

**STATE BOARD OF EQUALIZATION  
OPEN MEETING  
MINUTES OF MEETING HELD AUGUST 18, 2021**

In attendance: Commissioners Tom Katsilometes, Jeff McCray, Elliot S. Werk, and Janet Moyle; Maria Young, Phil Skinner, George Brown, Rick Smith, Jerott Rudd, Brett Jarvis, Nathan Nielson, Tom Arkoosh, Alan Dornfest, Matt Virgil.

Commissioner Katsilometes, Chairman for the State Board of Equalization, reconvened the State Board of Equalization for 2021 (Board) at 9:00 a.m. August 18, 2021. This morning, Mr. Rick Smith, Attorney representing Lumen Technologies, Inc. will deliver his closing remarks on Lumen Technologies, Inc., heard August 17, 2021.

Mr. Smith said this case is one of the most obvious cases he's seen in his experience where an adjustment needs to be made. Mr. Rudd spent much time yesterday talking about capitalization rates. Mr. Smith will discuss obsolescence and the weighting to be given to the cost approach. That is where he believes staff do not have good explanations.

It was clear from the state's presentation that they do the same thing for Lumen that they do for every telecommunication company. One example in their testimony was that the Beta used for everyone is 0.91, but the Beta for Lumen is 1.0, which is different than the industry capitalization rate. That is a problem. On the normalization issue, which is because Lumen has been receiving subsidy for the Connect America First program that is scheduled to end in 2021. The response was that the state isn't sure it will end. He found those comments and concerns about the normalization to be speculative. Commissioner Werk said he heard from staff yesterday that it isn't the continuation of funding, but that the funding created a huge asset the company utilizes into the future. Mr. Smith said that isn't his understanding. The model already reflects the additional revenue that would be earned. Part of it is that those assets have already been generating revenue and is reflective in the revenue picture.

Normalization isn't a big issue in this case. The real issue is obsolescence and the weighting between income and cost. There was overwhelming evidence that a good part of Lumen's assets are obsolete. The unused capacity doesn't have the value it would if those were revenue-producing assets. He heard no evidence that contradicted that. Mr. Smith discussed the cost approach and its applicability to this case. All the authorities say the income approach should be used. Lumen knows they have 70 – 80% of the system that isn't generating any revenue at all. They know there are substantial cost figures on the books that related to the copper pairs that is just sitting in the ground and will likely never be used again. There are serious problems with the cost approach for a telecommunications company like Lumen. Perhaps the state has a practice of using the 50%/50% weighting for telecommunications companies, but this evidence shows that is wrong.

Mr. Smith noted this state has authorized obsolescence in the past. He mentioned the PacifiCorp case and he is sure the Western States Association of Tax Administrators (WSATA) manual was cited in that case as authority for the proposition that adjustments are not made in a cost approach, because that is what the WSATA manual says. The District Court in the PacifiCorp case was not convinced by that. Appraisals are supposed to be adjusted to provide the best result and then go to the reconciliation process to decide how much weight to give to the corrected, or modified, approach. That is what the District Court affirmed in the PacifiCorp case and the Supreme Court

affirmed that decision. That was a different type of obsolescence. There is also precedent for this Board to use an in-utility method. Another example of the in-utility calculation is one that staff do for small power-producers. He detailed the method for the Board. The simpler alternative is to just change the weighting of the cost and income approaches to something other than 50%/50%. The answer to the question yesterday about why the weighting is 50%/50% was “because that is what has always been” done and that isn’t a very good answer.

Mr. Smith discussed the potential sale of Lumen assets compared to the net book value. There was no contradicting this point. The net book value is overstating the value of the tangible assets. He mentions the 2021 information to show what he views as desperation to find something to support a 50%/50% weighting for cost. If they are at 100% for small power-producers, given what must be less reliable financial information, how can they not be at 100% for a company like Lumen.

Mr. Smith reviewed the schedule he submitted as part of the prehearing memorandum. Mr. Chikolwa used the state’s process to arrive at the same totals, then used 75% for income and 25% weighting for cost, getting to \$199 million, then the 100% weighting to income. If he were a commissioner, this would be the most logical way to provide relief in this case given the overwhelming evidence that there is obsolescence and that the cost approach has been overweighted by the staff. If there is no obsolescence adjustment, then they cannot justify giving the cost approach even 40%. He would urge the Board to adopt one of the two alternatives: either 75% weighting to income or 100% weighting to income. He knows it is hard for the Board to not agree with staff, but he believes staff has given them that invitation by saying they’ve just always used the 50%/50% weighting. The Board doesn’t want to project the image they are just “rubber-stamping” staff and trusts the Board will review this objectively.

Commissioner Moyle commented that if staff hasn’t made an error, and there’s nothing she can find that is erroneous as appraisals are extremely subjective, so she doesn’t like the statement that the Board would “rubber-stamp” staff. She finds it a little rough. Mr. Smith apologized saying he didn’t mean to suggest that is all the Board does. He worries that is what happens in Property Tax appeals throughout the country. He didn’t mean to cast any aspersions on this Board. Brett Jarvis was recognized to speak and said the question before the Board today is the four questions in the appraisal. The sole issue before the Board is the valuation.

Commissioner Werk said he wants to fully understand the issue of obsolescence. He has heard very strongly from the appellant and reasonably strongly from staff. He understands there is copper that will not be used. On the state’s side, he heard the discussion about the historical cost-less-depreciation (HCLD) and that the copper is included in that evaluation. Mr. Rudd explained the HCLD again and the reason they don’t feel additional obsolescence is appropriate. He reviewed the approaches and values again. He believes the way they have calculated this is in the best interest of the taxpayer. Commissioner Werk noted he questions the state’s weighting. Mr. Smith is asking for a change and he wants to understand staff’s approach to the weighting. Mr. Rudd explained staff’s rationale.

Commissioner Moyle also has issues with the weighting. She spoke with Mr. Rudd this morning and asked him to re-run the appraisals using 60%/40% weighting with a Beta of 1.0. Conducting mass appraisals is hard. Mr. Rudd said he hasn’t had an opportunity to complete that yet, and said that by changing the Beta, it will change the yield rate. Commissioner Moyle said they know, based on their information, that the Beta is 1.0 and she would like to see those numbers. Mr. Rudd noted Commissioner Moyle has a good understanding of mass appraisal. He explained that in mass

appraisal of operating property, they try to develop a yield rate study that can be applied to every taxpayer in that industry. If they go to an approach of developing something specific for each company, then that takes away from the need for mass appraisal. He understands and is happy to provide those numbers. If taxpayers can change something in the mass appraisal for their company though, he anticipates several taxpayers requesting the same. Commissioner Moyle understands the complexities and the frustrations.

Mr. Smith asked to be recognized to respond to Commissioner Werk's questions. He endorses Commissioner Moyle's statements. It isn't sufficient for staff to have to be able to defend and justify its values simply because it's a mass appraisal process, and these imperfections are a part of the mass appraisal process. They are here today to find value and eliminate as many imperfections as possible. Mr. Smith responded to Mr. Rudd's response to Commissioner Werk about the 50%/50% weighting. Commissioner Werk asked about mass appraisals. He asked Mr. Skinner if there is a statutory construct to the mass appraisal that is being done by staff. Mr. Skinner said he will research and provide a response later today. Commissioner Werk said the reason for the question is that Commissioner Moyle has asked for an adjustment and staff responded that if they do that for every company they will be buried in requests for the same. Commissioner Moyle said it was staff's data that prompted her to ask for the adjustment. Staff knows the Beta is 1.0 and that is the only reason she asked. Mass appraisals are done until there is an appeal. Once there's an appeal, then staff can go more deeply into the numbers. Mr. Skinner read Idaho Code section 63-407. Every person has a right to a hearing and assessment on his property. Mr. Rudd said he didn't want it to be perceived that the taxpayer doesn't have a right to come before the Board of Equalization and talk about their specific company information. He was describing the method used. He respects the taxpayer's right to appeal and to talk about their specific details. Commissioner Werk clarified Commissioner Moyle's request: she asked staff to apply a Beta of 1.0 and apply that to a 60%/40% split meaning 60% income to 40% cost; then see what that value is. She said that is correct, but she also asked staff to use a 75%/25%. She doesn't have an issue with the yield rate, but by changing the Beta, the yield rate will also change. Commissioner Katsilometes asked how long it will take to get the information Commissioner Moyle has requested. Mr. Rudd said it should take about an hour.

Commissioner McCray asked that the Lumen presentation continue after lunch. Commissioner Katsilometes requested Alan Dornfest, Property Tax Policy Bureau Chief, present the value comparison report, ratio study, and agricultural land compliance report. The Board recessed briefly.

The Board reconvened and heard Alan Dornfest's presentation. Mr. Dornfest noted that Matt Virgil, Senior Consulting Appraiser, is on the phone to provide more detailed answers for any questions the Board may have. Mr. Dornfest said the report before the Board is a compilation of abstracts and shows the comparison between last year and this year. This is taxable value and the percent change in those values for each category in each county. In some cases, staff identified areas of concern and members of the Board have identified concerns. Those are highlighted in the report before the Board. In some of the agricultural categories, there were very small changes. Mr. Virgil's response to that was that they did test for compliance, according to the rule, every agricultural land category (there is a report attached the ratio study) and there were no non-compliance issues. In some cases, there were zero changes, and they find that acceptable. Counties have discretion of how to apply tools of analysis and if they feel there is no change necessary and it's not out of compliance, they can leave those values alone. He deferred to Mr. Virgil who said if there are questions, he will respond, but he feels it is summed up in the report provided. Commissioner Werk said his concern is allowing those zeros to proliferate over the years. It is easy on an annual basis to allow it, but he wants to ensure we don't fall behind and years later discover that there is a massive adjustment.

Commissioner Moyle said part of the reason for using a 5-year rolling average was to alleviate Commissioner Werk's concern. Commissioner Werk clarified that it will just show change more slowly. Commissioner Moyle said that is correct. Mr. Dornfest replied to Commissioner Werk saying they are very sensitive to the zero changes, but the consulting appraisers are testing everything, in accordance with rules. Several years ago, there were no rules guiding them, so they added rules very similar to residential and with the same tolerances and parameters. Mr. Virgil said he shares the same concerns Commissioner Werk has mentioned. The counties are more in line now than they have been. There are comments attached to the report. In Gooding County, there were significant changes due to changes in their questionnaire. Commissioner Moyle asked questions related to the categories in Gooding County. Mr. Dornfest noted there is an addendum for certain agricultural land values. He read the addendum and said he doesn't feel there is anything improper in the values.

Mr. Dornfest thanked Commissioner Werk for his questions on the preliminary report. There were significant concerns in Bonner County. The county failed to update their values and that has been corrected. Something similar happened in Cassia County; the values are now corrected. There was an error last year. Commissioner Katsilometes asked why Bonner County didn't submit current values for this year? Mr. Virgil said they have now submitted the correct numbers, but he doesn't know why they submitted the previous years' numbers. The numbers before the Board are correct. There are new staff, so perhaps there was just confusion.

Mr. Dornfest presented the summary of equalization recommendations for 2021 property values. This year, when they did the ratio studies, they found 33 categories of property in 25 counties that were not in compliance. This is the largest number of categories out of compliance they have ever seen. The good news is, with the consulting appraisers working with the counties these last several months (the counties were notified in March) and were able to bring all the categories into compliance, so he has no recommendations to this Board for further changes. In the summary, the Board can see the current status. The consulting appraisers were asked to provide justifications for what happened. There is no evidence anyone is out of compliance with ratio study standards. Commissioner Moyle noted some category changes, moving commercial to residential. In new construction and a category change, are they making sure the counties aren't putting those category changes into the new construction roll? Mr. Dornfest said the counties have been advised through guidance notes, and the rules about what goes on the new construction roll and what doesn't. There were changes in the law this year, with House Bill 389, so they further advised of what is appropriate. For instance, in a change of land category, it was previously permissible to put the additional value right into the new construction roll. They made them aware, early in the process, that it was no longer permissible. He's had personal discussions with at least a couple assessors on that issue and they assured him they understood. Commissioner McCray asked if there is any insight about why those 25 counties were initially out of compliance. Mr. Dornfest said, in his opinion, it is due to the dramatic increases they've seen in values. Some counties may have been borderline in the previous year. Mr. Virgil added that he believes it is also partially due to inventory shortage in many of the markets, slow building, and increased demand. They did see an increase in sales prices and predominantly across the state an increase in sales by county; demand is high, and supply is short.

Commissioner Werk thanked Mr. Dornfest and all his staff for all their work. This has been a difficult year with the legislative changes, all the staff turnover in the counties. Consulting appraisers must constantly find balance and he wanted everyone to know how much he appreciates them all.

The Board recessed until 2:00 p.m.

The Board reconvened and resumed the Lumen Technologies, Inc. deliberations. Commissioner Moyle said she found the 60%/40% weighting interesting and it's almost the mid-point of the two parties. Her preference would be to accept the value of the 60%/40% weighting with the Beta change. Commissioner McCray said he is amazed at the complexities of these cases and appreciates all the hard work. He agrees, and it's been stated by the Board, that they need to disregard the 2021 article regarding the sale of assets as it has little relevance to these deliberations, and they need to disregard the discounted cashflow model since it wasn't presented for consideration. Regarding the issue of obsolescence, he is sympathetic to the taxpayer's challenge in the change of business, but his question is whether the assets are obsolete. It may not be in use right now, but that doesn't mean it has no purpose. They've discussed impairment, and there is a reason the bar for impairing assets is so high. If it's truly obsolete, why wasn't it impaired? He's struggling with whether to include that or not. With the analysis that Commissioner Moyle requested, he isn't inclined to want to change the Beta. The reproducibility is important to all taxpayers, and if we're sticking to our values of fairness, he would prefer to treat them all the same. The weighting can be addressed versus changing the Beta for a particular taxpayer with the method the Bureau is using; therefore, he would like to keep the Beta at 0.91 that was used for all the telecommunications industry. It is clear in the WSATA handbook that the HCLD is not a good indicator for public service companies that are not regulated unless it's new construction. The other element discussed is if the property rate is not a rate-based utility or there is lapsed regulation, then the indicator must be weighted accordingly. He is in favor of adjusting the weighting to the benefit of the taxpayer and is open to discussing that weighting. He is comfortable with the 75% income to 25% cost. Commissioner Werk shares many of the same concerns and is torn on whether to change the Beta. He said it feels the Bureau has used 50%/50% due to inertia and he is comfortable changing the weighting; he just isn't sure how much. He hasn't heard a reasonable explanation about why the Bureau is using the 50%/50% weighting. He is comfortable with the 60%/40% and not changing the Beta. The Board has not yet provided direction and they continued the discussion. Commissioner McCray said he is willing to accept the 60%/40% weighting. Commissioner Werk recommended keeping the Beta at 0.91 and asked the Bureau to prepare a decision with 40% weight to cost and 60% to capital income using all the other details that were in the Bureau's appraisal.

Mr. Skinner reminded the Board this is not the time for a vote but instruction for the decisions to be drafted. Voting will occur on Friday.

Commissioner Katsilometes asked for direction for the decision(s) to be drafted. Commissioner Moyle agrees with Commissioner Werk's recommendation but would also like a decision drafted with 60%/40% using a Beta of 1.0 as well as the Beta of 0.91. She said the two are almost identical. Commissioner McCray will support the proposals requested. Mr. Skinner will prepare the two draft decisions for the Board and the Board will vote on one of the two Friday. Mr. Rudd said if they don't know the value for Lumen until Friday, the certification may be delayed. Mr. Skinner said he can have the draft decisions available to the Board Thursday afternoon for discussion and recommendation for the final decision. The Board will convene Thursday morning to discuss the draft decisions for the non-utility generators (NUGs), then reconvene Thursday afternoon to discuss the draft decisions for Lumen Technologies, Inc. so the voting can take place on Friday, in accordance with the agenda. Mr. Rudd voiced the same concerns with the NUG cases. Commissioner Katsilometes said the Board will provide clear guidance Thursday afternoon for all the decisions, so the Bureau should have enough time to be prepared for certification of values on Friday morning, as indicated on the agenda.

Commissioner Katsilometes recessed the Board until 9:00 a.m. on Thursday, August 19, 2021.

Maria Young  
Secretary

Tom Katsilometes  
Chairman of the Idaho State Board of Equalization