

Memorandum

To: Mr. Dean R. Kinnee
Chief, Assessment Policy and Standards Division

Date: June 18, 2003

From: Michael Lebeau
Tax Counsel
Legal Department

Subject: *Revenue and Taxation Code Section 68—Reallocating Land and Improvement Values*

This is in reply to your memorandum of April 15, 2003 in which you requested guidance concerning the comparability requirements under Revenue and Taxation Code section 68 and Property Tax Rule 462.500 for a property in _____ County. The facts and questions posed in your memorandum are restated below, followed by our responses.

Facts Presented

A public entity in _____ County acquired real property from the owner of a shopping center. That property had been used as a parking lot—a commercial use—and it included the land and the pavement necessary for that use. No improvement values were enrolled for the property taken, even though the property consisted of both land and pavement.

To replace that property, the owner of the shopping center constructed a parking structure on land it already owned. You ask whether (1) a parking structure would be considered a comparable replacement for "essentially vacant land" and (2) can the base year value of the land be transferred to an improvement? For the reasons discussed below, the answer to both question's is "yes."

Law and Analysis

1. **After the public entity acquired the property taken, a parking lot, the taxpayer built replacement improvements, a parking structure, on land that it had already owned prior to the acquisition. You ask whether "under these circumstances would a structure be considered a comparable replacement for essentially vacant land?"**

Yes, under the facts presented in this situation. Notwithstanding the assessor's failure to enroll an improvement value, the property taken consisted of both land and improvements. New improvements built on land already owned by the taxpayer at the time of taking will qualify as "replacement property" if they meet the requirements of Revenue and Taxation Code section 68 and Property Tax Rule 462.500.

(a) Was the property taken "essentially vacant land?"

No. Although the assessor failed to enroll an improvement value on the property taken, the facts indicate that the property taken consisted of both land and improvements. Thus, the property taken was not vacant land.

According to a follow-up telephone conversation between Supervising Tax Counsel Louis Ambrose and Ms. Glenna Schultz of your office, we learned that the assessor had enrolled a zero improvement value on the property taken. It was the assessor's position that the property taken was "essentially vacant land." However, notwithstanding the assessor's failure to enroll an improvement value, we disagree with that conclusion.

As described in your memorandum, the property taken consisted of "a portion of a paved parking lot for a shopping center." Containing an illustrative list of those types of property considered to be land and those considered to be improvements, subsection (b)(2) of Property Tax Rule 124 includes concrete flatwork and paved roads as examples of improvements. Since most paved parking lots for shopping centers include concrete flatwork and paved roads, it is our opinion that the property taken consisted of land and improvements, regardless of the assessor's failure to enroll an improvement value.

(b) Do new improvements built on land already owned by the taxpayer at the time of taking qualify as "replacement property"?

New improvements built on land already owned by the taxpayer at the time of taking will qualify as "replacement property" if they meet the requirements of Revenue and Taxation Code section 68 and Property Tax Rule 462.500.

As you are aware section 68 generally provides that taxpayers who purchase property to replace comparable property from which they are displaced may transfer their adjusted base year value from the property taken to a replacement property. Section 68 provides in part:

For purposes of Section 2 of Article XIII A of the Constitution, the term "change in ownership" shall not include the acquisition of real property as a replacement for comparable property if the person acquiring the real property has been displaced from property in this state by eminent domain proceedings, by acquisition by a public entity, or by governmental action which has resulted in a judgment of inverse condemnation.

The adjusted base year value of the property acquired shall be the lower of the fair market value of the property acquired or the value which is the sum of the following:

(a) The adjusted base year value of the property from which the person was displaced.

(b) The amount, if any, by which the full cash value of the property acquired exceeds 120 percent of the amount received by the person for the property from which the person was displaced.

While section 68 excludes certain acquisitions of real property from the definition of "change in ownership," it does not directly address whether new improvements built to replace property taken by the government are eligible for property tax relief. Property Tax Rule 462.500, the regulation that interprets and implements section 68, provides that new improvements are also eligible for relief under section 68. Subsection (f) of Property Tax Rule 462.500 provides:

Any new construction required to make replacement property comparable to the property taken shall, to that extent, be eligible for property tax relief, if such new construction is completed after March 1, 1975, and if it is completed on or after the earliest of the dates listed in subdivision (g)(3), and if a timely request is made for assessment relief.

Thus, under subsection (f) newly constructed improvements may qualify for relief. It is our opinion that the Legislature's findings and declaration for section 68 and the comparability requirements in Rule 462.500 do not prohibit the transfer of the base year value of a property taken—consisting of land and improvements—to a replacement property consisting of only improvements.

However, as indicated in the facts provided in your memorandum dated April 15, 2003, the taxpayer owned the land on which the replacement improvements were built *prior* to the date that the public entity began the process to acquire the original property. That *land* does not qualify as a "replacement property" since the taxpayer acquired the land outside the qualifying time limits for relief. Subsection (g)(3) provides that:

Replacement property shall be eligible for property tax relief under this section if it is acquired after March 1, 1975, and if it is acquired on or after the earliest of the following dates:

- (A) The date the initial written offer is made for the replaced property by the acquiring entity;
- (B) The date the acquiring entity takes final action to approve a project which results in an offer for or the acquisition of the replaced property; or
- (C) The date, as declared by the court, that the replaced property was taken.

We assume, for purposes of this analysis, that the taxpayer acquired the land prior to the earliest of the acquisition event dates provided in subsection (g)(3) of Rule 462.500. Thus, the land is ineligible for transfer of the base year value. Despite that ineligibility, the new improvements built on that land, as replacement improvements would qualify for a base year value transfer from the property taken, consisting of land and improvements, if the new construction was completed on or after the earliest of those dates and provided that they meet the requirements of comparability and ownership.

2. May the entire base year value of the property taken, consisting of both land and improvements, be transferred solely to land or solely to improvements?

Yes. Section 68 and Rule 462.500 allow the transfer of the base year value of a property taken—consisting of land and improvements—to a replacement property consisting of only improvements, since there is no prohibition or restriction on a reallocation of the base year values.

Based on the facts provided, the *property from which the taxpayer was displaced* was a paved parking lot, consisting of both land and improvements, while the *property acquired* by the taxpayer was new improvements of like utility (a newly constructed parking structure on land already owned by the taxpayer). Under the facts presented, the taxpayer's property eligible for the base year value transfer is the newly constructed improvements.

Improvements built on land already owned by the taxpayer as replacement improvements would qualify for the base year value transfer if they were built on or after the earliest dates contained in subsection (g)(3) of Rule 462.500 and provided that they meet comparability and ownership requirements. Subsection (f) of Rule 462.500 provides that:

[a]ny new construction required to make replacement property comparable to the property taken shall, to that extent, be eligible for property tax relief . . . if [such new construction] is completed on or after the earliest of the dates listed in subdivision (g)(3), and if a timely request is made for assessment relief.

Thus, under subsection (f), newly constructed improvements may qualify for relief even though the land on which they are situated is ineligible.

When calculating the new assessed value for the replacement property upon completion of the newly constructed improvements, the only written guidance regarding the proper allocation of base year values is found in subsection (d) of Rule 462.500:

(d) BASE YEAR VALUE OF REPLACEMENT PROPERTY. The following procedure shall be used by the assessor in determining the appropriate adjusted base year value of comparable replacement property:

(1) Compare the award or purchase price paid by the acquiring entity for the property taken or acquired with the full cash value of the comparable replacement property.

(2) If the full cash value of the comparable replacement property does not exceed 120 percent of the award or purchase price of the property taken, then the adjusted base year value of the property taken shall become the replacement property's base year value.

(3) If the full cash value of the replacement property exceeds 120 percent of the award or purchase price of the property taken, then the amount of the full cash value over 120 percent of the award or purchase price paid shall be added to the adjusted base year value of the property taken. The sum of these amounts shall become the replacement property's base year value.

(4) If the full cash value of the comparable replacement property is less than the adjusted base year value of the property taken, then that lower value shall become the replacement property's base year value.

(5) If there is no award or purchase price paid by the acquiring entity (i.e., an exchange) for the property taken, then the full cash value of the acquired property and the full cash value of the replacement property shall be determined by the assessor of the county in which each property is located for the purpose of applying the other provisions of this subdivision. The procedure set forth in subdivision (d) (1) through (d) (4) shall then be applied to determine the replacement property's base year value.

Subsection (d) of Rule 462.500 provides for the comparison between the award or purchase price paid by the public entity and full cash value of the replacement property. However, it does not prohibit or restrict the reallocation of the base year values when a replacement property consists of only newly constructed improvements. Consequently, we believe that the assessor may transfer the entire base year value of an original property consisting of land and improvements to a comparable replacement property consisting of only improvements.

The views expressed in this letter are only advisory in nature; they represent the analysis of the legal staff of the Board based on present law and the facts set forth herein, and are not binding on any person or public entity.

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