 531.3 and 531.4 clearly provide that it is appropriate for the assessor to levy escape assessments resulting from a taxpayer's misreporting information on the business property statement.

**D. Statutory or Regulatory Change**

Action by the Board to adopt a Property Tax Rule interpreting the equalization provisions of section 469 will add section 305.3 to Title 18 of the California Code of Regulations, Subchapter 3.

**E. Administrative Impact**

None

**F. Fiscal Impact****1. Cost Impact**

No additional costs.

## **2. Revenue Impact**

None

## **G. Taxpayer/Customer Impact**

Adoption of a Property Tax Rule interpreting the equalization provisions of section 469 will affect administrative procedures for the assessment appeals process at the county level and the functions of the clerks of the appeals boards, appeals board members, county assessors, county counsels, and each taxpayer seeking a reduction in assessment of his or her property's value following an audit conducted pursuant to section 469.

## **H. Critical Time Frames**

There is no critical time frame for adoption of a Property Tax Rule interpreting section 469 since a county assessor conducts audits pursuant to section 469 on an ongoing basis. The 60-day period for filing an application appealing the result of an audit disclosing property subject to an escape assessment commences on receipt of the proper notice of the escape assessment. Consequently, the equalization provisions of section 469 provide for the filing of an application for an equalization hearing before a local board of equalization or county assessment appeals board throughout the year.

Prepared by: Legal Division; Property Taxes Section  
Property Taxes Department; Policy, Planning, and Standards Division

Current as of: May 14, 2001

### **305.3. APPLICATION FOR EQUALIZATION UNDER REVENUE AND TAXATION CODE SECTION 469**

*Reference:* Sections 23, 408, 469, 531, 531.8, 533, 534, 1603, 1605, Revenue and Taxation Code.

**(a) GENERAL.** In addition to any rights of appeal of escape or supplemental assessments as described in Rule 305(d)(2) of this subchapter, if the result of an audit discloses property subject to an escape assessment for any year covered by the audit, then, pursuant to section 1605 of the Revenue and Taxation Code, an application may be filed for review, equalization, and adjustment of the original assessment of all property of the assessee at the location of the profession, trade, or business for that year, except any property that has previously been equalized for the year in question.

**(b) DEFINITIONS.** For purposes of subsection (a) of this regulation:

(1) "Audit" means any audit of the books and records of a taxpayer engaged in a profession, trade, or business who owns, claims, possesses, or controls locally assessable business tangible personal property and trade fixtures within the county that have a full value in excess of the amount set forth in section 469 of the Revenue and Taxation Code. For a multi-year audit, only those years that are equal to or in excess of the full value threshold of section 469 are eligible for equalization pursuant to subsection (a) of this rule.

(2) "Property subject to an escape assessment" means any individual item of the assessee's property that, upon the final conclusion of the audit, the assessor has determined to have been underassessed or not assessed at all when the assessor made the original assessment of the assessee's property, and which has not been previously equalized by an appeals board, regardless of whether the assessor actually makes or enrolls an escape assessment. Property is subject to an escape assessment even if the audit results disclose an overassessment of another portion of an item of the property, and the amount of the underassessment could be offset completely by the amount of overassessment.

(3) "Result of an audit" means the final conclusions reached by the assessor during the audit process as described in Rule 191 and shall include a description of any property subject to escape assessment.

(4) "Original assessment" means the assessment and any subsequent roll corrections or roll changes prior to the date of the commencement of the audit for the roll year for which the result of the audit discloses property subject to an escape assessment.

(5) "All property of the assessee" means any property, real or personal, assessed to the assessee at the location of the profession, trade, or business for the year of the audit.

(6) "Location of the profession, trade, or business" means a site, as determined by the board, where the property subject to the escape assessment is located. Site includes all property within the same appraisal unit as the property that is subject to escape assessment. Site also includes

other property not within the same appraisal unit as the property that is subject to escape assessment, when the other property and the property that escaped assessment function as part of the same economic unit of the profession, trade, or business. A "location of the profession, trade, or business" may include multiple parcels of real property, noncontiguous parcels, parcels with separate addresses, and parcels in separate revenue districts within the county.

(7) "Property that has been previously equalized for the year in question" means that the board has previously made a final determination of full value for property that was the subject of an appeals hearing or a stipulated agreement approved by the board. Property shall be deemed to have been previously equalized unless a hearing decision or stipulated agreement for the year in question specifically excludes that property as the subject of the hearing or stipulated agreement.

**(c) NOTICE OF AUDIT RESULTS.** Upon completion of an audit of the assessee's books and records, the assessor shall notify the assessee in writing of the results of the audit as defined in subsection (b)(3) of this rule for all property, locations, and years that were the subject of the audit. At the request of the assessee, the assessor shall permit the assessee or his or her designated representative to inspect or copy any information, documents, or records relating to the audit in accordance with the provisions of Revenue and Taxation Code section 408.

**(d) NOTICE FOR FILING AN APPLICATION.** An application shall be filed with the clerk no later than 60 days after the date of mailing by which the assessee is notified that the result of the audit has disclosed property subject to escape assessment. The notice shall be mailed to the assessee by regular United States mail directed to the assessee at the assessee's latest address known to the assessor, unless, prior to the mailing of the notice, the assessor is notified in writing by the assessee of a change in address. The notice for purposes of filing an application shall be one of the following, depending upon the conclusion(s) of the audit:

(1) Where an escape assessment is enrolled by the assessor, the notice shall be the tax bill based upon the results of the audit and resulting escape assessment(s) for counties of the first class or any county that has adopted a resolution pursuant to Revenue and Taxation Code section 1605, subdivision (c). If the county is not a county of the first class or has not adopted a resolution pursuant to Revenue and Taxation Code section 1605, subdivision (c), the notice of escape assessment pursuant to Revenue and Taxation Code section 534 shall serve as the notice.

(2) Where the assessor does not enroll an escape assessment resulting from the audit or when the escape assessment is enrolled but offset pursuant to Revenue and Taxation Code section 533, the assessor's written notification of the audit results for the property, locations, and each year that were the subject of the audit as described in subsection (c) of this rule shall be the notice. The notice of audit results showing property subject to escape assessment for each year shall indicate that it is the notice of the assessee's right to file an application.

**(e) EXAMPLES.** The following examples are illustrative of the foregoing criteria. Examples 1 and 2 concern "who may file" an application on the assessee's property. Examples 3, 4, and 5 clarify the "location" of the profession, trade, or business.

Example 1: Taxpayer DRK owns and is assessed for land, a building, and business property. The full value of the business tangible personal property and trade fixtures exceeds the dollar

threshold in Revenue and Taxation Code section 469. DRK leases the entire business to RCJ. The county assessor conducts an audit of DRK pursuant to section 469, and the result of the audit discloses property subject to an escape assessment. DRK, as the assessee, can file an application for equalization for all property, real and personal, where the property subject to the escape assessment is located. In addition, RCJ may file an application for equalization of DRK's property if RCJ qualifies as a person affected pursuant to rule 302 of this subchapter.

Example 2: Taxpayer DRK owns and is assessed for land and a building. DRK leases the land and building to RCJ. RCJ operates a business in DRK's building and is assessed for business tangible personal property and trade fixtures with a full value that exceeds the dollar threshold in Revenue and Taxation Code section 469. The county assessor conducts an audit of RCJ pursuant to section 469, and the result of the audit discloses property subject to an escape assessment. RCJ, as the assessee, can file an application for equalization on his personal property and trade fixtures only. RCJ cannot file an application on DRK's land and building as this is not property of the assessee. In addition, since DRK is not a person affected pursuant to rule 302 of the subchapter, he cannot file an application on either his land and building or RCJ's personal property and fixtures.

Example 3: An assessee conducts a profession, trade, or business on a campus-like setting that is composed of three separate buildings. Each building has its own address and assessor's parcel number and is owned and operated by the same assessee. If an audit discloses any property subject to an escape assessment, then all property of the assessee on the campus is eligible for equalization if the board determines that it functions and is operated as one economic unit of a profession, trade, or business.

Example 4: An assessee operates five grocery stores in a county. Although the stores are owned and operated by one assessee, carry the same type of merchandise, and share in common advertising, each store operates independently. If property subject to an escape assessment is discovered only at one store, the property at that store's location is subject to equalization following an audit. The other four stores are not considered property at the site of the profession, trade, or business where the escape assessment occurred, as they operate independently as separate economic units.

Example 5: An assessee owns and operates a department store with a parking garage on an adjacent parcel. The parcel that houses the parking garage has no personal property or fixtures located on it. If an audit discloses personal property subject to an escape assessment for the department store, the parking garage would also be eligible for equalization if the board determines that the parcels with the garage and the store are part of the same appraisal unit or economic unit of the profession, trade, or business.

**(f) JURISDICTION OF THE BOARD.** Nothing in this rule shall be interpreted to limit or enlarge a board's jurisdiction under specific statutory provisions or other rules of this subchapter.

**ISSUE: RESULT OF AN AUDIT**

<p align="center"><b>STAFF RECOMMENDATION</b></p> <p><b>LANGUAGE SUPPORTED BY:</b>                      BOARD STAFF                      CALIFORNIA ASSESSORS' ASSOCIATION                      COUNTY COUNSELS' ASSOCIATION OF CALIFORNIA                      CALIFORNIA ASSOCIATION OF CLERKS AND                      ELECTION OFFICIALS</p>	<p align="center"><b>ALTERNATIVE</b></p> <p><b>LANGUAGE SUPPORTED BY:</b>                      CAL TAX</p>
<p>Subsection (b)(2):                      (2) "Property subject to an escape assessment" means any individual item of the assessee's property that, upon the final conclusion of the audit, the assessor has determined to have been underassessed or not assessed at all when the assessor made the original assessment of the assessee's property, and which has not been previously equalized by an appeals board, regardless of whether the assessor actually makes or enrolls an escape assessment. Property is subject to an escape assessment even if the audit results disclose an overassessment of another portion of an item of the property, and the amount of the underassessment could be offset completely by the amount of overassessment.</p> <p>Subsection (b)(3):                      (3) "Result of an audit" means the final conclusions reached by the assessor during the audit process as described in Rule 191 and shall include a description of any property subject to escape assessment.</p>	<p>Subsection (b)(2):                      (2) "Property subject to an escape assessment" means any individual item of the assessee's property that, <del>upon the final conclusion of the audit, the assessor has determined to have</del> been underassessed or not assessed at all when the assessor made the original assessment of the assessee's property, and which has not been previously equalized by an appeals board, regardless of whether the assessor actually makes or enrolls an escape assessment. Property is subject to an escape assessment even if the audit <del>results</del> <u>discloses</u> an overassessment of another portion of an item of the property, and the amount of the underassessment could be offset completely by the amount of overassessment.</p> <p>Subsection (b)(3):                      (3) "Result of an audit" means <u>any information obtained from the taxpayer or other sources or the final</u> conclusions reached by the assessor during the audit process as described in Rule 191 and shall include a description of any property subject to escape assessment.</p>

**ISSUE: ASSESSEE**

<p align="center"><b>STAFF RECOMMENDATION</b></p> <p><b>LANGUAGE SUPPORTED BY:</b>  <b>BOARD STAFF</b>  <b>CALIFORNIA ASSESSORS' ASSOCIATION</b>  <b>COUNTY COUNSELS' ASSOCIATION OF CALIFORNIA</b>  <b>CALIFORNIA ASSOCIATION OF CLERKS AND</b>  <b>ELECTION OFFICIALS</b></p>	<p align="center"><b>ALTERNATIVE</b></p> <p><b>LANGUAGE SUPPORTED BY:</b>  <b>CAL TAX</b></p>
<p>None</p>	<p>Add to subsection (b):  <u>For purposes of this regulation:</u>  <u>(1) "A taxpayer engaged in a profession, trade, or business" means a firm with common ownership which includes all the legal entities or individuals that (a) together own and conduct a trade or business within the county and (b) own, claim, or possess property which the assessor combines to determine whether the full value of the locally assessable trade fixtures and business tangible personal property owned, claimed, possessed by the firm in the county meets the minimum criteria of paragraph one of section 469.</u>  <u>(2) "Assessee" means a firm as defined in subsection (1) above.</u></p>

**ISSUE: PROPERTY PREVIOUSLY EQUALIZED**

<p align="center"><b>STAFF RECOMMENDATION</b></p> <p><b>LANGUAGE SUPPORTED BY:</b>  <b>BOARD STAFF</b>  <b>CALIFORNIA ASSESSORS' ASSOCIATION</b>  <b>COUNTY COUNSELS' ASSOCIATION OF CALIFORNIA</b>  <b>CALIFORNIA ASSOCIATION OF CLERKS AND</b>  <b>ELECTION OFFICIALS</b></p>	<p align="center"><b>ALTERNATIVE</b></p> <p><b>LANGUAGE SUPPORTED BY:</b>  <b>CAL TAX</b></p>
<p>Subsection (b)(7):                      "Property that has been previously equalized for the year in question" means that the board has previously made a final determination of full value for property that was the subject of an appeals hearing or a stipulated agreement approved by the board. Property shall be deemed to have been previously equalized unless a hearing decision or stipulated agreement for the year in question specifically excludes that property as the subject of the hearing or stipulated agreement.</p>	<p>Subsection (b)(7):                      "Property that has been previously equalized for the year in question" means that the board has previously made a final determination of full value for <u>that item, category, or class of property</u> that was the subject of an <u>assessment</u> appeals hearing or <u>was the subject of</u> a stipulated agreement approved by the board. <u>An item, category, or class of Pproperty, or portion thereof,</u> shall be deemed to have been <u>the subject of a hearing or of a stipulated agreement only to the extent the board's decision or the stipulated agreement specifically identify the value of such item, category, or class, or portion thereof, as a value contested and resolved by the board</u> <del>previously equalized unless a hearing decision or stipulated agreement for the year in question</del> specifically excludes that property as the subject of the hearing or stipulated agreement.</p>