CALIFORNIA STATE BOARD OF EQUALIZATION

SUMMARY DECISION UNDER REVENUE AND TAXATION CODE SECTION 40

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

BNSF RAILWAY COMPANY (0804)

Petitioner

Appeal No.: SAU 24-024

Nonappearance Hearing Date: December 17, 2024[1]

Representing the Parties:

For the Petitioners: Peter Michaels, Attorney
Law Office of Peter Michaels

For the Respondent: Eric Boeing, Attorney III
Attorney for State-Assessed Properties Division

Michelle Cruz
Principal Property Appraiser
State-Assessed Properties Division

Appeals Attorney: Christian Younger, Attorney III

VALUES AT ISSUE

	Value	Penalty	Total
2024 Board-Adopted Unitary Value	$3,239,400,000	$0	$3,239,400,000
Petitioner's Requested Unitary Value	$3,052,092,000	$0	$3,052,092,000
Respondent's Appeal Recommendation	$3,239,400,000	$0	$3,239,400,000
Petitioner's Revised Requested Unitary Value	$3,102,324,600	$0	$3,102,324,600
Board Determined Value	$3,239,400,000	$0	$3,239,400,000

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[1] At the nonappearance hearing, the Board denied the petition by a unanimous vote of the Members participating, with Chair Lieber, Member Schaefer, Member Vazquez, and Controller Cohen voting aye.

Factual Background

BNSF Railway Company (BNSF or Petitioner) is an interstate railroad company with approximately 32,500 route miles of track in 28 states and three Canadian provinces with 3,031 miles of track in California. BNSF maintains an economic relationship with J.B. Hunt Transport Services, Inc. (JB Hunt), who provides various freight transportation services throughout the United States, Canada, and Mexico.

The 2024 Board-adopted unitary value of $3,239,400,000 for Petitioner is based on a 100 percent reliance on the Capitalized Earning Ability (CEA) value indicator. The 2024 interstate allocation factor for Petitioner is 7.74 percent.

On appeal, Petitioner contends that their 2024 Board-adopted unitary value is overstated and requests a revised unitary value of $3,052,092,000. Throughout the appeals process, Petitioner and the State-Assessed Properties Division (SAPD or Respondent) each submitted briefing, evidence, and argument throughout the appeals process to support their positions on the one issue raised in this petition. After the Appeals Conference, Petitioner revised its unitary value request to $3,102,324,600.

Legal Issue: Whether Respondent's CEA value indicator must be adjusted for Petitioner's intangible customer relationship with JB Hunt.

Findings of Fact and Related Contentions

Petitioner contends that SAPD's assessment should be adjusted to reflect the intangible, nontaxable value attributable to its customer relationship with JB Hunt. Petitioner and JB Hunt have a contractual economic relationship for the purpose of merging and streamlining freight rail transportation and freight trucking transportation to better serve customer supply chains. Petitioner contends that it generates significant revenue and profit as a result of its relationship with JB Hunt. To value the customer relationship, Petitioner hired FTI Consulting (FTI) to produce a valuation study by examining forecasted revenues, developing an attrition rate to account for potential loss of the customer relationship, identifying profit margins associated with forecasted revenues, applying contributory asset charges associated with forecasted cash flows, and deriving an appropriate discount rate.

Petitioner cites Revenue & Taxation Code (R&TC) section 110, subdivision (d), which states in part that the value of taxable property shall not include the value of intangible assets and rights. R&TC section 212, subdivision (c), further states in part that the value of intangible assets and rights shall not enhance or be reflected in the value of taxable property. Thus, Petitioner contends that its customer relationship with JB Hunt is a nontaxable, intangible asset that enhances Petitioner's value and thus must be recognized and excluded from its total value.

Petitioner further argues that its 34-year business relationship with JB Hunt is realistic and dependable and that an informed buyer would recognize the standalone value of Petitioner's customer relationship with JB Hunt. Petitioner contends that its customer relationship with JB Hunt can be isolated, quantified, and substantiated by verifiable and reliable information and data contained in the five-year average income stream. The FTI study estimates the value of the customer relationship from the five-year average CEA analysis by identifying the expected annual after-tax stabilized cash flow from the JB Hunt relationship by averaging the past five years of historical operating profits generated from the customer relationship. Then, FTI subtracted contributory asset charges for all other identifiable tangible and intangible assets. Finally, FTI applied the capitalization rate, growth rate, and risk factor to derive a customer relationship value of $1,771,000,000. After applying the Board's 7.74 percent interstate allocation factor, Petitioner contends the nontaxable, intangible customer relationship adjustment of $137,075,400 should be applied to its CEA value indicator.

Respondent contends that Petitioner has not provided sufficient evidence to identify a separate or enhanced stream of income attributable to its customer relationship with JB Hunt that is beyond what would be reasonably expected from prudent business operations. Respondent contends that the FTI study omitted the relied upon income stream; admitted Petitioner had not prepared customer relationship revenue forecasts beyond 2024, while simultaneously stating a 5.2 percent long-term growth rate, despite JB Hunt reporting declining revenues; applied a fifty-year term for its customer relationship without any contractual proof; and inappropriately utilized the "value in use"[2] methodology instead of market value to quantify its customer relationship.

Respondent cites *Elk Hills Power, LLC v. State Board of Equalization* (2013) 57 Cal.4th 593 to

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[2] The concept of use value is concerned with the value of property based on its utilization by a particular owner or group of owners. Use value is the value a specific property has for a specific use. (Assessors' Handbook section 502, *Advanced Appraisal* (1998) p. 10.)

contend that the Petitioner has failed to adequately demonstrate that the direct intangibles have created a separate stream of income or has enhanced the income stream above that which ordinarily would be reasonably expected from prudent business operations.

At the Appeals Conference on November 12, 2024, the parties generally incorporated by reference and renewed their contention as previously captured in the parties' briefings. Respondent stated it was unable to verify Petitioner's calculations due to relevant supporting information being redacted or omitted by Petitioner in its submitted petition. Without being able to verify and understand Petitioner's customer relationship calculation, Respondent stated it could not determine whether an adjustment was appropriate. On November 18, 2024, the parties met again to allow Respondent to view the data that was used in Petitioner's calculations. On November 20, 2024, Petitioner's representative provided revisions to its opinion of value, which have been reflected herein.

Applicable Law and Appraisal Principles

Burden of Proof

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

Value Standard

Section 1 of article XIII of the California Constitution states that all property must be valued at fair market value. Property Tax Rule 2, subdivision (a), states that "in addition to the meaning ascribed to them in the Revenue and Taxation Code, the words "full value", "full cash value", "cash value", "actual value" and "fair market value" mean the price at which a property, if exposed for sale in the open market with a reasonable time for the seller to find a purchaser, would transfer for cash or its equivalent under prevailing market conditions between parties who have knowledge of the uses to which the property may be put, both seeking to maximize their gains and neither being in a position to take advantage of the exigencies of the other."

Capitalized Earning Approach

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

Revenue & Taxation Code Section 212(c)

R&TC section 212, subdivision (c), states that "intangible assets and rights are exempt from taxation and, except as otherwise provided in the following sentence, the value of intangible assets and rights shall not enhance or be reflected in the value of taxable property. Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use."

Revenue & Taxation Code Sections 110(d)-(e)

R&TC section 110, subdivisions (d) and (e), state:

> (d) Except as provided in subdivision (e), for purposes of determining the "full cash value" or "fair market value" of any taxable property, all of the following shall apply:
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> > (1) The value of intangible assets and rights relating to the going concern value of a business using taxable property shall not enhance or be reflected in the value of the taxable property.
> >
> > (2) If the principle of unit valuation is used to value properties that are operated as a unit and the unit includes intangible assets and rights, then the fair market value of the taxable property contained within the unit shall be determined by removing from the value of the unit the fair market value of the intangible assets and rights contained within the unit.
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> > (3) The exclusive nature of a concession, franchise, or similar agreement, whether de jure or de facto, is an intangible asset that shall not enhance the value of taxable property, including real property.
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> (e) Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use.

*Elk Hills Power, LLC v. State Board of Equalization* (2013) 57 Cal.4th 593

In *Elk Hills*, the California Supreme Court held that if a taxpayer presents evidence that the value of intangible assets contributed in some way to the unit valuation of its taxable property, then a determination must be made to see if those intangible assets were necessary to the beneficial or productive use of the property. If they are not, then they could not have been taken into account in the valuation. Next, if the intangible assets are necessary to the beneficial or productive use of the taxable property, it must be determined whether the taxpayer has presented credible evidence that the fair market value of those assets has been improperly subsumed in the valuation. If so, the assessor is prohibited from using the value of intangible rights and assets to enhance the value of taxable property, and the fair market value of those assets must be removed. (*Elk Hills* at p.615.)

When utilizing the CEA value indicator, the Court held that not all intangible rights have a quantifiable fair market value that must be deducted. A distinction must be made between intangible assets having a direct or indirect contribution to the income stream, and it is only the value of intangibles that directly enhance the income stream that must be deducted from the CEA value indicator. (*Id.* at pp. 618-619.) Examples of intangible assets that directly enhance an income stream are goodwill, customer base, favorable franchise terms, and favorable operating contracts. (*Id.* at p. 618.)

Analysis and Disposition

Respondent is presumed to have correctly determined the value of the property at issue, and Petitioner bears the burden of proving otherwise. Here, Petitioner has a contractual, economic relationship with JB Hunt that allows for the merging and streamlining of freight rail and freight trucking transportation to better serve customer supply chains. Petitioner contends that this customer relationship is a nontaxable, intangible asset that enhances Petitioner's value and thereby must be excluded from its total value. Pursuant to *Elk Hills*, Petitioner must present credible evidence that the value of any intangible rights or assets directly enhance the income stream and have been improperly subsumed in the valuation of the taxable property. Petitioner and JB Hunt maintain a business relationship that allows for more streamlined and efficient operations for both companies, and although the relationship with JB Hunt may have enhanced Petitioner's value, Petitioner has not demonstrated a quantifiable enhancement to its income stream above that which would be ordinarily expected from prudent business operations (e.g. improper subsumption). Further, Petitioner has failed to demonstrate a direct enhancement to its income stream from the JB Hunt relationship, as opposed to any other relationship, that is above and beyond the beneficial or productive use of the taxable property. Thus, Petitioner has cited no legal or appraisal authority, nor provided any arguments or evidence that would substantiate the necessity of an intangible asset adjustment to its unitary property value. Accordingly, we find that Petitioner has not met its burden of proving Respondent erred by not including an adjustment for an intangible customer relationship with JB Hunt in Petitioner's 2024 Board-adopted unitary value.

DECISION

Accordingly, the 2024 petition for reassessment is denied, and the 2024 Board-adopted unitary value of $3,239,400,000 is affirmed. *

Sally J. Lieber____________, Chair

Antonio Vazquez_______, Member

Mike Schaefer_________, Member

Malia M. Cohen________, Controller

* The decision was rendered in Sacramento, California on December 17, 2024. This summary decision document was approved on February 19, 2025, in Sacramento, California.