

**WEST VIRGINIA
SECRETARY OF STATE
KEN HECHLER
ADMINISTRATIVE LAW DIVISION**

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JUL 29 3 27 PM '98

OFFICE OF WEST VIRGINIA
SECRETARY OF STATE

Form #3

**NOTICE OF AGENCY APPROVAL OF A PROPOSED RULE
AND
FILING WITH THE LEGISLATIVE RULE-MAKING REVIEW COMMITTEE**

AGENCY: State Tax Commission TITLE NUMBER: 110

CITE AUTHORITY: W. Va. Code §§ 11-1C-5(b) & 11-6G-1

AMENDMENT TO AN EXISTING RULE: YES NO

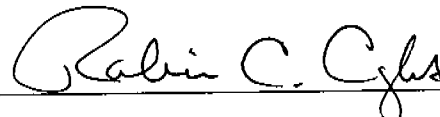
IF YES, SERIES NUMBER OF RULE BEING AMENDED: Series 1M

TITLE OF RULE BEING AMENDED: Valuation of Public Utility Property for Ad Valorem
Property Tax Purposes

IF NO, SERIES NUMBER OF RULE BEING PROPOSED: _____

TITLE OF RULE BEING PROPOSED: _____

THE ABOVE PROPOSED LEGISLATIVE RULE HAVING GONE TO A PUBLIC HEARING OR A PUBLIC COMMENT PERIOD IS HEREBY APPROVED BY THE PROMULGATING AGENCY FOR FILING WITH THE SECRETARY OF STATE AND THE LEGISLATIVE RULE-MAKING REVIEW COMMITTEE FOR THEIR REVIEW.



Robin C. Caphart, Cabinet Secretary

July 29, 1998

Date

\$12.90



**STATE OF WEST VIRGINIA
DEPARTMENT OF TAX AND REVENUE
TAX DIVISION**

CECIL H. UNDERWOOD
Governor

ROBIN C. CAPEHART
Cabinet Secretary

RICHARD E. BOYLE, JR.
State Tax Commissioner

SUMMARY OF RULE

110 C.S.R. 1M

Valuation of Public Utility Property for
Ad Valorem Property Tax Purposes

This rule describes the methodology for determining the market value of interstate public service corporation motor vehicles subject to proportional registration. Other technical amendments are also made to the rule.



STATE OF WEST VIRGINIA
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State Tax Commissioner

STATEMENT OF CIRCUMSTANCES

110 C.S.R. 1M

Valuation of Public Utility Property for
Ad Valorem Property Tax Purposes

House Bill 4713, passed on March 12, 1998 and in effect from date of passage, requires the State Tax Commissioner propose a legislative rule that describes the methodology for determining the market value of interstate public service corporation motor vehicles subject to proportional registration. That requirement is accomplished through amendment to this rule. Other technical amendments are also made to this rule.

APPENDIX B

FISCAL NOTE FOR PROPOSED RULES

Rule Title: Valuation of Public Utility Property For Ad Valorem Property Tax Purposes

Type of Rule: Legislative Interpretive Procedural

Agency: State Tax Commission
 Address: P.O. Box 1005
Charleston, WV 25324-1005

1. Effect of Proposed Rule

	ANNUAL		FISCAL YEAR		
	INCREASE	DECREASE	CURRENT	NEXT	THEREAFTER
<u>ESTIMATED TOTAL COST</u>	\$ 20,580	\$	\$20,580	\$21,960	\$23,440
PERSONAL SERVICES	15,060	0	15,060	16,120	17,260
CURRENT EXPENSE	4,520	0	4,520	4,840	5,180
REPAIRS & ALTERNATIONS	0	0	0	0	0
EQUIPMENT	1,000	0	1,000	1,000	1,000
OTHER	0	0	0	0	0

2. Explanation of above estimates:

Annual increase represents current year costs.

The estimated total cost for personal services is being increased to provide for an additional employee. The work is currently being accomplished by a temporary employee who is limited to 1,000 hours per year. The work requires a full-time employee.

Rule Title: Valuation of Public Utility Property For Ad Valorem Property Tax Purposes

3. Objectives of these rules:

The primary objective of this rule is to implement the new methodology for valuation of motor carriers as required by H.B. 4713, enacted March 12, 1998. The rule also makes technical amendments to 110 C.S.R. 1M.

4. Explanation of Overall Economic Impact of Proposed Rule.

A. Economic Impact on State Government.

The economic impact on state government should be minimal.

B. Economic Impact on Political Subdivisions; Specific Industries; Specific groups of Citizens.

Counties that have trucks that travel in interstate commerce may lose some tax revenues as the property taxes from those trucks will be distributed based on highway mileage. However, counties will gain tax revenues from the collection of taxes from interstate carriers. The overall fiscal impact is not reasonably estimated.

C. Economic Impact on Citizens/Public at Large.

See B above.

Date: _____

Signature of Agency Head or Authorized Representative

Richard E. Boyle, Jr.
State Tax Commissioner

DATE: July 28, 1998

TO: LEGISLATIVE RULE-MAKING REVIEW COMMITTEE

FROM: State Tax Commission

LEGISLATIVE RULE TITLE: Valuation of Public Utility Property for Ad Valorem
Property Tax Purposes

1. Authorizing statute(s) citation W. Va. Code §§ 11-1C-5(b) & 11-6G-1

2. a. Date filed in State Register with Notice of Public Comment Period?

June 2, 1998

b. What other notice, including advertising, did you give of the Public Comment Period?

Available on the Tax Commission Internet Site

c. Date of Public Comment Period: June 2, 1998 – July 2, 1998

d. Attach list of persons who appeared at hearing, comments received, amendments, reasons for amendments.

Attached X No comments received

e. Date you filed in State Register the agency approved proposed Legislative Rule following public comment period: (be exact)

July 28, 1998

f. Name and phone number(s) of agency person(s) to contact for additional information:

Jeff Amburgy 558-3940

John Montgomery 558-5330

3. If the statute under which you promulgated the submitted rules requires certain findings and determinations to be made as a condition precedent to their promulgation:

a. Give the date upon which you filed in the State Register a notice of the time and place of a hearing for the taking of evidence and a general description of the issues to be decided.

N/A

b. Date of hearing: _____

c. On what date did you file in the State Register the findings and determinations required together with the reasons therefor?

d. Attach findings and determinations and reasons:

Attached: _____

AGENCY APPROVED
TITLE 110
LEGISLATIVE RULE
STATE TAX COMMISSION

SERIES 1M
VALUATION OF PUBLIC UTILITY PROPERTY
FOR AD VALOREM PROPERTY TAX PURPOSES

FILED
JUL 23 3 27 PM '98
OFFICE OF THE SECRETARY OF STATE
OFFICE OF THE SECRETARY OF STATE
1998

§ 110-1M-1. General.

1.1 **Scope.** -- ~~These regulations clarify~~ This rule clarifies and implements State law as it relates to the appraisal, at market value, of property subject to taxation as public utilities; and general rules for distinguishing between operating and non-operating public utility property for ad valorem taxation purposes. ~~Because these regulations provide context modifications of relevant parts of 110 C.S.R. 1 and such regulations with context modifications were adopted by the Tax Commissioner, W. Va. Code § 11-1C-5(b) eliminates the requirement that this filing be subject to the proceeding requirements of W. Va. Code § 29A-3-1 et seq~~

1.2 **Authority.** -- W. Va. Code §§ 11-1C-5(b) and 11-6G-1.

1.3 **Filing Date.** --

1.4 **Effective Date.** --

§ 110-1M-2. Definition.

As used in ~~these regulations~~ this rule and unless the context clearly requires a different meaning, the following terms shall have the meaning ascribed herein, ~~and shall apply in the singular or in the plural.~~

2.1 **"Bands of investment technique"** means a synthesis of capital components used in financing an investment.

2.2 **"Capitalization rate"** means a rate, used to convert an estimate of income to an estimate of market value.

2.3 **"Commercial motor vehicle"** means a qualified motor vehicle registered under a proportional registration agreement, or a qualified motor vehicle that, except for the fact that it is engaged only in intrastate commerce, would otherwise be subject to registration under proportional registration agreements. "Commercial motor vehicle" status may, at the option of the party registering the vehicle, be conferred upon a non-qualified motor vehicle such as a vehicle, or a combination thereof, that have a gross vehicle weight of 26,000 pounds or less, that have only two axles, or are used in the transportation of charter parties.

2.3 4 **"Cost approach"** means the appraisal process in which cost of the property being valued is considered in determining an estimate of fair market value. As a general rule, original cost will be used to value public utility operating property; however, when such original cost is not available, replacement cost or reproduction cost may be considered.

2.5 **"Economic enhancement"** means an increase in value of a property arising from factors such as changes in use, an easing of restrictions upon the property, assemblage, or changes in supply and demand relationships.

2.4 6 **"Economic obsolescence"** means a loss in value of a property arising from factors such as changes in use, legislation that restricts or impairs property rights, or changes in supply and demand relationships.

2.5 7 **"Fair market value"** means the highest price in terms of money that a for which property will bring in a competitive and open market, assuming that the buyer and seller are acting prudently and knowledgeably, allowing sufficient time for the sale and assuming that the price is not affected by undue stimulations would sell if voluntarily offered for sale by the owner thereof, upon such terms as such property, the value of which is sought to be ascertained, is usually sold, and not the price which might be realized if such property were sold at a forced sale.

2.6 8 **"Final assessed values"** means values established by the Board of Public Works required by W. Va. Code § 11-6-11.

2.7 9 **"Functional obsolescence"** means a loss in value of a property due to changes in style, taste, or technology.

2.10 **"Gross capital cost"** means the actual cost of the new or used vehicle at the time of purchase, as illustrated on the bill of sale, purchase contract, or similar document showing the purchase price of the vehicle. The cost at the time of purchase means 100% of the cost as shown on the books and records of the purchaser and includes freight, installation charges, trade-ins, federal tax allowances and any applicable credits utilized by the purchaser at the time of purchase.

2.8 11 **"Income approach"** means the appraisal process of discounting an estimate of future benefits into an expression of present worth.

2.9 12 **"Market data approach"** means the appraisal process of examining sales data and translating such data into an estimate of present worth.

2.13 **"Operating property"** means utility operating property used for purposes immediately connected with providing the respective utility service. The Tax Commissioner construes "purposes immediately connected with providing utility service"

to be synonymous with properties considered by regulatory bodies in constructing the utility rate base for rate making purposes. The Tax Commissioner will therefore give primary consideration to whether property is included in utility operating property classification as reflected in the applicable uniform system of accounts when deciding operating non-operating property issues.

2.40 14 "**Original cost**" means the initial cost paid for constructing or acquiring property.

2.44 15 "**Physical deterioration**" means a loss in value due to wear and tear in service.

2.16 "**Proportional registration agreement**" means an agreement entered into by the West Virginia Commissioner of Motor Vehicles under the authority of West Virginia Code § 17A-2-10a.

2.42 17 "**Public service corporation**" means business entities contemplated by provisions of W. Va. Code § 11-6-1 et seq.

2.18 "**Qualified motor vehicle**" means a motor vehicle used, designed or maintained for the transportation of persons and property and:

2.18.1 Which is a self-propelled unit having a gross vehicle weight in excess of 26,000 pounds; or

2.18.2 Is a self-propelled unit having three or more axles, regardless of weight; or

2.18.3 Is used in combination with another vehicle, when the combined gross vehicle weight exceeds 26,000 pounds; or

2.18.4 the combined gross vehicle weight or combined registered gross vehicle weight of the two or more vehicles exceeds 26,000 pounds.

2.43 19 "**Rate base**" means that group of accounts or derivatives thereof, from the Uniform System of Accounts, on which a public utility is allowed a return on investment.

2.44 20 "**Regulation**" means the process wherein fees charged for public utility services are reviewed by applicable federal and state regulatory bodies oversight of public service corporations by applicable federal and state regulatory bodies.

2.15 21 **"Replacement cost"** means the cost, including material, labor, and overhead, that would be incurred in constructing an improvement having the same utility to its owner as the improvement in question, without necessarily reproducing exactly any particular characteristic of the property.

2.16 22 **"Reproduction cost"** means the cost, including material, labor, and overhead, that would be incurred in constructing an improvement having exactly the same characteristics as the improvement in question.

2.17 23 **"Return on investment"** means a margin of profit generally expressed as a percentage of investment capital.

2.18 24 **"Stock and debt technique"** means a process of reviewing market trading prices of securities in order to arrive at an estimate of value.

2.19 25 **"Tentative assessments"** means property valuation estimates furnished by the Tax Commissioner to the Board of Public Works in accordance with W. Va. Code § 11-6-9.

2.20 26 **"Uniform system of accounts"** means the most current system of accounting developed and required by state and federal regulatory bodies.

2.24 27 **"Unit rule"** means an appraisal of an integrated property as a whole without any reference to the values of its component parts.

~~2.22 **"Operating property"** means utility operating property is property used for purposes immediately connected with providing the respective utility service. The Tax Commissioner construes "purposes immediately connected with providing utility service" to be synonymous with properties considered by regulatory bodies in constructing the utility rate base for rate making purposes. The Tax Commissioner will therefore give primary consideration to whether property is included in utility operating property classification as reflected in the applicable uniform system of accounts when deciding operating non-operating property issues.~~

§ 110-1M-3. Situs.

~~3.1 Generally, when the cost approach is used, operating properties physically located in West Virginia will be considered for tax purposes; however,~~

~~3.1.1 When the income approach unit method is used, the correlated unit of value shall be allocated to the State of West Virginia using operating plant data after which;~~

3.1.2 Apportionment of ~~physical plant~~ property tax revenues, considering the location in the various taxing districts, will be made by the West Virginia State Auditor's Office.

§ 110-1M-4. Valuation of Operating Public Utility Property (excluding commercial motor vehicle property).

4.1 **Unit method.** -- The Tax Commissioner provides tentative assessments based on fair market value of operating property of public service corporations to be used as a guide by the Board of Public Works in establishing final assessed values for property tax purposes. In this regard the Tax Commissioner will use the "Unit Rule" where applicable in furnishing tentative valuation estimates for the Board's consideration.

4.2 **Generally accepted appraisal methods.** -- In determining tentative assessments the Tax Commissioner will consider, and use where applicable, three (3) generally accepted approaches to value: (A) cost, (B) income, and (C) market data. Application of these approaches will recognize the impact of regulation on the value of utility operating property where applicable.

4.2.1 **Cost approach.** -- Recognizing that many public service corporations are ~~predominantly~~ cost regulated, when the cost approach is used in the valuation process, original cost less applicable regulatory depreciation will be employed. ~~In applying the cost approach, the Tax Commissioner will consider three (3) types of depreciation: (a) physical deterioration, (b) functional obsolescence, and (c) economic obsolescence. For public service corporations no longer cost regulated, consideration may be given to using a depreciation method other than regulatory accounting.~~

4.2.2 **Income approach.** -- In developing income approach valuations, the Tax Commissioner will estimate capitalization rates considering the interrelationships of the income to be capitalized and the capitalization rate. In this regard, net operating income after taxes, but before interest expense on long-term debt, will be given primary consideration as the point on the income stream to be capitalized. The bands of investment technique will be employed in estimating appropriate capitalization rates.

4.2.3 **Market data approach.** -- Recognizing that a sufficient number of sales of public service corporations do not occur to enable application of the market data technique, the Tax Commissioner will consider the substitute stock and debt technique. The stock and debt technique will be used in instances where a utility class possesses actively traded stocks and bonds that enable reasonable valuation estimates to be made.

4.2.4 Adjustments. – In certain instances, adjustments shall be made to the appraisals. If the utility holds property under operating leases which is not being assessed in another manner, the property shall be added to the utility's appraisal. The influence of working capital will be subtracted from both the income approach and the market data approach. Consideration will be given for the subtraction from the approaches of the contribution of any other intangible property. A subtraction will only be made for intangible property having a value which is separate and distinguishable apart from the tangible property.

4.2.4 5 Correlations. – Once generated, the various estimates of value will be correlated into a final value estimate. The income approach value will generally be given primary consideration in the correlation process; however, all factors and conditions pertinent to each approach shall be considered and exceptions will be made for cause. Any functional obsolescence, economic obsolescence or economic enhancement will be recognized through the correlation process.

4.3 Classification of public utility and certain common carrier operating properties.

4.3.1 Electric utilities. -- Operating property for electric utilities shall primarily include such properties as are considered by the Federal Energy Regulatory Commission (FERC) as part of the rate base for rate making purposes. In determining which properties are properly included as operating public utility property, the most recent FERC Uniform System of Accounts prescribed for Electric Utilities shall be used.

4.3.2 Gas utilities. -- Operating property for natural gas utilities shall primarily include such properties as are considered by the Federal Energy Regulatory Commission (FERC) as part of the rate base for rate making purposes. In determining which properties are properly included as operating public utility property, the most recent FERC Uniform System of Accounts prescribed for Natural Gas Utilities shall be used.

4.3.3 Gas pipeline utilities. -- Operating property for natural gas utilities shall primarily include such properties as are considered by the Federal Energy Regulatory Commission (FERC) as part of the rate base for rate making purposes. In determining which properties are properly included as operating public utility property, the most recent FERC Uniform System of Accounts prescribed for Gas Pipeline Utilities shall be used.

4.3.4 Telephone companies. -- Operating property for telephone carriers shall primarily include such properties as are considered by the Federal Communications Commission (FCC) as part of the rate base for rate making purposes. In determining

which properties are properly included as operating public utility property, the most recent FCC Uniform System of Accounts prescribed for Telephone Utilities shall be used.

4.3.5 Telegraph carriers. -- Operating property for telegraph carriers shall primarily include such properties as are considered by the Federal Communications Commission (FCC) as part of the rate base for rate making purposes. In determining which properties are properly included as operating public utility property, the most recent FCC Uniform System of Accounts prescribed for Wire-Telegraph and Ocean-Cable Carriers shall be used.

4.3.6 Airline companies. -- Operating property for air carriers shall primarily include such properties as are considered as operating property by the ~~Civil Aeronautics Board (CAB)~~ Department of Transportation. In determining which properties are properly included as operating property, the most recent ~~CAB~~ Uniform System of Accounts and Reports for Certified Air Carriers shall be used.

~~4.3.7 Interstate motor carriers.~~ -- ~~Operating property for interstate motor carriers shall primarily include such properties as are considered as operating property by the Interstate Commerce Commission (ICC). In determining which properties are properly included as operating property, the most recent ICC Uniform System of Accounts for Common and Contract Motor Carriers of Passengers, and the most recent ICC Uniform System of Accounts for Class I and Class II Motor Carriers of Property shall be used.~~

4.3.8 I Interstate railroads. -- Operating property for interstate railroads shall primarily include such properties as are considered as operating property by the ~~Interstate Commerce Commission (ICC)~~ Surface Transportation Board. In determining which properties are properly included as operating property, the most recent ICC Uniform System of Accounts for Railroad Companies shall be used.

4.3.9~~8~~ Intrastate railroads. -- Operating property for intrastate railroads shall primarily include such properties as are considered by the West Virginia Public Service Commission as operating property. In determining which properties are properly included as operating property, the most recent Uniform System of Accounts for Railroad Companies as prescribed by the ~~Interstate Commerce Commission~~ Surface Transportation Board shall be used.

~~4.3.10 Intrastate motor carriers.~~ -- ~~Operating property for motor carriers shall primarily include such properties as are considered as operating property by the West Virginia Public Service Commission. In determining which properties are properly included as operating property, motor carriers shall use the most recent Uniform System of Accounts for Common and Contract Motor Carriers adopted by the PSC.~~

4.3.419 **Water utilities.** -- Operating property for water utilities shall primarily include such properties as are considered by the Public Service Commission as part of the rate base for rate making purposes. In determining which properties are properly included as operating public utility property, water utilities shall use the most recent Uniform System of Accounts of the National Association of Regulatory Utility Commissioners for Class A and B, and Class C and D water utilities.

4.3.4210 **Sewer utilities.** -- Operating property for sewer utilities shall primarily include such properties as are considered by the Public Service Commission as part of the rate base for rate making purposes. In determining which properties are properly included as operating public utility property, sewer utilities shall use the most recent Uniform System of Accounts of the National Association of Regulatory Utility Commissioners for Class A and B, and Class C and D sewer utilities.

4.3.4311 **Carline companies.** -- Operating property for carline companies shall include consideration of Rolling Stock used in transportation of freight or passengers.

4.3.4412 **Reorganization of regulatory bodies.** -- In the event that there should be a reorganization of federal or state regulatory bodies, and any of the above public service corporations would be required to report to an agency other than that listed above or in the event that there should be any other utilities deemed taxable by the Board of Public Works; operating property for such public service corporations shall include such properties as would be considered as operating by the appropriate state or federal regulatory body in the prescribed Uniform System of Accounts.

4.3.13 **Underground gas storage companies.** -- For public service corporations with underground gas storage and no other West Virginia property, operating property shall consist of only the gas stored underground.

4.3.45.14 **Exceptions.** -- Circumstances may arise where properties may be considered operating by the appropriate regulatory body but a portion of the property may be devoted to non-utility use. The Tax Commissioner may in these instances where deemed appropriate classify a portion of the property as non-operating and require that the non-operating portion so determined be assessed by the county assessor. In these instances adjustment to the public utility appraisal will be made to remove from the West Virginia unit values a proportionate value for such non-operating property.

§ 110-1M-5. Valuation of Commercial Motor Vehicles.

5.1 Classification of motor carrier operating property.

5.1.1 West Virginia based motor carrier – Operating property shall include every trailer, semi-trailer or power unit as a commercial motor vehicle used exclusively in this State or a trailer or semi-trailer of a West Virginia based interstate commercial motor vehicle business.

5.1.2 Interstate motor carrier – Operating property shall include each power unit used as a interstate commercial motor vehicle registered under a proportional registration agreement.

5.2 Appraisal method. – A cost approach shall be used to determine the appraised value of a commercial motor vehicle. The gross capital cost of the commercial motor vehicle shall be multiplied by a percentage factor representing the remainder of the vehicle's value after depreciation. Separate depreciation schedules shall be developed annually for power units and trailers.

5.2.1 West Virginia based carriers.

5.2.1.1 West Virginia based intrastate motor carriers – The Tax Commissioner shall annually provide tentative assessments of the power units, trailers and semi-trailers owned by West Virginia based intrastate motor carriers to be used as a guide by the Board of Public Works in establishing final assessed values for property tax purposes. On or before September fifteenth, the Tax Commissioner shall issue tentative assessments to each such carrier for its operating property.

5.2.1.2 West Virginia based interstate motor carriers – The Tax Commissioner shall annually provide tentative assessments of the trailers and semi-trailers owned by West Virginia based interstate motor carriers to be used as a guide by the Board of Public Works in establishing final assessed values for property tax purposes. On or before September fifteenth, the Tax Commissioner shall issue tentative assessments to each such carrier for its operating property.

5.2.2 Interstate motor carriers. The Tax Commissioner shall annually provide the depreciation schedule for power units to the West Virginia Commissioner of Motor Vehicles for use in assessing power units subject to proportional registration agreements. The property assessment and tax collection upon interstate power units will occur at the time of registration through the International Registration Plan.

5.3 Interstate Motor Carrier Apportionment Factor – For each interstate truck, road tractor and power unit registered under a proportional registration agreement, the appraised value, as determined under Subsection 5.1 of this rule, shall be multiplied by an apportionment factor the numerator of which represents the total fleet miles driven in the

most recent taxable year in West Virginia and the denominator of which represents the total fleet miles driven in the most recent taxable year everywhere; the mileage amounts shall be the mileage amounts as reported to the West Virginia Division of Motor Vehicles.

§ 110-1M-5 6. Taxpayer Returns For All Public Utility Property Except Commercial Motor Vehicles.

~~5-4~~ 6.1 The Tax Commissioner shall print taxpayer return forms. Such forms shall be distributed to taxpayers for completion and return.

~~5-2~~ 6.2 To assure equality and uniformity in administration, no assessor or taxpayer shall substitute or supplement any other form for the Tax Commissioner's prescribed returns, without the prior approval of the Tax Commissioner. All such approvals granted by the Tax Commissioner prior to the effective date of this rule is hereby withdrawn.

~~5-3~~ 6.3 All taxpayers shall prepare one (1) copy of the appropriate property tax return and file it with the Tax Commissioner.

~~5-4~~ 6.4 Public utility and common carrier property tax returns shall be filed no later than May 1st of each year.

~~5-5~~ The Tax Commissioner, for good cause shown, may grant an extension of filing deadlines.

§ 110-1M-7. Severability.

7.1 If any provision of this rule or the application of this rule to any person or circumstances is for any reason held to be invalid, the remainder of the rule and the application of the provisions to other persons or circumstances shall not be affected by the holding.



Kenneth G. Zenus
Tax Manager
Southern Region

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RECEIVED

JUL 01 1998

LEGAL DIVISION

June 29, 1998

The Honorable Richard E. Boyle, Jr.
State Tax Commissioner
c /o Legal Division, State Tax Commission
P.O. Box 1005
Charleston, WV 25324-1005

Re: Proposed Legislative Rule Title 110, Series 1M, Valuation of Public
Utility Property for Ad Valorem Property Tax Purposes

Dear Commissioner Boyle:

This letter is in response to the West Virginia State Tax Commission's June 2, 1998, filing of proposed legislative rule changes to Title 110, Series 1M, entitled "Valuation of Public Utility Property for Ad Valorem Property Tax Purposes".

AT&T Interstate Division and AT&T Communications of West Virginia, filing under the name of AT&T Communications, are subject to the valuation rules indicated in Title 110, Series 1M.

West Virginia H.B. 4713 (passed March 12, 1998) proposed a legislative rule that describes the methodology to be used in determining the market value of certain types of motor vehicles subject to proportional registration. Accompanying the proposed rules for motor vehicles, were rule changes inducted as "technical" amendments or "other technical" amendments to the current rules cover all companies classified as "utilities".

AT&T objects to the proposed rule changes and requests that public hearings be conducted regarding the proposed rule changes.

The proposed rule changes will have a substantial affect on AT&T Communications. Although the rule changes may appear to be “cosmetic/clean-up” changes, they are not. They establish new policies in valuing public utility property, with no consideration for the deregulation, which has occurred in the telecommunications industry.

The proposed changes do not consider the West Virginia Supreme Court’s ruling in the “Ohio Cellular” case. Nowhere, in the proposed rule changes, is it indicated that the state is to tax only “tangible” property. The rules continue to require that the unitary method be used in valuing utility companies. The unit method requires the development of a cost approach, an income approach and a stock & debt approach. The income and stock & debt approaches contain intangibles. The rules should be changed eliminating the use of the unit and replacing it with reproduction cost new less depreciation. If the unit method remains in effect, the rules must be changed explaining how intangibles will be removed from the income and stock & debt approaches.

The proposed rule changes will not be in accordance with nationally recognized valuation principles. For example, by deleting the words “functional obsolescence and economic obsolescence” it appears that no form of obsolescence will be considered in the cost approach.

The proposed rule changes goes on to indicate that “... functional obsolescence, economic obsolescence and economic enhancement will be recognized through the correlation process”. This is inappropriate, consideration of these factors should be applied directly to the cost approach. In addition, economic enhancement is not defined and the purpose of including it is not presented.

In addition, the proposed rules could be misleading unless they are compared to the existing rules. Section 4.2.4 is not identified as new language and only by comparing it to the current rules can it be determined that it has been added.

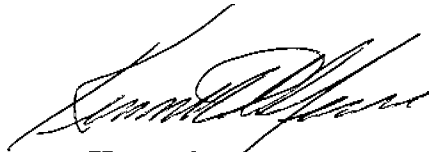
It is believed that West Virginia statutes requires that the proposed changes be clearly and separately stated before seeking public comment. Without indicating the purposes of the rule changes, companies are left to questions the motives for the changes.

Because of the above and other objections, AT&T recommends a public hearing be conducted regarding the proposed rule changes.

In addition, it is requested that AT&T Communications be notified directly, at the address indicated above, of any further actions concerning these rule changes.

If you have any further questions or require any additional information, please let me know.

Sincerely,



Kenneth G. Zenus

FAXED
1-6-98

RECEIVED

JUL 02 1998

LEGAL DIVISION

Before the

**WEST VIRGINIA STATE TAX COMMISSION
PROPERTY TAX DIVISION**

July 1, 1998

Comments of

**TRUCK RENTING AND LEASING
ASSOCIATION, INC.**

in the matter of

**VALUATION OF PUBLIC UTILITY PROPERTY FOR AD
VALOREM PROPERTY TAX PURPOSES**

Arthur Wolpert,
Chairman
President
AMI Leasing, Inc.
Worcester, MA

J. Michael Payne,
President & CEO
Truck Renting and
Leasing Association
Alexandria, VA

Frank E. Walter,
President
V.P. & General Manager
PacLease of Indiana
Indianapolis, IN

Thomas J. Fleming,
Secretary
President
Aim NationalLease
Girard, OH

Gary Alvord,
Treasurer
President
Ruan Transportation
Management Systems
Des Moines, IA

Robert L. Hunter
*Immediate Past
Chairman*
President
Hunter Idealease
Eau Claire, PA



July 1, 1998

Legal Division
State Tax Commission
P.O. Box 105
Charleston, WV 25324-1005

Re: 1998 Proposed Valuation of Public Utility Property for Ad Valorem Property Tax Purposes

Dear Sir or Madam:

The Truck Renting and Leasing Association (TRALA) is a national trade association serving the U.S. truck renting and leasing industry. TRALA represents over 650 member companies engaged in full-service truck leasing and short-term commercial and consumer truck rental. Collectively, our members are responsible for over 40% of all new truck registrations for medium and heavy-duty commercial trucks. TRALA is providing comments to the West Virginia State Tax Commission, Legal Division, concerning the 1998 Proposed Valuation of Public Utility Property for Ad Valorem Property Tax Purposes.

TRALA's Concerns with the 1998 Proposed Valuation of Public Utility Property for Ad Valorem Property Tax Purposes

TRALA would like to note a technical correction that needs to be made in the language of the proposed regulation. In section 4.3.7, *Interstate Motor Carriers*, the Interstate Commerce Commission (ICC) is referenced. The ICC was dissolved by the federal government in 1995 with the passage of the ICC Termination Act. The provision should make reference to the United States Department of Transportation, which has assumed responsibility for interstate motor carrier issues.

TRUCK RENTING AND LEASING ASSOCIATION

1725 Duke Street ☐ Suite 600 ☐ Alexandria, VA 22314-3457 ☐ Phone (703) 299-9120 ☐ Fax (703) 299-9115

State Tax Commission

July 1, 1998

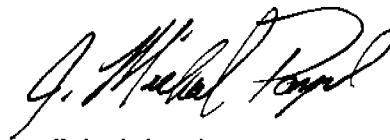
Page 2

The second comment addresses section 5.3, *Interstate Motor Carrier Apportionment Factor*. A technical correction is needed because the language that reads "*the numerator of which represents the total miles*" should read "*the numerator of which represents the total **fleet** miles.*"

In addition, TRALA urges the tax commission to include language in this section which clarifies that the property tax, as it pertains to interstate carriers, is remittable through the International Registration Plan (IRP). No reference to the IRP is included in the proposed regulations. It would be a tremendous administrative burden to TRALA members and their lessors if out of state carriers were required to make filings directly through the state Department of Revenue and not the IRP.

Thank you for your consideration.

Very truly yours,

A handwritten signature in black ink, appearing to read "J. Michael Payne". The signature is written in a cursive, flowing style.

J. Michael Payne
President & CEO



903 East 104th Street
Kansas City, MO 64114-0490

July 1, 1998

Legal Division
State Tax Commission
P.O. Box 1005
Charleston, WV 25324-1005

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JUL 02 1998

LEGAL DIVISION

Re: Comments of Sprint Communications Company, L.P.
Rule Title 110, Series 1M
Valuation of Public Utility Property for Ad Valorem Property Tax Purposes
W. Va. Code §§ 11-1C-5(b) & 11-6G-1

To whom it may concern:

Sprint Communications Company, L.P. (hereinafter referred to as "Sprint") hereby provides its comments regarding the above-referenced proposed rule filed by the West Virginia, Department of Tax and Revenue, State Tax Commission (hereinafter referred to as the "Department") on June 2, 1998.

Comments

The Statement of Circumstances, Summary of Rule, and Objectives attached to the request for comments indicate that, in addition to the stated purpose, "other technical amendments" are made to the rule.

Sprint objects to the inclusion of these "other technical amendments" without first, providing a description of the circumstances surrounding the need for, summarizing, and identifying the objective of each "other technical amendment." Many of these "technical amendments" establish new state policy or reverse long-standing, well-settled policy for valuing public utility property. Amendments of this nature require a clear and separate statement regarding the objective of each change before seeking public comment. See W. Va. Code § 29A-3-5 and -4(b).

Additionally, the Department's edited version of the amended statute is incomplete. For example, Section 4.2.4, which is new language, is not underscored in the proposed rule attached with the request for comments. Failure to identify all amendments to the statute is misleading.

Sprint hereby requests that the State Tax Commission redraft and resubmit the proposed rule by including a description of the circumstances surrounding the need for, a

summary, and an identification of the objective of each "technical amendment." Moreover, Sprint requests that the Department resubmit an edited version of the statute specifically identifying all proposed amendments.

Concerns regarding Specific Provisions

Section 2.19. What is the purpose of changing the definition of "Regulation"? The amended definition is much broader than the current version.

Section 4.2.1. What is the purpose of replacing "applicable depreciation" with "regulatory depreciation"? What is the purpose of removing the second sentence? The cost approach should consider all types of obsolescence.

Section 4.2.2. What is the purpose of replacing "long term debt" with "expense"?

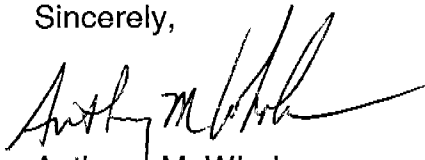
Section 4.2.4. What is the purpose of this addition? Leased property is taxed by the lessor, adding leased property to the tax base of the lessee results in double taxation. Additionally, allowing a subtraction for only "intangible property having a value which is separate and distinguishable apart from the tangible property" seems to be contrary to recent West Virginia Court decisions.

Section 4.2.5. Handling obsolescence in the correlation process is not generally accepted appraisal methodology. If obsolescence is handled in the correlation process, how would the obsolescence calculation be documented?

Summary

Sprint appreciates the opportunity to provide comments on the proposed rule and respectfully requests that the Department consider Sprint's request for resubmission of the proposed rule including a complete edited version of the statute. Sprint also requests that the Department comment on each of the specific concerns raised by Sprint above.

Sincerely,



Anthony M. Whalen
State Tax Counsel
(816) 854-5184

Cc: Mike Heaton

JACKSON & KELLY

ATTORNEYS AT LAW

1600 LAIDLEY TOWER

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July 2, 1998

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than 100 independent law firms*

RECEIVED

JUL 02 1998

LEGAL DIVISION

RECEIVED
JUL - 2 1998

VIA HAND DELIVERY

State Tax Commissioner

The Honorable Richard E. Boyle, Jr.
State Tax Commissioner
c/o Legal Division, State Tax Commission
State Capitol
Charleston, West Virginia 25305

Re: Comments of Monongahela Power Company, West Penn
Power Company and The Potomac Edison Company
Regarding Proposed Legislative Rule, Title 110, Series
1M

Dear Commissioner Boyle:

On June 2, 1998, the West Virginia Department of Tax and Revenue ("Tax Department") filed a proposed legislative rule to amend the existing legislative rule, Title 110, Series 1M, respecting the valuation of public utility property for property taxation purposes. For purposes of these comments, the existing rule, is referred to as the "Current Rule" and the June 2, 1998 filing as the "Proposed Rule."

Monongahela Power Company, West Penn Power Company and The Potomac Edison Company are public utilities operating in West Virginia, and are referred to in this letter collectively as "Allegheny Power."

GENERAL COMMENTS

1. Allegheny Power requests that the Tax Department conduct a public hearing concerning the Proposed Rule.

2. The objectives of several of the Proposed Rule changes are not clearly stated as required by law. In addition to changes proposed pursuant to the requirements of H. B. 4713, the Proposed Rule purports to make certain "technical amendments." Many are not merely technical but substantive in nature. Such changes to existing legislative rules must not be made or even submitted for public comment unless the Tax Department has first clearly and separately stated the objectives of the proposed changes. W.Va. Code § 29A-3-5 and -4(b).

3. The Proposed Rule fails to identify Section 4.2.4 as new language. Consequently, this proposed change is not properly presented for public comment.

4. The scope of many of the proposed changes is overbroad. According to H. B. 4713, the Proposed Rule is supposed to deal with the valuation of interstate public service corporation motor vehicles subject to proportionate registration. The Proposed Rule should concern itself with public service corporation motor vehicles only. Yet, as discussed in greater detail below, several proposed changes (e.g., new Section 4.2.1 and new 4.2.5) have implications for the valuation of all public service corporation property.

5. Deregulation of traditional public service corporations has and will significantly alter the meaning of the term "public service corporation." As a result of deregulation, some companies or portions of companies once regulated as utilities and therefore subject to valuation for property taxation purposes by the Board of Public Works will become deregulated and no longer subject to valuation by that body. These changes must eventually be addressed by both the Tax Department and the West Virginia Legislature. Particularly in light of the ongoing deregulation process, Allegheny Power submits that at this time the Tax Department should not promulgate rules which exceed the narrow scope outlined by H. B. 4713.

COMMENTS ON SPECIFIC PROPOSED CHANGES

6. Section 2.3. An apparent typo: The fourth word in the sixth line of this Section, "vehicles," should apparently be changed to "vehicle."

7. Sections 2.12 and 2.16. No changes to these terms, "operating property" and "public service corporation," are suggested at this time; but, as discussed above, the

process of deregulation is changing the scope and meaning of these concepts significantly. Under deregulation, property subject to valuation under the aegis of the Board of Public Works will necessarily decline. In the near future, Allegheny Power respectfully submits that the Tax Department should consider the changes which deregulation necessitates thoroughly and propose appropriate legislative rule changes for public comment in a separate filing.

8. Section 110-1M-4. The title of this Section, "Valuation of Operating Public Utility Property," has been modified to make clear that it does not apply to commercial motor vehicle property. That property, which was what H. B. 4713 directed the Tax Department to address, is now the subject of an entirely new Section 110-1M-5, entitled "Valuation of Commercial Vehicles." Thus, all changes to Section 110-1M-4 go to the valuation of various types of utility property other than motor vehicles. As previously discussed, Allegheny Power respectfully submits that the Tax Department should not be proposing such changes at this time.

9. Sections 4.2.1 and 4.2.5. These Sections are fundamentally changed by the proposed new language. Allegheny Power opposes the suggested changes. First, Section 4.2.1 of the Current Rule correctly states that the cost approach to valuation considers all three types of depreciation. The proposed changes -- contrary to sound and standard market valuation practice -- would require that functional obsolescence and economic obsolescence be considered only in the post-valuation process of correlation. Allegheny Power submits that the proposed changes should not be made and that the Tax Department must apply all three methods of depreciation in conducting cost-based valuations.

10. Section 4.2.2. The Proposed rule would alter the method for determining the capitalization rate under the income approach for valuing operating utility property by substituting the term "expense" for "long term debt." The purpose of the change is specifically to increase the income based valuation of utility property. There is no finding that the method of calculating income under the Current Rule is incorrect. Therefore, until such a finding is made Section 4.2.2 should not be changed.

11. Section 4.2.4. As noted above, this change from the Current Rule should have been identified in the Proposed Rule by underlining, but was not. Moreover, the objective of the proposed change is unstated and unclear. This is not a technical change and thus cannot be made (or submitted for public comment) without a clear and separate explanation of its objectives.

In addition, the Proposed Rule provides no standards for the various "adjustments" to be made "prior to correlation." Guidance as to when such adjustments may be appropriate should be spelled out in the Proposed Rule. The proposed addition of operating leases under all three methods of valuation is not justified and could cause double taxation of the same property. Moreover, the Proposed Rule (if promulgated at all) should unambiguously state that the value of intangible property will be subtracted from the Tax Department's valuation of utility operating property, not merely that "consideration will be given" to such an adjustment. Finally, the last sentence of the Proposed Rule inappropriately and without sufficient standards places the burden on the taxpayer to avoid valuation by the Tax Department that would include the value of the intangible property. The Proposed rule should include clear, fair standards to insure valuations of utility property that do not include the value of utility intangible property.

12. Section 110-1M-6. The Proposed Rule, for no apparent reason, would eliminate Current Rule 5.5, which merely provides that, for good cause the Tax Commissioner may grant an extension for the filing of the utility property tax return. This flexibility need not and should not be eliminated, and should be restored as Proposed Rule 6.6.

CONCLUSION

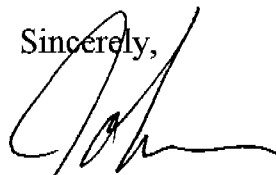
In summary, Allegheny Power respectfully urges the Tax Department to defer making any "technical amendments" at this time, but rather to limit changes to those dealing with valuation of utility motor vehicles, which was the sole and specific charge of H. B. 4713. The "technical amendments" are, for the most part, not clean-up but substantive changes which require explanation before being submitted for public comment. Moreover, on-going restructuring and deregulation of what have historically been viewed as public utilities make this an inappropriate juncture for proposing unexplained, piecemeal changes to the Rules for valuing utility operating property.

Allegheny Power appreciates the opportunity to submit these comments. Allegheny Power recognizes the substantial and varied demands on the Tax Department, and offers these comments as constructive input. If you have any questions about these

Hon. Richard E. Boyle, Jr.
July 2, 1998
Page 5

comments, or if we may provide any further information which might assist the Tax Department, please contact us.

Sincerely,

A handwritten signature in black ink, appearing to be 'John A. Mairs', written over the word 'Sincerely,'.

John A. Mairs

JAM/mb/CHASFS3:125204
cc: Wayne S. Wilson

July 2, 1998

Legal Division
State Tax Commission
P.O. Box 1005
Charleston, WV 25325-1005**RECEIVED**
JUL 06 1998
LEGAL DIVISION**Re: Comments on Proposed Changes to 110 C.S.R. 1M**

Gentlemen:

This letter is written for the purpose of submitting comments to the proposed rule changes on behalf of CSX Transportation, Inc. (CSXT). CSXT is a Class I Railroad doing business in West Virginia and is subject to assessment by the West Virginia Board of Public Works.

CSXT is particularly concerned with the changes proposed for ¶ 4.2.1 and old ¶ 4.2.4, now new ¶ 4.2.5, which deal with the cost approach and the correlation process respectively. The proposed rule eliminates the following language from the rule: "In applying the cost approach, the Tax Commissioner will consider three (3) types of depreciation: (a) physical deterioration, (b) functional obsolescence, and economic obsolescence. The last four lines of proposed ¶ 4.2.5 are new. The last sentence causes the most concern. The sentence reads, "Any functional obsolescence, economic obsolescence or economic enhancement will be recognized through the correlation process." These forms of depreciation, if present in the property, must be taken into account in the cost approach, not the correlation process. Functional and economic obsolescence are defined elsewhere in the proposed rule very similarly to the definitions contained in the IAAO's textbook (*Property Assessment Valuation*, 2nd ed., 1996). In the current rules there is a clear recognition that these two forms of obsolescence must be considered in the cost approach for the valuation of public utility property. However, the proposed rule indicates that they will not be considered in the cost approach, but will be "recognized" in the correlation process.

Correlation is the process of resolving the differences among various value indications after those indicators have been completed. The 1995 syllabus for the basic course on public utility valuation presented by the Wichita State University Workshop on Railroad and Utility Valuation contains a paper on reconciliation, or correlation, that was prepared by Jeff A. Amburgey, who is principally responsible for public utility valuations in West Virginia. In the last paragraph of that paper, Mr. Amburgey states,

"In conclusion, every unit appraisal should consider the three generally accepted approaches to value. The approaches should be reviewed to assure that no inconsistent or inappropriate assumptions have been applied. Once the indices of value have been finalized, the appraiser must reconcile the results of the approaches into a final value estimate." (emphasis added)

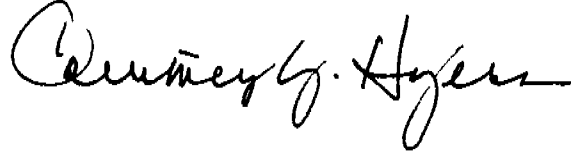
Under the rule as proposed, the appraiser would have a cost approach which had not been finalized since the appraiser would have failed to consider all forms of depreciation.

Leaving functional and economic obsolescence unaddressed in the cost approach violates sound appraisal principals and limits the taxpayer's ability to know whether, and to what extent, obsolescence has been addressed in the appraisal. Properly completing each value indicator is especially important in West Virginia where the computer model used in appraising most utilities actually weights the indicators in the correlation process according to the dollar relationship of the indicators. While the appraiser can override this feature of the appraisal model, the correlation process is particularly inappropriate in West Virginia to attempt to correct omissions in individual indicators. CSXT urges that the language referring to functional and economic obsolescence be restored to ¶ 4.2.1, and that the last sentence in new ¶ 4.2.5 be eliminated.

The elimination of the last sentence of new ¶ 4.2.5 would also avoid another potential area of confusion. Beginning with the 1998 tax year, there will be a phase-out of the assessment and taxation of all intangibles in West Virginia. The last sentence of new ¶ 4.2.5 refers to "economic enhancement". "Economic enhancement" is a practice that some utility appraisers have where they actually increase the value determined under the cost approach to reflect the fact that the assets have significant earnings. While this practice is questionable, at best, it is beyond doubt that any "economic enhancement" represents intangible value. Under the circumstances that presently exist in West Virginia, with the taxation of intangibles being phased-out, a reference to these intangible values in this rule will be confusing.

We appreciate the opportunity to respond to these proposed rule changes and would be happy to answer any questions that you might have.

Very truly yours,

A handwritten signature in black ink, appearing to read "Ramsey G. Hyers". The signature is written in a cursive style with a long horizontal flourish at the end.

GEORGE & LORENSEN P.L.L.C.

ATTORNEYS AT LAW ▲ PROFESSIONAL LIMITED LIABILITY COMPANY

SHAWN P. GEORGE
CHARLES O. LORENSEN

1526 KANAWHA BOULEVARD, EAST
CHARLESTON, WEST VIRGINIA 25311

TELEPHONE (304) 343-5555
FACSIMILE (304) 342-2513

July 2, 1998

VIA U.S. MAIL AND HAND DELIVERY
The Honorable Richard E. Boyle, Jr.
State Tax Commissioner
c/o Legal Division, State Tax Commission
P.O. Box 1005
Charleston, WV 25324-1005

RECEIVED

JUL 06 1998

LEGAL DIVISION

RE: Comments of American Electric Power Regarding Proposed Legislative Rule Title 110, Series 1M, Valuation of Public Utility Property for Ad Valorem Property Tax Purposes

Dear Commissioner Boyle:

On June 2, 1998, the West Virginia Department of Tax and Revenue, State Tax Commission ("Department"), filed a proposed legislative rule which constitutes an amendment to an existing legislative rule, both of which are cited as Title 110, Series 1M, entitled *Valuation of Public Utility Property for Ad Valorem Property Tax Purposes*. For purposes of this letter, the existing rule, filed effective July 26, 1991, will be referred to as the "Current Rule" and the June 2, 1998 filing will be referred to as the "Proposed Rule."

Appalachian Power Company, Ohio Power Company, Wheeling Power Company, Indiana Michigan Power Company, and AEP Communication LLC are affiliated corporations that are currently subject to the "public utility" property tax regime found in W.Va. Code §§ 11-6-1 *et seq.* These affiliated corporations do business as "American Electric Power" (and are collectively referred to herein as "AEP"). The Proposed Rule directly affects AEP, and AEP offers the following comments.

I. General Comments

The Summary, Objectives and Statement of Circumstances filed along with the Proposed Rule correctly indicate that the Tax Commissioner is required by H. B. 4713 (passed March 12, 1998) to propose a legislative rule that describes the methodology for determining market value of certain motor vehicles subject to proportional registration. However, the statements accompanying the Proposed Rule indicate that Proposed Rule "also makes *technical* amendments" or "*other technical* amendments" to the Current Rule without any further description, explanation or rationale.

AEP objects to the Department's characterization of changes made in the Proposed Rule with no relationship to the objectives to H. B. 4713; many of these so called "technical

Hon. Richard E. Boyle, Jr.
July 2, 1998
Page 2

amendments” are not merely stylistic or “clean-up” changes. They establish new—and in some cases inappropriate—policies of the State in valuing operating public utility property, reversing the Current Rule and prior rule filings that have set forth legislatively endorsed policies for decades. These policies should not be reversed under the guise of *technical amendments*. Relevant changes since the Current Rule’s promulgation, including deregulation trends in³ the telecommunications, gas and electric industries and the *Ohio Cellular* case, must be addressed by the Department. However, the so-called *technical amendments* reverse other, well-settled, policies without intervening changes.

The Department is required to “clearly and separately state” the objective of the changes before seeking public comment. W.Va. Code § 29A-3-5 and -4(b). We recommend that the Department comply with W.Va. Code § 29A-3-5 and -4(b) and refile the Proposed Rule for comment, separately stating the objectives of each and every so-called *technical amendment* and providing authority therefor. Without timely compliance with this legislative requirement, the public is left to speculate about the Department’s objectives and justification in several instances. We further recommend that the Department conduct a public hearing regarding the Proposed Rule.

Additionally, the Proposed Rule fails to identify (by underlining and strike-throughs) all the relevant changes from the Current Rule. The Proposed Rule as filed fails to identify Section 4.2.4 as being new language, even though Section 4.2.4 is not found in the Current Rule. This failure could mislead a reader into believing that Section 4.2.4 (which is presumably part of the “other technical amendments”) is not a change from current language unless the reader disregards the underlining and strike-throughs and compares the Proposed Rule side-by-side with the Current Rule. We recommend that this correction be made to comply with W.Va. Code § 29A-3-11(a)(1).

II. Specific Comments

Section 4.2.1. The Proposed Rule’s deletion of the second sentence of Section 4.2.1 in the Current Rule is inappropriate and constitutes a fundamental change. Under the Proposed Rule, functional obsolescence and economic obsolescence would presumably not be considered under the cost approach to value. This is not a generally accepted appraisal approach. The Current Rule correctly requires the consideration of functional obsolescence and economic obsolescence in the cost approach whereby the Proposed Rule eliminates these considerations. The Current Rule language in this regard should be retained and the Department should consistently adhere to the Current Rule’s policy in setting tentative assessments.

Section 4.2.2. The Proposed Rule, without any stated justification, strikes the phrase “long-term debt” and substitutes the term “expense” in the second sentence of Section 4.2.2. One might assume that this could be a subtle attempt to allow the Department, in setting tentative assessments,

Hon. Richard E. Boyle, Jr.
July 2, 1998
Page 3

to justify including short-term debt in determining capitalization rates. This would be inappropriate (and would artificially increase property values derived under the income approach). Short-term debt is predominantly used to finance working capital and not the investment in long-lived assets. AEP would not object to the addition of the term "expense" after the phrase "long-term debt" but objects to the deletion of the phrase "long-term debt."

Section 4.2.4. The Proposed Rule's new Section 4.2.4 (and this should be shown by underlining as stated above) authorizes certain "adjustments" without providing any standards and attempts to place inappropriate burdens upon taxpayers. First, the Proposed Rule makes reference to adjustments to (a) *add* property held under operating leases to the three approaches and (b) *subtract* the influence of working capital from the income approach and market data approach. The addition of "operating lease" property is unjustified and will result in double taxation of the same property. Moreover, without standards, the Proposed Rule is incomplete and ambiguous respecting both of these adjustments.

Second, the fourth and fifth sentences in Section 4.2.4 (both concerning *intangible property*) inadequately deal with the *Ohio Cellular* decision. The Department is statutorily required to appraise taxable operating public utility property. Through this filing, the Department appears to require taxpayers to prove (again without standards) that intangible property values are included within the income and market data approaches. As part of its statutory duty to make tentative assessments pursuant to W. Va. Code § 11-6-9(e), the Department must establish standards to assure that its methods comply with *Ohio Cellular* and do not systematically subject non-taxable intangible property of public utility companies to tax.

Section 4.2.5. The Proposed Rule states that "[a]ny functional obsolescence, economic obsolescence and economic enhancement will be recognized through the correlation process." This is erroneous. The term used in valuation literature as synonymous with *correlation* is *reconciliation*, and the authorities clearly state that *reconciliation* is a distinct step in the appraisal process performed after the individual value indicators have been developed. Accordingly, the new language in Section 4.2.5 should be removed.

Section 4.3.1. The Proposed Rule does not explicitly deal with the anticipated deregulation of at least some aspects of electricity sales and generation, despite the passage of H. B. 4277 during the 1998 Regular Session of the West Virginia Legislature and significant nationwide trends in this regard. While it may be too early to adopt precise appraisal and classification rules, the current procedures are likely to become inappropriate in a deregulated or partially deregulated electric power industry, especially in valuing electric generation facilities. In this regard, we recommend the following sentence be added to the end of Section 4.3.1: "If and when deregulation or partial

Hon. Richard E. Boyle, Jr.
July 2, 1998
Page 4

deregulation of the electric power industry is first implemented in West Virginia [and perhaps in other primary market states], the Tax Commissioner shall propose all necessary amendments to this Rule to reflect what properly constitutes the appropriate 'operating property' of electric utilities and the proper valuation thereof."

AEP appreciates this opportunity to comment upon the Proposed Rule and respectfully urges the Department to adopt AEP's recommended changes and incorporate them into the revised Rule (or another Proposed Rule filing that explains the objectives of the changes *before* the comment period ends) before submission to the Legislative Rulemaking Review Committee. Also included with these comments and incorporated herein by reference are comments of Thomas K. Tegarden addressing the Proposed Rule in light of accepted appraisal practices. As you will note, the points made by Mr. Tegarden, a recognized expert in the field of public utility appraisal, support AEP's comments. If you have any questions or need any additional information, please feel free to contact me.

Sincerely,



Charles O. Lorensen

Enclosure

cc: Earl Goldhammer, Esq.
Mark Pyle
Thomas K. Tegarden

**Comments on “Technical Amendments” to West Virginia Proposed Title 110 -
Valuation of Public Utility Property for Ad Valorem Property Tax Purposes**
by Thomas K. Tegarden, MAI, CAE

§110-1M-2. Definitions.

1. **2.4 5.** “**Economic obsolescence**” means a loss in value of a property arising from factors such as changes in use, legislation that restricts or impairs property rights or changes in supply and demand relationships.
2. **2.5 6.** “**Fair market value**” definition does not comply with current market value definition that is promulgated by *Uniform Standards of Professional Appraisal Practice* (USPAP - 1998 edition), which all state certified appraisers and any members of IAAO must abide by.

Suggest changing words in the definition to “most probable price” instead of “highest price”.

3. **2.7 8.** “**Functional obsolescence**” means a loss in value of a property due to changes in style, taste, or technology.

The definitions listed for economic obsolescence and functional obsolescence in the statutes are very similar to the wording used in IAAO’s textbook (*Property Assessment Valuation*, 2nd ed., 1996) and one is properly led to the conclusion that these forms of depreciation must be considered in the cost approach for the valuation of public utility property for ad valorem property tax purposes. However, such is apparently not the case as shown below in 4.2.1.

§ 110-1M-4. Valuation of Operating Public Utility Property (excluding commercial motor vehicle property). 4.2 Generally accepted appraisal methods.

4. **4.2.1. Cost Approach.** The proposed rule change in this section allows the Tax Commissioner to only deduct “**regulatory**” depreciation instead of “**applicable**” depreciation in the cost approach.

This change is significant in that it allows the Tax Commissioner to ignore the “**three (3) types of depreciation; (a) physical deterioration, (b) functional obsolescence, and (c) economic obsolescence.**”

This change is contrary to generally accepted appraisal principles and practices. In obtaining fair market value, one of the three generally accepted approaches to value is the cost approach. To perform the cost approach the appraiser **must** deduct all forms of depreciation from the estimated cost in order to have a reliable and accurate indication of value by this approach.

Regulatory depreciation is ‘book depreciation’ which is comprised of physical deterioration and *some* functional obsolescence. Book depreciation does not take into account all functional

obsolescence nor does it consider external or economic obsolescence at all. The regulatory agencies that promulgate the rules for accounting for the depreciation are indeed part of the reason a public utility incurs external (economic) obsolescence. It matters **not** whether the public utility is regulated or non-regulated. Generally accepted appraisal principles dictate that **all forms** of depreciation must be measured in determining value by the cost approach. For an appraiser to use regulatory depreciation as the amount of depreciation to deduct in the ad valorem appraisal process would be to accept the notion that book value and market value are the same. **THEY ARE NOT.**

It is clearly stated in appraisal literature that book value and market value are not the same; thus regulatory depreciation (book depreciation) is not acceptable for the appraiser in appraising any property, regulated or unregulated. Some of the most authoritative appraisal literature address this topic as follows:

“Book value is defined as the capital amount at which property is shown on the account books. Book value usually equals the original cost of the asset after subtracting reserves for depreciation and adding allocations for capital recapture. Book value and market value are usually not the same, so the values of the pro rata shares of ownership associated with each differ.” [The Appraisal of Real Estate, 10th ed., (Chicago: Appraisal Institute, 1992), 134.]

“The book depreciation for the improvements on a parcel of real estate is based on historical cost or another previously established figure that may have no relation to current market value.” [The Appraisal of Real Estate, 10th ed., (Chicago: Appraisal Institute, 1996), 451.]

“Book Depreciation is an accounting term that refers to the amount of capital recapture written off for an asset on the owner’s books...Book depreciation is not market-derived, in contrast to depreciation estimates developed by appraisers which are. An appraiser’s estimate of depreciation may help a client reach a conclusion about book depreciation, but the two concepts are distinct and should not be confused.” [The Appraisal of Real Estate, 11th ed., (Chicago: Appraisal Institute, 1996), 366.]

“The market value of the firm’s equity is often substantially different from its book value.” [Richard A. Brealey and Stewart C. Meyers, Principles of Corporate Finance, 4th ed. (New York: McGraw-Hill, Inc., 1991), 190.]

Not only is it necessary to adjust for external obsolescence in the appraisal process, it is unethical in practice to fail to investigate and take into account the loss in value resulting from external obsolescence. The following statement is from the *Uniform Standards of Professional Appraisal Practice* of the Appraisal Foundation.

This guideline also requires the appraiser to investigate and take into account not only that loss of value that results from deterioration due to age but also loss of value due to functional and economic obsolescence. Economic obsolescence is a major consideration when assets are considered as parts of a going concern.. [Appraisal Standards Board, *Uniform Standards of Professional Appraisal Practice*, (Washington, DC: Appraisal Foundation, 1992), S.R. 9-4(b), 43.]

5. **4.2.2 Income Approach.** In this section the words “on long term debt” are replaced with the word “expense.”

The proposed elimination of the words “on long-term debt” and replacement with “expense” is a subtle change which appears intended to allow the Tax Commissioner to include bands of investment (*such as short term debt or current liabilities*) in the capital structure that are used in computing the **financial structure** rather than the market **capital structure**. The typical market capital structure for similar companies is required in the appraisal process. There is very little debate about this concept, however for clarity we note the following statement from Brigham and Gapenski.

We are absolutely convinced that the procedures we recommend are correct — namely, firms should focus on market value capital structures and base their cost of capital calculations on market value weights. Because market values do change, it would be impossible to keep the actual capital structure on target at all times, but this fact in no way detracts from the validity of market value targets. [Eugene F. Brigham and Louis C. Gapenski, *Financial Management*, 7th ed. (New York: The Dryden Press, 1994), 599.]

It is also important to note what elements of capital comprise the makeup of the *capital structure* from an appraisal standpoint. For appraisal purposes, the capital structure consists **only of long-term debt, common stock, and where appropriate, preferred stock**. The capital structure should not be confused with *financial structure* or any other term used in financial literature. To understand what elements comprise the capital structure it is important to define capital structure and financial structure, which are defined as follows:

“**CAPITAL STRUCTURE** corporation’s financial framework, including LONG-TERM DEBT, PREFERRED STOCK, and NET WORTH. It is distinguished from **FINANCIAL STRUCTURE**, which includes additional sources of capital such as short-term debt, accounts payable, and other liabilities.” [John Downes and Jordan Elliot Goodman, *Dictionary of Finance and Investment Terms*, (New York: Barron’s, 1985), 54.]

“**FINANCIAL STRUCTURE** makeup of the right-hand side of a company’s **BALANCE SHEET**, which includes all the ways its assets are financed, such as trade accounts payable and short-term borrowings as well as long-term debt and

ownership equity. Financial structure is distinguished from CAPITAL STRUCTURE, which includes only long-term debt and equity.” [John Downes and Jordan Elliot Goodman, *Dictionary of Finance and Investment Terms*, (New York: Barron’s, 1985), 132.]

For the Tax Commissioner to include short term debt or current liabilities in the capital structure will cause the Tax Commissioner’s capitalization rates to be understated and the resulting utility values to be overstated, which will result in oppressive property taxes.

6. **4.2.4. Adjustments.** This section is new and a portion of the section is without merit or sound appraisal theory or practice. This new section allows the Tax Commissioner to double assess operating leased property in some cases by adding “Property held under operating leases” to all three approaches.

Leasing of equipment is a common and generally accepted business practice in our economy. Operating leases are treated as ordinary operating expenses on the books of public utilities and the capital investment is reported on the books of the owner, not the books of the user (utility). In other words, the utility’s books do not contain the investment in operating leased property, nor does the utility get to earn a rate of return on the leased property. Thus, the cost approach and the income approach do not contain any financial impact of the leased property for a rate-regulated public utility. This theory would extend to the stock and debt approach as well because there theoretically is no net impact on the net income available to the stockholder as a result of the operating lease.

That having been said, if a public utility has operating leases for property which is already being assessed at the local level, it would be improper for the state appraiser of the public utility to make any kind of adjustment in any of the appraisal approaches (cost, income or stock and debt) to try to capture any value for these properties. To do so would mean that the operating leased property would become double assessed (assessed both by the local assessor and the Tax Commissioner). Therefore, if the leased property is locally assessed, a taxpayer will be double assessed for the leased property by the Tax Commissioner.

The last two sentences in this section are ambiguous and are quoted below:

“Consideration will be given for the subtraction from the approaches of the contribution of any other intangible property. A subtraction will only be made for intangible property having a value which is separate and distinguishable apart from the tangible property.”

What does this mean? Does this mean that according to West Virginia law the only intangible property that is exempt from property taxation is that “intangible property having a value which is separate and distinguishable apart from the tangible property?” There is a lot of intangible property which is not separate and distinguishable apart from the tangible property. It sounds like the new proposed rules are intentionally trying to get around the law exempting intangible

property for public utilities. Some companies may have intangible assets which are generated through internal development such as computer software while other companies may have purchased similar application software. The latter company's intangible would show up on the balance sheet while the former company's would not. Some of the categories of intangibles are:

1. Technology (engineering drawings)
2. Contract (favorable supplier contracts)
3. Customer (customer lists)
4. Data processing (computer software)
5. Human capital (trained workforce)
6. Marketing (trademarks)
7. Location (leasehold interests - intangible real)
8. Goodwill (going-concern value)

If any of these are exempt under West Virginia law, they should be excluded from the West Virginia property taxes of the public utility as well.

7. **4.2.5. Correlations.** The last four lines in this section are new. The last sentence is without merit or sound appraisal theory or practice. The sentence reads, "**Any functional obsolescence, economic obsolescence or economic enhancement will be recognized through the correlation process.**"

The process of resolving the differences among various value indications is called reconciliation (old appraisal term was correlation). "*Reconciliation is the analysis of alternative conclusions to arrive at a final value estimate.*" [*The Appraisal of Real Estate*, 11th ed., (Chicago: Appraisal Institute, 1996), 601.] In the reconciliation (correlation) process the appraiser reconciles the differences among the various value indicators (the cost approach, income approach and sales comparison approach). The reconciliation process occurs after each approach to value has been completed. The appraiser cannot leave the cost approach incomplete (by failing to deduct all forms of depreciation) and expect to reconcile away any problems due to his incomplete work. That would be like using peaches from two baskets (one fresh and one spoiled) to make a peach cobbler. The final result (the cobbler) is tainted as a result of mixing the good with the bad.

Professional Qualifications of

Thomas K. Tegarden, MAI, CAE

Tegarden & Associates, Inc., 105 Point East Dr., Nashville, TN 37216-1403
(615) 226-2300 Office, (615) 226-4488 FAX

Degrees and Professional Appraisal Designations

B.S. Accounting, Middle Tennessee State University, 1967

MAI (Member, Appraisal Institute) - Appraisal Institute - certified through December 31, 2003 - Member No. 6275

CAE (Certified Assessment Evaluator) - International Association of Assessing Officers - certified through December 31, 2000 - Member No. 516

Tennessee Certified General Appraiser, Tennessee License No. CG-93

Maine Certified General Appraiser, Maine License No. CG-1302

Appraisal Education

I have taken numerous appraisal and appraisal related courses conducted by the Appraisal Institute (AI), the International Association of Assessing Officers (IAAO), and other organizations toward the goal of earning the MAI and CAE professional appraisal designations. I received the CAE in 1974 and the MAI in 1981. I have taken several additional appraisal courses through the Appraisal Institute, IAAO, and other organizations in order to maintain a "currently certified" status as an MAI and a CAE to continue to further my appraisal education. I am presently certified as an MAI through December 31, 1998 and as a CAE through December 31, 2000. As of the date of this report I have completed all the requirements under the continuing education program of the AI, the IAAO, and the appraisal license program of the State of Tennessee.

Professional Activities & Memberships

Appraisal Institute

MAI - Member, Appraisal Institute - Certificate #6275

Member of Local Chapter #37

Member of Professional Admissions Committee - Tennessee Chapter #37 - 1982

International Association of Assessing Officers (IAAO)

Member IAAO since 1972

CAE - Certified Assessment Evaluator - Certificate #516

Senior Instructor - IAAO's Educational Program

Demonstration Report Grader

Chairman - Residential Grading Committee & Chief Review Grader 1981-90

Member IAAO Course 2 Re-write subcommittee - 1985-86-87

Primary Author IAAO Course 102 - 1993 (*Income Approach to Value*)

One of Three Authors of IAAO Course 101 - 1992-1993

Member IAAO Executive Board - 1982-83

Member Professional Admissions Committee 1980-81

Member Constitutional Review Committee 1979

Professional Designation Advisor - States of KY and TN 1981-86
Faculty Associate - Lincoln Institute of Land Policy
Southern Association of State Property Tax Administrators
President - 1976, Treasurer - 1975
Tennessee Chapter of IAAO

Published Works

- "Future Expectations and Growth: Do They Affect Present Value?," *Journal of Property Tax Management*, Pub. 2:3, Panel Publishers, Inc., (1st Qtr., 1991)
- "Inflation and Utility Property Appraisal," *Public Utilities Fortnightly*, Vol. 123, No. 11 (May 25, 1989)
- "Controversy in the Valuation of Utility Property: A Rejoinder," *Public Utilities Fortnightly*, Vol. 123, No. 5 (March 2, 1989)
- "Appraising Public Utilities: Direct Capitalization and Present Value," *The Appraisal Journal*, January, 1989, The American Institute of Real Estate Appraisers
- "Direct Capitalization vs. Yield Capitalization: In the Appraisal of Public Utility Property," *Assessment Digest*, September/October, 1987, International Association of Assessing Officers
- "Creative Financing: The Assessor's Viewpoint," *Property Tax Journal*, September, 1983, International Association of Assessing Officers

Awards

- 1989 recipient of the **Verne W. Pottorff Professional Designee of the Year Award** from the International Association of Assessing Officers. This award is given annually to the IAAO professional designee who has most effectively promoted the interests and goals of the IAAO professional designation program.
- 1984 recipient of the **Bernard L. Barnard Award** from the International Association of Assessing Officers. This award is given annually to the author of the article published in the *Property Tax Journal* which has contributed the most to the improvement of assessment administration.

Experience

- Owner - Tegarden & Associates, Inc.** - duties include client consultation, appraisal of public utilities, railroads, special purpose properties, and expert testimony
- Was employed by the **Tennessee Public Service Commission** 15 years — 1967 - 1983 where I was Assistant Director of Assessments for 11 years. My duties included the annual appraisal and assessment of approximately \$4 billion (\$4,000,000,000) of railroad and public utility property
- Instructor - Seminar on Public Utility Valuation - Wichita State University** - sponsored by National Tax Association - Tax Institute of America and Wichita State University
- 1997 "Principles of Appraisal for Public Utility and Railroad Property"

- "Advanced Cap Rate Applications"
- 1996 "Principles of Appraisal for Public Utility and Railroad Property"
 - 1995 "Principles of Appraisal for Public Utility and Railroad Property"
 - 1994 "Principles of Appraisal for Public Utility and Railroad Property"
 - 1993 "Principles of Appraisal for Public Utility and Railroad Property" and "DCR Method" and "Weighted After-Tax Cost of Capital and Cap Rate"
 - 1992 "Principles of Appraisal for Public Utility and Railroad Property" and "Selection of Income & Rates in Yield Capitalization"
 - 1991 "Principles of Appraisal for Public Utility and Railroad Property"
 - 1990 "Principles of Appraisal for Public Utility and Railroad Property" and "Future Expectations and Growth: Do They Affect Present Value?"
 - 1989 "Principles of Appraisal for Public Utility and Railroad Property"
 - 1988 "Principles of Appraisal for Public Utility and Railroad Property"
 - 1987 "Principles of Appraisal for Public Utility and Railroad Property"
 - 1986 "Principles of Appraisal for Public Utility and Railroad Property" and "Direct Capitalization vs. Yield Capitalization"
 - 1985 "Principles of Appraisal for Public Utility and Railroad Property"
 - 1980 "Administrative Problems with Deferred Federal Income Taxes and the Investment Tax Credit"
 - 1978 "Demonstration Appraisal of Telephone Company"
 - 1976 "Special Problems Including Correlation"

Consultant to Georgia Department of Revenue - 1980, 1984, & 1985; Missouri State Tax Commission - 1980; Tennessee Attorney Generals Office - 1983; Citrus County, FL - 1983; St. Lucie County, FL - 1984; Oklahoma Tax Commission - 1983; Hendry County, FL - 1984; Putnam County, FL - 1990; Dallas County, TX Appraisal District - 1983, 1997; Michigan State Tax Commission - 1985; Florida Department of Revenue - 1985 - 1986; Colorado Legislative Council - 1988-89, Wyoming Tax Commission and State Board of Equalization - 1989 - 1990; Colorado Department of Property Taxation - 1989, 1991, 1993; City of Valdez, Alaska - 1990, 1992; South Dakota Department of Revenue - 1991, 1992; North Slope Borough, Alaska - 1994, 1997; Sarasota County, FL - 1995-96.

Faculty - Land Reform Training Institute (Instructor of appraisal course to students from 12 countries) Taoyuan, Taiwan, Republic of China

Faculty - Lincoln Institute of Land Policy

"The Economic Foundations of Railroad and Utility Valuation," Scottsdale, AZ, 1995

"Understanding the Capitalization Process," Scottsdale, AZ, 1994

"The WHYs and HOWs of Railroad and Utility Valuation," Scottsdale, AZ, 1991

Senior Instructor - Course II - The Income Approach to Valuation (International Association of Assessing Officers) - West Palm Beach, FL; Auburn University; Sarasota, FL; Troy, NY; Jacksonville, FL; Tampa, FL; Columbia, MO; Orlando, FL; Miami, FL; University of Virginia; Denver, CO, Austin, TX — 1983 - 1997

Senior Instructor - Contemporary Real Estate Finance (International Association of Assessing Officers) - Montana State University - Bozeman, MT - 1984

Senior Instructor - Introduction to Income Approach to Value Workshop - (International Association of Assessing Officers) Oklahoma City, OK - 1987, Lubbock, TX - 1988

Author and Instructor of copyrighted *Public Utility Basic Appraisal Course* - LaBelle, FL - 1984; Tallahassee - 1986, Cheyenne - 1989, 1990, 1991, 1992, 1993, 1995, 1996, 1997; Austin - 1989; Atlanta - 1992; Denver - 1994

Author and Instructor - *The Development and Use of the Compound Interest Tables and Using the HP-12C Calculator* (for Colorado Department of Revenue, 1991)

Program Speaker and Participant - Valuation Roundtable - Phoenix, AZ (Lincoln Institute of Land Policy) - 1984

Program Speaker and Participant - IAAO Public Utility Seminar - Nashville - 1997, New Orleans - 1995

Program Speaker - Annual Professional Seminar - Jointly Sponsored by American Institute of Real Estate Appraisers, International Association of Assessing Officers, and Society of Real Estate Appraisers

17th Seminar - "Creative Financing: The Assessor's Viewpoint" - Kansas City, MO - 1982

30th Seminar - "Valuation Issues in the Telecommunications Industry: The Capitalization Rate" - Chicago, IL - 1995

Instructor - CASPER (Computer Assisted Analysis of Special Purpose Properties for Education and Research) - Lincoln Institute of Land Policy - Cambridge, MA - 1982, 1983 - San Francisco, CA - 1983, Orlando, FL - 1984

Instructor - Microcomputer Techniques for Special Property Appraisal (Course 109) - Lincoln Institute of Land Policy - Orlando, FL - 1984

Instructor - Institute of Property Taxation - Kellogg School of Business - Michigan State University 1987 "The Appraisal of Railroads and Public Utilities," 1983 "Appraisal of Mineral Interests" and "The Appraisal of Railroads and Public Utilities"

Program Speaker - National Association of Railroad and Public Utility Tax Representatives - Atlanta, GA - 1983; Denver, Colorado - 1986

Instructor - North Carolina IAAO Candidates Club - University of North Carolina - Chapel Hill, NC - 1984

Instructor - International Association of Assessing Officers - Personal Property Seminar - Scottsdale, AZ and Virginia Beach, VA - 1985

Program Speaker - IAAO Conference

Houston, TX - 1996, "Regulation: Its Impact on Value"

Washington, D.C. - 1993, "The Appraisal of Public Utilities & Commercial Properties: What's the Difference?"

Montreal, Quebec - 1990, "The Role of the Consultant in the Ad Valorem Tax Process"

Nashville, TN - 1988, "The Valuation of Public Utilities & the Potential for Growth"
Louisville, KY - 1981, Detroit, MI - 1980, and Atlanta GA - 1976

Expert Testimony

Numerous times - state and federal courts, state assessment boards, public service commissions, and legislative committees as an expert appraisal witness regarding the valuation of public utilities, railroads, special purpose properties, commercial, industrial, and residential properties.

Bell Atlantic Corporation
1095 Avenue of the Americas
New York, NY 10036

RECEIVED
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State Tax Commissioner



June 30, 1998

The Honorable Richard E. Boyle, Jr.
State Tax Commissioner
c/o Legal Division
State Tax Commission
P.O. Box 1005
Charleston, WV 25324-1005

RE: Proposed Legislative Rule Title 110, Series 1M. Valuation of
Public Utility Property for Ad Valorem Property Tax Purposes

Dear Commissioner Boyle:

I am filing these comments on behalf of Bell Atlantic.

House Bill 4713, enacted on March 12, 1998, authorized the State Tax Commissioner to propose a legislative rule that describes the methodology for determining the market value of interstate public service corporation motor vehicles subject to proportional registration. This proposed rule, however, makes additional so called "technical amendments" to the rule which are objectionable.

The proposed rule changes which are characterized as "technical amendments fail to set forth clearly and separately the objective of the rules and a general description of the issues to be decided (as required by W. Va. Code §29A-3-4 (b) and §29A-3-5). As such, this rule-making process fails to comply with the rule-making requirements imposed by W. Va Code §29A-3-1 et seq.

The proposed rule changes do not take into account the current and pending deregulation of the telecommunications industry. Some of the rules and regulations as proposed are not consistent with §11-3-1 of the West Virginia Code which states that, "All property shall be assessed annually as of the first day of July at its true and actual value; that is to say, the price for which such property would sell if voluntarily offered for sale by the owner thereof," The definition in the statute relates to market value. It is our opinion that any rules or regulations that allow the Department to assess property using "regulated" based concepts are contradictory to this section of the statute.

Bell Atlantic requests that a public hearing be held by the Department regarding these proposed rule changes after the required rule-making procedures are satisfied.

More specific comments on the "technical amendments are attached hereto.

Specific Comments.

Proposed Rule 2.19 - "Regulation" means the oversight of public service corporations by applicable federal and state regulatory bodies.

Comment - The current rule defines regulation as "the process wherein fees charge for public utility services are reviewed by applicable federal and state regulatory bodies. It specifically addresses "fees charged" for "public utility" services. The proposed rule change expands the definition to include a vague concept of

“oversight” and it changes the term “public utility” to “public service corporations.” True regulation relates to the fees that are charged by public utilities and W. Va. Code §1-1C-5(a) (2)(D) only authorizes the tax commissioner to assess parcels or other property “which are an integral part of the public utility’s function as a utility....” In addition, the concept of regulatory “oversight” is too vague. Many corporations may be required to file some kind of documentation with the appropriate state or federal regulatory bodies, but in no way are they “regulated” based on earnings.

Rule 2.20 – “Replacement cost” - While there has been no change in this rule, the term “to its owner” should be eliminated from the definition of replacement cost because “to its owner” suggests value in use principles rather than market value principles. As stated above, Section 11-3-1 of the West Virginia Code requires that true and actual value be the standard, not value in use.

Proposed Rule 2.12 - The definition of operating property is exactly the same except that the word “property” is eliminated prior to the word “used for purposes immediately connected with providing the respective utility service.” As a result of the Ohio Cellular case, the definition should be restricted to personal property defined in W. Va. Code §11-5-3.

Proposed Rule 4.2.1 - Cost Approach. In the proposed rule change, “applicable” depreciation was replaced with “regulatory” depreciation. Depreciation should reflect physical wear and tear, functional and economic obsolescence, as stated in the current rule. These are market based concepts whereas “regulatory” depreciation pertains only to regulatory accounting requirements. Also, there is no definition of what is meant by “cost regulated” public service corporations. The last sentence should read as follows: For public service corporations no longer rate base regulated, depreciation shall be based on generally accepted accounting principles. The current rule should be retained because it is based on market value principles.

Proposed Rule 4.2.4 – Adjustments. - The term “operating leases” is not specific enough. In general, the lessor is responsible for property taxes. Capital leases are different because typically the property is owned after lease termination. If anything, this rule should only relate to capitalized leases because they are generally viewed as ownership. The proposed rule change is unjustified because it may result in double taxation of the same property. In addition, the last sentence of this section requires that taxpayers provide proof that intangible property values are included in the income and market approaches. Because the cost approach generally values just the tangible assets, it should be given predominate weight in the correlation process. This would eliminate most intangibles from the valuation process without requiring a statutory change in the method of taxation (i.e. the unit method).

Proposed Rule 4.2.5 - Correlations - The second sentence should read: “The cost approach should generally be given primary consideration in the correlation process.” The last sentence referring to functional and economic obsolescence and or “enhancement” should be eliminated. These concepts are accounted for only in the cost approach, before the correlation process. The Appraisal of Real Estate, Tenth edition, says on page 555: “The appraiser weighs the relative significance, applicability, and defensibility of each value indication and relies most heavily on the approach that is most appropriate to the nature of the appraisal.” Because the state is authorized to tax only tangible assets and limited intangible assets (see Ohio Cellular), the cost approach is the best indicator of value.

Bell Atlantic appreciates the opportunity to comment on these proposed rules. We believe that the above changes should be incorporated into the Department’s revised rules and further appreciate the chance to comment on these rules in a hearing format before the Legislative Rulemaking Review Committee.

Sincerely



Michael J. Mupo
Director of Property Tax
212-395-1293



July 1, 1998

State Tax Commissioner

The Honorable Richard E. Boyle, Jr.
State Tax Commissioner
1900 Kanawha Boulevard East, Room WW-300
State Capitol Building
Charleston, WV 25305

**RE: Comments of Mountaineer Gas Company Regarding Proposed
Legislative Rule Title 110, Series 1M, Valuation of Public Utility
Property for Ad Valorem Property Tax Purposes**

Dear Commissioner Boyle:

On behalf of our client, Mountaineer Gas Company, Deloitte and Touche LLP wishes to comment on the Proposed Legislative Rule cited as Title 110, Series 1M, entitled *Valuation of Public Utility Property for Ad Valorem Property Tax Purposes*.

Mountaineer Gas Company is currently subject to the "public utility" property tax regime found in W.Va. Code §§ 11-6-1 *et seq.* The Proposed Rule directly affects Mountaineer Gas, and Mountaineer Gas offers the following comments.

I. General Comments

The Summary, Objectives and Statement of Circumstances filed along with the Proposed Rule correctly indicate that the Tax Commissioner is required by H. B. 4713 (passed March 12, 1998) to propose a legislative rule that describes the methodology for determining market value of certain motor vehicles subject to proportional registration. However, the statements accompanying the Proposed

Rule indicate that Proposed Rule “also makes *technical* amendments” or “*other technical* amendments” to the Current Rule without any further description, explanation or rationale.

Mountaineer Gas objects to the Department’s characterization of changes made in the Proposed Rule with no relationship to the objectives to H. B. 4713; many of these so called “technical amendments” are not merely stylistic or “clean-up” changes. They establish new, and in many cases, inappropriate and unlawful policies of the State in valuing operating public utility property, reversing the Current Rule and prior rule filings that have set forth legislatively endorsed policies for decades. These policies should not be reversed under the guise of *technical amendments*. Of course, there have been relevant changes since the Current Rule’s promulgation, including deregulation trends and the *Ohio Cellular* case, that the Department must address. However, the so-called *technical amendments* reverse other, well-settled, policies without intervening changes.

The Department is required to “clearly and separately state” the objective of the changes before seeking public comment. W.Va. Code § 29A-3-5 and -4(b). We recommend that the Department comply with W.Va. Code § 29A-3-5 and -4(b) and refile the Proposed Rule for comment, separately stating the objectives of each and every so-called *technical amendment* and providing authority therefor. Without timely compliance with this legislative requirement, the public is left to speculate about the Department’s objectives and justification in several instances. We further recommend that the Department conduct a public hearing regarding the Proposed Rule.

Additionally, the Proposed Rule fails to identify (by underlining and strike-throughs) all the relevant changes from the Current Rule. The Proposed Rule as filed fails to identify Section 4.2.4 as being new language, even though Section 4.2.4 is not found in the Current Rule. This failure could mislead a reader into believing that Section 4.2.4 (which is presumably part of the “other technical amendments”) is not a change from current language unless the reader disregards the underlining and strike-throughs and compares the Proposed Rule side-by-side

with the Current Rule. We recommend that this correction be made to comply with W.Va. Code § 29A-3-11(a)(1).

II. Specific Comments

Section 4.2.1 The Proposed Rule's deletion of the second sentence of Section 4.2.1 in the Current Rule is inappropriate and constitutes a fundamental change. Under the Proposed Rule, functional obsolescence and economic obsolescence would presumably not be considered under the cost approach to value. This is not a generally accepted appraisal approach. The Current Rule correctly requires the consideration of functional obsolescence and economic obsolescence in the cost approach whereby the Proposed Rule eliminates these considerations. The Current Rule language in this regard should be retained and the Department should consistently adhere to the Current Rule's policy in setting tentative assessments.

Section 4.2.2 The Proposed Rule, without any stated justification, strikes the phrase "long-term debt" and substitutes the term "expense" in the second sentence of Section 4.2.2. This proposed change is clearly outside of the stated Objective, and accordingly, we object to the proposed change.

Section 4.2.4 The Proposed Rule's new Section 4.2.4 (and this should be shown by underlining as stated above) authorizes certain "adjustments" without providing any standards and attempts to place inappropriate burdens upon taxpayers. First, the Proposed Rule makes reference to adjustments to (a) *add* property held under operating leases to the three approaches and (b) *subtract* the influence of working capital from the income approach and market data approach. The addition of "operating lease" property is unjustified and will result in double taxation of the same property. Moreover, without standards, the Proposed Rule is incomplete and ambiguous respecting both of these adjustments.

Second, the fourth and fifth sentences in Section 4.2.4 (both concerning *intangible property*) inadequately deal with the *Ohio Cellular* decision. The Department is statutorily required to appraise taxable operating public utility

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property. Through this filing, the Department appears to require taxpayers to prove (again without standards) that intangible property values are included within the three approaches to value. As part of its statutory duty to make tentative assessments pursuant to W.Va. Code § 11-6-9(e), the Department must establish standards to assure that its methods comply with *Ohio Cellular* and do not systematically subject non-taxable intangible property of public utility companies to tax. For instance, the standards should clearly set out the method(s) that will be employed to subtract from the income approach the "intangible income" realized by Mountaineer Gas for the margins realized from the buy/sell arrangements for natural gas.

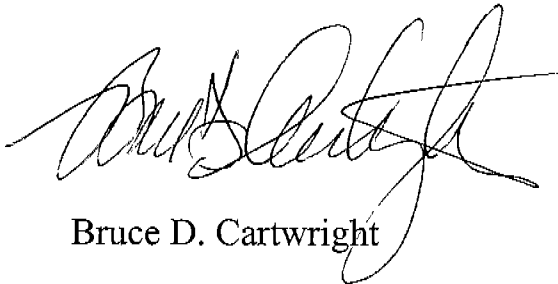
Section 4.2.5 The Proposed Rule states that "[a]ny functional obsolescence, economic obsolescence and economic enhancement will be recognized through the correlation process." This change violates generally accepted appraisal standards. Proper appraisal standards mandate that correlation can only be accomplished after each approach to value has been adjusted to account for all forms of depreciation; physical, functional and economic. In general, the appraiser should use or give weight to the approach that is most supportable given the available data that is within the constitutional and statutory scheme of taxation. Accordingly, the new language in Section 4.2.5 should be removed.

Section 5.5 The Proposed Rule eliminates the Commissioner's authority to grant an extension of filing deadlines, for good cause. The Current Rule correctly authorizes the Commissioner to grant extensions of filing deadlines for those taxpayers who have demonstrated "good cause." Elimination of this provision will unduly burden good faith taxpayers. Accordingly, the Current Rule language should be retained.

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Mountaineer Gas appreciates this opportunity to comment upon the Proposed Rule and respectfully urges the Department to adopt Mountaineer Gas's recommended changes and incorporate them into the revised Rule (or another Proposed Rule filing that explains the objectives of the changes *before* the comment period ends) before submission to the Legislative Rulemaking Review Committee. If you have any questions or need any additional information, please feel free to contact me.

Respectfully Submitted,

A handwritten signature in black ink, appearing to read "Bruce D. Cartwright", written in a cursive style.

Bruce D. Cartwright

BDC/bdc

cc: Deana LeFevre, General Counsel, Mountaineer Gas Company
Charles O. Lorensen, George & Lorensen P.L.L.C.

**PUBLIC COMMENTS AND RESPONSES
VALUATION OF PUBLIC UTILITY PROPERTY
FOR AD VALOREM PROPERTY TAX PURPOSES
110 C.S.R. 1M**

COMMENT 1: 110 C.S.R. 1M, § 4.3.7 - Suggestion was made to correct the reference to the Interstate Commerce Commission which has been dissolved. The new reference should be United States Department of Transportation.

RESPONSE: This section was deleted.

COMMENT 2: 110 C.S.R. 1M, § 5.3 - Objection was made to the language which states "the numerator of which represents total miles". Commentator suggested the language "the numerator of which represents total fleet miles".

RESPONSE: The language used in the proposed rule closely follows the language of H.B.4713 which appears to describe a vehicle by vehicle appraisal method and not a fleet appraisal method; however, in practice the mileage figures for proportional registration are indeed fleet figures. Therefore, the rule was changed to reflect the word fleet in both the numerator and denominator.

COMMENT 3: Suggestion was made to include a reference, as it pertains to interstate motor carriers, that the property tax is payable through International Registration Plan. It was suggested that it should be clear that these companies will not be filing with the Tax Commission.

RESPONSE: Language to that effect was inserted into Section 5.2.2.

COMMENT 4: Objection was made as to the characterization of certain proposed changes as technical amendments. Commentators viewed some changes as new policies which reverse the current rule. One commentator stated that since deregulation was changing the term "public service company" that any rule changes should be limited to those required by H.B. 4713.

RESPONSE: H.B. 4713 required the Tax Commission to establish a rule relating to the valuation of commercial motor vehicles. The Commission decided to insert these changes into the existing rule concerning public utility valuation. The Tax commission decided to also update the existing rule in order to provide more specific information concerning current Tax Commission practices. The treatment of this matter in the agency approved rule does not reflect a change in policy; rather, it provides more

specific information concerning the process used by the Tax Commissioner in carrying out the general provisions contained in the current rule.

COMMENT 5: 110 C.S.R. 1M, § 4.2.4 - Section was not underlined indicating that it was new language.

RESPONSE: This comment is correct. Subsection 4.2.4 is now underlined.

COMMENT 6: 110 C.S.R. 1M, § 4.2.1 - Objection to the removal of the language concerning consideration of functional obsolescence and economic obsolescence. Commentators describe this as a fundamental change which is not a generally accepted appraisal practice.

RESPONSE: When setting the public utility valuations, the Tax Commission relies heavily on the income approach to value. To the extent that the income approach and hence the final valuation is less than the cost approach, obsolescence is indeed recognized. The treatment of this matter in the agency approved rule does not reflect a change in policy; rather, it provides more specific information concerning the process used by the Tax Commissioner in carrying out the general provisions contained in the current rule.

COMMENT 7: 110 C.S.R. 1M, § 4.2.2 - Objection to the striking of the phrase “long term debt” and replacing it with the word “expense”. Commentators describe this an attempt by the Commission to either increase income to capitalize or decrease the rate of capitalization.

RESPONSE: The sentence in question describes the income stream to be capitalized. The previous language stated the stream should be net operating income after taxes, but before interest on long term debt. In actuality, the net operating income historically utilized by the Tax Commission corresponds with net operating income as computed for regulatory purposes. This net operating income calculation includes interest expense from both short term and long term debt. Therefore, the proposed change from interest on “long term debt” to interest “expense” simply recognizes the actual construction of net operating income. The treatment of this matter in the agency approved rule does not reflect a change in policy; rather, it provides more specific information concerning the process used by the Tax Commissioner in carrying out the general provisions contained in the current rule.

COMMENT 8: 110 C.S.R. 1M, § 4.2.4 - Objection was made relative to the addition of property held under operating leases as an adjustment to the approaches to value.

Commentators felt that this property was assessed to the lessor and would therefore result in double assessments.

RESPONSE: The Tax Commission currently adds property held under operating leases to the approaches to value in situations where the lessee is responsible for reporting the property to the Board of Public Works. The treatment of this matter in the agency approved rule does not reflect a change in policy; rather, it provides more specific information concerning the process used by the Tax Commissioner in carrying out the general provisions contained in the current rule. This section was modified to explain that leased property will not be added to the utility appraisal in instances where the property is being assessed in another manner.

COMMENT 9: 110 C.S.R. 1M, § 4.2.4 - Objection was made to the last two sentences relating to deduction from the approaches to value for other intangible personal property. Commentators felt that the language did not adequately deal with the Ohio Cellular decision. Commentators felt that the requirement that the intangible personal property have a value separate and distinguishable apart from the tangible personal property before consideration of a deduction was too restrictive. Commentators felt that this placed a burden of proof on the taxpayers to show an intangible value when the Tax Commission was responsible for determining the value.

RESPONSE: As defined in Section 2.26, the unit method involves an appraisal of an integrated property as a whole without any reference to the value of its component parts. To the extent that the method captures nontaxable intangible property, the new language was designed to allow for the subtraction of the influence of such intangible property; however there are certain intangible influences, such as location, which are a part of the tangible property and should not be subtracted. The Tax Commission therefore feels that the requirement that the intangible property have a value separate from the tangible property is necessary and not contrary to the Ohio Cellular decision.

COMMENT 10: 110 C.S.R. 1M, § 4.2.5 - Objection was made as to the last sentence which was added that reads "Any functional obsolescence, economic obsolescence or economic enhancement will be recognized through the correlation process". Commentators felt that these factors should be recognized in the cost approach prior to correlation.

RESPONSE: See response to Comment 6.

COMMENT 11: 110 C.S.R. 1M, § 4.3.1 - Objection was made to the classification of operating property for Electric Utilities. Commentator felt that some language should be added stating that electric deregulation may cause a change in what constitutes "operating property" of electric companies.

RESPONSE: The Tax Commission feels that the rule should not attempt to cover all potential future scenarios. In the event that deregulation causes the rule to be outdated, any necessary amendments to the rule can be proposed at that time.

COMMENT 12: 110 C.S.R. 1M, § 2.7 - Suggestion was made to change wording from “highest price” to “most probable price”.

RESPONSE: This definition was changed to conform with the statutory definition in W.V. Code § 11-3-1.

COMMENT 13: 110 C.S.R. 1M, § 4.2.1 - Objection was made to replacing the word “applicable” with the word “regulatory”. Commentator suggested that regulatory depreciation would not take into account all functional obsolescence nor would it consider economic obsolescence.

RESPONSE: The treatment of this matter in the agency approved rule does not reflect a change in policy; rather, it provides more specific information concerning the process used by the Tax Commissioner in carrying out the general provisions contained in the current rule. The obsolescence issue was addressed in Comment 6.

COMMENT 14: Objection was made stating that since the state was to tax only tangible property the rules should be changed eliminating the use of the unit method and replacing it with reproduction cost new less depreciation. Commentator suggested that if the unit method remains in effect, the rules must be changed explaining how intangibles will be removed.

RESPONSE: The Commission intends to continue using the unit method to value public utility property. Section 4.2.4 was added to the rule to allow for the removal of the influence of nontaxable intangible property. The rule is intended to provide general guidelines for the appraisal process and does not deal with specific calculations.

COMMENT 15: 110 C.S.R. 1M, § 4.2.5 - Objection was made that the term economic enhancement had not been defined.

RESPONSE: This comment is correct and a definition was added to the rule.

COMMENT 16: 110 C.S.R. 1M, § 2.19 - Objection was made to the change in the definition of regulation. Commentators felt the term “oversight” was too vague.

RESPONSE: The previous definition referred to regulation of the fees charged by public utility companies. Many companies required to be assessed by the Board of Public Works are no longer regulated in that sense, so the definition was changed to merely "oversight" by applicable regulatory bodies.

COMMENT 17: 110 C.S.R. 1M, § 2.3 - Suggestion was made that the fourth word in the sixth line should be vehicle instead of vehicles.

RESPONSE: The change was made.

COMMENT 18: 110 C.S.R. 1M, § 2.12 - Suggestion was made to leave this definition unchanged.

RESPONSE: The only change made to this definition was removal of the phrase "is property" which was redundant.

COMMENT 19: 110 C.S.R. 1M, (Previous Section 5.5) - Suggestion was made that the previous Section 5.5 should not be eliminated.

RESPONSE: The Tax Commission has no statutory authority to grant filing extensions. Additionally, the historical practice of the Tax Commission has been that no filing extensions can be granted. The treatment of this matter in the agency approved rule does not reflect a change in policy; rather, it provides more specific information concerning the process used by the Tax Commissioner in carrying out the general provisions contained in the current rule.

COMMENT 20: 110 C.S.R. 1M, § 4.2.5 - Objection was made to the inclusion of the term economic enhancement. Commentator suggested that recognizing an economic enhancement would necessitate the capture of intangible property.

RESPONSE: Just as economic obsolescence is reflected by an appraisal that is less than the cost valuation, an economic enhancement is reflected by an appraisal that is in excess of the cost valuation. The cost valuation utilized by the Tax Commission is based upon historical cost. Oftentimes, land and buildings have been purchased many years ago and therefore have an understated historical cost. Therefore, it would be incorrect to assume that this economic enhancement must represent intangible property.

COMMENT 21: 110 C.S.R. 1M, § 2.20 - Objection was made to the definition of replacement cost. Commentator felt the words “to its owner” suggested value in use rather than true and actual value.

RESPONSE: This definition was not changed from the previous rule which had been approved by the West Virginia Legislature. Additionally, this definition corresponds to definitions found in other appraisal texts.

COMMENT 22: 110 C.S.R. 1M, § 2.12 - Suggestion was made that due to the Ohio Cellular case, the definition of operating property should be limited to personal property as defined in W. Va. Code.

RESPONSE: The definition of operating property refers to accounts classified as operating by regulatory bodies. There is no reason to limit this definition to personal property.

COMMENT 23: 110 C.S.R. 1M, § 4.2.1 - Suggestion was made to change the wording of the last sentence to read “For public service corporations no longer rate base regulated, depreciation shall be based on generally accepted accounting principles.”

RESPONSE: This section was changed to allow for consideration of a depreciation method other than regulatory accounting if the utility was no longer cost regulated. The commentator’s suggestion contains the word “shall” which would make it mandatory. The current wording will allow the Tax Commission to “consider” the depreciation method described by the commentator.

COMMENT 24: 110 C.S.R. 1M, § 4.2.5 - Suggestion was made that since the state is authorized to tax only tangible assets, that the cost approach would be the best indicator of value.

RESPONSE: This section was modified to suggest that while the income valuation was to be given primary consideration, exceptions would be made for cause. The commentator’s proposed language is contrary to the generally accepted appraisal practice that dictates that all three approaches be considered. The section as modified will allow for consideration of any special circumstances.