November 20, 2009

TO COUNTY ASSESSORS:

MERCED COUNTY
ASSESSMENT PRACTICES SURVEY

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

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

Fieldwork for this survey was performed by the BOE's County-Assessed Properties Division from January through February 2008. The report does not reflect changes implemented by the assessor after the fieldwork was completed.

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

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

Sincerely,

/s/ David J. Gau

David J. Gau
Deputy Director
Property and Special Taxes Department

DJG:ps
Enclosure
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INTRODUCTION

Although county government has the primary responsibility for local property tax assessment, the State has both a public policy interest and a financial interest in promoting fair and equitable assessments throughout California. The public policy interest arises from the impact of property taxes on taxpayers and the inherently subjective nature of the assessment process. The financial interest derives from state law that annually guarantees California schools a minimum amount of funding; to the extent that property tax revenues fall short of providing this minimum funding level, the State must make up the difference from the general fund.

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

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

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

¹This report covers only the assessment functions of his office.
SCOPE OF ASSESSMENT PRACTICES SURVEYS

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

In addition, pursuant to Revenue and Taxation Code\(^2\) section 75.60, the BOE determines through the survey program whether a county assessment roll meets the standards for purposes of certifying the eligibility of the county to continue to recover costs associated with administering supplemental assessments. Such certification is obtained either by satisfactory statistical result from a sampling of the county's assessment roll, or by a determination by the survey team—based on objective standards defined in regulation—that there are no significant assessment problems in the county. The statutory and regulatory requirements pertaining to the assessment practices survey program are detailed in Appendix B.

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

Since this survey did not include an assessment sample pursuant to Government Code section 15640(c), our review included an examination to determine whether "significant assessment problems" exist, as defined by Rule 371.\(^3\)

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

\(^2\) Unless otherwise stated, all statutory references are to the California Revenue and Taxation Code.
\(^3\) All rule references are to sections of the California Code of Regulations, Title 18, Public Revenues.
EXECUTIVE SUMMARY

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

The assessor is effectively managing most administrative programs, including appraiser certification, assessment appeals, assessment roll changes, and exemptions. However, in the area of implementing disaster relief, the assessor continues to fail to include the correct appeals filing period in the notice of proposed reassessment as required by section 170(c).

As well, most of the assessor's programs for assessing real property are effectively managed. However, we do have a recommendation for improving the assessment of California Land Conservation Act (CLCA) properties. Additionally, we note one area for improvement in the taxable possessory interest program.

The assessor has effective programs for the audit of business property accounts, business equipment valuation, discovery of leased equipment, and discovery and valuation of aircraft, vessels, and animals.

Despite a few problems, we found most properties and property types are assessed correctly. We found no significant assessment problems as defined in Rule 371. Accordingly, pursuant to section 75.60, Merced County continues to be eligible for recovery of costs associated with administering supplemental assessments.

Since Merced County was not selected for assessment sampling pursuant to Government Code section 15643(b), this report does not include the assessment ratios that are generated for surveys that include assessment sampling.

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

RECOMMENDATION 1: Include the correct appeals filing period in the notice of proposed reassessment for property subject to disaster relief as required by section 170(c). ..........................................10

RECOMMENDATION 2: Revise the CLCA assessment program by: (1) establishing a base year value for CLCA homesites at market value; (2) properly inputting compatible use income on CLCA property; and (3) using appropriate risk components for different types of agricultural properties.........................................................25

RECOMMENDATION 3: Exempt property used exclusively for public school purposes from taxable possessory interest assessments. ...........27
OVERVIEW OF MERCED COUNTY

Merced County lies in the heart of California's San Joaquin Valley, about 100 miles southeast of San Francisco and 275 miles north of Los Angeles. The county encompasses about 2,000 square miles. Merced County is bordered by the counties of Stanislaus to the north, Mariposa to the east, Madera and Fresno to the south, and San Benito and Santa Clara to the west. This agricultural county was chartered in 1856.

Just after the Central Pacific Railroad constructed its lines down the San Joaquin Valley in 1872, the City of Merced was established as the county seat. Milk, poultry, cotton, almonds, sweet potatoes, and alfalfa are the leading commodities grown in the county. There are six incorporated cities in the county: Atwater, Dos Palos, Gustine, Livingston, Los Banos, and Merced. Currently, Merced County has a population of over 240,000.

The following table displays information pertinent to the 2007-08 assessment roll:\(^4\)

<table>
<thead>
<tr>
<th>PROPERTY TYPE</th>
<th>ASSESSMENTS</th>
<th>ENROLLED VALUE</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Secured Roll</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Residential</td>
<td>64,149</td>
<td></td>
</tr>
<tr>
<td>Commercial/Industrial</td>
<td>3,517</td>
<td></td>
</tr>
<tr>
<td>Rural</td>
<td>12,287</td>
<td></td>
</tr>
<tr>
<td>Other Secured</td>
<td>1,306</td>
<td></td>
</tr>
<tr>
<td><strong>Total Secured</strong></td>
<td><strong>81,259</strong></td>
<td><strong>$19,109,061,000</strong></td>
</tr>
<tr>
<td><strong>Unsecured Roll</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>8,245</td>
<td><strong>$1,067,138,000</strong></td>
</tr>
<tr>
<td><strong>Total Assessment Roll</strong></td>
<td><strong>89,504</strong></td>
<td><strong>$20,176,199,000</strong></td>
</tr>
</tbody>
</table>

\(^4\) A Report on Budgets, Workloads, and Assessment Appeals Activities 2007-08
The following table illustrates the growth in assessed values over recent years as reported in the BOE's annual reports.\(^5\)

\[
\begin{array}{|c|c|c|c|}
\hline
\text{ROLL YEAR} & \text{TOTAL ROLL VALUE} & \text{INCREASE} & \text{STATEWIDE INCREASE} \\
\hline
2007-08 & $20,176,199,000 & 11.4\% & 9.6\% \\
2006-07 & $18,110,254,000 & 21.3\% & 12.3\% \\
2005-06 & $14,932,765,000 & 15.9\% & 11.1\% \\
2004-05 & $12,888,671,000 & 10.8\% & 8.3\% \\
2003-04 & $11,627,130,000 & 8.3\% & 7.3\% \\
\hline
\end{array}
\]

\(^5\) State Board of Equalization Annual Report, Table 7.
ADMINISTRATION

This section of the survey report focuses on administrative policies and procedures of the assessor's office that affect both the real property and business property assessment programs. Subjects addressed include the assessor's budget and staffing, appraiser certification, assessment appeals, staff property procedures, disaster relief, assessment roll changes, and exemptions.

Budget and Staffing

To enable the assessor to perform his duties, the county board of supervisors annually funds the assessor's office through the county's general fund. The allotted funds are provided so the assessor can produce a timely assessment roll, administer legally permissible exemptions, maintain a set of current maps delineating property ownership, defend assessments as required before an appellate body, and provide information and services to the public as needed.

As shown in the following table, the assessor's budget has grown approximately 30 percent over recent years:

<table>
<thead>
<tr>
<th>BUDGET YEAR</th>
<th>GROSS BUDGET</th>
<th>ANNUAL INCREASE</th>
<th>PERMANENT STAFF</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>$3,371,582</td>
<td>7.69%</td>
<td>36</td>
</tr>
<tr>
<td>2006-07</td>
<td>$3,130,790</td>
<td>1.97%</td>
<td>37</td>
</tr>
<tr>
<td>2005-06</td>
<td>$3,070,217</td>
<td>14.96%</td>
<td>37</td>
</tr>
<tr>
<td>2004-05</td>
<td>$2,670,658</td>
<td>3.01%</td>
<td>38</td>
</tr>
<tr>
<td>2003-04</td>
<td>$2,592,586</td>
<td>NA</td>
<td>38</td>
</tr>
</tbody>
</table>

Staffing for the assessor's office has remained relatively stable over recent years. Currently, there are a total of 36 employees. Staff consists of the assessor, the assistant assessor, a chief appraiser, a chief auditor-appraiser, 2 supervisors, 5 auditor-appraisers, 10 real property appraisers, 5 technicians, and 9 assessment clerks.

The State-County Property Tax Administration Program was discontinued in 2005-06. However, the assessor still has funds remaining; the remaining funds will be used to pay salaries for six employees. These funds will be fully expended during 2007-08, after which time the staff will remain as permanent employees with county funding.

Appraiser Certification

Section 670 provides that no person shall perform the duties of an appraiser for property tax purposes as an employee of any county or city and county unless he or she holds a valid certificate issued by the BOE. There are a total of 21 certified appraisers on staff. We found the
assessor and his staff possess the required certificates. Additionally, we found the auditor-appraisers performing mandatory audits meet the requirements referenced in section 670(d). The assessor does not use contract appraisers.

Section 671(a) requires each holder of a valid appraiser's certificate issued by the BOE to complete a minimum of 24 hours of training each year. Holders of advanced certificates must complete a minimum of 12 hours of training each year per section 671(b).

In Merced County, the assistant assessor performs the duties of the training coordinator. Her responsibilities as training coordinator include:

- Arranging for staff to attend a variety of training opportunities each year, including courses and seminars presented by the BOE, conferences, and classes presented by outside organizations.

- Tracking training hours to ensure staff have the requisite training each year to maintain their appraisal certifications.

The assessor has an effective program for monitoring the training requirements and needs of his staff.

**Staff Property Procedures**

The BOE's assessment practices survey includes a review of the assessor's internal controls and safeguards as they apply to staff-owned properties. This review is done to ensure there are adequate and effective controls in place to prevent the assessor's staff from being involved in valuing property in which they have an ownership interest.

One method used by the assessor to discover employee-owned properties or businesses in Merced County is to require employees who perform appraisals or audits to complete and sign the State of California, Fair Political Practices Commission Form 700, *Statement of Economic Interests* (FPPC Form 700) on a yearly basis. The FPPC Form 700 requests information regarding employee ownership in any real property, other than a primary residence, as well as ownership interest in any business entity. Information provided includes the nature of the interest and the percentage of ownership.

The assessor also becomes aware of employee-owned property from either voluntary disclosure by the employee or by name recognition on permits and recorded documents. Employees are not allowed to value property that they own within the county. Appraisals are initially performed by a supervisor or by a chief appraiser. When an appraisal is completed, it is forwarded to the assessor for final review and approval.

We reviewed a number of appraisal files for employee-owned properties and found no problems.
Assessment Appeals

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

Merced County Ordinance 829 provides for the creation of the county's assessment appeals board and defines its rules. In addition, the assessment appeals board has adopted local rules regarding the conduct of its business. Currently, there is one appeals board consisting of three members, all appointed by the board of supervisors. All members are required to complete the training, as specified in section 1624.02, when appointed to the board.

The regular filing period for appeals in Merced County is July 2nd through November 30th. No appeal in the last five years has gone unresolved for more than two years.

The following table illustrates the assessment appeals workload for recent years:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Appeals Workload:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Appeals Filed</td>
<td>184</td>
<td>181</td>
<td>126</td>
<td>173</td>
<td>242</td>
</tr>
<tr>
<td>Appeals Carried Over From Prior Year</td>
<td>193</td>
<td>182</td>
<td>237</td>
<td>373</td>
<td>276</td>
</tr>
<tr>
<td>Total Appeals Workload</td>
<td><strong>377</strong></td>
<td><strong>363</strong></td>
<td><strong>363</strong></td>
<td><strong>546</strong></td>
<td><strong>518</strong></td>
</tr>
<tr>
<td>Resolution:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Withdrawn</td>
<td>107</td>
<td>115</td>
<td>127</td>
<td>232</td>
<td>61</td>
</tr>
<tr>
<td>Stipulation</td>
<td>28</td>
<td>28</td>
<td>34</td>
<td>59</td>
<td>33</td>
</tr>
<tr>
<td>Appeals Reduced</td>
<td>5</td>
<td>9</td>
<td>19</td>
<td>4</td>
<td>47</td>
</tr>
<tr>
<td>Appeals Upheld</td>
<td>8</td>
<td>18</td>
<td></td>
<td>14</td>
<td>1</td>
</tr>
<tr>
<td>Other Determination</td>
<td>31</td>
<td></td>
<td>1</td>
<td></td>
<td>3</td>
</tr>
<tr>
<td>Total Resolved</td>
<td><strong>179</strong></td>
<td><strong>170</strong></td>
<td><strong>181</strong></td>
<td><strong>309</strong></td>
<td><strong>145</strong></td>
</tr>
<tr>
<td>To Be Carried Over</td>
<td>198</td>
<td>193</td>
<td>182</td>
<td>237</td>
<td>373</td>
</tr>
</tbody>
</table>

The majority of appeals involved commercial, industrial and rural properties. The high number of withdrawn applications is mostly due to the assessor's efforts to ensure the taxpayer is fully informed regarding the value on the roll and the validity of the assessed value.

The clerk of the board of supervisors is responsible for providing applications for changed assessment to the public. Assessment appeal applications are obtained at the board of supervisors' office or through the county's website. The clerk of the board receives the
application, affixes the date received, and reviews it for completeness. If the application is not valid, a letter is sent to notify the taxpayer. Valid applications are reconciled with the assessor's database, logged, and a hearing date is set.

The assessor receives a copy of each application from the clerk of the board, tracks the appeal on a computerized spreadsheet, and sends a letter to the applicant requesting information pursuant to section 441(d). Once the applicant has complied with the request, either the chief property appraiser or the chief auditor-appraiser will assign the appeal to an appraiser or auditor-appraiser.

The appraiser or auditor-appraiser contacts the applicant to explain the assessment and to determine whether there is a basis for reduction of the taxable value. If there is a basis for reduction of the taxable value and if the appraiser can reach an agreement on the value with the applicant, then the applicant may decide to withdraw the appeal or agree to a stipulated value. Applicants deciding to withdraw the appeal are asked to send the clerk of the board a letter confirming the decision to withdraw the appeal. Subsequently, the assessor will perform a roll correction.

If the applicant agrees to a stipulated value, a letter outlining the stipulated values is sent to the applicant for signature. Upon receipt of the signed letter, the assessor forwards the letter to the appeals board for approval. Once approved by the appeals board, the stipulated value is then enrolled by the assessor's office.

If no agreement is reached, the hearing process continues. The appraiser or auditor-appraiser assigned to the appeal, the chief appraiser or chief auditor-appraiser, and the assistant assessor, all represent the assessor's office at board hearings.

We reviewed several assessment appeals' files prepared by the assessor's staff and found them to be well documented and complete. Overall, the assessor's assessment appeals program is well administered.

Disaster Relief

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

To obtain relief under section 170, assessees must make a written application to the assessor requesting reassessment. In addition, if the assessor is aware of any property that has suffered damage by misfortune or calamity, then the assessor must provide the last known assessees with an application for reassessment. Alternatively, the board of supervisors may, by ordinance, grant the assessor the authority to initiate the reassessment without the need for an application if the assessor is aware and determines that within the preceding 12 months taxable property located in the county was damaged or destroyed by misfortune or calamity.
Upon receipt of a properly completed application, or if the assessor initiates reassessment without application via ordinance, the assessor shall reassess the property for tax relief purposes. If the sum of the full cash values of the land, improvements, and personal property before the damage or destruction exceeds the sum of the values after the damage by $10,000 or more, the assessor shall then determine the percentage reductions in current market value and reduce the assessed values by those percentages. However, the amount of the reduction shall not exceed the actual loss.

The assessor discovers instances of disaster or calamity by reviewing newspaper articles, building permits, and fire reports from the fire districts, field canvassing, and by taxpayer-initiated contacts. Upon discovery of a disaster or calamity, the assessor mails an application for reassessment to the property owner. Returned applications are logged, analyzed, and processed if accepted. If denied, property owners are notified by letter. The Merced County Board of Supervisors last amended the disaster relief ordinance in 2002.

In our prior survey, we recommended the assessor include the correct appeals filing period in the notice of proposed reassessment as required by section 170(c). However, the proposed reassessment notice has not been revised as recommended and does not include the appeals filing period as required by section 170(c).

**RECOMMENDATION 1:** Include the correct appeals filing period in the notice of proposed reassessment for property subject to disaster relief as required by section 170(c).

The assessor's notice of proposed reassessment for property subject to disaster relief does not properly inform assessees of their appeal rights as required by section 170(c). The notice used by the assessor is the same notice used to notify an assessee of a supplemental assessment, and consequently, contains the incorrect appeals filing period of 60 days—the filing period for supplemental assessments pursuant to section 1605(c). However, section 170(c), which governs reassessment of property damaged by misfortune or calamity, provides that the applicant may appeal the proposed reassessment to the local board of equalization within six months of the date of mailing the notice.

The assessor's failure to properly advise assessees of the six-month appeals filing period is misleading and does not conform to the statutory provisions.

**Assessment Roll Changes**

Each year the assessor must complete the local assessment roll and deliver it to the auditor by July 1. Once the roll is delivered to the auditor, any correction that would decrease the amount of unpaid taxes requires the consent of the board of supervisors. All changes to the roll are authorized by specific statutes, and any roll change must be accompanied by the appropriate statutory reference.
Assessment roll changes fall under two general categories: escape assessments and corrections. An escape assessment is an assessment of property that was not assessed or was under assessed, for any reason, on the original roll. A correction is any type of authorized change to an existing assessment except for an underassessment caused by an error or omission of the assesse.

For 2007-08, the assessor processed 850 changes to the secured roll and 516 changes to the unsecured roll.

Real property appraisers, auditor-appraisers, and title support staff initiate roll changes. For any change that results in an escape assessment, the computer system automatically generates a notice of enrollment of escape assessment. The assessor mails this notice ten days before the change is entered on the roll pursuant to section 531.8. Merced County has adopted a resolution in accordance with section 1605(c), which allows the tax bill to suffice as the section 534 notice of enrollment of escape assessment. Therefore, a separate notice of enrollment of escape assessment is not needed.

Upon forwarding the roll to the county auditor, the assessor notifies the county auditor to apply penalties and interest when required by citing the appropriate statutory provisions. The assessor also notes penalties on the roll pursuant to Rule 261, and complies with section 532 statute of limitations for making escape assessments. In addition, he makes roll corrections for decline-in-value properties within the one-year statute of limitations pursuant to section 4831(b). The board of supervisors has not adopted an ordinance in accordance with section 531.9 to allow the assessor to cancel low-value roll changes.

**Low-Value Property Tax Exemption**

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

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

The Merced County Board of Supervisors originally enacted a low-value property tax exemption resolution on January 5, 1988. The county subsequently revised the resolution several times, finally adopting Resolution 98-247 on December 22, 1998. This current resolution, in effect until rescinded, exempts from property taxation all property on the secured roll with a base year value, and all property on the unsecured roll with a full value, of $2,000 or less.

For the 2007-08 roll, the assessor identified 948 low-value properties qualifying for a total exemption of $584,643. In applying the low-value property tax exemption, the assessor first enrolls the assessment for both real and personal property and then applies the low-value
property tax exemption. The assessor's computer system tracks low-value property qualifying for the tax exemption. Each property is exempt only until its full value or factored base year value exceeds the tax exemption limit. When property exceeds the limit, the assessor enrolls the taxable value.

In accordance with section 155.20(e)(1), the assessor correctly enrolls low-value new construction unless the total base year value of the property is below the tax exemption limit. For personal property, the assessor correctly determines the lien date value for the exempted property each year.

The assessor consistently applies the tax exemption to all eligible properties. We found no problems with the low-value property tax exemption program.

**Exemptions**

**Church and Religious Exemptions**

Article XIII, section 3(f) of the California Constitution authorizes exemption of property used exclusively for religious worship. This constitutional provision, implemented by section 206, exempts buildings, the land on which they are situated, and equipment used exclusively for religious worship, when such property is owned or leased by a church. Property that is reasonably and necessarily required for church parking is also exempt under article XIII, section 4(d) of the California Constitution, provided that the property is not used for commercial purposes. The church parking exemption is available for owned or leased property meeting the requirements of section 206.1. The Legislature has also implemented the religious exemption in section 207, which exempts from property taxation property owned by a church and used exclusively for religious worship or for both religious worship and school purposes (excluding property used solely for schools of collegiate grade).

County assessors administer the church and religious exemptions. The church exemption, including the church parking exemption, requires an annual filing of the exemption claim. The religious exemption requires a one-time filing by the claimant, although the assessor annually mails a form to claimants to confirm continuing eligibility for the exemption. Once granted, the religious exemption remains in effect until terminated or until the property is no longer eligible for the exemption.
For the 2007-08 assessment roll, the assessor processed 90 church exemption claims and 137 religious exemption claims. The following table illustrates the number of church and religious exemptions granted and the amount of assessed value exempted in Merced County for recent years:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>CHURCH</th>
<th>EXEMPTED VALUE</th>
<th>RELIGIOUS</th>
<th>EXEMPTED VALUE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>90</td>
<td>$33,227,071</td>
<td>137</td>
<td>$66,356,848</td>
</tr>
<tr>
<td>2006-07</td>
<td>77</td>
<td>$27,226,089</td>
<td>129</td>
<td>$58,568,228</td>
</tr>
<tr>
<td>2005-06</td>
<td>79</td>
<td>$27,720,472</td>
<td>146</td>
<td>$65,206,107</td>
</tr>
<tr>
<td>2004-05</td>
<td>76</td>
<td>$30,846,627</td>
<td>154</td>
<td>$62,463,373</td>
</tr>
<tr>
<td>2003-04</td>
<td>70</td>
<td>$18,376,966</td>
<td>165</td>
<td>$54,396,549</td>
</tr>
</tbody>
</table>

The assessor properly processes church and religious exemption claims. We found no problems with these programs.

Welfare Exemption

Article XIII, section 4(b) of the California Constitution authorizes the Legislature to exempt property owned and used exclusively for religious, hospital or charitable purposes by organizations formed and operated exclusively for those purposes. When the Legislature enacted section 214 to implement this constitutional provision, a fourth purpose (scientific) was added. Both the organizational and property use requirements must be met for the exemption to be granted.

The welfare exemption is co-administered by the BOE and county assessors. The BOE is responsible for determining whether an organization itself is eligible for the welfare exemption and for issuing Organizational Clearance Certificates (OCCs) to qualified organizations. The assessor is responsible for determining whether the use of a qualifying organization's property is eligible for exemption and for approving or denying exemption claims.

The assessor may not grant a welfare exemption on an organization's property unless the organization holds a valid OCC issued by the BOE; and, if the property is a low-income housing property owned and operated by a limited partnership, which has a qualified organization (OCC holder) as the managing general partner, then it must also hold a valid Supplemental Clearance Certificate (SCC) issued by the BOE. The assessor may, however, deny an exemption claim, based on non-qualifying use of the property, notwithstanding that the BOE has issued an OCC or SCC to the claimant.
The following table shows the number of welfare exemptions granted and the amount of assessed value exempted in Merced County for recent years:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>WELFARE EXEMPTION</th>
<th>EXEMPTED VALUE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>175</td>
<td>$227,068,500</td>
</tr>
<tr>
<td>2006-07</td>
<td>177</td>
<td>$215,496,154</td>
</tr>
<tr>
<td>2005-06</td>
<td>182</td>
<td>$197,212,811</td>
</tr>
<tr>
<td>2004-05</td>
<td>204</td>
<td>$158,259,370</td>
</tr>
<tr>
<td>2003-04</td>
<td>149</td>
<td>$76,566,747</td>
</tr>
</tbody>
</table>

We reviewed a variety of first-time and annual filings for the welfare exemption, including claims for low-income housing property, some of which were owned by a limited partnership holding an SCC. We found the assessor properly administers the welfare exemption. Accordingly, we have no recommendations in this area.

**Homeowners' and Disabled Veterans' Exemptions**

The homeowners' exemption is authorized by Article XIII, section 3(k) of the California Constitution. This constitutional provision, implemented by section 218, exempts $7,000 of the full value of a dwelling when occupied by an owner as a principal place of residence.

The disabled veterans' exemption is authorized by article XIII, section 4(a) of the California Constitution. This constitutional provision, implemented by section 205.5, exempts a specified amount of the full value of a dwelling when occupied as a principal place of residence by an owner who is a qualified disabled veteran (or unmarried surviving spouse of a deceased disabled veteran). The amount of exemption is $100,000 or, for qualifying low-income veterans, $150,000. Both of these amounts are adjusted annually by a cost of living index.

The homeowners' exemption requires a one-time filing. Once granted, the exemption remains in effect until such time as title to the property changes, the owner does not occupy the dwelling as his or her principal place of residence as of the lien date, or the property is otherwise ineligible. The $100,000 disabled veterans' exemption requires a one-time filing; annual filing is required if the $150,000 low-income veterans' exemption is claimed to determine continued eligibility.
The following table illustrates the number of properties and the amount of assessed value exempted under the homeowners' and disabled veterans' exemptions for recent years:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>HOMEOWNERS'</th>
<th>EXEMPTED VALUE</th>
<th>DISABLED VETERANS'</th>
<th>EXEMPTED VALUE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>31,950</td>
<td>$223,154,764</td>
<td>302</td>
<td>$27,534,534</td>
</tr>
<tr>
<td>2006-07</td>
<td>32,146</td>
<td>$224,570,124</td>
<td>289</td>
<td>$24,871,770</td>
</tr>
<tr>
<td>2005-06</td>
<td>32,731</td>
<td>$228,323,454</td>
<td>298</td>
<td>$24,902,847</td>
</tr>
<tr>
<td>2004-05</td>
<td>31,660</td>
<td>$221,080,473</td>
<td>286</td>
<td>$23,206,383</td>
</tr>
<tr>
<td>2003-04</td>
<td>31,582</td>
<td>$220,398,272</td>
<td>267</td>
<td>$21,045,804</td>
</tr>
</tbody>
</table>

Our review of the assessor's records indicated that the assessor properly processes and administers both the homeowners' and the disabled veterans' exemptions. We have no recommendations for either of these programs.
ASSESSMENT OF REAL PROPERTY

The assessor's program for assessing real property includes the following principal elements:

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

Article XIII A of the California Constitution provides that, absent post-1975 new construction or changes in ownership, the taxable value of real property shall not exceed its 1975 full cash value, except that it can be adjusted annually for inflation by a factor not to exceed two percent.

Change in Ownership

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

Document Processing

All documents recorded with the Merced County Recorder's Office are made available in electronic format to the assessor on a daily basis. The assessor has developed a program that sorts the entire database of the recorder's office by document type for the recorded documents the assessor is interested in reviewing.

The selected documents are screened for any parcels that may require cartographic editing, such as lot line adjustments, lot splits, or other newly created parcels. Legal descriptions are verified, and all recorded documents that pertain to changes in ownership are identified by the title department under supervision of the chief appraiser. Document codes associated with each file determine the routing of the file for further processing.

The percentage of change in ownership involved is documented and entered into the assessor's computer system, which tracks ownership for future events. Appraisals are assigned by geographic area and property type. If transfer documents indicate that a sale involved unusual financing, a trade, or included personal property, the appraiser determines whether a cash equivalency adjustment is warranted. Once the appraisal has been completed, it is submitted to
the chief appraiser, who reviews the documents for correctness and whether it meets appropriate standards.

A history of the number of reappraisals resulting from changes in ownership and their affect on the assessment roll in recent years is illustrated in the table below:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>DOCUMENTS RECEIVED</th>
<th>REAPPRAISABLE EVENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>11,143</td>
<td>5,928</td>
</tr>
<tr>
<td>2006-07</td>
<td>14,588</td>
<td>5,561</td>
</tr>
<tr>
<td>2005-06</td>
<td>18,450</td>
<td>8,532</td>
</tr>
<tr>
<td>2004-05</td>
<td>14,704</td>
<td>7,743</td>
</tr>
</tbody>
</table>

By county ordinance, assessor parcel numbers are required to be noted on all real property documents submitted for recordation. When a change in ownership occurs, the assessor's staff codes the documents so that the homeowner's exemption is removed. Files are flagged where staff determines that the transferee might be eligible for this exemption or for a base year value transfer. Applications for these types of exclusions or exemptions are sent out weekly.

Over the past several years nearly all of the deeds received from the recorder have had the form BOE-502-A, Preliminary Change of Ownership Report (PCOR) attached. The recorder charges a $20 fee when a deed is recorded without a PCOR. The PCOR is available at either the assessor's or the recorder's office.

**Section 69.5 Exclusion**

Section 69.5 generally allows for the transfer of the base year value of a principal residence to a replacement residence of equal or lesser value, provided the property owner is at least 55 years of age, the properties are within the same county, and the owner files a timely claim.

We reviewed several section 69.5 base year value transfer exclusions and found all documents and procedures to be in compliance. In addition, the assessor is currently submitting to the BOE quarterly section 69.5 reports as required by section 69.5(b)(7).
The following table depicts the number of section 69.5 claims granted in Merced County in recent years:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>SECTION 69.5 CLAIMS GRANTED</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006-07</td>
<td>37</td>
</tr>
<tr>
<td>2005-06</td>
<td>45</td>
</tr>
<tr>
<td>2004-05</td>
<td>34</td>
</tr>
</tbody>
</table>

Section 63.1 Exclusion

Section 63.1 generally excludes from the definition of change in ownership the purchase or transfer of the principal residence and the first $1 million of other real property between parents and their children. Certain transfers from grandparents to their grandchildren are also excludable.

We reviewed several section 63.1 transfers and found the assessor's practices and procedures to be in compliance with property tax laws. The assessor submits to the BOE quarterly section 63.1 reports as recommended by the BOE.

The following table depicts the number of section 63.1 claims granted in Merced County over recent years:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>SECTION 63.1 CLAIMS GRANTED</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006-07</td>
<td>24</td>
</tr>
<tr>
<td>2005-06</td>
<td>27</td>
</tr>
<tr>
<td>2004-05</td>
<td>22</td>
</tr>
</tbody>
</table>

We found this program fully complies with section 63.1.

Section 408.1 Transfer List

Pursuant to section 408.1(a), the assessor is required to make available to the public a list showing property transfers that have occurred in the prior two years. The list must include the names of the transferor and transferee if available, the assessor's parcel number (APN), the address of the sold property, the date of transfer, the date of recordation, the document reference number, and, where it is known by the assessor, the amount of consideration paid.

The assessor makes available to the public for a fee the list required by section 408.1. This list is updated monthly. Properties are listed by alphabetical order according to the transferee's name, with all the required information.
Legal Entity Ownership Program (LEOP)

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

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

When the assessor receives the LEOP listing from the BOE, the assessor reviews the list, identifies the parcels involved, and updates the computer database. We found the assessor properly and promptly revalued all parcels undergoing a change of ownership, and reassigned business property to accounts of the new owner.

New Construction

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

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

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

The assessor discovers most new construction activity from issued building permits. The assessor receives building permits from seven permit-issuing agencies, including the county of Merced and the cities of Merced, Atwater, Gustine, Dos Palos, Los Banos, and Livingston. The Merced County Environmental Health Division of the Public Health Department issues all
permits for wells and the Planning and Community Development Department handles building permits. Other methods used by the assessor to discover new construction include review of newspaper articles, field canvassing by appraisers in their assigned areas, and new construction reported on form BOE-571-L, Business Property Statement.

The following table shows the number of new construction permits processed for recent years:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>PERMITS</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>2,081</td>
</tr>
<tr>
<td>2006-07</td>
<td>1,967</td>
</tr>
<tr>
<td>2005-06</td>
<td>2,132</td>
</tr>
<tr>
<td>2004-05</td>
<td>1,870</td>
</tr>
<tr>
<td>2003-04</td>
<td>1,844</td>
</tr>
</tbody>
</table>

Building permits are reviewed by the chief appraiser, who determines if the proposed construction constitutes reappraisable new construction. Building permits considered non-assessable are documented on the building record before being discarded. Building permits considered assessable are issued a supplemental number and forwarded to the appraiser assigned to that area for review.

To obtain construction cost information, the assessor sends a questionnaire to each owner of property that has been issued a building permit. The new construction questionnaires are sent most often for permits indicating residential additions, alterations, pools, patios, and certain electrical permits. Approximately 50 percent of the questionnaires originally sent are completed and returned to the assessor.

The cost data obtained from the questionnaires is desk-reviewed and compared with cost guides. For new construction events that concern both real property and business property, an equipment status report is used to transfer information between the real property staff and the personal property staff. Field inspections are conducted for most new construction.

Valuation

In valuing new construction, the assessor uses all appropriate approaches to value. When valuing residential new construction, the appraisers coordinate the market approach with the cost approach as developed from local construction cost data and the Assessors' Handbook Section 531, Residential Building Costs. When valuing commercial and industrial properties, the assessor develops his cost indicator from the Marshall Valuation Service, and reconciles that indicator with both the income and market approaches. In all new construction valuations, the appraisers attempt to obtain the actual costs from the property owners. The assessor has a thorough and accurate assessment program for new construction.
Declines in Value

Section 51 requires the assessor to enroll on the lien date an assessment that is the lesser of a property's factored base year value (FBYV) or its current full cash value, as defined in section 110. Thus, if a property's full cash value falls below its FBYV on any given lien date, the assessor must enroll that lower value. If, on a subsequent lien date, a property's full cash value rises above its FBYV, then the assessor must enroll the FBYV adjusted for inflation up to two percent.

Due to a recent weakening of the local real estate market, the number of properties experiencing a decline in value below their FBYV has increased dramatically. Residential parcels make up the majority of the new parcels in decline-in-value status. In prior years the properties experiencing declines in value were mostly commercial, industrial, and multi-residential properties.

The following table shows the number of decline-in-value properties over recent years:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>DECLINE-IN-VALUE PROPERTIES</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>5,999</td>
</tr>
<tr>
<td>2006-07</td>
<td>247</td>
</tr>
<tr>
<td>2005-06</td>
<td>225</td>
</tr>
<tr>
<td>2004-05</td>
<td>297</td>
</tr>
<tr>
<td>2003-04</td>
<td>908</td>
</tr>
</tbody>
</table>

To discover property with a current market value that has declined below its FBYV, the assessor relies on his appraisers' knowledge of current property values and on taxpayers' requests for value reviews. In requesting a value review, the taxpayer may come into the assessor's office and complete a Request for Review of Assessment form, or the assessor's staff will complete a request for review form for the taxpayer by telephone.

Once a request is submitted, the chief appraiser gives the request to the supervising appraiser for assignment. The chief appraiser tracks the progress of the request. The appraiser contacts the taxpayer for more information, if needed, and may physically inspect the property. The chief appraiser and the assessor review the final values before they are enrolled.

Merced County has a large quantity of subdivisions or homogeneous tracts; therefore, when a decline in value is discovered in one of these subdivisions or tracts, the appraiser will typically review the entire subdivision or tract and reduce all the values of the homes within the subdivision or tract, if appropriate.

Decline-in-value properties are identified with a taxability code and tracked by the computer system. The taxability code prevents the system from automatically applying the inflation factor to the prior year's taxable value and alerts the chief appraiser of the required annual reviews.
A value notice is sent to the property owner when: (1) the assessed value has changed due to a decline in value; (2) the reduced value is to remain on the roll for the current assessment year; or (3) the decline in value has been fully or partially restored. This notice meets the requirements of section 619(b) and (c).

Overall, the assessor's decline-in-value program is effective and well administered.

**Supplemental Assessments**

Sections 75 through 75.80 mandates that the assessor issue supplemental assessments for changes in ownership and the completion of new construction that occur after the lien date. A supplemental assessment is an assessment that reflects the increase or decrease in assessed value resulting from a change in ownership or completion of new construction for the fiscal year. If a change in ownership or completed new construction occurs on or after January 1 and on or before May 31, two supplemental assessments result from the same event: one for the remainder of the current fiscal year, another for the entire next fiscal year. Clarification regarding supplemental assessments resulting from the completion of new construction is contained in Rule 463.500.

The assessor's computer system processes all supplemental assessments. Appraisers initiate supplemental assessments whenever they establish a new value due to a change in ownership or completed new construction. The computer system automatically calculates supplemental assessment amounts and generates the notice for mailing to the taxpayer. This notice of supplemental assessment includes all of the information required by section 75.31.

After sending the notices to property owners, the assessor forwards supplemental assessment information to the county auditor-controller. Most supplemental tax bills are issued within 60 days from the date the notice of supplemental assessment is issued. This process ensures that supplemental assessments are processed in a timely manner.

We examined several new construction and transfer events and found the assessor processes supplemental assessments as required. The assessor correctly makes two supplemental assessments for events occurring on or after January 1, and on or before May 31, and one supplemental assessment for events occurring on or after June 1, and on or before December 31. Additionally, the assessor properly applies the inflation factor for the following lien date on properties experiencing a supplemental assessment event on or after January 1, and on or before June 30.

We found the assessor grants the builders' exclusion authorized in section 75.12 when claims are timely filed and appropriate. The assessor properly makes supplemental assessments for leasehold improvements, manufactured homes, taxable possessory interests, new construction, and the unrestricted portions of California Land Conservation Act properties.

The assessor's supplemental assessment program is efficiently coordinated and complies with applicable provisions of property tax law.
California Land Conservation Act Properties

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

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

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

For the 2007-08 roll year, Merced County had approximately 3,427 parcels comprising 451,909 acres encumbered by CLCA contracts. The total assessed value of these lands was $1,017,104,667. Included in this acreage were 4,473 acres in nonrenewal status.

Under the provisions of section 423.3, the Merced County Assessor appropriately reduces the factored base year value of CLCA properties and enrolls the lowest of the discounted factored base year value, the restricted value, or the current market value as the taxable value. Additionally, in accordance with Government Code section 51240, the county has adopted a more restrictive cancellation fee rather than the statutorily required minimum fee of 12.5 percent. Merced County's CLCA contracts specify a 10-year enrollment period and a 25 percent cancellation fee.

Most of the rural property in Merced County is devoted to agricultural use, with dairies, chickens, almonds, and cattle producing the largest percentage of value. The county surpassed the $2 billion mark in gross production value of agricultural commodities in 2006, and is one of the largest producing agricultural counties in the nation. Row and field crops, along with turkeys and eggs, are also large commodities within the county.

The valuation of CLCA property in Merced County is the responsibility of the real property appraiser assigned to that specific area. The appraisers mail CLCA questionnaires biannually, and analyze the returned information with other sources of agricultural data to determine the income and expenses for various crop types throughout the county. The data is entered in the computer system to value agricultural properties. Restricted values are automatically calculated in the computer system using the correct capitalization rate, including components for property taxes and risk.

We found the assessor also correctly estimates the income stream for living improvements by utilizing an inclining-stable-declining premise. Supplemental assessments are being made correctly for the unrestricted portions of the contracted parcels.
Homesites

Section 428 provides that the restricted valuation standard for CLCA land does not apply to residences or the site of a residence. AH 521 at page II-51 provides that "even though it might be highly unlikely (or impossible where local zoning regulations forbid the separate parcelization and/or sale of a homesite on an agricultural property) for the homesite to actually be bought and sold in the marketplace, the homesite must be valued as though it were a separate appraisal unit and traded in that manner." In other words, the homesite must be valued at the lesser of the factored base year value or the current market value of a comparable homesite.

Income and Expenses

Agricultural preserve property encumbered by a CLCA contract is assessed on the basis of its agricultural income-producing ability, including any compatible use income.

In defining the income to be capitalized when valuing open-space properties subject to enforceable restrictions, section 423(a)(3) provides that revenue shall be the amount of money or money's worth, which the land can be expected to yield to an owner-operator. Although this income can be derived from any permitted use of the land under the terms by which it is enforecably restricted, section 428 prohibits residential uses from receiving a restricted valuation.

Under these provisions, and in accordance with Government Code sections 51238.1, 51238.2 and 51238.3, the assessor must assume that any use – other than a residential use – allowed by a contract is a compatible use. As indicated, when income generated by this use is attributable to the land, it must be capitalized in the manner specified for restricted properties.

Capitalization Rates

Section 423(b) prescribes the composition of the capitalization rate to be used in determining CLCA-restricted land values. It requires that the capitalization rate shall be the sum of the following components:

- An interest component annually determined and announced by the BOE;
- A risk component based on the location and characteristics of the land, the crops to be grown thereon and the provisions of any lease or rental agreement to which the land is subject;
- A component for property taxes; and
- A component for amortization of any investment in perennials over their estimated economic life when the total income from land and perennials other than timber exceeds the yield from other typical crops grown in the area.

In developing the capitalization rate used in valuing CLCA properties, the assessor correctly uses the current interest component provided annually by the BOE, and also includes components for risk and taxes. However, there are a couple areas needing improvement.
Recommendation

We have the following recommendation for improving the CLCA assessment program.

**RECOMMENDATION 2:** Revise the CLCA assessment program by: (1) establishing a base year value for CLCA homesites at market value; (2) properly inputting compatible use income on CLCA property; and (3) using appropriate risk components for different types of agricultural properties.

Establish a base year value for CLCA homesites at market value.

We found the assessor incorrectly establishes the base year value for homesites based on the homesites per acre proportionate share of the total value of the entire property. The value allocated to the homesite should be its current market value as a residential site separate and apart from the rest of the CLCA property. Also, when a property changes ownership, the land value should be allocated properly between the homesite and the remaining acreage.

Section 428 provides that the restricted valuation standard for CLCA land does not apply to residences or the site of a residence. AH 521 at page II-51, provides that even though it might be highly unlikely (where local zoning regulations forbid the separate parcelization and/or sale of a homesite on an agricultural property) for the homesite to actually be bought and sold in the marketplace, the homesite must be valued as though it were a separate appraisal unit and traded in that manner. In other words, the homesite must be valued at the lesser of the factored base year value or the current market value of a comparable homesite. AH 521 also provides that in determining the value of the residence and homesite, the comparative sales approach is the best method.

By not establishing the base year value for homesites at current market value, the assessor is underassessing those homesites.

Properly input compatible use income on CLCA property.

We found that the assessor attempts to recognize compatible uses for foreign improvement sites on CLCA properties. However, since he does not obtain the information from taxpayers and since his system is not capable of accounting for compatible uses, he arbitrarily increases the crop production of the property to account for compatible use income. This is inappropriate and fails to follow the provisions contained in AH 521.

AH 521 specifically provides that, for foreign improvement sites on CLCA property, the appraiser must first estimate the income and the duration of the compatible use, then capitalize the income as a level annuity. Finally, the present worth of the restricted reversionary value of the land is added to the present worth of the annuity to obtain the value of the compatible use of the property.

The assessor's practice may result in erroneous assessments of CLCA properties.
Use appropriate risk components for different types of agricultural properties.

The assessor uses the same risk component in the valuation of all properties under CLCA contract, regardless of location, property characteristics, or type of crop involved. We found no study or market data to support the use of only one risk rate.

Typically, farmers recognize varying degrees of risk among different types of agricultural properties. Factors such as price stability, production costs, the availability of water, and the probability of damage due to wind and flooding might increase or decrease the risk of a particular property. These factors can affect the income stream to properties relying on production, whereas properties receiving cash rent would not be subject to the same risks.

AH 521 recommends a basic risk component of one percent as a standard guideline for purposes of developing the capitalization rate used in the valuation of CLCA properties. AH 521 also notes that the risk component will vary according to the risks associated with the development of the income to be capitalized. In addition, because location and characteristics of land vary throughout the county, it is reasonable to expect variations in the risk rate used by the assessor. The use of the same risk rate for all properties may result in incorrect assessments of CLCA properties.

**Taxable Government-Owned Properties**

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

For the 2007-08 assessment roll, the assessor enrolled 46 taxable government-owned properties with a total assessed value of approximately $6.7 million.

The assessor determines the status of government-owned properties at the time of acquisition by comparing tax rate area maps to the county's list of government agencies located within each tax rate area. If the property acquired is outside the agency's jurisdiction, the assessor values these taxable government-owned properties annually at the lowest of the restricted value, the factored base year value, or the current market value. Upon annexation by an agency, the assessor exempts these properties since they are now within that agency's boundaries.

We found the assessor correctly values improvements on taxable government-owned properties and properly refrains from issuing supplemental assessments for changes in ownership of taxable government-owned properties. The assessor correctly did not cancel the only CLCA property located on taxable government-owned land, as it was not acquired through condemnation. There are no taxable possessory interests located on any taxable government-owned land in the county.
**Taxable Possessory Interests**

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

For the 2007-08 assessment roll, the assessor enrolled 281 taxable possessory interests with a total assessed value of $55,602,004. Each year, the assessor sends form BOE-502-P, *Possessory Interests Annual Usage Report*, to 60 public agencies owning real property in the county, seeking information on private uses of publicly owned real property. The assessor estimates a response rate of 90 percent to his requests for information. The assessor also discovers taxable possessory interests through periodic inspections of government-owned properties. The assessor, with the assistance of the chief appraiser, performs the majority of the taxable possessory interest appraisals.

The assessor has a comprehensive program for the discovery and enrollment of taxable possessory interests in all publicly owned land in Merced County. We found that the terms of possession used for valuation purposes are reasonable, rents are market-derived, appraisals are well documented, values are determined in a uniform manner, and extensive information is maintained for each taxable possessory interest in a computer database that is updated frequently.

However, we did find one area that needs improvement in the assessor's program for the assessment of taxable possessory interests.

**RECOMMENDATION 3:** Exempt property used exclusively for public school purposes from taxable possessory interest assessments.

The assessor has assessed a food and beverage concessionaire's use of property at the campuses of the local community college. The concessionaire provides food and beverage service to one campus and, if requested to do so, to one other campus. The assessor has based the assessments on the terms of the written lease agreements.

However, property used exclusively for providing services to public schools, community colleges, state colleges, and state universities is exempt from property taxation under article XIII, section 3(d) of the California Constitution. This constitutional provision exempts property used exclusively for public school purposes. It does not require that the public school own the property; thus, privately owned property used exclusively for such purposes may be exempted. The assessor's practice is contrary to the provisions of the California Constitution and, is therefore, an inappropriate assessment of the use of publicly owned property.
Leasehold Improvements

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

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

When real property is reported on form BOE-571-L, Business Property Statement (BPS), coordination between the real property and business property divisions of the assessor's office is important. The reported cost should be examined by both an appraiser in the real property division and an auditor-appraiser in the business property division. The divisions should determine the proper classification of the property to ensure appropriate assessments are being made by each division and to avoid escape and double assessments. The assessor must determine whether costs are for repair and maintenance, and are, therefore, not assessable, whether additions are properly classified as structural improvements or fixtures, and/or if additions are properly enrolled.

The Merced County Assessor follows the guidelines in Assessors' Handbook Section 504, Assessment of Personal Property and Fixtures, for classification between trade fixtures (personal property) and structures (real property).

Discovery

The primary discovery tools for leasehold improvements are through the BPS and form BOE-571-D (Supplemental Schedule for Reporting Monthly Acquisition and Disposal of Property Reported on Schedule B of the Business Property Statement), review of building permits, lease documents, audits, depreciation schedules, field checks, and bulk transfer notices. All costs reported on the BOE-571-L and BOE-571-D are investigated when the audit is conducted.

We found the assessor has an established process for sharing information between the real property and business property staff. Under this process, the business property staff communicates with the real property staff by providing a copy of the BPS and form BOE-571-D, as well as a locally developed building status report. The real property staff reviews the information and contacts the owner of the leasehold improvements to determine if the reported cost is for a trade fixture, a structural improvement, or some non-assessable item such as repair or maintenance.

Subsequently, the real property staff informs the business property staff what action they took on the information provided by the business property staff. This process is in place to prevent double assessments and escaped assessments.
When the real property staff discovers leasehold improvements that should be assessed by the business property staff, they use the Equipment Status Report to alert the business property staff when leasehold improvements have been discovered. The real property staff is responsible for the assessment of leasehold improvements classified as structures; the business property staff is responsible for assessing leasehold improvements classified as fixtures. We reviewed assessments for leasehold improvements, foreign improvements, and cell towers and found no problems.

Valuation

Structural items are classified as real property and assessed at the lower of their factored base year value or current market value. Leasehold improvements are assessed to the lessee except when there exists a documented agreement between lessor and lessee to do otherwise.

When leasehold improvements are abandoned, the business property division deactivates the account and notifies the real property division, who then determines whether the leasehold improvements should be added to the lessor's secured account. Supplemental assessments are applied to structural leasehold improvements on both the secured and unsecured rolls.

We found no problems with the assessment of leasehold improvements.

Pipeline Rights-of-Way

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

Prior to the appellate court decision in 1993, the BOE developed "density classifications" for comparative appraisal purposes to value pipeline rights-of-way. In 1996, the state passed legislation that precluded legal challenge by taxpayers of any assessment made in accordance with the BOE's density classifications. Accordingly, assessors lose this statutory presumption of correctness if they value rights-of-way using another method.

For the 2007-08 roll, Merced County had six pipeline rights-of-way assessed at approximately $2.5 million. For each inter-county pipeline assessed by the BOE, the assessor correctly values the local pipeline rights-of-way using the appropriate density classification and value schedule found in section 401.10(a)(1)(A). The assessor also maintains separate assessments for each parcel of the pipeline right-of-way. However, for billing purposes, the assessor combines each assessment into a single, countywide assessment per taxpayer, as required by section 401.8. The assessor also values multiple pipelines in a right-of-way using the standard prescribed by section 401.10(a)(3)(A).

We found pipeline rights-of-way in Merced County are valued in accordance with sections 401.8 through 401.12.
ASSESSMENT OF PERSONAL PROPERTY AND FIXTURES

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

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

As of February 2008, the assessor's staff assigned to the business property division consisted of seven positions: one chief auditor-appraiser, five auditor-appraisers, and one real property appraiser. The real property appraiser works in conjunction with the auditor-appraisers to ensure the correct classification and allocation of real and personal property items assessed to businesses. This staffing mix maximizes the coordination of real property and business property assessments.

Audits

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

Prior to January 1, 2009, section 469 required county assessors to audit, at least once every four years, the books and records of any taxpayer engaged in a profession, trade, or business, if the taxpayer has assessable trade fixtures and business tangible personal property valued at $400,000 or more. These statutorily required audits are commonly referred to as mandatory audits. Additionally, a county assessor may audit the books and records of taxpayers with holdings below $400,000 in value under the authority of section 470. These audits are referred to as non-mandatory audits. Generally, county assessors perform both mandatory and non-mandatory audits to ensure that their audit program includes a representative sample of all sizes and types of taxpayers with personal property holdings subject to the property tax.

Effective January 1, 2009, county assessors are no longer required to audit all taxpayers with trade fixture and business tangible personal property holdings of $400,000 or more at least once every four years. Instead, the county assessors are required to annually audit a significant number of audits as specified in section 469, as amended. The significant number of audits required is at least 75 percent of the fiscal year average of the total number of mandatory audits the assessor was required to have conducted during the 2002–03 fiscal year to the 2005–06 fiscal year, with at least 50 percent to be selected from a pool of those taxpayers with the largest
assessments. Thus, while section 469 still mandates a certain level of audits that must be performed annually, assessors now have some flexibility in determining which accounts will comprise this mandated workload.

The following table shows the total number of audits completed in Merced County for recent years:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>TOTAL AUDITS</th>
<th>MANDATORY AUDITS</th>
<th>NONMANDATORY AUDITS</th>
<th>NET VALUE CHANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>158</td>
<td>107</td>
<td>51</td>
<td>$133,396,410</td>
</tr>
<tr>
<td>2006-07</td>
<td>151</td>
<td>122</td>
<td>29</td>
<td>$49,842,466</td>
</tr>
<tr>
<td>2005-06</td>
<td>108</td>
<td>70</td>
<td>38</td>
<td>$135,951,468</td>
</tr>
</tbody>
</table>

Based on the assessor's recent audit workload history, the assessor is in compliance with the requirements of section 469.

Statute of Limitations

Section 532 provides that when the assessor discovers through an audit that property has escaped assessment, an assessment of such property must be enrolled within four years after July 1 of the assessment year during which the property escaped assessment. If the assessor cannot complete an audit within the prescribed time period, the assessor may request, pursuant to section 532.1, a waiver of the statute of limitations from the taxpayer to extend the time for making an assessment.

The assessor's office does not request waivers when a mandatory audit cannot be completed within the statutory time frame defined in section 532. Instead, the assessor completes the audit for the year when the statute of limitations will expire and then schedules the remaining three years for audit in the next fiscal year.

We found the assessor's office had eight audits that were carried over for fiscal year 2007-08. For these accounts, we verified that the assessor completed an audit for the one year subject to expiration due to the statute of limitations and for the remaining three years in the following fiscal year.

Audit Quality

An audit should follow a standard format so that the auditor-appraiser may easily determine whether the property owner has correctly reported all taxable property. Audit narratives and summaries should include adequate documentation, full value calculations, reconciliation of the fixed assets totals to the general ledger and financial statements, review of asset invoices, reconciliation between reported and audit amounts, an analysis of expense accounts, and an analysis of depreciation and obsolescence factors that may affect the value of the business property.
We found that the assessor performs change in control (ownership) reviews, verifies leased equipment, enrolls construction in progress, accounts for supplies, and properly classifies equipment, among other things. In all cases, mandatory audits reviewed were accurate, well documented, and supported by a comprehensive audit checklist defining the areas of investigation.

**Business Property Statement Processing**

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

We reviewed the assessor's property statement processing procedures and files to ensure that they conform to statutory and regulatory guidelines. A sampling of BPSs was reviewed to verify the use of BOE-prescribed forms, processing by certified staff, completeness of the property statements, application of penalties, coordination with the real property division, record storage, and retention.

During our review, we found that staff checked for completeness and for a valid signature on all BPS forms, and that all statements were date-stamped when received. If a statement was unsigned, a copy was made and the original was returned to the taxpayer. If a statement was received late, the date-stamped envelope was retained and a penalty was added as prescribed by section 463. If a statement reported any additions or deletions to real property items, those changes were referred to the real property division for review.

Our review included verifying written authorization for agents to sign property statements on behalf of the property owners. We found that the assessor maintained the written authorizations in the business property files and that the BPSs were being processed properly.

Beginning in 2005-06, the Merced County Assessor began accepting efiled property statements. In 2007-08, the assessor received approximately 40 electronically filed property statements. The assessor's assessment system accommodates signature authentication for each taxpayer. The method of efile signature authentication is in compliance with section 441(k).
The following table displays the assessor's workload of property statements for businesses, leased equipment, and other property types for the 2007-08 assessment roll:

<table>
<thead>
<tr>
<th>CATEGORY</th>
<th>PROPERTY STATEMENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>12,287</td>
</tr>
<tr>
<td>Apartments</td>
<td>924</td>
</tr>
<tr>
<td>Direct Bill</td>
<td>1,501</td>
</tr>
<tr>
<td>Financial</td>
<td>48</td>
</tr>
<tr>
<td>Gen. Business</td>
<td>3,116</td>
</tr>
<tr>
<td>Leased Equip.</td>
<td>355</td>
</tr>
<tr>
<td>Service Stations</td>
<td>62</td>
</tr>
<tr>
<td>Vessels</td>
<td>2,646</td>
</tr>
<tr>
<td>Aircraft</td>
<td>311</td>
</tr>
<tr>
<td>Water Company</td>
<td>5</td>
</tr>
<tr>
<td>Power Company</td>
<td>5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>21,260</strong></td>
</tr>
</tbody>
</table>

**Discovery**

The discovery of taxable property is an essential function of the county assessor. It is a difficult but necessary task to maintain accurate and current listings of assessable business properties. Discovery sources are field canvassing, review of building permits, business licenses, business directories, telephone directories, form BOE-600-B, *Report of Locally Assessable Equipment Leased to State Assessees*, and tenant information supplied from landlords.

The assessor has an adequate discovery program. We found no problems with the assessor's BPS processing program.

**Direct Billing**

Many California assessors utilize an assessment procedure called "direct billing" or "direct assessment." It is a method of assessing certain lower-value business property accounts without the need of annual filing of a BPS. The assessor establishes an initial value for the business property and continues that value for several years. Property statement filings or field reviews are only periodically required. Examples of businesses suitable for direct billing include apartments, barber shops, beauty parlors, coin-operated launderettes, small cafes and small restaurants, and professional firms with small equipment holdings.
The direct billing program is beneficial to both the taxpayer and the assessor. It results in a reduction of paperwork for taxpayers and fewer BPSs that must be processed annually by the assessor's staff, increasing time available for the auditor-appraisers to perform other required duties.

The Merced County Assessor has a direct billing program. The accounts that are direct-billed are generally stable and are less than $10,000 in full cash value of reportable business property. Every four years the assessor sends a BPS to direct-billed taxpayers to determine if there have been any substantial changes of business property, including increased equipment, decreased equipment, sale of the business, any change in ownership, or a change in location. The assessor then decides whether the account is still suitable for direct billing.

If the account is no longer suitable for direct billing, the account reverts back to a regular account and resumes yearly BPS mailings. For fiscal year 2007-08, the assessor directly billed 1,501 accounts.

**Business Equipment Valuation**

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

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

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

Valuation factors are the product of price index factors and the percent good factors. The proper choice and application of valuation factors to historical cost produces an estimate of market value.

The assessor uses primarily AH 581 and the California Assessors' Association's business assessment factors to value assessable machinery and equipment. In some instances, the assessor uses factors developed from his own studies for some categories of equipment in use past their normal service lives. The assessor also uses the *Marshall Valuation Service* when valuing large industrial propane tanks.

**Leased Equipment**

The business property division is responsible for the discovery, valuation, and assessment of leased equipment. This type of property is one of the more difficult to assess correctly. Common problems include difficulty in establishing taxability and taxable situs, reporting errors by lessees.
and lessors, valuation (whether the value of the equipment should be the lessor's cost or the cost for the consumer purchasing the equipment), and double or escape assessments resulting from combined lessor and lessee reporting. These issues are discussed in detail in Assessors' Handbook Section 504, Assessment of Personal Property and Fixtures.

Lessees are required to report all leased property (taxable property in their possession, but belonging to others) on their annual property statement. They are also required to provide information on the type of property, the year of acquisition and manufacture, the cost, a description or lease number, and the owner's name and address. A cross-check of information reported by lessors and lessees verifies the accuracy of the reported information.

In Merced County, the assessor sends a supplemental form, titled Lessor's Report of Leased Equipment, along with the BPS to accommodate the reporting of numerous leased assets. Whenever possible an auditor-appraiser processes leasing company returns first in order to facilitate expedient coordination with lessee enrollments.

The auditor-appraiser first reviews the submitted statement for completeness, and begins processing the statement by addressing the lease expirations occurring during the reporting period. Copies of "drop-off" or contractually expired leased equipment declarations are filed in the lessee's property record to aid in future processing of the lessee's statement. The auditor-appraiser then cross-references the current reported cost information with previous enrollments to ensure reasonableness. New taxable equipment information is updated and new assessments are created as necessary.

When processing lessee's statements that include leased equipment reported on Part III of the BOE-571-L, an auditor-appraiser cross-references the reported information with the lessor's property statement to determine if the equipment is already assessed to the lessor of the property. If the reported leased equipment has not been reported and enrolled to the lessor, the processor can either enroll the equipment and assess it to the lessee or contact the lessor for further information. This exercise helps reduce the possibility of double or escape assessments.

We reviewed the annual property statements of several lessors and lessees recently processed by the business property staff. We focused our analysis on the valuation methods, completeness of reporting, tracking of equipment, correct assessee designation, correct expired lease disposition, and correct processing procedures. The assessor maintains effective procedures for the enrollment and tracking of leased equipment. We found the assessor properly distinguishes between leases and conditional sales contracts, and follows correct appraisal and assessment procedures.

**Manufactured Homes**

A "manufactured home" is defined in Health and Safety Code sections 18007 and 18008, and statutes prescribing the method of assessing manufactured homes are contained in sections 5800 through 5842. A manufactured home is subject to local property taxation if sold new on or after July 1, 1980, or if its owner requests conversion from the vehicle license fee to local property taxation. Manufactured homes should be classified as personal property and enrolled on the secured roll.
In Merced County, manufactured homes are located in 36 mobilehome parks, rented land, and on fee-owned land. Manufactured homes located in mobilehome parks and on rented land are assigned an assessor parcel number beginning with 910. Manufactured homes owned by the owner of the land on which they are situated are identified as personal property and enrolled under the land's assessor parcel number. For the 2007-08 roll, there were 1,585 manufactured homes enrolled under a 910 assessment number, and 1,884 enrolled under the lands' assessment numbers. The value of manufactured homes totaled $89,353,159.

The assessor learns of new taxable manufactured home sales, new installations, and voluntary conversions of manufactured homes through periodic State Department of Housing and Community Development listings. These listings are supplemented by dealer reports of sale, building permits, deed recordings, form BOE-502-AH, Preliminary Change of Ownership Reports, and periodic tax clearance notifications from the county tax collector's office.

Each appraiser is responsible for manufactured home assessments in his or her assigned areas. In determining the full cash value of a manufactured home on rented or leased land, the assessor, pursuant to section 5803, must take into consideration the sales prices listed in recognized value guides for manufactured homes. Recognized value guides include, but are not limited to, the Kelley Blue Book Manufactured Housing Used Value Guide (Blue Book) and the National Automobile Dealers Association's Manufactured Housing Appraisal Guide (NADA).

In previous years, the assessor would compare the NADA with the sales price and adjust accordingly for any site influence. For the 2007-08 roll, the assessor has transitioned from the NADA to the Assessors' Handbook Section 531.35. When applicable, supplemental assessments are processed. The assessor also properly notifies the auditor-controller not to impose special assessments on manufactured homes.

The assessment program for manufactured homes is well-administered, and we have no recommendations.

**Aircraft**

There are two categories of aircraft that are subject to personal property tax: general aircraft (certain qualified historical aircraft may qualify for an exemption) and certificated or commercial aircraft.

**General Aircraft**

General aircraft are privately owned aircraft used for pleasure or business but not authorized to carry passengers, mail, or freight on a commercial basis (the contrast between general aircraft and certificated aircraft is discussed below). Section 5363 requires the assessor to determine the market value of all aircraft according to standards and guidelines prescribed by the BOE. Section 5364 requires the BOE to establish such standards. On January 10, 1997, the Board approved the Aircraft Bluebook-Price Digest (Bluebook) as the primary guide for valuing aircraft with the Vref Aircraft Value Reference (Vref) as an alternative guide for aircraft not listed in the Bluebook.
For 2007-08, the Merced County Assessor assessed 296 general aircraft with a total value of $30,078,582. Each of the five auditor-appraisers performs valuation and administrative duties related to the assessor's aircraft program. The assessor discovers aircraft through airport operators' tenant listings, the Federal Aviation Administration website, the landing aviation database, and other counties' referrals.

In Merced County, only certificated property appraisers assume valuation duties regarding aircraft. An aircraft property statement is mailed each year to the known owner of each aircraft in the county. The form requests the owner to report the year, make, model, and tail number of the aircraft, as well as installed avionics, engine air hours since last major overhaul, date of last overhaul, overall condition, air worthiness status, cost information, and transfer information if the aircraft has been sold since the last lien date.

Upon receipt of the taxpayer-submitted aircraft property statement, the assessor utilizes an electronic version of the *Bluebook* to calculate a market value indicator. Adjustments for sales tax, overall condition of the aircraft, additional or special equipment, airframe hours, and engine hours since last major overhaul, are properly incorporated into the calculation to determine a market value estimate. The values of newer aircraft are most affected by the presence or lack of optional equipment, while the values of older aircraft are influenced more by the condition of the aircraft.

We reviewed several general aircraft records for valuation methodology, legal signatures on the property statement, and the application of late-filing or failure-to-file penalties pursuant to section 5367. We found the assessor's procedures for the discovery and valuation of general aircraft conform to statutory provisions and guidelines set forth in the Assessor's Handbook Section 577, *Assessment of General Aircraft*.

**Certificated Aircraft**

Certificated aircraft are aircraft operated by air carriers (including air taxis that are operated in scheduled air taxi operation). Unlike general aircraft, which are normally assessed at a rate of 100 percent at the place where they are "habitually located" on the lien date, the assessments of certificated aircraft are allocated among taxing jurisdictions based upon ground and flight time and the number of arrivals and departures during a representative period (the period is designated by the BOE). Certificated aircraft are assessed in accordance with the methods described in section 401.17.

Two commercial air carriers flew in and out of the Merced Municipal Airport during the 2007-08 assessment year. For the 2007-08 roll, the assessor enrolled a total of $618,970 in assessed value to these two air carriers.

Auditor-appraisers responsible for certificated aircraft valuation predicate their appraisals on the aircraft statement reported costs. The appraiser then applies a percentage based on ground and flight time and the number of arrivals and departures in Merced County during the representative period to the reported costs, to derive a pro rata estimate of the taxable value for the certificated aircraft.
We reviewed the certificated aircraft appraisal procedures and found them to be correctly administered and the estimates of value to be properly calculated.

**Historical Aircraft**

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

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

There were 15 historical aircraft assessed on the 2007-08 roll with a total value of $920,960. The assessor properly obtains signed affidavits in the format prescribed by the BOE, as well as certifications of attendance for historical aircraft exemptions claimed pursuant to section 220.5(c).

We reviewed several historical aircraft assessments and exemption claims. We found the assessor properly granted the exemption when the legal conditions were met. We also were able to confirm that the assessor correctly applies the statutorily allowed partial exemption when the affidavit is filed late, between February 16th and August 2nd. We reviewed several declarations of historical aircraft claimant forms and found no problems.

**Vessels**

Assessors must annually appraise all vessels at market value. The primary sources used for the discovery of assessable vessels include reports from the State Department of Motor Vehicles (DMV), referrals from other counties, information provided by the vessel owners themselves, certificates of documentation issued by the United States Coast Guard, harbormasters' reports, and field canvassing.
The following table details the number of vessel assessments and their assessed values for Merced County for recent years:

<table>
<thead>
<tr>
<th>ROLL YEAR</th>
<th>PLEASURE VESSELS</th>
<th>ASSESSED VALUE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>2,646</td>
<td>$25,705,417</td>
</tr>
<tr>
<td>2006-07</td>
<td>2,650</td>
<td>$25,064,289</td>
</tr>
<tr>
<td>2005-06</td>
<td>2,539</td>
<td>$22,453,827</td>
</tr>
</tbody>
</table>

An auditor-appraiser is responsible for vessel-related property statement processing; after processing the statements, the statements are reviewed by the chief auditor-appraiser. The primary sources of discovery of assessable vessels are from DMV reports, referrals from other counties, and from vessel owners themselves. The assessor mainly uses the *ABOS Marine Blue Book* and, if needed, the *National Automobile Dealer Association’s Marine Appraisal Guide* (Winter Editions) to value vessels. If current or reliable information is not available in the published value guides, the assessor may use the values of similar vessels within his own database, or other sources to obtain current, comparable sales data.

Upon receipt of completed vessel statements, an auditor-appraiser processes each statement and derives a value using one of the published value guides, adding sales tax as required. For vessels not new to the county, values are derived from a depreciation table obtained from a vessel value study conducted by the Shasta County Assessor.

In reviewing a sample of vessel assessments, we found that appropriate valuation methods were employed, including adding sales tax, and adjusting for condition and additional equipment. We found that procedures for processing, appraising, and assessing vessels were adequate; we have no recommendations.

**Animals**

Section 1(a) of Article XIII of the California Constitution mandates that all property is taxable unless specifically exempt under the California Constitution, the laws of the United States, or, in the case of personal property, by act of the Legislature. Most animals are exempt from taxation. Pets are exempt under section 224. Many animals that are considered business inventory are exempt under sections 129 and 219, and by Rule 133.

Merced County has very few assessable animals. Most animals are reported on either form BOE-571-F, *Agricultural Property Statement*, or form BOE-571-F2, *Registered and Show Horse Statement*. Methods of discovering taxable animals include referrals from the real property division, telephone yellow pages, animals reported on the *Agricultural Property Statements*, and audits of agricultural property.

We reviewed the procedures for discovering and assessing taxable animals and found that the program is well administered.
APPENDIXES

A. County-Assessed Properties Division Survey Group

Merced County

Chief
Dean Kinnee

Survey Program Director:
Benjamin Tang Principal Property Appraiser

Survey Team Supervisor:
Sally Boeck Supervising Property Appraiser

Survey Team Leader:
Alan Dannen Associate Auditor-Appraiser

Survey Team:
Jeffrey Arthur Associate Auditor-Appraiser
Catherine Houlihan Associate Auditor-Appraiser
Zella Cunningham Associate Property Appraiser
Deborah Scherer Associate Property Appraiser
Andrew Austin Assistant Property Appraiser
Chandra Williams Associate Tax Auditor
Prubjit Singh Tax Technician I
B. Relevant Statutes and Regulations

Government Code

15640. Survey by board of county assessment procedures.

(a) The State Board of Equalization shall make surveys in each county and city and county to determine the adequacy of the procedures and practices employed by the county assessor in the valuation of property for the purposes of taxation and in the performance generally of the duties enjoined upon him or her.

(b) The surveys shall include a review of the practices of the assessor with respect to uniformity of treatment of all classes of property to ensure that all classes are treated equitably, and that no class receives a systematic overvaluation or undervaluation as compared to other classes of property in the county or city and county.

(c) The surveys may include a sampling of assessments from the local assessment rolls. Any sampling conducted pursuant to subdivision (b) of Section 15643 shall be sufficient in size and dispersion to insure an adequate representation therein of the several classes of property throughout the county.

(d) In addition, the board may periodically conduct statewide surveys limited in scope to specific topics, issues, or problems requiring immediate attention.

(e) The board's duly authorized representatives shall, for purposes of these surveys, have access to, and may make copies of, all records, public or otherwise, maintained in the office of any county assessor.

(f) The board shall develop procedures to carry out its duties under this section after consultation with the California Assessors' Association. The board shall also provide a right to each county assessor to appeal to the board appraisals made within his or her county where differences have not been resolved before completion of a field review and shall adopt procedures to implement the appeal process.

15641. Audit of records; appraisal data not public.

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

No appraisal data relating to individual properties obtained for the purposes of any survey under this chapter shall be made public, and no state or local officer or employee thereof gaining knowledge thereof in any action taken under this chapter shall make any disclosure with respect thereto except as that may be required for the purposes of this chapter. Except as specifically provided herein, any appraisal data may be disclosed by the board to any assessor, or by the board or the assessor to the assessee of the property to which the data relate.
The board shall permit an assessee of property to inspect, at the appropriate office of the board, any information and records relating to an appraisal of his or her property, including "market data" as defined in Section 408. However, no information or records, other than "market data," which relate to the property or business affairs of a person other than the assessee shall be disclosed.

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

15642. Research by board employees.

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

15643. When surveys to be made.

(a) The board shall proceed with the surveys of the assessment procedures and practices in the several counties and cities and counties as rapidly as feasible, and shall repeat or supplement each survey at least once in five years.

(b) The surveys of the ten largest counties and cities and counties shall include a sampling of assessments on the local assessment rolls as described in Section 15640. In addition, the board shall each year, in accordance with procedures established by the board by regulation, select at random at least three of the remaining counties or cities and counties, and conduct a sample of assessments on the local assessment roll in those counties. If the board finds that a county or city and county has "significant assessment problems," as provided in Section 75.60 of the Revenue and Taxation Code, a sample of assessments will be conducted in that county or city and county in lieu of a county or city and county selected at random. The ten largest counties and cities and counties shall be determined based upon the total value of locally assessed property located in the counties and cities and counties on the lien date that falls within the calendar year of 1995 and every fifth calendar year thereafter.

(c) The statewide surveys which are limited in scope to specific topics, issues, or problems may be conducted whenever the board determines that a need exists to conduct a survey.
(d) When requested by the legislative body or the assessor of any county or city and county to perform a survey not otherwise scheduled, the board may enter into a contract with the requesting local agency to conduct that survey. The contract may provide for a board sampling of assessments on the local roll. The amount of the contracts shall not be less than the cost to the board, and shall be subject to regulations approved by the Director of General Services.

15644. Recommendations by board.

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

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

(a) Upon completion of a survey of the procedures and practices of a county assessor, the board shall prepare a written survey report setting forth its findings and recommendations and transmit a copy to the assessor. In addition the board may file with the assessor a confidential report containing matters relating to personnel. Before preparing its written survey report, the board shall meet with the assessor to discuss and confer on those matters which may be included in the written survey report.

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

The board may, for good cause, extend the period for filing the response.

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

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

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

75.60. Allocation for administration.

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

(b) For purposes of this section:

(1) "Actual administrative costs" includes only those direct costs for administration, data processing, collection, and appeal that are incurred by county auditors, assessors, and tax collectors. "Actual administrative costs" also includes those indirect costs for administration, data processing, collections, and appeal that are incurred by county auditors, assessors, and tax collectors and are allowed by state and federal audit standards pursuant to the A-87 Cost Allocation Program.

(2) "Eligible county or city and county" means a county or city and county that has been certified by the State Board of Equalization as an eligible county or city and county. The State Board of Equalization shall certify a county or city and county as an eligible county or city and county only if both of the following are determined to exist:

(A) The average assessment level in the county or city and county is at least 95 percent of the assessment level required by statute, as determined by the board's most recent survey of that county or city and county performed pursuant to Section 15640 of the Government Code.

(B) For any survey of a county assessment roll for the 1996-97 fiscal year and each fiscal year thereafter, the sum of the absolute values of the differences from the statutorily required assessment level described in subparagraph (A) does not exceed 7.5 percent of the total amount of the county's or city and county's statutorily required assessed value, as determined pursuant to the board's survey described in subparagraph (A).
(3) Each certification of a county or city and county shall be valid only until the next survey made by the board. If a county or city and county has been certified following a survey that includes a sampling of assessments, the board may continue to certify that county or city and county following a survey that does not include sampling if the board finds in the survey conducted without sampling that there are no significant assessment problems in the county or city and county. The board shall, by regulation, define "significant assessment problems" for purposes of this section, and that definition shall include objective standards to measure performance. If the board finds in the survey conducted without sampling that significant assessment problems exist, the board shall conduct a sampling of assessments in that county or city and county to determine if it is an eligible county or city and county. If a county or city and county is not certified by the board, it may request a new survey in advance of the regularly scheduled survey, provided that it agrees to pay for the cost of the survey.

Title 18, California Code of Regulations

Rule 370. Random selection of counties for representative sampling.

(a) SURVEY CYCLE. The board shall select at random at least three counties from among all except the ten largest counties and cities and counties for a representative sampling of assessments in accordance with the procedures contained herein. Counties eligible for random selection will be distributed as equally as possible in a five-year rotation commencing with the local assessment roll for the 1997–98 fiscal year.

(b) RANDOM SELECTION FOR ASSESSMENT SAMPLING. The three counties selected at random will be drawn from the group of counties scheduled in that year for surveys of assessment practices. The scheduled counties will be ranked according to the size of their local assessment rolls for the year prior to the sampling.

(1) If no county has been selected for an assessment sampling on the basis of significant assessment problems as provided in subdivision (c), the counties eligible in that year for random selection will be divided into three groups (small, medium, and large), such that each county has an equal chance of being selected. One county will be selected at random by the board from each of these groups. The board may randomly select an additional county or counties to be included in any survey cycle year. The selection will be done by lot, with a representative of the California Assessors' Association witnessing the selection process.

(2) If one or more counties are scheduled for an assessment sampling in that year because they were found to have significant assessment problems, the counties eligible for random selection will be divided into the same number of groups as there are counties to be randomly selected, such that each county has an equal chance of being selected. For example, if one county is to be sampled because it was found to have significant assessment problems, only two counties will then be randomly selected and the pool of eligible counties will be divided into two groups. If two counties are to be sampled because they were found to have significant assessment problems, only one county will be randomly selected and all counties eligible in that year for random selection will be pooled into one group.
(3) Once random selection has been made, neither the counties selected for an assessment sampling nor the remaining counties in the group for that fiscal year shall again become eligible for random selection until the next fiscal year in which such counties are scheduled for an assessment practices survey, as determined by the five-year rotation. At that time, both the counties selected and the remaining counties in that group shall again be eligible for random selection.

(c) ASSESSMENT SAMPLING OF COUNTIES WITH SIGNIFICANT ASSESSMENT PROBLEMS. If the board finds during the course of an assessment practices survey that a county has significant assessment problems as defined in Rule 371, the board shall conduct a sampling of assessments in that county in lieu of conducting a sampling in a county selected at random.

(d) ADDITIONAL SURVEYS. This regulation shall not be construed to prohibit the BOE from conducting additional surveys, samples, or other investigations of any county assessor's office.


(a) For purposes of Revenue and Taxation Code Section 75.60 and Government Code Section 15643, "significant assessment problems" means procedure(s) in one or more areas of an assessor's assessment operation, which alone or in combination, have been found by the BOE to indicate a reasonable probability that either:

(1) the average assessment level in the county is less than 95 percent of the assessment level required by statute; or

(2) the sum of all the differences between the board's appraisals and the assessor's values (without regard to whether the differences are underassessments or overassessments), expanded statistically over the assessor's entire roll, exceeds 7.5 percent of the assessment level required by statute.

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

(1) Uniformity of treatment for all classes of property.

(2) Discovering and assessing newly constructed property.

(3) Discovering and assessing real property that has undergone a change in ownership.

(4) Conducting mandatory audits in accordance with Revenue and Taxation Code Section 469 and Property Tax Rule 192.

(5) Assessing open-space land subject to enforceable restriction, in accordance with Revenue and Taxation Code Sections 421 et. seq.
(6) Discovering and assessing taxable possessory interests in accordance with Revenue and Taxation Code Sections 107 et. seq.

(7) Discovering and assessing mineral-producing properties in accordance with Property Tax Rule 469.

(8) Discovering and assessing property that has suffered a decline in value.

(9) Reviewing, adjusting, and, if appropriate, defending assessments for which taxpayers have filed applications for reduction with the local assessment appeals board.

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

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

The Merced County Assessor's response begins on the next page. The BOE has no comments on the response.
September 29, 2009

Mr. Dean R. Kinnee, Chief  
County-Assessed Properties Division  
State Board of Equalization  
P.O. Box 942879  
Sacramento Ca 94279-0062

Dear Mr. Kinnee:

We would like to acknowledge the Board’s survey team members. They conducted their business with consideration, professionalism and diligence. Having the survey team in the office allowed for open discussion as to practices and procedures that were being reviewed. I have nothing but praise for the difficult task they have maintaining equity throughout the state in operating procedures and valuation practices.

Since the time when the survey team was here, the state has stumbled into severe economic times. I would like to thank the Board of Supervisors in Merced for funding that allows the Assessor to maintain a manageable level of service to the citizens of Merced County.

Attached is my written response to the survey of the 2007-2008 assessment roll. As per Section 15645 of the government code we have included a written response.

Sincerely,

[Signature]

Kent B. Christensen  
Merced County Assessor-Recorder
RECOMMENDATION 1: Include the correct appeals filing period in the notice of proposed reassessment for property subject to disaster relief as required by section 170(c).

Response to recommendation 1:

We concur and made the change immediately.

RECOMMENDATION 2: Revise the California Land conservation Act assessment program by: (1) establishing a base year value for CLCA homesites at market value; (2) properly inputting compatible use income on CLCA property; and (3) using appropriate risk components for different types of agricultural properties.

Response to recommendation 2:

(1) We concur and will begin that transition of converting all restricted homesites to reflect market value as of the date of the base year.

(2) We concur and will work to incorporate that ability into the property tax system. Currently the system does not have the capability to handle short term income streams.

(3) We concur and will add additional risk rates to properties that are identified as having additional risk.

RECOMMENDATION 3: Exempt property used exclusively for public school purposes from taxable possessory interest assessments.

Response to recommendation 3:

We disagree as to the meaning of exclusively. The word by definition means that they shall only serve to students. The possessory interest in question is a food service company that has catering contracts with nonschool groups on campus. Therefore we believe that they do not exclusively serve the school and are subject to taxation.