

# Personal Property Manual



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## PART 1 – Fundamentals of Personal Property

This overview provides recommendations for defining, classifying, discovering, reporting, verifying, and valuing personal property for ad valorem tax purposes.

The purpose of this overview is to present methods that assessing officers can use to achieve uniform and equitable personal property valuations.

### 1.1 What Property Is Taxable for Property Taxes

In Washington State, all property is taxable unless it is specifically exempt. The authority to tax real and personal property is found in [RCW 84.36.005](#), which states:

*All property now existing or that is hereafter created or brought into this state shall be subject to assessment and taxation... excepting such as is exempted from taxation by law.*

In addition, Article 7, Section 1, of the [Washington State Constitution](#) defines property as:

*The word “property” as used herein shall mean and include everything, whether tangible or intangible, subject to ownership.*

### 1.2 Definition of Personal Property

All property can be divided into two major categories—real property and personal property. Real property includes land, buildings, structures, and affixed improvements generally classified as immovable, e.g., paving, fencing. ([RCW 84.04.090](#).)

Personal property ([RCW 84.04.080](#)) by its nature is not permanently attached and, therefore, is movable. The chief characteristic of personal property is its mobility. Whether an item is real or personal property in a particular situation usually can be determined by the intent of the owner and the means of attachment. If an item is affixed to the land so that it loses its original physical character and cannot be restored to its original condition as a practical matter, it loses its nature as personal property and becomes real property. Generally speaking, if an item can be removed without damaging either the item or the real property, it is personal property. For example, if a tenant installs a light switch in the wall, the wall could be damaged by its removal. Therefore, it may be real property. However, if a tenant places a sign on top of the roof, there is no intent of permanent installation, and the sign can be easily removed when the tenant leaves. The sign is personal property.

Personal property for the purpose of taxation falls into two categories—tangible and intangible. Tangible personal property is an item that has a physical existence.

Tangible personal property includes, but is not limited to, the following:

1. Office furniture and equipment, computers, software
2. Store equipment

3. Manufacturing equipment
4. Signs
5. Communication equipment
6. Professional libraries
7. Motor vehicles not subject to excise tax
8. Farm machinery and equipment
9. Leased equipment—videos
10. Small tools
11. Commercial watercraft
12. Leasehold improvements not part of realty
13. Building improvements on exempt land
14. Supplies not held for sale

Intangible personal property includes representations of rights to property. There exist rights and privileges for ownership but no physical existence. Intangible personal property includes, but is not limited to, the following:

1. Franchises
2. Patents
3. Prospecting or mining leases on public or private land
4. Public utility easements owned by public service corporations other than railroads

### 1.3 Discovery of Personal Property

The extent to which taxable personal property can be assessed depends upon its discovery. Disclosure of personal property is often contingent on initially identifying the owner of the property. Complete discovery depends upon adequate staffing, funds, and other necessary resources. Basic policies and standards governing the discovery of personal property are essential.

Some of the basic sources and tools available to the assessor in discovering personal property are as follows:

1. Personal property listing forms
2. Real property field appraiser reports and records
3. Physical inspections
4. Real Estate Excise Tax Affidavits
5. City and county business licenses
6. State business licenses—New and Closed Business Listing
7. Chamber of commerce memberships
8. New business listings from the news media
9. Building permits
10. Previous audits, accounting records and income tax returns

11. City directories, suburban cross-reference
12. Telephone directories
13. Public records: Uniform Commercial Code (UCC) reports, corporation charters
14. Classified advertisements
15. Web sites

Once the property has been discovered and the owner identified, the assessor establishes an account and a file for the business.

## 1.4 Reporting Personal Property

In an ideal world, appraisers would physically list individual personal property items. Time and personnel constraints, however, usually dictate the use of a reporting form that is completed by the taxpayer or his agent and is filed by the April 30 filing deadline for property as of January 1.

The personal property listing form calls for the taxpayer's listing of original costs by type of property and by year of acquisition. Some formats require the property owner to recalculate total acquisition cost for each category each year. There is, however, no itemized list that allows the appraiser to verify complete reporting on an item-by-item basis. This can create some problems. For example, a real property appraiser checking leasehold improvements cannot verify the listing without an itemization. A form allowing itemization minimizes many problems relating to additions, deletions, and categorization of assets.

If the form has special instructions and space for items such as leasehold improvements, work in progress, and leased equipment, some issues can be minimized even if the form does not allow for itemization.

## 1.5 Verification and Auditing

### 1.5.1 Authority

State statute gives the assessor or their representative the authority to examine the personal property, books, and records of the taxpayer. [RCW 84.40.340](#) says that the taxpayer shall furnish all information pertaining to property in this state to the assessor on request even if the records may be maintained outside this state.

### 1.5.2 Audit Program

The assessor should establish an audit program designed to facilitate the full and proper listing of all personal property in the county. It is the assessor's responsibility to assure that all property is being assessed and appraised on a uniform basis. In order to accomplish this task, the assessor's office must have the necessary staff, funds, and programs.

It is important to audit for the following reasons:

1. Ensure uniformity.
2. Ensure correctness of property listed

3. Ensure complete listing of all property.
4. Taxpayers will not always list correctly, whether through ignorance of law or misinterpretation of requirements.
5. Verify that the costs listed conform to office standards, i.e., cost includes freight and installation, but not sales tax.

Placing an emphasis on major accounts, accounts with significant changes from the previous year, accounts that have leased equipment, and accounts that are suspected of being improperly reported will maximize the effectiveness of an audit program. All accounts should be audited periodically. Remember that the purpose of an audit is to verify that all personal property items have been reported and that the information given is accurate. A physical inspection will help to verify the completeness of reports.

In determining whether all assessable items have been reported, special attention should be directed to standby equipment, permanently idled equipment, retired or fully depreciated equipment, and uninstalled equipment. Regardless of book values, such equipment must be listed and valued unless specifically exempted. The status of personal property as of the assessment date determines its assessability and situs for tax purposes.

To verify that all taxable property is reported, compare the total reported costs with those shown in the general ledger or balance sheet of the business. It is important that acquisition costs include charges for freight and installation and costs necessary to make equipment operational. Remember that sales tax is not taxable and should be deducted from the asset's total cost. In addition, the cost of an asset should reflect the gross cost before an adjustment for trade-in allowance.

Verify that leased items, of which the business is either lessor or lessee, have been properly reported and assigned to the correct party. If leasehold improvements exist, the appraiser must ensure that they are being assessed on either the real property roll or the personal property roll and not double assessed. When in doubt, assess the leasehold improvements as personal property. A double assessment can be fixed if one is made. Simultaneous review of real and personal property records can help assure an accurate assessment of leasehold improvements. An audit program that is carefully planned and managed and then properly executed is a tremendous asset to any county. The program usually is cost-effective and, if properly managed, gives credibility to the assessor's office.

A well-managed program will pay for itself through the discovery of omitted property and omitted value. Law requires that omitted property and omitted value be placed on the rolls for the current year and any previous year for which the omission was made up to a maximum of three prior assessment years.

## 1.6 Valuation

### 1.6.1 Valuation Techniques

The cost, income, and sales comparison approaches should be considered in the appraisal of personal property. The degree of dependence upon any one approach will change with the availability of reliable data. Certain types of personal property do not readily lend themselves to development of all three generally accepted approaches. In many instances, sufficient sales data of assets in use in a business is not available at the retail trade level, so more reliance may be placed on the cost and income approaches.

### 1.7 Sales Comparison Approach

The sales comparison approach may have limited application in appraising machinery and equipment used in businesses since sales of used items are generally few and are often liquidation sales, which are typically not representative of the market value at the retail trade level in use in a business. On the other hand, list prices, including delivery and installation costs, can be good indications of value when supported by the marketplace. Be sure that the property is valued at the proper trade level. Trade and cash discounts should be subtracted from the list prices, particularly if the equipment sold is still at the wholesale level of trade. If reliable sales data is available, the adjustment process can be applied in the same manner as in real property with one exception. Sales of comparable real properties usually have a positive adjustment for time because of appreciation. Since depreciation of machinery and equipment may outpace inflationary effects, sales of this type of property may require a negative adjustment over time, when inflationary effects and depreciation are combined.

### 1.8 Cost Approach

This is the most common and generally applicable approach for the valuation of personal property. Costs used in the cost approach can be historical and/or original acquisition, replacement, or reproduction cost, although often only original or acquisition costs are readily available for personal property. The cost approach provides an estimate of value based on the depreciated cost of the property. Total acquisition cost includes freight, trade-in allowance, installation, and any fees incurred to get machinery operational.

Any equipment acquired through lease purchase agreement should be assessed on the basis of the historical cost new, if possible. If that is not possible, be sure to add the value, if any, of the total payments made to the final payment, along with the down payment or trade-in, to account for the total original cost. The historical cost new or the acquisition cost including the value of the payments and other items are then trended and depreciated to reflect the current market value.

The appraiser must recognize that appraisal and accounting practices may differ in depreciating machinery. Accounting practices provide for recovery of the cost of an asset, while appraisal practices strive to estimate a value related to the current market.

The Department of Revenue supplies a percent good table for various rates of depreciation and guidelines for the counties to use in determining value. Using percent good tables is conducive



to a mass appraisal system. A percent good table, based on declining balance depreciation rates and trending factors are combined to create the combined percent good valuation table. A trending table tracks the price increases or decreases of specific types of equipment over time. They are available from a number of sources, such as Marshall & Swift and the U.S. Bureau of Labor Statistics. The Department of Revenue develops its own trend based upon data collected from monthly reports published by the Bureau of Labor Statistics and then averages the results with a Marshall & Swift trend for the average of all machinery and equipment.

A percent good table estimates a percentage of remaining value of an asset. A combination of the trend and percent good tables produces the Department's annual personal and industrial property valuation combined table.

The valuation table depreciates property to a minimum level of 15 percent for most types of property. This takes into consideration salvage or residual value as long as the equipment is in use; regardless of age or condition, it is considered to have value. This is the value-in-continued-use concept. The appraiser must be aware that the use of the tables will yield an estimate of value for equipment in average condition. When equipment has been subject to either excessive use or has been underutilized, the appraiser may want to make adjustments for condition. Experience and judgment are necessary when some types of equipment defy the tables. Documentation noting the reason for any variance from the tables is necessary to explain the variance in case the account is selected for a ratio audit.

## 1.9 Income Approach

The income approach produces an estimate of the present worth of income to be received in the future. Assessors use it only when adequate and reliable income and expense data can be obtained. Application of this method is usually limited to valuing leased equipment.

When using the income approach for valuing property, several items must be considered: the expected future income stream, the economic life of the property, and an appropriate market-based capitalization rate. Difficulties in both forecasting future income streams and deriving market-based capitalization rates often discourage appraisers from applying the income approach in valuing personal property and industrial machinery and equipment.

## 1.10 Trade Level

The appraiser must value taxable personal property at the retail trade level. All approaches to personal property valuation must take into consideration trade level, which refers to the production and distribution stages of a product. There are at least three distinct levels of trade: the manufacturing level, the wholesale level, and the retail level. Incremental costs (such as freight, overhead, handling, and installation) are added to a product as it advances from one level of trade to the next, thereby increasing its cost and value as a final product. Both the cost and value of goods will differ depending on the level of trade.

The positive in the trade level approach is that the property is being valued equitable, uniformly, and consistently with like properties regardless of ownership and/or cost as reflected on the accounting records.

## 1.11 Supplies

Supplies are stocks of goods intended to be consumed by the business or during the production process but are not part of the raw materials, i.e., inventory that is processed into the finished product. Examples of supplies include office supplies; hotel/motel bath soaps, shampoo, etc; beauty shop shampoo, hair color, etc., not separately billed to the client; chemicals; clothing; pallets; paper; fuels; and repair parts. Taxable supplies are those not held for resale. Inventory held for resale is exempt.

Value supplies at their acquisition cost, average inventory per month. (Annual supplies expense ÷ 12 may be used as the value when the average amount of supplies typically on hand is one month's worth.)

Construction in progress, commonly referred to as CIP or CWIP (Construction Work in Progress), is usually recorded at 100 percent of cost on records of the taxpayer. Items that should be considered by the appraiser in this area are as follows:

1. Construction in progress may include real and personal property.
2. Construction in progress will not be reflected in the fixed assets or equipment ledger of the taxpayer. In most cases, it is reflected on the balance sheet at full cost. Normally, it will not be journalized to a fixed asset account until the project or asset is finished.

Value construction in progress assets at 100 percent of cost until placed in service.

## 1.12 Leasehold Improvement

These are typically improvements made by a tenant to a leased structure, or they are improvements owned by a lessee and constructed on publicly owned property.

These improvements may include things such as interior partitions, carpeting, wiring, plumbing, floor covering, heating and air conditioning, signs, painting, or exterior improvements such as paving and fencing.

Leasehold improvements may be double assessed or omitted from assessment unless particular attention is paid to lessor and lessee asset values and real and/or personal property parcels and accounts. Leasehold improvements are found most commonly in shopping centers, restaurants, retail stores, public land, and office buildings.

Close coordination between the real property and personal property departments is necessary when assessing leasehold improvements. The tenant improvements should be classified carefully and assessed either as real or personal. Do not omit them from assessment. Values in excess of millions of dollars could be overlooked. It is recommended that these assets be valued as personal property of the tenant because they benefit the tenant directly. If they were paid for by the landlord, it is usually recommended that they be valued as personal property of the landlord rather than real property since in most cases they benefit only the tenant.

In some instances, leasehold improvements are assessed as real property because the improvements are of a permanent nature and remain with the lessor at the end of the lease. Generally, if the Marshall & Swift manual is relied upon for real property valuation, the cost factor accounts for basic floor covering, electrical, plumbing, air conditioning, and heating. All of these are common items listed as leasehold improvements.

Consideration should be made for signs, specialized wiring for machinery, light fixtures, and foundations for machinery as these items should be assessed as personal property. When at all possible, the owner should supply an itemized list so that the personal property appraiser can coordinate with the real property appraiser. The lease may be reviewed to determine how the improvements are classified, i.e., real or personal property. If at the time of lease expiration, the ownership of the leasehold improvements transfers to the lessor, assess the leasehold improvements as real property at that time. If at the time of lease expiration, the lessee retains ownership (usually being required to remove those improvements to return the real property to its original condition), assess the leasehold improvements as personal property.

However, assess unique tenant improvements that no other future tenant could or would use as personal property—even when they are affixed or when ownership of those improvements transfers to the lessor. Tenant-specific improvements rarely add value to the real property even if they are left behind when the tenant vacates. Nevertheless, the tenant does benefit from those improvements during the term of the lease; therefore, they are regarded as personal property. Additionally, if the improvement's life is less than the lease term, the lessee owes personal property tax. Improvements on public lands are always personal property.

The approach used to value leasehold improvements as real property should be in accordance with similar real property in your county. Value these assets as personal property based on the specific item and/or the life of the asset. This allows for uniformity and equalization.

### 1.13 Filing Deadline

Personal property must be listed by the taxpayer and filed with the county assessor on or before April 30. A postmark on or before April 30 is also acceptable.

Before January 1 each year, the assessor must mail, or electronically transmit, a listing form to persons at their last known address. Even if the assessor fails to send the listing form to the taxpayer, the taxpayer is still required to file the listing by the deadline. ([RCW 84.40.040.](#))

Every individual, corporation, limited liability company, association, partnership, trust, or estate shall list all personal property in his or its ownership, possession, or control which is subject to taxation pursuant to the provisions of this title. ([RCW 84.40.185.](#))

### 1.14 Filing Penalty

A penalty of 5 percent of the amount of tax (not to exceed \$50 per calendar day) is assessed for each month the listing is late. The maximum penalty is 25 percent. If the taxpayer fails to file a listing form due to reasonable cause and not due to willful neglect, the penalty may be waived. ([RCW 84.40.130.](#)) A reasonable cause policy is recommended to ensure fairness. Willful failure

to file can result in a 100 percent penalty; see WAC 458-12-110 – Listing of personal property by the assessor – Penalties for failing to list personal property and for making a false or fraudulent listing.

### 1.15 Listing Requirements

On the listing form, the taxpayer must include a description of the property, the cost of the item, and the year of acquisition. The cost should include freight and installation charges and consideration should be given for any trade-in value. The cost should not include sales tax. Example: A taxpayer purchased a new welder for \$5,000, which included \$250 for freight. There was no installation charge. Sales tax was charged on the \$5,000 bringing the total to \$5,400. The taxpayer should report \$5,000 as the acquisition cost. This includes the freight charges but excludes the sales tax.

### 1.16 Failure to File

In all cases of failing to obtain a statement of personal property, the assessor must determine the amount of and assess the value of all property. To do this without a listing form, the assessor must estimate the value of the personal property. In order to estimate the value of property, the assessor should:

1. Confirm the business is still operating in the county.
2. Inspect the business (if possible).
3. Make an itemized listing of the property. This can be as general as “restaurant equipment,” if specifics are not known.
4. Provide the taxpayer with a Notice of Estimated Assessment, Value, and Penalties.

When estimating the value of property, reasonable judgment must be used. Although it may seem like a good idea to overestimate, there are certain pitfalls associated with doing so. For instance: After receiving an estimate of the value of personal property that is in excess of the market value, the taxpayer files an appeal, and the value is lowered. Time and resources have been used for naught. If the levy setting process takes place using the overestimated value, and later the value is lowered, the taxing district loses budgeted tax dollars. Be reasonable, using your experience as judgment for the estimation. ([RCW 84.40.200](#).) Also, willful failure to file can result in a 100 percent penalty; see WAC 458-12-110 – Listing of personal property by the assessor – Penalties for failing to list personal property and for making a false or fraudulent listing.

### 1.17 Statement of Valuation

The assessor must send a statement of value (Notice of Value) to the taxpayer. The taxpayer may appeal the value by filing a petition with the board of equalization. The petition must be filed with the board on or before July 1 of the year of the assessment or determination, within 30 days after the date of an assessment, value change notice, or other notice has been mailed, or within a time limit of up to 60 days adopted by the county legislative authority, whichever is later. ([RCW 84.40.200](#) and [84.40.038](#).)

## 1.18 Assessment Date

All personal property subject to tax is to be listed and assessed every year with reference to its value and ownership on January 1 of the assessment year. ([RCW 84.40.020.](#))

## 1.19 Exemptions

Household goods and furnishings in actual use by the taxpayer in his residence, and not for sale or commercial use, are exempt. Personal property of each head of family (sole proprietor) is exempt up to a maximum of \$15,000 if the taxpayer meets the definition of head of family. ([RCW 84.36.110](#) and [WAC 458-16-115](#))

The inventory of a business is not subject to property tax. ([RCW 84.36.477.](#)) "Business inventories" means...

*"...all livestock, inventories of finished goods and work in process, and personal property not under lease or rental, acquired, or produced solely for the purpose of sale or lease or for the purpose of consuming the property in producing for sale or lease a new article of tangible personal property of which the property becomes an ingredient or component."*

Business Inventories does not include...

*"...personal property acquired or produced for the purpose of lease or rental if the property was leased or rented at any time during the calendar year immediately preceding the year of assessment and was not thereafter remanufactured, nor does it include property held within the normal course of business for lease or rental for periods of less than thirty days."*

Custom computer software, except embedded software, is exempt from taxation. Retained rights in computer software are exempt. Modifications to canned software are exempt, but the underlying canned software remains subject to tax. Master or golden copies of computer software are exempt. ([RCW 84.36.600.](#))

Under [RCW 84.36.630](#), all qualifying farm machinery and equipment is exempt from the state property tax. **Qualifying** machinery and equipment must (1) be **owned** by an active farmer, (i.e., someone who is in the business of farming) and (2) have been used in the business of farming during each year the claim for exemption is made. Additionally, equipment claimed for exemption must also have been used **exclusively** in growing, raising, or producing agricultural products. Equipment **not qualifying** includes (1) equipment used in growing, raising, or producing agricultural products for a person's own consumption, (2) equipment used in the selling of animals from stockyards, slaughter houses, and packing houses, and (3) equipment used in cultivating or raising timber. The claim for exemption must be submitted annually with the personal property listing form in the county for which the listing form is made. For a listing of qualifying farming activities refer to [RCW 82.04.213](#) and [15.85.020](#).

*"Farmer" means any person engaged in the business of growing, raising, or producing, upon the person's own lands or upon the lands in which the person has a present right of possession, any agricultural product to be sold. "Farmer" does not include a person*

*growing, raising, or producing such products for the person's own consumption; a person selling any animal or substance obtained therefrom in connection with the person's business of operating a stockyard or a slaughter or packing house; or a person in respect to the business of taking, cultivating, or raising timber.*

Other exemptions may be found in [chapter 84.36 RCW](#).

### [Application for Exemption of Farm Machinery and Equipment](#)

## 1.20 Personal Property Moving into the County

Personal property being moved from one county in Washington to another county in Washington, between January 1 and July 1 should be assessed in whichever county first lists and assesses the property. ([RCW 84.44.080](#).) Usually, the county where the property is being relocated will contact the previous county to verify listing and assessment. Be careful to avoid a double assessment.

## 1.21 Personal Property Moving into the State

When personal property is moved into Washington from outside the state between January 1 and July 1, the owner is required to list the property for assessment purposes. The property must have been in existence and owned by the taxpayer on January 1. If the owner can show that the property has already been assessed in another state or county, it should not be assessed again in Washington. The burden of proof is upon the taxpayer to produce documentation. ([RCW 84.44.080](#).)

## 1.22 Perfection of Personal Property Liens

The lien on personal property is established on January 1 of the assessment year. However, it is not perfected until the property is listed and valued by the assessor. So even though a taxpayer may have listed the property, the lien is not protected until the assessor has valued the property. Subsequent sale of the personal property does not affect the lien for taxes. If necessary, the lien may be placed upon real property of the taxpayer (selected by the treasurer) and charged on the tax rolls. ([RCW 84.60.020](#).)

## 1.23 Valuation Guidelines, Indexes, and Indicators

Annually, the Department of Revenue issues *Personal and Industrial Property Valuation Guidelines (Guidelines)*. These *Guidelines* consist of (1) an explanation of changes from the prior year and information about how to use the *Guidelines*, (2) Business Index, (3) Personal and Industrial Property Valuation Combined Table and the Supplemental Valuation Tables.

The *Guidelines* are published as a guide in estimating the market value of property in average condition. Adjustments to the estimated market value must be made by the assessor's office when the taxpayer can substantiate any excessive obsolescence not already taken into account in the tables.

The reasons for using "Original Cost New Less Depreciation" as the basis for valuation are that the information is easily obtainable, this method lends itself readily to a computerized mass

appraisal format, the taxpayer has a permanent record of the cost, and the trend and depreciation table can be easily updated. However, the assessor is not required to use this information to determine the value of the property. Sometimes a business or assets are sold. The new owner will list the original cost, but the assessor may use the prior information to value the property. From time to time, market studies are conducted to see if changes are warranted to the *Guidelines*.

The index portion of the *Guidelines* is an alphabetical list of business types or classes of property. Locate the type of property in the index, and you will find reference to the Table/Column number to use to value the property.

The percent good table is made up of two components. A declining balance depreciation rate is built into the table, and the column number in the index represents the depreciation rate (24 equals 24 percent). The table also employs a trend. The purpose of the table is to start with the historical cost of the item, trend the cost to today's market, and then depreciate the cost for normal wear and tear. The Department uses the producer price index from the U.S. Bureau of Labor Statistics and the Marshal & Swift trend factors to trend costs. The figures across the top of the table are the rate of the declining balance depreciation. The higher the number the faster the item will depreciate or the shorter the life of the item. To use the table, locate the year of acquisition, and then determine the proper table or column by referencing the index. Where the lines for the acquisition year and depreciation rate intersect is the "percent good." Multiply the percent good figure by the acquisition cost to find the market value of the property for that year.

Additional information on the *Guidelines* may be found in the Valuation Guidelines portion of this manual.

## 1.24 Depreciation

Depreciation means different things to different professions. Businesses usually track depreciation for federal income tax reporting purposes.

Accounting: To an accountant, depreciation is a systematic process of allocating the cost of an asset over the period of time the owner is expected to benefit from the use of the asset. In other words, the \$5,000 cost of the welder is spread over the 5-year life of the welder. Each year, the book value of the asset is reduced by \$1,000 (straight line method of depreciation) to record the loss in value or wear and tear on the equipment, assuming the welder is worth less money after one year of use.

Appraisal: To an appraiser, depreciation is the process of measuring the loss in value of an asset. An appraiser is trying to determine the market value of the asset. Book value, used by the accountant, may or may not reflect actual market value. Loss in value may come from physical depreciation (wear and tear on the equipment), functional obsolescence (outdated computer due to new technology), or economic obsolescence (legislative action such as the spotted owl protection).

There are different methods of depreciation. The straight-line method reduces the value of the asset equally each year over the life of the asset. A declining balance method of depreciation

allows for the largest depreciation to occur in the earliest years of use of the item. The declining balance method is used in the Department of Revenue valuation tables. Each year the rate of depreciation is applied to the previous year's balance. Here's an example of the loss in value of an item using a 30 percent depreciation rate:

<i>Cost of Equipment: \$10,000</i>			
Year 1	\$7,000	(10,000 x .30 = 3,000	so 10,000 - 3,000 = 7,000)
Year 2	\$4,900	(7,000 x .30 = 2,100	so 7,000 - 2,100 = 4,900)
Year 3	\$3,430	(4,900 x .30 = 1,470	so 4,900 - 1,470 = 3,430)
Year 4	\$2,401	(3,430 x .30 = 1,029	so 3,430 - 1,029 = 2,401)
Year 5	\$1,680	(2,401 x .30 = 720	so 2,401 - 720 = 1,680)
Year 6	\$1,176	(1,680 x .30 = 504	so 1,680 - 504 = 1,176)
Etc.			



## PART 2 – Valuation Guidelines, Index, and Indicators

The *Personal and Industrial Property Valuation Guidelines (Guidelines)* are published annually by the Department of Revenue as **guides** in estimating market values of equipment using the trended investment methodology. Because **mass appraisal** of property does not lend itself to traditional market valuation techniques, the Department recommends the use of the *Guidelines*. Their use will produce standardization and equalization in the assessment of property.

The *Guidelines* may not be applicable in all instances in achieving the statutory mandate of 100 percent true and fair value. These valuation indicators are published as a guide in estimating market value, but they do not include any consideration for abnormal or extraordinary obsolescence that may be relevant in specific circumstances or markets. When unique situations are identified, these factors should be considered separately and in addition to the value indications of the tables.

These valuation indicators are recognized as an authoritative guide in estimating market value by the State Board of Tax Appeals and Washington State Courts.

### 2.1 Valuation of Personal and Industrial Property

Here are the three approaches to valuing property.

1. **Cost Approach:** Costs used in the cost approach can be original acquisition, replacement, or reproduction cost, although often only original or acquisition costs are readily available for personal property. The cost approach provides an estimate of value based on the depreciated cost of the property. Total acquisition cost includes freight, trade-in allowances, installation, and any fees incurred to get machinery operational.
2. **Market or Sales Comparison Approach:** Market sales of used machinery and equipment, when compared to historical cost, contributes to trending and economic life built into the “Valuation Indicator” depreciation tables.
3. **Income Approach:** When reliable income and expense data on equipment leases are available, the income approach can provide good value estimates for leased equipment.

### 2.2 The Valuation Indicators Are a Cost Approach

Although the **market** or **comparative sales** and **income approaches** can be used in machinery and equipment valuation, it is usually the **cost approach** that is relied upon most heavily in arriving at a valuation estimate for **mass appraising**.

The cost approach is nothing more than reproducing the cost of an asset and applying a rate of depreciation that represents a loss in value attributable to depreciation. In using this method, as

with the Valuation Indicators, we are taking the historical cost of an asset, trending the cost up to today's level, and then allowing for normal declining balance depreciation (RCNLD).

### **RCNLD = Reproduction Cost New Less Depreciation**

Review of terms:

**Reproduction Cost:** Is the cost of producing an exact replica using the same or very similar materials, design, and workmanship.

As compared to:

**Replacement Cost:** Represents the principle of substitution, replacing the item with property functionally equivalent, having the same utility, to the subject, not necessarily an exact replica.

**Trend:** The Department of Revenue develops its own trend based upon a simple average of two indexes data collected from the Producer Price Index (PPI) administered by the U.S. Bureau of Labor Statistics and the Cost Indexes published by Marshall & Swift Cost Service.

The following is a sample of the trend used in Department's *Guidelines*:

Age	Year	Trend	
1	2015	100.0%	or 1.000
2	2014	101.2%	or 1.012
3	2013	102.4%	or 1.024
4	2012	104.2%	or 1.042
5	2011	107.0%	or 1.070
<b>Example:</b>			
<b>2011 Cost X Trend = Trended Cost 1/1/15</b>			
<b>2011 Asset Cost = \$20,000</b>			
<b>\$20,000 X 1.070 = <u>\$21,400</u></b>			

(Before applying depreciation)

## 2.3 Depreciation

Depreciation is the loss in value from all causes. There are generally three recognized types of depreciation:

1. Physical deterioration, which results from wear and tear, decay, and structural failure.
2. Functional obsolescence, which results from poor design and style or from changes in technology.
3. Economic obsolescence, which results from economic forces, such as legislative enactments or changes in supply-and-demand relationships.

The Valuation Indicators used in the *Guidelines* incorporate declining balance depreciation.

**Declining balance depreciation** is a method of depreciation where the depreciable basis for the next year is reduced by the depreciation deduction taken in the current year.

**DECLINING BALANCE DEPRECIATION TABLES WITHOUT TREND FACTORS:**

Age	30.0%	27.0%	25.0%	24.0%	22.0%	20.0%	19.0%	18.0%
1	70.0%	73.0%	75.0%	76.0%	78.0%	80.0%	81.0%	82.0%
2	49.0%	53.3%	56.3%	57.8%	60.8%	64.0%	65.6%	67.2%
3	34.3%	38.9%	42.2%	43.9%	47.5%	51.2%	53.1%	55.1%
4	24.0%	28.4%	31.6%	33.4%	37.0%	41.0%	43.0%	45.2%
5	16.8%	20.7%	23.7%	25.4%	28.9%	32.8%	34.9%	37.1%
6	11.8%	15.1%	17.8%	19.3%	22.5%	26.2%	28.2%	30.4%
7	8.2%	11.0%	13.3%	14.6%	17.6%	21.0%	22.9%	24.9%
8	5.8%	8.1%	10.0%	11.1%	13.7%	16.8%	18.5%	20.4%
9	4.0%	5.9%	7.5%	8.5%	10.7%	13.4%	15.0%	16.8%
10	2.8%	4.3%	5.6%	6.4%	8.3%	10.7%	12.2%	13.7%
11	2.0%	3.1%	4.2%	4.9%	6.5%	8.6%	9.8%	11.3%
12	1.4%	2.3%	3.2%	3.7%	5.1%	6.9%	8.0%	9.2%
13	1.0%	1.7%	2.4%	2.8%	4.0%	5.5%	6.5%	7.6%
14	0.7%	1.2%	1.8%	2.1%	3.1%	4.4%	5.2%	6.2%
15	0.5%	0.9%	1.3%	1.6%	2.4%	3.5%	4.2%	5.1%

The Department of Revenue conducts age-life studies that establish the remaining useful or **economic life** of various types of equipment. From this study, the Department constructs a “percent good table” based on the declining balance method of depreciation that is used with an index. The index classifies personal property and assigns the appropriate “percent good table” to each classification.

## 2.4 Valuation Indicators Combine Trend and Depreciation

The following table is a sample portion of a combined trend and depreciation table. (See *Personal and Industrial Property Valuation Guidelines – Trended Investment Method* for a complete set of tables that include Trend I and Trend II Tables.)

By consolidating the trend data with the depreciation analysis (percent good table), the Personal Property Valuation Table is produced. Note below that the valuation table depreciates property to a minimum level of 15 percent good (85 percent depreciation). The table arrives at a minimum value by taking into consideration a salvage or residual value and the **value-in-use** concept.

<b>TREND I COMBINED TABLES FOR PERSONAL AND INDUSTRIAL PRO</b>												
<b>Percent Good Indicators -- For January 1, 2016 Valuations</b>												
AGE	YEAR	Trend I	30.0%	24.0%	20.0%	19.0%	18.0%	16.0%	14.0%	12.0%	10.0%	8.5%
Economic Life (Years) →			5	6	7	8	8	9	11	13	15	18
1	2015	1.000	0.700	0.760	0.800	0.810	0.820	0.840	0.860	0.880	0.900	0.915
2	2014	1.012	0.496	0.585	0.648	0.664	0.681	0.714	0.749	0.784	0.820	0.848
3	2013	1.024	0.351	0.450	0.524	0.544	0.565	0.607	0.651	0.698	0.747	0.784
4	2012	1.042	0.250	0.348	0.427	0.449	0.471	0.519	0.570	0.625	0.684	0.731
5	2011	1.070	0.180	0.271	0.351	0.373	0.397	0.448	0.504	0.565	0.632	0.687
6	2010	1.088	0.150	0.210	0.285	0.307	0.331	0.382	0.440	0.505	0.578	0.638
7	2009	1.097	0.150	0.161	0.230	0.251	0.273	0.324	0.382	0.448	0.525	0.589
8	2008	1.133	0.150	0.150	0.190	0.210	0.232	0.281	0.339	0.408	0.488	0.557
9	2007	1.169	0.150	0.150	0.157	0.176	0.196	0.243	0.301	0.370	0.453	0.526
10	2006	1.218	0.150	0.150	0.150	0.150	0.167	0.213	0.269	0.339	0.425	0.501
11	2005	1.269	0.150	0.150	0.150	0.150	0.150	0.186	0.242	0.311	0.398	0.478
12	2004	1.329	0.150	0.150	0.150	0.150	0.150	0.157	0.217	0.287	0.375	0.458
13	2003	1.355	0.150	0.150	0.150	0.150	0.150	0.150	0.191	0.257	0.344	0.427
14	2002	1.368	0.150	0.150	0.150	0.150	0.150	0.150	0.166	0.228	0.313	0.394
15	2001	1.379	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.203	0.284	0.364
16	2000	1.388	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.180	0.257	0.335
17	1999	1.405	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.158	0.234	0.310
18	1998	1.411	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.212	0.285
19	1997	1.426	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.193	0.264
20	1996	1.451	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.173	0.245
21	1995	1.479	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.150	0.156	0.229

Used properly, this table will give an estimate of market value.

**Trend X Percent Good (1 Minus Depreciation) = RCNLD Factor**

Example using 5-year age table:

$$1.173 \times 37.1\% \text{ (18\% declining balance table from previous page)} = 0.435 \text{ or } \underline{43.5\%}$$

$$\underline{\text{Trend X Percent Good X Cost}} = \boxed{\text{Market Value}}$$

See *Personal and Industrial Property Valuation Guidelines – Trended Investment Method* at:

<http://dor.wa.gov/FindTaxes-Rates/Property-Tax/personal-property-valuation-guidelines>

## PART 3 – Listing Forms (formerly called affidavits)

**OBJECTIVE:** To maximize class participation in sharing information on listing forms used in the assessment of personal property for ad valorem tax purposes.

Possible topics for discussion:

1. General instructions
2. Equipment listings
3. Software
4. Supplies
5. Class suggestions
6. Other forms that have proven useful for assessment purposes

### 3.1 Listing of Personal Property of a New Business

Information that should ordinarily be obtained for a new business needs to be more detailed and should include the following:

1. Name of business.
2. Type of business (e.g., bowling alley, quick mart).
3. Type of ownership (e.g., sole proprietorship, partnership, franchise, or corporation).
4. Situs of personal property and mailing address of the business.
5. Name and address of owner(s), including e-mail.
6. Telephone number of business.
7. Name and title of the person supplying the information.
8. Name, address, and telephone number of the party keeping records for the business, including e-mail.
9. Beginning date of the business and the business fiscal year.
10. For leased equipment: the name and address of the lessor; information on the equipment including name of manufacturer, date of manufacture, description, model number, serial number, list price, and original cost (if available); and lease information including, the lease number and terms of lease or, if possible, a copy of the lease agreement itself.
11. For loaned or consigned items (e.g., vending machines, amusement devices, and jukeboxes): the name and address of their owner(s) and a brief description.
12. Whether the business rents or leases items in its inventory as part of its normal operation (such items may be assessable inventory).
13. Leasehold improvements may be assessed as real property, so be careful to avoid double assessment.
14. Equipment owned by the business but located at another site within the jurisdiction, including a brief description and address.

## PART 4 – Supplemental Valuation Tables A & B

To demonstrate some specific valuation procedures in the Supplemental Valuation Table A & B, including the valuation of video arcade games, videos, and disks, title plants, and other specialty personal property.

### 4.1 Valuing Video Arcade Games, Videos, and DVDs

#### **Difference Between Video Arcade Games**

In the context of the *Guidelines*, video arcade games are not those games you can rent at the video store. The category of video games under the business activity of *Amusement Devices* on page 1 of the *Index* does not refer to the games you can rent and use with a home game console. This category of business activity predates those games and refers to machines typically found in an arcade. Supplemental Table A says to value these machines at 60 percent, 37 percent, and 20 percent of untrended cost for machines one, two, and three plus years of age.

How should video games—the kind you can rent and use in your home console—be valued? These items fit into the same category as rental Video Tapes, Laser Discs, and DVDs. These items tend to have a very short shelf life in business and may not be held for rental more than a few months.

#### **Videotapes, DVDs, and Property Held or Owned for Short-Term Rental**

Videos and all other rental assets rented for less than 30 days at a time are to be valued at their retail value (retail trade level). These may be new or used assets held for rent. The valuation *Guidelines* recommend valuing videos and DVDs on an average per video value for video rental inventory – individual video values could be less for older ones or much more for new-releases purchased just prior to assessment date. Documented costs may be used if an accurate count or estimate of inventory is unknown and if the cost represents cost at retail trade level.

The assessed value is intended to reflect the average per tape or disk value for the entire inventory of tapes and disks that remain in the rental inventory—not liquidation value. The price of used tapes for sale reflects liquidation value, but retail trade level value must be greater than liquidation value. Value property in the rental inventory at the retail trade level only; used tapes held only for sale are exempt business inventory.

### 4.2 Valuing Title Plants

Title Plants have a graduated rate scale based on the number of real property parcels reported to the Department for Ratio purposes. We developed this method after a study and considerable analysis with assistance from the Washington Land Title Association. Value each title plant physically located within each county, including title plants for other counties.

### 4.3 Valuing Computer Software

The following is to aid in your understanding of Washington State laws regarding property valuation of computer software. ([WAC 458-12-251](#).)

**Computer software** is a set of directions or instructions that exist in the form of machine-readable or human-readable code, is recorded on physical or electronic medium, and directs the operation of a computer system or other machinery and/or equipment. Computer software includes the associated documentation that describes the code and/or its use, operation, and maintenance and typically is delivered with the code to the user. Computer software does not include databases, but it does include the computer programs and code that are used to generate databases. Computer software can be custom, canned, or a mixture of both.

**Custom software** is computer software that is specially designed for the specific needs of a single person or a small group of persons. Custom software includes modifications to canned software and can be developed in-house by the user, by outside developers, or by both.

**Canned software**, also referred to as prewritten, "shrink-wrapped," or standard software, is computer software that is designed for and distributed "as is" for multiple persons who can use it without modifying its code and which is not otherwise considered custom software.

**Embedded Software** is computer software that resides permanently on an internal memory device in a computer system or other machinery and equipment, is not removable in the ordinary course of operation, and is of a type necessary for the routine operation of the computer system or other machinery and equipment. Embedded software can be either canned or custom.

### **Valuation**

The 1991 Legislature defined computer software and established valuation methods. For the 2009 assessment year, canned software shall be assessed as illustrated in the following example:

- Canned software acquired in 2008 shall be valued at 100 percent of its full acquisition cost.
- Canned software acquired in 2007 shall be listed at 100 percent and valued at 50 percent of its full acquisition cost.
- All software, canned or custom, purchased in 2006 and before is exempt.

In cases where canned software is specially modified for the user, the canned component of the computer software retains its identity as canned software; and the modifications are considered custom software and not taxable.

**Embedded software** is taxable and shall be valued as an integral part of the computer system, machinery, or equipment in which it is housed, at the established life of the equipment.

All **custom software**, except embedded software, shall be exempt from property taxation.

For Supplemental Valuation Tables, see *Personal and Industrial Property Valuation Guidelines – Trended Investment Method at:*

<http://dor.wa.gov/Find-Taxes-Rates/Property-Tax/personal-property-valuation-guidelines>

## PART 5 – Leased Equipment and Trade Level

The following is to define the different types of leases and ways to distinguish them. Also covered are the factors affecting lease values and valuing personal property at the appropriate trade level.

### 5.1 Leased Equipment Definitions

**Lessor** The owner of the property.

**Lessee** The renter of the property.

**Lease** A contract between an owner (**lessor**) and a tenant or renter (**lessee**) (), the terms of which provide that the lessee is to have legal possession of the property of the lessor for an agreed duration of time, upon the payment of certain agreed rents and the performance of stated obligations.

### 5.2 Types of Leases

All leases are classified as either **capital** or **operating**.

#### Operating Lease Characteristics

Short term, less than asset life.

Lessor must lease the equipment for more than one time to recapture his investment.

#### **Example of an Operating Lease**

Straight Lease: This type of contract grants to the lessee, by the lessor, the possession and use of certain equipment for a given period of time and makes no provision or requirement for purchase by the lessee.

#### Capital Lease Characteristics

Long term, the duration of which matches the life of the asset.

Has the characteristics of a purchase rather than a lease.

Lessor usually recaptures his investment and profit from one lease term.

#### **Examples of Capital Leases**

Lease Purchase Contract: This type of contract states that the lessee has agreed to pay the full value of the payment through monthly payments, and at the end of the contract term, the lessor shall transfer title and ownership to the lessee.

Lease with Option to Buy: This type of contract states that the lessee agrees to pay certain stipulated payments for the possession and use of the property. At the end of the lease term, the asset is available for purchase by the lessee for a nominal final payment.



### **Criteria for a Capital Lease**

If the terms of the lease meet any one of the following four criteria, it is classified as a **capital lease**, and the lessee is required to **record** the present value of the minimum lease payments as **an asset** and to record a corresponding liability:

1. If the lease transfers ownership of property to the lessee by the end of the lease term, it is a capital lease.
2. If the lease contains a bargain purchase option, it is a capital lease.
3. If the lease term is equal to 75 percent or more of the estimated economic life of the leased property, it is a capital lease.
4. If the present value, at the beginning of the lease term, of the minimum lease payments is equal to at least 90 percent of the fair value of the leased property minus the lessor's investment credit, it is a capital lease.

If none of the four criteria is met, the lease is classified as an **operating lease**, which requires only disclosure in the financial statements.

### **True Leases vs. Security Agreements**

**True Lease** – does not transfer ownership, and the lessor pays the personal property taxes.

**Installment Contract** – transfers ownership to the lessee and in most cases requires the lessee to pay the personal property taxes.

**PTA 10.1.2009 "True Lease" or Security Agreement** sets criteria for determining whether an agreement was intended to be a true lease or an installment contract. PTA 10.1.2009, can be accessed at:

[https://dor.wa.gov/sites/default/files/legacy/Docs/Pubs/Prop\\_Tax/PTA10\\_1\\_2009.pdf](https://dor.wa.gov/sites/default/files/legacy/Docs/Pubs/Prop_Tax/PTA10_1_2009.pdf)

## **5.3 Factors Affecting Value**

The valuation of leased equipment is usually complicated by several factors:

- Determination of useful or economic life
- Applicable cost
- Level of trade

### **Lease Date vs. Installment Date**

Installment date is used for assessment—**NOT** the lease date.

### **Double Assessments**

To avoid double assessments of leased equipment, counties should be consistent. Require both lessee and lessor to list the property as a cross reference. Normally, we recommend that the lessor be assessed.

### **Exempt Property**

Leased equipment may be exempt if used by nonprofit organizations specified in [chapter 84.36 RCW](#) and the benefit of the exemption inures to the user. The Department of Revenue will issue a determination letter to the county identifying exempt personal property. Personal property of nonprofit organizations should not be exempted unless you have a determination letter from the Department of Revenue.

## 5.4 Trade Level

The appraiser should value personal property at the level of trade at which it is found. Trade level may be defined as value at the point in the production stream where an item of manufactured personalty is found, or the production-distribution level in which a product is found. The concept of trade level requires the following:

1. Appraise property at the level of trade where it rests.
2. Disregard ownership in determining value.
3. Carry forward all increments of value for the property as it moves through the channels of trade.

Normally, there are three (or four) levels of trade to be considered:

### 1. **Manufacturer's Level**

This level should be used in the appraisal process only when the property is in the hands of the manufacturer and in the local manufacturer's plant.

### 2. **Wholesale Level**

As property moves through the channels of trade, it increases in value by virtue of freight, overhead, and intercompany profit. These value factors added to the property will result in equity regardless of ownership. Thus, when property moves from the manufacturer's level to the wholesale level, the increments of value must be recognized at that level.

### 3. **Distributor Level**

In some cases, this level is synonymous with the wholesale level. However, in certain cases, there is a difference and, if so, it must be recognized in the appraisal process.

### 4. **Retail Level**

The retail level is relevant in the appraisal of many properties. Property normally attains maximum value to this point (includes freight, installation, etc.).

**Trade level** is a valid concept and is recognized by professionals, appraisers, attorneys, and the courts. Most often, the trade level concept is used when valuing inventories, which are exempt from personal property taxation in this state. It recognizes that incremental costs (such as freight overhead, handling, and installation) are added to a product. Property reaches its maximum value as it reaches the consumer level.

Problems associated with the trade level concept include:

- Arriving at the appropriate value at the various levels of trade when the manufacturer does not reflect, record, or recognize the various levels on their accounting records.

- Arriving at the appropriate value of leased equipment when the manufacturer may also be the distributor, consumer, and lessor.

The positive aspect to the trade level approach is that the property is being valued equitably, uniformly, and consistently with like properties regardless of ownership and/or cost as reflected on the accounting methods.

**PART 6 – Assessment of Supplies**

# Property Tax Advisory

**Property Tax Advisories are interpretive statements authorized by RCW 34.05.230.**

NUMBER: PTA 9.1.2009

ISSUE DATE: 02/02/09

## **ASSESSMENT OF SUPPLIES**

This Property Tax Advisory is issued as a guide in clarifying the assessment of supplies for the 2003 and subsequent assessment years. The advisory should not be used to determine the taxability of furniture and fixtures or machinery and equipment.

Taxable assets in this category, like all other assets, are valued at market value as of the assessment date. Since these assets are often consumed during the year, the average inventory method is used to determine the cost for the basis of the valuation if the year-end inventory is not representative of what is typically on hand. In many cases, one-twelfth of the annual cost for the taxable assets is a good estimate of the market value. This suggests that, on average, one month's worth of supplies is on hand at any given time during the year. When it can be shown that more or less inventory is typically on hand, a different measure of average inventory may be used. For example, divide the annual cost of supplies by 52 when only one week's worth of supplies are typically on hand.

An exception to the average inventory method is used to determine the value of spare parts, especially when they are not typically consumed within the year. If this is the case, all of the parts are listed on the personal property affidavit and valued in the same manner as other personal property, with one exception. Since the parts have not been put in service, they do not tend to depreciate. Hence, they are generally assessed at their original cost. However, trend factors may be applied if deemed appropriate to arrive at the market value. Applying a trend factor does not always equate to an increase in the replacement cost estimate; some trend factors indicate a decline in cost/value from one year to the next.

**BUSINESS SUPPLIES - GENERAL DEFINITION:** Business supplies means:

- (1) Products or materials not held for sale in the normal course of business.
- (2) Materials that do not become an ingredient or component of an article being manufactured for sale or lease (RCW 84.40.210).

As a "general" rule of thumb, items that purchasers should have paid sales or use tax on are considered consumable supplies.

**BUSINESS INVENTORIES - DEFINITION:** Business inventories are exempt from ad valorem property taxation. "Business inventories" is defined in RCW 84.36.477 and means:

- (1) All livestock;
- (2) All personal property held for sale or lease in the normal course of business; and
- (3) All property becoming an ingredient or component of any article of tangible personal property being manufactured for sale or lease.

Generally, items purchased with a resale certificate are business inventories. "Business inventories" does not include personal property acquired to lease or rent to others unless the requirements of RCW 84.36.477 are met.

The above list is not inclusive. For a more complete listing of exempt business inventories, see RCW 84.36.477.

**PACKAGING MATERIALS - DEFINITION:** "Packaging materials" means and includes all boxes, crates, bottles, cans, bags, drums, cartons, wrapping papers, cellophane, twines, gummed tapes, wire, bands, excelsior, wastepaper, and all other materials in which tangible personal property may be contained or protected within a container for transportation or delivery to a purchaser.

**DUNNAGE - DEFINITION:** The term "dunnage" means any material used for the purpose of protecting or holding cargo in place during shipping by any type of carrier. Examples of these types of materials include wood blocks, timbers, separating forms, bulkheads, double floors, or any other type of bracing or support structures.

#### **EXAMPLES AMONG VARIOUS BUSINESS CATEGORIES:**

##### **MANUFACTURING/PROCESSING**

**PACKAGING MATERIALS:** The location in the production stream is the determining factor whether packaging materials are inventory or supplies.

When the manufacturer or processor packages manufactured or processed products for a final sale, all packaging materials in which the product is held for sale become a part of that product and are considered inventory for resale. Examples of packaging components used to contain a product held for sale might include some or all of the following: individual wrappings of each item; cardboard used for layering; the package containing each item; the box holding numerous individual items; staples, banding, glue, or other material used to seal the box; pallets holding numerous boxes which might also be sealed in plastic and/or banded together for shipping.

If the product has not been completed and is packaged for shipment to another step in the manufacturing process where it will be repacked, the materials or containers used to ship the

product from one step to another are considered supplies. Containers may be considered equipment if they are returned and are reusable by the shipper.

"Dunnage," as defined in this advisory, is always considered a supply item to the user whether it is returned to the user or not.

**CHEMICALS:** All chemicals used in processing or manufacturing of a product are considered inventory if they react chemically with, or become a component of, the product. An example of this process is chemicals used in a pulp mill for digesting and bleaching pulp. The chemicals react to the cellulose in the pulp fibers altering the fiber and also becoming an ingredient of the final product. Another example is carbon used to form a chemical reaction with alumina to remove oxygen content. This alters the final product produced in an aluminum reduction plant and, therefore, is considered a part of the end product.

**OTHER SUPPLIES:** All other materials (except packaging) **NOT** held for resale or stockpiled to become an ingredient or component in the manufactured or processed finished product are taxable supplies.

## SERVICE

**DEFINITION:** A "service business" means conducting any type of personal service for others that does not involve the sale of a product. Examples include, but are not limited to, attorneys, hairdressers, doctors, dentists, dry cleaners, nursing homes, accountants, etc.

**SUPPLIES:** "Supplies" means all materials consumed in the rendering of the service. Exceptions to this rule are:

- (1) Businesses that make a separate charge for material used in the service provided. An example of this type of business is custom meatpacking. The wrapping paper is considered an inventory item because the charge for cutting and wrapping is separate from the charge made for the meat.
- (2) In a business providing parts used in the repair of items of tangible personal property, the parts are considered inventory even though they are not held for resale.
- (3) Materials are considered inventory if they become a part of an item for sale in trade shops, such as newspaper publishers, printing shops, photographers, typesetters, processing for hire, etc., are considered inventory.

**INVENTORY:** Items held for sale which are not part of the rendition of the personal service are considered inventory.

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## COMMERCIAL/WHOLESALE

For commercial/wholesale businesses, supplies are considered to be any product or material not held for sale in the normal course of business. Examples of commercial/wholesale businesses and the supplies used in such businesses include but are not limited to:

RESTAURANTS -- Paper napkins, straws, "doggie bags," cleaning supplies, and plastic silverware.

CLOTHING STORES -- Hangers, bags or boxes, wrapping paper, cash register tapes, and cleaning supplies.

MOTELS -- Cleaning supplies, advertising items, coffee, cups, and plasticware.

RETAIL STORES -- Sacks, boxes, other wrapping material, cleaning supplies, cash register tapes, computer paper, and office supplies.

GROCERY STORES -- Grocery bags, cleaning supplies, and office supplies.

WHOLESALE OUTLETS -- Packaging materials other than those enclosing the product, cleaning supplies, cash register tapes, computer paper, office supplies, fuel stored for vehicles, and fleet maintenance parts.

## AGRICULTURE/AQUACULTURE

Supplies are any items not influential in the growing of a crop or the raising of animals.

Items under this definition that are NOT SUBJECT TO AD VALOREM PROPERTY TAX include:

- (1) Feed, whether grown or purchased, used in the raising of livestock or water animals for meat, seafood, or dairy purposes.
- (2) Fertilizers or insecticides used to enhance the growing of a current year's crop.

TAXABLE SUPPLIES under the above definition include but are not limited to petrochemicals held in storage and used in vehicles, veterinary supplies, and cleaning supplies. Spare parts and small tools that are sometimes classified as supplies for accounting purposes are also taxable.

## CONSTRUCTION/LOGGING

Supplies are considered any material used in the performance of the involved activity other than materials used in the construction of an improvement to real property.

Examples of these types of supplies would include but are not limited to explosives, petrochemicals, spare parts, tires, small tools, and other cleaning supplies.

## PART 7 – Audit Preparation

The following provides an overview of what constitutes effective auditing skills.

Most audits are limited to data gathering, brief reconciliation, and record review. This can be done through **mail audits** or at the physical site of the business records. The final results are usually not disclosed at the conclusion of the physical review of records.

### 7.1 Overview of Audit Procedures

1. As an auditor/appraiser, you are the public relations and liaison officer between the assessor's office and the taxpayer.
2. Make an appointment in advance. When you arrive for the appointment, introduce yourself, present a copy of the appointment letter, and show your identification. **Explain the purpose of your visit.**
3. Be punctual.
4. Be prepared to tell the taxpayer which records are necessary to perform the audit, even though previous notification was sent.
5. Familiarize yourself with the books as to type before proceeding. Request a plant inspection if necessary.
6. Prepare the form you will use before making the call.
7. Determine if the business is on a **calendar** or **fiscal year** basis.
8. Check books for cost and year of acquisition of equipment. Compare with depreciation schedule, income tax return, and financial statement. If on a fiscal year basis, check for equipment purchased after the close of books at fiscal year end but prior to calendar year end. Check for freight, sales tax, and installation costs.
9. Check for leased equipment. Determine if it is to be reported by lessee or lessor. Lessor's name address and any pertinent information should be obtained and checked against assessment records to avoid double assessments.
10. Check for vehicles that may be subject to personal property tax.
11. Submit your reports to your supervisor, marking both the name and audit number for identification and filing purposes.
12. Review the **leasehold improvements** with real estate appraisers to determine if improvements have been assessed.



## 7.2 Audit Checklist

1. Give brief description of business (including product lines or service and trade level).
2. Check for other businesses or affiliates with other tangible property at this location.
3. Observe the age and condition of plant equipment.
4. Check list of books and records from which information is obtained.
5. Note any obsolete or shop-worn equipment that is not accounted for.
6. Check for **supplies, small tools, and spare parts**.
7. Gather equipment data:
  - Recapture **fully depreciated items** that were written off.
  - **Include installation and freight costs** in the equipment costs.
  - Recapture **trade-in** adjustments.
  - Check for **leased equipment**.
  - Check for expensed assets not on the depreciation list.
  - Check for equipment delivered prior to the lien date but not recorded.
8. In your opinion, was the property statement filed in a manner indicating willful concealment, non-disclosure, removal, transfer, or misrepresentation of tangible property? If yes, state reason for your conclusion.
9. Have **leasehold improvements** been reported?
  - a. Is business located on private property or exempt land?
  - b. Are leasehold improvements on buildings assessed with real property assessments?

## 7.3 Listing of Personal Property of a New Business

See Section 3.1 for details

## 7.4 Sample Letters

The following are several sample letters from counties, including an audit field/worksheets.

### Notice of Personal Property Audit

Dear Property Owner:

A number of property owners in our county have been selected on a sampling basis for a personal property audit.

**All income information received will be kept strictly confidential as required by Washington State law.**

Please see items checked:

\_\_\_\_\_ Mail copies of records to this office as soon as possible. The data must include the signature of the owner, company officer, or your accountant. *If you prefer to have an auditor/appraiser come to your office, please call.*

\_\_\_\_\_ An auditor/appraiser will be at your location on \_\_\_\_\_ at \_\_\_\_\_. If this date/time is not convenient, please contact us to set a new date/time. Also, if your records are at a different location, please call to let us know.

Please have copies of the following records available:

\_\_\_\_\_ Current depreciation schedule

\_\_\_\_\_ Equipment register

\_\_\_\_\_ IRS Schedule \_\_\_\_\_ (Income information may be deleted if desired.)

\_\_\_\_\_ Year-end financial statements showing asset totals. (Income information may be deleted if desired.)

\_\_\_\_\_ General ledger

\_\_\_\_\_ Information on any leased equipment

\_\_\_\_\_ Other \_\_\_\_\_

Thank you for your cooperation. If you have any questions, please call the Personal Property Department at (xxx) xxx-xxxx

Sincerely,

Xxxxx Xxxxx  
Xxxx County  
(xxx) xxx-xxxx

## Personal Property Mail Audit Instructions

Dear Property Owner:

Your personal property account has been designated for audit. To minimize the costs of this program, property owners are being asked to supply data by mail.

The audit will involve records pertaining to equipment and supplies in your possession as of December 31, 20xx. Your cooperation in mailing as many of the following documents as are applicable to your business will be greatly appreciated.

1. Your most current federal income tax depreciation schedule, with all exhibits. This should include all equipment, fully depreciated or not.  
  
This schedule should identify what the asset is. Although the IRS may not require this information, it is essential to our work and may be in *your* best interest.
2. A list of all equipment and supply purchases for 20xx if you are not enclosing a 20xx depreciation schedule.
3. Year-end balance sheet and income statement. If you firm does not produce financial statements, please enclose your Schedule C (or Schedule F) and the balance sheet from your federal tax return.
4. General and subsidiary ledger pages that tie to the balance sheet if accounting year-end is other than December 31, 20xx.
5. A list of non-owned (or leased) assets and the owner's name and address.

Please mail these documents to me within 30 days of the date of this letter.

If you need assistance, please call me at (xxx) xxx-xxxx.

Sincerely,

Xxxx Xxxxxxx  
xxx County  
Personal Property Auditor-Appraiser

**Audit Work Sheet**  
**\_\_\_\_\_ County Department of Personal Property**

Assessment year audited \_\_\_\_\_ Account Number \_\_\_\_\_

**Section I**

	Mailing Name/Address	Business Location
Name	_____	_____
Address	_____	_____
City/State/Zip	_____	_____

**Section II**

General

1. Fiscal closing
2. Supplies

Equipment

1. Are the following included in the cost?
  - Freight
  - Installation costs
2. Is fully depreciated equipment reported?
3. Is lease purchase equipment capitalized at full cost?
4. Are small tools capitalized?
5. Is self-manufactured equipments reported at proper cost:
6. Does any equipment of the premises belong to other?

Other

1. Penalty added
2. Tour premises?

## **Audit Information**

### **Section III**

Years audited

Nature of business

Audit date

Person contacted

Title

Accountant/Bookkeeper

Phone Number

E-mail

### **Omitted Property**

Dear Property Owner:

A recent audit by the Washington State Department of Revenue has revealed equipment and/or supplies that were not included on your personal property affidavit. The omitted value has been added to the affidavit(s) for the omitted year(s). Enclosed are your copies of the affidavit(s) for the omitted year(s).

A value notice will be mailed within a few weeks showing the amended assessed value. If you wish to appeal the assessed value, a petition must be filed by July 1 or within 30 days after the value notice is mailed, whichever is later.

If you have any questions, please call (xxx) xxx-xxxx within 10 days of the date of this letter.

Sincerely,

Xxxxx Xxxxx  
Xxxx County

## APPENDIX A – Laws and Rules

### A.1 Selected Personal Property Tax Laws and Rules

#### 84.04 RCW Definitions

- [84.04.080](#) "Personal property."
- [84.04.090](#) "Real property."
- [84.04.150](#) "Computer software" and related terms.

#### 84.08 RCW General powers and duties of department of revenue

- [84.08.030](#) Additional powers – To test work of assessors – Supplemental assessment lists – Audits.
- [84.08.210](#) Confidentiality and privilege of tax information – Exceptions – Penalty.

#### 84.36 RCW Exemptions

- [84.36.005](#) Property subject to taxation.
- [84.36.015](#) Property valued at less than five hundred dollars – Exceptions.
- [84.36.070](#) Intangible personal property – Appraisal.
- [84.36.110](#) Household goods and personal effects – Fifteen thousand dollars actual value to head of family.
- [84.36.120](#) Household goods and personal effects – Definitions.
- [84.36.255](#) Improvements to benefit fish and wildlife habitat, water quality, and water quantity – Cooperative assistance to landowners – Certification of best management practice – Limitation – Landowner claim and certification.
- [84.36.477](#) Business inventories.
- [84.36.595](#) Motor vehicles, travel trailers, campers, and vehicles carrying exempt licenses.
- [84.36.600](#) Computer software.
- [84.36.630](#) Farming machinery and equipment.

[84.36.635](#) Property used for the manufacture of alcohol fuel or biodiesel fuel.

#### **[84.40 RCW](#) Listing of property**

[84.40.020](#) Assessment date – Average inventory basis may be used – Public inspection of listing, documents, and records.

[84.40.025](#) Access to property required.

[84.40.030](#) Basis of valuation, assessment, appraisal – One hundred percent of true and fair value – Exceptions – Leasehold estates – Real property – Appraisal – Comparable sales.

[84.40.037](#) Valuation of computer software – Embedded software.

[84.40.038](#) Petition county board of equalization – Limitation on changes to time limit – Waiver of filing deadline – Direct appeal to state board of tax appeals.

[84.40.040](#) Time and manner of listing.

[84.40.060](#) Personal property assessment.

[84.40.070](#) Companies, associations – Listing.

[84.40.080](#) Listing omitted property or improvements.

[84.40.085](#) Limitation period for assessment of omitted property or value – Notification to taxpayer of omission – Procedure.

[84.40.110](#) Examination under oath – Default listing.

[84.40.120](#) Oaths, who may administer – Criminal penalty for willful false listing.

[84.40.130](#) Penalty for failure or refusal to list – False or fraudulent listing, additional penalty.

[84.40.185](#) Individuals, corporations, limited liability companies, associations, partnerships, trusts, or estates required to list personalty.

[84.40.190](#) Statement of personal property.

[84.40.200](#) Listing of personalty on failure to obtain statement – Statement of valuation to person assessed or listing – Exemption.

[84.40.340](#) Verification by assessor of any list, statement, or schedule – Confidentiality, penalty.



**84.44 RCW Taxable situs**

- [84.44.010](#) Situs of personalty generally.
- [84.44.020](#) Gas, electric, water companies – Mains and pipes, as personalty.
- [84.44.030](#) Lumber and sawlogs.
- [84.44.050](#) Personalty of automobile transportation companies – Vessels, boats and small craft.
- [84.44.080](#) Owner moving into state or to another county after January 1st.
- [84.44.090](#) Disputes over situs to be determined by department of revenue.

**84.56 RCW Collection of taxes**

- [84.56.070](#) Personal property – Distraint and sale, notice, property incapable of manual delivery, property about to be removed or disposed of.
- [84.56.090](#) Distraint and sale of property about to be removed, dissipated, sold, or disposed of – Computation of taxes, entry on rolls, tax liens.
- [84.56.120](#) Removal of property from county or state after assessment without paying tax.
- [84.56.150](#) Removal of personalty – Certification of tax by treasurer.
- [84.56.160](#) Certification of statement of taxes and delinquency.
- [84.56.170](#) Collection of certified taxes – Remittance.
- [84.56.220](#) Lien of personalty tax follows insurance.
- [84.56.240](#) Cancellation of uncollectible personalty taxes.
- [84.56.250](#) Penalty for willful noncollection or failure to file delinquent list.

**84.60 RCW Lien of taxes**

- [84.60.010](#) Priority of tax lien.
- [84.60.020](#) Attachment of tax liens.
- [84.60.040](#) Charging personalty tax against realty.

**458-07 WAC Valuation and revaluation of real property**

[458-07-030](#) True and fair value – Defined – Criteria – Highest and best use – Data from property owner.

**458-12 WAC Property tax division – Rules for assessors**

[458-12-005](#) Definition – Property – Personal.

[458-12-010](#) Definition – Property – Real.

[458-12-012](#) Definition – Irrigation systems – Real – Personal.

[458-12-050](#) Omitted property and omitted value.

[458-12-055](#) Taxable situs – Real property.

[458-12-060](#) Listing of personal property.

[458-12-110](#) Listing of personal property by the assessor – Penalties for failing to list personal property and for making a false or fraudulent listing.

[458-12-115](#) Personalty – Taxable situs – In general.

[458-12-120](#) Situs of personalty – Beer kegs.

[458-12-155](#) Listing of property – Public lands – Federal lands – Exclusive or concurrent jurisdiction.

[458-12-175](#) Listing of property – Public lands – Leasehold interests and improvements.

[458-12-251](#) Computer software – Definitions – Valuation.

[458-12-310](#) Valuation of property – Personal property.

**458-14 WAC County boards of equalization**

[458-14-015](#) Jurisdiction of county boards of equalization.

[458-14-025](#) Assessment roll adjustments not requiring board action.

**458-16 WAC Property tax – Exemptions**

[458-16-115](#) Personal property exemptions for household goods, furnishings, and personal effects, and for the head of a family.

## A.2 Other Laws and Rules

### 82.08 RCW Retail sales tax

[82.08.02565](#) Exemptions – Sales of machinery and equipment for manufacturing, research and development, or a testing operation – Labor and services for installation – Exemption certificate – Rules.

### 82.12 RCW Use tax

[82.12.02565](#) Exemptions – Machinery and equipment used for manufacturing, research and development, or a testing operation.

### 82.29A RCW Leasehold excise tax

[82.29A.010](#) Legislative findings and recognition.

[82.29A.020](#) Definitions.

### 458-29A WAC Leasehold excise tax

[458-29A-100](#) Leasehold excise tax–Overview and definitions.

[458-29A-200](#) Leasehold excise tax–Taxable rent and contract rent.

[458-29A-400](#) Leasehold excise tax–Exemptions.

[458-29A-500](#) Leasehold excise tax–Liability.

[458-29A-600](#) Leasehold excise tax–Collection and administration.

## A.3 Property Tax Advisories

[6.2.2011](#) Property Taxability of Motor Vehicles

[7.1.2009](#) Sales Tax as an Element of Value

[9.1.2009](#) Assessment of Supplies

[10.1.2009](#) "True Lease" or Security Agreement