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STATE OF CALIFORNIA
BOARD OF EQUALIZATION

In the Matter of the Petition for
Reassessment of the 2024 Unitary Value for:

**SOUTHERN CALIFORNIA EDISON
COMPANY (0148)**

Petitioner

**APPEALS ATTORNEY'S
HEARING SUMMARY FOR
ORAL HEARING ON
PROPERTY TAX PETITION**

Appeal No.: SAU 24-003

Representing the Parties:

For the Petitioners:

Mardiros H. Dakessian, Attorney
Dakessian Law, LTD.

Charles Moll, Attorney
McDermott Will & Emery

For the Respondent:

Sonya Yim, Attorney V
Attorney for State-Assessed Properties Division

David Lujan, Attorney
Attorney for State-Assessed Properties Division

Jack McCool, Chief
State-Assessed Properties Division

Appeals Attorney:

Sarah J. Wilkman, Attorney III

PROPOSED VALUES

	Value	Penalty	Total
2024 Board-Adopted Unitary Value	\$38,986,400,000	\$0	\$38,986,400,000
Petitioner's Requested Unitary Value	\$32,915,600,000 ¹	\$0	\$32,915,600,000
Respondent's Appeal Recommendation	\$38,986,400,000	\$0	\$38,986,400,000

¹ As rounded, per Petitioner's 2024, Petition 529-A.

ISSUES

1. **Whether Petitioner Has Shown that the State-Assessed Properties Division (SAPD or Respondent) Has Failed to Reconcile the Historical Cost Less Depreciation (HCLD) Value Indicator and the Capitalized Earning Ability (CEA) Indicator of Value.**
2. **Whether Petitioner Has Shown that Respondent Erred in Placing 75 Percent Reliance on the HCLD Value Indicator and 25 Percent Reliance on the CEA Indicator of Value.**
3. **Whether Petitioner Has Shown that Respondent Must Adjust the Board-Adopted Value for SCE's Liabilities for the 2017/2018 Wildfires and Mudslides.**
4. **Whether Petitioner Has Shown that Respondent Improperly Assessed the Wildfire Mitigation Capital Expenditures.**
5. **Whether Petitioner Has Shown that Respondent Erred in its Treatment of Wildfire Insurance Fund-Related Contributions.**

Appeals Attorney's Recommendation and Note²

The Appeals Attorney recommends that the Board deny the petition for reassessment, based on the evidence and argument submitted to the record to date.

This appeal involves an amount in controversy that is \$500,000, or more, in tax and thus is governed by Rev. and Tax. Code (R&TC) section 40. Please see Staff Comment on page 38 for additional detail.

Background Information

Southern California Edison Company (SCE or Petitioner), a wholly-owned subsidiary of Edison International, is a public utility subject to rate regulation by the California Public Utilities Commission (Commission or CPUC). SCE is primarily engaged in the business of supplying electric energy in central, coastal, and southern California, excluding the City of Los Angeles and certain other cities. Petitioner's service area encompasses 50,000 square miles, which includes 103,000 miles of distribution and transmission lines, serving a population of approximately 15 million people.

The CPUC establishes rates for utilities under its jurisdiction in a rate-setting procedure called

² Unless the Board holds otherwise, the Board shall take official notice of: Petitioner's property statement filed with the Board and any attachments thereto; any reports to regulatory agencies such as the U.S. Securities and Exchange Commission and the California Public Utilities Commission (CPUC), and any annual reports to shareholders; the Appraisal Data Report (ADR) prepared by the State-Assessed Properties Division (SAPD) together with any workpapers; the Notice of Unitary Value; any correspondence between SAPD and Petitioner, and the existence of any lawsuits between the Board and Petitioner.

1 the General Rate Case (GRC).³ In establishing rates for utilities, the CPUC considers the utilities' rate
2 base. Rate base is the value of property on which a public utility is permitted by the Commission to
3 earn a specified rate of return. In general, the rate base consists of the cost of property as used by the
4 utility in providing service.

5 Petitioner's 2024 Board-adopted value of \$38,986,400,000 is based on 75 percent reliance on
6 the Historical Cost Less Book Depreciation (HCLD)⁴ value indicator (\$41,046,987,454) and 25
7 percent reliance on the Capitalized Earning Ability⁵ (CEA) value indicator (\$32,804,550,405).

8 On appeal, Petitioner contends that their 2024 Board-adopted unitary value is overstated and is
9 instead requesting a unitary value of \$32,915,600,000.

10 In the briefing and evidence submitted, Petitioner and the State-Assessed Properties Division
11 (SAPD or Respondent) each discussed general information relevant to the context of the five specific
12 issues raised within the briefings, including information related to SCE's past, current, and future
13 financial and economic situation, along with the risks associated with wildfires, the context of the
14 Board's valuation, and the state of the regulated electric generation industry as a whole. The Appeals
15 Attorney will first provide a summary of these general concerns to provide context to the consideration
16 of the specific issues raised within this Petition. Then, the five specific issues will be addressed under
17 headings: Issue 1 through Issue 5.⁶

18 At the Appeals Conference, the parties did not reach agreement on any of the issues raised and
19 affirmed they were pursuing a full hearing before the Board.

22 ³ The Commission's Rules of Practice and Procedure Article 2 and Appendix A of the Commission decision (D07-07-004)
set the rules and procedures for GRC review process.

23 ⁴ The HCLD value indicator is a form of the cost approach to value. The Historical Cost Less Depreciation (HCLD) value
24 indicator derivation includes the historical or original acquisition cost of all property less nontaxable items and property
25 assessed elsewhere. This results in the taxable historical cost. The taxable historical cost is then reduced for the assessee's
26 regulatory accounting depreciation of the taxable property. This results in the assessable HCLD. The value of any
possessory interest and/or noncapitalized leased properties are added to arrive at the final HCLD value indicator. HCLD is
one of the more important indicators of value for closely regulated public utilities. See Cal. Bd. Of Equaliz. *Unitary*
Valuation Methods (UVM) (2003), pp. 1-4.

27 ⁵ The CEA value indicator is a form of the income approach to value. The income approach to value may be generally
described as any method that converts future anticipated income into present value. The conversion process is commonly
known as income capitalization. See Cal. Bd. Of Equaliz. *UVM*, (2003), pp. 35-37.

28 ⁶ The Appeals Attorney notes that Petitioner's 2024 Reply brief lists seven specific issues. (Reply, p. 2.) However, due to
the nature of these issues, they are organized differently for purposes of this Hearing Summary: Petitioner's listed issue 1 is
addressed in this Hearing Summary's general concerns; Petitioner's issues 6 and 7 are covered in this Hearing Summary's
combined Issues 1 & 2; Petitioner's issue 5 corresponds to this Hearing Summary's issue 3, Petitioner's issues 2 and 4 are
covered in this Hearing Summary's issue 4; and Petitioner's issue 3 is addressed in this Hearing Summary's Issue 5.

General Concerns Raised by the Parties

As a prefatory matter, each party provided remarks on the overall reasonableness of SCE's 2024 Board-adopted unitary value. Petitioner contends that the mere magnitude of the \$8 billion discrepancy between the HCLD and CEA value indicators is unacceptable from an appraisal standpoint, which in short, allegedly supports their general claim that SAPD's appraisal is unlawful and improper. (Petition for Reassessment and Claim for Refund ("Petition"), pp. 2-3 and p. 10.) Respondent notes that Petitioner had \$2.7 billion of asset additions this year.⁷ (SAPD Analysis, p. 4) The Appeals Attorney notes the Appraisal Data Report (ADR) is included as Exhibit 2 of the SAPD Analysis; the ADR summarizes Petitioner's 2024 calendar year asset additions and retirements and provides a high-level comparison of the 2024 assessment with Petitioner's 2023 assessment.

Petitioner raises four general concerns⁸, asserting these are the various business risks and other factors affecting SCE's 2024 unitary value: 1) the context of increasing catastrophic wildfires in California; 2) California's use of "inverse condemnation"⁹, its impact on Investor-Owned utilities and uncertainty as to whether the CPUC will allow liability to be recovered in the rate base even if the utility acts prudently¹⁰; 3) the challenges and cost prohibitive nature of obtaining insurance coverage due to wildfire risk arising from its ordinary operations, as well as recent impacts to the California homeowner insurance market; 4) Wildfire Mitigation Plans and the Wildfire Insurance Fund, including specifically California's Senate Bill (SB) 901¹¹ (Ch. 626, Stats. 2018) and the Wildfire Insurance Fund

⁷ Respondent notes the approximately \$2.7 billion in additions is exclusive of both retirements and approximately \$2.8 billion in construction work in progress (CWIP). (SAPD Analysis, p. 5, fn. 10.)

⁸ See Petition, pp. 3-8.

⁹ Inverse condemnation is a legal concept that entitles property owners to just compensation if their property is damaged by a public use. This liability rule applies to all government agencies, as well as utilities. After a wildfire, inverse condemnation is the way that victims of fires (residents, businesses, and local agencies) recover their costs. See League of California Cities "Inverse Condemnation Fact Sheet" <https://www.counties.org/post/inverse-condemnation-fact-sheet>.

¹⁰ Petitioner cites 2017 CPUC ruling for San Diego Gas & Electric company (SDG&E), which held SDG&E liable for damages due to finding SDG&E had not taken reasonable actions prior to 2007 and thus not properly invoked inverse condemnation to allow cost sharing through utility rates. (CPUC, App. No. 15-09-010 and Decision 17-11-033.)

However, the courts have expressed skepticism regarding the uncertainty of recoverability that Petitioner cites; in *Pac. Bell v. So. Cal. Edison Co.* (2012) 208 Cal.App.4th 1400, the Court noted in response to Edison's argument that the loss-spreading rationale should not apply to an investor-owned public utility due to lacking the taxing authority to raise rates without the approval of the CPUC, "Edison has not pointed to any evidence to support its implication that the Commission [CPUC] would not allow Edison adjustments to pass on damages liability during its periodic reviews." (*Id.* at 1407.) However, it should be noted the legal standards applicable to CPUC's consideration of rate base recoverability in this case have since changed.

¹¹ SB 901 established, among other provisions, CPUC's reasonableness review of utility activities to determine whether, or not, cost recovery through the rate base is allowable when the wildfire is caused by the utility's equipment, without altering California's application of inverse condemnation.

1 created by Assembly Bill (AB) 1054¹² (Ch. 79, Stats 2019), which statutorily required Petitioner to
2 make an initial contribution of \$2.4 billion, and 10 annual contributions of \$95 million each, and
3 Petitioner's statutory requirement to maintain reasonable insurance coverage, which must be exhausted
4 prior to Wildfire Insurance Fund reimbursement becoming available to Petitioner.¹³ (Petition, pp. 3-8.)

5 However, Respondent notes that the broad risks Petitioner cited do not acknowledge the
6 adjustments already within Petitioner's 2024 Board-adopted unitary value, which total approximately
7 \$2.7 billion. (SAPD Analysis, p. 2.) Respondent highlights four specific adjustments which have
8 already been included in SCE's 2024 Board-adopted value:

- 9 • AB 1054 requires SCE to pay an additional \$95 million per year for 5 additional
10 years into the wildfire fund. Staff has made an adjustment to account for this
11 requirement which resulted in an approximately \$112 million value reduction.
- 12 • SCE has requested a .85% wildfire risk premium be added to its capitalization
13 rate. Staff has made an adjustment to account for this request, which resulted in an
14 approximately \$465 million value reduction.
- 15 • AB 1054 requires SCE to make \$1.6 billion in capital expenditures over a three
16 year period for fire risk mitigation purposes. The assembly bill precludes SCE from
17 earning an equity return on these capital expenditures. As of the 2024 lien date, SCE
18 has made all \$1.6 billion in capital expenditures for this purpose. Staff has made an
19 adjustment to account for SCE's inability to earn an equity return on these
20 expenditures, which resulted in an approximately \$524 million value reduction.
- 21 • Staff made an obsolescence adjustment to the HCLD indicator to acknowledge
22 additional obsolescence resulting from the .85% equity risk premium addition to the
23 capitalization rate. This adjustment resulted in an approximately \$1.6 billion value
24 reduction.

25 (SAPD Analysis, pp. 2-3; see also SAPD Analysis, Exhibit 2, Appraisal Data Report. See also
26 Appraisal Narrative, 2024 Lien Date, for Southern California Edison Company.)

27 Then, Respondent contends, these, among other arguments regarding a general increase in
28 business risk due to wildfires, are the same arguments Petitioner made—and the Board rejected—for

¹² Assembly Bill 1054 (Ch. 79, Stats. 2019) (AB 1054) created a \$21 billion fund funded by contributions from investor-owned utilities, including Petitioner, and from ratepayers. This fund is available to pay certain wildfire claims made against Petitioner and other fund participants.

¹³ Petitioner also notes that maintaining \$1 billion of insurance coverage has become increasingly expensive, citing \$450 million in costs for FY 2022-2023, and estimates that cost increasing, which questions their ability to obtain a reasonable amount of wildfire insurance at a reasonable cost. (Petition, p. 7-8.)

1 the last four years.¹⁴ Further, Respondent notes these are also the same arguments the CPUC rejected
2 in SCE's request for a wildfire risk premium adjustment to increase the return on equity¹⁵ (ROE)
3 allowed in 2019. (SAPD Analysis, p. 3; citing CPUC Decision 19-12-056 (Dec. 19, 2019), pp. 40-41.)
4 In the CPUC case,¹⁶ the CPUC stated:

5 After considering the evidence on market conditions, trends, creditworthiness, interest rate
6 forecasts, quantitative financial models, additional risk factors including business risk [which
7 includes wildfire risk], and interest coverage presented by the parties and applying our
8 informed judgment ... We find that SCE's authorized test year 2020 ROE should be 10.30%.
9 *This ROE is reasonably sufficient to assure confidence in the financial soundness of the utility
and to maintain investment grade credit ratings while balancing the interests between
shareholders and ratepayers.*¹⁷

10 Further, Respondent notes that CPUC's final conclusion was that "*We find that the passage of AB 1054
11 and other investor supportive policies in California have mitigated wildfire exposure faced by
12 California's utilities.*" (SAPD Analysis, p. 3 citing CPUC Decision 19-12-056, at p. 37; emphasis
13 added by Respondent.) The CPUC also stated, "[b]ased on the above financial, business, and
14 regulatory risks discussion, we conclude the ROE ranges adopted in the proceedings...adequately
15 compensate the utilities for these risks." (*Id.*, at p. 40.) Respondent notes that Petitioner also
16 recognized its significant reduction of risk of liability, as Petitioner voluntarily significantly reduced its
17 ROE increase request in the CPUC case following the passage of AB 1054 from 6 percent to .85
18 percent, which was also ultimately rejected by the CPUC. (SAPD Analysis, p. 3 citing CPUC Decision
19 19-12-056, at p. 28.)

22 ¹⁴ California State Board of Equalization, Appeal SAU 20-015, decided December 16, 2020, Appeal SAU 21-007, decided
23 December 14, 2021, SAU 22-006, decided December 13, 2022, and SAU 23-010, decided December 12, 2023. The Appeals
24 Attorney notes each of these four prior petition years is being contested by Petitioner in superior court. However, the instant
petition is to be decided de novo by the Board.

25 ¹⁵ A utility's Rate of Return, or Cost of Capital, is the weighted average cost of debt, preferred equity, and common stock, a
26 utility has issued to finance its investments. Return on Equity (ROE) is the return to common equity. The CPUC attempts
27 to set the authorized ROE at a level that is adequate to enable the utility to attract investors to finance the replacement and
expansion of its facilities so it can fulfill its public utility service obligation. In practice, this level is determined by
estimating market returns on investments for other companies with similar levels of risk. In general, a higher ROE allows
greater earnings and would be appropriate to reflect increased risks and uncertainties. See generally:

28 <<https://www.cpuc.ca.gov/industries-and-topics/electrical-energy/electric-costs/cost-of-capital>> and
<<https://www.cpuc.ca.gov/industries-and-topics/electrical-energy/electric-costs/historical-electric-cost-data/rate-of-return>>
[As of Dec. 2, 2024.]

¹⁶ California Public Utilities Commission Decision 19-12-056 (D1912056) (Dec. 19, 2019), p. 28 available at
<<https://docs.cpuc.ca.gov/DecisionsSearchForm.aspx>> [as of Nov. 28, 2024].

¹⁷ *Id.* at pp. 40-41, emphasis added by Respondent.

Respondent also notes that while the risk of catastrophic wildfires by Petitioner's business remains, the CPUC and the credit markets all recognize that risk has been significantly reduced. Respondent points to Petitioner's press release recognizing a significant reduction to its risks, stating, **"[it] has reduced the probability of catastrophic wildfires associated with its equipment by about 75%-80% since 2018"**.¹⁸ Further, Respondent notes that Fitch Ratings, one of the three major credit rating agencies, upgraded Petitioner's long-term issuer credit ratings from 'BBB-/Outlook Positive' to 'BBB-/Outlook Stable'.¹⁹ (SAPD Analysis, p. 4.) Respondent notes this opinion was reviewed and reconfirmed by Fitch on December 18, 2023.²⁰ (SAPD Analysis, p. 4, fn 8.)

In addition, Respondent notes that similar to SCE's 2023 unitary value, SAPD has again allowed an increased equity risk premium of .85 percent to Petitioner's 2024 overall capitalization rate. (SAPD Analysis, p. 5.) This equity risk premium resulted in an approximately \$2 billion value reduction, which was allowed to acknowledge risk that might not be captured in the other adjustments allowed for the Petitioner. (*Ibid.*)

Respondent also maintains that any increase to ordinary insurance cost is already accounted for in its appraisal. (SAPD Analysis, p. 4.)

In the Reply to SAPD's Analysis, Petitioner contends that SAPD's claims of multiple and generous adjustments misrepresent the adjustments to date and that the Board should not conflate the wildfire risk premium adjustment discussion with the specific issues raised in SCE's petition (discussed *infra*). (Petitioner's Reply to SAPD Analysis ("Reply"), pp. 2-4.) Petitioner further argues that Respondent incorrectly negated the mentioned adjustment to account for SCE's inability to earn an equity return on the wildfire mitigation capital expenditures, by erroneously increasing the cost indicator through an AB 1054 securitization cost addback, which resulted in a net increase of \$524 million in assessed value. (Reply, p. 4) Additionally, they note that while Petitioner's credit rating has

¹⁸ Edison International, Southern California Edison Improves Grid Safety, Significantly Reduces Wildfire Threat (March 27, 2023) <[Southern California Edison Improves Grid Safety, Significantly Reduces Wildfire Threat | Edison International Newsroom](https://www.sce.com/sites/default/files/AEM/Wildfire%20Mitigation%20Plan/2023-2025/2023-03-27_SCE_2023_WMP_R0.pdf)> (as of October 2, 2024.) Further details are set forth in Petitioner's 2023-2025 Wildfire Mitigation Plan available at <https://www.sce.com/sites/default/files/AEM/Wildfire%20Mitigation%20Plan/2023-2025/2023-03-27_SCE_2023_WMP_R0.pdf> (as of Dec. 2, 2024.)

¹⁹ Fitch Ratings, Fitch Upgrades Edison International's & So. Cal. Ed's IDRs to 'BBB'; Outlook Stable (April 28, 2023) <[Fitch Upgrades Edison International's & So. Cal. Ed's IDRs to 'BBB'; Outlook Stable \(fitchratings.com\)](https://www.fitchratings.com/entity/southern-california-edison-company-80088928)> (as of December 2, 2024.)

²⁰ <https://www.fitchratings.com/entity/southern-california-edison-company-80088928> (As of December 2, 2024.)

1 increased, the significance of the increase is misleading as BBB is still within the lowest tier of
2 investment grade. (*Ibid.*)

3 **Appeals Conference**

4 Parties met at the Appeals Conference on November 15, 2024. At the conference, Petitioner and
5 Respondent discussed and renewed their positions as captured in the briefings.

7 **Appeals Attorney's Analysis and Comments**

8 While these general risks and factors are relevant to the context of this appeal, the Appeals
9 Attorney notes no general concern raised proves *ipso facto* that Respondent erred in the calculation of
10 SCE's 2024 Board-adopted unitary value. Petitioner is merely providing a general assertion that
11 Respondent did not consider, or fully consider, the risk Petitioner faces as a part of its 2024
12 assessment, which it contends is visible due to the value differential between the HCLD and CEA
13 approaches. However, Respondent confirms it has considered many factors in its assessment,²¹ and
14 also highlights certain adjustments²² within SCE's 2024 valuation that reflect increased wildfire risk,
15 including the allowance of a 0.85 percent wildfire risk premium added to the capitalization rate.²³
16 Further, the Appeals Attorney notes that Petitioner maintains the burden of showing that Respondent's
17 underlying assessment is incorrect or illegal. (*ITT World Communications v. Santa Clara* (1980) 101
18 Cal.App.3d 246; see also Cal. Code Regs., tit. 18, § 5541, subd. (a).) This requires specificity and
19 verifiable evidence or error. Accordingly, to the extent that Petitioner is using these general risks and
20 factors to assert specific errors exist within Respondent's calculations supporting the assessment at
21 issue, Petitioner maintains the burden of providing evidence and proving the existence of such alleged
22 specific errors within Respondent's calculation of the 2024 Board-adopted unitary value in the
23 following five specific issues raised.

24 At the hearing, the parties should be prepared to discuss these general contentions as they relate
25 and provide context to the specific issues raised in this petition.

26 /

28 ²¹ Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.)

²² Detailed in SCE's 2024 Appraisal Data Report Narrative.

²³ Note, this risk premium is above what the CPUC was willing to entertain for Petitioner; discussed *supra* at p. 6. See also California Public Utilities Commission Decision D1912056 referenced in ftn. 16.

ISSUES 1 AND 2

Whether Petitioner Has Shown that Respondent Has Failed to Reconcile the Historical Cost Less Depreciation (HCLD) Value Indicator and the Capitalized Earning Ability (CEA) Indicator of Value and/or Otherwise Erred in Placing 75 Percent Reliance on the HCLD Value Indicator and 25 Percent Reliance on the CEA Indicator of Value.

Petitioner's Contentions

Based on the two contentions described below, Petitioner requests that the Board revise its 2024 unitary value by instead placing 25 percent reliance on the HCLD value indicator and 75 percent reliance on the CEA value indicator.²⁴ (Petition, pp. 11-12.)

Petitioner asserts Respondent has not reconciled the value difference between the HCLD and CEA value indicators, rendering the value conclusion invalid.

Petitioner asserts Respondent's appraisal is flawed as the two value approaches utilized produced widely varying results. (Petition, p. 10.) Petitioner alleges that due to this disparity, and as Respondent's analysis does not explicitly state the value approaches were reconciled, Respondent must have decided to simply weigh the HCLD value indicator as 75 percent and the CEA value indicator 25 percent, without any reconciliation or reason for doing so in an analytical manner based on verified market data, which, in Petitioner's opinion, is contrary to the guidance within Assessors' Handbook (AH), section 501, *Basic Appraisal* (AH 501). (*Id.* pp. 10-11.) Petitioner also asserts that the disparity in value indicators signals the existence of substantial obsolescence or impairment, as AH 502, *Advanced Appraisal*, warns is possible. (*Id.* p. 9-11.)

Petitioner asserts Respondent has improperly weighted the HCLD value indicator as 75 percent and the CEA approach at 25 percent.

Petitioner asserts that Respondent has arbitrarily and improperly weighted the value indicators, which is underscored by the admission that it is the same reliance used to value Petitioner's property in each of the past 10 years, despite recent changes in circumstances and increasing risks and costs related to the ownership of Petitioner's property. (*Id.* at pp. 11-12.) Petitioner instead requests that the

²⁴ Petitioner asserts this adjustment would result in a reduction to its unitary value of \$4,121,218,524. (Petition, p. 9.) However, the Appeals Attorney notes that this estimation is dependent upon success of Petitioner's other requested issues and is currently indeterminable as to what value is attributable to this issue solely.

1 Board instead weigh the two value indicators as 75 percent income approach and 25 percent cost
2 approach. (*Ibid.*)

3 Petitioner further asserts that Property Tax Rule²⁵ 8 indicates the income approach must be
4 granted additional weight. (*Id.* at p. 12.) Petitioner asserts that the rate base determined by the CPUC is
5 intended to achieve a fair balance between what ratepayers bear and what utility shareholders earn, and
6 not to establish the fair market value of the utility's property. (*Id.* at p. 12.) Petitioner further argues
7 that the HCLD indicator calculated by SAPD is unreliable when Respondent includes assets not
8 included in the rate base and does not recognize impairments due to regulatory restrictions placed on
9 certain assets (i.e., the inability to earn a return), and as such, additional reliance placed on the income
10 indicator would capture the economic impairment due to wildfire risks and increased regulatory
11 restrictions. (*Id.* at p. 12-13.) Petitioner cites that the Ernst & Young, LLP (EY) report²⁶ it
12 commissioned in the SAU 20-015 appeal for lien date 2020, supports this view and reconciles the two
13 approaches appropriately, in its opinion, and considers Petitioner's perceived flaws with Respondent's
14 approach.²⁷ (*Id.* at p. 13.)

15 Petitioner further contends that Respondent acknowledges a limited understanding of
16 "regulatory lag"²⁸ but continues to argue that the CEA indicator should be given less reliance in
17 Petitioner's overall value, contrary to Rule 8. (*Id.* at p. 13.)

18 Petitioner asserts the changes that have taken place during the last 10 years in terms of wildfires
19 and shifts in the business environment and regulatory restrictions, coupled with Respondent's failure to
20 reconcile the \$8 billion difference in the HCLD and CEA approaches have rendered Respondent's
21 appraisal completely disconnected from what a willing buyer would pay. (*Id.* at p. 14.)

22 In its reply, Petitioner asserts that its argument that the difference between the two value
23

24 ²⁵ All references to "Property Tax Rule" or "Rule(s)" are to sections of title 18 of the California Code of Regulations.

25 ²⁶ Petitioner has included a draft copy of the Ernst & Young, LLP (EY) Valuation Analysis, November 9, 2020 (EY Report)
26 as Petition, Appendix B). However, it should be noted this report was prepared for lien date 2020, **not lien date 2024**, i.e.
27 the subject of this appeal; thus, while referenced, the EY report is not an appraisal for the lien date at issue. Further, the EY
28 report does not publish any conclusion as to what it believed to be the proper weighting, nor is this attached report the
finalized copy.

²⁷ Petitioner does not, however, acknowledge that the draft 2020 EY Report does not provide its conclusion as to the
relative weight placed on each of the two approaches to value, and merely states more relative weight was placed on the
income approach. (Petition, Appendix B, p. 59 of 2024 Petition pdf.)

²⁸ Regulatory lag is the time delay between a utility's costs and any adjustment CPUC may make to the rate base to account
for these costs. This process creates a lag between the time the assets are placed in service and the time the company begins
to get a recover of and recovery on the assets.

1 indicators is attributable to obsolescence is supported by AH 502, *Advanced Appraisal*, which states a
2 “CEA indicator which is much lower than HCLD may indicate that obsolescence exists in the
3 property.” (Reply, pp. 13-14.) Additionally, Petitioner reasserts that Respondent has not reconciled the
4 indicators in an analytical manner and is distracting from that failure by requesting Petitioner “provide
5 a reconciliation of value indicators in an analytical manner” based on “reasoned and defensible opinion
6 of verified market data” (Reply, p. 15-16.) Petitioner concludes by reasserting SAPD’s duty is to
7 reconcile the indicators, and the difference between the two approaches suggests Respondent has not
8 addressed all economic and functional obsolescence. (Reply, p. 16.)

9 Based on the foregoing rationales, Petitioner requests that the Board adopt Petitioner’s
10 requested weighting of the value indicators.

11 **Respondent’s Contentions**

12 Respondent has conducted its appraisal by calculating and reconciling the HCLD and CEA
13 value indicators, consistent with relevant law and appraisal guidance.²⁹ Respondent notes significant
14 differences in the two value approaches can and may occur, as stated in Assessors’ Handbook, section
15 501 (AH 501) *Basic Appraisal*, without compromising the validity of the underlying value approach,
16 quoting:

17 The reconciliation of value indicators from the separate approaches to value and the
18 resulting final value estimate is the next step in the appraisal process. *Theoretically*, the
19 approaches to value should produce identical value indicators. *In practice, however,*
20 *this is rarely the case, and significant differences may occur.* To produce a final value
21 estimate, the appraiser reconciles the indicators from each approach utilized. Value
22 indicators should be reconciled considering: (1) the appropriateness of the approach
given the purpose of the appraisal; and (2) the adequacy and reliability of the data
available to perform the appraisal. The appraiser should examine and reconcile all
value indicators.

23 (SAPD Analysis, p. 6; citing AH 501, p. 62, emphases added.) Specifically, Respondent notes that
24 when analyzing and reconciling value indicators to arrive at a final value estimate, the criteria
25 described in AH 502 should be considered:

26 The final value estimate is an appraiser’s *opinion of value*. There is no mathematical formula or
27 statistical technique to which the appraiser can ultimately refer in order to reach the final value
28 estimate. It is an opinion that should be based on the appraiser’s application of generally
accepted appraisal methods and procedures. It is generally inappropriate to use the arithmetic
mean of the value indicators as the final value estimate. Simply calculating an average implies

²⁹ Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.)

1 that all the value indicators have equal validity. While this may occur in certain instances, it is
2 usually not the case. Appraisers must follow Rule 3, noted above, and consider the
3 appropriateness of the value approaches, the relative accuracy of the value indicators, and the
quantity and quality of the data available when reconciling value indicators to reach the final
value estimate.

4 (SAPD Analysis, p. 6; citing AH 502, p. 111; Emphasis added by Respondent.)

5 Respondent notes the HCLD approach is a reliable indicator of market value for closely
6 regulated public utilities like Petitioner, as HCLD, with some modification, approximates the rate base
7 that regulators use in establishing revenue requirements. (SAPD Analysis, pp. 6-7; citing *Unitary*
8 *Valuation Methods (UVM)* (2003), p. 1.) HCLD reflects the market value contribution of all taxable
9 property including the depreciated historical cost of plant in service, possessory interests, construction
10 work in progress, and materials and supplies, and is:

11 A generally accepted method for valuing property interests of rate base regulated utilities,
12 whether centrally or locally assessed, is by use of the historical cost approach. Certain
13 industries have been and continue to be subject to rate base regulation, as a result of which
14 authorized earnings, or rates of return, are set by regulators and measured by rate base. Under
15 Rule 3(d), the assessing agency shall consider as relevant to value the amount actually invested
16 in the property or the amount invested less depreciation, if the income from the property is
17 regulated by law and the regulatory agency uses historical cost, historical cost less depreciation
(HCLD), or trended original cost as a rate base. Thus, the historical cost approach is considered
relevant for estimating the market value of public utility properties depending upon regulatory
influences.

18 (AH 502, p. 146.) Further, HCLD is,

19 **one of the more important indicators of value for closely regulated public utilities.** The
20 general practice of the California Public Utilities Commission (CPUC) and most other
21 regulatory agencies is to use historical or original cost less depreciation (with various
22 adjustments) as the rate base. The regulatory agencies establish a rate base and a rate of
return; utilities are permitted to earn at this established rate on the rate base.

23 (SAPD Analysis, p. 7; citing *UVM*, p. 1. Emphasis added.)

24 Respondent also notes that Property Tax Rule 8, subdivision (a), indicates the CEA value
25 indicator is appropriate to use when the property has “an established income stream...,” and here,
26 Petitioner has an established income stream. (SAPD Analysis, p. 7.)

27 Respondent states that consistent with the relevant HCLD and CEA value indicator authorities
28 and considerations, and Petitioner being a utility, rate regulated by the CPUC, Respondent considered

1 HCLD to be the most reliable indicator of value, placing 75 percent reliance on the indicator. (SAPD
2 Analysis, p. 7.) Respondent notes that due to Petitioner's significant growth in actual and planned
3 capital expenditures to replace and expand distribution and transmission infrastructure, and to
4 construct and replace generation assets, Petitioner is experiencing "regulatory lag." (*Ibid.*)
5 Accordingly, in Respondent's opinion, it is appropriate to weight the CEA value indicator 25 percent
6 to account for regulatory lag in rate adjustment for items on which Petitioner is not currently earning a
7 return. (*Ibid.*)

8 Respondent also notes the 75/25 percent reliance on HCLD and CEA respectively is the same
9 reliance used by SAPD to value Petitioner's property in each of the past 13 years, as well as the same
10 reliance Respondent places on the value indicators of other investor-owned, rate-regulated utilities.
11 (*Ibid.*) Respondent contends, while Petitioner sees this consistency as a flaw or indication that changes
12 have not been reflected related to the climate, utility industry, and to Petitioner specifically,
13 Respondent asserts Petitioner ignores the fact that a change in weighting is not the sole method by
14 which significant value adjustments can be made to reflect such factors, such as the approximately
15 \$2.7 billion downward adjustment Respondent has already made to account for wildfire risk. (*Id.* at p.
16 8.)

17 Respondent also notes that Petitioner's assertion that the difference between the HCLD and
18 CEA methods is entirely attributable to economic obsolescence is wholly unsubstantiated. (*Id.* at 8.)
19 Further, Respondent notes it is unclear how Petitioner arrived at its requested weighting of the CEA
20 and HCLD indicators. (*Ibid.*) Respondent points out that in 2020, Petitioner requested 50 percent
21 weighting of the CEA value indicator in its original petition. (*Ibid.*) Then in 2021, Petitioner requested
22 a 35 percent weighting of the CEA value indicator based on the same arguments, with no explanation
23 for the change. (*Id.* at p. 8.) Now, in 2024, Petitioner requests a 75 percent weighting of the CEA value
24 indicator based on the same arguments and presumptive risk analysis developed in 2020, without
25 explanation for the change. (*Ibid.*) Respondent concludes while Petitioner criticizes SAPD's reasoning,
26 Petitioner has not provided a basis for the reconciliation of the value indicators it requests in this
27 petition in an "analytical manner" that is based on a "reasoned and defensible opinion of verified
28 market data". (*Ibid.*, quoting Petition, p. 11, citing AH 502, p. 62.)

1 For these reasons, Respondent maintains no adjustment can be recommended as to this issue.

2 **Appeals Conference**

3 Parties met at the Appeals Conference on November 15, 2024. At the conference, Petitioner and
4 Respondent discussed and renewed their positions as captured in the briefings.

6 **Applicable Law and Appraisal Principles**

7 **Burden of Proof**

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

12 **Value Standard**

13 Property Tax Rule 2, subdivision (a) states that “in addition to the meaning ascribed to them in
14 the Revenue and Taxation Code, the words “full value,” “full cash value,” “cash value,” “actual
15 value,” and “fair market value” mean the price at which a property, if exposed for sale in the open
16 market with a reasonable time for the seller to find a purchaser, would transfer for cash or its
17 equivalent under prevailing market conditions between parties who have knowledge of the uses to
18 which the property may be put, both seeking to maximize their gains and neither being in a position to
19 take advantage of the exigencies of the other.”

20 **HCLD Approach to Value**

21 Property Tax Rule 3, subdivision (d) provides the HCLD approach to value shall be
22 considered “[i]f the income from the property is regulated by law and the regulatory agency uses
23 historical cost or historical cost less depreciation as the rate base, the amount invested in the property
24 or the amount invested less depreciation computed by the method employed by the regulatory
25 agency.” HCLD, with some modification, approximates the rate base that regulators use in
26 establishing revenue requirements. (See *UVM*, p. 1.) HCLD reflects the market value contribution of
27 all taxable property including the depreciated historical cost of plant in service, possessory interests,
28 construction work in progress, and materials and supplies. (AH 502, p. 146.) HCLD is,

one of the more important indicators of value for closely regulated public utilities. The general practice of the California Public Utilities Commission (CPUC) and most other regulatory agencies is to use historical or original cost less depreciation (with various adjustments) as the rate base. The regulatory agencies establish a rate base and a rate of return; utilities are permitted to earn at this established rate on the rate base.

(UVM (2003), p. 1.) Further, Board guidance states,

Appraisal depreciation in the form of obsolescence may be present in utility property and deducted from HCLD. Such deductions may be proper when the utility's economic income has been impaired and the rate or tariff-setting regulators have recognized such impairment.

(UVM, p. 1.)

Depreciation and the Cost Approach

In general, the cost approach recognizes three types of depreciation: physical deterioration, functional obsolescence, and external, or economic, obsolescence, through the application of the Board's replacement cost new trend factors and "percent" good factors. Obsolescence may occur when property is outmoded (functional obsolescence) or when some event has substantially diminished the future earning power of the property (economic obsolescence). (See Assessors' Handbook section 501, *Basic Appraisal* (January 2002), pp. 80-83.) Functional obsolescence is the loss of value in a property caused by the property's loss of capacity to perform the function for which it was intended. (*Id.* at p. 81.) Economic obsolescence is the diminished utility of a property due to adverse factors external to the property being appraised and is incurable by the property owner. (*Id.* at p. 82.) The existence of any additional or extraordinary obsolescence must be supported with verifiable documentation and evidence, consistent with Board Guidelines. (See Property Tax Rule 6, subds. (d) & (e); Assessors' Handbook section 502, *Advanced Appraisal* (Reprinted January 2015) (AH 502), pp. 20-21; *Unitary Valuation Methods*, (2003), p. 30; and Cal. Bd. of Equalization, *Guidelines for Substantiating Additional Obsolescence*, at p. 1.)

Income Approach to Value

Property Tax Rule 8, subdivision (a), states that "the income approach is used in conjunction with other approaches when the property under appraisal is typically purchased in anticipation of a money income and either has an established income stream or can be attributed a real or hypothetical income stream by comparison with other properties." Subdivision (b) describes the income approach

1 to value as the valuation method whereby, “an appraiser values an income property by computing the
2 present worth of a future income stream. This present worth depends upon the size, shape, and
3 duration of the estimated stream and upon the capitalization rate at which future income is discounted
4 to its present worth.” Subdivision (c) provides that “the amount to be capitalized is the net return
5 which a reasonably well-informed owner and reasonably well-informed buyers may anticipate on the
6 valuation date that the taxable property existing on that date will yield under prudent management and
7 subject to legally enforceable restrictions as such persons may foresee as of that date.”

8 **Reconciliation of Value Indicators**

9 Property Tax Rule 3 requires that, in estimating value, the assessor shall consider one or more
10 of the approaches to value “as may be appropriate for the property being appraised,” which includes
11 the comparative sales approach, the cost approach (e.g., HCLD valuation methodology), or the
12 income approach (CEA valuation methodology). The appropriateness of an approach is often related
13 to the type of property being appraised and the available data. (AH 502, p. 109.) In addition, the
14 validity of a value indicator will depend upon the accuracy of data and adjustments made to the
15 approach. That is, the accuracy of a value indicator depends on the amount of available comparable
16 data, the number and type of adjustments, and the dollar amount of adjustments. Finally, if a large
17 amount of comparable data is available for a given approach, the appraiser may have more confidence
18 in that approach. For example, if income, expense, and capitalization rate data can be obtained from
19 many properties comparable to the subject, the appraiser may attribute significant accuracy to the
20 income approach. The greatest reliance should be placed on that approach or combination of
21 approaches that best measures the type of benefits the subject property yields. The final value estimate
22 reflects the relative weight that the appraiser assigned, either implicitly or explicitly, to each approach.
23 (AH 502, p. 112.)

24 **Appeals Attorney’s Analysis and Comments**

25 Respondent is presumed to have correctly determined the value of the property at issue, and
26 Petitioner bears the burden of proving otherwise.

27 Here, Petitioner contends that because Respondent’s calculated HCLD value indicator exceeds
28 the CEA value indicator by approximately \$8 billion, Respondent’s 2024 Board-adopted unitary value

1 is flawed, as the various approaches to value must yield approximately the same results, and
2 differences of such a magnitude indicate that the value indicators were not reconciled. Further,
3 Petitioner contends Respondent did not reconcile the two value indicators, as required by Property Tax
4 Rule 3 and Board Guidance, but instead “simply states that the final value estimate is an appraiser’s
5 opinion of value.” (Petition, p. 11.) Petitioner appears to be asserting the Board should adopt the
6 appraisal judgment of the 2020 draft EY Report or, alternatively, adjust the weighting of the indicators
7 pursuant to its request, without putting forth any specific argument or evidence to support their request
8 for additional weight to be placed on the CEA value indicator, despite bearing the burden of proof to
9 show error or illegality.

10 Respondent contends that Board guidance clearly states that significant differences may occur
11 in validly calculated indicators. (SAPD Analysis, p. 6, citing AH 501, p. 62.) Further, Respondent
12 notes that the HCLD value indicator is a reliable indicator of value for closely regulated public
13 utilities, like Petitioner, because HCLD, with some modification, approximates the rate base that
14 regulators use in establishing revenue requirements. Accordingly, Respondent contends, in light of all
15 available evidence, it was reasonable and appropriate to place 75 percent reliance on the HCLD value
16 indicator, which reflects the consideration of many factors, including: Petitioner’s “regulatory lag,”
17 Petitioner’s established income stream, the relative reliance placed on the value indicators of other
18 rate-base regulated utilities, and consistency with Property Tax Rules 3, 6, and 8, as well as relevant
19 Board guidance. Further, Respondent contends Petitioner’s allegation that the difference in the HCLD
20 and CEA value indicators being attributed to obsolescence is wholly unsupported. Accordingly,
21 Respondent concludes Petitioner has provided no evidence or argument to require a revised weighting
22 of the value indicators.

23 Based on the evidence and arguments submitted to the record to date, the Appeals Attorney
24 finds that Petitioner has not provided specific evidence or argument to prove that its HCLD indicator is
25 overstated, nor has Petitioner shown that its CEA value indicator should be granted additional reliance.
26 Petitioner’s contention instead appears to rest on its request that the Board find Respondent’s appraisal
27 judgment and valuation approach flawed, without Petitioner providing any specific evidence, and that
28 the Board should instead adopt the appraisal judgment of the draft 2020 EY Report or Petitioner’s

1 unsupported claims in the instant petition.³⁰ However, it is well settled that the burden of proof is on
2 the Petitioner, and that such treatment would be not only unsupported under relevant law and appraisal
3 principles, but also inequitable in comparison to other rate-regulated electric-generating utility
4 assessees that are also assessed by this Board.

5 At the hearing, the parties should be prepared to discuss the issue; further, Petitioner should be
6 prepared to explain: why, specifically, as a rate-base regulated utility, it believes Respondent's HCLD
7 indicator is less reliable, despite HCLD being considered to be one of the more important indicators of
8 value for closely regulated utilities, and provide a rationale relying upon verifiable evidence and
9 relevant legal and appraisal principles; additionally, why, specifically, Petitioner believes its CEA
10 value should be granted more relative reliance in comparison to the HCLD value indicator and what
11 verifiable evidence or relevant legal and appraisal principles support that request; and why Petitioner's
12 value indicators should be weighted differently compared to other similarly situated investor-owned,
13 rate-regulated utilities.

14 15 **ISSUE 3**

16 **Whether Petitioner Has Shown that Respondent Must Adjust the Board-Adopted Value for SCE's**
17 **Accrual for Liabilities for the 2017/2018 Wildfires and Mudslides.**

18 **Petitioner's Contentions**

19 Petitioner asserts the 2024 Board-adopted value does not account for SCE's accrual for
20 liabilities for the 2017/2018 wildfires and mudslides, erroneously disregarding costs for estimated
21 claims and settlements pre-AB 1054, just as Respondent has done in its 2019 through 2024
22 assessments. (Petition, p. 14.) Petitioner argues that Respondent has improperly made no adjustments
23 to reflect the expected losses and settlement payments in SCE's unitary assessments, despite valuation
24 of a going concern requiring consideration of forecasted future expenses, as a potential buyer would
25 become responsible for those liabilities and factor those obligations into the purchase price. (*Id.* at pp.
26 14-18.) On this basis, Petitioner requests an adjustment of \$689 million from both the HCLD and
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³⁰ Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.)

1 CEA values to account for these operating expenses above and beyond insurance recoveries. (*Id.* at p.
2 17; Petition, Exhibit B.)

3 Petitioner asserts that Respondent ignores Petitioner’s wildfire-related expenses as past
4 expenses that are not anticipated to be incurred again in the future. (*Id.* at p. 17.) Petitioner refutes this
5 treatment by stating that its request for an adjustment of \$689 million represents quantifiable
6 operating expenses which negatively impact the going concern value of its property, rather than a
7 contractual or financing liability. (*Ibid.*) Petitioner contends such expenses are ordinary and necessary
8 parts of SCE’s operation as a going concern, and even if they were not ordinary in the “new normal”
9 of year-round wildfires in California, Respondent does not provide citation to support excluding a
10 non-ordinary expense that is anticipated in the future.³¹ (*Id.* at pp. 16-17.) Petitioner further asserts
11 that Rule 8 and AH 502 require the inclusion of anticipated income and operating expenses, and that
12 Respondent cites no authority to exclude a non-ordinary expense that is anticipated in the future.
13 (*Ibid.*)

14 In its Reply, Petitioner does not dispute that the liabilities at issue stem from 2017 and 2018
15 events, but asserts that SAPD is wrong that these claims and settlements will neither continue to
16 increase, nor be paid in the foreseeable future. (Reply, p. 11.) Between December 31, 2022, and
17 December 31, 2023, SCE claims to have accrued additional losses of \$630 million additional losses
18 related to these events, bringing its total to \$8.7 billion in settlements related to these events. (*Id.*, p.
19 11-12.) Additionally, Petitioner generally renews its contentions as to this issue, and notes that AB
20 1054’s remedies do not address the losses/settlements related to the 2017 and 2018 Wildfire/Mudslide
21 events, as it only covers wildfires occurring on or after July 2019. (*Id.*, p.12.) Petitioner concludes by
22 reasserting that while the initial liability stems from past events, that does not change that it is
23 resulting in ongoing expenses to SCE as claims are settled and paid, and such expenses would be
24 considered by any willing buyer, and thus, must be allowed in its opinion. (*Id.* at p. 13.)

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28 ³¹ In support, Petitioner cites a general statement from AH 502 to support this position. AH 502, p. 67 states, “Cost trends relating to the components of operating expenses should be studied to estimate the future level of operating expenses.” Petitioner asserts such costs are anticipated to continue in the future, but does not address the likelihood of such claims in the context of AB 1054, which is designed to reduce the likelihood of such expenses if and until the wildfire mitigation fund is exhausted.

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Respondent's Contentions

Respondent notes Petitioner claims that SAPD has erroneously disregarded \$689 million of accrued liability related to "Wildfire-related claims" dating back to 2017 and 2018, and requests that adjustments be made to both the HCLD and CEA value indicators because a knowledgeable buyer would take these liabilities into account when valuing those assets. (SAPD Analysis, p. 8.) In general, Respondent notes that it is unclear, however, why these liabilities, which arguably reduce the value of Petitioner's *business* as a going concern, necessarily results in a reduction to the value of its *property* as a going concern or its taxable unitary value, nor why Petitioner equates the valuation of its *property* as a going concern with the value of its *business* as a going concern, as none of the authorities Petitioner cites supports that proposition. (*Id.* at pp. 8-9, emphases added by Respondent.)

Respondent notes that consistent with the California Constitution Article XIII, section 1, the standard of value is fair market value. (SAPD Analysis, p. 8.) Further, for state-assessed properties, the California Supreme Court has stated:

From our review of the relevant constitutional and statutory provisions, we conclude that unit taxation is properly characterized not as the taxation of real property or personal property or even a combination of both, but rather as the taxation of *property as a going concern*. First, what the Board assesses is the value of the public utility *property* as a going concern; it considers the earnings of the *property* as a whole, and does not consider, less still assess, the value of any single real or personal asset.

(*Id.* at p. 9, quoting *ITT*, (1985) 37 Cal.3d at 864-865, emphases added by Respondent.) Respondent notes this is explained for purposes of California property tax purposes by AH 502 as follows:

"Going concern value" is a term that has been used in a variety of contexts, and more than one definition of the term can be found in the appraisal literature. Also, there are different meanings for California property tax purposes and more than one meaning even within California property tax law.

¶ ... ¶

Outside the property tax arena, going concern appraisals are commonly conducted for hotels and motels, restaurants, bowling alleys, industrial enterprises, shopping centers, retail stores, and similar business operations using real property. Generally, the real property is considered an integral part of the business operation. Without an allocation among the various elements contributing value to the business operation, however, *such an appraisal is not appropriate for California property tax purposes....*

1 Where the unit principle of valuation is used, it has been said that the assessable property
2 is valued as a going concern. *This means only that the taxable property of the business*
3 *should be valued as if put to beneficial or productive use. It does not mean that the entire*
value of the business can be assessed or that the going concern value is assessable.

4 (*Ibid.*, quoting AH 502, p. 157, emphases added by Respondent.) Accordingly, Respondent notes their
5 appraised value reflects the total market value of all taxable *property* as a unit owned or used by
6 Petitioner, not the “firm value,” which can be thought of as an estimate of the price a potential buyer
7 might be willing to pay for the entire *business*. (SAPD Analysis, p. 9.) Respondent contends the entire
8 business or firm value, by itself, is not relevant to California unitary property taxation. (*Ibid.*)

9 Respondent also remarks that this context is why the CPUC’s consideration of liabilities in
10 evaluating a proposed acquisition is irrelevant, because CPUC is instead evaluating the *entire business*.
11 (*Id.* at pp. 9-10.)

12 Respondent goes on to note that Petitioner’s equating of “firm value” with the value of the
13 entire company, requiring a decline in the unitary value of taxable property when firm value declines,
14 is reasoning that ignores the fundamental difference between the value of “*the entire company*” and the
15 unitary value of “*the company’s taxable property*.” (*Id.* at p. 10; emphases added by Respondent.)
16 Instead, because Petitioner’s “Wildfire-related claims” are for the settlement or potential settlements of
17 litigation arising out of wildfires and mudslides that occurred in 2017 and 2018, Respondent notes it
18 does not reduce the value of Petitioner’s taxable property, making a downward adjustment
19 inappropriate. (*Ibid.*)

20 Additionally, Respondent contends Petitioner’s request for the same deduction to be made to
21 the CEA value indicator is also not appropriate for the same reasons. (*Id.* at pp. 10-11.) Respondent
22 notes the premise of the CEA value indicator calculation is to convert (or capitalize) a *future* income
23 stream into present worth (Rule 8, subd. (a).), and the amount to be capitalized is,

24 the net return which a reasonably well informed owner and reasonably well informed buyers
25 may *anticipate* on the valuation date that the taxable property existing on that date will yield
26 under prudent management and subject to such legally enforceable restrictions as such persons
may foresee as of that date.

27 (SAPD Analysis, p. 10; citing Rule 8, subd. (c), emphasis added.) Thus, Respondent contends it is
28 clear that neither past nor non-ordinary expenses may be deducted from a future income stream to be
capitalized. (*Ibid.*) Accordingly, as Respondent notes the costs for which Petitioner seeks a reduction

1 are past expenses and, regardless of whether other wildfire or mudslide liabilities will ordinarily incur
2 again in the future, it is undisputed that the particular liabilities at issue have been accrued from
3 claims that occurred in the past and will not reoccur. (*Ibid.*)

4 Respondent also notes that Petitioner's argument that wildfire liabilities should now be
5 considered ordinary expenses and that they will occur in the future, may or may not actually be true,
6 but regardless, it is only these particular liabilities from these past events that are at issue. (*Ibid.*)
7 Further, Respondent notes it is undisputed that these particular liabilities are accrued for liability
8 related to claims that resulted from wildfires and mudslides in 2017 and 2018, all of which occurred in
9 the past and will not recur. (*Ibid.*)

10 Finally, Respondent notes that while Petitioner appears to be arguing that since these past
11 liabilities will actually be paid at some time in the future, they are deductible when calculating the
12 CEA value indicator; however, Respondent notes the mere fact that they may be paid in the future does
13 not mean that such expenses qualify as deductible, ordinary operating expenses. (*Id.* at pp.10-11.)

14 For these reasons, Respondent maintains no adjustment can be recommended as to this issue.

15 **Appeals Conference**

16 Parties met at the Appeals Conference on November 15, 2024. At the conference, Petitioner and
17 Respondent discussed and renewed their positions as captured in the briefings.

19 **Applicable Law and Appraisal Principles**

20 **Burden of Proof**

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

25 **Value Standard**

26 See Issues 1 and 2, Applicable Law, p. 14.

27 **Income Approach to Value**

28 See Issues 1 and 2, Applicable Law, pp. 15-16.

1 Subdivision (c) provides that “the amount to be capitalized is the net return which a reasonably
2 well-informed owner and reasonably well informed buyers may anticipate on the valuation date that
3 the taxable property existing on that date will yield under prudent management and subject to legally
4 enforceable restrictions as such persons may foresee as of that date.” Net return is the difference
5 between gross return and gross outgo. (Rule 8, subd. (c).) Amortization, depreciation, and debt
6 retirement are explicitly excluded from gross outgo. (*Ibid.*)

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8 **Appeals Attorney’s Analysis and Comments**

9 Respondent is presumed to have correctly determined the value of the property at issue, and
10 Petitioner bears the burden of proving otherwise.

11 Here, Petitioner contends that Respondent’s calculated unitary value inappropriately excludes
12 Petitioner’s \$689 million in liabilities related to the 2017/2018 wildfires and mudslides and requests a
13 corresponding reduction to each value indicator. Petitioner asserts such an adjustment is necessary as
14 the liabilities reduce its firm value, or going concern as a business, and certainly would be considered
15 by any prospective buyer or the CPUC in any proposed transaction. Further, Petitioner contends such
16 an adjustment to the CEA value indicator calculation is necessary as such expenses are ordinary and
17 reoccurring, as liabilities have continued to accrue in the current year related to the 2017/2018
18 Wildfires/Mudslides. Petitioner further contends Respondent misinterprets Property Tax Rules and
19 Assessors’ Handbooks by denying Petitioner’s requested adjustments to the HCLD and CEA value
20 indicators.

21 However, as Respondent points out, Petitioner has provided no specific argument, evidence, or
22 legal or appraisal authority to support its proposed deduction of the past and non-ordinary expenses
23 related to its pre-AB 1054 liabilities for property tax purposes. For purposes of the HCLD approach,
24 Petitioner does not provide evidence or authority to support that such liabilities reduce Petitioner’s
25 property tax value. Additionally, as Respondent points out, for purposes of the CEA approach, such a
26 deduction would be directly contrary to Property Tax Rule 8 and relevant Board guidance. Further, no
27 legal or appraisal support is provided with respect to the proposed deduction to the HCLD or CEA
28 value indicators, as such expenses are undisputedly related to past events that are unlikely to occur in

1 the future, even if the liability from such past events is still being finalized as remaining claims are
2 settled, litigated, or otherwise resolved.

3 Accordingly, based on the evidence and arguments submitted to the record to date, the Appeals
4 Attorney notes that Petitioner has not shown specific evidence or argument to prove that the claimed
5 expenses must be deducted from both the CEA and HCLD value indicators, nor has Petitioner shown
6 that such expenses represent ordinary and future, anticipated operating expenses.³² Further, the
7 Appeals Attorney notes such expenses are explicitly excluded from the CEA approach under Property
8 Tax Rule 8, as Respondent contends. Additionally, even if wildfire liabilities should now be
9 considered ordinary expenses reasonably occurring in the future, it is undisputed that these particular
10 liabilities are a result of liability resulting from past wildfires and mudslides (in 2017 and 2018), which
11 are not appropriate to deduct from the future income stream to be capitalized. Petitioner's argument
12 appears to rest on the Board finding Respondent's appraisal judgment and approach to these wildfire
13 liabilities as flawed, without providing any specific evidence or legal or appraisal support to
14 substantiate such flaws, and that the Board grant Petitioner's unsupported request to deduct \$689
15 million from both the CEA and HCLD value indicators.³³ However, it is well settled that the burden of
16 proof is on the Petitioner.

17 At the hearing, the parties should be prepared to discuss the issue; further, Petitioner should be
18 prepared to explain: what legal and appraisal support exists to support the deduction of these liabilities
19 expenses from the CEA and HCLD value approaches; and how Petitioner's requested adjustment can
20 be reconciled with Property Tax Rule 8 and other Board issued guidance, as quotes from the Assessors
21 Handbooks' cited in isolation do not supersede Property Tax Rule 8 or the Board's guidance in
22 context.

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28 ³² Even if one were to accept that it is ordinary for utilities to be regularly liable for causing or contributing to wildfire or
mudslide incidents, the Legislature designed AB 1054 to mitigate the likelihood of wildfire expenses going forward.

³³ See Petition p. 2 and Petition, Exhibit B; however, note that such claimed amounts mathematically tie to the requested
revised reliance on the HCLD and CEA value indicators in Issues 1 and 2, and the accuracy thereof may be contingent upon
the Board's determination of Issues 1 and 2.

ISSUE 4**Whether Petitioner Has Shown that Respondent Improperly Assessed \$699 million in Wildfire Mitigation Capital Expenditures in the HCLD Value Indicator****Petitioner's Contentions**

Petitioner contends that Respondent improperly assessed \$1.6 billion of wildfire mitigation capital expenditures in its 2024 assessment of SCE, based on the incorrect assumption that these assets generate a cash flow from ratepayers, allowing SCE to realize a return on investment for these capital expenditures. (Petition p. 21.) Petitioner contends that under AB 1054, SCE is required to make capital expenditures to the wildfire mitigation fund but is precluded from earning both a rate of return of and a return on the investment. (*Ibid.*) Petitioner asserts this inclusion results in approximately \$699 million that should be removed from SCE's HCLD indicator.³⁴ (*Ibid*; see also Petition, Exhibit D.)

Petitioner further asserts that a potential buyer would not have the opportunity to recover the wildfire mitigation capital expenditures, and thus conclude that the first \$1.6 billion of wildfire mitigation capital expenditures have little or no value. (Petition, p. 21.) Petitioner cites the analysis in the draft 2020 EY report to support that a prospective buyer would not pay for a \$1.6 billion capital expenditure that produces no return. (*Id.* at p. 22.) Petitioner argues that Respondent's appraisal assumes that the expenditures are being capitalized and included in the rate base, on which utilities are permitted to earn a return, and concludes that if the capital expenditures are not included in Petitioner's rate base, they must be removed from the HCLD value indicator. (*Id.* at pp 22-23, citing Assessors' Handbook 502, p. 147.)

Petitioner then argues that in the alternative, these capital expenditures are intangible assets exempt from taxation, as such expenditures are statutorily required for Petitioner to continue to operate, and thus confer intangible rights upon Edison and any future purchaser. (*Id.* at p. 23.)

Petitioner then adds that the property it spent \$1.6 billion replacing has been discarded, so even if Petitioner may have the right to continue to receive a return with respect to the formerly owned property, since such property is no longer owned by Petitioner the right to receive a return on

³⁴ Assessing officers are presumed to have properly performed their duties. (Evid. Code, § 664.)

1 the former property is an intangible right not assessable for property tax purposes. (*Id.* at p. 23.)
2 Further, the cost of this property should be removed from the HCLD and the income Edison receives
3 with respect to this intangible right should be excluded from the CEA indicator. (*Ibid.*)

4 In their Reply, Petitioner contends SAPD's explanation excerpted from AH 502, "The HCLD
5 for property tax appraisal purposes, therefore, differs from the rate base as established by the
6 regulatory agency. Some items included in the rate base are not included in the HCLD and some items
7 included in the rate base are included in the HCLD," is misleading, and in context is only meant to
8 acknowledge Construction Work in Progress (CWIP)'s exclusion from the rate base but taxability for
9 property tax purposes. (Reply pp.6-7, quoting AH 502, pp. 146-147.) Petitioner also contends SAPD
10 misunderstands the concept of "return of" capital in a regulatory context. (Reply, p. 7-8.) Specifically,
11 Petitioner contends that while SAPD argues that Petitioner is being paid back for its cost through a
12 special surcharge paid by ratepayers, CPUC D.20-11-007 requires that the special surcharges
13 collected from ratepayers will repay the bondholders of the Recovery Bond, such that Petitioner will
14 not recover either the return of or a return on the wildfire mitigation investments. (*Id.*, p. 7.)
15 Petitioner then argues that SAPD ignores basic valuation principles, as Petitioner contends assets, to
16 have value under a CEA approach, must produce income, or, under the HCLD approach, must be
17 included in the rate base. (*Id.*, p. 8.) Finally, Petitioner generally renews several of its arguments,
18 reaffirming the wildfire mitigation investments are not included in their rate base, (*Id.*, p. 8), and that
19 as the expenditures were required under AB 1054, the intangible value of being compliant with AB
20 1054 makes them intangible assets that are not assessable. (*Id.*, pp. 10-11.)

21 **Respondent's Contentions**

22 Respondent contends no adjustment is appropriate for this issue. Respondent notes Petitioner
23 essentially argues that because these costs are not included in rate base, these assets have no value and
24 must be excluded entirely from the HCLD value indicator. (SAPD Analysis, p. 11.) However,
25 Respondent explains that whether or not property is included in the rate base of a regulated utility is
26 not solely determinative of whether it has "value" for property tax purposes and thus must or must not
27 be included in HCLD. (*Ibid.*) Respondent cites AH 502, which states:

28 The HCLD for property tax appraisal purposes therefore, differs from the rate base as
established by the regulatory agency. Some items included in rate base are not included
in the HCLD, and some items not included in the rate base are included in the HCLD.

1 (*Ibid.*, citing AH 502, p. 146-147.) Therefore, Respondent contends Petitioner's view is false that all
2 costs excluded from rate base must be excluded from HCLD. (*Ibid.*)

3 Specifically, Respondent notes the wildfire mitigation capital expenditures have value, as
4 Petitioner spent \$1.6 billion to purchase those assets and had they not, Petitioner (or any potential
5 purchaser) would not be compliant with AB 1054. (*Ibid.*)

6 Respondent notes SAPD has recognized that there is an impact on value to these capital
7 expenditures being excluded from the rate base and has made a proper adjustment in Petitioner's 2024
8 Board-adopted value.³⁵ (SAPD Analysis, pp. 11-12.) Respondent notes when making capital
9 expenditures, firms expect both a "return of" their invested capital as well as a "return on" their
10 invested capital. (*Ibid.*) Respondent notes a "return of" capital accounts for a recovery of the
11 investment while a "return on" capital accounts for a reward for making an investment. (*Ibid.*, citing
12 AH 502, p. 62.) Both of these components are captured in the capitalization rate, which provides
13 explicitly or implicitly for both the return of and the return on capital. (*Ibid.*)

14 Respondent contends that because AB 1054 prohibits Petitioner from earning a return on
15 equity but does not prohibit earning a "return of" or a debt return on its capital expenditure, SAPD
16 made appropriate adjustments to the HCLD cost indicator to account for this, by calculating the
17 present value of the income using a discount rate that excludes the equity portion of the
18 capitalization rate. (SAPD Analysis, p.12.) The excluded equity portion represents the return *on* the
19 investment, and properly leaves in the rate for return *of* the investment. (*Ibid.*) Respondent then
20 removed the difference between this present value amount and the total \$1.6 billion capital
21 expenditure, resulting in an approximately \$736 million reduction to the HCLD value indicator,
22 which was reflected in Petitioner's 2024 Board-adopted unitary value. (*Ibid.*)

23 Respondent also contends that Petitioner's alternative arguments that the capital
24 expenditures are intangible assets exempt from taxation, and that the property Petitioner spent \$1.6
25 billion replacing has been discarded and is no longer owned by Petitioner, are each claimed
26 without evidence. (SAPD Analysis, p. 12.) Respondent asserts that these arguments ignore the fact
27 that \$1.6 billion dollars of tangible, depreciable equipment was purchased and is currently installed
28

³⁵ \$736 million was deducted from the HCLD value indicator. See SAPD Analysis, p. 12.

1 as a part of Petitioner's physical infrastructure. (*Ibid.*) Respondent states that the equipment that
2 was actually replaced and discarded will be removed from the HCLD value indicator and therefore
3 has no unitary value, as is done with all equipment that is retired and removed from an assessee's
4 books and records. (*Ibid.*) Therefore, Respondent recommends no adjustment as to this issue.

5 **Appeals Conference**

6 Parties met at the Appeals Conference on November 15, 2024. At the conference, Petitioner and
7 Respondent discussed and renewed their positions as captured in the briefings.

9 **Applicable Law and Appraisal Principles**

10 **Burden of Proof**

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

15 **Value Standard**

16 See Issues 1 and 2, Applicable Law, p. 14.

17 **HCLD Approach to Value**

18 See Issues 1 and 2, Applicable Law, pp. 14-15.

19 **Appeals Attorney's Analysis and Comments**

20 Respondent is presumed to have correctly determined the value of the property at issue, and
21 Petitioner bears the burden of proving otherwise.

22 Here, Petitioner contends that Respondent should deduct the entire \$1.6 billion wildfire capital
23 expenditures from its HCLD value indicator because Petitioner is not allowed to earn a rate of return
24 on the expenditures, and a prospective buyer would not pay for a \$1.6 billion capital expenditure that
25 produces zero return. Petitioner also argues that if the capital expenditures are not included in the rate
26 base, they should be removed from the HCLD value indicator. However, Respondent explains that the
27 HCLD approach for property tax appraisal purposes differs from the rate base, and that the capital
28 expenditures have value as Petitioner spent \$1.6 billion to purchase assets from which Petitioner will

1 earn a return of the expenditures through depreciation and a return on the expenditures through the
2 reimbursement of interest paid for debt service. Respondent additionally contends that since AB 1054
3 prohibits Petitioner from earning an equity return on this capital expenditure but does not prohibit it
4 from earning a return of or a debt return on its capital expenditure, Respondent has already adjusted the
5 HCLD value indicator appropriately for these expenses: by calculating the present value of the income
6 using a discount rate that excludes the equity portion of the capitalization rate, reflecting that Petitioner
7 will not receive a *return on* the investment, but properly leaves the rate for *return of* its capital
8 expenditure, which Petitioner will receive the benefit of. Respondent noted this calculation resulted in
9 an approximately \$736 million reduction to the HCLD value indicator, which was already reflected in
10 Petitioner's 2024 Board-adopted unitary value.

11 Petitioner contends in the alternative that the capital expenditures, by being compliant with AB
12 1054, makes them intangible assets exempt from taxation, but provides no explanation, evidence, or
13 legal or appraisal basis or authority to support this contention.³⁶ Petitioner further contends that the
14 property Petitioner spent \$1.6 billion replacing has been discarded and is no longer owned by
15 Petitioner, but, as Respondent points out, Petitioner has provided no specific evidence of retired assets
16 being assessed within its 2024 unitary value. Further, Respondent states that the \$1.6 billion dollars of
17 tangible, depreciable equipment was purchased and is currently installed as part of Petitioner's
18 physical infrastructure.

19 Based on the evidence and arguments submitted to the record to date, the Appeals Attorney
20 finds that Petitioner has not shown specific evidence or argument to prove error within Respondent's
21 calculation of the existing adjustment to the HCLD attributable to these assets, but instead Petitioner
22 continues to assert the full \$1.6 billion should be removed from the HCLD value indicator.

23 At the hearing, the parties should be prepared to discuss the issue; further, Petitioner should be
24 prepared to explain: what legal and appraisal support exists to show Respondent erred in its
25 calculation; why, specifically, Petitioner asserts there is no assessable value attributable to the capital
26 expenditures, despite Petitioner receiving a *return of* its capital expenditure; and what legal and
27

28 ³⁶ Cal. Const. Art. XIII, section 1 states: "Unless otherwise provided by this Constitution or the laws of the United States [a]ll property is taxable and shall be assessed at the same percentage of fair market value." The appeals attorney notes exemption from property tax does not wholly correspond to income tax or accounting deductions and the California Constitution specifically requires a constitutional or statutory basis for any exemption in property tax.

1 appraisal principles support the exemption of such assets for property tax purposes, such that the
2 deduction of the full \$1.6 billion from the HCLD approach is required under California property tax
3 law. Additionally, if Petitioner continues to argue that it is being assessed on the asset costs of retired
4 assets, Petitioner must provide verifiable evidence of the retirement of such assets to substantiate such
5 requested adjustments consistent with the well settled burden of proof.

6 7 **ISSUE 5**

8 **Whether Petitioner Has Shown that Respondent Erred in Its Treatment of Wildfire Insurance** 9 **Fund Related Contributions.**

10 **Petitioner's Contentions**

11 Petitioner notes that SCE made an initial contribution of \$2.4 billion to the Wildfire Insurance
12 Fund, which is intended to provide some insurance coverage in the event of a catastrophic wildfire
13 event, on September 9, 2019, and thereafter Petitioner will make 10 annual contributions of
14 approximately \$95 million per year to the fund, consistent with section 3292, subdivision (a) of the
15 California Public Utilities Code.³⁷ (Petition, p. 18.) Petitioner asserts Respondent erred in its treatment
16 of the Wildfire Insurance Fund-related contribution by ignoring the initial contribution of \$2.4 billion,
17 instead arguing that the initial contribution and annual payments should be treated as insurance
18 premiums and spread ratably over Petitioner's updated estimated 20-year coverage period, yielding an
19 annual estimated insurance fund expense of \$213 million. (Petition, pp. 18-19.) Petitioner contends
20 the proper treatment of these expenses would reduce the CEA value indicator by \$1,447,865,602 and
21 the overall unitary value by \$1,085,899,202.³⁸ (Petition, pp. 9, 18 and Petition, Exhibit C.)

22 Petitioner claims the Wildfire Insurance Fund contributions are being treated similarly to
23 prepaid insurance under Generally Accepted Accounting Principles (GAAP). (Petition, p. 18.) As no
24 period of coverage was provided in AB 1054, Petitioner is allocating the total expense ratably based
25 on its updated estimated twenty-year period of coverage. (*Ibid.*)

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27
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³⁷ Petitioner cites its Form 10k (2024), at 151-152.

³⁸ Petitioner cites Petition, Exhibit C to reflect the requested adjustment in value attributable to the disallowed expenses. However, the Appeals Attorney notes such a calculation is dependent upon the Board's consideration of Issues 1 & 2.

1 Next, Petitioner refutes SAPD's arguments, presumably from the 2020 petition discussion,
2 that a prospective purchaser would not consider the \$2.4 billion prepaid insurance in the company's
3 value. (Petition, p. 19-20.) Instead, Petitioner contends Wildfire Insurance Fund contributions are
4 equivalent to the payment of insurance premiums, and that a potential purchaser would be willing to
5 pay more for a utility that had prepaid this annual contribution, as compared to a utility that had not
6 done so, due to the increased estimated insurance premiums the purchaser would have to make absent
7 these fund contributions. (Petition, pp. 20-21.)

8 Then, Petitioner argues that SAPD is mischaracterizing the prepaid expense as excludable
9 amortization or depreciation expense, as the expense at issue constitutes prepaid insurance or some
10 other intangible asset that will reduce future expenses, as the initial contribution was a legal
11 prerequisite that gave Petitioner the right to participate in the Fund, which is an intangible right. (*Id.*, p.
12 19.)

13 Additionally, Petitioner contends that AH 502 states that property insurance may be prepaid for
14 three years and deducted as an expense in a direct capitalization income approach, though in
15 Petitioner's case the coverage is estimated at 15 years, and that an "appraiser would annualize this
16 expense in direct capitalization." (*Id.* at p. 20, citing AH 502, p. 71-72.)

17 Petitioner further contends that the \$213 million annual expense should be included in the CEA
18 value indicator because future insurance premiums are bound to increase consistent with the wildfire
19 risk conditions in California. (Petition, p. 20.)

20 Petitioner additionally notes Respondent's proper treatment of such expenses may actually
21 increase income in future years due to reduced future expenses, and that portion of the increased
22 income related to the initial contribution should be removed from the income approach as income from
23 an intangible asset. (*Id.* at p. 20.)

24 Finally, Petitioner claims that Respondent's treatment of the fund contributions is nonuniform
25 in its application to all state assessees, claiming that the initial contribution was allowed for another
26 state assessee. (Petition, p. 20-21.) On this basis, petitioner asserts respondent is acting arbitrarily,
27 unfairly, or otherwise non-uniform in its treatment of Petitioner. (*Ibid.*)
28

1 In their Reply, Petitioner renews the above arguments. (Reply, pp. 8-9.) Petitioner further
2 contends that SAPD has incorrectly interpreted *De Luz Homes, Inc. v. County of San Diego* (“*De Luz*”)
3 (1955) 45 Cal.2d 546, explaining that while *De Luz* precludes a deduction for “depreciation of the
4 property,” it does not preclude a deduction for operating and maintenance expenses, and prepaid
5 insurance are such expenses. (*Id.*, at p. 9.) Petitioner cites to AH 502 to support its argument, wherein
6 under a direct capitalization method, like the CEA, “expenses are annualized even though some
7 expenditures may not actually occur on an annual basis” and prepaid property insurance is provided as
8 an example. (Reply, p. 9, citing AH 502.)

9 Additionally, Petitioner references that Member Gaines’ comments in the Board hearing of
10 their 2020 petition appeared to support this treatment of such expenses as annualized expenses
11 removable from the CEA calculation. (Reply, p. 9.)

12 Petitioner argues that while Respondent is attempting to create a requirement that another
13 future AB 1054-like contribution will occur, the guidance does not create a requirement that the
14 deduction of the prepaid insurance is only allowed when an identical payment is guaranteed to occur in
15 the future. (Reply, pp. 9-10.) Petitioner also asserts that these prepaid insurance expenses would be
16 viewed as relevant expenses to any prospective buyer and be considered regular and reoccurring in
17 light of wildfire likelihood in California. (*Ibid.*) Additionally, Petitioner notes the requested treatment
18 is consistent with its audited financial statements. (*Ibid.*) Petitioner concludes that the adjustment of
19 approximately \$1.07 billion (CEA-adjusted present value of the annual expensing of \$214 million over
20 the remaining coverage period) for the prepaid insurance contribution of \$2.4 billion and the annual
21 contributions of \$95 million is reasonable and should be allowed. (*Id.* at 10.)

22 **Respondent’s Contentions**

23 Respondent contends that consistent with Property Tax Rule 8 and Board issued appraisal
24 guidance, Respondent appropriately disallowed the \$2.4 billion initial contribution as an expense in the
25 CEA value indicator. (SAPD Analysis, pp. 12-13; citing *UVM* pp. 35-37 and AH 502, p. 74.)
26 Respondent explains amortization and depreciation are not deducted when computing the future
27 income stream to be capitalized because doing so would artificially lower that future income stream by
28 subtracting non-cash expenses and would also cause the future income stream to no longer be a *future*

1 income stream (since it would then include past expenses); in other words, deducting either is contrary
2 to the principles on which the CEA indicator is premised. (SAPD Analysis, p. 13.) Thus, pursuant to
3 Property Tax Rule 8 and AH 502's interpretation thereof, Respondent did not allow the \$2.4 billion
4 initial contribution as an expense in the CEA value indicator because the contribution was made in a
5 previous year. (*Ibid.*)

6 Respondent contends Petitioner admits that the Wildfire Insurance Fund-related initial
7 contribution is both a past, non-recurring expense and that it is now being amortized over a 20-year
8 period³⁹ and Respondent maintains the treatment of amortized costs in the CEA indicator of value is
9 explained in Rule 8 and AH 502. (*Ibid.*) Further, in *De Luz*, the California Supreme Court made clear
10 that amortized costs are not deducted from the anticipated income to be capitalized.⁴⁰

11 While Respondent acknowledges the specific items which the *De Luz* Court considered were
12 leasehold improvements, Respondent maintains the Court's logic applies to capitalized assets
13 generally. (SAPD Analysis, p. 14.)

14 Additionally, Respondent notes that the accounting treatment of the initial contribution is
15 undisputed: an asset entitled "Wildfire Insurance Fund contributions" was created on Petitioner's
16 balance sheet and a corresponding amortized portion is deducted on SCE's income statement. (SAPD
17 Analysis, p. 14.) Thus, Respondent asserts that consistent with AH 502, *De Luz*, and generally
18 accepted appraisal practice, the initial contribution's treatment for property tax valuation purposes
19 should also be undisputed. (*Ibid.*)

20 Then, Respondent asserts Petitioner's contention that the expense be treated akin to prepaid
21 insurance, ratably deducted over some coverage period, misses the issue, as the issue is not over
22

23
24 ³⁹ Petitioner's 2024 10-k indicates the asset was amortized over 15 years in 2022 and 2023. (SCE 10-k, p. 74.)

25 ⁴⁰ Respondent includes selected excerpts to support its summary of *De Luz*. (SAPD Analysis, p. 14.) In determining what
26 costs would be considered in valuing a leasehold interest under a capitalization of income method, the Court stated that:
27 ...anticipated net earnings equal expected gross income less necessary expenditures for maintenance, operation,
28 and taxes.[fn omitted] *No deduction is made for the cost of the lease to the present lessee, i.e., his charges for rent
and amortization of improvements*, for to a prospective assignee the value of a leasehold is measured solely by
anticipated gross income less *expected necessary* expenditures.

(*De Luz Homes, Inc. v. County of San Diego, supra*, p. 566, emphasis added.) The Court concluded:

Furthermore, in determining the income to be capitalized to establish value for appraisal purposes, *no deduction
can be made for amortization*. [Citation.] '[N]o concept of income which includes ... depreciation in capital value
as a positive or negative item of income, is acceptable as a basis of valuation under the 'capitalized income'
method.' [Citation.]

(*Ibid.*)

1 whether the initial contribution is or is not prepaid insurance. (*Ibid.*) Respondent confirms that
2 Petitioner's ordinary insurance expense was allowed, but instead asserts the issue is over whether the
3 initial contribution is an ordinary, recurring expense and Petitioner has admitted that it is not in its
4 2024 10-K.⁴¹ (*Ibid.*)

5 Next, Respondent contends Petitioner's argument that the amortized expense will be
6 reoccurring due to the new reality of wildfires is also misframed; instead, Respondent asserts the issue
7 is whether the Petitioner will need to make another AB 1054-like initial contribution, something no
8 one can know at this time. (SAPD Analysis, p. 15.)

9 Respondent also notes that Petitioner itself does not know how long the AB 1054 fund will last,
10 as in 2019, SCE estimated 10 years (SCE 2020 10-k, p. 65), while in 2020-2023, the estimate was
11 increased to 15 years in its 2020 Form 10-k (SCE 2020 10-k, p. 122.). (SAPD Analysis, p. 15.)
12 However, Respondent notes that in 2019, the CPUC stated that "arguments positing that the fund may
13 be exhausted before 2035 are premature." (*Ibid.*; quoting CPUC, Decision D19-12-056, p. 37.)
14 Accordingly, Respondent concludes any deduction allowed of this initial contribution based on some
15 likelihood that some future AB 1054-like contribution will have to be made is pure speculation. (SAPD
16 Analysis, p. 15-16.) Respondent summarizes that because the \$2.4 billion initial contribution is a past
17 expense that need not be paid again, and because its deduction as amortization in future years is only
18 for the purpose of computing accounting net income, the initial contribution is not deductible from the
19 future income stream to be capitalized for property tax purposes. (*Ibid.*)

20 Respondent also reaffirms that while the initial contribution is not deductible, the required
21 annual contributions to the Wildfire Insurance Fund are allowable, as they are ordinary expenses
22 expected to be paid for a 10-year term. (*Ibid.*) Respondent notes this resulted in a \$502 million
23 reduction to the CEA value indicator, which has already been included in Petitioner's 2023 Board-
24 adopted value. (SAPD Analysis, p. 15-16.)

25 Finally, Respondent disputes inequitable treatment amongst state assessees occurred, as the
26 allowance or disallowance of the initial contributions were based on a consistent application of the
27

28 ⁴¹ SAPD Analysis, pp. 14-15, citing Edison International's 2024 Form 10-K, p. 6, where SCE lists various "non-core items" that "management does not consider representative of ongoing earnings," which includes a line item under this descriptor stating, "Charges of \$213 million (\$153 million after-tax) recorded in 2023 and \$214 million (\$154 million after-tax) recorded in 2022 from the amortization of SCE's contributions to the Wildfire Insurance Fund."

1 same principles to all utilities who contributed to the fund. (SAPD Analysis, p. 16.) Respondent further
2 affirms that all other arguments made by Petitioner on this issue remain unpersuasive, particularly that
3 valuation violates Article XIII, Section 1 of the California Constitution, the Due Process Clauses of the
4 state and federal Constitutions, the Equal Protection Clauses of the state and federal Constitutions, and
5 those that attempt to liken the initial contribution to a deductible intangible asset. (*Ibid.*)

6 For these reasons, Respondent recommends no adjustment as to this issue.

7 **Appeals Conference**

8 Parties met at the Appeals Conference on November 15, 2024. At the conference, Petitioner and
9 Respondent discussed and renewed their positions as captured in the briefings.

11 **Applicable Law and Appraisal Principles**

12 **Burden of Proof**

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

17 **Value Standard**

18 See Issues 1 and 2, Applicable Law, p. 14.

19 **Income Approach to Value**

20 See Issues 1 and 2, Applicable Law, pp. 15-16.

21 **The Income Approach: Amortization and Depreciation**

22 The income approach to value is generally described as any method that converts future
23 anticipated income into present value. (UVM, p. 35.) It is premised on the assumption that investors
24 will buy and sell property based on the income it is *expected* to yield. (*Ibid.*) The income that is
25 converted into present value is appraisal income, or “net return” as defined by Rule 8. (UVM, pp. 35-
26 37; Rule 8, subd. (c).) Net return is the difference between gross return and gross outgo. (Rule 8,
27 subd. (c).) Amortization and depreciation are explicitly excluded from gross outgo. (*Ibid.*) AH 502
28 explains why this is the case:

The reference to depreciation and amortization in subdivision (c) [of Rule 8] refers to the
accounting concept of depreciation (in this context, **amortization is a synonym for**

1 **depreciation**). Accounting depreciation and **amortization** charges are **non-cash**
2 **expenses** designed to spread, or match, the cost of a **previously incurred** cash
3 expenditure over future accounting periods. There are at least two theoretical reasons for
4 the exclusion of accounting depreciation charges as expenses. First, doing so incorporates
5 the recognized cash flow concept of the amount of income to be capitalized. Second,
6 accounting depreciation is a means of capital recovery based on past expenditures.
7 **However, in real estate valuation the point is not to recover past expenditures, but**
8 **rather to estimate the value that future income will be able to recover.**

9 (AH 502, p. 74; Emphases added.) In other words, amortization and depreciation are not deducted
10 when computing the future income stream to be capitalized because doing so would artificially lower
11 that future income stream by subtracting non-cash expenses and would also cause the future income
12 stream to no longer be a *future income* stream, as it would include past expenses. The *Supreme Court*
13 has confirmed this understanding in *De Luz*; the Court concluded,

14 Furthermore, ***in determining the income to be capitalized*** to establish value for appraisal
15 purposes, ***no deduction can be made for amortization.*** [Citation.] ‘[N]o concept of income
16 which includes ... depreciation in capital value as a positive or negative item of income, is
17 acceptable as a basis of valuation under the ‘capitalized income’ method.’ [Citation.]

18 (*De Luz Homes, Inc. v. County of San Diego, supra*, p. 566, emphasis added.)

19 **Appeals Attorney’s Analysis and Comments**

20 Respondent is presumed to have correctly determined the value of the property at issue, and
21 Petitioner bears the burden of proving otherwise.

22 Here, Petitioner contends that Respondent’s calculated present value deduction for the
23 remaining, future Wildfire Insurance Fund payments understates the annualized and prepaid-expenses
24 associated with the full contribution to the wildfire insurance fund; instead, Petitioner asserts the initial
25 contribution of \$2.4 billion and the 10 annualized payments should be treated as prepaid insurance
26 expenses, and capitalized within the Respondent’s CEA value indicator calculation as expenses over a
27 20-year period, as such treatment is reasonable in its opinion, as well as consistent with its own,
28 recently revised, accounting treatment of such expenses.

However, Respondent notes Petitioner admits the initial contribution has been amortized, and
contends amortized or past, non-ordinary expenses are not properly deducted from the CEA Value
calculation, as a capitalized earning approach only correctly reflects future, ordinary expenses, not past
expenses, consistent with relevant Property Tax Rule 8 and appraisal principals.

1 Based on the evidence and arguments submitted to the record to date, the Appeals Attorney
2 finds that Petitioner has not shown specific evidence or argument to prove error within Respondent's
3 calculation, which deducts the present value of the future remaining annual payments of \$95 million
4 already reflected in Petitioner's 2024 Board-adopted value. Instead, Petitioner continues to assert the
5 full \$2.4 billion initial fund should be annualized and deducted as ordinary, operating, prepaid
6 insurance expenses (\$214 million annualized as asserted in Petition) as it is "reasonable" and
7 analogous to prepaid insurance payments. However, Petitioner fails to reconcile its request with
8 Property Tax Rule 8 and relevant Board guidance, which explicitly disallows amortized expenses from
9 being deducted in the CEA approach, as the CEA calculation is designed to capitalize future income.

10 In general, the Appeals Attorney notes the difference between the parties in this issue seems to
11 stem from Petitioner's disagreement that accounting principles and treatment do not have directly
12 identical treatment under relevant property tax law and appraisal principles.

13 Additionally, Petitioner claims the expense at issue alternatively constitutes some other
14 intangible asset that will reduce future expenses, based presumably on the fact that the initial
15 contribution was a legal prerequisite that gave Petitioner the right to participate in the fund, but
16 Petitioner provides no explanation, evidence or legal or appraisal authority that supports the treatment
17 of such as an intangible or nontaxable right.

18 Also, Petitioner claims inequitable treatment, violation of due process and equal protection
19 clauses, and otherwise unfair or inequitable application of relevant law compared to other state
20 assesseees but provides no evidence thereof.

21 At the hearing, the parties should be prepared to discuss the issue; further, Petitioner should be
22 prepared to explain: how Respondent specifically erred in its calculation and treatment of Petitioner's
23 remaining Wildfire Insurance Fund annual payments in Petitioner's 2024 Board-adopted unitary value;
24 why, specifically, Petitioner asserts the amortized, initial contribution, must be capitalized and
25 reflected as an annualized ordinary expense, despite *De Luz*, Property Tax Rule 8, and relevant Board
26 guidance; and what legal or appraisal principles, if any, support the allowance of past, amortized
27 expenses in a capitalized earning approach to value, as Petitioner asserts.

Staff Comment: Rev. & Tax. Code, Section 40

As noted above, this matter is subject to R&TC section 40. The Board's decision on this petition is final. (Cal. Code Regs., tit. 18, § 5345, subd. (a)(1).) Thus, within 120 days from the date of the Board's vote to decide the appeal, a written opinion (i.e., Summary Decision or Formal Opinion) must be published on the Board's website. (Cal. Code Regs., tit. 18, § 5552, subds. (b), (f).)

Following the conclusion of this hearing, if the Board votes to decide the appeal, but does not specify whether a Summary Decision or a Formal Opinion should be prepared, staff will expeditiously prepare a nonprecedential Summary Decision and submit it to the Board for consideration at a subsequent meeting. (Cal. Code Regs., tit. 18, § 5551, subd. (b)(2).) Unless the Board directs otherwise, the proposed Summary Decision would not be confidential pending its consideration by the Board (Cal. Code Regs., tit. 18 § 5551, subd. (b)(5)); accordingly, it would be posted on the Public Agenda Notice for the meeting at which the Board will consider and vote on the Summary Decision.

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