No. S194121

IN THE

SUPREME COURT OF CALIFORNIA

ELK HILLS POWER, LLC,
Plaintiff and Appellant,

v.

CALIFORNIA STATE BOARD OF EQUALIZATION AND COUNTY OF KERN,
Defendants and Respondents.

After A Decision By The Court of Appeal
Fourth Appellate District, Division One, Case No. D056943,
San Diego Superior Court Case No. 37-2008-00097074-CU-MC-CTL
The Honorable Ronald L. Styn

APPELLANT'S OPENING BRIEF

LAW OFFICE OF PETER MICHAELS
Peter W. Michaels (93212)
6114 La Salle Avenue, #445
Oakland, California 94611
Telephone: (510) 547-0255

GIBSON DUNN & CRUTCHER
Julian W. Poon (219843)
Blaine H. Evanson (254338)
333 South Grand Avenue
Los Angeles, California 90071
Telephone: (213) 229-7000

MOONEY, WRIGHT & MOORE, PLLC
Paul J. Mooney (*pro hac vice*)
Arizona State Bar No. 006708
1201 South Alma School Rd., Ste. 16000
Mesa, AZ 85210
Telephone: (480) 615-7500
Attorneys for Plaintiff and Appellant
Elk Hills Power, LLC

No. S194121

IN THE

SUPREME COURT OF CALIFORNIA

ELK HILLS POWER, LLC,
Plaintiff and Appellant,

v.

CALIFORNIA STATE BOARD OF EQUALIZATION AND COUNTY OF KERN,
Defendants and Respondents.

After A Decision By The Court of Appeal
Fourth Appellate District, Division One, Case No. D056943,
San Diego Superior Court Case No. 37-2008-00097074-CU-MC-CTL
The Honorable Ronald L. Styn

APPELLANT'S OPENING BRIEF

LAW OFFICE OF PETER MICHAELS
Peter W. Michaels (93212)
6114 La Salle Avenue, #445
Oakland, California 94611
Telephone: (510) 547-0255

GIBSON DUNN & CRUTCHER
Julian W. Poon (219843)
Blaine H. Evanson (254338)
333 South Grand Avenue
Los Angeles, California 90071
Telephone: (213) 229-7000

MOONEY, WRIGHT & MOORE, PLLC
Paul J. Mooney (*pro hac vice*)
Arizona State Bar No. 006708
1201 South Alma School Rd., Ste. 16000
Mesa, AZ 85210
Telephone: (480) 615-7500
Attorneys for Plaintiff and Appellant
Elk Hills Power, LLC

TABLE OF CONTENTS

TABLE OF CONTENTS (cont'd)

TABLE OF AUTHORITIES

Cases

TABLE OF AUTHORITIES (CONT'D)

Statutes

TABLE OF AUTHORITIES (CONT'D)

Other Authorities

ISSUE PRESENTED FOR REVIEW

Whether the Fourth District court of appeal erred in holding that the value of intangible rights known as "Emission Reduction Credits" can be expressly included in the taxable value of Elk Hills Power's tangible property in violation of the longstanding constitutional exemption and statutory prohibition against the taxation of intangible assets, and in direct contravention of settled precedent from this Court and every appellate district in the state upholding those limits on the taxing power? (Cal. Const., art. XIII, §2; Rev. and Tax. Code, §110(d) and §212.)

INTRODUCTION

The court of appeal's decision in this case ("Decision") contravenes both an express constitutional exemption and statutory prohibitions against the property taxation of intangible assets and rights. (Cal. Const., art. XIII, §2; Rev. and Tax. Code, §110 and §212.) In determining that Appellant's undisputedly intangible Emission Reduction Credits ("ERCs") are subject to assessment, the court of appeal disregarded Article XIII, §2 of the Constitution and Sections 110 and 212 of the Revenue and Taxation Code. In doing so, the Decision also deviated from this Court's decision in *Roehm v. County of Orange* (1948) 32 Cal.2d 280 (hereinafter, *Roehm*), which for more than sixty years has served as the guiding precedent in this state for

the exclusion of value associated with intangible assets and rights from property taxation.

Article XIII, §2 of the California Constitution prohibits the Legislature from imposing property taxes on intangible assets and rights other than those specifically enumerated in that section. (Cal. Const., art. XIII, §2.) ERCs, like almost all other intangible assets, are not listed in Article XIII, §2. (*Ibid.*) Therefore, ERCs are not subject to property taxation under California law. In *Roehm*, this Court upheld the exemption for intangible assets, noting that taxation of intangible rights and assets through the property tax system would be "an administrative impossibility and an ethical monstrosity." (*Roehm*, 32 Cal.2d at pp.288-89.)

The Legislature amended Section 110 of the Revenue and Taxation Code in 1995 to codify *Roehm* and its progeny. The 1995 amendments clarified how intangible property is to be valued for property tax purposes and, most importantly here, how the value of intangible assets and rights must be removed from the value of real, personal and unitary property.[1]

---

[1] "The board may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in a primary function of the assessee. When so valued, those properties are known as 'unitary property'." (Rev. and Tax. Code, §723.) Unitary property includes land, improvements and personal property owned or leased by a state assessee and used in its primary operation. (State Assessment Manual (2000) pp.18-19.) **EHP's unitary property is referred to herein as "EHP's Plant."**

Specifically, as it applies to this case, the Legislature added Subdivision 110(d)(2), which requires that intangible value be removed from **unit valuation**. (Rev. and Tax. Code, §110(d)(2).) Subdivision 110(d)(2) provides as follows:

> If the principle of **unit valuation** is used to value properties that are operated as a unit and the unit includes intangible assets and rights, then the fair market value of the taxable property contained within the unit shall be determined **by removing from the value of the unit the fair market value of the intangible assets and rights contained within the unit.**

(*Ibid.*, emphasis added.)

In this case, the Board was charged with the **unit valuation** of EHP's electric generation plant – the very type of valuation addressed in Subdivision 110(d)(2). The Board, however, did not follow the mandate of Subdivision 110(d)(2), which required the Board to remove the value of the intangible ERCs from the unit valuation of EHP's Plant. Rather, the Board admittedly and expressly **added** a cost component for ERCs to the valuation of the Plant. (Board's Answer to Petition for Review, p.3.)

The Fourth District interpreted Section 110 of the Revenue and Taxation Code in such a way as to nullify Subdivision 110(d). Specifically, the court of appeal disregarded the constitutional limitations set forth in Subdivision 110(d) by misinterpreting Subdivision 110(e). By so doing, the court of appeal's Decision overrides the only provision that deals specifically with how to exclude the value of intangible rights in a unit

valuation; namely, Subdivision 110(d)(2). The court of appeal's new test violates the California Constitution by permitting the property taxation of intangible assets or rights deemed "necessary" to the beneficial and productive use of tangible real or personal property. This construction of Subdivision 110(e) effectively negates Subdivision 110(d).

Under the court of appeal's new test, an intangible asset or right is subject to property tax if it is "necessary" to the beneficial and productive use of associated tangible, taxable property. (Decision, pp.39-40.) Applying its new test to the facts of this case, the court of appeal held that because ERCs are "necessary" to the operation of EHP's Plant, it was proper for the Board to include the value of intangible ERCs in its valuation of EHP's Plant. (*Ibid.*)

Under the Constitution and Section 212 of the Revenue and Taxation Code, all intangible assets or rights are exempt from property taxation, regardless of their kind or variety, and regardless of whether they are "necessary" to the beneficial and productive use of taxable property. (Cal. Const., art. XIII, §2.) There are no qualifications or exceptions to this important constitutional limitation on property taxation.

The Fourth District court of appeal's Decision has created an improper exception to this important rule of California jurisprudence. Accordingly, its Decision should be reversed, and this matter should be

remanded to the trial court with directions to enter judgment in favor of EHP as a matter of law based on the undisputed facts in the record below.

STATEMENT OF THE CASE

EHP appeals to this Court from the decision of the Fourth Appellate District, Division One, dated May 10, 2011 (the "Decision"). EHP instituted the original action in San Diego County Superior Court against Defendants and Respondents the California State Board of Equalization (the "Board") and Kern County, to challenge the Board's decision to assess intangible ERCs owned and used by Elk Hills Power for tax years 2004 through 2008. (1 CT 1-13.)[2]

Because this case involved a purely legal issue, both parties filed motions for summary judgment. (1 CT 105-23; 2 CT 226-251.) The trial court denied EHP's motion and granted the Board's cross-motion on the basis of Revenue and Taxation Code §110**(f)**, finding that ERCs are an "attribute" of real property.[3] (1 RT 57:2-9; 4 CT 833:17-22.)

---

[2] All references to the Clerk's Transcript include reference to the volume, page number and lines, where applicable. For example 1 CT 125:5-14, refers to Volume 1 of the Clerk's Transcript at p.125, lines 5-14. Likewise, references to the Reporter's Transcript include reference to the volume, page number and lines.

[3] In reaching his decision, the trial judge expressed doubts about his application of Section 110, so EHP filed a Motion for New Trial, arguing for application of the basic tenet of tax law that any doubt arising from the construction of a taxing statute must be resolved in favor of the taxpayer and against the taxing authority. (4 CT 763-69.) (*California Motor Transp. Co. v. State Bd. of Equalization* (1948) 31 Cal.2d 217, 223-24.) The trial

On appeal to the Fourth District, the court of appeal affirmed the trial court's decision, but notably relied upon a different subdivision of the Revenue and Taxation Code; namely, Subdivision 110**(e)**. (Decision, pp.40-41.) Specifically, the court of appeal determined that Subdivision 110**(e)** – and that subdivision alone – determines the outcome of this case.[4]

The court of appeal held that because ERCs are "**necessary**" to the beneficial and productive use of EHP's business, Subdivision 110(d) does not apply at all and the value of the ERCs need not be removed from the unitary value of the Plant. The court of appeal reasoned:

> [A]lthough section 110, subdivision (d)(1) can forbid valuing taxable property by reflecting the value of the intangible assets that relate to it as a "going concern" business, **that subdivision (d)(1) will not apply to a situation otherwise expressly provided for in its subdivision (e).** Specifically, **where the presence of intangible assets is "necessary" for the property to be put to beneficial or productive use, then the unitary valuation may assume the presence of such necessary assets**. (§110, subd. (e).) This kind of power plant is subject to particular forms of regulation, these ERCs are properly deemed "necessary" for its beneficial and productive use, and therefore the ERC contribution to the value of the plant is a permissible consideration in the overall valuation determination. **There is no basis to remove the value of the**

---

court denied EHP's Motion for New Trial (4 CT 885-86), but the judge again noted that he had gone "back-and-forth" in resolving the legal issue presented herein. (2 RT 64:11-16.)

[4] No doubt, this was influenced at least partly by the Board's decision to shift the emphasis of its legal argument from Subdivision 110(f) in the trial court to Subdivision 110(e) on appeal. Because of this shift in the emphasis of the Board's argument, the first time EHP focused its legal arguments on Subdivision 110(e) was in its Reply Brief.

ERCs from the value of the unit, where the unit cannot legally operate without them.

(Decision, pp.39-40, emphasis added.)[5] Rather than interpreting Subdivisions 110(d) and (e) harmoniously, the court of appeal interpreted Subdivision 110(e) in such a way as to override Subdivision 110(d)(2) – the very provision applicable to this case of **unit valuation**. More importantly, the Fourth District interpreted Subdivision 110(e) in a way that negates the constitutional property tax exemption for intangible assets and rights codified by Subdivision 110(d).

Believing the court of appeal misstated the facts upon which it relied in reaching its decision, EHP filed a timely Petition for Rehearing, which was denied on June 7, 2011. Thereafter, EHP filed a timely Petition for Review on June 20, 2011, which was granted on August 24, 2011.

SUMMARY OF FACTS

The parties agreed and the trial court expressly found that ERCs are intangible rights. (1 RT 57:1-2.) "They [ERCs] are an intangible, I'll make that finding on the record . . . ." (*Ibid.*) Notably, the California Legislature

---

[5] Although the Decision refers to Subdivision 110(d)(1), it completely fails to address Subdivision 110(d)(2), which specifically applies to cases such as this one that involve unit valuation. It also fails to address Subdivision §110(d)(3), but its interpretation of Subdivision 110(e) and its holding will be applied to all three subparts of Subdivision 110(d), thereby creating a conflict with other statutes. (See Rev. and Tax. Code, §107.7 [providing that intangible assets and rights of a cable system, including franchises, are not subject to property taxation.].)

has stated that ERCs are not "property" at all. "Certificates evidencing ownership of approved reductions issued by [an air quality] district shall not constitute instruments, securities, **or any other form of property**." (Health and Safety Code, §40710, emphasis added.) Taxing ERCs as "property" is clearly inconsistent with the legislative determination that ERCs are not property at all.

A. Emission Reduction Credits ("ERCs").

The California Clean Air Act enables air quality control districts, including the San Joaquin Valley Unified Air Pollution Control District, to reduce the emission of air pollutants by means of an "emission credit system" and a "district banking and offset system". (Health & Safety Code, §40709, *et seq.*) An air pollution control district issues ERCs to an emission source, *e.g.* an electric generation plant, when the source or plant reduces its emissions beyond what is required by government permits and rules by adding controls, replacing or removing equipment, or closing a plant. (See Health & Safety Code §40709(a); San Joaquin Valley Air Pollution Control District Rule 2301, §3.6.) (1 CT 125:25-126:5.) Once issued, the ERC becomes an intangible right belonging to the plant owner, which can be "banked" to offset future emission increases, or sold to other companies in need of emission offsets. (See Health & Safety Code

§40709(a); San Joaquin Valley Air Pollution Control District Rule 2301, §3.2, §3.3.) (1 CT 126:5-10.)

A plant owner seeking to construct a new plant may find itself in the position of having to purchase ERCs to "offset" future emissions, as part of the process of obtaining "authority to construct" its plant. (San Joaquin Valley Air Pollution Control District Rule 2201, §3.25.) (1 CT 126:11-15.) This is the position that EHP found itself in when constructing its Plant in Kern County. (1 CT 126:23-27.)

In constructing the Plant, EHP took two steps to comply with the emission requirements of the San Joaquin Valley Unified Air Pollution Control District and the California Energy Commission. (1 CT 126:15-27.) First, EHP agreed to install "best available control technology" that would significantly reduce emissions. (1 CT 126:15-22; 143:8-11.) Second, EHP purchased ERCs at market rates, in order to offset future emissions. (1 CT 126:23-27; 143:11-14.)

Critically, as applied to this case, ERCs do not attach directly to a particular parcel of real property, plant or other emission source. (1 CT 127:1-7; 143:14-16.) Rather, ERCs are inherently separate from real property. (1 CT 127:1-10; 143:18-19.) They can be independently bought and sold. (1 CT 127:3-7.) They can be banked for future use. (1 CT 126:5-10; 14:16-18.) They can be leased or traded. (1 CT 127:3-7; 143:16-

18.) In other words, ERCs have a value separate and independent from that of the real property itself. (1 CT 127:7-9; 143:18-19.)

EHP purchased the ERCs at issue in this case in order to construct the plant in Kern County. (1 CT 601:23-27.) As part of the process of obtaining its "authority to construct" the plant, EHP "surrendered" the certificates evidencing its ERCs to the San Joaquin Valley Unified Air Pollution Control District, which allowed EHP to begin producing electricity at specified levels. (2 CT 289-293.)

B. The Board's Assessment Of ERCs.

As noted above, the Board is charged in this case with determining "unitary value," which means it must value EHP's tangible real and personal property as a "unit" – a functioning combination of real and personal property, a collection of land, buildings and equipment. (Cal. Const., art. XIII, §19; Rev. and Tax. Code, §723.) This fact, which is undisputed by the parties, requires the application of Subdivision 110(d)(2) of the Revenue and Taxation Code, the only statutory subdivision that specifically addresses the prohibition against property taxation of intangible value in unit valuation. Subdivision 110(d)(2) explicitly requires the Board to remove the value of intangible rights from the unit valuation.

C. The Board Admittedly Added Specific Values For Intangible ERCs To Its Cost Approach.

In each of the five tax years at issue, the Board utilized the cost approach in valuing EHP's Plant. (1 CT 137:15-17; 3 CT 513:12-14.) In determining EHP's unit value for each tax year using the cost approach, the Board took the extraordinary step of **adding-in** a separate value component for intangible ERCs. In fact, the Board has openly admitted that it "**included a standard estimated replacement cost for the deployed ERCs**" to its unit valuation of EHP's Plant. (Board's Answer to Petition for Review, p.3, emphasis added.)

D. The Board Failed To Remove The Value of Intangible ERCs From Its Income Approach.

For tax years 2006, 2007 and 2008, the Board also utilized the income approach to determine EHP's unit value. (3 CT 513:14-18.) The income approach is appropriate for valuing property that produces income, but it is not intended to value the business enterprise – only the tangible real and personal property that functions together as a unit.

One inherent problem with the income approach is that it also captures the value of intangible assets that are necessary in order for the property to produce income. (See *South Bay Irrigation Dist. v. California-Am. Water Co.* (1976) 61 Cal.App.3d 944, 988.) Thus, under the income approach, the assessor must take an affirmative step to exclude value

associated with intangible assets. In the wake of the 1995 amendments to Section 110, the Board adopted a specific procedure to make this adjustment under the income approach. (3 CT 530-33.)

The Board admitted that it failed to apply its own methodology to exclude income attributable to ERCs from its income approach valuation. (Answer to Petition for Review, p.3.) The Board's express addition of the cost component for ERCs to its cost approach, **and** its failure to remove the income attributable to ERCs from its income approach, resulted in the property taxation of intangible assets, in direct violation of the Constitution and Section 110(d)(2) of the Revenue and Taxation Code.[6]

STANDARD OF REVIEW

The issue presented by this appeal – whether ERCs must be excluded from assessment for property tax purposes under Section 110 – is a purely legal issue that is subject to this Court's independent *de novo* review. (*Mola Dev. Corp. v. Orange County Assessment Appeals Bd.*

---

[6] The Decision asserts there is a factual dispute regarding the Board's treatment of ERCs (Decision, p.12), and that the Board's worksheets (entered into the record by both parties) can be "interpreted either way" (Decision, p.36), stating: "Jackson's exhibits also show the ERC site-specific adjustments for certain years, and they exclude the ERC costs from the total plant cost estimate." (Decision, p.37, emphasis added.) The Board admitted below that it included a cost component for the ERCs in each of its valuations. (1 RT 7:3-11; 3 CT 565:17-23; Respondents' Brief, Court of Appeal, p.5) Accordingly, there is no "factual dispute" regarding how ERCs were valued by the Board for the five tax years at issue in this litigation, and the court of appeal's suggestion to the contrary is inaccurate.

(2000) 80 Cal. App.4th 309, 316; *GTE Sprint Communications Corp. v. County of Alameda* (1994) 26 Cal.App.4th 992, 1001.)

Moreover, in performing a *de novo* review of an order granting summary judgment, an appellate court must view the evidence in the light most favorable to the losing party, resolving evidentiary doubts and ambiguities in favor of the party against whom summary judgment was entered. (*Martinez v. Combs* (2010) 49 Cal.4th 35, 68.)

Finally, as noted previously (*ante* at n.3), in construing tax statutes, courts must construe any ambiguity in favor of the taxpayer. (*California Motor Transp. Co. v. State Board of Equalization* (1948) 31 Cal.2d 217, 223-24.)

ARGUMENT

As interpreted by this Court in *Roehm*, Article XIII, Section 2 is a limitation on the Legislature's power to tax property. In this case, the Fourth District has interpreted Section 110 of the Revenue and Taxation Code in such a way as to violate this constitutional provision by permitting the property taxation of ERCs, and potentially countless other types intangible assets and rights deemed "necessary" to the beneficial and productive use of tangible property.

During the last sixty-plus years, this Court has provided guidance three times on the issue of how intangible assets should be dealt with for

property tax purposes. (See *Roehm*, 32 Cal.2d at p.290 [upholding the property tax exemption for intangible liquor licenses]; *Michael Todd Co. v. County of Los Angeles* (1962) 57 Cal.2d 684, 693 [upholding the property tax exemption for intangible copyrights]; *De Luz Homes, Inc. v. County of San Diego* (1955) 45 Cal.2d 546, 565-66 [upholding the property tax exemption for intangible business enterprise value].) In each instance, this Court upheld the constitutional exemption for intangible rights. (*Ibid.*) It is time for this Court to reaffirm this important constitutional limitation on the state's power to tax only specifically enumerated property.

I. THE CALIFORNIA CONSTITUTION AND SECTION 110 PROHIBIT THE PROPERTY TAXATION OF INTANGIBLE ASSETS AND RIGHTS.

The California Constitution places express limits on property taxation. Specifically, it limits taxing authorities to the taxation of tangible property, and a limited number of intangible assets specifically enumerated in Article XIII, §2. (Cal. Const., art. XIII, §2.) The only intangible assets subject to property taxation are "notes, debentures, shares of capital stock, bonds, solvent credits, deeds of trust, or mortgages," and "any legal or equitable interest therein." (*Ibid.*) In fact, the California Legislature has chosen not to tax any of the enumerated types of intangible assets or rights. (Rev. and Tax. Code, §212.) Therefore, all intangible assets are currently

either not subject to property taxation or exempt from property taxation under California law.

In this case, the parties agreed and the trial court expressly found that ERCs are intangible rights. (1 RT 57:1-2.) Article XIII, §2 mandates that intangible assets and rights cannot be taxed unless they are specifically enumerated within that section of the Constitution. ERCs are not. (See generally *Silicon Valley Taxpayers Ass'n v. Santa Clara County Open Space Auth.* (2008) 44 Cal.4th 431, 448 [holding that courts are charged with enforcing the provisions of the California Constitution and they "may not lightly disregard or blink at . . . a clear constitutional mandate."].)

A. This Court Upheld The Constitutional Property Tax Exemption for Intangible Rights In *Roehm*.

Intangible assets and rights are commonly associated with the value of real, personal and unitary property, whether the intangible right is a liquor license, a copyright, a franchise, an ERC, or one of many other intangible rights associated with the going-concern of a business. Accordingly, the question of how to uphold Article XIII, §2 of the Constitution by excluding the value of intangible assets and rights for property tax purposes has been the topic of numerous court decisions over the last sixty-plus years, beginning with this Court's seminal decision in *Roehm*. Decided in 1948, *Roehm* validated the constitutional prohibition

against property taxation of intangible rights, and it has remained a guiding principle on this important issue ever since.

The *Roehm* case posed the question of whether Orange County could assess a liquor license, an intangible asset, for property tax purposes. (See *Roehm*, 32 Cal.2d at p.281.) Applying Article XIII, §2, this Court held that a liquor license is not assessable, because it is an intangible right protected from taxation under the Constitution. (See *id.* at p.290.) As noted above, the *Roehm* Court interpreted Article XIII, Section 2 of the California Constitution as follows: "The first clause is a grant of power to the Legislature to provide for the assessment, levy, and collection of taxes, **but it does not grant power to provide for the taxation of intangible assets other than those listed**." (*Id.* at p.285, emphasis added.) Because liquor licenses are not included in the list of specified intangibles, the Court found that the taxpayer's liquor license was not assessable. (See *id.* at p.290.)

In *Roehm*, this Court recognized the public importance of its decision and acknowledged that its ruling would and should extend beyond liquor licenses to protect other intangible assets and rights from property taxation:

> **Virtually the same reasoning could be advanced for the taxation of other forms of governmental permits**, stock exchange seats, press association memberships, memberships in social, professional and fraternal clubs, patents, copyrights, goodwill, judgments, causes of action, and insurance policies, which have never been taxed as property in this state during

> its entire existence. These contentions therefore raise questions of **public importance** that involve numerous rights and privileges other than liquor licenses, **for the characteristics that it is claimed make liquor licenses taxable as property would likewise make numerous other rights and privileges taxable as property**.

(*Id.* at p.283, emphasis added.)

This appeal likewise addresses an issue of great public importance to numerous California taxpayers, a fact that is clearly reflected in the broad range of *amicus curiae* letters filed in support of EHP's petition for review. These letters were submitted by public policy tax associations, business trade associations, and individual property taxpayers.[7]

Also in *Roehm*, the Court explained the important policy underlying the constitutional exemption from taxation for intangibles. The Court went so far as to state that the taxation of intangible property would constitute "an impossibility." (*Id.* at p.288.) Commenting on the 1933 amendments to the California Constitution, which added the intangibles exemption, the Court observed: "It was precisely this evil which required remedial

[7] The following individual taxpayers and organizations submitted *amicus curiae* letters: California Taxpayers Association, Institute for Professionals in Taxation, California Chamber of Commerce, Council on State Taxation, California Cable and Telecommunications Association, California League of Food Processors, California Manufacturers and Technology Association, California Retailers Association, Industrial Environmental Association, National Federation of Independent Business, Time Warner Cable, and Western States Petroleum Association.

legislation, but it was an evil which legislation could not fully reach and remedy without a change in the state constitution." (*Ibid.*)

Roehm is predicated on recognition of "the policy of eliminating altogether property taxation of all intangibles except solvent credits and substituting therefor taxation of the income derived from such intangibles." (*Id.* at p.282, emphasis added.) In other words, the value of intangibles is taxed through the state income tax system, and should not be double-taxed through the property tax system. (See *Beery v. County of Los Angeles* (1953) 116 Cal.App.2d, 290, 298 & fn.1 [finding that income tax is in lieu of property tax on intangibles and intangibles are no longer taxable under property tax laws]; *County of Stanislaus v. Assessment Appeals Bd.* (1989) 213 Cal.App.3d 1445, 1453; Cal. Atty. Gen., Indexed Letter, No. 10485 (February 4, 1936), p. 3 ["The exemption from taxation of intangibles is conditioned only upon the passage or adoption of a net income tax act, and such an act having passed it seems to follow as a necessary conclusion that intangibles, except solvent credits, are no longer taxable, whether owned by individuals or corporations. Not being taxable, intangibles, other than solvent credits, owned by public utility corporations should not be assessed by the State Board of Equalization."].)

Roehm establishes that the prohibition against taxing intangible property is "clearly supported by the considerations of policy underlying

the amendments to the Constitution and the legislation pursuant thereto." (*Roehm*, 32 Cal.2d at p.287.) *Roehm* explains that property taxation is "supplemented . . . by taxes imposed upon or measured by net income including income derived from all kinds of intangible rights and privileges." (*Id.* at p.289.) Unequivocally, *Roehm* invalidates property taxation of intangible rights and privileges, while validating income taxation of associated earnings:

> It follows from the foregoing construction of the 1933 amendments to the Constitution and section 111 of the Revenue and Taxation Code [subsequently repealed] that only the intangibles therein specified are to be regarded as personal property for purposes of taxation. **Liquor licenses as well as other intangible values not included in the list of intangibles specified in that constitutional provision and in section 111 are therefore not subject to ad valorem taxation as personal property.**

(*Id.* at p.290, emphasis added.)

In *Michael Todd v. County of Los Angeles* (1962) 57 Cal.2d 684, this Court emphatically reinforced that policy. (*Id.* at p.691.) In *Michael Todd*, the taxpayer took an extreme position, arguing that, for property tax purposes, a copyrighted motion picture should be valued at "scrap" or "salvage value." (*Id.* at p.696.) In rejecting the taxpayer's position, the Court explained that property should be valued at its "highest and best" use. (*Ibid.*) The decision in *Michael Todd* is premised on the recognition that the presence of intangibles is assumed so that property can be valued at its beneficial and productive use and not (as urged by the taxpayer) as "scrap."

(*Ibid.*) Like the intangible liquor license in *Roehm*, however, the intangible motion picture copyright in *Michael Todd* was excluded from property taxation. (See *id.* at p.691.)

ERCs are among the intangible rights that fall within the ambit of protection against property taxation articulated by this Court in *Roehm* and *Michael Todd*. Notably, ERCs are very similar to liquor licenses or other government permits. Like a liquor license, an ERC is an intangible right that belongs to the business entity and does not relate to the property itself. Like a liquor license, which is "necessary" for the beneficial and productive use of a bar, restaurant or liquor store, an ERC is necessary for the beneficial and productive use of a power plant.

The following analogy illustrates how the court of appeal's Decision in this case radically deviates from this Court's seminal decision in *Roehm*. In this case, the Board's actions in expressly adding a cost component for ERCs is comparable to an assessor expressly adding a cost component for a liquor license to the value of a bar in assessing the tangible property. According to the Decision, if the value of a bar's real and personal property was determined to be $200,000 using the cost approach, and the cost of the liquor license was $50,000, an assessor would be justified in valuing the property at $250,000, and the owner would have to pay property taxes not only on the value of the tangible property, but also on the value of the

intangible asset simply because the liquor license is deemed "necessary" to the beneficial and productive use of the bar's tangible property. The result reached by applying the court of appeal's new test is plainly contrary to this Court's holding in *Roehm* that an intangible liquor license is not subject to property taxation under the Constitution. (*Roehm*, 32 Cal.2d at p.290.)

In this case, rather than applying this Court's holding in *Roehm*, the court of appeal erroneously relied upon the following dicta. (Decision, pp.25-26.)

> Intangible values, however, that cannot be separately taxed as property may be **reflected in** the valuation of taxable property. Thus, in determining the value of property, assessing authorities may *take into consideration* earnings derived therefrom, which may depend upon the possession of intangible rights and privileges that are not themselves regarded as a separate class of taxable property.

(Roehm, 32 Cal.2d at p.285, emphasis added.) This dicta cannot possibly be interpreted to mean that the entire value of a liquor license can be indirectly taxed as a matter of law – by expressly adding the cost of the liquor license to the cost of the associated bar – as the Board has done with the ERCs at issue here. Indeed, such an interpretation of the dicta in *Roehm* would eviscerate the *Roehm* holding.

As discussed at greater length below (pp.23-27, *post*), the 1995 amendments to Section 110 of the Revenue and Taxation Code codified *Roehm* and *Michael Todd*, and clarified both, by explaining that while the

"presence" (or existence) of intangible assets and rights necessary to the beneficial and productive use of tangible property may be **"assumed"** for purposes of property taxation – under Subdivision 110**(e)** – the **value** of such intangibles must still be **excluded** from property taxation – under Subdivision 110**(d)**. (Rev. and Tax. Code, §110(d) and (e).) It follows that the Decision must be reversed because a separate value component for intangible ERCs was intentionally added by the Board to EHP's unit value. The Fourth District's new test, which allows the taxation of intangible assets and rights deemed "necessary" to the beneficial and productive use of tangible property, directly undermines this Court's decisions in *Roehm* and *Michael Todd.*

The doctrine of *stare decisis* "is based on the assumption that certainty, predictability and stability in the law are the major objectives of the legal system." (*People v. Garcia* (2006) 39 Cal.4th 1070, 1080, quoting *Moradi-Shalal v. Fireman's Fund Ins. Cos.* (1988) 46 Cal.3d 287, 296.) This Court's decision in *Roehm* has been the law of this state for more than sixty years. There is no legal basis for this Court to deviate from its important holding in that case, which properly upheld the constitutional limitation on the property taxation of intangibles.

B. Section 110 Reaffirms The Constitutional Exemption For Intangibles.

Senate Bill 657, the Omnibus Property Tax Reform Act of 1995, codified *Roehm, Michael Todd,* and their progeny by amending Revenue and Taxation Code Sections 110 and 212, which address the property tax treatment of intangible assets. The amendments clarified existing law regarding how the full cash value of tangible real, personal and unitary property should be determined when associated intangible assets or rights are present, and how the value of such intangible assets and rights should be removed for property tax purposes. (2 CT 434, 439-440, 448.)

These amendments were enacted after appellate courts, in 1993 and 1994, rejected multiple attempts by taxing authorities, including the Board, to assess intangible property in five different contexts. (*Shubat v. Sutter County Assessment Appeals Bd.* (1993) 13 Cal.App.4th 794; *County of Orange v. Orange County Assessment Appeals Bd.* (1993) 13 Cal. App.4th 524; *Service America Corp.* v. *County of San Diego* (1993) 15 Cal.App.4th 1232; *County of Los Angeles* v. *County of Los Angeles Assessment Appeals Bd.* (1993) 13 Cal.App.4th 102; *GTE Sprint Communications Corp.* v. *County of Alameda* (1994) 26 Cal.App.4th 992.)

The relevant subdivisions of Section 110, as amended, provide:

> (d) Except as provided in subdivision (e), for purposes of determining the "full cash value" or "fair market value" of any taxable property, **all of the following shall apply**:
>
> > (1) The value of intangible assets and rights relating to the **going concern value of a business using taxable property shall not enhance or be reflected in the value of the taxable property**.
> >
> > (2) If the principle of **unit valuation** is used to value properties that are operated as a unit and the unit includes intangible assets and rights, then the fair market value of the taxable property contained within the unit **shall be determined by removing from the value of the unit the fair market value of the intangible assets and rights contained within the unit**.
> >
> > (3) The exclusive nature of a concession, franchise or similar agreement, whether de jure or de facto, is an intangible asset that shall not enhance the value of taxable property, including real property.
>
> (e) Taxable property may be assessed and valued by **assuming the presence of** intangible assets or rights necessary to put the taxable property to beneficial or productive use.
>
> (f) For purposes of determining the "full cash value" or "fair market value" of real property, intangible attributes of real property shall be reflected in the value of the real property. These intangible attributes of real property include **zoning, location, and other attributes that relate directly to the real property involved**.

(Rev. and Tax. Code, §110, emphasis added.) A copy of Section 110 – in its entirety – is attached to this brief.

This Court has explained the rules of statutory construction as follows:

> The fundamental rule of statutory construction is that the court should ascertain the intent of the Legislature so as to effectuate the purpose of the law. Moreover, "every statute should be construed with reference to the whole system of law of which it is a part **so that all may be harmonized and have effect." If possible, significance should be given to every word, phrase, sentence and part of an act in pursuance of the legislative purpose.**

(*Select Base Materials v. Board of Equalization* (1959) 51 Cal.2d 640, 645, quoting *Stafford v. Los Angeles Retirement Bd.* (1954) 42 Cal.3d 795, 799 (emphasis added); see also *Moyer v. Workmen's Comp. Appeals Bd.* (1973) 10 Cal.3d 222, 230.)

The key to deciding this case is in harmonizing the three relevant subdivisions of Section 110 – Subdivisions 110(d), (e) and (f) – and interpreting them in a manner that is consistent with the limitations prescribed by the California Constitution. In fact, these subdivisions can and should be interpreted in a constitutional and harmonious manner.

First, the three numbered subparts of Subdivision 110(d) set forth the general constitutional rule that intangible assets and rights are exempt from property taxation and that their presence shall not enhance or be reflected in the assessed value of tangible real and personal property. Under Subdivision 110(d), intangible assets and rights cannot even be considered in property taxation "except as provided in Subdivision 110(e)."

Second, Subdivision 110(e) cannot be construed to override the constitutional and statutory rule that the value of intangible assets and

rights must be excluded from the value of real and personal property for property taxation purposes. Rather, Subdivision 110(e) codifies the holding in *Michael Todd* and states that property must be valued at its highest and best use, rather than salvage value, and that assessors, including the Board, may "assume the presence" of intangibles that are necessary to the beneficial and productive use of tangible property. Accordingly, Subdivision 110(e) does apply in this case to the extent that the Board is permitted to **assume the presence** (or existence) of ERCs in valuing EHP's Plant at its highest and best use, which is as a functioning electric generation facility, rather than as a collection of equipment, valued at its "salvage" value.[8] (Rev. and Tax. Code, §110(e).)

Finally, Subdivision 110(f) does not apply here, because ERCs are not an "attribute" of real property like zoning, location, architecture and view. (Rev. and Tax. Code, §110(f).)

This is the proper construction of Section 110 in this case, because it harmonizes the three key subdivisions of the statute in a way that gives complementary meaning and legal effect to all three provisions. More

---

[8] Highest and best use is defined as the "[t]he most profitable use of a property at the time of the appraisal; that available use and program of future utilization that produces the highest present land value; must be legal, physically possible, financially feasible, and maximally profitable." (Assessment Appeals Manual (2003) p.13.)

importantly, it is the only construction that is consistent with the constitutional exemption.

II. THE COURT OF APPEAL'S DECISION CONTRAVENES THE CONSTITUTION, SECTION 110 AND *ROEHM.*

In this case, the parties agreed, and the trial court expressly found, that ERCs are intangible rights. (1 RT 57:1-2.) On that basis alone, ERCs cannot be taxed under the California Constitution and their value must be removed from the unit valuation of EHP's property under Subdivision 110(d)(2) of the Revenue and Taxation Code. The court of appeal misinterpreted Subdivision 110(e), in such a way as to override Subdivision 110(d). The Decision cannot be correct, because Subdivision 110(d)(2) is the very subdivision that the California Legislature specifically enacted to govern cases such as this that involve **unit valuation**.

Pursuant to Subdivision 110(d)(2), "[i]f the principle of unit valuation is used to value properties that are operated as a unit and the unit includes intangible assets and rights, then the fair market value of the taxable property contained within the unit, **shall be determined by removing from the value of the unit the fair market value of the intangible assets and rights contained within the unit.**" (Rev. and Tax. Code, §110(d)(2), emphasis added.) The Board's own Handbook properly describes the application of Subdivision 110(d)(2) as follows:

> Section 110(d)(2) indicates that if the principle of unit valuation is used to value taxable property, **then the fair market value of any intangible assets or rights contained within the unit must be removed**. This rule recognizes that a business enterprise value typically will contain many intangible assets and rights.

(1 CT 153, emphasis added.)

The adoption of Subdivision 110(d)(2) is arguably a direct codification of the First District court of appeal's decision in *GTE Sprint Communications Corp. v. County of Alameda* (1994) 26 Cal. App. 4th 992, which was a case involving both a state-assessee (like EHP) and property valued on a unitary basis (like the power plant here). (See *id.* at p.995.)

In *GTE Sprint*, the taxpayer provided the Board with "detailed evidence" identifying and separately valuing its intangibles. (See *id.* at p.998.) The Board deliberately disregarded that evidence and, as in this case, failed to exclude the value of the intangibles from its unitary assessment of Sprint's property. (See *id.* at pp.999, 1004) The Court held that the exclusion of the identified intangibles was required under California law: "[T]he Board's appraisers are required by law **to identify and value intangible assets**, if any, and **exclude these values from the appraisal of the taxpayer's property**." (*Id.* at p.999, emphasis added.) The Court concluded: "where the types of intangible assets identified by [the taxpayer] may reasonably be said to exist, the Board **must** exclude

their values when assessing the tangible property for taxation." (*Id.* at p.1007, emphasis added.)

This case is strikingly similar to the *GTE Sprint* case. Just as here, the Board in *GTE Sprint* took the position that "it was not directly taxing [the] intangible assets, but instead it was taxing the value of the tangible property as enhanced by the intangible values." (*Id.* at p.995.) As here, the Board in *GTE Sprint* ignored evidence presented by EHP, identifying and valuing the ERCs on the Board's own form, BOE Form 529-I, *Schedule of Intangible Information*. (See *id.* at p.999.) In *GTE Sprint*, the court of appeal held that such an approach was not acceptable:

> In our view the Board and its appraisers erred in assuming that unit valuation, especially when calculated by the CEA [capitalized earnings ability] method, necessarily taxes only the intangible values as they enhance the tangible property. **This absolutist approach obscures the Board's duty to exclude intangible assets from assessment.**
>
> . . .
>
> "The Board's definition of the unit usually includes items that are nontaxable . . . . Under the unit concept, the procedure is to estimate unitary value, then make the allocation between states (if any) **and then deduct from the allocated unit value the value of nontaxable items located within California**." (*The Appraisal of Public Utilities* (1981) pp.8-9.)

(*Id.* at p.1004-5, emphasis added.) Notably, in finding support for its position, the Court in *GTE Sprint* quoted and relied upon language contained in the Board's own Manual, "The Appraisal of Public Utilities

(1981)," which supports the practice of separately valuing and removing the income associated with intangibles.

Ironically, the Decision in this case cites *GTE Sprint* for the proposition that "an assessor cannot merely pay **lip service** to the concept of exempting intangible assets from taxation." (Decision, p.27, emphasis added.) However, the Board's actions in this case and the Fourth District's express approval of those actions disregard the First District's clear holding in *GTE Sprint* and subvert the constitutional exemption.[9]

A. The Court of Appeal's Holding Misconstrues Section 110 And Violates The Constitution.

The court of appeal acknowledged its proper role in interpreting Section 110: "When construing a statute, the courts will strive to harmonize and give effect to both constitutional and statutory provisions and will uphold the legislative act unless it clearly conflicts with a state

---

[9] Disregarding the holding in *GTE Sprint*, the Board relied below on the case of *American Sheds, Inc. v. County of Los Angeles* (1998) 66 Cal.App. 4th 384, a case involving site-specific operating permits, to justify its actions in this case. (Respondents' Brief, court of appeal, pp.31-32.) Notably, *American Sheds* did not involve a state-assessed taxpayer whose property is valued on a unitary basis like *GTE Sprint* and EHP. Moreover, in *American Sheds*, the Los Angeles County Assessor did not **add** a separate value component for the government permits like the Board did here. Instead, the assessor employed a royalty valuation method, which purposefully **excluded** income associated with the intangibles in that case. (*American Sheds*, 66 Cal. App. at 396, emphasis added.) The court concluded that the taxpayer failed to produce evidence that the assessor in fact assessed the taxpayer's intangibles. (See *id.* at p.395-96.) It did not repudiate the principle that intangibles may not be taxed.

constitutional provision." (Decision, p.15, citing *Professional Eng'rs in California Gov't v. Wilson* (1998) 61 Cal. App.4th 1013, 1025.) While correctly quoting this important rule of statutory construction, the court of appeal altogether failed to apply that rule and it interpreted Subdivision 110(e) in a way that creates a clear conflict with the Constitution.

The Court held that because ERCs are "**necessary**" to the beneficial and productive use of EHP's Plant, Subdivision 110(d) does not apply at all and the value of the ERCs need not be removed from the unitary value of the Plant, stating: "There is no basis to remove the value of the ERCs from the value of the unit, where the unit cannot legally operate without them." (Decision pp.39-40, emphasis added.) Earlier in its Decision, the court further described its new test: "We think that determining whether this **'necessary'** criteria is present, with respect to intangible assets relating to a given taxable property, will be the critical factor for determining whether section 110, subdivision (d) **or** subdivision (e) will govern the treatment of the intangible assets." (Decision p.20, emphasis added.)

The court of appeal was wrong in reasoning that only Subdivision 110(d) **or** Subdivision 110(e) could apply, and in ultimately determining that Subdivision 110(d)(2) – the subdivision specifically addressing unit valuation – does not apply to this case. The two subdivisions are not mutually exclusive; they are complementary. The court or appeal erred by

allowing Subdivision 110(e) to override Subdivision 110(d) – in this case and in countless others as well.

Specifically, the Decision misconstrues the introductory clause of Subdivision 110(d) – **"[e]xcept as provided in subdivision (e)"** – in such a way as (1) to promote Subdivision 110(e) to mean something more than its simple mandate that property be valued at its highest and best use, and (2) to demote Subdivision 110(d), which affirms the general constitutional exemption against taxing intangible rights. The introductory phrase to Subdivision 110(d) – "except as provided in Subdivision 110(e)" – simply means that when intangibles are necessary for the beneficial and productive use of tangible property, the property should be valued at its highest and best use by "assuming the presence" of those intangibles, but it does not negate the remainder of Subdivision 110(d).

For example, it should be is *assumed*, as a matter of law, that a business selling alcohol will obtain a liquor license. It is *assumed* that a commercial motion picture is copyrighted. It is *assumed* that a cable television company will obtain a franchise. Likewise, it is *assumed* that an electric generation facility will obtain ERCs. It is taken as a given – or *assumed* – that owners of business property capable of being put to productive or beneficial use will obtain those intangible rights or assets that are required to conduct that business. Since *Roehm*, it has been recognized

that presence of those intangible rights may be assumed, but the value of those intangible rights must be excluded from the assessed value of the tangible property.

The Board's own manual, *Assessors' Handbook 502*, unambiguously articulates the purpose of Subdivision 110(e):

> Sections 110(e) and 212(c) **do not authorize adding an increment** to the value of taxable property to reflect the value of intangible assets and rights necessary to put the taxable property to beneficial or productive use. Instead, these sections indicate that, in valuing taxable property, it is appropriate to **assume** the presence of the intangible assets and rights which are necessary to put taxable property to beneficial or productive use. . . . **Although the presence of the intangible assets are assumed in the valuation of the tangible property, this does not mean that their values are included in that valuation**.

(1 CT 153, emphasis added.)

Relying upon the Board's Handbook, the Second District court of appeal appropriately explained the distinction between "assuming" the presence of intangibles and assessing intangibles as follows:

> [S]ection 212, subdivision (c) provides that "the value of intangible assets and rights shall not enhance or be reflected in the value of taxable property." But subdivision (c) also provides that "[T]axable property may be assessed and valued by **assuming** the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use." (See also §110, subds. (d) & (e).)
>
> . . .
>
> The California State Board of Equalization Assessors Handbook explains the interaction of these two concepts: "**Even though intangible assets and rights are not subject to taxation**, the second fundamental principle states that

> tangible property should nonetheless be assessed and valued by **assuming** the presence of those intangible assets and rights that are necessary to put the tangible property to beneficial or productive use. Under this principle, an appraiser valuing tangible property must assume the presence of any intangible assets or rights necessary to the beneficial or productive use of the property being valued. **The 'beneficial or productive use' is equivalent to the highest and best use of the property**." (State Bd. of Equalization, Assessors' Handbook – Treatment of Intangible Assets and Rights (1998) p. 150.)

(*Watson Cogeneration Co. v. County of Los Angeles* (2002) 98 Cal. App.4th 1069-70, 1070, emphasis added.)

Similarly, in *County of Los Angeles v. Southern California Edison Co.* (2003) 112 Cal. App. 4th 1108, a case involving the valuation of an electric generation facility, the Second District court of appeal stated:

> County contends the real property value should include the value of operating permits and intangible assets essential to the operation of a plant and the going concern value of the plants as businesses. County cites no authority for these arguments.
> . . . . Property is valued for purposes of property tax by **assuming** the presence of intangible assets necessary to put the property to productive use, **but excluding the value of those intangible assets**, and also excluding the value of intangible assets relating to the going concern value of a business (Rev. and Tax. Code, §§110, subds. (d), (e), 212, subd. (c).)

(*Id.* at p.1122, emphasis added.)[10]

---

[10] EHP acknowledges that the *Southern California Edison* case involved a valuation for documentary transfer tax purposes, rather than property tax purposes, but it cites to the property tax law at issue here in reaching its decision. (Rev. and Tax. Code, §11935(b).)

The court of appeal's fundamental mistake in this case lies in its failure to understand that Subdivision 110(d) states the constitutional rule; namely, that intangible assets and rights are exempt from property taxation and their presence cannot enhance or be reflected in the valuation of tangible property. Subdivision 110(e) does not override that rule; rather, it provides that the presence of necessary intangibles can be assumed so that property can be valued at its highest and best use.

In no circumstances, however, does Subdivision 110(e) permit the Board or an assessor to **add a cost component** for "necessary" intangible rights to the value of the tangible property as the Board did here, or fail to remove intangible rights from a value calculated using an income approach. Simply put, Subdivision 110(e) does not permit the Board to "assume" the value of the "necessary" intangible assets or rights, it only permits the Board to "assume" their presence. In summary, Subdivision 110(e) does nothing more than allow the Board to value EHP's tangible property at its highest and best use as a functioning power plant, rather than as a random collection of equipment at its "salvage" value.

B. The Court of Appeal's Holding Contradicts The Applicable Legislative History.

As this Court has explained, its role in "interpreting or construing a statute is to ascertain and effectuate the legislative intent." (*Laurel Heights Improvement Ass'n v. Regents of Univ. of California* (1993) 6 Cal.4th 1112,

1127, citing *City of San Jose v. Superior Court* (1993) 5 Cal.4th 47, 54.) When appropriate, the court "will look to legislative history as an extrinsic aid" to assist the Court in its task. (*Ibid.*)

The court of appeal's Decision in this case acknowledges the importance of determining legislative intent in construing the amendments to Section 110: "In construing all these related statutory provisions, our task is to select the construction that comports most closely with the Legislature's apparent intent, with a view toward promoting rather than defeating the statutes' general purpose, and avoiding any construction that would lead to unreasonable, impractical or arbitrary results." (Decision, p.40, citing *Mejia v. Reed* (2003) 31 Cal.4th 657, 663; *Copley Press, Inc. v. Superior Court* (2006) 39 Cal.4th 1272, 1291.) Although the court of appeal paid lip-service to the importance of legislative intent, it disregarded the entire legislative history regarding the amendments to Section 110 in deciding this case.[11]

The Legislature did not intend that Subdivision 110(e) would negate Subdivision 110(d). The opposite is true. In a letter dated September 15,

---

[11] Inexplicably, the court of appeal refused to even consider the *amicus curiae* brief filed by California Taxpayers' Association ("Cal-Tax") below, which specifically addressed the legislative history underlying the 1995 amendments to Section 110, and provided a separate Appendix containing copies of the entire legislative history, along with a request for judicial notice. (See Order denying Cal-Tax's application for leave to file *amicus curiae* brief and request for judicial notice, dated December 23, 2010.)

1995, Senator Ken Maddy, author of the amendments at issue, explained the language of Subdivision 110(e) as follows:

> The bill provides that the intangible assets and rights relating to the going concern (such as goodwill and trade names) are not to be reflected in the value of property. However, under subdivision (e) of Section 110 of the Revenue and Taxation Code as added by the bill, property may be valued **assuming the existence** of intangible assets necessary to put the property to productive use. **This subdivision makes it clear that property need not be valued at salvage value but at its value when put to beneficial or productive use. For example, under the terms of the bill, an assessor could not use a liquor license to enhance the value of taxable property. However, the assessor may assume the presence of a license so that a bar's taxable property may be taxed as a bar and not at salvage value (i.e., as a warehouse).**

(2 CT 450, emphasis added.) As Senator Maddy explained, the purpose of adding Subdivision 110(e) was to permit the Board and local assessors to value property at its beneficial and productive use which, in Senator Maddy's words, requires them to "**assume the existence**" of certain intangible assets and rights. (Rev. and Tax. Code, §110(e).)

Nearly fifty years ago, this Court explained the meaning of the phrase "value of property when put to beneficial or productive use." (*Michael Todd,* 57 Cal.2d at p.696.) In *Michael Todd*, the Court explained that "market value" for assessment purposes was the "value of property when put to beneficial or productive use" and "not merely whatever residual value may remain after the property is demolished, melted down, or otherwise reduced to its constituent elements." (*Ibid.*) Under *Michael*

Todd, taxing authorities are permitted to value tangible property based on its market value when put to beneficial or productive use, and not simply at "salvage or scrap value." (*Ibid.*)

If the court of appeal had interpreted Subdivision 110(e) by considering the legislative intent – as it acknowledged is proper – it would not have misconstrued the statute as it did. Instead, it would have recognized that Subdivision 110(e) does not swallow Subdivision 110(d) or eviscerate the constitutional property tax exemption for intangible property. Rather, the Legislature merely intended for this Court's holding in *Michael Todd* to apply – property in California must be valued at its "beneficial and productive use." In this case, it merely means that EHP's property should be valued as a power plant. It does not mean that the cost or value of "necessary" intangible rights can be added or otherwise included, as here.

C. The Court Of Appeal's Holding Contravenes The Board's Interpretation of Section 110.

"Assessors' handbooks [published by the Board] have been relied upon by the courts and been accorded great weight in the interpretation of valuation questions." (*Watson Cogeneration Co. v. County of Los Angeles* (2002) 98 Cal.App.4th 1066, 1070, fn.2, citing *CAT Partnership v. County of Santa Cruz* (1998) 63 Cal.App.4th 1071, 1085, fn. 12; *Prudential Ins. Co. v. City and County of San Francisco* (1987) 191 Cal.App.3d 1142, 1155.)

Published by the Board in 1998, *Assessors' Handbook 502* contains a fifteen-page chapter entitled: "Treatment of Intangible Assets and Rights," which addresses how to remove the value of intangibles from the valuation of taxable property. (1 CT 151-166.) Notably, this chapter contains a table, listing "Examples of Intangible Assets and Rights," which includes the "**right to do business**." (1 CT 155.)

ERCs fall within this category of assets. ERCs grant an electric generation facility the "**right to do business**" as an electric generation plant. The intangible right to do business belongs to the business owner, not the land owner. The right to do business runs with the business, not with the land or other tangible property. The right to do business has specifically been identified as an intangible right that is not subject to assessment. (1 CT 155.) (*County of Stanislaus v. Assessment Appeals Bd.* (1989) 213 Cal.App.3d 1445, 1454.)

Just beneath the table of intangible assets and rights in *Assessors' Handbook 502* is a section entitled "Government Permits," which states:

> Other intangible rights, such as government permits to use property for particular purposes, usually represent potential economic benefits that could accrue to property owners. The holder of a special use permit, for example, has obtained the right to make a substantial income from the operation authorized on the property. **While the operator has generally made a substantial expenditure to obtain this special use permit which allows use of his or her property for a purpose which, absent such right, would be illegal on every other property in the county, the permit itself**

> **represents an intangible right that cannot be assessed for property tax purposes.** However, in the case of an intangible asset such as a special use permit which is necessary to put the property to beneficial or productive use, the taxable property may be assessed and valued by **assuming the presence** of the special use permit.

(1 CT 155-56, emphasis added.) Clearly, in its Handbook, the Board properly described the interrelationship between Subdivisions 110(d) and 110(e). Inexplicably, the Board ignored its own publication in assessing ERCs, which, like other type of government permits, convey the "right to do business," an intangible right the Board has repeatedly acknowledged is not subject to California property tax.

EHP reported the actual cost of its ERCs for each of the tax years on the Board's own form 529-I, "Schedule of Intangible Information." (1 CT 176-85.) Rather than removing the value of intangible ERCs from the unitary value, as it was required to do under Subdivision 110(d)(2), the Board deliberately added the value of ERCs to its assessment under the "replacement cost" approach in each of the tax years at issue. (1 CT 127:19-23; 137:17-19; 3 CT 507:2-6, 12-16; 512:17-513:11-16; 534-542.)

In addition, the Board failed to follow its own methodology for excluding value attributable to intangibles from its "capitalized earnings" [income] approach. Courts have recognized that, under an "income" approach to value, earnings necessarily emanate, in part, from intangible rights, and are not subject to property taxation. (See, e.g., *Los Angeles*

SMSA v. State Bd. of Equalization (1992) 11 Cal. App. 4th 768, 773.) Following the 1995 amendments to Section 110, the Board recognized the necessity of removing intangible value from an income approach, and it developed a specific methodology for that purpose, which is articulated in the Board's publication, "Unitary Valuation Methods." (3 CT 530-33.) As stated therein:

> When income to be capitalized is derived from operating a property, sufficient income shall be **excluded** to provide a return on any nontaxable operating assets **such as intangible items**.

(3 CT 533, emphasis added.) (See also Cal. Code Regs. Tit. 18, Chap. 1, Rule 8(e) ["When income from operating a property is used, sufficient income shall be excluded to provide a return on working capital and other nontaxable operating assets . . . ."].)

The Board failed to follow this stated methodology. During three of the tax years at issue herein, the Board used a "capitalized earnings" [income] approach to compute the unitary value of the Plant. In those three years, the Board undisputedly failed to follow its own procedure for removing ERCs from its calculations. (Board's Answer to Petition for Review, p.3.) The Board's actions clearly violate Subdivision 110(d)(2).

Finally, the Board ignored the advice of its own legal counsel regarding how ERCs should be treated in property taxation. In March of 2005, Kristine Cazadd, the Board's current Interim Executive Director and

former Chief Counsel, authored and distributed a Memorandum which concluded that ERCs are nontaxable (the "Cazadd Memorandum").[12] (1 CT 207-210.) The Cazadd Memorandum contained numerous legal citations to the California Constitution, the Revenue and Taxation Code, California case law, and the *Assessors' Handbook Section 502*. (*Ibid.*) Notably, the Cazadd Memorandum concluded:

> . . . **ERCs are analogous to liquor licenses or billboard use permits and are, thus, exempt from property taxation whether they are 'used' or 'banked.'** There is no conflict between the Revenue and Taxation Code provisions and the California Constitution or the Assessors' Handbook section 502, in this regard.

(1 CT 209, emphasis added.) The Cazadd Memorandum also warned:

> The current staff policy of treating ERCs as intangible attributes and including them in the taxable value of any property (including electric generation facilities) **violates the Constitution and statutory law. . . . The Board should adopt a clear policy that complies with the Constitution (as well as its own published advice) without waiting for a court order and risking the expense of litigation.**

(*Ibid.*, emphasis added.) Respectfully, the Board should have followed the advice of its counsel.

D. The Trial Court Improperly Relied Upon Subdivision 110(f), Which Does Not Apply Here.

While the court of appeal relied upon Subdivision 110**(e)** of the Revenue and Taxation Code in reaching its decision, the trial court relied

[12] Ms. Cazadd was Assistant Chief Counsel, Property Tax Division, at the time she authored this memorandum. (1 CT 212.)

upon subdivision 110**(f)**. (1 RT 57:2-9; 4 CT 833:17-22.) Subdivision 110(f) of the Revenue and Taxation Code provides as follows:

> For purposes of determining the "full cash value" or "fair market value" of real property, intangible attributes of real property shall be **reflected** in the value of the real property. These intangible attributes of real property include zoning, location, and other attributes that **relate directly** to the real property involved.

(Rev. and Tax. Code, §110(f), emphasis added.)

There are three reasons why Subdivision 110(f) does not support the Board's express addition of a value component for ERCs to the unitary value of EHP's Plant. First, Subdivision 110(d)(2) expressly requires removal of **all** intangible assets and rights from the unitary property, and Subdivision 110(f) must be read in harmony with that subdivision, not interpreted in such a way as to negate it. Second, Subdivision 110(f) provides that certain intangible rights shall be "**reflected**" in the value of the property, but it does not authorize the express addition of a cost component associated with intangible rights, which is what undisputedly occurred in this case. Third, Subdivision 110(f) expressly applies only to intangible **"attributes"** that **"relate directly"** to the real property. The statute gives examples of such attributes, which include location and zoning. Location, zoning, view, architecture, soil condition, and other physical characteristics are integral parts of the value of real property, and it is impossible to assign a separate value to such attributes. Therefore,

Subdivision 110(f) recognizes that these limited attributes – characteristics that are inherent in, and inseparable from, real property – may be "reflected" in the value of the real property.[13]

An explanation taken directly from the Board's own publication, Assessors' Handbook 502, is helpful in understanding what Subdivision 110(f) means:

> As additional examples, the presence of an ocean view, the proximity to a sewage treatment plant, or the convenient access to public infrastructure (*e.g.*, freeways) or services (*e.g.*, garbage collection) may all be considered intangible attributes of the real property. **These items also will be inherent in the physical location of the property**.
>
> . . .
>
> In contrast to intangible attributes of real property, intangible assets and rights of the business operation utilizing the real property **cannot** enhance or be reflected in the value of the real property. A **liquor license** associated with the current use of the real property as a bar or liquor store is **not** an intangible attribute of real property, but is a **non-taxable intangible asset or right of the business operation. Franchises, permits and licenses to operate a cable television system likewise are non-assessable intangible rights and assets, and not assessable attributes of the physical property** used to conduct the cable television business.

(1 CT 156-57, emphasis added.)

---

[13] The trial court mistakenly found that the present case was analogous to *Mitsui Fudosan Inc. v. County of Los Angeles* (1990) 219 Cal. App. 3d 525. (4 CT 842:5-8; 1 RT 56:28-57:1.) The trial court failed to understand that ERCs are not at all like TDRs, which arise directly from the ownership of real property, and which also run with the land.

The examples of intangible attributes listed in Subdivision 110(f) and in the Assessors' Handbook (*e.g.*, zoning, location, ocean view, proximity to a sewage treatment plant, access to public infrastructure or services) are fundamentally different from non-assessable, intangible assets and rights of a business enterprise (*e.g.*, liquor licenses, franchises, permits, and licenses to operate). Clearly, government-issued credits, such as ERCs, are more analogous to the latter group because they "permit" the enterprise the "right to do business." In this case, the ERCs permit EHP to operate as an electric generation facility. Equally clearly, ERCs are not a physical attribute of the real property. Rather, ERCs arise from the operating characteristics of the business enterprise, and are not tied to any specific real property. (1 CT 126:5-10; 127:3-7, 143:16-18.) When conveyed to the purchaser, no real property rights are transferred. In fact, under Health and Safety Code §40710, no property rights whatsoever are conveyed. (Health & Safety Code, §40710.)

In *Shubat v. Sutter County Assessment Appeals Board* (1993) 13 Cal.App.4th 794, the Third District recognized this important distinction between **intangible attributes** of real property that are inherent to and inseparable from a specific land parcel, and **nontaxable intangible rights** that relate directly to the business enterprise. Similar to the Board's argument to the trial court in this case, the Assessor in *Shubat* argued that

franchise rights and going-concern value were akin to zoning, location, view and architecture, and, therefore, could be "subsumed" within the value of the taxable property of the cable television company. (See *id.* at p.803.) The Third District dismissed the Assessor's argument as follows:

> This argument too is frivolous. There is a fundamental distinction between the attributes identified by the Assessor and the intangibles involved in this dispute. Zoning, location and other such attributes **relate directly to the real property** involved. They are an integral part of and effectively define it. By contrast, intangibles such as going concern value or franchise rights **relate to the business being conducted on the real property**. They relate to the real property only in their connection with the business using it.

(*Id.* at p.803, emphasis added.)

ERCs do not "relate directly to the real property" like zoning, view, architecture and location. Rather, they relate solely to the business enterprise conducted on the real property – electric power generation. Hypothetically speaking, if EHP's business was to close, the District would have to return the ERCs to EHP, and EHP could thereafter sell, lease or trade those ERCs on the open market, or bank them for future use. (1 CT 126:5-10; 127:3-7, 143:16-18.) Likewise, if federal or District emission requirements were to change, or if EHP was able to install improved pollution control devices, the District could likewise return ERCs to EHP for sale, leasing, trading or banking. Thus, it is entirely possible the Plant could be sold separate and apart from the ERCs.

Such a hypothetical sale illustrates that ERCs do not attach directly to a particular parcel of real property. Nor are ERCs "attributes" of real property. Rather, ERCs are entirely separate from the property, and can be independently bought sold, leased or banked for future use. (1 CT 126:5-10; 127:1-10; 143:16-19.) Therefore, ERCs cannot be reflected in the unitary value of the Plant under Subdivision 110(f).

III. THIS COURT SHOULD REVERSE THE COURT OF APPEAL'S INCORRECT DECISION.

A. The Decision Adversely Affects Taxpayers Who Own Intangible Assets.

As mentioned previously (*ante,* p.23), there were five appellate court decisions in the years immediately preceding the amendments to Section 110, each testing the prohibition against property taxation of intangibles. (2 CT 439-440.) In each of those cases, appellate courts rejected attempts by the Board or county assessors to assess intangible assets and rights. In amending Section 110 of the Revenue and Taxation Code, the Legislature sought to codify those (and other) holdings. (*Ibid.*)

First, in *Shubat v. Sutter County Assessment Appeals Bd. No. 1* (1993) 13 Cal. App.4th 794, the Third District held that a cable television company's "right to do business," which included its favorable franchise terms, was an intangible right exempt from property taxation under the Constitution and *Roehm*. (*Id.* at pp.802-04.)

Second, in *County of Orange v. Orange County Assessment Appeals Bd. No. 1* (1993) 13 Cal. App.4th 524, another cable television case, the Fourth District determined that the assessor's method of valuing the taxpayer's tangible property improperly captured "intangibles which are not subject to taxation such as existing franchises or licenses to construct . . . going concern value, and goodwill." (*Id.* at p.533.)

Third, in *Service America Corp. v. County of San Diego* (1993) 15 Cal.App.4th 1232, the Fourth District, again based on *Roehm*, held that a ballpark concession company's "concession agreement and its going-business value" were not taxable. (*Id.* at p.1242.)

Fourth, in *County of Los Angeles v. County of Los Angeles Assessment Appeals Bd.* (1993) 13 Cal. App.4th 102, the Second District likewise found that a rental car company's concession rights were "valuable but intangible business opportunities" and could not be assessed. (*Id.* at p.113.)

Fifth, as discussed previously, the First District decided *GTE Sprint* in 1994, the year immediately preceding the amendments to Section 110, holding that intangible rights owned by a unitary taxpayer had to be removed from the valuation of the unit. (*GTE Sprint,* 26 Cal.App.4th at p.999.)

The holdings from all five of these cases are now effectively codified by Revenue and Taxation Code Section 110(d)(1),(2) and (3). However, each of these cases would be decided differently under the Fourth District's new test. According to the Decision, if franchises, concession rights, licenses to construct and other "right to do business" intangibles are "necessary" to the beneficial and productive use of real and personal tangible property – which they inevitably are – then their value can be expressly added to the value of the taxable real and personal property.

In other words, the court of appeal's Decision in this case effectively eviscerates all three subparts of Subdivision 110(d), and calls into question the many holdings from various districts that the 1995 amendments codified. If the Decision is left intact, business taxpayers throughout the State of California are at risk of having their intangible rights – including franchises, concession rights, licenses and other intangibles granting the "right to do business" – assessed for property tax purposes. In the area of tax law at least, there are compelling reasons not to change the rules in a way that undermines settled expectations.

For more than half a century, the law of California, as articulated by this Court, has been clear and unambiguous – intangible assets and rights are not subject to property taxation. The cases decided by this Court, together with many others decided by the appellate courts throughout

California over the last sixty-plus years, are entitled to deference in the interpretation of Section 110. That statute was expressly amended in 1995 to codify the legal principles articulated in these cases, and taxpayers are entitled to rely upon that law. In summary, there is no reason why the Board cannot follow existing California law and stop assessing ERCs.

B. There Are Sound Public Policy Reasons Underlying The Constitutional Exemption For Intangibles.

As this Court explained over sixty years ago in *Roehm*, intangible assets and rights that are associated with the operation of a business enterprise should be (and are) taxed to the business through California's state income tax rather than through property tax. (*Roehm*, 32 Cal.2d at p.289.) One of this Court's three decisions dealing with the constitutional exemption of intangibles dealt specifically with the issue of "business" value. In *De Luz Homes*, this Court held that the exemption against taxing intangibles extended to the valuation of a business. (*De Luz Homes*, 45 Cal.2d at pp.565-66.) Indeed, that holding was part of what the Legislature codified in Section 110, explicitly prohibiting the taxation of a business when valuing its tangible real and personal property. (Rev. and Tax. Code, §110(d)(1) ["The value of intangible assets and rights relating to the **going concern value of a business** using taxable property shall not enhance or be reflected in the value of the tangible property."], emphasis added.)

In the field of appraisal, the distinction between intangible "going-concern" value and the value of tangible property is likewise recognized. For example, the leading treatise on the subject, *The Appraisal of Real Estate* (13th ed.), devotes a significant part of Chapter Two to the importance of identifying the property interests to be valued, and it has an entire section that discusses the concept known as "Business Value." (*Id.* at pp.29-31.) Specifically, the treatise notes:

> For certain types of properties (*e.g.*, hotels and motels, restaurants, bowling alleys, manufacturing enterprises, athletic clubs, landfills), the physical real estate assets are integral parts of an ongoing business. The market value of such a property (including all the tangible and intangible assets of the going concern, as if sold in aggregate) is commonly referred to by laymen as *business value* or *business enterprise value*, but in reality it is market value of the going-concern, including real property, personal property and the intangible assets of the business.
>
> * * *
>
> **Going-concern value includes the incremental value associated with the business concern, which is distinct from the value of the tangible real and personal property.**

(*Id.* at p.29, emphasis added.) Although there is little dispute that businesses often have "going-concern" value above and beyond the value of their tangible real and personal property, it is only the tangible real, personal and unitary property that is subject to taxation in California.[14]

---

[14] California is hardly alone in having a Constitution that prohibits the taxation of intangible assets and rights. The vast majority of states in this country (at least 33) have either statutory or constitutional provisions in

The classic example of this important distinction in the property tax arena is the valuation of a hypothetical hamburger stand. Two identical buildings, both of which were built at the same time, and both of which are equipped with the personal property necessary to prepare and sell food, might be located on different corners at the same intersection. One bears the name of its owner, "Joe's Hamburgers" and the other is franchised by "McDonald's." For property taxation purposes, the law in California (as elsewhere), requires that these two "identical" properties be valued comparably, so as to ensure "equalization," "uniformity" and non-discrimination in the application of the state's tax laws. (Cal. Const., art. XIII, §1.) However, one of these two "businesses enterprises" has a distinct advantage derived from years of advertising, as well as goodwill and customer loyalty associated with McDonald's "intangible" brand. That is the core reason why – for property tax purposes – the "business enterprise" value is not taxed. Thus, to the extent one of these two businesses is more profitable, it will pay more than the other in state income taxes, but the tangible property should be taxed the same.[15]

---

place to prevent the taxation of such property. A list of citations to the laws of those 33 states can be provided, if necessary.

[15] Other examples could also be cited, such as hotels and resorts where the "brand" determines occupancy rates (*e.g.*, a "Marriott" hotel versus a "Day's Inn"), or the profitability of a retail center anchored by a "Nordstrom" store versus a "Wal-Mart" store.

In *Roehm*, this Court acknowledged that the taxation of intangibles could result in the non-reporting or concealment of valuable intangibles. (See *Roehm*, 32 Cal.2d at p.290 [noting that the taxation of intangibles might "induce taxpayers to convert highly taxable intangibles into tax-free intangibles or to conceal them."].) By way of example, the *Roehm* court hypothesized that "subjection of patents or copyrights to such taxes would lead to the transfer of such rights to foreign corporations in exchange for corporate stock specifically exempted from property taxation by section 212 of the Revenue and Taxation Code." (*Ibid.*)

As noted earlier, in *Roehm*, this Court also observed that the taxation of intangible rights and assets is "an administrative impossibility and an ethical monstrosity." (*Id.* at p.288.) Indeed, the administrative burdens associated with trying to identify, value and then tax all "intangibles" would be significant. As it is, the Board has adopted numerous provisions to deal with the requirement ***not*** to value and tax intangibles. One can only imagine how much more work would be required to set-up a system first to identify and then to determine values for countless intangibles, let alone the litigation that would ensue over such a significant change in California law.

Finally, another reason for following what has been clear law in California regarding the taxation of intangibles such as the ERCs at issue here is a policy that is much more current. In recent years, there has been a

significant emphasis in the enactment of laws to encourage the development of so-called "green energy." In fact, this emphasis is manifest in the very legislation that created ERCs, and which requires them to be purchased and surrendered in the operation of a power plant.[16]

If ERCs and other similar eco-supportive intangible rights become subject to property taxation in California, the court of appeal's Decision will create a significant disincentive to property owners purchasing such intangible rights. Hence, this Court's ultimate decision about how emission-related "credits" such as ERCs should be treated for property tax purposes could very well have an adverse impact on the implementation of such environmental programs.

CONCLUSION

ERCs are not assessable because they are intangible rights that are exempt from taxation under the California Constitution. (Cal. Const., art. XIII, §2.) Moreover, the California Legislature has statutorily mandated that the value of these intangible ERCs must be removed from the unitary value of EHP's Plant. (Rev. and Tax. Code, §110(d)(2).) The court of appeal misinterpreted Subdivision 110(e) of the Revenue and Taxation

---

[16] As the Court is aware, California recently enacted so-called "cap-and-trade" legislation (AB32, now codified as Health and Safety Code §38500), which implicates the purchase and sale of intangible "carbon **credits**." The legislation introducing ERCs and the more recent cap-and-trade law are both aimed at reducing emissions and protecting the environment.

Code in contravention of the Constitution, Subdivision 110(d) and *Roehm*. For these reasons, this Court should reverse the court of appeal's Decision in favor of the Board and remand this case for entry of judgment in favor of EHP as a matter of law.

RESPECTFULLY SUBMITTED this 21st day of October, 2011.

LAW OFFICE of PETER MICHAELS
Peter W. Michaels

and

GIBSON, DUNN & CRUTCHER, LLP
Julian W. Poon
Blaine H. Evanson

and

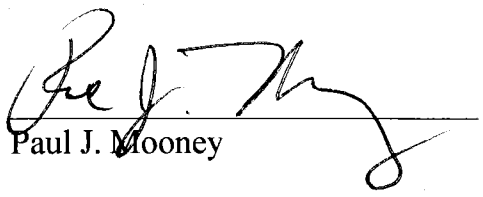
MOONEY, WRIGHT & MOORE, PLLC

By: _____
Paul J. Mooney (*Pro Hac Vice*)
Attorneys for Plaintiff/Appellant EHP

CERTIFICATE OF WORD COUNT

Pursuant to Rule 8.204(c) of the California Rules of Court, I hereby certify that this brief contains 12,993 words, including footnotes, but excluding the Table of Contents, the Table of Authorities, the statement of the "Issue Presented for Review," Certificate of Service, this Certificate of Compliance, and any attachments. I have relied on the word count of the computer program used to prepare the brief.

RESPECTFULLY SUBMITTED: October 21, 2011.



Paul J. Mooney

CERTIFICATE OF SERVICE BY MAIL

Elk Hills Power, LLC v. California State Board of Equalization, et al.

Supreme Court No. S 194121

(Court of Appeal No. D056943)

(Superior Court Case No. 37-2008-00097074-CU-MC-CTL)

1. At the time of service I was at least 18 years of age and not a party to this legal action.

2. My business address is 1201 S. Alma School Rd., Ste. 16000, Mesa, AZ 85210.

3. On October 21, 2011, I hand-delivered the original and thirteen (13) copies of:

   Appellant's Opening Brief

   in a FedEx box to the FedEx location in Phoenix, Arizona, for overnight delivery to the Clerk of the California Supreme Court, as expressly authorized by Rule 8.25(b)(3)(B) of the California Rules of Court. The FedEx box was addressed as follows: Clerk, Supreme Court of California, 350 McAllister Street, San Francisco, California 94102-4797.

4. On October 21, 2011, I also enclosed copies of

   Appellant's Opening Brief

   in envelopes and deposited the sealed envelopes with the U.S. Postal Service, with the postage fully prepaid. The envelopes were addressed as follows:

Tim Nader, Esq. Deputy Attorney General 110 West A Street, Suite 1100 San Diego, CA 92101 *Attorneys for Defendant and Respondent, California State Board of Equalization* (619) 645-2210	2 copies

Jerri S. Bradley, Esq. Deputy County Counsel County of Kern 1115 Truxtun Ave., 4th Floor Bakersfield, CA 93301 *Attorney for Defendant/Respondent, Kern County* (661) 868-3819	2 copies

5. I am a resident of or employed in the county where the mailing occurred. The mailed documents were sent from Mesa, Arizona.

I declare under penalty of perjury, according to the laws of the State of California, that the foregoing is true and correct.

Date: October 21, 2011

Kim Simonis
Printed Name

Signature

California Revenue and Taxation Code Section 110

(a) Except as is otherwise provided in Section 110.1, "full cash value" or "fair market value" means the amount of cash or its equivalent that property would bring if exposed for sale in the open market under conditions in which neither buyer nor seller could take advantage of the exigencies of the other, and both the buyer and the seller have knowledge of all of the uses and purposes to which the property is adapted and for which it is capable of being used, and of the enforceable restrictions upon those uses and purposes.

(b) For purposes of determining the "full cash value" or "fair market value" of real property, other than possessory interests, being appraised upon a purchase, "full cash value" or "fair market value" is the purchase price paid in the transaction unless it is established by a preponderance of the evidence that the real property would not have transferred for that purchase price in an open market transaction. The purchase price shall, however, be rebuttably presumed to be the "full cash value" or "fair market value" if the terms of the transaction were negotiated at arms length between a knowledgeable transferor and transferee neither of which could take advantage of the exigencies of the other. "Purchase price," as used in this section, means the total consideration provided by the purchaser or on the purchaser's behalf, valued in money, whether paid in money or otherwise. There is 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, exclusive of that lien amount, involved in the transaction. This presumption may be overcome if the assessor establishes by a preponderance of the evidence that all or a portion of the value of those improvements is not reflected in that consideration. If a single transaction results in a change in ownership of more than one parcel of real property, the purchase price shall be allocated among those parcels and other assets, if any, transferred based on the relative fair market value of each.

(c) For real property, other than possessory interests, the change of ownership statement required pursuant to Section 480, 480.1, or 480.2, or the preliminary change of ownership statement required pursuant to Section 480.4, shall give any information as the board shall prescribe relative to whether the terms of the transaction were negotiated at "arms length." In the event that the transaction includes property other than real property, the change in ownership statement shall give information as the board shall prescribe disclosing the portion of the purchase price that is allocable to all elements of the transaction. If the taxpayer fails to provide the prescribed information, the rebuttable presumption provided by subdivision (b) shall not apply.

(d) Except as provided in subdivision (e), for purposes of determining the "full cash value" or "fair market value" of any taxable property, all of the following shall apply:

(1) The value of intangible assets and rights relating to the going concern value of a business using taxable property shall not enhance or be reflected in the value of the taxable property.

(2) If the principle of unit valuation is used to value properties that are operated as a unit and the unit includes intangible assets and rights, then the fair market value of the taxable property contained within the unit shall be determined by removing from the value of the unit the fair market value of the intangible assets and rights contained within the unit.

(3) The exclusive nature of a concession, franchise, or similar agreement, whether de jure or de facto, is an intangible asset that shall not enhance the value of taxable property, including real property.

(e) Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use.

(f) For purposes of determining the "full cash value" or "fair market value" of real property, intangible attributes of real property shall be reflected in the value of the real property. These intangible attributes of real property include zoning, location, and other attributes that relate directly to the real property involved.