

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 SUMMARY DECISION UNDER REVENUE AND TAXATION CODE SECTION 40

3 In the Matter of the Petition for)
4 Reassessment of the 2018 Unitary Value for:)

5)
6 FRONTIER CALIFORNIA, INC. (201))

7 Petitioner)

Appeal No.: SAU 18-011

Case ID No.: 1056696

Nonappearance Hearing Date:

December 12, 2018¹

10
11 Representing the Parties:

12 For the Petitioner:

Peter W. Michaels, Attorney at Law
Ryan Ivey, Duff & Phelps, LLC

14 For the Respondent:

Sonya Yim, Tax Counsel III
Attorney for the State-Assessed Properties Division

Samuel Wang, Principal Property Appraiser
State-Assessed Properties Division

18 Appeals Attorney:

Susan Galbraith, Tax Counsel

19 **VALUES AT ISSUE**

	Value	Penalty	Total
21 2018 Board-adopted Unitary Value	\$2,394,300,000	\$0	\$2,394,300,000
22 Petitioner's Requested Unitary Value	\$2,184,943,855	\$0	\$2,184,943,855
Respondent's Appeal Recommendation	\$2,394,300,000	\$0	\$2,394,300,000

24 **Factual Background**

25 Frontier California, Inc. (Petitioner), formerly Verizon California, Inc., is a wholly owned
26 subsidiary of Frontier Communications Corporation and the second largest incumbent local exchange
27

28 ¹ The Board voted unanimously to deny the petition for reassessment and affirm the 2018 Board-adopted unitary value of \$2,394,300,000.

1 carrier in the State of California. Petitioner is regulated by the California Public Utilities Commission
2 (CPUC), and like other state-assessed incumbent local telephone companies, is designated as a
3 telephone service provider of last resort (POLR).

4 After petitioner's purchase of Verizon wireline assets in California, Florida, and Texas in 2016, a
5 purchase price allocation (PPA) was performed for the property acquired in the transaction in
6 accordance with Financial Accounting Standards Board *Accounting Standards Codification 805 (ASC*
7 *805)*. A PPA is the process whereby a company, when purchasing another company, allocates the
8 purchase price to various assets and liabilities accounts. It is typically conducted for financial and tax
9 reporting requirements when mergers and acquisitions occur. A PPA for property plant and equipment
10 (PP&E) represents the assets' fair market value at the time of the transaction. In this case, the fair market
11 value pursuant to the PPA for petitioner's PP&E specific to California was \$3.4 billion as of April 1,
12 2016.

13 For the 2018 unitary valuation appraisal, petitioner provided respondent with a lien date 2018
14 Fair Market Value Appraisal prepared by Duff & Phelps (D&P study) on March 14, 2018. The study
15 develops the Replacement Cost New (RCN) for the taxable property, then subtracts depreciation and
16 extraordinary obsolescence, and adds the value of real property to determine the total value of
17 petitioner's unitary property.
18

19 Respondent utilized the same appraisal methodology for petitioner's 2018 unitary valuation as
20 was used for the 2017 unitary valuation. Respondent relied on the 2016 PPA as the starting point,
21 adjusted for purchases and asset retirements since the 2016 PPA date, applied appropriate trend and
22 percent good factors to all the taxable costs according to their acquisition years, estimated remaining
23 economic lives for various asset categories, and then adjusted for functional and economic obsolescence,
24 to arrive at the Replacement Cost New Less Depreciation (ReplCLD) value indicator. The 2018 Board-
25 adopted unitary value was based on 100 percent reliance on the ReplCLD value indicator.
26

27 **Legal Issue 1: Whether petitioner has shown that respondent's excess capital adjustment for the**
28 **rural footprint reflected in the 2018 unitary value was inappropriate.**

1 **Findings of Fact and Related Contentions**

2 Petitioner states that its network “serves many rural areas that are uneconomical [and] believes a
3 capital cost adjustment in these areas is appropriate. The requested adjustment is conservative in that it
4 applies to census blocks deemed rural which account for only 6 percent of overall network. A rural
5 footprint capital adjustment should be made, in the amount of \$117,840,851 [Attachment 1].” (Petition,
6 p. 1.)

7 Respondent states that petitioner provided the D&P study performed for lien date 2018, which
8 included a \$175 million value adjustment for excess capital to account for the difference in ReplCLD
9 value indicators between building an all fiber network rather than a fixed wireless network for a very
10 rural part of petitioner’s service area.

11 Respondent states that it agreed with petitioner that a value adjustment was warranted for excess
12 capital since petitioner was planning to push out fixed wireless services in the same rural area. However,
13 respondent further asserts that it found deficiencies in petitioner’s excess capital calculation and made
14 several modifications to address the deficiencies. After respondent’s modifications, the 2018 ReplCLD
15 value indicator reflects a \$57 million value adjustment for excess capital.

16 Respondent also contends that petitioner has not provided any information to show how
17 respondent’s value adjustment in the original appraisal was inappropriate or insufficient. Furthermore,
18 respondent argues that petitioner failed to provide documentation to support the \$118 million adjustment
19 petitioner made in excess of the adjustment made by respondent, thus failing to provide any support or
20 evidence showing how petitioner’s value adjustment for this issue was appropriate and the value
21 adjustment respondent had already allowed was inappropriate.

22 It is well settled that the burden of proof in contesting the validity of an assessment is on the
23 petitioner. (ITT World Communications, Inc. v. Santa Clara County (1980) 101 Cal.App.3d 246.)
24 Respondent states that petitioner has failed to provide any evidence to substantiate its claim for an
25 additional adjustment for excess capital and has not met its burden in contesting the validity of the
26 assessment. For these reasons, respondent recommends that no adjustment be made for this issue.
27
28

Applicable Law and Appraisal Principles

Burden of Proof

Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.) Therefore, Petitioner has the burden of showing that the assessment is incorrect or illegal. (*ITT World Communications v. Santa Clara* (1980) 101 Cal.App.3d 246; see also Cal. Code Regs., tit. 18, § 5541, subd. (a).)

ReplCLD Value Indicator

Property Tax Rule 6, subdivision (a), provides, in part: “The reproduction or replacement cost approach to value . . . is preferred when neither reliable sales data . . . nor reliable income data are available . . .” In general, the ReplCLD valuation methodology is estimated by applying trend factors—price level changes, including the application of “current prices to the labor and material components of a substitute property capable of yielding the same services and amenities, with appropriate additions as specified . . .” (Property Tax Rule 6, subd. (d).) Then, the resulting adjusted cost amount is “reduced by the amount that such cost is estimated to exceed the current value of the reproducible property by reason of physical deterioration, misplacement, over- or underimprovement, and other forms of depreciation or obsolescence. The percentage that the remainder represents of the reproduction or replacement cost is the property’s percent good.” (Property Tax Rule 6, subd. (e).)

Analysis and Disposition

Respondent is presumed to have correctly determined the value of the property at issue, and petitioner bears the burden of proving otherwise. Here, petitioner states that its network serves many rural areas that are uneconomical, believes a capital cost adjustment is appropriate, and that its requested adjustment is conservative. Respondent agreed with petitioner that an adjustment for excess capital was appropriate and made a \$57 million adjustment. However, petitioner has not provided additional documentation to support its claim for an additional adjustment of \$118 million for excess capital. Therefore, the Appeals Attorney finds that petitioner has not met its burden of proving that respondent’s excess capital adjustment for the rural footprint reflected in the 2018 unitary value was inappropriate and does not recommend any further adjustments for this issue.

1 **Legal Issue 2: Whether petitioner has shown that respondent’s appraised value for buildings in the**
2 **2018 unitary valuation was inappropriate.**

3 **Findings of Fact and Related Contentions**

4 Petitioner asserts that its replacement square footage is “significantly smaller than existing
5 square footage. Telephone central office buildings, which were generally constructed decades ago, are
6 larger than necessary for equipment current[ly] housed inside. The Board’s reliance on trended purchase
7 price allocation building costs prevents recognition of this super-adequacy. An inutility adjustment for
8 buildings should be made, in the amount of a \$61.3 million.” (Petition, p. 1.)

9 Respondent asserts that its valuation for petitioner’s buildings was based on the 2016 PPA. Since
10 the PPA represents the fair market value of the property at the time of the transaction, any obsolescence
11 for super-adequacy would be reflected in the PPA and is therefore already reflected in the unitary value.
12 Respondent further contends that petitioner has not provided any new information or documentation to
13 support a \$61 million reduction for buildings due to super adequacy, and has also failed to provide any
14 evidence or support to show that respondent’s appraised value for the buildings was inappropriate.
15 Respondent states that there is no basis for adjusting the Board-adopted value, and recommends that no
16 adjustment be made for this issue.

17 **Applicable Law and Appraisal Principles**

18 **Burden of Proof**

19 Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.)
20 Therefore, the petitioner has the burden of showing that the assessment is incorrect or illegal. (*ITT*
21 *World Communications v. Santa Clara* (1980) 101 Cal.App.3d 246; see also Cal. Code Regs., tit. 18, §
22 5080 subd. (a).)

23 **ReplCLD Value Indicator**

24 Property Tax Rule 6, subdivision (a) provides, in part: “The reproduction or replacement cost
25 approach to value . . . is preferred when neither reliable sales data . . . nor reliable income data are
26 available” In general, the ReplCLD valuation methodology is estimated by applying trend
27 factors—price level changes, including the application of “current prices to the labor and material
28 components of a substitute property capable of yielding the same services and amenities, with

1 appropriate additions as specified . . .” (Property Tax Rule 6, subd. (d).) Then, the resulting adjusted
2 cost amount is “reduced by the amount that such cost is estimated to exceed the current value of the
3 reproducible property by reason of physical deterioration, misplacement, over- or under-improvement,
4 and other forms of depreciation or obsolescence. The percentage that the remainder represents of the
5 reproduction or replacement cost is the property’s percent good.” (Property Tax Rule 6, subd. (e).)

6 **Analysis and Disposition**

7 Respondent is presumed to have correctly determined the value of the property at issue, and
8 petitioner bears the burden of proving otherwise. Here, petitioner asserts that the square footage it
9 would require to replace its buildings is significantly less than its existing square footage and that a
10 \$61.3 million inutility adjustment should be made. Respondent states that obsolescence for super
11 adequacy would be reflected in the PPA and in petitioner’s unitary value, and that petitioner has not
12 provided any evidence to support its claim that the requested adjustment of \$61.3 million for super
13 adequacy is justified. Therefore, the Appeals Attorney finds that petitioner has not met its burden of
14 proving that respondent’s appraised value for buildings in the 2018 unitary valuation was inappropriate
15 and recommends that no adjustment be made for this issue.

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17 **Legal Issue 3: Whether petitioner has shown that respondent’s economic obsolescence**
18 **adjustment reflected in the 2018 unitary valuation was inappropriate.**

19 **Findings of Fact and Related Contentions**

20 Petitioner asserts that “Historically, the Board has measured economic obsolescence by using
21 forward-looking calculations based on projected customer counts for the next three calendar years. The
22 Board’s 2018 calculation covers four years, with [the] first year reflecting actual customer counts, as of
23 lien date. Economic obsolescence should measure anticipated loss in value due to future customer
24 losses. Past customer losses should not have been included in [the] 2018 calculation of economic
25 obsolescence. An economic obsolescence should be made, consistent with past net present value
26 calculations by the Board, in the amount of \$30, 215, 294 [Attachment 2].” (Petition, p. 1.)

27 Petitioner claims that respondent’s economic obsolescence calculation was incorrect because
28 respondent included one year of an actual count of past customer losses in addition to anticipating

1 future losses, rather than relying only on an anticipated loss of customers in future calendar years.
2 Respondent asserts that it relied on the 2016 PPA as a starting point for the ReplCLD value indicator,
3 and that the PPA represents the fair market value of the property at the time of the transaction.
4 Respondent further asserts that including the actual number of customer losses since the PPA date in its
5 economic obsolescence calculation provides more accurate information as to petitioner’s actual
6 operations and value. Respondent states that its calculations resulted in a \$426 million adjustment for
7 economic obsolescence in petitioner’s 2018 ReplCLD value indicator. Finally, respondent asserts that
8 petitioner has not provided information to explain how respondent’s inclusion of actual customer losses
9 in the economic obsolescence calculation was inappropriate, nor has petitioner provided documentation
10 to support its claim for \$30 million in additional adjustments for economic obsolescence. For these
11 reasons, respondent recommends that no adjustment be made for this issue.

Applicable Law and Appraisal Principles

Burden of Proof

14 Assessing officers are presumed to have properly performed their duties. (Evid. Code, §
15 664.) Therefore, the petitioner has the burden of showing that the assessment is incorrect or illegal.
16 (*ITT World Communications v. Santa Clara* (1980) 101 Cal.App.3d 246; see also Cal. Code Regs., tit.
17 18, § 5080 subd. (a).)

ReplCLD Value Indicator

19 Property Tax Rule 6, subdivision (a), provides, in part: “The reproduction or replacement cost
20 approach to value . . . is preferred when neither reliable sales data . . . nor reliable income data are
21 available . . .” In general, the ReplCLD valuation methodology is estimated by applying trend
22 factors—price level changes, including the application of “current prices to the labor and material
23 components of a substitute property capable of yielding the same services and amenities, with
24 appropriate additions as specified . . .” (Property Tax Rule 6, subd. (d).) Then, the resulting adjusted
25 cost amount is “reduced by the amount that such cost is estimated to exceed the current value of the
26 reproducible property by reason of physical deterioration, misplacement, over- or underimprovement,
27 and other forms of depreciation or obsolescence. The percentage that the remainder represents of the
28 reproduction or replacement cost is the property’s percent good.” (Property Tax Rule 6, subd. (e).)

1 **Analysis and Disposition**

2 Respondent is presumed to have correctly determined the value of the property at issue, and
3 petitioner bears the burden of proving otherwise. Here, petitioner asserts that respondent should have
4 measured economic obsolescence using customer counts projected for the next three years and should
5 not have included actual customer counts in its calculations for economic obsolescence. Respondent
6 asserts that including the actual number of customer losses provides more accurate information. In
7 addition, respondent asserts that petitioner has not provided information to explain how respondent's
8 inclusion of actual customer losses in the economic obsolescence calculation was inappropriate, nor has
9 petitioner provided documentation to support its claim for \$30 million in additional adjustments for
10 economic obsolescence. Therefore, the Appeals Attorney finds that petitioner has not met its burden of
11 proving that respondent's economic obsolescence adjustment in the 2018 unitary valuation was
12 inappropriate and recommends that no adjustment be made for this issue.

13 **Decision**

14 Accordingly, the petition for reassessment is denied and the 2018 Board-adopted unitary value
15 of \$2,394,300,000 is affirmed.*

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17 George Runner _____, Chairman

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19 Diane L. Harkey _____, Member

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21 Jerome Horton _____, Member

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24 * The decision was rendered in Sacramento, California on December 12, 2018. This summary decision
25 document was approved on February 26, 2019, in Sacramento, California.

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