STATE OF CALIFORNIA

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TO COUNTY ASSESSORS:

ASSESSMENT OF PROPERTIES
SUBJECT TO 1911, 1913, AND 1915 ASSESSMENT BONDS

The Board has provided guidance to assessors for the valuation of real property encumbered by improvement bonds in the recently revised Assessors' Handbook Section 501, Basic Appraisal. This subject is addressed at page 69 of that manual where it states:

Land Value and Improvement Bonds

General

"Local governments assist private parties in financing the development of land by participating in the formation of local special assessment districts. These districts issue improvement bonds to the general public that are used in the construction of land improvements, or infrastructure, such as roads, schools, and utility services, that generally enhance land value. To obtain improvement bond financing, land parcels benefiting from the improvements must be pledged as security for the bond debt. These liens run with the land. The bonds are typically repaid over a period of years by special levies against the parcels collected along with property taxes.

"Appraisers should be familiar with two categories of bonds: (1) improvement bonds issued under the Improvement Bond Act of 1911, the Municipal Improvement Act of 1913, or the Improvement Bond Act of 1915; and (2) improvement bonds issued under the Mello-Roos Community Facilities Act of 1982."

Bonds Under the 1911, 1913, or 1915 Acts

"The nominal sale price of a property encumbered by an outstanding 1911, 1913, or 1915 Act improvement bond is not the 'purchase price' of the property as defined in section 110(b). Since purchase price is defined as 'the total consideration provided by the purchaser or on the purchaser's behalf, valued in money, whether paid in money or otherwise,' where this type of improvement bond is present, the total consideration provided by the purchaser is in part 'paid in money' and in part 'paid otherwise.' The 'paid otherwise' consideration in the case of a property that sells subject to a 1911, 1913, or 1915 Act bond is the fair market value of the outstanding improvement bond.

"A bond, until retired, remains an encumbrance against the property. The existence of the bond may influence the sale price, and, as a result, the sale price may not reflect the property's market value. The appraiser should be aware of this when considering the sale price as an indicator of market value or when selecting comparables in areas where this type of financing is used.

"Rule 4(a) requires that the appraiser 'convert a noncash sale price to its cash equivalent by estimating the value in cash of any tangible or intangible property other than cash which the seller accepted in full or partial payment for the subject property and adding it to the cash portion of the sale price . . . .' As an application of this general requirement, the sale price of a property encumbered by a 1911, 1913, or 1915 Act bond must be adjusted to reflect the fair market value of the outstanding bond. The fair market value of the outstanding improvement bond to be added to the sale price, if any, may be determined by the following methods: (1) reference to sales of comparable properties; or (2) by discounting the bonds to a cash equivalent amount. The adjusted sale price is arrived at by adding the market value of the improvement bond to the sale price of the property. The sale price so adjusted is the 'purchase price' of the property as defined in section 110(b).

"This does not mean, however, that the adjusted sale price must be enrolled as market value in all cases. Otherwise similar properties may sell for the same sale price regardless of the existence or nonexistence of 1911, 1913, or 1915 Act bonds. If this is the case, and can be supported with market data, the appraiser may conclude that the fair market value of the subject property encumbered with a 1911, 1913, or 1915 Act bond is equal to its nominal sale price and not its adjusted sale price that includes the fair market value of the 1911, 1913, or 1915 Act bond."

Although the above language appears in Chapter 5 "Measurement of Value" and reflects the current position of the Board, there is some concern that one may conclude that an adjustment to the sale price is always proper where such unpaid bonds exist. This would not be a correct application of the Board's position.

As the title of the chapter indicates, the objective of an appraisal is to measure current market value. In other words, the job before the appraiser is to determine the appropriate assessed value of property by looking to the evidence provided by the participants in the marketplace. The comparative sales approach provides the best indicator of land value when a sufficient number of recent sales of comparable properties exist, and section 110(b) provides that the fair market value in any sale shall be the purchase price paid, unless it is established by a preponderance of the evidence that the property would not have transferred for that price in an open market transaction. Thus, if the nominal sale price does not meet the definition of "purchase price" under section 110(b), then adjustments, either downward or upward, will be required. As with any valuation utilizing this approach, all available evidence of market value needs to be examined. The final determination of whether the amount of the unpaid bonds should be added is based on whether or not the "total consideration provided by the purchaser or on the purchaser's behalf, valued in money, whether paid in money or otherwise," equates to fair market value per section 110(b).

In some cases, the appropriate value to enroll will be the nominal sale price, because the market data shows, for example, sales of comparable properties with unpaid bonds and sales of comparable properties without unpaid bonds in approximately the same range of value. In other instances, the sale price adjusted to reflect the cash equivalent value of the outstanding bond will be the appropriate value to enroll, where, for example, market evidence indicates that comparable properties were sold for a significantly higher price with the bonds retired. In either case, the final result must be fair market value.

It is also important to clarify this concept, when necessary, to homeowners purchasing newer properties in subdivisions heavily encumbered by bonds for specific improvements in that development. These new owners are frequently surprised when the value of their property for property tax purposes exceeds the sale price paid. Therefore, an explanation of the market data used to derive the adjustment may assist such homeowners in understanding that they received more, in terms of the improvements and amenities paid for by the bonds, than comparable properties in other subdivisions without such bonds. In each case, the market data should demonstrate that the fair market value of their particular properties is more than what they actually paid in the purchase price.

Hopefully, this information serves to clarify the procedures used when valuing properties encumbered by 1911, 1913, and 1915 improvement bonds, and assists in answering taxpayer inquiries concerning their expectations that the nominal sale price is the market value. If you have any questions, please contact our Technical Services Unit at (916) 445-4982.

Sincerely,

Richard C. Johnson

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Property Taxes Department

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