

KERN COUNTY ASSESSMENT PRACTICES SURVEY

AUGUST 2006

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August 24, 2006

TO COUNTY ASSESSORS:

KERN COUNTY
ASSESSMENT PRACTICES SURVEY

No. 2006/033

A copy of the [Kern County Assessment Practices Survey Report](#) is enclosed for your information. The Board of Equalization (BOE) completed this survey in fulfillment of the provisions of sections 15640-15646 of the Government Code. These code sections provide that the BOE shall make surveys in each county and city and county to determine that the practices and procedures used by the county assessor in the valuation of properties are in conformity with all provisions of law.

The Honorable James W. Fitch, Kern County Assessor-Recorder, was provided a draft of this report and given an opportunity to file a written response to the findings and recommendations contained therein. The report, including the assessor's response, constitutes the final survey report which is distributed to the Governor, the Attorney General, and the State Legislature; and to the Kern County Board of Supervisors, Grand Jury, and Assessment Appeals Board.

Fieldwork for this survey was performed by the BOE's County Property Tax Division from September through November 2004. The report does not reflect changes implemented by the assessor after the fieldwork was completed.

Mr. Fitch and his staff gave their complete cooperation during the survey. We gratefully acknowledge their patience and courtesy during the interruption of their normal work routine.

These survey reports give government officials in California charged with property tax administration the opportunity to exchange ideas for the mutual benefit of all participants and stakeholders. We encourage you to share with us your questions, comments, and suggestions for improvement.

Sincerely,

/s/ David J. Gau

David J. Gau
Deputy Director
Property and Special Taxes Department

DJG:jm
Enclosure

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INTRODUCTION

Although county government has the primary responsibility for local property tax assessment, the State has both a public policy interest and a financial interest in promoting fair and equitable assessments throughout California. The public policy interest arises from the impact of property taxes on taxpayers and the inherently subjective nature of the assessment process. The financial interest comes from the fact that more than one-half of all property tax revenue is used to fund public schools and the State is required to backfill any shortfalls from that property tax funding.

The assessment practices survey program is one of the State's major efforts to address these interests and to promote uniformity, fairness, equity, and integrity in the property tax assessment process. Under this program, the State Board of Equalization (BOE) periodically reviews the practices and procedures of (surveys) every county assessor's office. This report reflects the BOE's findings in its current survey of the Kern County Assessor-Recorder's Office.¹

The assessor is required to file with the board of supervisors a response that states the manner in which the assessor has implemented, intends to implement, or the reasons for not implementing the recommendations contained in this report. Copies of the response are to be sent to the Governor, the Attorney General, the BOE, the Senate and Assembly, and the Kern County Grand Jury and Assessment Appeals Board. That response is to be filed within one year of the date the report is issued and annually thereafter until all issues are resolved. The Honorable James W. Fitch, Kern County Assessor-Recorder, elected to file his initial response prior to the publication of our survey; it is included in this report following the Appendixes.

While typical management audit reports emphasize problem areas, they say little about operations that are performed correctly. Assessment practices survey reports also tend to emphasize problem areas, but they also contain information required by law (see *Scope of Assessment Practices Surveys*) and information that may be useful to other assessors. The latter information is provided in the hope that the report will promote uniform, effective, and efficient assessment practices throughout California.

¹ The report covers only the assessment functions of the assessor-recorder's office.

SCOPE OF ASSESSMENT PRACTICES SURVEYS

Government Code sections 15640 and 15642 define the scope of an assessment practices survey. As directed by those statutes, our survey addresses the adequacy of the procedures and practices employed by the assessor in the valuation of property, the volume of assessing work as measured by property type, and the performance of other duties enjoined upon the assessor.

In addition, pursuant to Revenue and Taxation Code² section 75.60, the BOE determines through the survey program whether a county assessment roll meets the standards for purposes of certifying the eligibility of the county to continue to recover costs associated with administering supplemental assessments. Such certification is obtained either by satisfactory statistical result from a sampling of the county's assessment roll, or by a determination by the survey team-based on objective standards defined in regulation—that there are no significant assessment problems in the county. The statutory and regulatory requirements pertaining to the assessment practices survey program are detailed in Appendix B.

Our survey of the Kern County Assessor's Office included reviews of the assessor's records, interviews with the assessor and his staff, and contact with officials in other public agencies in Kern County who provided information relevant to the property tax assessment program.

Since this survey did not include an assessment sample pursuant to Government Code section 15640(c), our review included an examination to determine whether "significant assessment problems" exist, as defined by Rule 371.³

This report offers recommendations to help the assessor correct assessment problems identified by the survey team. The survey team makes recommendations when assessment practices in a given area are not in accordance with property tax law or generally accepted appraisal practices. An assessment practices survey is not a comprehensive audit of the assessor's entire operation. The survey team does not examine internal fiscal controls or the internal management of an assessor's office outside those areas related to assessment. In terms of current auditing practices, an assessment practices survey resembles a compliance audit—the survey team's primary objective is to determine whether assessments are being made in accordance with property tax law.

² Unless otherwise stated, all statutory references are to the California Revenue and Taxation Code.

EXECUTIVE SUMMARY

As stated in the Introduction, this report emphasizes problem areas we found in the operations of the assessor's office. However, it also identifies program elements that we found particularly effective and describes areas of improvement since our last assessment practices survey.

In our 2000 Kern County Assessment Practices Survey, we made 27 recommendations to address problems in the assessor's assessment policies and procedures. The assessor implemented 19 of the recommended changes. The remaining eight recommendations that were not implemented are repeated in this report.

In the area of administration, we noted several positive aspects:

- The assessor has consistently turned the assessment roll over to the auditor-controller timely.
- The assessor has annually met or surpassed the State-County Property Tax Administration Program goals.
- The assessor's programs for assessment appeals; assessment roll changes; low-value property exemption; church, religious, and welfare exemptions; and the racehorse administrative tax are all operated effectively.

Administrative components of the assessor's programs that need improvement follow:

- The notice informing the applicant of a proposed reassessment, due to property damage caused by misfortune or calamity, does not reflect the current statutory time period in which to file an appeal.
- The assessor uses several outdated forms and includes an inaccurate statement in the cover letter for the annual property statements. In addition, the *Notice of Supplemental Assessment* does not conform to the provisions of section 75.31.

In the area of real property assessment, the assessor has effective programs for the enrollment of new construction, declines in value, California Land Conservation Act property, water company property, and pipeline rights-of-way. Other real property programs have areas where improvement is needed:

- The assessor still does not timely apply the penalty for failure to file the *Change of Ownership Statement*.
- The assessor inappropriately issues supplemental assessments for taxable government-owned properties when there is a change in ownership and does not issue supplemental assessments for possessory interests.

- The assessor does not properly establish base year values for taxable government-owned properties.
- The assessor still does not assess all taxable possessory interests or the possessory interests in land improved with aircraft hangars. In addition, the assessor does not properly apply Rule 21 to taxable possessory interests, deduct expenses from gross income when valuing possessory interests by the income approach, and follow section 61(b)(2) when assessing possessory interests.
- The assessor does not assess all leasehold improvements reported on business property statements.
- The assessor continues to inappropriately value non-producing petroleum property on a per well basis, still does not properly account for abandonment costs in the cash flow analysis, and does not develop capitalization rates for cogeneration facilities independent of the primary use of the associated property.
- The assessor does not appraise mining property as an appraisal unit for purposes of measuring declines in value.

The assessor has an effective audit program. In addition, we found no problems with the assessment of leased equipment, manufactured homes, aircraft, vessels, or animals. One area, however, needs improvement:

- The assessor is still not following the guidelines in Assessors' Handbook Section 581, *Equipment Index and Percent Good Factors* (AH 581), in establishing maximum index factors.

Despite the problems noted above, we found that most properties and property types are assessed correctly.

We found no significant assessment problems as defined in Rule 371. Since Kern County was not selected for assessment sampling pursuant to Government Code section 15643(b), this report does not include the assessment ratios that are generated for surveys that include assessment sampling. Accordingly, pursuant to section 75.60, Kern County continues to be eligible for recovery of costs associated with administering supplemental assessments.

Here is a list of the formal recommendations contained in this report, arrayed in the order that they appear in the text.

RECOMMENDATION 1: Revise the notice informing a taxpayer of the proposed reassessment to reflect the current statutory time period in which to file an appeal.....12

RECOMMENDATION 2: Revise the assessment forms program by: (1) using only current forms and approved rearranged forms, (2) including only permissible requirements on the cover letter for the annual mineral property statement, and (3) conforming the language of the *Notice of Supplemental Assessment* to the requirements of section 75.31(e).17

RECOMMENDATION 3: Timely apply the penalty for failure to file a change in ownership statement as prescribed in section 482(a).21

RECOMMENDATION 4: Issue all supplemental assessments according to statutory guidelines.25

RECOMMENDATION 5: Establish the base year value for taxable government-owned property according to BOE guidelines.27

RECOMMENDATION 6: Improve the possessory interest program by: (1) assessing all taxable possessory interests, (2) reviewing improvement-only possessory interests for escape assessments, (3) reviewing all taxable possessory interests with stated terms of possession for declines in value, (4) deducting expenses from gross income when valuing possessory interests by the income approach, and (5) revaluing taxable possessory interests at the end of the reasonably anticipated term of possession used for their assessment.28

RECOMMENDATION 7: Assess all leasehold improvements.31

RECOMMENDATION 8: Revise the mineral property assessment program by: (1) consistently valuing non-producing and marginal petroleum properties, (2) properly accounting for abandonment expenses in the cash flow analysis, (3) developing capitalization rates for cogeneration facilities independent of the primary use of the associated property, and (4) appraising mining property as an appraisal unit for the purpose of measuring declines in value....32

RECOMMENDATION 9: Use the Assessors' Handbook Section 581, as intended, when valuing older equipment.38

RESULTS OF 2000 SURVEY

Change in Ownership

We recommended the assessor apply the penalty for a failure to file a change in ownership statement as prescribed in section 482. The assessor has not implemented this recommendation and it is repeated in this report.

We recommended the assessor ensure the reappraisal of all real property owned by legal entities that have experienced a change in ownership, review business property statements to discover legal entities that have experienced changes in control, and implement a written policy for making cash equivalent adjustments. These recommendations have been implemented.

Declines in Value

We recommended the assessor develop a comprehensive appraisal program for the review of properties that experience a decline in value. This recommendation has been implemented.

Taxable Possessory Interests

We recommended the assessor review all uses of the county fairgrounds to discover taxable possessory interests and review improvement-only possessory interests for escape assessments. These recommendations have not been implemented and are repeated in this report.

We recommended the assessor increase documentation on the possessory interest appraisal records. This recommendation has been implemented.

Taxable Government-Owned Properties

We recommended the assessor develop a program to discover all qualifying taxable government-owned properties. This recommendation has been implemented.

Leasehold/Tenant Improvements

We recommended the assessor improve coordination between the real and business property staff. Since the assessor has not implemented this recommendation, and we found a number of escaped leasehold improvements, we repeat this recommendation with a focus toward assessing all leasehold improvements.

Water Companies

We recommended the assessor consider the income approach in valuing property owned by private water companies and develop written procedures for assessing property owned by water companies. Currently, the assessor has considered the income approach, but primarily relies on the sales comparison and the historical cost less depreciation (HCLD) approaches to value. Also,

the assessor relies on Assessors' Handbook Section 542, *Assessment of Water Companies and Water Rights*, as a written procedural source. There for we will not repeat these recommendations.

Petroleum Property

We recommended the assessor revise the valuation method for non-producing petroleum property, properly account for abandonment costs in the cash flow analysis of petroleum producing property, and develop capitalization rates for cogeneration facilities independent of the primary use of the associated property. These recommendations have not been implemented and are repeated in this report.

Estimated Assessments

We recommended the assessor inspect the property or audit the records for every estimated assessment within four years of non-filing of the business property statement. This recommendation has been implemented.

Valuation of Business Personal Property

We recommended the assessor use the BOE's equipment index factors as intended. This recommendation has not been implemented and we repeat it in this report.

Audit Program

We recommended the assessor bring the mandatory audit program to current status, expand the nonmandatory audit program, and obtain a signed waiver of the statute of limitations when an audit will not be performed timely. These recommendations have been implemented.

Vessels and General Aircraft

We recommended the assessor apply the 10 percent penalty to all non-filers of the aircraft statement and field check aircraft when owners request a reduction in assessment. These recommendations have been implemented.

We also recommended that the assessor consider make, model, and engine differences when appraising all vessels and use the BOE-prescribed vessel property statement. These recommendations have been implemented.

Manufactured Homes

We recommended the assessor consider the values listed in recognized value guides in the assessment of manufactured homes, apply the California Consumer Price Index inflation factor to the base year value of all manufactured homes without regard to the ownership of the underlying land, and annually assess all manufactured homes at the lesser of the factored base year value or the current market value. These recommendations have been implemented.

OVERVIEW OF KERN COUNTY

Kern County was created on April 2, 1866, after the discovery of oil in Bakersfield in 1865. Agriculture and oil are Kern County's largest industries. The total value of agricultural commodities produced exceeded \$3 billion in 2004, with the top five commodities being grapes, almonds, milk, citrus, and cotton.

Kern County lies in the southern end of the Central Valley. It is bordered on the north by Kings, Tulare, and Inyo counties; on the east by San Bernardino County; on the south by Los Angeles and Ventura counties; and on the west by San Luis Obispo and Santa Barbara counties. It is California's third-largest county, having an area of 8,141 square miles, and an estimated population of nearly 735,000.

Kern County has 11 municipalities that encompass more than 400 square miles. Bakersfield is the center of county government.

The following table displays information pertinent to the 2004-05 assessment roll:

	NUMBER OF ASSESSMENTS	ASSESSED VALUE
Secured Roll	382,195	\$45,389,639,000
Unsecured Roll	22,713	\$2,280,152,000
Total Assessment Roll	404,908	\$47,669,791,000

The next table illustrates the growth in assessed values for recent years:

ROLL YEAR	TOTAL ROLL VALUE	INCREASE	STATEWIDE INCREASE
2004-05	\$47,669,791,000	8.6%	8.3%
2003-04	\$44,928,215,000	1.10%	7.3%
2002-03	\$44,441,337,000	(2.8%)	7.3%
2001-02	\$45,624,925,000	6.5%	9.4%
2000-01	\$42,846,057,000	6.1%	8.3%
1999-00	\$40,009,648,000		

ADMINISTRATION

This section of the survey report focuses on administrative policies and procedures of the assessor's office that affect both the real property and business property assessment programs. Subjects addressed include the assessor's budget and staffing, the State-County Property Tax Administration Program (PTAP), appraiser certification, assessment appeals, disaster relief, assessment roll changes, low-value property exemption, exemptions, racehorse administrative tax, and assessment forms.

Budget and Staffing

As shown in the following table, the assessor's office has benefited from increased budget levels in recent years. PTAP funds are accounted for separately from the assessor's official budget. In addition to the permanent and the PTAP staff shown below, there are two part-time staff and two contract appraisers.

BUDGET YEAR	GROSS BUDGET ⁴	INCREASE	PERMANENT STAFF*	PTAP FUNDS RECEIVED	PTAP STAFF
2003-04	\$7,080,681	2.0%	96	\$1,211,318	13
2002-03	\$6,946,056	5.0%	96	\$1,211,318	15
2001-02	\$6,597,601	3.0%	96	\$1,211,318	15
2000-01	\$6,416,541	5.0%	97	\$1,211,318	15
1999-00	\$6,113,676		94	\$1,211,318	17

* Includes the assessor

The assessor has several work units within his office. Reporting directly to the assessor are the assistant assessor, the confidential administrative assistant, and the business manager. The assistant assessor is responsible for the Realty, Special Properties, and Assessment Standards Divisions, and the information systems unit, which provides supports functions for the assessor and recorder's office.

The Realty Division appraises agricultural, commercial, and residential properties; the Special Properties Division includes business properties and the Natural Resources Section, which appraises oil and gas properties; and the Assessment Standards Division includes the Mapping and Title Sections.

State-County Property Tax Administration Program

In 1995, the Legislature established the State-County Property Tax Administration Program (PTAP). This program, which was later entitled the State-County Property Tax Administration Loan Program, provided state-funded loans to eligible counties for the improvement of property

⁴ County of Kern Budget Unit Financing Uses Detail. Budget dollars do not include PTAP funds.

tax administration.⁵ This program expired June 30, 2001 and was replaced with the Property Tax Administration Grant Program, which is available to counties for fiscal years 2002-03 through 2006-07.⁶ The grant program operates in essentially the same manner as the loan program except that if a county fails to meet its contractual performance criteria, the county will not be obligated to repay the grant but will be ineligible to continue to receive a grant.

If an eligible county elected to participate, the county and the State Department of Finance entered into a written contract, as described in section 95.31. The contract provides that the county must agree to maintain a base funding and staffing level in the assessor's office equal to the funding and staffing levels for the 1994-95 fiscal year. This requirement prevents a county from using PTAP funds to supplant the assessor's existing funding.

For most counties, the contract provides that verification of performance is provided to the State Department of Finance by the county auditor-controller.

Kern County has participated in the PTAP since April 1, 1996. For contract year 2003-04, the assessor received a grant of \$1,211,318. The county's required base funding and staffing levels for the assessor's office is \$5,471,570 and 94 positions, respectively. The Kern County Auditor-Controller has certified to the State Department of Finance that the county met the contractual requirements for every year under contract. The most current agreement between the state and the county was entered into on January 1, 2004. The period of agreement is for one year.

The assessor proposed the use of the grant money to fund appraisal processing, clerical and support positions, and overtime as needed. With the aid of the PTAP grant, the assessor increased the 2003-04 assessment roll by over \$18 billion, including the assessment appeals board's decisions on two cases totaling more than \$13 billion.

Appraiser Certification

Section 670 provides that no person shall perform the duties of an appraiser for property tax purposes unless he or she holds a valid certificate issued by the BOE. There are a total of 56 certified appraisers on staff, of whom 47 hold advanced certificates and 4 have permanent appraiser's certificates, and 5 have temporary certificates. We found that the assessor and his staff possess the required certificates. Additionally, we found that the auditor-appraisers performing mandatory audits meet the requirements referenced in section 670(d).

The assessor uses one contract appraiser who assists in the performance of appraisal work of properties associated with the extraction and/or the production of hydrocarbons. This contract meets the requirements set forth in section 674 as to compensation and confidentiality.

⁵ Chapter 914, Statutes of 1995, in effect October 16, 1995. The Property Tax Administration Loan Program expired June 30, 2001.

⁶ State-County Property Tax Administration Program funding has been suspended for two years, beginning with the 2005-06 California State Budget.

Assessment Appeals

The assessment appeals function is prescribed by article XIII, section 16 of the California Constitution. Sections 1601 through 1641.5 are the statutory provisions governing the conduct and procedures of assessment appeals boards and the manner of their creation. As authorized by Government Code section 15606, the BOE has adopted Rules 301 through 326 to regulate the assessment appeal process.

Kern County has one assessment appeals board consisting of three officers. The total membership of the board is five members, appointed by the board of supervisors, who rotate for the hearings. The county does not have any hearing officers.

The following table illustrates the appeal workload in recent years:

APPEALS	FISCAL YEAR				
	2003-04	2002-03	2001-02	2000-01	1999-00
Total Appeals:					
Applications Received	669	1,111	1,498	1,208	1,354
Carried Over	1,176	2,546	1,757	1,030	1,256
Total	1,845	3,657	3,255	2,238	2,610
Resolution:					
Denied-lack of Appearance	12	33	10	20	77
Hearing-reduced	1	0	0	2	0
Hearing-increased	0	0	0	0	0
Hearing-upheld	6	1,012	26	9	198
Invalid	0	0	5	3	92
Stipulation	569	3	11	96	230
Withdrawn	778	1,433	657	351	983
Other	0	0	0	0	0
Disposition unknown	0	0	0	0	0
Total	1,366	2,481	709	481	1,580
Carried over to next year	479	1,176	2,546	1,757	1,030

The assessments appeals clerk receives all applications for assessment reduction. When the clerk verifies that the application is valid, the application is date stamped. A copy of the application is sent to the assessor. The assessor's staff then meets with the taxpayer to review the assessment. After the review, if the assessor's staff and the taxpayer have not agreed to stipulate or the taxpayer does not withdraw the application, the assessor will inform the assessment appeals clerk to schedule a hearing before the assessment appeals board.

We found no problems with the assessor's program for assessment appeals.

Disaster Relief

Section 170 permits a county board of supervisors to adopt an ordinance that allows immediate property tax relief on qualifying property damaged or destroyed by misfortune or calamity. The property tax relief is available to the owner of any taxable property whose property suffers damage exceeding \$10,000 (without his or her fault) in a misfortune or calamity. In addition, section 170 provides procedures for calculating value reductions and restorations of value for the affected property.

To obtain relief under an ordinance, assesseees must make a written application to the assessor requesting reassessment. However, if the assessor is aware of any property that has suffered damage by misfortune or calamity, the assessor must either provide the last known assessee with an application for reassessment, or he or she may revalue the property on lien date.

Upon receipt of a properly completed application, the assessor shall reassess the property for tax relief purposes. If the sum of the full cash values of the land, improvements, and personal property before the damage or destruction exceeds the sum of the values after the damage by \$10,000 or more, the assessor shall then determine the percentage of value reductions and reduce the assessed values accordingly.

The Kern County Board of Supervisors has adopted a continuous disaster relief ordinance, pursuant to section 170, that allows the assessor to grant tax relief to taxpayers whose properties have been damaged or destroyed through calamity or disaster.

The assessor uses a variety of methods to discover property that has been damaged or destroyed, including newspaper articles, building permits issued for repairs, and the appraiser's knowledge of their assigned areas. However, the primary source of discovery is through contact by the taxpayer.

We found that the overall disaster relief program is conducted in conformance with section 170. The assessor's application and instruction to the taxpayer are in accordance with the changes in law that became operative in 1997. However, we did find one area of the assessor's program that needs to be revised.

RECOMMENDATION 1: Revise the notice informing a taxpayer of the proposed reassessment to reflect the current statutory time period in which to file an appeal.

The assessor's notice to taxpayers whose property has been revalued because of a calamity or disaster incorrectly states that the taxpayer has 14 days from the date of notice to appeal the proposed assessment.

Section 170(c) provides that the taxpayer has six months from the date of the reassessment notice to file an appeal. The notice used by the assessor may cause a taxpayer to believe they have missed the deadline for filing an appeal, when they may still have time. Proper notification

under section 170(c) is a statutory requirement that ensures that all parties are informed of their rights.

Assessment Roll Changes

The assessor must complete the local assessment roll and deliver it to the auditor by July 1 of each year. After delivery of the assessment roll to the auditor, if a correction is made that will decrease the amount of the unpaid taxes, the consent of by the board of supervisors is necessary. Specific statutes authorize all changes to the roll, and any roll change must be accompanied by the appropriate statutory reference.

Assessment roll changes fall under two general categories: escape assessments and corrections. An escape assessment is an assessment of property that was not assessed or was underassessed, for any reason, on the original roll. A correction is any type of authorized change to an existing assessment except for an underassessment caused by an error or omission of the assessee.

The following table shows the number of secured and unsecured roll changes processed by the assessor in recent years:

ROLL YEAR	NUMBER OF CHANGES
2003-04	14,678
2002-03	13,103
2001-02	13,920
2000-01	19,659
1999-00	12,219

We reviewed the assessor's roll change practices and procedures as well as a number of roll changes. The assessor's process satisfies the notification requirements of section 534. We found no problems with the assessment roll change program.

Low-Value Property Exemption

Section 155.20 authorizes a county board of supervisors to exempt all real property with a base year value, and personal property with a full value, so low that the total taxes, special assessments, and applicable subventions on the property would be less than the assessment and collection costs if the property were not exempt.

Section 155.20(b)(1) provides that a county board of supervisors shall not exempt property with a total base year value or full value of more than \$5,000, or more than \$50,000 in the case of certain possessory interests. A board of supervisors must adopt a low-value property exemption before the lien date for the fiscal year to which the exemption is to apply. At the option of the board of supervisors, the exemption may continue in effect for succeeding fiscal years.

In Kern County, the board of supervisors concluded that the low-value threshold for cost-effective assessments was \$2,000 for both real and personal property. When a property is determined to qualify for the low-value property exemption, the appraisal record is so noted and the property is not indicated on the assessment roll.

Low-value real property qualifying for the exemption is tracked on the assessor's computer system. When the factored base year value of a previously exempt property exceeds the \$2,000 benchmark, the taxable value is reflected on the assessment roll.

We found no problems with the low-value property exemption program.

Exemptions

In the Kern County Assessor's Office, two fiscal support technicians process all exemptions. The staff refers to an informal set of written procedures, Assessors' Handbook Section 267, *Welfare, Church, and Religious Exemptions*, and documents received in various exemption workshops taught by the BOE for processing guidelines.

Church and Religious Exemptions

The church exemption is authorized by article XIII, section 3(f), of the California Constitution. This constitutional provision, implemented by section 206 of the Revenue and Taxation Code, exempts buildings, the land on which they are situated, and equipment used exclusively for religious worship, when such property is owned or leased by a church. Property that is reasonably and necessarily required for church parking also is exempt, under article XIII, section 4(d), provided that the property is not used for commercial purposes. The church parking exemption is available for owned or leased property meeting the requirements of section 206.1.

Article XIII, section 4(b), authorizes the Legislature to exempt property used exclusively for religious, hospital or charitable purposes and owned or held in trust by a corporation or other entity. The corporation or entity, however, must meet the following requirements: (1) it must be organized and operated for those purposes; (2) it must be non-profit; and (3) no part of its net earnings can inure to the benefit of any private shareholder or individual. The Legislature has implemented this constitutional authorization in section 207 of the Revenue and Taxation Code, which exempts property owned by a church and used exclusively for religious worship and school purposes.

County assessors administer the church and religious exemptions. The church exemption and the church parking exemption require an annual filing of the exemption claim. The religious exemption requires a one-time filing by the claimant, although the assessor annually mails a form to claimants to confirm continuing eligibility for the exemption. Once granted, this exemption remains in effect until terminated or until the property is no longer eligible for the exemption.

The following table summarizes the church exemptions processed in recent years:

ROLL YEAR	NUMBER OF EXEMPTIONS	EXEMPT ASSESSED VALUE
2004-05	199	\$59,524,797
2003-04	201	\$57,099,279
2002-03	205	\$55,694,810
2001-02	196	\$52,020,270
2000-01	200	\$51,690,778

We found that the assessor is careful to allow the church exemption only for worship and related uses, and that there were no problems with the assessor's church exemption program.

The following table summarizes the religious exemptions processed in recent years:

ROLL YEAR	NUMBER OF EXEMPTIONS	EXEMPT ASSESSED VALUE
2004-05	852	\$274,579,937
2003-04	835	\$263,339,767
2002-03	844	\$251,319,164
2001-02	825	\$240,998,131
2000-01	828	\$229,243,288

Our review of the assessor's religious exemption program found that the assessor is very careful to adhere to statutory requirements regarding filing. When claimants fail to return the annual termination notice, the assessor promptly contacts the claimant by telephone to obtain the necessary documentation. If this fails, an appraiser will field inspect the property to verify continued eligibility for the religious exemption.

The assessor maintains an effective religious exemption program.

Welfare Exemption

The welfare exemption from local property taxation is available for property owned and used exclusively for qualifying religious, hospital, scientific, or charitable purposes by organizations formed and operated exclusively for those purposes. Both the organizational and property use requirements must be met for the exemption to be granted.

The BOE and county assessors coadminister the welfare exemption. Effective January 1, 2004, the BOE became responsible for determining whether an organization itself is eligible for the welfare exemption and for issuing *Organizational Clearance Certificates* to qualified nonprofit organizations. And, the assessor became responsible for determining whether the use of a

qualifying organization's property is eligible for exemption and for approving or denying exemption claims.

The assessor may not grant a welfare exemption on an organization's property unless the organization holds a valid *Organizational Clearance Certificate* issued by the BOE. The assessor may, however, deny an exemption claim, based on non-qualifying use of the property, notwithstanding the claimant's *Organizational Clearance Certificate* issued by the BOE.

The following table summarizes welfare exemptions granted in recent years:

ROLL YEAR	NUMBER OF EXEMPTIONS	EXEMPT ASSESSED VALUE
2004-05	1,016	\$691,716,906
2003-04	920	\$665,510,251
2002-03	768	\$658,584,349
2001-02	722	\$599,374,088
2000-01	694	\$569,960,513

We reviewed a variety of welfare exemption claims on file at the assessor's office. Specific property types that we reviewed included:

- Low-income housing and hospitals (partial exemptions);
- Reasonably necessary staff housing, including parsonages; and
- Religious schools.

The assessor maintains well-documented welfare exemption claim records including a permanent file for every organization. The fiscal support technician uses a claim checklist to ensure that all documentation and verification requirements have been met before processing the exemption.

We found no problems with the assessor's welfare exemption program.

Racehorse Administrative Tax

Racehorses domiciled in California are subject to an annual tax in lieu of ad valorem property tax. Sections 5701 through 5790 outline the provisions of this tax. Specific procedures and forms are prescribed by Rules 1045 and 1046. Rule 1045(a)(2) requires the assessor to furnish BOE-prescribed forms to racehorse owners for reporting the in-lieu tax.

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to taxpayers that own or board racehorses in Kern County. As required by Rule 1045(c)(3), the assessor retains the forms received for a minimum of five years.

We found no problems with the racehorse administrative tax program.

Assessment Forms

Government Code section _____ requires the BOE to prescribe the use of all forms for the assessment of property for taxation.⁷ For the 2004 lien date, the BOE prescribed 75 forms for use by county assessors and one form for use by county assessment appeals boards. Generally, the assessor has the option to change the appearance (size, color, etc.) of a prescribed form but cannot modify, add to, or delete from the specific language on a prescribed form. The assessor may also rearrange information on a form provided that the assessor submits such a form to the BOE for review and approval. Assessors may also use locally developed forms to assist them in their assessment duties.

The BOE annually sends three _____ checklists to assessors for (1) property statements, (2) exemption forms, and (3) miscellaneous forms. Assessors are asked to indicate on the checklists which forms they will use in the succeeding assessment year and to return the checklists and any rearranged forms to the BOE by October 15 in the case of property statements and miscellaneous forms and by December 1 in the case of exemption forms. By February 10, assessors are also required to submit to the BOE the final prints (versions) of all BOE-prescribed forms they will use in the following year.

For the 2004 lien date, the Kern _____ Assessor used 65 BOE-prescribed forms. The assessor submitted his checklist, rearranged forms, and final prints to the BOE in a timely manner. Eight forms were rearranged by the assessor and approved by the BOE.

In addition to the BOE-prescribed _____, the assessor uses 47 locally developed forms, form letters, and questionnaires. The assessor has 11 BOE-prescribed forms and 5 locally developed forms on his website. The assessor is in compliance with general forms procedures; however, we found several problems with both the assessor's paper forms and forms on his website.

RECOMMENDATION 2: Revise the assessment forms program by: (1) using only current forms and approved rearranged forms, (2) including only permissible requirements on the cover letter for the annual mineral property statement, and (3) conforming the language of the *Notice of Supplemental Assessment* to the requirements of section 75.31(e).

Use only current forms and approved rearranged forms.

The assessor has six rearranged forms on the office website that were revised after they were submitted to, and approved by, the BOE. In addition, many website forms and two forms used in the office are outdated.

⁷ Also sections 480(b), 480.2(b), 480.4, and Rules 101 and 171.

As previously explained, Government Code section 15606 provides that the BOE shall prescribe and enforce the use of all forms for the assessment of property for taxation. By using unapproved rearranged forms and outdated forms, the assessor is not complying with the statutory provisions pertaining to assessment forms.

Include only permissible requirements on the cover letter for the annual mineral property statement.

In his instructions for the completion of the annual mineral property statement, the assessor states that failure to properly complete, sign, and *collate* the pre-approved or supplied forms and all attachments may result in the assessor refusing to accept the statement pursuant to section 441(g).

Section 441(g) provides that the assessor may refuse to accept any property statement he or she determines to be in error. There is no requirement for the taxpayer to collate his or her statement, and it would be improper for the assessor to refuse a statement that is not collated.

Conform the language of *Notice of Supplemental Assessment* to the requirements of section 75.31(e).

The assessor's *Notice of Supplemental Assessment* does not advise the assessee of the auditor's action when there is a negative supplemental assessment.

If the supplemental assessment is a negative amount, section 75.31(e) requires that the notice advise the assessee that the auditor shall refund a portion of the taxes paid on assessments made on the current roll, or the roll being prepared, or both.

By omitting the required information on the notice, the assessor is failing to inform the taxpayer of a situation where a refund may be due.

ASSESSMENT OF REAL PROPERTY

In Kern County the Realty Division processes all real property assessments. The assessor's program for assessing real property includes the following principal elements:

- Revaluation of properties that have changed ownership.
- Valuation of new construction.
- Annual review of properties that have experienced declines in value.
- Annual reevaluations of certain properties subject to special assessment procedures, such as lands subject to California Land Conservation Act contracts, and taxable government-owned lands.

Unless there is a change in ownership or new construction, article XIII A of the California Constitution provides that the taxable value of real property shall not exceed its 1975 full cash value factored at no more than 2 percent per year for inflation.

Change in Ownership

Section 60 defines change in ownership as a transfer of a present interest in real property, including the beneficial use thereof, the value of which is substantially equal to the value of the fee simple interest. Sections 61 through 69.5 further clarify what is considered a change in ownership and what is excluded from change in ownership for property tax purposes. Section 50 requires the assessor to establish a base year value for real property upon a change in ownership, based on the property's fair market value on the date of change in ownership pursuant to section 110.1.

Discovery and Document Processing

The assessor's primary means of discovering properties that have changed ownership is to review deeds and other recorded documents. Since the assessor is also the recorder, the assessor's computer system is connected to the recorder's system, facilitating the receipt of all recorded documents. The recorder requires that a *Preliminary Change of Ownership Report (PCOR)* accompany documents submitted for recordation that transfer the ownership of real property. A \$20 fee is added to the recording fee when a PCOR is not received.

Title support specialists and technicians analyze PCORs, deeds, and other recorded documents to determine the percentage of ownership transferred and if the events are reappraisable. The documents are tracked in the computer system.

The number of reappraisals generated by recorded changes in ownership over recent years is summarized in the following table:

ROLL YEAR	NUMBER OF REAPPRAISALS
2003-04	57,708
2002-03	56,962
2001-02	49,793
2000-01	22,514
1999-00	22,931

We found the assessor establishes the correct base year value, complies with the presumption in Rule 2 that the sale price reflects the full cash value of the property, and uses reasonable appraisal techniques. He also correctly values partial interest transfers, applies the annual inflation adjustment, and enrolls supplemental assessments.

Parent-Child and Base Year Value Transfer Exclusions

Certain transfers may be excluded from reassessment provided that a claim is timely filed with the assessor and certain other requirements are met. Section 63.1 allows for the exclusion from the change in ownership of property transferred between a parent and child, or from a grandparent to a grandchild when the parent is deceased. Section 69.5 allows qualified homeowners over the age of 55 or disabled to transfer the base year value of their principal residence to a qualifying replacement dwelling.

We reviewed several claims for base year value transfer exclusions processed by the assessor. We found that the claim forms were filed timely and included the required information, and that all required signatures were present. On claim forms for persons over 55 years of age or disabled, the assessor is diligent in verifying property values and transfer dates for both the original and replacement dwellings, and confirming eligibility for the homeowners' exemption. A similar degree of diligence was noted on the parent/child transfer exclusion claims reviewed. Additionally, the assessor contacts taxpayers when more information is necessary.

Improvement Bonds

Improvement bonds are instruments used to finance construction of public improvements, such as sewers, sidewalks, lighting, and water lines that generally enhance the land value of privately owned real property. Land directly benefiting from such improvements is pledged as security for payment of the construction loan. The improvement bond is a lien that runs with the land and binds the owner and all successors in interest in accordance with the 1911 or 1915 Bond Acts.

Section 110(b) provides a rebuttable presumption that the value of improvements financed by the proceeds of an assessment resulting in a lien imposed on the property by a public entity is reflected in the total consideration paid for a property exclusive of the lien amount. The assessor

can overcome this presumption by a preponderance of evidence that all or a portion of the value of those improvements is not reflected in that consideration.

We reviewed several recently transferred properties located in active bond assessment districts and found that the assessor does not add any amount for improvement bonds. The assessor conducted studies that indicate that there is no difference in the sales price of property with or without outstanding bonds.

Legal Entity Ownership Program (LEOP)

Section 64 provides that certain transfers of ownership interests in a legal entity constitute a change in ownership of all real property owned by the entity and its subsidiaries. Rule 462.180 interprets and clarifies section 64, providing examples of transactions that either do or do not constitute a change in entity control and hence either do or do not constitute a corresponding change in ownership of the real property owned by the entity. Discovery of these types of changes in ownership is difficult for assessors because ordinarily there is no recorded notice of the real property transfer.

To help assessors, the BOE's LEOP unit investigates and verifies changes in entity control and legal ownership reported by legal entities, transmitting to each county a listing, with corresponding property schedules, of legal entities that have reported a change in control under section 64(c) or change in ownership under section 64(d). However, many of the acquiring entities do not provide specific information about the real property involved—for example, the county of location, the assessor's parcel number, etc. Because of the limited data provided by many entities, LEOP advises assessors to independently research each entity's property holdings to determine whether all affected parcels have been identified and properly reappraised.

We reviewed a number of properties on the LEOP list for Kern County and found no errors pertaining to identification and change in ownership enrollment. We found the assessor processes LEOP notices properly and timely reappraises all properties that have undergone changes in entity control.

Change in Ownership Statements

When a transfer document is received without a PCOR, the assessor mails Form BOE-502-AH, *Change of Ownership Statement (COS)*, to the new owner. A COS is also sent when there is insufficient or incomplete information on the PCOR. If there is no response after 45 days, a second request is sent.

In our prior survey report, we recommended that the assessor timely apply the penalty for a failure to file a COS, as prescribed in section 482(a). We repeat this recommendation.

RECOMMENDATION 3: Timely apply the penalty for failure to file a change in ownership statement as prescribed in section 482(a).

We found that the assessor does not apply the section 482(a) penalty until 45 days after the second request has been sent, rather than after the first request.

Section 482(a) provides that the penalty applies if, upon written request from the assessor, a required party fails to file the statement within 45 days after the request. Timely application of the section 482(a) penalty is mandatory. Consequently, the assessor is not in compliance with applicable statutes.

New Construction

Section 70 defines newly constructed property, or new construction, as (1) any addition to real property since the last lien date; or (2) any alteration of land or improvements since the last lien date that constitutes a major rehabilitation of the property or converts the property to a different use. Further, section 70 establishes that any rehabilitation, renovation, or modernization that converts an improvement to the substantial equivalent of a new improvement, constitutes a major rehabilitation of the improvement. Section 71 requires the assessor to determine the full cash value of newly constructed real property on each lien date while construction is in progress and on its date of completion and provides that the full cash value of completed new construction becomes the new base year value of the newly constructed property.

Rules 463 and 463.500 clarify the statutory provisions of sections 70 and 71, and Assessors' Handbook Section 502, *Advanced Appraisal*, Chapter 6, provides guidance for the assessment of new construction.

There are several statutory exclusions from what constitutes new construction; sections 70(c), (d), and (e), and sections 73 through 74.7 address these exclusions.

Discovery

Most new construction activity is discovered from a review of building permits. Currently, the assessor receives building permits from 14 permit-issuing agencies: the Kern County Building, Fire, and Health Departments; and the cities of Bakersfield, Arvin, Delano, McFarland, Maricopa, Ridgecrest, Shafter, Taft, Tehachapi, Wasco, and California City. The assessor does not have a formal program for discovery of non-permitted new construction. Other discovery methods used include field inspections, newspaper articles, and declarations on business property statements.

Permit Processing

The assessor does not have a self-reporting program for new construction. Cost information is obtained from building permits and taxpayers. New construction questionnaires are mailed as needed by the appraisal staff.

Most cities send their permits monthly to the assessor in hard copy form. Only the Kern County departments and the City of Bakersfield send permit data electronically. Most permits are accompanied by building plans and all permits received are forwarded to property appraisers for review and valuation. After the permits are reviewed and valued, the records are forwarded to the section senior and the section supervisor for review. After review, the values are keyed into the system and the supplemental notice is generated.

The following table shows the permit workload over recent years:

ROLL YEAR	PERMITS RECEIVED	PERMITS RESULTING IN REVALUATION
2003-04	14,234	4,856
2002-03	13,361	3,285
2001-02	11,751	2,628
2000-01	10,244	2,435
1999-00	11,885	2,504

The assessor follows specific procedures to ensure proper processing of all permits. The processing procedures are thorough and provide for effective retrieval of information upon which an appraiser may make informed decisions.

Valuation

The assessor values new construction by estimating the full value of new construction as of the date of completion. The appraiser determines the completion status of new construction from an on-site inspection and a review of the notice of completion from the building department. Several cost sources are used in valuing new construction, including Assessors' Handbook Section 531, *Residential Building Costs*, the owner's actual cost, and Marshall Valuation Service for commercial and industrial appraisals. All permits are field reviewed unless the proposed work is determined to be maintenance or repairs. Permits that are considered as maintenance or repairs are recorded with no value change.

We reviewed several appraisal records with new construction activity and found no problems with the assessor's program for assessing new construction.

Construction in Progress (CIP)

On each lien date, section 71 requires the assessor to enroll construction in progress at its fair market value. On subsequent lien dates, if the new construction is still incomplete, the assessor must again enroll the construction in progress at its fair market value. This process continues until the new construction is complete, at which time the new construction is assessed at its fair market value upon completion and a base year value is estimated. We found no problems in the valuation of construction in process.

Declines in Value

Section 51 requires the assessor to enroll on the lien date an assessment that is the lesser of a property's factored base year value or its current full cash value, as defined in section 110. Thus, if a property's full cash value falls below its factored base year value on any given lien date, the assessor must enroll that lower value. If, on a subsequent lien date, a property's full cash value

risers above its factored base year value, then the assessor must enroll the factored base year value.

The Kern County Assessor has developed a computer program to assist in the valuing and annual processing of residential properties experiencing declining values. The program analyzes current sales in geographical areas (neighborhoods) to determine whether existing decline-in-value assessments should be changed. This is an effective program for residential properties.

Discovery of value declines in commercial, industrial, residential income-producing, and agricultural properties is accomplished through other means. One such method is by the appraiser's familiarity with his or her assigned geographic area and specialty. In addition, taxpayers' requests for reviews of value and assessment appeals filed also trigger reviews for declines in value.

Appraisal files for properties with decline-in-value assessments are adequately documented. Most contain either a comparable sales listing or an income approach. For those properties that were subject to an assessment appeal, the documentation is more comprehensive.

Each decline-in-value assessment is specially coded to prevent the computer program from applying the annual inflation factor to the prior year's taxable value and to ensure that the assessment will be analyzed for the up-coming lien date. Due to a strengthening of the local real estate market, the number of single family residences with market value lower than the factored base year value (FBYV) has declined between 2002-03 and 2004-05. However, commercial and industrial properties have not experienced the same recovery that single family-residences experienced.

The following table shows the number of decline-in-value assessments for recent years:

ROLL YEAR	PROPERTIES AT LESS THAN FBYV
2004-05	11,415
2003-04	20,951
2002-03	25,034

We found the decline-in-value assessments complete, reasonable, and well supported. The assessor has an effective program for annually reviewing and adjusting real property assessments to reflect declines in value.

Supplemental Assessments

Sections 75 through 75.80 mandate supplemental assessments for changes in ownership and the completion of new construction occurring on or after July 1, 1983. A supplemental assessment is an assessment that reflects the increase or decrease in assessed value resulting from a change in ownership or completion of new construction for the fiscal year. If a change in ownership or completed new construction occurs between January 1 and May 31, two supplemental assessments result from the same event: one for the remainder of the current fiscal year, another for the entire

next fiscal year. Clarification regarding supplemental assessments resulting from the completion of new construction is contained in Rule 463.500.

Processing

The assessor processed approximately 55,000 supplemental assessments for 2003-04 using an automated system. Appraisers value properties subject to changes in ownership or new construction events, and then forward the valuations for data entry. The computer system automatically calculates supplemental assessment amounts and generates notices to be mailed to property owners. The notice provided by the automated system includes all of the information required by section 75.31.

After sending the notices to property owners, the assessor forwards supplemental assessment information to the county auditor.

Enrollment

We examined several new construction and transfer events and found that the assessor processes small value and negative supplemental assessments as required. The assessor correctly makes two supplemental assessments for events occurring on or after January 1 but on or before May 31, and one supplemental assessment for events occurring on or after June 1 but on or before December 31. Additionally, the assessor properly applies the inflation factor for the following lien date when a supplemental assessment event occurs on or after January 1 but on or before May 31.

The assessor prorates supplemental assessments correctly and issues supplemental notices in a timely manner. We examined assessment escapes and found no supplemental assessments processed outside of the statute of limitations set by section 75.11(d). Additionally, the assessor properly issues supplemental assessments for business fixtures, leasehold improvements, manufactured homes, and the unrestricted portion of CLCA properties.

The assessor's supplemental program is accurate and in compliance with all applicable provisions of law with the following exception.

RECOMMENDATION 4: Issue all supplemental assessments according to statutory guidelines.

We found the assessor issues supplemental assessments for taxable government-owned properties when there is a change in ownership.

Section 52(d) and Letters To Assessors 2000/037, *Guidelines for the Assessment of Taxable Government-Owned Properties*, provide that taxable government-owned properties are not subject to supplemental assessment and, therefore, should be enrolled on the lien date following acquisition. The assessor's practice has resulted in overassessments.

We also found that the assessor does not issue supplemental assessments on possessory interests due to the completion of new construction or a change in ownership. Possessory interest

transfers and new construction activity during the year are not identified by an event date, but are enrolled as of the lien date.

Section 75.14 provides that all property subject to the assessment limitations of article XIII A of the California Constitution shall be subject to supplemental assessments. Possessory interests, which are real property, are subject to article XIII A of the California Constitution and, therefore, subject to supplemental assessment. The assessor's practice is contrary to law and has resulted in underassessments.

California Land Conservation Act Property

Pursuant to the California Land Conservation Act (CLCA) of 1965, agricultural preserves may be established by a city or county for the purpose of identifying areas within which the city or county will enter into agricultural preserve contracts with property owners.

Property owners who place their lands under contract agree to restrict the use of such lands to agriculture and other compatible uses; in exchange, the lands are assessed at a restricted value. Lands under contract are valued for property tax purposes by a method that is based upon agricultural income-producing ability (including income derived from compatible uses, e.g., hunting rights and communications facilities). Although such lands must be assessed at the lowest of the restricted value, current market value, or factored base year value, the restricted value typically is the lowest.

Sections 421 through 430.5 prescribe the method of assessment for land subject to agricultural preserve contracts. Assessors' Handbook Section 521, *Assessment of Agricultural and Open-Space Properties* (AH 521), provides BOE-approved guidance for the appraisal of these properties.

For the 2004-05 tax roll, Kern County had approximately 1,570,000 acres encumbered by CLCA contracts and 144,000 acres restricted under the Farmland Security Zone. Acreage in nonrenewal status represented approximately 47,000 acres of the total restricted acreage. The total assessed value for CLCA land and restricted living improvements for 2004-05 was approximately \$1.9 billion.

Most of the rural property in Kern County consists of rangeland, and land with fruit, nut, and vegetable crops. The bulk of the agricultural revenue generated in Kern County is derived from grapes, almonds, milk, citrus, and cotton.

Valuation

The valuation of CLCA property in Kern County is the responsibility of the agriculture crew. The crew uses a computer program to calculate restricted values for CLCA land. The computer program then compares the restricted value, the factored base year value, and the current market value, and automatically enrolls the lowest value. Homesites are valued according to section 428. Pursuant to section 52(a), supplemental assessments are not issued for restricted land and living improvements.

The assessor uses CLCA questionnaires, which are mailed annually, and include compatible use income in the valuation process. There are few CLCA properties within Kern County that have compatible uses but there are some cell tower sites and hunting rights.

The capitalization rate and rents are updated in the program annually. To develop the capitalization rate, the assessor uses a risk rate of ½ percent for grazing, 1 percent for irrigated farmland, and 2 percent for trees and vines. The assessor uses an overall rate of 3 to 5 percent for irrigated farmland, 1 to 2 percent for rolling hills grazing land, and 6 to 8 percent for trees and vines.

We reviewed a number of CLCA appraisal files and found the assessor has an effective and comprehensive CLCA program that is in compliance with all applicable statutes.

Taxable Government-Owned Property

Article XIII, section 3, of the California Constitution exempts from property taxation any property owned by local governments, except as provided in article XIII, section 11. Section 11 provides that land, and improvements thereon, located outside a local government's or local government agency's boundaries are taxable at a restricted value if the property was taxable at the time of acquisition. Improvements that were constructed to replace improvements that were taxable when acquired are also taxable. These lands and taxable improvements are commonly referred to as taxable government-owned properties.

For the 2004-05 assessment roll, Kern County had 275 taxable government-owned properties with a total assessed value of approximately \$12.6 million.

The assessor determines the status of government-owned properties at the time of acquisition by comparing tax-rate area maps to the county's list of government agencies located within each tax-rate area. The residential supervising appraiser values these taxable government-owned properties annually at the lowest of (1) its restricted value, (2) its adjusted base year value, or (3) its current fair market value.

We reviewed a number of appraisal files of taxable government-owned properties. The assessor valued most properties correctly. However, we noted one incorrect assessment procedure.

RECOMMENDATION 5: Establish the base year value for taxable government-owned property according to BOE guidelines.

The assessor's policy has been to establish the base year value of taxable government-owned property at the time of acquisition based on the current market value.

BOE guidelines set forth in LTA 2000/037, *Guidelines for the Assessment of Taxable Government-Owned Properties*, dated June 23, 2000, provide that the base year value for taxable government-owned property acquired after March 1, 1975, is established at either the lower of the current fair market value or the 1967 assessed value multiplied by the appropriate BOE-published factor for the assessment of taxable publicly owned lands as of the date of the change in ownership.

The assessor's practice has resulted in the overassessment of taxable government-owned property.

Taxable Possessory Interests

A taxable possessory interest results from the possession, a right to possession, or a claim to a right to possession of publicly owned real property, in which the possession provides a private benefit to the possessor and is independent, durable, and exclusive of rights held by others. The assessment of a taxable possessory interest in tax-exempt publicly owned property is based on the value of the rights held by the possessor; the value of the rights retained by the public owner is almost always tax exempt.

The assessor's program for discovering possessory interests includes an annual polling of all government entities in the county requesting information on agreements with private parties. Staff appraisers annually contact approximately 25 public agencies by letter or in person to request current information on new or changed tenancies and rents. There are currently 543 taxable possessory interests with a total value of approximately \$124 million, or 0.27 percent of the local assessment roll value for 2004-05.

In our prior survey report, we recommended that the assessor assess all taxable possessory interests at the county fairgrounds and review improvement-only possessory interests for escape assessments. We found the assessor is not reviewing all private uses at the fairgrounds for taxable possessory interests and improvement-only possessory interest assessments have not been reviewed for escape assessments. Therefore, we are repeating these two recommendations.

The assessor is responsible for identifying and valuing taxable possessory interests upon their creation, renewal, or assignment of the lease, and upon the construction of new improvements on the property. We found three additional areas where this program needs improvement.

RECOMMENDATION 6: Improve the possessory interest program by: (1) assessing all taxable possessory interests, (2) reviewing improvement-only possessory interests for escape assessments, (3) reviewing all taxable possessory interests with stated terms of possession for declines in value, (4) deducting expenses from gross income when valuing possessory interests by the income approach, and (5) revaluing taxable possessory interests at the end of the reasonably anticipated term of possession used for their assessment.

Assess all taxable possessory interests.

In our previous two survey reports, we recommended that the assessor review all private uses at the Kern County Fairgrounds for possible possessory interests. Yet, we found no assessments for fairground possessory interests. In addition, we found no possessory interest assessments at the Bakersfield Centennial Garden and Convention Center (Center).

We obtained a list of commercial and food vendors from the Kern County Fair Association and a three-year event log from the Center. We found a number of uses that warrant assessment as taxable possessory interests. Some of the main events held at the Center since its opening in 1998 include professional hockey games, a circus, and an ice show. In addition, the Center has many yearly events with at least a five-year history of use.

Section 107 provides, in part, that independent, durable, and exclusive possession (or right to or claim) of publicly-owned real property is a taxable interest. Failure to assess interests having these characteristics will lead to the escape of taxable property.

Review improvement-only possessory interests for escape assessments.

We found a number of properties with improvement assessments but no land assessments in Kern County. These are hangars at an airport. The airport is subject to a land lease to a private entity that sublets space to hangar owners. The land lease also constitutes a taxable possessory interest and should be assessed in compliance with section 107 and Rules 20, 21, and 29.

Although the improvements were properly assessed, the land, which is owned by a public agency, has escaped assessment.

Review all taxable possessory interests with stated terms of possession for declines in value.

We found that, for lien dates subsequent to the establishment of the base year value, the assessor enrolls the factored base year value until the contract term of possession expires or there is a change in ownership.

Section 51 requires the assessor to assess real property, including taxable possessory interests, at the lesser of the base year value (adjusted annually for inflation by no more than 2 percent) or the current fair market value, taking into consideration any reductions in value due to damage, depreciation, or any other factors causing a decline in value. In determining the current fair market value of a possessory interest with a stated term of possession, Rule 21 provides that the stated term of possession must be used unless there is clear and convincing evidence that the lessor and lessee have agreed to a different term.

Though not required to reappraise all properties each year, the assessor should develop a program to periodically review the assessments of possessory interests with stated terms of possession to ensure that declines in value of taxable possessory interests are consistently recognized. Failing to assess a taxable possessory interest using the stated term of possession may overstate its taxable value.

Deduct expenses from gross income when valuing possessory interests by the income approach.

The assessor does not deduct operating expenses from the income before capitalizing the income stream into a value.

Assessors' Handbook Section 510, *Assessment of Taxable Possessory Interests*, provides that allowed expenses paid by the public owner should be deducted from the estimated economic rent.

A public owner will incur some expenses in managing each possessory interest. In addition, lease terms may require the public owner to pay all or portions of insurance, maintenance, or utilities. By estimating the fair market value without deducting for expenses paid by the lessor, the assessor is overassessing the property.

Revalue taxable possessory interests at the end of the reasonably anticipated term of possession used for their assessment.

We found several possessory interests that the assessor failed to revalue at the end of their reasonably anticipated terms of possession.

Section 61(b) provides that the creation, renewal, extension, or assignment of a taxable possessory interest is a change in ownership for property tax purposes. However, section 61(b)(2) provides that the renewal or extension of a taxable possessory interest during the reasonably anticipated term of possession used to value the interest by the assessor does not result in a change in ownership until the end of that reasonably anticipated term of possession. Under this provision, it is important that the assessor establish a tracking system of the reasonably anticipated term of possession to indicate when a possessory interest has changed ownership and is subject to reappraisal.

Failure to recognize a change in ownership at the end of the reasonably anticipated term of possession used to value the possessory interest may result in underassessments and is contrary to statutory provisions. Implementation of a tracking system that notifies the appraiser when a term of possession expires, and a reappraisal is required, would help alleviate this assessment problem.

Leasehold Improvements

Leasehold improvements are all improvements or additions to leased property that have been made by the tenant or lessee. Such improvements can be secured to the real property or assessed to the lessee on the unsecured assessment roll.

Commercial, industrial, and other types of income-producing properties require regular monitoring by the assessor because, as tenants change over a period of time, they may add and remove improvements that may result in assessable new construction. These changes must, by law, be reflected in the property's assessment if they qualify as new construction.

When real property is reported on Form BOE-571-L, *Business Property Statement (BPS)*, coordination between the Realty and Special Properties Divisions of the assessor's office is important. Both an appraiser in the Realty Division and an auditor-appraiser in the Business Section of the Special Properties Division should examine the reported cost. The units should determine the proper classification of the property to ensure appropriate assessment by each unit and avoid escapes and double assessments. The assessor must determine whether costs are for

repair and maintenance and are, therefore, not assessable, whether additions are properly classified as structural improvements or fixtures, and/or if additions are properly enrolled.

The most common methods of discovery for leasehold improvements are the BPS and building permits. Schedule B of the BPS is specifically used for reporting real property installed by the tenant. Additions or deletions of real property are reported annually using this form.

In Kern County, the business property staff receives and reviews the BPSs. If there are any new costs for structural improvements reported on the Schedule B, the auditor-appraiser informs the Realty Division on the *Informational Transmittal Form*. Property installed by the lessee is generally enrolled on the unsecured roll and assessed to the lessee, while, property installed by the lessor is enrolled on the secured roll and assessed to the lessor.

We reviewed the assessor's foreign improvement, billboard, and cell tower assessments and found no problems. However, in comparing itemized structure costs reported on the BPS to the corresponding real property record, we found evidence of reported structural improvements that were not assessed.

RECOMMENDATION 7: Assess all leasehold improvements.

We found several properties with substantial leasehold improvements that were reported on the BPS but were not assessed. This illustrates a lack of communication between the Realty and Special Properties Divisions of the assessor's office. Although the assessor has developed a form to facilitate that communication, its use appears to be sporadic.

The practice has contributed to the underassessments of real property, resulting in lost tax revenue.

Water Company Property

Taxable water company property may include the property of private water companies, mutual water companies, and some property of government-owned water systems. Each type of water company property presents different assessment issues.

We reviewed water supply sources annually inspected by the Kern County Department of Environmental Health, the California State Department of Health Services' Branch of Drinking Water Field Operations, and the California Public Utilities Commission (CPUC). Among them, we identified 130 mutual water companies and 42 private water companies regulated by the CPUC. We found that the value of mutual water company property was correctly reflected in the assessments of the lots served by the water system and that the assessor correctly values regulated water company property by using historical costs with proper adjustments.

Mineral Property

By statute and case law, mineral properties are taxable as real property. They are subject to the same laws and appraisal methodology as all real property in the state. However, there are three mineral-specific property tax rules that apply to the assessment of mineral properties. They are

Rule 468, Oil and Gas Producing Properties, Rule 469, Mining Properties, and Rule 473, Geothermal Properties. These rules are interpretations of existing statutes and case law with respect to the assessment of mineral properties, and are specific to mineral properties only.

Kern County is rich in mineral deposits and is a significant producer of minerals in the state. The mineral property value for the county is \$12,463,877,331. Mineral property represents almost 28 percent of the county's local assessment roll. This type of property is appraised by the assessor's Natural Resources Section.

Kern County is the largest producer of petroleum in the state, accounting for 77 percent of the state's production. The county also produces clay, shale, limestone, gold, silica, decorative rock, sand, and gravel. The country's largest Borax mining facility is located in Kern County.

Kern County has a large number of power-producing facilities that are locally assessed. Many of these are cogeneration plants associated with various petroleum-producing properties. There are also wind generation installations. If the cogeneration facilities are wholly owned by the petroleum property owner and do not provide steam to petroleum facilities owned by unrelated parties, the cogeneration installation is assessed as part of the petroleum property. Otherwise the cogeneration facility is assessed as an independent property.

As the number one producer of petroleum in California, the assessor's Natural Resources Section typically sets the standard with respect to petroleum appraisals. Parcels are assigned to appraisers on a geographic basis. Many of the appraisers in this Section have been working with petroleum and other complex properties for a number of years. The appraisers look at the extended futures markets and poll market participants about their expectations for prices, which is the proper methodology for developing accurate market value property appraisals.

In our prior survey report, we recommended the assessor revise the valuation method for non-producing petroleum property, properly account for abandonment costs in the cash flow analysis of petroleum-producing property, and develop capitalization rates for cogeneration facilities independent of the primary use of the associated property. The assessor has not implemented these recommendations and they are repeated here along with one additional recommendation.

RECOMMENDATION 8: Revise the mineral property assessment program by:
(1) consistently valuing non-producing and marginal petroleum properties, (2) properly accounting for abandonment expenses in the cash flow analysis, (3) developing capitalization rates for cogeneration facilities independent of the primary use of the associated property, and (4) appraising mining property as an appraisal unit for the purpose of measuring declines in value.

Consistently value non-producing petroleum properties.

The assessor inconsistently values non-producing or marginal mineral rights on a per well basis, with no consideration for properties with a higher or lower density of wells per acre. The

assessor relies on an estimate of market value that is calculated on a per-acre basis but applies it to each property on a per-well basis. The assessor assumes a lease rent of \$10.00 per acre on a ten-acre well site, discounted at a rate of 10 percent to arrive at the minimum value of \$1,000 per well.

By valuing the mineral rights on a per well basis, properties with a greater well density are valued higher than a similar size property with a lower well density. For example, a ten-acre well site with four wells would be valued, using the assessor's methodology, at \$4,000 (four wells @ \$1,000 each). However, if the valuation was done on a per ten-acre well site basis, the value would be \$1,000. The assessor should apply the value to each property on the same basis that it is estimated.

The discount rates for mineral-producing properties used by the assessor range from 12-16 percent. Discount rates reflect perceived risk. Non-producing properties are perceived by the industry to have a higher risk. Therefore, the discount rate used for non-producing properties should reflect a higher rate than the discount rates used for producing properties. The discount rate of 10 percent used by the assessor for non-producing properties suggests that non-producing properties are a lower risk than producing properties. Additionally, a higher discount rate would make the analysis more consistent with published county guidelines for rate selection.

Properly account for abandonment expenses in the cash flow analysis.

The assessor defers abandonment expenses up to three years after the end of production.

Assessors' Handbook Section 566, *Assessment of Petroleum Properties*, recommends that abandonment expenses be included immediately after the end of economic production or as an annual expense to a sinking fund. Abandonment expenses should be immediately recognized to avoid the assumption that abandonment expenses will be available from other sources.

Deferring abandonment expenses beyond the economic life of the property will result in overassessments. The magnitude of this effect depends upon the length of time until abandonment and the amount of the expense.

Develop capitalization rates for cogeneration facilities independent of the primary use of the associated property.

The assessor's procedures manual for cogeneration facilities provides that the discount rate used for facilities assessed as part of an oil field is the same as the one used for the field; however, the manual also states that for independently owned and operated facilities the discount rate should range from 13-17 percent.

The risks associated with electricity production are unique and separate from those associated with the production of oil and gas. The assessor's procedures manual raises an equalization problem. In essence, all the facilities share the same risks of generating electricity and steam. However, for cogeneration facilities owned by petroleum companies, the assessor's manual directs the substitution of the petroleum risk rate for the cogeneration risk rate.

Computerized cash flow analyses make the application of different discount rates to different components of an income stream easy. Discounted cash flows should be evaluated using rates similar to the returns that investors in the cogeneration or petroleum industries would expect. Factors affecting the price of electricity are quite different than those affecting the price of petroleum. Income generated from the sale of electricity should be discounted at the same rate, whether it is for a plant whose sole purpose is to sell directly to the grid or if the electricity generated is incidental to the generation of steam for enhanced recovery or processing of food.

Appraise mining property as an appraisal unit for the purpose of measuring declines in value.

The assessor uses the royalty method to estimate the value of mineral rights. For the value estimates of fixtures and improvements, the assessor uses the cost approach or other appropriate methods. The assessor does not combine the value of mineral rights and improvements before determining whether to enroll the adjusted base year value or the current market value for the mineral rights.

Rule 469(e)(2)(C) provides that declines in value must be recognized when the market value of the appraisal unit (i.e., land, improvements including fixtures, and reserves) is less than the current adjusted base year value of the same unit, except for leach pads, tailings facilities, or settling ponds. Thus, the value of the mining property components should be combined before any analysis of current market value versus factored base year value is made.

Pipeline Rights-of-Way

Intercounty pipeline rights-of-way were assessed by the BOE from approximately 1982 until 1993, when an appellate court ruled that such assessments were outside the BOE's constitutional authority.⁸ The court ruled that while the pipelines themselves are properly assessed by the BOE, the right-of-way through which the pipelines run must be locally assessed. Subsequent to this court ruling, the Legislature added sections 401.8 through 401.12, governing the valuation of intercounty pipeline lands and rights-of-way.

Kern County has 40 pipeline right-of-way assessments on the local roll with a total assessed value of \$39,371,687. All the pipeline rights-of-way are of low and transitional density and are valued by one auditor-appraiser.

The assessor maintains a separate base year value for each separate right-of-way interest, but assesses the rights-of-way to a single countywide parcel according to section 401.8(a). We found that all pipeline rights-of-way in the county are being valued in accordance with the provisions of sections 401.8 through 401.12.

⁸ *Southern Pacific Pipe Lines Inc. v. State Board of Equalization* (1993) 14 Cal.App.4th 42.

ASSESSMENT OF PERSONAL PROPERTY AND FIXTURES

The assessor's program for assessing personal property and fixtures includes the following major elements:

- Discovery and classification of taxable personal property and fixtures.
- Mailing and processing of annual property statements and questionnaires.
- Annual revaluation of taxable personal property and fixtures.
- Auditing taxpayers whose assessments are based on information provided in property statements.

Audit Program

A comprehensive audit program is essential to the successful administration of any tax program that relies on information supplied by taxpayers. A good audit program discourages deliberate underreporting, helps educate those property owners who unintentionally misreport, and provides the assessor with additional information to make fair and accurate assessments.

The Kern County Assessor's Office performs out-of-county audits, as well as out-of-state audits, using existing audit staff. Additionally, they subscribe to California Counties Cooperative Audit Service Exchange (CCCASE). They complete audits of locally sited taxpayers for other California counties and, occasionally, contract with other counties to complete audits of remotely sited taxpayers. The supervising auditor-appraiser reviews all audits and addresses pertinent issues with the appropriate auditor-appraiser before finalizing an audit.

The following table shows the total number of audits completed over recent years:

DESCRIPTION	ROLL YEAR 2004-05	ROLL YEAR 2003-04	ROLL YEAR 2002-03	ROLL YEAR 2001-02	ROLL YEAR 2000-01
Audits Scheduled					
Mandatory	192	207	155	184	168
Nonmandatory	54	22	48	50	38
Total Audits Scheduled	246	229	203	234	206
Unfinished From Prior Year	0	14	1	0	6
Total Audit Workload	246	243	204	234	212
Audits Completed					
Mandatory	192	219	144	183	174
Nonmandatory	54	24	46	50	38
Total Audits Completed	246	243	190	233	212
Mandatory Audits Carried Forward	0	0	14	1	0

The findings of all the completed audits shown above, both mandatory and nonmandatory, expressed as full cash value, are summarized in the following table:

ROLL YEAR	ESCAPES	REFUNDS	NET CHANGE
2003-04	\$109,387,930	\$51,377,195	\$58,010,735
2002-03	\$127,651,105	\$84,310,940	\$43,340,165
2001-02	\$128,129,687	\$84,516,624	\$43,613,063
2000-01	\$78,450,307	\$78,059,758	\$390,549
1999-00	\$302,722,817	\$259,944,305	\$48,778,512

Mandatory Audits

Pursuant to section 469, audits are mandatory for taxpayers reporting business tangible personal property and trade fixtures valued at \$400,000 or more.

The total mandatory audit workload for Kern County is presently 750 or an average of about 187 per year over a four-year period.

We reviewed a number of completed mandatory audits. The audit files were organized, comprehensive, and addressed issues particular to the taxpayer. Additionally, taxpayers were properly notified of audit findings and appeal rights.

Business Property Statement Program

Section 441 requires each person owning taxable personal property (other than a manufactured home) having an aggregate cost of \$100,000 or more to annually file a property statement with the assessor; other persons must file a property statement if requested by the assessor. Property statements form the backbone of the business property assessment program. Several variants of the property statement address a variety of property types, including commercial, industrial, and agricultural property, vessels, and certificated aircraft.

The business property statements processed for the roll year 2004-05 are shown in the table below:

	SECURED		UNSECURED		TOTAL	
CATEGORY	NO.	ASSESSED VALUE	NO.	ASSESSED VALUE	NO.	ASSESSED VALUE
Commercial	1,674	\$285,173,948	8,364	\$593,257,060	10,038	\$878,431,008
Industrial	443	\$1,084,192,504	1,940	\$875,817,548	2,383	\$1,960,010,052
Agricultural	524	\$189,417,507	482	\$127,002,386	1,006	\$316,419,893
Total	2,641	\$1,558,783,959	10,786	\$1,596,076,994	13,427	\$3,154,860,953

The auditor-appraisers in the Kern County Assessor's Office carry out most business property statement processing functions under the direct control of the supervising auditor-appraiser. The assessor requires all business property to be reported, regardless of the amount.

We found that staff checked for completeness, changes in control/ownership, authorized signatures, full disclosures of property based on prior year's statement, and leased equipment disclosures when processing property statements. Staff also applied valuation factors and service lives consistent with prior year's appraisals and office policy as detailed in the Business Section's *Policies and Procedures Manual*.

Taxpayer self-reporting is the principal means of discovering assessable property. Other means of discovering assessable business property include field canvassing, reviewing fictitious business name filings, newspaper articles and advertisements, city and county business licenses, referrals from other counties, and BOE notifications. We found the assessor employs effective and efficient methods to discover taxable business and personal property.

The Kern County Assessor uses a direct billing program. This program is used to efficiently process the assessment of qualified lower-valued business accounts without annual business property statements. It results in a reduction of paperwork for taxpayers and the assessor's office, thereby increasing time available for auditor-appraisers to perform other duties.

The accounts that are direct-billed are generally stable and less than \$50,000 in full cash value of reportable business property. Every four years, the assessor sends a business property statement to direct-billed taxpayers to determine if there have been any substantial changes of business property, including increased or decreased amounts of equipment, sale of business, change in

ownership, or change in location. If the account is determined to no longer be suitable for direct billing, the account is converted back to a regular annual-filing account. If a business property statement is requested, but not returned, the assessor contacts the taxpayer in an effort to secure the requested information and the taxpayer is dropped from the direct billing program.

Our review of the assessor's direct billing program indicates that the assessor effectively accomplishes the goals of the program.

Business Equipment Valuation

Commercial, Industrial, and Agricultural Equipment

Assessors value most machinery and equipment using business property value factors. Value factors are derived by combining price index factors (trend factors) with percent good factors. A value indicator is obtained by multiplying a property's historical (acquisition) cost by an appropriate value factor.

Section 401.5 provides that the BOE shall issue information that promotes uniformity in appraisal practices and assessed values. Pursuant to that mandate, the BOE annually publishes Assessors' Handbook Section 581, *Equipment Index and Percent Good Factors* (AH 581).

The equipment index factors measure the annual trended value of goods (normally upward trends) over their service lives. The percent good factors are intended to reflect the average annual loss in value that commercial or industrial equipment will suffer over its service life. The factors are based on averages and represent a reasonable estimate of annual changes for the majority of business machinery and equipment.

The assessor combines the equipment index factor and the percent good factor into one factor (valuation factor). These valuation factors are integrated into the assessor's computer system. We found that the assessor has adopted the BOE factors and correctly applies them in valuing computer equipment. However, we make one recommendation for improvement in the valuation of older equipment.

RECOMMENDATION 9: Use the Assessors' Handbook Section 581, as intended, when valuing older equipment.

For older machinery and equipment, the assessor did not follow the guidelines in the AH 581 to modify the printed index factor to establish a maximum index factor. The recommended maximum price index factor is based on the factor associated with the year in which the equipment reaches 125 percent of the equipment's estimated useful service life. By not using maximum price index factors in the formulation of combined valuation factors, the assessor is overstating the valuation factor used to value machinery and equipment.

Leased Equipment

The Business Section is responsible for the discovery, valuation, and assessment of leased equipment. This type of property is one of the more difficult to assess correctly. Common

problems include difficulty in establishing taxability and taxable situs, reporting errors by lessees and lessors, valuation (whether the value of the equipment should be the lessor's cost or the cost for the consumer to purchase), and double or escape assessments resulting from lessor and lessee reporting. These issues are discussed in detail in Assessors' Handbook Section 504, *Assessment of Personal Property and Fixtures*.

When property is leased, both lessors and lessees should report such property on their annual property statement. At the end of such a lease, the lessee may acquire the equipment or return it to the lessor. When a lessee obtains ownership and retains possession of equipment at the end of the lease, the assessor should confirm that the lessee reports the property. A crosscheck of information reported by the lessor and the lessee verifies the accuracy of the reported information.

We reviewed the assessor's procedures for assessing leased equipment in Kern County. We found that leases are correctly distinguished from conditional sales contracts and that the assessor does a good job in the discovery, processing, tracking, valuation, assessee determination, and coordination of leased equipment.

Manufactured Homes

A "manufactured home" is defined in Health and Safety Code sections 18007 and 18008, and statutes prescribing the method of assessing manufactured homes are contained in sections 5800 through 5842. A manufactured home is subject to local property taxation if sold new on or after July 1, 1980, or if its owner requests conversion from the vehicle license fee to local property taxation. Manufactured homes should be classified as personal property and enrolled on the secured roll.

For the 2003-04 assessment roll, there were 20,375 manufactured homes enrolled at a total assessed value of \$564,393,841. The table below presents the assessor's manufactured home statistics over recent years:

ROLL YEAR	NUMBER OF MANUFACTURED HOMES	ASSESSED VALUES
2003-04	20,375	\$564,393,841
2002-03	20,109	\$541,805,362
2001-02	19,877	\$522,237,891
2000-01	19,655	\$510,081,837
1999-00	19,383	\$501,736,248

The assessor is notified of assessable manufactured homes by the California Department of Housing and Community Development, dealer reports of sale, and building permits. Once the information is received, the appropriate data are entered into the computer system. If the manufactured home is already enrolled, the appraisal records are forwarded to the appraisal staff

for review. If the manufactured home has not been enrolled, a new appraisal record is created and forwarded to an appraiser for a field check, inventory, and valuation.

We found that the assessor has an effective assessment program for manufactured homes.

Aircraft

General Aircraft

General aircraft are privately owned aircraft that are used for pleasure or business but that are not authorized to carry passengers, mail, or freight on a commercial basis (general aircraft contrast with certificated aircraft, discussed below). Section 5363 requires the assessor to determine the market value of all aircraft according to standards and guidelines prescribed by the BOE. Section 5364 requires the BOE to establish such standards. On January 10, 1997, the BOE approved the *Aircraft Bluebook-Price Digest (Bluebook)* as the primary guide for valuing aircraft, with the *Vref Aircraft Value Reference (Vref)* as an alternative guide for aircraft not listed in the *Bluebook*.

The table below presents the assessor's aircraft assessment workload over recent years:

ROLL YEAR	NO. OF AIRCRAFT	ASSESSED VALUES
2004-05	951	\$89,379,920
2003-04	929	\$86,867,200
2002-03	936	\$79,394,650
2001-02	917	\$79,096,410
2000-01	932	\$95,517,082

An auditor-appraiser III is responsible for valuing general aircraft. An aircraft property statement is mailed annually to the known owner of each aircraft in the county. Upon receipt of the aircraft property statement, the auditor-appraiser incorporates adjustments to the indicated book value for sales tax, overall condition of the aircraft, additional or special equipment, airframe hours, and engine hours since last major overhaul to determine a market value estimate. The values of newer aircraft are most affected by the presence or lack of optional equipment while the values of older aircraft are influenced more by the condition of the aircraft. Field situs checks are made on a case by case basis according to taxpayer claims of deferred maintenance, airworthiness, etc.

We found the assessor's procedures for the assessment of general aircraft to be correctly administered and the estimates of value to be properly calculated.

Certificated Aircraft

Certificated aircraft are aircraft operated by air carriers (including air taxis that are operated in scheduled air taxi operation). Unlike general aircraft, which are normally assessed at a rate of 100 percent at the place where they are "habitually located" on the lien date, the assessments of

certificated aircraft are allocated among taxing jurisdictions based upon ground and flight time and the number of arrivals and departures during a representative period (the period is designated by the BOE). In 2004, when fieldwork for this survey was performed, certificated aircraft were to be assessed in accordance with methods described in section 401.15.

Several airlines fly in and out of Kern County. The auditor-appraiser in charge of aircraft predicates his appraisals of certificated aircraft on the audited costs of the business property statements of the airlines. The auditor-appraiser then applies the percentage of time the aircraft was situated in Kern County based on a one week sample, ground time and air time, to the airline's total audited fleet estimate of value, to derive a pro rata estimate of the certificated aircraft value.

We reviewed the certificated aircraft appraisals and audits and found the procedures to be correctly administered and the pro rata estimates of values to be properly calculated.

Historical Aircraft

Aircraft of historical significance can be exempted from taxation if they meet certain requirements. Section 220.5 defines "aircraft of historical significance" as (1) an aircraft that is an original, restored, or replica of a heavier than air, powered aircraft 35 years or older; or (2) any aircraft of a type or model of which there are fewer than five such aircraft known to exist worldwide.

The historical aircraft exemption is not automatic. Each year, the owner of a historical aircraft must submit an affidavit on or before 5:00 p.m., February 15, paying a filing fee of \$35 upon the initial application for exemption. Along with these requirements, aircraft of historical significance are exempt only if the following conditions are met: (1) the assessee is an individual owner who does not hold the aircraft primarily for purposes of sale, (2) the assessee does not use the aircraft for commercial purposes or general transportation, and, (3) the aircraft was available for display to the public at least 12 days during the 12-month period immediately preceding the lien date for the year for which exemption is claimed.

For the 2004-05 assessment roll, the assessor granted exemptions to 61 qualifying historical aircraft. We reviewed the declarations of historical aircraft claimants and found no problems.

Vessels

Assessors must annually appraise all vessels at market value. The primary sources used for the discovery of assessable vessels include Department of Motor Vehicles (DMV) reports, referrals from other counties, and information provided by the vessel owners themselves.

The assessor's Business Section assessed about 4,500 vessels on the 2004-05 assessment roll with a total assessed value of over \$26 million. One auditor-appraiser and one fiscal support technician process vessel assessments. The auditor-appraiser handles all appraisal duties, while the fiscal support technician handles all non-appraisal duties.

The value guides used by the assessor include the *Anderson and Bugg Outboard Service* valuation guide and the *National Automobile Dealers Association Marine Appraisal Guide*. Occasionally, additional market data are obtained from the Internet.

The following table shows the assessor's vessel workload statistics over recent years:

ROLL YEAR	NO. OF VESSELS	ASSESSED VALUES
2004-05	4,495	\$37,897,828
2003-04	4,249	\$27,887,485
2002-03	3,883	\$30,873,205
2001-02	3,742	\$28,427,100
2000-01	3,461	\$24,985,700

We found the assessor's vessel assessment program complies with all statutory requirements.

Animals

The California Constitution mandates that all property is taxable unless specifically exempted by the Constitution, the laws of the United States, or, in the case of personal property, by act of the Legislature. Most animals are exempt from taxation. Pets are exempted under section 224. Many animals that are considered business inventory are exempted by sections 129 and 219, and by Rule 133.

Taxable animals in Kern County consist principally of horses held for breeding, show, and rodeos. Discovery methods for assessable animals include intercounty communications of transfers, newspaper articles and advertisements, telephone yellow pages, business directories, assessable animals reported on Form BOE-571-F, and audits of agricultural property.

Most animals are reported on Form BOE-571-F, *Agricultural Property Statement*. Taxable animals include those that are held or used in connection with the owner's business, trade, or profession; those used to produce offspring for sale at a net profit; and those with proficiency that have gained substantial monetary or other awards.

Based on our review of several agricultural statements, the assessor properly discovers, identifies, and appraises assessable animals. The discovery program has been broadened to include beehives despite the fact that bees are exempt. Overall, we found the animal assessment program to be effective and well administered.

APPENDIXES

A. County Property Tax Division Survey Group

Kern County

Chief, County Property Tax Division

Mickie Stuckey

Survey Program Director:

Arnold Fong

Principal Property Appraiser

Survey Team Supervisor:

Bob Reinhard

Supervising Property Appraiser

Survey Team Leader:

James Lovett

Senior Specialist Property Appraiser

Survey Team:

Jim McCarthy

Senior Mining and Petroleum Appraisal Engineer

Zella Cunningham

Associate Property Appraiser

Robert Donay

Associate Property Appraiser

Nick Winters

Associate Property Appraiser

Lloyd B. Allred

Associate Property Auditor-Appraiser

Ancil Aydelott

Associate Property Auditor-Appraiser

B. Relevant Statutes and Regulations

Government Code

15640. Survey by board of county assessment procedures.

- (a) The State Board of Equalization shall make surveys in each county and city and county to determine the adequacy of the procedures and practices employed by the county assessor in the valuation of property for the purposes of taxation and in the performance generally of the duties enjoined upon him or her.
- (b) The surveys shall include a review of the practices of the assessor with respect to uniformity of treatment of all classes of property to ensure that all classes are treated equitably, and that no class receives a systematic overvaluation or undervaluation as compared to other classes of property in the county or city and county.
- (c) The surveys may include a sampling of assessments from the local assessment rolls. Any sampling conducted pursuant to subdivision (b) of Section 15643 shall be sufficient in size and dispersion to insure an adequate representation therein of the several classes of property throughout the county.
- (d) In addition, the board may periodically conduct statewide surveys limited in scope to specific topics, issues, or problems requiring immediate attention.
- (e) The board's duly authorized representatives shall, for purposes of these surveys, have access to, and may make copies of, all records, public or otherwise, maintained in the office of any county assessor.
- (f) The board shall develop procedures to carry out its duties under this section after consultation with the California Assessors' Association. The board shall also provide a right to each county assessor to appeal to the board appraisals made within his or her county where differences have not been resolved before completion of a field review and shall adopt procedures to implement the appeal process.

15641. Audit of Records; Appraisal Data Not Public.

In order to verify the information furnished to the assessor of the county, the board may audit the original books of account, wherever located; of any person owning, claiming, possessing or controlling property included in a survey conducted pursuant to this chapter when the property is of a type for which accounting records are useful sources of appraisal data.

No appraisal data relating to individual properties obtained for the purposes of any survey under this chapter shall be made public, and no state or local officer or employee thereof gaining knowledge thereof in any action taken under this chapter shall make any disclosure with respect thereto except as that may be required for the purposes of this chapter. Except as specifically provided herein, any appraisal data may be disclosed by the board to any assessor, or by the board or the assessor to the assessee of the property to which the data relate.

The board shall permit an assessee of property to inspect, at the appropriate office of the board, any information and records relating to an appraisal of his or her property, including "market data" as defined in Section 408. However, no information or records, other than "market data," which relate to the property or business affairs of a person other than the assessee shall be disclosed.

Nothing in this section shall be construed as preventing examination of that data by law enforcement agencies, grand juries, boards of supervisors, or their duly authorized agents, employees, or representatives conducting an investigation of an assessor's office pursuant to Section 25303, and other duly authorized legislative or administrative bodies of the state pursuant to their authorization to examine that data.

15642. Research by board employees.

The board shall send members of its staff to the several counties and cities and counties of the state for the purpose of conducting that research it deems essential for the completion of a survey report pursuant to Section 15640 with respect to each county and city and county. The survey report shall show the volume of assessing work to be done as measured by the various types of property to be assessed and the number of individual assessments to be made, the responsibilities devolving upon the county assessor, and the extent to which assessment practices are consistent with or differ from state law and regulations. The report may also show the county assessor's requirements for maps, records, and other equipment and supplies essential to the adequate performance of his or her duties, the number and classification of personnel needed by him or her for the adequate conduct of his or her office, and the fiscal outlay required to secure for that office sufficient funds to ensure the proper performance of its duties.

15643. When surveys to be made.

- (a) The board shall proceed with the surveys of the assessment procedures and practices in the several counties and cities and counties as rapidly as feasible, and shall repeat or supplement each survey at least once in five years.
- (b) The surveys of the 10 largest counties and cities and counties shall include a sampling of assessments on the local assessment rolls as described in Section 15640. In addition, the board shall each year, in accordance with procedures established by the board by regulation, select at random at least three of the remaining counties or cities and counties, and conduct a sample of assessments on the local assessment roll in those counties. If the board finds that a county or city and county has "significant assessment problems," as provided in Section 75.60 of the Revenue and Taxation Code, a sample of assessments will be conducted in that county or city and county in lieu of a county or city and county selected at random. The 10 largest counties and cities and counties shall be determined based upon the total value of locally assessed property located in the counties and cities and counties on the lien date that falls within the calendar year of 1995 and every fifth calendar year thereafter.
- (c) The statewide surveys which are limited in scope to specific topics, issues, or problems may be conducted whenever the board determines that a need exists to conduct a survey.
- (d) When requested by the legislative body or the assessor of any county or city and county to perform a survey not otherwise scheduled, the board may enter into a contract with the requesting local agency to conduct that survey. The contract may provide for a board sampling of assessments on the local roll. The amount of the contracts shall not be less than the cost to the board, and shall be subject to regulations approved by the Director of General Services.

15644. Recommendations by board.

The surveys shall incorporate reviews of existing assessment procedures and practices as well as recommendations for their improvement in conformity with the information developed in the surveys as to what is required to afford the most efficient assessment of property for tax purposes in the counties or cities and counties concerned.

15645. Survey report; final survey report; assessor's report.

- (a) Upon completion of a survey of the procedures and practices of a county assessor, the board shall prepare a written survey report setting forth its findings and recommendations and transmit a copy to the

assessor. In addition the board may file with the assessor a confidential report containing matters relating to personnel. Before preparing its written survey report, the board shall meet with the assessor to discuss and confer on those matters which may be included in the written survey report.

(b) Within 30 days after receiving a copy of the survey report, the assessor may file with the board a written response to the findings and recommendations in the survey report. The board may, for good cause, extend the period for filing the response.

(c) The survey report, together with the assessor's response, if any, and the board's comments, if any, shall constitute the final survey report. The final survey report shall be issued by the board within two years after the date the board began the survey. Within a year after receiving a copy of the final survey report, and annually thereafter, no later than the date on which the initial report was issued by the board and until all issues are resolved, the assessor shall file with the board of supervisors a report, indicating the manner in which the assessor has implemented, intends to implement, or the reasons for not implementing the recommendations of the survey report, with copies of that response being sent to the Governor, the Attorney General, the State Board of Equalization, the Senate and Assembly and to the grand juries and assessment appeals boards of the counties to which they relate.

15646. Copies of final survey reports to be filed with local officials.

Copies of final survey reports shall be filed with the Governor, Attorney General, and with the assessors, the boards of supervisors, the grand juries and assessment appeals boards of the counties to which they relate, and to other assessors of the counties unless one of these assessors notifies the State Board of Equalization to the contrary and, on the opening day of each regular session, with the Senate and Assembly.

Revenue and Taxation Code

75.60. Allocation for administration.

(a) Notwithstanding any other provision of law, the board of supervisors of an eligible county or city and county, upon the adoption of a method identifying the actual administrative costs associated with the supplemental assessment roll, may direct the county auditor to allocate to the county or city and county, prior to the allocation of property tax revenues pursuant to Chapter 6 (commencing with Section 95) and prior to the allocation made pursuant to Section 75.70, an amount equal to the actual administrative costs, but not to exceed 5 percent of the revenues that have been collected on or after January 1, 1987, due to the assessments under this chapter. Those revenues shall be used solely for the purpose of administration of this chapter, regardless of the date those costs are incurred.

(b) For purposes of this section:

- (1) "Actual administrative costs" includes only those direct costs for administration, data processing, collection, and appeal that are incurred by county auditors, assessors, and tax collectors. "Actual administrative costs" also includes those indirect costs for administration, data processing, collections, and appeal that are incurred by county auditors, assessors, and tax collectors and are allowed by state and federal audit standards pursuant to the A-87 Cost Allocation Program.
- (2) "Eligible county or city and county" means a county or city and county that has been certified by the State Board of Equalization as an eligible county or city and county. The State Board of Equalization shall certify a county or city and county as an eligible county or city and county only if both of the following are determined to exist:
 - (A) The average assessment level in the county or city and county is at least 95 percent of the assessment level required by statute, as determined by the board's most recent survey of that county or city and county performed pursuant to Section 15640 of the Government Code.
 - (B) For any survey of a county assessment roll for the 1996-97 fiscal year and each fiscal year thereafter, the sum of the absolute values of the differences from the statutorily required assessment level described in subparagraph (A) does not exceed 7.5 percent of the total amount of the county's or city and county's statutorily required assessed value, as determined pursuant to the board's survey described in subparagraph (A).
- (3) Each certification of a county or city and county shall be valid only until the next survey made by the board. If a county or city and county has been certified following a survey that includes a sampling of assessments, the board may continue to certify that county or city and county following a survey that does not include sampling if the board finds in the survey conducted without sampling that there are no significant assessment problems in the county or city and county. The board shall, by regulation, define "significant assessment problems" for purposes of this section, and that definition shall include objective standards to measure performance. If the board finds in the survey conducted without sampling that significant assessment problems exist, the board shall conduct a sampling of assessments in that county or city and county to determine if it is an eligible county or city and county. If a county or city and county is not certified by the board, it may request a new survey in advance of the regularly scheduled survey, provided that it agrees to pay for the cost of the survey.

Title 18, California Code of Regulations

Rule 370. Random selection of counties for representative sampling.

- (a) **SURVEY CYCLE.** The board shall select at random at least three counties from among all except the 10 largest counties and cities and counties for a representative sampling of assessments in accordance with the procedures contained herein. Counties eligible for random selection will be distributed as equally as possible in a five-year rotation commencing with the local assessment roll for the 1997–98 fiscal year.
- (b) **RANDOM SELECTION FOR ASSESSMENT SAMPLING.** The three counties selected at random will be drawn from the group of counties scheduled in that year for surveys of assessment practices. The scheduled counties will be ranked according to the size of their local assessment rolls for the year prior to the sampling.
- (1) If no county has been selected for an assessment sampling on the basis of significant assessment problems as provided in subdivision (c), the counties eligible in that year for random selection will be divided into three groups (small, medium, and large), such that each county has an equal chance of being selected. One county will be selected at random by the board from each of these groups. The board may randomly select an additional county or counties to be included in any survey cycle year. The selection will be done by lot, with a representative of the California Assessors' Association witnessing the selection process.
 - (2) If one or more counties are scheduled for an assessment sampling in that year because they were found to have significant assessment problems, the counties eligible for random selection will be divided into the same number of groups as there are counties to be randomly selected, such that each county has an equal chance of being selected. For example, if one county is to be sampled because it was found to have significant assessment problems, only two counties will then be randomly selected and the pool of eligible counties will be divided into two groups. If two counties are to be sampled because they were found to have significant assessment problems, only one county will be randomly selected and all counties eligible in that year for random selection will be pooled into one group.
 - (3) Once random selection has been made, neither the counties selected for an assessment sampling nor the remaining counties in the group for that fiscal year shall again become eligible for random selection until the next fiscal year in which such counties are scheduled for an assessment practices survey, as determined by the five-year rotation. At that time, both the counties selected and the remaining counties in that group shall again be eligible for random selection.
- (c) **ASSESSMENT SAMPLING OF COUNTIES WITH SIGNIFICANT ASSESSMENT PROBLEMS.** If the board finds during the course of an assessment practices survey that a county has significant assessment problems as defined in Rule 371, the board shall conduct a sampling of assessments in that county in lieu of conducting a sampling in a county selected at random.
- (d) **ADDITIONAL SURVEYS.** This regulation shall not be construed to prohibit the Board from conducting additional surveys, samples, or other investigations of any county assessor's office.

Rule 371. Significant assessment problems.

- (a) For purposes of Revenue and Taxation Code Section 75.60 and Government Code Section 15643, "significant assessment problems" means procedure(s) in one or more areas of an assessor's assessment

operation, which alone or in combination, have been found by the Board to indicate a reasonable probability that either:

- (1) the average assessment level in the county is less than 95 percent of the assessment level required by statute; or
- (2) the sum of all the differences between the board's appraisals and the assessor's values (without regard to whether the differences are underassessments or overassessments), expanded statistically over the assessor's entire roll, exceeds 7.5 percent of the assessment level required by statute.

(b) For purposes of this regulation, "areas of an assessor's assessment operation" means, but is not limited to, an assessor's programs for:

- (1) Uniformity of treatment for all classes of property.
- (2) Discovering and assessing newly constructed property.
- (3) Discovering and assessing real property that has undergone a change in ownership.
- (4) Conducting mandatory audits in accordance with Revenue and Taxation Code Section 469 and Property Tax Rule 192.
- (5) Assessing open-space land subject to enforceable restriction, in accordance with Revenue and Taxation Code Sections 421 et. seq.
- (6) Discovering and assessing taxable possessory interests in accordance with Revenue and Taxation Code Sections 107 et. seq.
- (7) Discovering and assessing mineral-producing properties in accordance with Property Tax Rule 469.
- (8) Discovering and assessing property that has suffered a decline in value.
- (9) Reviewing, adjusting, and, if appropriate, defending assessments for which taxpayers have filed applications for reduction with the local assessment appeals board.

(c) A finding of "significant assessment problems," as defined in this regulation, would be limited to the purposes of Revenue and Taxation Code Section 75.60 and Government Code Section 15643, and shall not be construed as a generalized conclusion about an assessor's practices.

ASSESSOR'S RESPONSE TO BOE'S FINDINGS

Section 15645 of the Government Code provides that the assessor may file with the BOE a response to the findings and recommendation in the survey report. The survey report, the assessor's response, and the BOE's comments on the assessor's response, if any, constitute the final survey report.

The Kern County Assessor's response begins on the next page. The BOE has no comments on the response.

JAMES W. FITCH
ASSESSOR-RECORDER

RECEIVED

JUL 14 2006

ANTHONY ANSOLABEHRE
Assistant Assessor

JEANI SMITH
Assistant Recorder



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Telephone (661) 868-3485
1115 Truxtun Avenue
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July 11th, 2006

Ms. Mickie Stuckey, Chief
County Property Taxes Department, MIC: 62
State Board of Equalization
P.O. Box 942879
Sacramento, CA 94279-0062

RECEIVED
JUL 14 2006
JEANI SMITH
Assistant Recorder

Dear Ms. Stuckey:

Pursuant to Section 15645 of the California Government Code, the following constitutes the Assessor's Response to the recommendations presented in this Assessment Practices Survey for Kern County.

I would like to express my appreciation to the Board's Survey Team for the professional and conscientious manner in which the survey was conducted. Their positive acknowledgements and constructive comments regarding how my Office works are appreciated.

We welcome the examination of our work and processes. Your constructive recommendations provide us the opportunity to focus on current policies and procedures which allow us to complete our mission of providing accurate, timely and fair assessments, while providing the highest level of benefit to the taxpayers and customers we serve.

As you are aware, Kern County has experienced significant growth over the last several years and is currently recognized as one of the fastest growing counties in the State. That growth has placed a great strain on our resources. We continue to explore new methods of doing more with less. However, the lack of adequate staffing levels threatens our ability to complete our legal mandates, despite our desire to do otherwise.

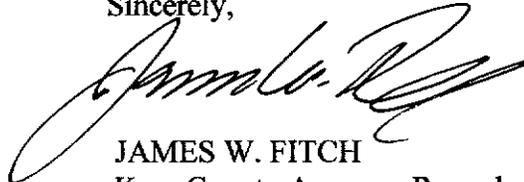
I would like to take this opportunity to express my concern over the recent suspension of the Property Tax Administration Program (PTAP). Here in Kern County, the PTAP funds 15% of our staff and part of the computer system programming support. Clearly, a lack of these resources will have a detrimental impact on our accuracy, production and general operations.

Ms. Mickie Stuckey

Ms. Mickie Stuckey
Page Two
July 11th, 2006

I also want to thank the staff of the Kern County Assessor's Office for their dedication, professionalism and commitment to serving the citizens of Kern County.

Sincerely,

A handwritten signature in black ink, appearing to read "James W. Fitch". The signature is fluid and cursive, with a large initial "J" and "F".

JAMES W. FITCH
Kern County Assessor-Recorder

JWF:kc

Recommendation #1: Revise the notice informing the applicant of the proposed reassessment to reflect the current statutory time period in which to file an application.

We concur. We have revised the Notice to reflect the correct filing time period according to Revenue and Taxation Code Section 170 (c) .

Recommendation #2: Revise the assessment forms program by: 1) using only current forms and approved rearranged forms, 2) including only permissible requirements on the cover letter for the annual mineral property statement and, 3) conforming the language of the Notice of Supplemental Assessment to the requirements of Section 75.31 (e).

- 1) We concur. We have reviewed and updated all of the mandated forms used by our office.
- 2) We concur. The cover letter for the annual mineral property statement has been revised to remove the requirement of collation.
- 3) We concur. The Notice of Supplemental Assessment has been revised to meet the notification requirements of Section 75.31 (e).

Recommendation #3: Timely apply the penalty for failure to file a change in ownership statement as prescribed in Section 482 (a).

As time and available staff permit, the Assessor will attempt to increase timely enforcement of the penalty for failure to file a change in ownership statement.

Recommendation #4: Issue all supplemental assessments according to statutory guidelines.

We concur. Supplemental assessments will be enrolled on possessory interests when there is completion of new construction or a change in ownership.

Recommendation #5: Establish the base year value for taxable government-owned property according to BOE guidelines.

We concur. Appraisal staff valuing taxable government-owned property are being directed to follow the BOE guidelines as set forth in LTA 2000/037 in establishing the base year value.

Recommendation #6: Improve the possessory interest program by 1) assessing all taxable possessory interests, 2) reviewing improvement-only possessory interests for escape assessments, 3) reviewing all taxable possessory interests with stated terms of possession for declines in value, 4) deducting expenses from gross income when valuing possessory interests by the income approach, and 5) revalue taxable possessory interests at the end of the reasonably anticipated term of possession used for their assessment.

- 1) As limited staff and resources allow, the Assessor will discover and assess all taxable possessory interests. Since the SBE survey team was in Kern County, the Board of Supervisors has passed a Low Value Resolution as authorized by R & T Code Section 155.20. This Resolution exempts temporary or transient possessory interests in publicly owned fairgrounds, convention centers, or similar facilities up to a value of \$40,000. Many of the private interests listed in the SBE footnote for this recommendation may now be exempted under this Resolution.
- 2) As limited staff and resources allow, the Assessor will review and correct improvement-only possessory interests without land values at the Kern Valley Airport.
- 3) As limited staff and resources allow, the Assessor will review all taxable possessory interests with stated terms of possession for declines in value.
- 4) As limited staff and resources allow, the Assessor will, where it is appropriate and can be documented, deduct operating expenses from the forecast income before capitalizing the income stream into value.
- 5) As limited staff and resources allow, the Assessor will revalue the taxable possessory interests at the end of the reasonably anticipated term of possession.

Recommendation #7: Assess all leasehold improvements.

We concur. When a taxpayer reports leasehold costs for structural improvements on a Business Property Statement, that information should be transmitted by the Business Section to the Realty Division for assessment. In some cases, that apparently did not happen. We are planning changes which will improve the intra-departmental transmittal of this information.

Recommendation #8 (1): Consistently value non-producing and marginal petroleum properties.

The BOE cites two problems, inconsistent valuation methodology and the capitalization rate:

- 1) First, we agree that we should apply the value to each property on the same basis that it is estimated and we are reviewing our methodology.
- 2) The BOE says that the discount rate is too low for marginal and non-producing properties. If we used the rates that the BOE suggests, the answer, when rounded to the nearest \$1,000 in value, would be the same. By market convention, we round all of our petroleum related mineral values to the nearest \$1,000, so implementing this may not affect the assessed value. We will, however, continue to review the capitalization rate for non-producing and marginal petroleum properties.

Recommendation #8 (2): Properly account for abandonment expenses in the cash flow analysis.

We respectfully disagree for the following reasons discussed below, among others. Also, we would like to point out that the Board is focusing on an issue which would have a negligible effect on most appraisals. In the examples discussed below, the value difference between the Board's recommended methodology and that of Kern is less than the amount of rounding, so it would not have any effect to the enrolled value.

- 1) This Section of the AH 566 to which the Board refers is ambiguous and we feel that it is being misinterpreted by the Board.
- 2) We account for abandonment costs when they are anticipated to occur. This is consistent with Board Rule 8, the Assessors' Handbook 501 and 502, and the decision in *Dominguez Energy L.P. v. County of Los Angeles*. The BOE's recommendation is in conflict with the above and would, generally, result in an underassessment.
- 3) The recommendation by the Board to not defer well abandonment costs is in conflict with overwhelming market evidence that owners typically defer these costs until many years after a well has been idled.
- 4) As for the recommendation to use a sinking fund to account for abandonment cost, its use is not supported by the market evidence. Also, its use may result in undervaluing the property.
- 5) Also, it should be pointed out that, in most cases, the value difference would be negligible. In a typical discounted cash flow analysis with an economic life of about 20 years, moving the abandonment costs from year 22 to 20 will have a negligible effect on the value conclusion. For a one-well lease, with a well-depth of 2,500 feet, the future abandonment cost is expected to be about \$14,100. At a discount rate of 15%, the present value factor for year 22 is 0.0495, resulting in a present value of (\$699). For year 20 the present value factor is 0.0655, resulting

in a present value of (\$924). The difference ($924 - 699 = 225$) is about \$200 in value. So a typical one-well lease would have a value difference so small the, due to rounding, may have no effect on the value enrolled.

In one very large appraisal (with a market value in excess of \$1,000,000,000 in 2005) moving the terminal abandonment cost (estimated to be \$71,000,000) from 2 years after the economic limit to the year in which the economic limit was reached, resulted in a lower estimate of market value by \$490, which due to rounding, may not have any effect on the value enrolled.

Recommendation #8 (3): Develop capitalization rates for cogeneration facilities independent of the primary use of the associated property.

- 1) We agree that when valuing cogeneration facilities separately from a petroleum producing property, the rate selected should reflect the risk of cogeneration.
- 2) We also agree that when valuing cogeneration facilities with the petroleum producing property, the rate or rates selected should reflect the risk of both cogeneration and petroleum production.
- 3) We will update the manual to reflect this.

Recommendation #8 (4): Appraising mining property as an appraisal unit for the purpose of measuring declines in value.

We concur. As limited staff and resources allow, the Assessor will implement this recommendation.

Recommendation #9: Use the Assessors' Handbook Section 581, as intended, when valuing older equipment.

We agree and have implemented this recommendation.
