

Industrial Properties Get Their Due

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Jun 1, 2008 12:00 PM

For over a decade, tax authorities in many jurisdictions have recognized that intangible assets and rights must be removed when assessing certain types of properties for tax purposes. This recognition of non-taxable intangibles has typically been limited to hospitality and retail properties, where intangible assets are easier to pinpoint.

Assessors often believe industrial properties consist of solely taxable real estate and personal property, and don't remove the intangible assets for valuation purposes. That could change, however, in the next few years, due to changes in financial reporting standards made earlier this decade, including the advent of FASB 141 and 142, which address the reporting treatment of intangibles acquired by publicly traded companies.

Gaining traction

As auditors have learned to apply FASB 141 and 142, the number and types of intangibles reported to regulatory authorities have increased. The above chart provides a few examples of the kinds of data industrial companies have begun to report to the Securities and Exchange Commission following large industrial plant acquisitions.

In each example, a portion of the purchase price paid was allocated to specific intangible assets and rights. For instance, Harvest Energy Trust allocated over \$118 million of the price it paid for a refinery in Newfoundland, Canada in 2006 to engineering drawings, marketing contracts and customer lists.

In the past, intangibles were usually reported along with property, plant and equipment and not delineated. Thus, assessors could not see the intangible assets much less understand their value. FASB 141 and 142 have changed that.

The identification of specific intangible assets by industrial companies in financial reporting of acquisitions represents a big step forward. It gives legitimacy to specific intangibles, both for the company reporting them and for other companies in the same industry.

Intangibles are exempted from taxation in a number of states. For example, in California, statutes, regulations and appellate court decisions exempt most industrial plant intangibles.

Property taxpayers who can identify and place a value on intangible assets and rights are entitled to exclude the value of those intangibles in determining their property's assessed value. Similar tax exemptions can be found in other states, such as Texas and Washington.

Doing the math

Once intangibles are identified, the amount of intangible value to be deducted from the property's total value must be determined. This is established by a review of comparable sales or a cash flow analysis. An appraiser should be retained to develop the valuation using the appropriate ad valorem tax standard.

For example, every industrial property has employees and a market expense to recruit and train can be estimated. This figure is an "avoided cost" to a buyer and represents the fair market value of that workforce for ad valorem tax purposes. The same technique can be used to value drawings, manuals and software.

Normally, property owners do not determine the value of intangibles by using the local property tax value standard. By valuing intangibles that way, the taxpayer derives a quantitative value for the tangible real and personal property that should be subject to property tax.

In most jurisdictions, the taxing authorities include in industrial property tax assessments the value of the real estate and the value of the intangibles, despite the fact that in many states intangibles are not taxable assets. Therefore, owners and operators of industrial properties need to follow these key steps:

- Determine how the taxing authorities appraise your properties for ad valorem tax value. If they include real estate and

intangibles in their assessment, take stock of the intangible assets and rights used in connection with your properties.

- Order appraisals for all the properties' intangibles, basing those appraisals on local ad valorem value standards.
- Present the facts to the taxing authorities and request that the value of the intangibles be excluded from the taxable value of your properties.

If you and the authorities cannot agree, file a tax appeal.

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INDUSTRIAL INTANGIBLES PROVE DIVERSE

New reporting requirements enable industrial property owners to call attention to intangible assets so they can be deducted from property valuations.

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>	Buyer	Acquisition price	Intangible assets	Intangible assets identified
2007	Western Refining	\$1.14 billion	\$68 million	Rights-of-way, customer relationships, paid-up technology, licenses and permits, trademarks
2007	Tesoro Corp.	\$1.81 billion	\$146 million	Air emission credits, software licenses; permits and plans, dealer supply agreements
2006	Harvest Energy Trust	\$1.38 billion	\$1.18 billion	Engineering drawings, marketing contracts, customer lists

Sources: Western Refining, Tesoro Corp., Harvest Energy Trust

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