

CALIFORNIA SUPREME COURT

PROPERTY TAX TREATMENT OF
INTANGIBLE ASSETS AND RIGHTS

ELK HILLS POWER (2013)

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CALIFORNIA REVENUE AND TAXATION
CODE SECTION 212

➤ **Revenue and Taxation Code §212(c):**

Intangible assets and rights are exempt from taxation and, except as otherwise provided in the following sentence, **the value of intangible assets and rights shall not enhance or be reflected in the value of taxable property.** 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.

ASSESSORS' HANDBOOK 502 (Advanced Appraisal)

Government Permits:

"... 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.** . . ." (pages 154 155)

EMISSION REDUCTION CREDITS



SUPREME COURT DECISION ELK HILLS POWER (COST APPROACH)

➤ *Board Improperly Assessed Elk Hills's ERCs Under the Replacement Cost Approach*

- ✓ "... [the Board] impermissibly added the fair market value of the ERCs to the unit whole as part of its replacement cost valuation, and then failed to deduct that value prior to assessment. (§ 110(d)(1), (2).) **In failing to deduct the fair market value of the ERCs, the Board directly taxed Elk Hills's intangible right in violation of section 212(c).**

SUPREME COURT DECISION ELK HILLS POWER (INCOME APPROACH)

➤ *Board Properly Assumed the Presence of the ERCs Under the Income Capitalization Approach*

- ✓ "There are two lines of income capitalization cases that illustrate when a section 110(d)(2) **deduction is and is not required.**"
- ✓ "... the value of intangibles that directly enhance that income stream cannot be subsumed in the valuation of taxable property (§ 110(d)(1)), and must be deducted from the unit prior to assessment (§ 110(d)(2)).
- ✓ "...intangible assets like the **goodwill** of a business, **customer base**, and **favorable franchise terms or operating contracts** all make a **direct contribution** to the going concern value of the business as reflected in an income stream analysis. Only the latter category of intangible assets and rights has a **quantifiable fair market value that must be deducted from an income stream analysis prior to taxation.**

ELK HILLS POWER v. CALIFORNIA STATE BOARD OF EQUALIZATION

➤ “DIRECT” INTANGIBLE ASSETS and RIGHTS

- ✓ franchise rights
- ✓ right to do business
- ✓ goodwill
- ✓ trademarks
- ✓ patents
- ✓ favorable contracts and licenses
- ✓ customer lists
- ✓ work force
- ✓ brands

SUPREME COURT DECISION ELK HILLS POWER (INCOME APPROACH)

➤ “INDIRECT” INTANGIBLE ASSETS and RIGHTS

- ✓ “... under an income stream approach, not all intangible rights have a quantifiable fair market value that must be deducted.”
- ✓ “The difference is one of degree; intangible rights . . . merely allow for the taxable property to generate income when put to its beneficial or productive use. **Thus, their contribution to the income stream is indirect...**”
- ✓ “Elk Hills has not articulated a basis for attributing to the surrendered ERCs a separate stream of income related to enterprise activity, or indeed any separate stream of income at all.”
- ✓ Burden of proof
 - Isolate and quantify “baked-in” earnings attributable to intangibles
 - Liquor license?!?!?