

No. 42558-1-II

IN THE COURT OF APPEALS  
OF THE STATE OF WASHINGTON  
DIVISION II

\_\_\_\_\_  
GRAYS HARBOR ENERGY LLC

Plaintiff/Appellant,

v.

GRAYS HARBOR COUNTY

Defendant/Respondent.

\_\_\_\_\_  
ON APPEAL FROM THURSTON COUNTY SUPERIOR COURT

THE HONORABLE CAROL MURPHY, JUDGE

\_\_\_\_\_  
BRIEF OF RESPONDENT  
\_\_\_\_\_

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## **I. INTRODUCTION**

Respondent Grays Harbor County (hereafter, “the County”), for the most part, agrees with appellant Grays Harbor Energy LLC’s (hereafter, “Grays Harbor Energy”) introductory statement at pages 1-2 of its opening brief. The County has not identified a previous reported appellate case directly addressing the sole issue presented in this appeal. But applicable statutory and administrative provisions, as well as the unambiguous language in WAC 458-12-342 will lead this Court to conclude, as did the trial court correctly below, that WAC 458-12-342(1) does not exempt Grays Harbor Energy’s personal property from assessment and taxation while its power plant was considered “new construction.”

## **II. ASSIGNMENTS OF ERROR**

Grays Harbor Energy assigns error to two Thurston County Superior Court holdings in the trial court’s August 12, 2011 Order Denying Plaintiff Grays Harbor Energy LLC’s Motion for Entry of Judgment on Property Tax Refunds, and ruling that WAC 458-12-342(1) has no application to this case. Appellant’s Opening Brief at 2.

## **III. RESTATEMENT OF THE ISSUE**

The following issue is raised by Grays Harbor Energy’s assignments of error:

1. Whether the trial court correctly held that WAC 458-12-342(1) does not preclude assessment or taxation of the taxpayer's personal property during periods when its electrical generation facility was unfinished or "new construction."

Analysis of relevant authorities will compel this court to hold, as did the Thurston County Superior Court below, that WAC 458-12-342(1) has no application to assessment or taxation of its personal property and does not exempt Grays Harbor Energy's personal property from assessment or taxation while its plant remained unfinished.

#### **IV. RESTATEMENT OF THE FACTS**

The facts material to the issue before the court here are essentially undisputed. The County agrees with the facts stated in Section IV (A) of Grays Harbor Energy's opening brief concerning the sale and acquisition of its Grays Harbor power plant near Elma, Washington. Appellant's Opening Brief at 3-4.

The County does not believe the sale price is material to the issue of law presented in this appeal. See Appellant's Opening Brief at 4. Grays Harbor Energy's plant was completed and commenced operation in 2007. Its plant remained in a partially constructed state on the four assessment dates in question, January 1 of 2004, 2005, 2006, and 2007, in question. See Appellant's Opening brief at 6. However, the County does not believe that the statements contained in Section IV (B) of Grays

Harbor Energy's opening brief are entirely accurate or even relevant to determination of the issue of whether WAC 458-12-342(1) precludes assessment or taxation of Grays Harbor Energy's personal property during the time its electrical generation plant remained unfinished. Appellant's Opening Brief at 5-6.<sup>1</sup>

The County concurs with the procedural history of this case described in Sections IV (C) and (D) of Appellant's Opening Brief at pages 6-11.

## V. STANDARD OF REVIEW

Grays Harbor Energy properly characterizes the trial court's order below, in its opening brief at page 11, as treating Grays Harbor Energy's Motion for Judgment on Property Tax Refunds as "essentially a motion for summary judgment." VRP 19<sup>2</sup> Since the issue for review here also involves interpretation of an agency rule (WAC 458-12-342), interpretation of an agency rule is a question of law reviewed de novo. *Cobra Roofing Service, Inc. v. Department of Labor and Industries*, 122 Wn. App. 402, 409, 97 P.3d 17 (2004) ("[w]e interpret agency regulations as if they were statutes . . . [and] review the . . . regulation de novo");

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<sup>1</sup> For example, the assertion that, "[h]ad the project been cancelled, the remainder of the equipment would have been scrapped" is speculative and remains an issue of fact to be determined by the trial court below on remand. See Appellant's Opening Brief at 6. See also, Footnote 14, *post*.

<sup>2</sup> A copy of the trial court's August 12, 2011 Verbatim Report of Proceedings is attached to Grays Harbor Energy's opening brief filed in this case.

*Western Washington Operating Engineers Apprenticeship Committee v. Washington State Apprenticeship and Training Council*, 130 Wn. App. 510, 518, 123 P.3d 533 (2005) (“[w]e review the regulations and statutes . . . de novo”). Further, the court’s interpretation of an agency rule cannot create an absurd result. 130 Wn. App. at 518.

## **VI. SUMMARY OF ARGUMENT**

WAC 458-12-342(1) clearly and unambiguously applies only to assessment of real property and does not provide for any exemption from property tax assessment or taxation, whether for real or personal property. In any case, tax exemptions are creatures of statutes for the legislature to adopt, not for state agencies such as the Department of Revenue (“DOR”) to impose.<sup>3</sup> See WAC 458-16-100(2)(f) (“Property shall be exempt from taxation only when the legislature has created an exemption by clear and explicit language.”) A tax exemption cannot be imposed by DOR regulation.<sup>4</sup> Grays Harbor Energy’s personal property is thus neither exempt from assessment nor taxation under WAC 458-12-342(1), nor even falls within this rule’s application.

This Court determined in *Grays Harbor Energy, LLC v. Grays Harbor County*, 151 Wn. App. 550, 213 P.3d 609 (2009), review denied,

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<sup>3</sup> “Such property as the legislature may by general laws provide shall be exempt from taxation.” Wash. Const. Art. VII, § 1.

<sup>4</sup> See Footnote 11, *post*.

168 Wn.2d 1014, 227 P.3d 852 (2010) (“*Grays Harbor I*”) that under RCW 84.12.200(12) and RCW 84.12.280, “all of [Grays Harbor Energy’s] operating property, other than its land and buildings, should be assessed and taxed as personal property.” 151 Wn. App. at 554. The Court did not address Grays Harbor Energy’s argument with respect to WAC 458-12-342(1) here.<sup>5</sup>

WAC 458-12-342(1) has no application to assessment or taxation of Grays Harbor Energy’s personal property irrespective of the state of completion of its power plant on the assessment dates in question.

## VII. ARGUMENT

### A. **WAC 458-12-342 does not address assessment or taxation of personal property and, by its clear terms, applies only to real property during “new construction.”**

The only issue for review in this case remains Grays Harbor Energy’s claim that WAC 458-12-342(1) exempts personal property from assessment or taxation during the years when its facility is “new construction.” Appellant’s Opening Brief at 3. WAC 458-12-342(1)

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<sup>5</sup> Grays Harbor Energy’s assertion that the County did not respond to its allegations regarding WAC 458-12-342(1) in its *Grays Harbor I* briefing is misleading. See Appellant’s Opening Brief, Footnote 18, at 12. Although Grays Harbor Energy mentions its same interpretation of the rule in passing in its Brief of Respondent filed July 21, 2008, it did not identify this issue for the Court in either an assignment of error or its statement of issues, thereby failing to “flag” this issue for the Court. The County’s focus was on the proper classification of Grays Harbor Energy’s property as real or personal. Since the Court held that all of its property, except for land and buildings, is properly assessed and taxed as personal property under RCW chapter 84.12, WAC 458-12-342(1) does not apply since the rule applies to real property, not personal property.

states:

New construction covered under the provisions of RCW 36.21.070 and 36.21.080, and defined in WAC 458-19-005 (2)(q), shall be assessed at its true and fair value as of July 31st each year regardless of its percentage of completion. In instances when new construction continues after July 31 of any year, the increase in value of the property due to the new construction that occurs between August 1 of that year through July 31 of the following year is added to the assessment roll as "new construction" in the following year. ***New construction as used in this section refers only to real property***, as defined in RCW 84.04.090 and further defined in WAC 458-12-010, and also to improvements, as described in WAC 458-12-005(4), located on leased public land, for which a building permit was issued or should have been issued pursuant to chapter 19.27, 19.27A, or 19.28 RCW or other laws providing for building permits. [Emphasis added.]

By this regulation's clear terms, it explains when an assessor may add *real property new construction* to the assessment rolls. Nowhere does this regulation ever use the term "personal property." Under its plain language, WAC 458-12-342 is a rule of assessment for real property, not a tax exemption.

Moreover, this regulation appears intended to implement RCW 36.21.080, which states:

The county assessor is authorized to place any property that is increased in value due to construction or alteration for which a building permit was issued, or should have been issued, under chapter 19.27, 19.27A, or 19.28 RCW or other laws providing for building permits on the assessment rolls for the purposes of tax levy up to August 31st of each year. The assessed valuation of the property shall be considered as of July 31st of that year.

This statute is referred to as the New Construction Statute (NCS). *Fifteen-O-One Fourth Ave. Ltd., Partnership v. Department of Revenue*, 49 Wn. App. 300, 301, 742 P.2d 747 (1987). The plain language of WAC 458-12-342(1) is clearly consistent with the intent of RCW 36.21.080, which is explained by the *Fifteen-O-One Fourth Avenue* court:

The NCS . . . is an attempt to establish accurate fair market values. If property is improved by new construction, its value will presumably increase. By valuing new construction and construction in progress as of July 31, instead of the previous January 1, the assessor is able to include in the next year's taxes at least part of the value of improvements made each year.

49 Wn. App. at 306.

The plain language of WAC 458-12-342(1) that “new construction” refers only to “construction or alteration for which a building permit was issued, or should have been issued” is completely consistent with and supports RCW 36.21.080. Building permits are necessary to construct or modify buildings, not personal property. See, RCW chapter 19.27.

Nevertheless, Grays Harbor Energy attempts to read into Rule 342 an implied exemption for its personal property on-site at its Elma plant during the assessment years in question, 2004 to 2007. Brief of Appellant at 17. But as noted earlier, the initial flaw in Grays Harbor Energy’s assertion lies in the fact that the plain language of WAC 458-12-342(1) fails to state or even imply that the regulation precludes or exempts assessment or taxation of *personal property*. WAC 458-12-342(1) simply says that new construction “shall be assessed at its true and fair value as of

July 31st each year regardless of its percentage of completion.” It becomes even clearer that this rule applies only to real property when one notes that this rule explicitly states that “[n]ew construction as used in this section refers only to *real property*, as defined in RCW 84.04.090 and further defined in WAC 458-12-010...”<sup>6</sup>

Consequently, Grays Harbor Energy’s claim that WAC 458-12-342(1) limits the County Assessor’s ability to assess and tax its personal property while its *real property facility* is in construction is not supported by this rule’s clear language. Nowhere in Rule 342 is it stated that *new construction* applies to personal property; to the contrary, the rule expressly states that *new construction as used in that section refers only to real property*.<sup>7</sup>

Second, Grays Harbor Energy’s interpretation of Rule 342 conflicts with provisions in WAC 458-12-115 (“Rule 115”). Rule 115 provides that personal property shall be listed and assessed in the county where situated as of 12 noon on January 1st of each year, and with respect to goods in

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<sup>6</sup> RCW 84.04.090 defines “real property” as including buildings, structures, improvements or other fixtures of any kind. Also, the application of RCW 84.12.280, requiring “all . . . operating property other than lands and buildings . . . be assessed and taxed as personal property” lends further support to the County’s position that real property “new construction” addressed by WAC 458-12-342(1) remains subject to assessment and taxation as personal property.

<sup>7</sup> RCW 84.04.090 defines “real property” as including buildings, structures, improvements or other fixtures of any kind. Also, the application of RCW 84.12.280, requiring “all . . . operating property other than lands and buildings . . . be assessed and taxed as personal property” lends further support to the County’s position that real property “new construction” addressed by WAC 458-12-342(1) remains subject to assessment and taxation as personal property.

transit to this State, the fact they may be in their original package on the date of assessment is immaterial. This requirement is consistent with RCW 84.40.020, which requires personal property to be taxed with reference to its value and ownership on January 1 of the assessment year, but conflicts with Grays Harbor Energy's asserted exemption of personal property from assessment or taxation. WAC 458-12-115 contains no provision recognizing any exemption from personal property assessment where a taxpayer intends to use or actually uses personal property in construction.

Third, Grays Harbor Energy's proffered interpretation of WAC 458-12-342(1) also directly conflicts with WAC 458-12-310, which addresses valuation of personal property, but does not exempt personal property in either "new construction" or "work in progress." On the contrary, WAC 458-12-310 states that "Work in process in the hands of the processor or manufacturer shall be valued at the stage of production where found (costs to date) or cost to a competitor." This rule fails to make any mention of exempting personal property assessment or taxation during either "new construction" or "work in progress."

Grays Harbor Energy's assertion that "the rule's implication that new construction that is classified as *personal property* is *not* subject to assessment and taxation" essentially asks the court to imply a tax exemption for personal property under WAC 458-12-342(1). Appellant's Opening Brief at 13. But the Supreme Court rejects regulation

interpretations that *imply* a tax exemption: “taxation is the rule and exemption is the exception, and where there is an exception, the intention to make one should be expressed in unambiguous terms.” *TracFone Wireless, Inc. v. Department of Revenue*, 170 Wn.2d 273, 296-97, 242 P.3d 810 (2010), citing several cases. Where taxing regulations are concerned, “[e]xemptions may not be created by implication.” *TracFone Wireless, supra*, citing *Belas v. Kiga*, 135 Wn.2d 913, 935, 959 P.2d 1037 (1998).

The County’s position is supported by DOR rule stating that “[a]ll property located in Washington is subject to assessment and taxation, except property expressly exempted from taxation by law,” and “[p]roperty shall be exempt from taxation only when the legislature has created an exemption by clear and explicit language.” WAC 458-16-100(2).

Grays Harbor Energy’s argument is also refuted by the fact that DOR advises in its published reference manual addressing personal property assessment and taxation that construction in progress (“CIP”) assets are valued at 100 percent of cost until placed in service. Sec. 1.11, *Personal Property Manual for Washington State* (September 2009).<sup>8</sup> Although it is for the court to make the interpretation determination, considerable deference must be given to DOR’s interpretation as the

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<sup>8</sup> Cited excerpts from the *Personal Property Manual for Washington State* are attached to this brief at Appendix A.

agency charged with enforcing the statute. *Harley H. Hoppe & Associates, Inc. v. King County*, 162 Wn.App. 40, 54, 255 P.3d 819, review denied, 172 Wn.2d 1019, 262 P.3d 64 (2011), citing *S. Martinelli Co., Inc. v. Dept. of Revenue*, 80 Wn. App. 930, 937, 912 P.2d 521 (1996).

It is also significant that DOR makes no reference to WAC 458-12-342(1) as forming any basis for a personal property tax exemption for personal property involved in a business' CIP or Construction Work in Progress ("CWIP") when discussing personal property exemptions in its manual. See Sections 1.11 and 1.19, *Personal Property Manual for Washington State*. It would stand to reason that if WAC 458-12-342(1) truly were intended to exempt CIP or CWIP from personal property assessment or taxation, DOR would have at least referred to this rule in its reference manual.<sup>9</sup> The fact that any reference or citation to this rule is noticeably absent from DOR's *Personal Property Manual for Washington State* is highly indicative that no such exemption authority is intended or exists under this rule.

**B. Grays Harbor Energy's personal property is subject to assessment and taxation regardless of whether its plant is "new construction" under WAC 458-12-342, which must be read in conjunction with RCW 84.40.020 and other personal property tax statutes.**

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<sup>9</sup> In this same vein, Grays Harbor Energy fails to explain why, if its interpretation of Rule 342 validly imposes a personal property tax exemption, there is no such reference by DOR in Chapter 458-16 WAC to any exemption of personal property under "new construction." WAC 458-16 contains property tax exemption explanations to taxpayers, but does not have any reference mentioning, let alone supporting Grays Harbor Energy's interpretation of WAC 458-12-342(1).

Neither can Grays Harbor Energy find support for its argument exempting its personal property from assessment and taxation in WAC 458-19-005(2)(p), defining “new construction,” which states: “New Construction’ means the construction or alteration of any property for which a building permit was issued, or should have been issued, under chapter 19.27, 19.27A, or 19.28 RCW or other laws providing for building permits, which results in an increase in the value of the property.” It is important to note that nowhere in WAC 458-19-005(2) (p) is personal property, equipment or other non-real property of any kind even mentioned at all.

This Court ruled that RCW 84.12.280 requires all of Grays Harbor Energy’s property other than land and buildings to be assessed and taxed as personal property. 151 Wn.App. at 554. But, as Grays Harbor Energy concedes in its opening brief, the Court did not address whether WAC 458-12-342(1) exempts its personal property from assessment and taxation. Appellant’s Opening Brief at 12. The decision in *Grays Harbor I* provides no support for Grays Harbor Energy’s assertion here that its personal property is not subject to assessment for tax assessment years 2004-2007 (tax payment years 2005-2008). Neither does Grays Harbor Energy provide any other pertinent legal authority bolstering its unwarranted interpretation that WAC 458-12-342(1) somehow exempts its personal property from assessment and taxation when its plant was in “lay-up mode,” or actively under construction.

Moreover, Grays Harbor Energy's assertion of a "construction in progress" exemption under WAC 458-12-342(1) cannot be reconciled with the statutory requirement in RCW 84.40.020 that all personal property subject to tax must be listed and assessed every year with reference to its value and ownership on January 1 of the assessment year. Grays Harbor Energy's position is also unsupported by personal property valuation requirements found in WAC 458-12-310, which states in relevant part:

As in the valuation of all other classes of tangible property for ad valorem tax purposes, market value is the assessment goal. To attain that goal, the trade level concept for inventory and leased equipment shall be considered.

Trade level may be defined as value at the point in the production stream where an item of manufactured personalty is found, or the production-distribution level in which a product is found.

In appraising tangible personal property, the assessor shall give recognition to the trade level at which the property is situated and to the principle that tangible property normally increases in value as it progresses through production and distribution channels. Such property normally attains its maximum value as it reaches the consumer level.

...

**Raw material** in the hands of the processor or manufacturer should be valued at their cost to the owner or to a competitor.

**Work in process** *in the hands of the processor or manufacturer shall be valued at the stage of production where found (costs to date) or cost to a competitor...*

[Emphasis added.]

It's clear that WAC 458-12-310 makes no mention at all of

exempting *personal property* as “new construction.”<sup>10</sup> Rule 310 only refers to “work in process,” which involves work on a “product or good” in process, rather than construction of a facility in which the product is manufactured (such as electrical power in this case). More important, this rule provides that the County Assessor may define “trade level” and assess personal property “at the point in the production stream **where an item of manufactured personalty is found**, or the production-distribution level in which a product is found.” In other words, the County Assessor may value Grays Harbor Energy’s personal property on hand (i.e., on site) as of January 1, 2004 (as well as on January 1 of each subsequent three assessment years in question, 2005, 2006 and 2007) at that point where such items of manufactured personalty are found, regardless of the extent to which Grays Harbor Energy’s plant is completed and operational.

Grays Harbor Energy’s assertion in this appeal that its personal property is not assessable or taxable while its plant remains unfinished also conflicts with the requirement of WAC 458-12-060(2) that all nonexempt personal property located in the county as of 12:00 p.m. on January 1st of the assessment year be listed on a prescribed form and delivered to the County Assessor on or before April 30<sup>th</sup>.

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<sup>10</sup> Grays Harbor Energy’s claim that “the rule’s implication that new construction that is classified as *personal property* is *not* subject to assessment and taxation” [emphasis in original] (Appellant’s Opening Brief at 13) is not only unsupported by the clear text of WAC 458-12-342(1), but the appellant fails to cite any DOR administrative interpretation supporting its interpretation. To the contrary, there is a notable lack of any reference by DOR to WAC 458-12-342(1) as forming any basis for exempting personal property during CIP or CWIP. See Sec. 1.11 and 1.19 at Appendix A hereto (*Personal Property Manual for Washington State*).

Assessing Grays Harbor Energy's personal property on January 1 of each assessment year (2004-2007) regardless of the status of its plant completion is also consistent with a DOR regulation requiring a manufacturer to make and deliver to the Assessor a personal property listing, including "...the manufacturer's stock, engines, machinery, and other nonexempt personal property, together with the year of acquisition and total original cost for each category..." WAC 458-12-060(4). "Manufacturer's stock" includes all articles purchased, received, or otherwise held for the purpose of being used in whole or in part in any process or processes of manufacturing, combining, rectifying, or refining." *Id.* Manufacturer's stock defined by this rule clearly encompasses Grays Harbor Energy's personal property intended for and ultimately used to complete its Elma plant.

Application of WAC 458-12-342 to real property, but not personal property, is also supported by RCW 36.21.070 and RCW 36.21.080, which are explicitly cited in Rule 342. RCW 36.21.070 states that "[u]pon receipt of a copy of a building permit, the county assessor shall, within twelve months of the date of issue of such permit, proceed to make a physical appraisal of the building or buildings covered by the permit." RCW 36.21.080 states:

The county assessor is authorized to place any property that is increased in value due to construction or alteration for which a building permit was issued, or should have been issued, under chapter 19.27, 19.27A, or 19.28 RCW or other laws providing for building permits on the assessment rolls for the purposes of tax levy up to August 31st of each

year. The assessed valuation of the property shall be considered as of July 31st of that year.

Both statutes cited above expressly refer to issuance of a *building permit* or construction for which a *building permit* was issued that involves “new construction” as that term is used in WAC 458-12-342(1). A building permit is required for real property, not personal property. RCW 84.04.090, also cited in Rule 342, defines “real property” to include the land itself, “and all buildings, structures or improvements or other fixtures of whatsoever kind thereon.”

Consequently, the statutes and rules discussed above make it immaterial that the taxpayer’s facility may be unfinished when assessing and taxing *personal property*. Grays Harbor Energy’s interpretation of Rule 342 is unsupported by these other statutes and rules, and its personal property is subject to assessment and taxation as of January 1 of each assessment year in question here.

**1. Full value of Grays Harbor Energy’s personal property is subject to assessment and taxation.**

Grays Harbor Energy’s flawed analysis attempting to read an exemption for its personal property into WAC 458-12-342(1) violates Washington’s statutory rule of construction of tax statutes requiring the court to strictly interpret exemption provisions against the taxpayer. “[W]hen interpreting exemption or deduction provisions, ‘the burden of showing qualification for the tax benefit . . . rests with the taxpayer . . .

[and] in the case of doubt or ambiguity, [the provisions are] to be construed strictly, though fairly and in keeping with the ordinary meaning of their language, against the taxpayer.” *Simpson Investment Co. v. Department of Revenue*, 141 Wn.2d 139, 149-50, 3 P.3d 741 (2000), citing *Group Health Coop. of Puget Sound, Inc. v. Washington State Tax Commission*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967). Exemptions may not be created by implication. *Belas*, 135 Wn.2d at 935.

Since WAC 458-12-342 does not expressly provide that personal property is exempt from assessment or taxation, or even addresses tax exemptions at all, Grays Harbor Energy is essentially asking this Court to *imply* a personal property tax exemption into WAC 458-12-342(1).<sup>11</sup> This cannot be done. *Belas, supra*.

In its opening brief, Grays Harbor Energy also confuses the point of whether its personal property is legally subject to assessment and taxation with the *process* of valuing its personal property. Appellant’s Opening Brief at 19. The issue is not whether “[t]he full value of personal property, in particular machinery like power generation equipment, is not realized until it is fully installed . . .” *Id.* The real issue is what is the *true and fair value* of the personal property in question. RCW 84.40.030. Grays Harbor

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<sup>11</sup> Grays Harbor Energy’s implication in this respect also fails to cite any legal authority permitting a state agency such as Department of Revenue to even adopt an administrative regulation granting a tax exemption that is not authorized by statute. “The Department has authority to adopt only procedural rules; it cannot enact or amend the law by making rules.” *Fidelity Title Co. v. Department of Revenue*, 49 Wn. App. 662, 666, 745 P.2d 530 (1987), citing RCW 82.32.300 and *Coast Pacific Trading, Inc. v. Department of Revenue*, 105 Wn.2d 912, 917, 719 P.2d 541 (1986).

Energy lifts a partial quote from a discussion of valuation techniques in the publication *Standard on Valuation of Personal Property* by the International Association of Assessing Officers (IAAO) (December 2005), to argue that, short of actual installation and operation of personal property as part of the taxpayer's fully-functional facility, personal property has zero value.<sup>12</sup> Appellant's Opening Brief at 19. This assertion is incorrect and contrary to Washington law and attempts to ignore any market value short of the highest and best use of an asset. Grays Harbor Energy omits discussion of other points by the IAAO that "[t]he cost, sales comparison, and income approaches should be considered in the appraisal of personal property as long as the market within the trade level is in equilibrium." *Standard on Valuation of Personal Property* at 8. In assessing personal property during construction of an unfinished facility, the cost approach is most favored. "Costs used in the cost approach can be original construction cost, new or used acquisition cost, replacement, or reproduction costs." *Id.*

The County is not limited under Washington law to a "fully installed and operating" market approach to valuing Grays Harbor Energy's personal property. The County Assessor "may use a market approach, a cost approach, and a capitalization of income approach when assessing market value." *Welch Foods Inc. v. Benton County*, 136 Wn. App. 314, 326, 148 P.3d 1092 (2006), citing *Folsom v. Spokane County*, 106 Wn.2d

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<sup>12</sup> The complete text of the *Standard on Valuation of Personal Property* is attached to this brief at Appendix B.

760, 763, 725 P.2d 987 (1986).<sup>13</sup>

Grays Harbor Energy's claim that "personal property that is not fully installed and operational to its maximum productivity is . . . without value in the market place" is only supported by a self-serving statement from its former project director that "the remainder of the equipment would likely have been scrapped" had its project been cancelled. Appellant's Opening Brief at 20. The appellant's assertion of personal property valuation must be weighed in contrast with County Assessor's January 1, 2007 assessment indicating a trended and depreciated asset listing showing a valuation under the cost approach of \$192,225,688.<sup>14</sup> This presents a factual dispute concerning the valuation of personal property during the years in question that the trial court must determine after remand. Nevertheless, the full value of Grays Harbor Energy's personal property is subject to assessment and taxation.

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<sup>13</sup> With respect to DOR's centralized valuation of public utilities under RCW chapter 84.12, DOR:

...may consider the cost approach, the income approach and the stock and debt approach to value. Any one of the three approaches to value, or all of them, or a combination of approaches may finally be used in making the final determination of true cash value, depending upon the circumstances.

WAC 458-50-080(2). To the extent that the County Assessor must comply with RCW chapter 84.12 in valuing Grays Harbor Energy's property, this regulation provides clear guidance to the Assessor to utilize any one of these three approaches to value.

<sup>14</sup> The January 1, 2007 analysis by the Assessor is not part of the record for review since the tax refund trial below has been stayed pending this Court's review of the legal issue pertaining to interpretation of WAC 458-12-342(1) and this valuation is not relevant to the legal issue to be decided here. However, an excerpt of this valuation is appended to this brief at Appendix C. This information is provided only to show that there remains a dispute between the parties as to the correct valuation of Grays Harbor Energy's personal property for assessment years 2004 through 2007, which must be decided on remand.

**2. Any ambiguity whether a tax statute or regulation grants a tax exemption must be interpreted in favor of taxation and against the taxpayer.**

When the court reviews a tax regulation, a tax law exemption is narrowly construed. “Taxation is the rule and exemption is the exception; and anyone claiming a benefit or deduction from a taxable category has the burden of showing that he qualifies for it.” *North Central Washington Respiratory Care Services, Inc. v. Department of Revenue*, 165 Wn. App. 616, citing *Budget Rent–A–Car of Washington–Oregon, Inc. v. Department of Revenue*, 81 Wn.2d 171, 174–75, 500 P.2d 764 (1972). See also, WAC 458-16-100(2)(d).

The court construes “a tax exemption statute that creates ‘doubt or ambiguity’ ” strictly “ ‘ *against the taxpayer,* ’ ” “though fairly and in keeping with the ordinary meaning of [its] language.” *Sacred Heart Medical Center v. Department of Revenue*, 88 Wn. App. 632, 637, 946 P.2d 409 (1997) (emphasis added) (quoting *Group Health Cooperative of Puget Sound, Inc. v. Washington State Tax Commission*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967)); WAC 458-16-100(2)(b)-(c). But “a statute is not ambiguous merely because different interpretations are conceivable.” *Tesoro Refining and Marketing Co. v. Department of Revenue*, 135 Wn. App. 411, 422, 144 P.3d 368 (2006), quoting *Agrilink Foods, Inc. v. Department of Revenue*, 153 Wn.2d 392, 396, 103 P.3d 1226 (2005).

Grays Harbor Energy erroneously refers to RCW 84.40.020 as “a tax-imposition statute.” Appellant’s Opening Brief at 20. But RCW 84.40.020 is not a tax-imposition statute, but an *assessment* statute. *See, Northern Commercial Company v. King County*, 63 Wn.2d 639, 642-43, 388 P.2d 546 (1964) (“The fundamental purpose of the statute is to produce a true and fair evaluation of the property assessed within the contemplation of Const. Art. 7, § 2”). On the other hand, RCW 84.36.005 *is a tax-imposition statute* that provides:

***All property*** now existing, or that is hereafter created or brought into this state, ***shall be subject to assessment and taxation for state, county, and other taxing district purposes***, upon equalized valuations thereof, fixed with reference thereto on the first day of January at twelve o'clock meridian in each year, excepting such as is exempted from taxation by law. [Emphasis added.]

This section allows only those exemptions that are provided by law. Consequently, WAC 458-12-342, *as an administrative rule*, cannot establish a statutory exemption even if it did contain language (which it does not) purporting to exempt personal property from assessment or taxation. See Footnote 11, *supra*.

To the extent Grays Harbor Energy is asserting that Rule 342 is a property tax exemption, it has the burden of showing that it qualifies for such an exemption. *North Central Washington Respiratory Care Services, supra*. But the clear language of Rule 342 and the lack of any statutory support for Grays Harbor Energy’s claim of exemption leave no doubt that the trial court interpreted Rule 342 correctly. The fact that the taxpayer

manages to formulate some, albeit implausible, interpretation, does not make WAC 458-12-342(1) ambiguous. *Tesoro Refining, supra*.

### VIII. CONCLUSION

The plain language of WAC 458-12-342(1) clearly does not apply to personal property and does not grant any exemption from assessment or taxation of property. This regulation is a rule that only specifies the timing of real property assessment while that property remains “new construction.” Grays Harbor Energy’s creative interpretation of this rule lacks statutory support, is contrary to rules of judicial interpretation and DOR regulation addressing property tax exemptions. This Court should reject Grays Harbor Energy’s appeal and affirm the trial court’s summary judgment order below and remand for further proceedings.

DATED this 15<sup>th</sup> day of June, 2012.

Respectfully Submitted,

By:   
JAMES G. BAKER  
Senior Deputy Prosecuting Attorney  
WSBA #12446

JGB/lh

## **APPENDIX A**

Cited excerpts from the Washington State Department of Revenue  
(Property Tax Division)  
Personal Property Reference Manual (September 2009)

Reference Manual

# Personal Property



Property Tax Division  
September 2009

### 1.11 Supplies

Supplies are stocks of goods intended to be consumed by the business or during the production process but are not part of the raw materials, i.e., inventory that is processed into the finished product. Examples of supplies include office supplies; hotel/motel bath soaps, shampoo, etc; beauty shop shampoo, hair color, etc., not separately billed to the client; chemicals; clothing; pallets; paper; fuels; and repair parts. Taxable supplies are those not held for resale. Inventory held for resale is exempt.

Value supplies at their acquisition cost, average inventory per month. (Annual supplies expense ÷ 12 may be used as the value when the average amount of supplies typically on hand is one month's worth.)

Construction in progress, commonly referred to as CIP or CWIP (Construction Work in Progress), is usually recorded at 100 percent of cost on records of the taxpayer. Items that should be considered by the appraiser in this area are as follows:

1. Construction in progress may include real and personal property.
2. Construction in progress will not be reflected in the fixed assets or equipment ledger of the taxpayer. In most cases, it is reflected on the balance sheet at full cost. Normally, it will not be journalized to a fixed asset account until the project or asset is finished.

Value construction in progress assets at 100 percent of cost until placed in service.

### 1.12 Leasehold Improvement

These are typically improvements made by a tenant to a leased structure, or they are improvements owned by a lessee and constructed on publicly owned property.

These improvements may include things such as interior partitions, carpeting, wiring, plumbing, floor covering, heating and air conditioning, signs, painting, or exterior improvements such as paving and fencing.

Leasehold improvements may be double assessed or omitted from assessment unless particular attention is paid to lessor and lessee asset values and real and/or personal property parcels and accounts. Leasehold improvements are found most commonly in shopping centers, restaurants, retail stores, public land, and office buildings.

Close coordination between the real property and personal property departments is necessary when assessing leasehold improvements. The tenant improvements should be classified carefully and assessed either as real or personal. Do not omit them from assessment. Values in excess of millions of dollars could be overlooked. It is recommended that these assets be valued as personal property of the tenant because they benefit the tenant directly. If they were paid for by the landlord, it is usually recommended that they be valued as personal property of the landlord rather than real property since in most cases they benefit only the tenant.

In some instances, leasehold improvements are assessed as real property because the improvements are of a permanent nature and remain with the lessor at the end of the lease.

### 1.18 Assessment Date

All personal property subject to tax is to be listed and assessed every year with reference to its value and ownership on January 1 of the assessment year. (RCW 84.40.020.)

### 1.19 Exemptions

Household goods and furnishings in actual use by the taxpayer in his residence, and not for sale or commercial use, are exempt. Personal property of each head of family (sole proprietor) is exempt up to a maximum of \$15,000 if the taxpayer meets the definition of head of family. (RCW 84.36.110 and WAC 458-16-115)

The inventory of a business is not subject to property tax. (RCW 84.36.477.) "Business inventories" means...

*"...all livestock, inventories of finished goods and work in process, and personal property not under lease or rental, acquired, or produced solely for the purpose of sale or lease or for the purpose of consuming the property in producing for sale or lease a new article of tangible personal property of which the property becomes an ingredient or component."*

Business Inventories does not include...

*"...personal property acquired or produced for the purpose of lease or rental if the property was leased or rented at any time during the calendar year immediately preceding the year of assessment and was not thereafter remanufactured, nor does it include property held within the normal course of business for lease or rental for periods of less than thirty days."*

Custom computer software, except embedded software, is exempt from taxation. Retained rights in computer software are exempt. Modifications to canned software are exempt, but the underlying canned software remains subject to tax. Master or golden copies of computer software are exempt. (RCW 84.36.600.)

Under RCW 84.36.630, all qualifying farm machinery and equipment is exempt from the state property tax. **Qualifying** machinery and equipment must (1) be **owned** by an active farmer, (i.e., someone who is in the business of farming) and (2) have been used in the business of farming during each year the claim for exemption is made. Additionally, equipment claimed for exemption must also have been used **exclusively** in growing, raising, or producing agricultural products. Equipment **not qualifying** includes (1) equipment used in growing, raising, or producing agricultural products for a person's own consumption, (2) equipment used in the selling of animals from stockyards, slaughter houses, and packing houses, and (3) equipment used in cultivating or raising timber. The claim for exemption must be submitted annually with the personal property listing form in the county for which the listing form is made. For a listing of qualifying farming activities refer to RCW 82.04.213 and 15.85.020.

*"Farmer" means any person engaged in the business of growing, raising, or producing, upon the person's own lands or upon the lands in which the person has a present right of possession, any agricultural product to be sold. "Farmer" does not include a person*

*growing, raising, or producing such products for the person's own consumption; a person selling any animal or substance obtained therefrom in connection with the person's business of operating a stockyard or a slaughter or packing house; or a person in respect to the business of taking, cultivating, or raising timber.*

Other exemptions may be found in [chapter 84.36 RCW](#).

#### Application for Exemption of Farm Machinery and Equipment

### **1.20 Personal Property Moving into the County**

Personal property being moved from one county in Washington to another county in Washington, between January 1 and July 1 should be assessed in whichever county first lists and assesses the property. ([RCW 84.44.080](#).) Usually, the county where the property is being relocated will contact the previous county to verify listing and assessment. Be careful to avoid a double assessment.

### **1.21 Personal Property Moving into the State**

When personal property is moved into Washington from outside the state between January 1 and July 1, the owner is required to list the property for assessment purposes. The property must have been in existence and owned by the taxpayer on January 1. If the owner can show that the property has already been assessed in another state or county, it should not be assessed again in Washington. The burden of proof is upon the taxpayer to produce documentation. ([RCW 84.44.080](#).)

### **1.22 Perfection of Personal Property Liens**

The lien on personal property is established on January 1 of the assessment year. However, it is not perfected until the property is listed and valued by the assessor. So even though a taxpayer may have listed the property, the lien is not protected until the assessor has valued the property. Subsequent sale of the personal property does not affect the lien for taxes. If necessary, the lien may be placed upon real property of the taxpayer (selected by the treasurer) and charged on the tax rolls. ([RCW 84.60.020](#).)

### **1.23 Valuation Guidelines, Indexes, and Indicators**

Annually, the Department of Revenue issues *Personal and Industrial Property Valuation Guidelines (Guidelines)*. These *Guidelines* consist of (1) an explanation of changes from the prior year and information about how to use the *Guidelines*, (2) Business Index, (3) Personal and Industrial Property Valuation Combined Table and the Supplemental Valuation Tables.

The *Guidelines* are published as a guide in estimating the market value of property in average condition. Adjustments to the estimated market value must be made by the assessor's office when the taxpayer can substantiate any excessive obsolescence not already taken into account in the tables.

The reasons for using "Original Cost New Less Depreciation" as the basis for valuation are that the information is easily obtainable, this method lends itself readily to a computerized mass

**APPENDIX B**

*Standard on Valuation of Personal Property*

International Association of Assessing Officers

(Approved December 2005)

# Standard on Valuation of Personal Property

Approved December 2005

## **International Association of Assessing Officers**

The assessment standards set forth herein represent a consensus in the assessing profession and have been adopted by the Executive Board of the International Association of Assessing Officers. The objective of these standards is to provide a systematic means by which concerned assessing officers can improve and standardize the operation of their offices. The standards presented herein are advisory in nature and the use of, or compliance with, such standard is purely voluntary. If any portion of these standards is found to be in conflict with state law or the Uniform Standards of Professional Appraisal Practice (USPAP), USPAP and state law shall govern.

**Acknowledgments** This revision of the 1996 Standard on the Valuation of Personal Property was begun in 2004 under the direction of Kenneth C. Uhrich, Gary McCabe, CAE and Scott McAlpine members of the IAAO Technical Standards Committee. The standard also benefited from the support, recommendations, and thorough reviews of Lisa A. Hobart, PPS; Neal R. Cook, MAI; Jim Todora, CAE, MAI; Joyln Stotts; Nancy Tomberlin; Val Courtright; David Savedra; Steve D. Pruitt; Bruce Woodzell, and the IAAO Personal Property Section. At the time of adoption of the standard by the IAAO Executive Board, the IAAO Technical Standards Committee was composed of Peter L. Davis, chair, Alan S. Dornfest, AAS; Gary McCabe, CAE, Scott McAlpine; Bill Marchand, and Kenneth C. Uhrich.

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# Standard on Valuation of Personal Property

## 1. Scope

This standard is intended to provide recommendations for defining, classifying, discovering, reporting, verifying, and valuing personal property for ad valorem tax purposes. It is beyond the scope of this standard to address unique valuation issues that may arise in the appraisal of personal property associated with public utilities, telecommunications, railroads, or similar properties.

## 2. Introduction

The purpose of this standard is to present methods and techniques that assessing officers can use to achieve uniform and equitable personal property valuations. Effective administration of a personal property assessment system depends, in part, on legislation and regulations that provide clear direction for determining the proper status of personal property for assessment and taxation. Such administration also requires an adequate budget to obtain the resources necessary to assess personal property accurately and equitably.

## 3. Definition of Personal Property

Property means an aggregate of things or rights to things whose possession is protected by law.

Two broad categories of property are real and personal. “Real property is the rights, interests, and benefits connected with *real estate*. Real estate is the physical parcel of land, improvements to the land (such as clearing and grading), improvements attached to the land (such as paving and buildings), and appurtenances (such as easements that cross the parcel or give access to the parcel). Personal property is defined by exception: property that is not real is personal. The salient characteristic of personal property is its movability without damage either to itself or to the real estate to which it is attached” (International Association of Assessing Officers 1990, 76).

Personal property by its nature is not permanently attached and therefore is movable. Criteria for distinguishing whether an item is real or personal property in a particular situation usually include intent of owner, means of attachment, contribution to highest and best use of the property (real estate), relevant case law including sales and use tax cases if considered relevant, and statutory, regulatory, and legal guidelines.

Personal property is divisible into two classes—tangible and intangible. Examples of tangible personal property are material items such as animals, marine vessels, aircraft, motor vehicles, furniture and fixtures, machinery and equipment, tools, dies, jigs, patterns, and stock in trade (in-

cluding inventories held for resale, supplies, and materials in process). Examples of intangible personal property are representations of rights of ownership to property—cash, shares, annuities, patents, stocks, bonds, notes receivable, insurance policies, accounts receivable, licenses, contracts, franchises, money market certificates, certificates of deposit, and copyrights—as well as goodwill.

An assessment statute should explicitly define the types of personal property subject to and exempt from assessment and taxation. State and provincial agencies should provide supporting rules, regulations, and guidelines as required. Legislation should also explicitly define the situs (location for tax purposes) of personal property and should specify a common assessment date for all taxing authorities.

## 4. Discovery of Personal Property

The extent to which personal property can be assessed depends upon its discovery. Complete discovery requires adequately trained staff and supporting resources. Taxation agencies should be empowered to issue binding rules and regulations covering the discovery of personal property. Disclosure of personal property is often contingent on identifying the owner of the property. Sources that may be useful in the discovery of personal property and its owners include the following:

- previous assessment records and previous personal property statements or returns
- physical inspection (on-site review)
- personal property listing form, return, rendition, declaration, or statement
- real property field appraiser reports and the property characteristic file
- audits (desk, office, field, or correspondence)
- state, provincial, and local sales tax permits
- federal, state, provincial, municipal, and county business licenses and registrations
- building permits
- chambers of commerce membership lists
- new business listings from news media
- public records (such as trade name records, Uniform Commercial Code [UCC] forms, corporation charters, partnership articles, and assumed name notices)
- property transfer documents, including recorded bill(s) of sale

- classified advertisements
- telephone directories
- city directories
- accounting records, including financial statements
- various state and federal tax returns (usually restricted to audit records)
- Internet research on business operations and contacts
- Web sites, specifically leasing and sales
- advertisement flyers
- other resources that can be helpful include access to governmental databases—Department of Motor Vehicles (DMV) or Department of Revenue records providing lists of manufactured home owners or lists of corporate taxpayers by jurisdiction.

Once the property has been discovered and the owner identified, an appraiser should inspect the property and establish an account or record for the owner (or business). The appraiser should speak to the owner, manager, or other authorized person; explain the purpose of the visit; and obtain the necessary data. A standard form or checklist, showing the date of inspection, should be used to verify ownership, the nature of the property, and the situs as of the assessment date.

Information that should be obtained about a business includes the following:

- name of the business
- type of business (e.g., restaurant or hotel)
- type of ownership (e.g., sole proprietorship, partnership, franchise, or corporation)
- mailing address of the business
- name and address of the owner(s)
- telephone number of the business
- name/title of the person supplying the information
- name, address, and telephone number of the party keeping records for the business
- beginning date of the business within the assessment jurisdiction
- e-mail addresses
- North American Industrial Classification System codes (NAICS) (formerly known as Standard Industrial Codes [SIC] in the U.S.)

Fiscal year information that should be obtained about the personal property of the business includes the following:

- a complete listing of all tangible personal property, including machinery, equipment, furniture, fixtures, computers, and other tangible fixed assets with their location, year purchased and year manufactured, and acquisition or construction cost together with what is included in this cost amount, such as shipping, freight, sales tax, licenses, and so forth
- a complete listing, with full descriptions and costs, of all leasehold improvements, noting which items may already be assessed as real property
- a complete listing of leased equipment with the name and address of the lessor, information on the equipment (including name of manufacturer, date of manufacture, description, model number, serial number, list price, and original cost, if available), lease number, and terms of lease (if possible, a copy of the lease agreement should be obtained)
- a complete listing of loaned or consigned items including a brief description (e.g., vending machines), and the name and address of their owner(s)
- a complete listing of items in inventory, rented or leased as part of the business' normal operation

## 5. Reporting of Personal Property

The physical inspection and listing of individual personal property items is dictated by time, financial resources, and the availability of trained personnel. Typically, these constraints require the use of a reporting form (also called a rendition, return, schedule, or listing) completed by the taxpayer or the taxpayer's agent. All reporting forms should be subject to audit by the assessor, or the assessor's agent, to determine the accuracy and validity of the information provided in the return document. The assessor should mail reporting forms or make them available early enough to allow for their timely completion. Forms and instructions should also be available on the assessor's Web site. The assessor's mailing address and telephone number should always be included on the listing form. Web sites and all documents sent from the assessor's office should include the office's e-mail address.

The first year a taxpayer files a reporting form, the information reported should include a listing of all personal property giving a description, date acquired, and original acquisition or construction cost of each item. If an item was acquired used, the manufacture date and historic cost of the item should be determined if possible. In subsequent years, the taxpayer may be asked to report

only additions and deletions to the initial listing, with appropriate details and costs. This system promotes verification and valuation accuracy. Value trending and depreciation factors can be applied to each item individually or to a group of items, such as furniture, fixtures, and equipment (FF&E), acquired in a given year.

The form should contain sufficient instructions to help the taxpayer prepare and file a complete and accurate listing of all taxable personal property. The instructions on the form should also specify the reporting method required and give specific instructions on how to report construction in progress, acquisition costs (including installation, freight, taxes of all types, and fees), and expensed and fully depreciated assets as well as leased assets. The form should contain a statement that all listings are confidential and are subject to audit.

Implementation of an electronic filing process should be considered in order to provide a high level of customer service. The American National Standards Institute (ANSI) has approved electronic data interchange standards through the Accredited Standards Committee (ASC X12 transaction data sets). This standard enables taxpayers with accounts in multiple jurisdictions to efficiently automate the annual filing of personal property returns.

## 6. Verification and Auditing

### 6.1 Authority

Statutes should contain enabling language for regulatory compliance and enforcement measures. Such laws should give assessors and their representatives authority to examine the property, books, papers, and accounts of taxpayers. Statutes should also provide appropriate penalties for those who fail to file timely returns, file inaccurate information, or deny the assessor access to property and records. Further, statutes should require property owners to file personal property statements in each jurisdiction in which the owners have personal property.

### 6.2 Audit Program

The assessor should establish an audit program designed to facilitate the full and proper listing of all taxable personal property in the assessment jurisdiction. In general, emphasis should be placed on the audit of new accounts, major accounts, accounts with significant changes from the previous year, and accounts that are suspected of being inaccurately reported based on objective analysis.

Statistically valid sampling techniques should be employed to ensure that the audit program is equitable. The purpose of an audit is to verify that all taxable personal property items have been reported and that the information given is accurate. A physical inspection may help to verify the completeness of reports.

To ensure fair and equitable treatment, the scope of an

audit program must be clearly defined before the process begins. For example, in establishing audit criteria, it may be useful to identify particular industry segments for examination to maximize resources in a given year or assessment cycle. Audit programs may include one or more of the following activities:

- Review listing changes from one year to the next with taxpayer contact if there are questions.
- Review correctness of data before making changes; contact taxpayers requesting additional information as necessary.
- Request that government revenue agency depreciation schedules be submitted with all listings.
- Obtain copies of government revenue agency depreciation schedules for (specify percentage) of total filings.
- Obtain actual copies of ledger listings from (specify percentage) of total filings.
- For mail audits, request specific documentation from selected accounts or business types.
- Physically inspect and audit records of specifically targeted accounts or business types.
- Physically inspect and audit (specify percentage) of all personal property accounts each year

When conducting a detailed audit with inspection, the appraiser examines a detailed plant fixed-asset ledger or similar record, if available, that provides information on each item such as asset description, serial number, manufacturer, date of purchase, date of installation, location, acquisition cost, depreciation charges, and retirement provisions. The appraiser verifies that assessable items have been completely and accurately reported. Assessable costs may include charges for installation, freight, taxes, and fees (if applicable), unless specifically excluded by law.

Attention should be directed to standby equipment, permanently idled equipment, retired or fully depreciated equipment, and uninstalled equipment. Regardless of book value, such equipment and inventory should be listed and valued unless specifically exempted. Idle, retired, abandoned, or fully depreciated property may not have a value-in-use and may be reported on the company's books as having \$0.00 value, but the property may have a value-in-exchange. The amount of value-in-exchange should be determined based on market research of used machinery and equipment of similar use and condition. The status of personal property as of the assessment date is critical to determining an item's assessability or taxability (ratatability).

The appraiser should compare total reported costs with

those shown in the general ledger or balance sheet in order to verify that all property has been reported. The appraiser should be familiar with the nature of the cost being reported (original, acquisition [new or used], replacement, impaired) and the nature of the cost found on the general ledger (book, net book, market). Recent changes in reporting requirements by the United States Federal Accounting Standards Board attempt to tie depreciation life to market evidence such as leases.

The appraiser should verify that leased items, for which the business is either the lessor or lessee, have been properly reported and assigned to the correct party. If leasehold improvements exist, the appraiser should ensure that they are being assessed on either the real property roll or the personal property roll.

Simultaneous review of real and personal property records can also help to ensure complete assessment of property.

Time and cost considerations sometimes dictate that the appraiser will not be able to verify the proper reporting of each item of personal property at each site or business being audited. Often, verifying a sampling of major items listed in the detailed plant ledger, a walk-through inspection, and an examination of the general ledger, balance sheet, or other appropriate records will suffice. It may also be helpful to check a sample of recent invoices to see if the taxable assets have been accurately reported. The overall objective of the audit and verification process is to promote proper reporting.

State and provincial agencies may establish audit programs as part of their oversight or equalization and assessment responsibilities. Assessment jurisdictions may complete taxpayer audits or may be allowed to employ private auditing firms to complete the reviews. Larger jurisdictions will sometimes offer audit services to smaller jurisdictions for a fee or jurisdictions may combine audit resources in other ways.

### 6.3 Quality Assurance

Quality assurance methods and techniques used for personal property are similar to those used for real property. Verification of reported data against independent sources is a good way to check the accuracy of the reported costs and inventory of items listed.

Section 10 of the IAAO *Standard on Ratio Studies* (1999) provides comprehensive guidance for assessors planning to conduct a quality assurance program for personal property.

## 7. Valuation

### 7.1 Trade Level

All approaches to personal property valuation should consider trade level, which refers to the production and distribution stages of a product. The appraiser should

recognize three distinct basic levels of trade: the manufacturing level, the wholesale level, and the retail level. Incremental costs (such as freight, overhead, handling, installation, and sales taxes paid on installed costs) are added to a product as it advances from one level of trade to the next, thereby increasing its value as a final, in-service product. Thus the value of goods will differ, depending on their level of trade. The appraiser should value personal property at its current level of trade, theoretically to a buyer within that same trade level. Such considerations are particularly important in inventory valuation.

### 7.2 Valuation Techniques

The cost, sales comparison, and income approaches should be considered in the appraisal of personal property as long as the market within the trade level is in equilibrium. If demand exceeds supply or supply exceeds demand, i.e., unbalanced markets, one or more of the three approaches may produce distorted results. The degree of dependence on any one approach could also change with the availability of reliable data. Units of comparison, such as value of personal property per square foot, for comparable properties can be used to check the value estimates derived from the standard appraisal approaches. Such units of comparison can also be used when the data required for other approaches are unavailable. Examples include cost/value per square foot of FF&E in an office building or cost/value per square foot of inventory for a retail business.

The valuation method and techniques employed should be based on the appraiser/assessor's value standards. In most jurisdictions, market value is defined by value-in-exchange, that is, the value to the next buyer as of the lien date, and highest and best use principles. The highest and best use of an asset will likely be as fully installed and operational to its maximum productivity.

#### 7.2.1 Cost Approach

Costs used in the cost approach can be original construction cost, new or used acquisition cost, replacement, or reproduction costs. Allocated cost can be used if items are purchased in bulk, although often only original or acquisition costs are readily available for personal property assessment purposes. The cost approach provides an estimate of value based on the depreciated cost of the property. In applying the cost approach to personal property, the appraiser must identify make and model number, year acquired, and total acquisition costs, including installation, freight, taxes, and fees. The acquisition costs should then be trended and depreciated as appropriate to reflect current market values. Acquisition costs of equipment obtained pursuant to a lease-purchase agreement should include the total payments, not just the final payment. If financing costs are factored into

the lease payments, an adjustment to the “selling price” may be required.

The assessor should recognize that appraisal and accounting practices for depreciating personal property may differ. Accounting practices provide for recovery of the cost of an asset (the return of the asset), whereas appraisal practices strive to estimate a value related to the current market and should consider both return of the asset and return on the asset. A productive asset may continue to have value at the end of its scheduled life or conversely, an asset may lose its value prior to the end of its scheduled life. Appraisal practice must consider accrued depreciation in the forms of physical deterioration, functional obsolescence, and external (economic) obsolescence. The appraiser/auditor should also be familiar with the purchase accounting methods used by businesses in their jurisdiction. A company’s depreciation schedule should provide life tables for various asset categories.

The restoration or modification of machinery or equipment may be treated differently for assessment and accounting purposes. For accounting purposes, the restoration/modification cost may be entered as a different asset, whereas the appraiser/assessor would add the cost to the original item and adjust the effective age of the asset.

Useful guidelines in the form of depreciation schedules or tables are available from state or provincial assessing authorities, professional valuation companies, and appraisal publishing firms. Because the personalty of a business normally is acquired throughout the year, acceptable depreciation schedules will permit the full year’s depreciation or will consider the average age of six months (half-year convention). Generally, these guides are sufficiently accurate for use in mass appraisal of property. If guides do not exist for specific types of personal property, it is recommended that they be developed. Depreciation schedules can be developed from a study of asset lives and resale prices. The schedules can be asset specific or for general categories such as personal computers or furniture and fixtures. Most schedules base annual depreciation on a percentage of original cost or replacement cost.

However, there can be particular types of property where standard depreciation schedules may not apply and an accurate depreciation estimate can only be made by using an alternate method. One such method is the capitalization of income (rent) loss due to the inefficiency of the property. It is similar to the practice in real estate valuation of calculating the depreciation due to rent loss caused by internal or external forces. An example would be if an existing machine can only run eight hours per day, but a modern replacement can run ten hours per day, the loss in revenue from the two hours of non-production could be capitalized and the amount subtracted from the replacement cost. Whether the obsolescence

was functional or economic would depend on whether the forces reducing the production hours were internal or external. The appraiser/assessor’s experience and judgment should inform their decision of whether to use a standard schedule, develop a new schedule, or apply an alternate method of calculating depreciation.

### **7.2.2 Sales Comparison Approach**

The sales comparison approach may have limited application for appraising machinery and equipment used in business because sales of used items are generally few and are often liquidation sales, which typically are not at market value, or are bulk asset purchases. In such circumstances, list prices including delivery costs and sales taxes, when supported by the marketplace, can be good indicators of value. Used assets acquired in bulk purchases may have been sold in an arm’s-length transaction so market data may be evident. The value of an individual item to the entire sale price (purchase price allocation) may be available in the buyer’s records.

Care must be taken to assure that the property is valued at the proper level of trade. Trade and cash discounts should be subtracted from the list prices, particularly if the equipment sold is still at the wholesale level of trade. If reliable sales data are available, the adjustment process can be applied in the same manner as for real property. If an adjustment for time of sale is made, the adjustment may be negative due to additional accrued depreciation of the property or positive due to inflation.

### **7.2.3 Income Approach**

The income approach produces an estimate of the present worth of income to be received in the future. To apply this approach, the appraiser must estimate the income stream over the remaining economic life of the subject property. This is an important concept; the future income-generating capacity of personal property is typically short-lived compared to real estate. The direct capitalization technique (Income divided by Rate equals Value [ $I/R=V$ ]) can be used if the single-year income applied is indicative of the annual income for the remaining life of the asset and the capitalization rate reflects the recapture period of the asset. Personal property can also be valued using a yield capitalization technique, which values the changing productivity (income) of the asset over its projected remaining life more accurately than  $I/R=V$ . Many industries use gross income multipliers (GIM) or gross rent multipliers (GRM) to value personal property that has typical and similar operating expenses. When applying the income approach to value personal property, it is important to capitalize income from the rental of an asset not the income of the business that owns the asset.

Typical gross incomes may differ under various leasing

arrangements; lessors may be able to supply average gross revenues for each type and model. The historical pattern of net income streams, together with an analysis of current leasing patterns, will suggest the likely shape of future income streams. The capitalization technique chosen should be consistent with the anticipated income stream.

When reliable lease data on equipment leases are available, the income approach can provide good value estimates. Lessors should be required to document operating expenses to be deducted from the gross income. These expenses include management expenses directly associated with the production of lease revenue, equipment maintenance expenses, and the like.

Developing an appropriate capitalization rate is a critical step in the capitalization process. Capitalization rates contain provisions for return on the investment (discount rate) and capital recovery (return of the investment), as discussed in the cost approach. In addition, property taxes may be accounted for as a component of the capitalization rate. (See *Standard on Mass Appraisal of Real Property* [IAAO 2002].)

Data on the economic lives of various types of personal property can be obtained from a number of sources. Lessors are perhaps the best source, although typical economic lives should be documented with dates of acquisition and disposal of actual items. U.S. federal tax guidelines for modified accelerated cost recovery systems (MACRS) can be helpful as a starting point. Economic life data can also be used to estimate recapture rates. When the income approach is applied, consideration should be given to the salvage or scrap value, if any, when the property has reached the end of its normal life expectancy (remaining economic life equals 0). An analysis of resale values of used equipment can be helpful in determining salvage value.

In cases where property is both sold and leased, gross income multipliers (GIM) should be developed. Gross income multipliers can provide reliable value estimates for personal property items that have similar operating expenses, discount rates, and remaining economic lives.

### **7.3 Valuation Guidelines for Tangible Personal Property**

As discussed in section 7.2, the cost, sales comparison, and income approaches should be considered in the appraisal of tangible personal property. However, certain types of personal property do not readily lend themselves to development of all three generally accepted approaches. If sufficient sales data are available to support use of the sales comparison approach, it should receive primary consideration. In many instances, however, sufficient sales data are not available, and in these instances, more

reliance should be placed on the cost approach or the income approach. The assessor must always consider the quality and quantity of the available market data.

The following are procedures typically used in the valuation of common types of tangible personal property.

#### **7.3.1 Machinery and Equipment**

Machinery and equipment (M&E) are items of personal property used in the normal conduct of business that are not permanently attached to the real estate and, unlike inventory, are not intended to be sold. Utility and ability to produce income are factors that influence the economic life of machinery and equipment. The market value of machinery and equipment typically follows a declining path once the assets are acquired and put into operation due to normal wear and tear and technological changes. Salvage or scrap value should be considered at the end of economic life.

The most common approach for the valuation of machinery and equipment is the cost approach, although the sales comparison approach should receive primary consideration when adequate data are available. In particular, small equipment, for which there is often an active resale market, may lend itself to valuation by the sales comparison approach.

Machinery and equipment can be classified as short-lived (computer) or long-lived (drill press), so not all M&E can be grouped together for depreciation purposes.

#### **7.3.2 Furniture and Fixtures**

The procedures described for the appraisal of machinery and equipment are generally used in the appraisal of furniture and fixtures (F&F). Because F&F generally have similar lives, they are often grouped into one item for depreciation purposes.

#### **7.3.3 Leased Equipment**

Valuation of leased equipment is complicated by such factors as the wide variety of leased equipment, the variety of leasing arrangements, rapidly changing technologies, and changing market conditions. These factors can cause the quality and quantity of available market data to vary.

The income approach is often used in valuing leased equipment because data on sales and rental rates are usually available. When sales data are available, emphasis should be given to income multipliers derived from market data.

The cost approach may be used cautiously in the valuation of leased equipment because markups of cost to list prices vary from one company to another on the same type of equipment and also vary with the level of trade. If manufactured cost is the only information that is reported,

the appraiser should obtain more data from the lessor or compare the equipment in question with similar equipment of known cost.

### 7.3.4 Inventories

The term inventories includes specific categories of goods held for resale in the course of business, goods in the process of production (termed goods in process), and raw materials.

Whether certain types of goods are classified as inventories or as something else will change depending on the trade level at which the appraisal is being made. Machinery and other equipment that remain classified as inventories at the manufacturing, wholesale, and retail levels become machinery and equipment upon reaching the end user.

Inventory valuation, both for goods in process and for finished goods, should include the value of labor, materials, and overhead expended during production.

There are many methods for estimating the value of inventories. Some of the more common ones are:

- last in, first out (LIFO)
- first in, first out (FIFO)
- weighted average
- lower of cost or market

The most commonly used method for ad valorem purposes is lower of cost or market. First in, first out (FIFO) is also an acceptable measure of inventory replacement costs. Taxpayers often use last in, first out (LIFO) for income tax purposes, but it does not reflect inventory value for property tax purposes. The weighted average method provides for distribution of inventory costs throughout the year.

Caution should be exercised when inventory values are estimated from the owner's accounting records because most accounting systems use an original acquisition cost basis for pricing inventory and this does not necessarily reflect market value as extracted from the marketplace, which may be more or less than original cost.

### 7.3.5 Supplies

Supplies are stocks of goods that are intended to be consumed during the production process, but are not part of the raw materials inventory that is processed into the finished product. Examples of supplies include chemicals, clothing, pallets, paper, shipping materials, fuels, and repair parts. Unlike inventory, supplies are not held for resale. Supplies should be valued at their acquisition cost.

### 7.3.6 Consigned Goods

Consigned goods are personal property in the possession of an agent, held for sale by that agent. They should be valued, at the appropriate level of trade, as part of the consignor's inventory.

### 7.3.7 Imports and Exports

Assessors should be aware of the legal status of import and export merchandise in order to determine its taxable status. If there is no exemption provided by statute, then the techniques for estimating the value of inventories should be used for valuing imports and exports.

## 7.4 Valuation Guidelines for Intangible Personal Property

The discovery, reporting, verification, and proper valuation of intangible personal property is difficult and can be expensive. The methods for discovering, reporting, verifying, and auditing intangibles are the same as for tangible personal property. Pertinent information includes type of asset, name of issuer, date of acquisition, legal life, expected useful life, face value or par value, market value, and dividends or other income. Individual research can lead to sources that provide information on the selling prices of intangible personal property.

Statutes should provide concise guidance on the assessment of intangible personal property. The benefit/cost ratio of intangible personal property taxation is such that many states have exempted intangible personal property from taxation. For a listing of state and provincial treatment of intangible property, see *Property Tax Policies and Administrative Practices in Canada and the United States* (IAAO 2000).

Those states that continue to assess intangible property primarily do so for public utilities by using a unit valuation method. When centrally assessed property is not held by a public utility, the separation of tangible from intangible value may be required. Recent letter rulings and case law should be researched to provide guidance in this area. Careful review should underscore the purpose, use, and how necessary and integral the identified intangible personal property is to the taxable tangible personal property. This review could entail the examination of the taxpayer's books, records, and filings with regulatory agencies.

## 7.5 Compliance with USPAP

IAAO requires that all appraisal work performed by its members in the United States and Canada be compliant with the *Uniform Standards of Professional Appraisal Practice* (USPAP) of the Appraisal Foundation (2005 [updated annually]) and the *IAAO Code of Ethics and Standards of Professional Conduct* (2005). USPAP Stan-

dards relevant to the valuation of personal property are Standard 6: Mass Appraisal, Development and Reporting; Standard 7: Personal Property Appraisal, Development; and Standard 8: Personal Property Appraisal, Reporting. Standard 6 defines the appropriate form for developing mass appraisal methods and the structure for reporting the results. Standards 7 and 8 provide guidance on the proper process to follow so that the results are based on sound conclusions and are well documented. USPAP contains adequate jurisdictional exceptions to accommodate the various provisions of state, county, and municipal laws.

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*Bibliographic computer databases are available through the IAAO library on various aspects of personal property assessment. The databases can be searched to provide customized listings. Databases relevant to personal property valuation are as follows:*

*Assessment manuals in the United States.* 196 citations.

*Provincial assessment manuals in Canada.* 69 citations.

*Price guides for personal property.* 255 citations.

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*Issues in intangibles valuation.* 101 citations.

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## Glossary of Terms

**Acquisition cost.** The cost used in accounting to represent the purchase price of an asset. If installation and other associated costs are included, this cost should be referred to as total acquisition cost.

**Chattel.** An item of tangible movable or immovable property except real estate, freehold, and things (such as buildings) connected with real property.

**Consigned goods.** A type of inventory in the possession of a selling agent but owned by another party. The seller has no equity, no control of price or sale, and receives none of the profit (as such) from sale of the property (but may receive a sales commission).

**Construction in progress.** Property that is in a process of change from one state to another, such as the conversion of personal property from inventory to fixed asset by installation or the conversion of personalty to realty by becoming a fixture.

**Discovery.** The process whereby the assessor identifies all taxable property in the jurisdiction and ensures that it is included on the assessment roll.

**Economic life.** The period of time over which an asset's operation is economically feasible. The economic life may or may not be equivalent to the physical life of the asset.

**External (economic) obsolescence.** The loss in appraisal value (relative to the cost of replacing a property with

property of equal utility) resulting from causes outside the property that suffers the loss. Usually locational in nature in the depreciation of real estate, it is more commonly marketwide in personal property and is generally considered to be economically unfeasible to cure.

**Effective age.** An age assigned to an asset based on a combination of its actual age and condition.

**Finished goods.** Inventory at the end stage of a manufacturing process. Finished goods are the result of combining raw materials with labor, capital, machine time, and other components of production.

**First in, first out (FIFO).** An inventory cost-accounting procedure whereby unsold inventory, including inventory carried over from prior years, is valued at the price most recently paid for inventory purchases.

**Fixed assets.** Personal property that has been brought to the point of highest and best use, that is, it is fully installed and used to produce income in an economically feasible manner. In a business: permanent assets required for the normal conduct of a business.

**Fixture.** Generally, an asset that has become part of real estate through attachment in such a manner that its removal would result in a loss in value to either the asset or the real estate to which the asset is affixed.

**Goods held for sale or resale.** Any inventory held for sale by a wholesaler, distributor, or retailer after having passed through one or more other levels of trade.

**Goods in process.** Inventory, formerly raw materials, that has begun to undergo the manufacturing process that will result in finished goods.

**Historical cost.** The cost new to the first owner of personal property.

**Intangible property.** That class of personal property in which value is based on evidence of ownership rather than physical or tangible characteristics, for example, notes, bonds, insurance, patents, and accounts receivable.

**Inventory.** The group of personal property items whose value is exhibited by value-in-exchange, that is, ownership is solely for the purpose of sale rather than use.

**In-transit goods.** Personal property that is in movement from one jurisdiction to another. In-transit goods are not assessable because they lack situs.

**Last in, first out (LIFO).** An inventory cost-accounting procedure whereby unsold inventory, including inventory carried over from the prior year, is valued at the prices paid for the earliest inventory purchases.

**Leasehold improvements.** Items of personal property, such as furniture and fixtures associated with a lessee (the tenant), that have been affixed to the real property owned by a lessor.

**Lower of cost or market.** An inventory accounting concept which states that the present value of inventory is based on the lower of either historic cost or current selling price (example: obsolete inventory items).

**Original cost.** The cost as recorded on the books of the current owner.

**Remaining economic life (REL).** The number of years in the future during which the operation of an asset is anticipated to be economically feasible, often expressed as a percentage of the total economic life (REL %).

**Situs.** The taxable location of an asset. For personal property, situs may be the physical location of the property or, in the instance of highly mobile property, the more-or-less permanent location of the property owner.

**Supplies.** A type of personal property, usually treated as inventory, that is consumed as part of the process of bringing other assets to a saleable condition.

**Tangible property.** Property whose value is measured in accordance with its actual physical presence.

**Trade level.** Refers to the production and distribution stages of a product. Appraisers recognize three distinct levels of trade: the manufacturing level, the wholesale level, and the retail level. Personal property should be assessed at the trade level at which it is found. The valuation of the inventory of one owner should be based on the price for which it would be exchanged with a similar

business at the same trade level, for example, from one manufacturer to another. Value-in-exchange increases as a property moves from manufacturing through to retail levels of trade.

**Trending factor.** A figure representing the increase in selling price over a period of time. Trending accounts for the relative difference in the value of a dollar between two periods.

**Unit cost.** A valuation guideline expressing the relationship between cost or value of inventory or fixed assets and some unit of measure, for example, cost per square foot or per employee.

**Value-in-exchange.** The amount an informed purchaser would offer for personal property under given market conditions.

**Value-in-use.** The value applied to furniture, fixtures, and equipment as installed and in-use for generation of income or performing its function.

**Weighted average.** A method of inventory cost accounting whereby inventory is valued according to the unit price of all units owned throughout the year. It is calculated by dividing total acquisition cost of all inventory by the number of units owned.



## **Assessment Standards of the International Association of Assessing Officers**

DECEMBER 2005

Standard on Valuation of Personal Property

AUGUST 2004

Guide to Assessment Administration Standards

AUGUST 2004

Standard on Manual Cadastral Maps and Parcel Identifiers

AUGUST 2004

Standard on Property Tax Policy

SEPTEMBER 2003

Standard on Automated Valuation Models

JULY 2003

Standard on Administration of Monitoring and Compliance Responsibilities

JULY 2003

Standard on Digital Cadastral Maps and Parcel Identifiers

JANUARY 2003

Standard on Facilities, Computers, Equipment, and Supplies

FEBRUARY 2002

Standard on Contracting for Assessment Services

FEBRUARY 2002

Standard on Mass Appraisal of Real Property

JULY 2001

Standard on Assessment Appeal

JULY 2001

Standard on Public Relations

JULY 2001

Standard on Valuation of Property Affected by Environmental Contamination

DECEMBER 2000

Standard on Professional Development

JULY 1999

Standard on Ratio Studies



To order any standards listed above or to  
check current availability and pricing, go to:  
<http://www.iaao.org/publications/standards.html>

**APPENDIX C**

Excerpt (Certification and pages 1-2) from the Grays Harbor County  
Assessor's valuation  
of  
Grays Harbor Energy, LLC's natural gas-fired, combined cycle gas turbine  
merchant power plant at 401 Keys Road, Elma, Washington  
as of January 1, 2004

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**ASSESSOR**

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**GRAYS HARBOR COUNTY**  
**STATE OF WASHINGTON**

**CERTIFICATION**

I hereby certify that to the best of my knowledge and belief the information entered on this petition is a true and fair presentation of the facts relating to this appeal.

Signed this 12th day of Apr. 7, 2007.

David L. Hoels  
Deputy

Cherri Rose-Konschu  
Assessor

**Subject Property:**

The subject property is a state of the art, 628 megawatt, natural gas-fired, combined cycle gas turbine (CCGT) merchant power plant, located at 401 Keys Road, Elma, Washington. Construction of the power plant began in October 2001. Duke Energy North America was the original owner and developer of the property. Commercial operation was expected to begin in 2003. In September 2002, construction was suspended with construction of the \$450 million dollar facility approximately 56% complete. The Assessor's Office was informed by officials from Duke Energy that construction would resume when natural gas prices decreased. The suspension was due to an increase in gas prices and the energy manipulation charges in the California Energy Manipulation case of 2000–2001. There may also have been overbuilding in the industry, although this is not clear. The property was placed in a preservation mode to protect assets.

The generated power was expected to connect with the BPA transmission system at the nearby Satsop switchyard.

Major components that have been installed at the facility include (2) GE-7FA gas turbines, (1) GE D-11 steam turbine, (2) Aalborg Pioneer GT8, triple pressure heat recovery steam generators (HRSG), a 7,000 ton York YK electric chiller system, a 9-cell GEA mechanical draft cooling tower, concrete structural supports for all major pieces of equipment, and much of the computer system for operating the power plant. The site is approximately 22.57 acres in size.

**Zoning:**

The subject property is zoned I-2, Industrial. The intended use is a permitted use under this designation.

**Flood Plain:**

The subject property is located in Zone X, which is outside the 100-year and 500-year flood plain.

**Scope of Appraisal Analysis:**

An inspection of the facility was completed in June of 2003 (new construction). Gerry Lillybridge and David Hoefs of the Grays Harbor County Assessor's Office met with Bob Moroney and Andrew McNeil of Duke Energy, and with Randall Preston of Energy Northwest. Andrew McNeil was the project director for the Grays Harbor power plant. A tour of the facility was conducted and the future of the project was discussed. At this time Duke Energy had no intention of disposing of the power plant. Another inspection of the property was conducted in May/June 2004.

The assets were analyzed as was a study by Elmore Energy, LLC, regarding market value of new power generation equipment. Also a pending sale by Duke Energy to Nevada Power Company was considered (\$186 million for 1,200 MW and ~60% completion).

The appraisal date is January 1, 2004.

On the above date, Gerry Lillybridge determined a Fair Market Value for the suspended construction power plant of **\$97,748,130**. Of this value, \$97,545,000 was attributed to improvements and \$203,130 was attributed to land. In 2003 the assessed value of the improvements was \$119,124,000.

For purposes of this current appraisal, being written in April of 2007 and utilizing a valuation date of January 1, 2004, two of the three approaches to value will be analyzed. These two approaches are the Cost Approach and the Sales Comparison Approach. The Income approach is not applicable as the subject property's construction is not complete and there is no income being derived from the facility.

**Cost Approach:**

The Cost Approach is computed utilizing the **Trended Investment Technique** as determined by the Washington State Department of Revenue, for industrial properties. The original costs are first trended to bring them up to current costs and are then depreciated. Based on the Department of Revenue's schedule, the turbines are depreciated at 7.5%. All other electrical manufacturing M & E is depreciated at 12%. For clarification, the 16% depreciation assigned to gas and diesel generators is for small portable generators only. It is not to be used for power plant generators. Buildings and land improvements are depreciated at 4%.

The original cost of installed improvements for the power plant is \$250,125,891. According to the asset listing submitted, \$20,836,000 in cost was assigned to buildings, structural supports and land improvements. Unfortunately, the asset listing did not adequately break out these kinds of improvements from machinery & equipment. Only \$8,971,011 of their asset listing was deemed to be buildings and land improvements. The remaining balance of \$11,864,989 was linked to machinery & equipment and depreciated at those higher rates.

The trended and depreciated asset listing presents a value via the Cost Approach of **\$192,225,688** for improvements to the site. This value not include \$8,377 designated as personal property, and \$4,019,604 for interest on Duke Capital Corp. Advances.

Gerry Lillybridge valued these assets at \$97,545,000 or 50.7% of what the Cost Approach indicates. In other words he allowed 49.3% of the value of the assets to adjust for the economic obsolescence involved in the suspension of construction due to high fuel prices and other considerations.

Please refer to the Cost Approach Work Up on the following three pages.

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STATE OF WASHINGTON

BY \_\_\_\_\_  
DEPUTY

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON  
DIVISION II

GRAYS HARBOR ENERGY LLC,

Plaintiff/Appellant,

No.: 42558-1-II

v.

**DECLARATION OF MAILING**

GRAYS HARBOR COUNTY,

Defendant/Respondent.

**DECLARATION**

I, Randi M. Toyra hereby declare as follows:

On the 1st day of June, 2012, I mailed a copy of the Brief of Respondent to George C. Mastrodonato and Michael B. King, Carney Badley Spellman, P.S., 701 Fifth Ave., Suite 3600, Seattle, WA 98104-7010, by depositing the same in the United States Mail, postage prepaid.

I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct to the best of my knowledge and belief.

DATED this 1st day of June, 2012, at Montesano, Washington.

