Best Practices

Deducting Intangible Asset Value for Property Tax Purposes: How "Necessary Intangibles" Are Treated in Two Recent Cases

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Two recent judicial decisions provide professional guidance on when—and how—intangible asset value can be excluded from the taxpayer's total unit value. This issue is particularly complicated when the subject intangible assets are the types of intangible assets that are "necessary" for the taxpayer to operate as a going concern business. Such right-to-do-business intangible assets include various types of licenses, permits, and franchises.

Introduction

Two recent state Supreme Court cases examine an important set of issues involving the unit valuation of companies for property tax purposes. The issues relate to the exemptions for intangible assets that are common in many states.

The two cases address the treatment of the taxpayer intangible assets that are necessary to the operation of the business. If the taxpayer intangible assets are necessary, can they be excluded? Or, do the intangible assets represent assets or rights like building permits that cannot effectively be excluded because they do not generate a specific stream of income, or cannot be held separately from the subject unit of property?

These two cases—*Gold Creek Cellular of Montana dba Verizon Wireless and AT&T Mobility v. Department of Revenue*,[1] and *Elk Hills Power v. Board of Equalization*[2]—may add to the debate concerning when intangible assets can be deducted from a unit value. Although each case was decided under a statute that was specific to the state and has unique language, the cases still provide guidance to taxpayers, legal counsel, and valuation analysts on how courts may apply intangible property exemptions in the future.

This discussion analyzes these cases and argues that the Montana Supreme Court was correct in holding that the intangible asset exemption includes assets necessary to the operation of the taxpayer business enterprise.

The California Supreme Court was also correct in holding that the replacement cost of certain necessary intangible assets cannot be legally added to the value of the taxpayer business determined under the cost approach. However, the court's analysis was incomplete in suggesting that an exemption could be denied in the income approach when the intangible assets' income contribution cannot be specifically determined.

After reviewing these and other cases, this discussion concludes that the proper analytical procedure is to exclude intangible property in each valuation approach, consistently. Indeed, the best procedure, and the procedure that could have avoided the confusion introduced in *Elk Hills*, is to exclude the intangible asset value from the reconciled overall unit value in order to obtain the same result.

Background

For over 120 years, it has been the practice of states to value certain types of taxpayer companies using the "unit" approach to valuation.[3] The taxpayer companies valued in this way are typically public utilities like electric, gas and water transmission and distribution companies, telephone companies, railroads and airlines. The premise of the unit approach is that there is value in the going concern—from all these properties operating together as one unit—that may be greater than the summation of the values of the individual properties within the system.

Because the taxpayer's property usually crosses so many local government boundaries, the unit valuation principle is generally applied on a "central assessment" basis by the state's department of revenue. State assessment authorities use the three generally accepted valuation approaches—cost, income, and market—to determine the value of the taxpayer's unit.

By its nature, the cost approach does value the individual properties, although adjustments for functional and economic obsolescence often are made at the system—or unit—level. After determining separate values for the unit using the cost, income or market approach methods, the appraiser "correlates" or "reconciles" these values into a single value conclusion, after considering the strengths and weaknesses of each valuation method.

States began using the unit approach in the 19th century, when a larger share of property ownership in this country was tangible—real estate or tangible personal property. In the 20th century, we saw an explosion in the value of intangible property. And, such intangible property represents an ever-increasing proportion of the nation's wealth.[4]

As a result, and perhaps because intangible property is difficult to value, states began enacting property tax exemptions for intangible property. Most states now have such exemptions.

Intangible property exemptions have presented a number of issues in their application. For instance, it is not always clear whether a property interest represents a separate type of property that would qualify for the exemption, or whether it is simply an attribute of property that is taxable. The classic example is the location feature of real estate, which may "enhance" the value of real estate but is not a separate type of property in its own right. Thus, location is an intangible attribute of real property that affects its value and is properly considered as part of the real property's taxable value.

Some state taxing authorities have used this concept of enhancement to argue that all of—or at least most of—the intangible assets of a centrally assessed company are not exempt. That is, the taxpayer intangible assets are necessary for the operation of the business enterprise or the taxpayer intangible assets may have no independent value apart from the enterprise. And, therefore, such taxpayer intangible assets are taxable because they enhance the value of the taxpayer's tangible, taxable property.

This argument was rejected in the California case of *GTE Sprint Communications Corp. v. County of Alameda*. In that decision, the court held that although the unit value may be enhanced by the presence of intangible property, the statutory exemption requires that the value of the property must be excluded from the unit value.[5]

In contrast, with respect to the sometimes elusive intangible asset called "goodwill," the Utah Supreme Court in *Beaver Count v. WilTel* held that for a telecommunications company, it was not necessary to exclude the increment of value that represents the difference between the tangible property value standing alone, and the business enterprise value of the entire unit.[6]

In that decision, the court likened this goodwill to the assemblage value concept in real estate appraisal, where the process of assembling disparate properties into an operating system creates an intangible attribute, similar to location. That intangible attribute enhances the value of the taxpayer's unit and does not require adjustment.

The Montana Case—*Gold Creek Cellular of Montana dba Verizon Wireless and AT&T Mobility v. Department of Revenue*

In 1999, the Montana legislature passed a broad exemption for intangible personal property. The statute defines "intangible personal property" as property "that has no intrinsic value but is the representative of value," or "property that lacks physical existence, including goodwill."

The statute then provides a nonexhaustive list of property that meets that definition: "certificates of stock, bonds, promissory notes, licenses, copyrights, patents, trademarks, contracts, software, and franchises."

After years of litigation over the scope of this exemption, and how intangible property should be extracted from the unit for centrally assessed taxpayers, the Department of Revenue promulgated a rule to define goodwill as only "booked" goodwill, and to impose restrictions on the definition of intangible personal property:

> (12) "Intangible personal property" has the following attributes
>
> (a) Intangible personal property must be separable from the other assets in the unit and capable of being held under separate title or ownership.

(b) Intangible personal property must be able to be bought and sold, separate from the unit of operating assets, without causing harm, destroying, or otherwise impairing the value of the unit of assets being valued through the appraisal process.

(c) Intangible personal property must have value as a result of its ability to create earnings that exceeds their contributory value to the unit; or, it must be capable or earning an income as a standalone entity or apart from the other assets of the unit.

(d) Intangible personal property is not the same as intangible value. Intangible value is the value of an entity as a going concern—its ability to make excess revenues over the normal rate of return. Intangible value is part of the overall value of assets. Intangible value is not exempt from property taxation in Montana.[9]

This definition raised a host of issues for taxpayers. For instance, subparagraph (a), requiring that an asset must be capable of being owned outside the unit, suggests that goodwill would not meet the definition of intangible personal property, yet goodwill is one of the examples of such property listed in the statute.

Subparagraph (c) purports to exclude all intangibles that earn *only* their cost of capital, so if a license is purchased for $1 million but earns only its cost of capital, none of the value would presumably be included as intangible property value. In contrast, if an intangible asset earned *more* than the cost of capital, subparagraph (d) would seem to exclude it as an exempt asset by characterizing it as intangible value rather than as intangible property.

Although each of these conditions is problematic in developing a sound definition of intangible personal property, the one that is the most troublesome is subparagraph (b). The subparagraph requires that an asset must be capable of being sold and not affect the operation of the business. In other words, if an asset is necessary to the operation of the business, then it could not qualify as an exempt intangible asset.

The Montana Supreme Court had little difficulty holding that this definition of intangible personal property exceeded the Department's rulemaking authority—which is to promulgate rules consistent with the statute. The court noted that FCC licenses, for instance, are clearly exempt because licenses are specifically listed in the statute as examples of intangible personal property. Yet, FCC licenses would not satisfy the rule. This is because they could not be sold without affecting the business operations of a wireless company.

The Department conceded that the statute controls the exemption for the listed items such as goodwill. However, the court stated the Department could not save invalid rules by declining to enforce them according to their terms. Thus, the court accepted the taxpayers' argument that the listed items provide examples of the scope of the exemption, and if even a listed item would not satisfy the rule, it must be too restrictive.[10]

The most objectionable provision of the Department of Revenue's rule—subparagraph (b)—may have resulted from an attempt to address two aspects of intangible property valuation and exemption that have troubled both tax administrators and the courts.

First, as noted above, when is an intangible actually a property interest, as opposed to an attribute that affects the value of taxable property?

Second, even if a property right satisfies the definition of "property," can its separate value be determined and deducted from the taxpayer's unit value when it is necessary to put the tangible assets to beneficial use?

The Department's position effectively was that intangibles necessary for the business simply "enhance" the value of the tangible property, or are so integral to the business enterprise that they cannot be excluded in the unit valuation. Indeed, the appraisal handbook adopted by the Montana Department indicates that, "Given the nature of unitary valuation, dividing up the unit in order to exempt certain assets is problematic at best, and is contrary to the basic unit concept."[11]

The procedure used by the Department essentially represents the view that the unitary concept trumps the intangible property exemption.

The Montana Supreme Court rejected both arguments either explicitly or implicitly in *Gold Creek*. The California Supreme Court also addressed those issues recently, and although it also rejected these arguments for the most part, it allowed the valuation of certain intangible assets in the income approach with an analysis that has troubling implications for centrally assessed taxpayers.

The California Case—*Elk Hills Power v. Board of Equalization*

California has been a leader among states in the recognition of the intangible property exemption and in adopting appraisal principles to exclude such property from unit valuation.[13]

The California legislature codified the holding of *GTE Sprint v. Alameda County*, and the Board of Equalization developed the country's best analysis of intangible valuation in Section 502 of the *California Assessor's Handbook*, Chapter 6.[14]

In *Elk Hills*, the California Supreme Court applied this authority to a complex issue involving an unusual intangible asset. While purporting to remain faithful to the statutory requirements in holding that this intangible asset could not be added to value in the cost approach, the court paradoxically held that it need not be excluded in the income approach.

The assets in question are known as emission reduction credits (ERCs). These credits are creatures of California state law. The ERCs must be obtained in order to qualify for construction of a power plant, but unlike most types of permits, they are transferable and have a saleable value.

The court summarized the law applicable to the treatment of these ERCs as follows:

> Sections 212(c) and 110(d) prohibit the direct taxation of certain intangible assets and rights, including the ERCs in this case. However, in assessing taxable property under section 110(e), the Board may "assum[e] the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use."[15]

These three statutes correctly identify generally accepted valuation principles, as recognized in *GTE Sprint*. First, in valuing tangible property as part of a business enterprise unit, an appraiser may assume the presence of intangible assets necessary to put the tangible property to productive use. Second, the intangible assets themselves must be removed from the unit value. Finally, any "enhancement" that occurs as a result of all the property operating together is not taxable.

An example is helpful to illustrate these principles. Let's assume a taxpayer company owns tangible assets that have a $5 billion value "in use" in the business but have a $4 billion "scrap" value. In addition, there are intangible assets or rights necessary to the operation of the tangible assets and the business that are worth $3 billion. Let's assume the value of the taxpayer business enterprise, reflecting the earnings capability of all these assets working together, is $10 billion.

In this example, the value of the taxable assets should be $5 billion. The value is higher than the $4 billion liquidation value. This is because the intangible assets or rights allow the tangible assets to operate in their most productive use. That extra $1 billion is the first level of "enhancement," and it is taxable even though it is attributable in some way to the influence of the intangible assets or rights that allow the business to operate as a going concern.

However, the $10 billion taxpayer business enterprise value is $2 billion higher than the sum of the tangible assets ($5 billion) and the intangible assets ($3 billion). This extra $2 billion is a second level of "enhanced" value that should not be taxed. It is the equivalent of goodwill, which in some states is not specifically included as an exempt intangible asset.

The court in *Elk Hills* ruled that ERCs are not a form of property.[16] In many states, that recognition would have ended the case. That is because, usually, only intangible property is exempt, not intangible "rights."

Although it was not important to the outcome of the case, the court was probably incorrect in concluding that the ERCs are not a type of property. The ERCs share all the normal characteristics of property, including the capability of being specifically identified, valued, and transferred to another party.[17]

In any event, California's exemption is broader than those of most states; the exemption applies to intangible property and "rights." Nevertheless, the taxing authority asserted that the presence of ERCs was necessary to the operation of the unit, and so should be taxable pursuant to Section 110(e). The court rejected that argument:

> The Board argues that its site-specific adjustment for ERCs and other "soft costs" is not direct taxation, but rather

an appropriate assessment of the plant, assuming the presence of the intangibles that are necessary to its productive use. However, there is a meaningful difference between assuming the presence of an intangible asset and adding value to the unit whole to account for the presence of that intangible asset. (See, e.g. *Shubat, supra*, 13 Cal.App.4th at p. 804 ["While we agree intangible values *may be reflected* in the value of a possessory interest, it does not follow such values are subsumed as a matter of law."].)[18]

This conclusion is consistent with the principles outlined above. In the example, we assumed there are intangible assets or rights worth $3 billion, which add value to the taxpayer's unit. This is because they allow the taxpayer's unit to operate as a going concern.

However, the assets are still intangible. And, because the assets are exempt, they should not be added to the taxable value in a "bottom up" valuation such as the cost approach. We also assumed that because of those intangible assets, the value of the tangible assets was enhanced above its liquidation value. The court would have properly allowed taxation of this element of value.

The same principles would require that the value of the intangible assets be deducted in the "top down" valuation analysis used in the income approach. If the asset or right is intangible, and it is capable of being valued as the ERCs apparently were, then the value of the asset or right should be deducted from the unit value.

However, here the court appeared to diverge from a consistent and conceptually sound analysis. The court recognized two separate types of intangible assets—those which can be valued and deducted in the income (and presumably market) approach, and those which cannot. The court reasoned that, "under an income stream approach, not all intangible rights have a quantifiable fair market value that must be deducted."[19]

The court divided intangible assets and rights between those which "make a direct contribution to going concern value as reflected in an income stream analysis," and those which make an indirect contribution such as ERCs "which merely allow for the taxable property to generate income when put to its beneficial or productive use."[20]

Later, the court described the former category of intangible assets as "intangibles related to enterprise activity."[21] The court suggested that the category of intangible assets that make an indirect contribution, and are not related to "enterprise actively," was not exempt in the income approach.[22]

A Critique of *Elk Hills*

Although the *Elk Hills* decision should be viewed as a substantial taxpayer victory, the court introduced unnecessary confusion and the potential for future conflict in applying the intangible asset exemption in unit valuation approaches other than the cost approach.

First, it is unclear whether the court meant that some intangible assets could never be exempt in these approaches, or that the evidence was simply not sufficient to show the value in that case. At one point, the court suggested there was an evidentiary reason for distinguishing between "direct" and "indirect" contributions, at least in that case. Thus, the court stated the issue was whether the intangible asset has a "quantifiable fair market value,"[23] which is a question that should be subject to proof and expert opinion.

The court ruled that "Elk Hills has not articulated a basis for attributing to the surrendered ERCs a separate stream of income related to enterprise activity, or indeed any separate stream of income at all." Again, this judicial comment suggests a failure of proof on this issue. And, this suggests that a taxpayer could obtain deduction of ERC or related intangible asset value in the income approach with sufficient evidence of its value.

On the other hand, the court suggested that for assets of this character, where a contribution is "indirect," it will never be appropriate to deduct a value from the unit. Either the asset is "related to enterprise activity," or it is not. The court noted that, apparently, Elk Hills had presented evidence on the value of the ERCs.[24]

However, the court rejected that evidence because of the nature of the ERC intangible asset. The court gave examples of "enterprise activity" intangible assets: goodwill, customer base, favorable franchise terms or operating contracts, patents and copyrights, and assembled work force.[25]

For examples of intangible assets that make an indirect contribution, it cited cases holding that FCC licenses and landfill use permits were not exempt.[26]

To the extent *Elk Hills* can be read to permit taxation of intangible assets if their income contribution to the enterprise is "indirect," the decision is unsound.

First, it is inconsistent with the court's determination that the value of the intangible asset or right could not be added to taxable value in the cost approach. In other words, if an asset qualifies as an intangible asset in the cost approach, and assuming it can be valued, there is no reason why the result should be any different in the income or market approach.

Second, the inquiry into whether a contribution is direct or indirect is elusive, and ultimately unnecessary and irrelevant. It was undisputed in *Elk Hills* that ERCs were necessary to the operation of the business. This would suggest they had a direct effect on enterprise value. How much more direct could the effect of an asset be if no income could be produced without it?

One could argue that this "but for," or "all or nothing" test is exactly what the court was attempting to use as a basis for distinguishing assets that produce discrete amounts of revenue from those that are necessary for the entire business operation.

If an intangible asset is actively used in the business and produces incremental revenue, one could argue the state is better able to identify discrete revenues or cash flows to deduct in the income approach.

In contrast, if the intangible asset's presence is necessary for any income to be generated, then it is impractical to deduct income attributable to the intangible asset, since on a "but for" basis, *all* the income is attributable to the asset.[27]

Accordingly, it was arguably correct for the court in *Elk Hills* to hold that an income approach deduction would not be allowed for intangible rights when there is no specific income attributable to those rights. However, that should not be the end of the analysis.

The court failed to consider that the exemption for ERCs could be recognized in ways other than deducting a stream of income associated with the intangible asset.

It was undisputed in the case that the ERCs were transferable, and apparently they had value.

Accordingly, the value of the intangible asset could have been determined using methods other than an income approach, and deducted from the correlated value. This step would have addressed the court's concern in the income approach with those intangible assets that do not have an identifiable income. And it would have avoided the obvious inconsistency in the court's logic that an asset is exempt in one approach but not the other.

It is common for state appraisers to make a bottom-line deduction for the value of intangible or other exempt property, *after* the relevant valuation approaches are considered and correlated.

For instance, pollution control equipment is exempt from property tax in many states, and states typically include the cost of the equipment in the cost approach and make no specific deductions in the income or market approaches. Then, after correlating the three approaches into a single unit value, the appraiser deducts the value of the equipment, often using a market-to-book adjustment.[28]

The practice of making the deduction for exempt property after the correlation process is so widely recognized that it is recommended as the preferred method in two appraisal guides used by some state appraisers.[29]

"It is counterintuitive to conclude that assets of this value and importance are not operational assets related to the 'enterprise activity.'"

One other problem with the court's analysis in *Elk Hills* is the suggestion that FCC licenses for wireless telecommunications companies would be among the intangible assets that provide only an "indirect" contribution to the income being generated. It is true that such FCC licenses are necessary for any wireless company to operate.

However, the FCC licenses cover discrete territories and/or band-widths, and most wireless companies own many licenses to provide service around the country. Accordingly, there are discrete income streams associated with each license. Also, the assets are operational to the same extent as cell towers: each allows the company to transmit signals over a specific geographical area.

Finally, the costs of FCC licenses are much higher than permits or rights that merely allow a company to operate or to build or operate a plant. Indeed, they comprise a substantial portion of the total business value.[30]

It is counterintuitive to conclude that assets of this value and importance are not operational assets related to the "enterprise activity." Wireless licenses can be transferred and are sold from one user to another, and there is no logical basis for not excluding them from taxation the same as any other intangible asset.

The court cited *Los Angeles SMSA Ltd. Partnership v. State Bd. of Equalization*,[31] as support for its use of FCC licenses as an example of "indirect" intangibles. In that case, a division of the California Court of Appeals did hold it was not necessary to deduct FCC licenses from taxable value. But that holding effectively adopted the taxing authorities' "enhancement" argument, which was later rejected in *GTE Sprint* and ultimately disapproved in 1995 statutory amendments.

Under the law since 1995, and consistent with sound valuation principles, an intangible may enhance the value of the tangible, taxable property, but still must be excluded from the unit value. Consider the example used earlier, with specific reference here to FCC licenses and cell towers and related equipment:

> Assume a company owns cell towers and equipment that have a value "in use" in the wireless business of $5 billion, but have "scrap" value of $4 billion. In addition, there are FCC licenses and other intangible assets or rights that are necessary to the operation of the tangible assets and the business, and are worth $3 billion. The value of the business enterprise, reflecting the earnings capability of all these assets working together, is $10 billion. In this example, the value of the cell towers and equipment should be $5 billion. The value is higher than the liquidation value of $4 billion because the intangible assets or rights allow those tangible assets to operate in their most productive use. That extra $1 billion is "enhanced" value that is taxable even though it is attributable in some way to the influence of the intangible assets or rights that allow the business to operate as a going concern. However, the business enterprise value of $10 billion is $2 billion higher than the sum of the tangible assets ($5 billion) and the intangible assets ($3 billion). This extra $2 billion is "enhanced" value that should not be taxed. It is equivalent of goodwill.[32]

Even if FCC licenses were to be considered the type of "indirect" intangible asset suggested in *Elk Hills*—because they arguably do not generate a discrete income stream—they should be excluded from tax. This is because they are capable of being valued at the end of the appraisal process. FCC licenses are frequently traded, and there is an ascertainable value that can be deducted from the unit value *after* the correlation of the results from the relevant valuation methods.

Synthesis of *Gold Fork* and *Elk Hills* and Conclusion

The *Gold Fork* and *Elk Hills* cases each deal with issues arising from the definition of intangible property or rights, and the extent to which they must have characteristics separate from the unit.

Must intangible assets be capable of being owned and used separately from the unit? In *Gold Fork*, the Montana Supreme Court held they do not, due in part to the fact that the exemption statute listed goodwill as an example. In *Elk Hills*, the California Supreme Court agreed: even if an intangible asset is necessary to the operation of the taxpayer's unit, it must be excluded from value.

A separate but related question is whether an intangible asset must be capable of generating its own discrete income in order to be excluded in the income approach?

Stated differently, if an intangible asset is necessary to the operation of a business, it likely will not have an identifiable income stream, so does that mean it cannot be exempt under this approach? The Montana Supreme Court implicitly rejected this notion by holding that a rule was invalid that excluded "necessary" intangibles from the exemption.

In contrast, the California court indicated there must be a "direct" relationship between the intangible and the business enterprise in order to qualify an intangible asset for deduction in the income approach. However, the court did not carry its analysis far enough (or perhaps the issue was not presented). It is logical that there may be no discrete or incremental income attributable to a "necessary" intangible, since all income will be lost without the presence of that intangible. Thus, there may be no specific amount that can be deducted in the income approach.

However, this situation simply requires the intangible asset deduction to be taken in a different way. The intangible asset exemption can and should be recognized at the end of the appraisal process, by deducting the intangible asset value from the unit value after all the relevant methods have been correlated into a single value.

In this way, unit valuation principles are followed, requiring the consideration of all intangible assets needed for valuation of the property in its highest and best use in the taxpayer's business enterprise. But the legislature's mandate to exempt intangible property can also be respected.

Notes:

1. 310 P.3d 533 (Mont., Sept. 24, 2013).
2. 304 P.3d 1052 (Cal., Aug. 12, 2013).
3. See generally R. Smith, "Is the Unit Approach Viable? A Legal Perspective," 10 *Journal of Property Tax Assessment and Administration* (Issue 2, 2013); R. Smith, "A Critique of "Enhancement" and Other Theories for Taxing Intangibles," 14 *Journal of Property Valuation and Taxation* 18 (Fall 2002). As discussed in these articles, the unit method traces its roots, and validation, to the famous case of Adams Express Co. v. Ohio State Auditor, 165 U.S. 194, 221-22 (1897), aff'd after rehearing, 166 U.S. 185, 218-20 (1897). See also State Railroad Tax Cases, 92 U.S. 575, 616 (1875). In Adams

Express, the U.S. Supreme Court held it was not a constitutional violation for states to tax intangible property:

> Now, whenever separate articles of tangible property are joined together, not simply by a unity of ownership, but in a unity of use, there is not infrequently developed a property, intangible though it may be, which in value exceeds the aggregate of the value of the separate pieces of tangible property. Upon what theory of substantial right can it be adjudged that the value of this intangible property must be excluded from the tax lists, and the only property placed thereon be the separate pieces of tangible property?

166 U.S. at 219-20. It is noteworthy that the state of Ohio did not exempt intangible property, so statements like these do not reflect what is now a statutory directive to exclude intangible property in states where that property in exempt.

4. This growth in the value of intangible property was well underway even in 1897, when the Supreme Court made the following observation in the Adams Express case: "In the complex civilization of today a large portion of the wealth of a community consists in intangible property, and there is nothing in the nature of things or in the limitations of the Federal Constitution which restrains a State from taxing at its real value such intangible property. . . ." 166 U.S. at 218.
5. 32 Cal. Rptr. 2d 882 (Cal. Ct. App. 1994).
6. Beaver County v. WilTel, Inc., 995 P.2d 602, 611-12 (Utah 2000).
7. 310 P.3d 533 (Mont., Sept. 24, 2013).
8. MCA § 15-6-218.
9. Administrative Rules of Montana 42.22.101(12).
10. The court identified "assembled work force" and trade names as additional examples of intangible property that met the statutory definition but did not satisfy the new rule. And it noted that "the Department's distinction between intangible property and intangible value appears to sweep up goodwill, as goodwill is often defined by is ability to make excess revenues over the normal rate of return." 310 P.3d at 537.
11. *Appraisal Handbook, Unit Valuation of Centrally Assessed Properties*, p. VI-2, Western States Association of Tax Administrators – Committee on Centrally Assessed Property (August 2009) ("WSATA Handbook"), p. VI-3. The Montana Department's requirement that necessary intangibles cannot fall within the definition of "intangible personal property" actually goes beyond the explicit standards set out in the WSATA handbook, which states that for a intangible to constitute "property," "it must be clearly and separately identifiable; . . . it must be capable of being valued; and . . . it must be capable of being sold separately and apart from the unit." Id., p. VI-4. Thus, there is no requirement that if the intangible is sold separately, its absence cannot affect the operation of the unit.
12. 304 P.3d 1052 (Cal. Supreme Court, Aug. 12, 2013).
13. See R. Smith, "A Critique of 'Enhancement' and Other Theories for Taxing Intangibles," 14 *Journal of Property Valuation and Taxation* 18 (Fall 2002).
14. http://www.boe.ca.gov/proptaxes/pdf/ah502.pdf
15. 304 P.3d at 1056. Section 212(c) provides: "Intangible assets and rights are exempt from taxation and, except as otherwise provided in the following sentence, the value of intangible assets and rights shall not enhance or be reflected in the value of taxable property. Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use." Section 110(d) provides in relevant part: "Except as provided in subdivision (e), for purposes of determining the 'full cash value' or 'fair market value' of any taxable property, all of the following shall apply: [¶] (1) The value of intangible assets and rights relating to the going concern value of a business using taxable property shall not enhance or be reflected in the value of the taxable property. [¶] (2) If the principle of unit valuation is used to value properties that are operated as a unit and the unit includes intangible assets and rights, then the fair market value of the taxable property contained within the unit shall be determined by removing from the value of the unit the fair market value of the intangible assets and rights contained within the unit." Section 110(e) provides: "Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use."
16. 304 P.3d at 1066, n. 7.
17. See, e.g., Roehm v. County of Orange, 32 Cal. 2d 280 (Cal. 1948) ("Although a liquor license is merely a privilege so far as the 283*283 relations between the licensee and the state are concerned, it is property in any relationship between the licensee and third persons, because the license has value and may be sold"); Dodds v. Shamer, 339 Md. 540 (Md. Ct. App.1995) ("We have recognized that property is a term that has broad and comprehensive significance; it embraces "'everything which has exchangeable value or goes to make up a man's wealth—every interest or estate which the law regards of sufficient value for judicial recognition'"); Boss Co., Inc. v. Bd. of Com'rs of Atlantic City, 192 A. 2d 584 (N.J: 1963) ("Thus, the liquor license is a legal interest in the nature of an economic asset, created and protected by statute, and because it has monetary value and is transferable, either by consent of the licensee or by operation of law (in the special statutorily-described sense), it possesses the qualities of property"). See generally. Reilly and Schweihs, *Guide to Intangible Asset Valuation* 3-4 (AICPA

ed. 2013) (discussing necessary characteristics of intangibles as property interests); Reilly and Schweihs, *Valuing a Business* 325 (4th ed. 2000).

18. 304 P.3d at 1066.
19. 304 P.3d at 1067.
20. Id.
21. Id. at 1068. The court used this phrase twice.
22. Presumably, this logic would require that these intangibles would also not be exempt in the market approach, since their discrete contribution to value might not be determinable. The same "but for" or "all or nothing" principles might be applied.
23. Id. at 1067. The court used that term twice.
24. See id. at 1068: "Elk Hills purports to have produced evidence showing that the ERCs had independent value that had to be deducted from total income generated by the powerplant, using the Board's own method of unitary valuation."
25. Id. at 1067-68.
26. Id. at 1067, citing Los Angeles SMSA Ltd. Partnership v. State Bd. of Equalization (1992) 11 Cal.App.4th 768, 774-778, 14 Cal. Rptr. 2d 522 (1992); American Sheds, Inc. v. County of Los Angeles, 66 Cal.App.4th 384, 388, 78 Cal. Rptr. 2d 58 (1998).
27. This "but for" analysis highlights a difference between intangible property on the one hand, and rights or privileges that do not have all the characteristics of property. A right or privilege may be granted for a building permit or a license to conduct business, for instance, and without such threshold rights, a business cannot operate and no income can be generated. However, there is no separate value associated with such assets, and no separate stream of income that can be associated with them other than all the income of the business on a "but for" basis.
28. See PacifiCorp, Inc. v Department of Revenue, 31 P.3d 64 (2001). For instance, assume the exempt property has a book value of $1 billion; and assume the total cost approach value is $10 billion and, after correlating with the income and market approaches, the unit value is $8 billion. The ratio of market value to book value is 80 percent, and so 80 percent of the exempt value is deducted, or $800 million in this example.
29. See WSATA Handbook, supra note 11, at VI-4; National Conference of Unit Value States, *Unit Valuation Standards*, at ¶¶ VI-4, 1.F.3.
30. For instance, in the most recent Annual Report for Verizon Communications, as of December 31, 2012, the company reports a book value for FCC licenses of $77.744 billion, almost as much as the value for all tangible property, plant and equipment ($88.642 billion), and the latter figure includes all of the company's wireline assets. See p. 52, at the following web address: http://www.verizon.com/investor/app_resources/interactiveannual/2012/downloads/12_vz_ar_financial.pdf
31. 11 Cal.App.4th 768, 774-778, 14 Cal. Rptr. 2d 522 (1992).
32. The view that intangible assets like FCC licenses, goodwill, and customer relationships must be excluded from any "enhancement," regardless of the method used, is supported in a 2011 decision of the Utah Supreme Court. In T-Mobile, the court reasoned as follows:

    > Intangible assets such as "synergy value" and "customer base" are associated with the business being conducted on the property; they are not directly attributable to tangible property. See Shubat v. Sutter Cnty. Assessment Appeals Bd. No. 1, 13 Cal.App.4th 794, 17 Cal.Rptr.2d 1, 7 (1993) ("[I]ntangibles such as going concern value or franchise rights relate to the business being conducted on the real property. They relate to the real property only in their connection with the business using it."). And while assets associated with the business being conducted on the property, such as customer base and "going concern value," can enhance tangible property, it does not follow that these assets constitute enhancement value. See id. at 6. Rather, to the extent that accounting goodwill includes enhancement value attributable to T-Mobile's tangible property, that value is reflected in the value of the physical property itself and can be captured by a unitary method of appraisal. See WilTel, 2000 UT 29, ¶¶ 7, 36-41, 995 P.2d 602 (indicating that intangible value that is captured in a unitary appraisal is directly attributable to tangible property and is not required to be deducted from the appraisal); see also Shubat, 17 Cal. Rptr.2d at 7 ("Intangible values ... that cannot be separately taxed as property may be reflected in the valuation of taxable property." (alteration in original) (internal quotation marks omitted).

    T-Mobile USA, Inc. v. Utah State Tax Com'n, 254 P. 3d 752, 764 (Utah 2011) (footnotes omitted).

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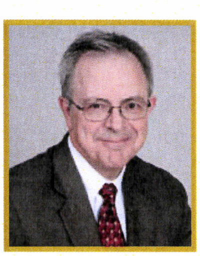

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