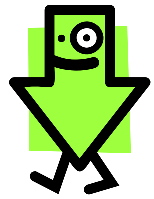
State Tax Commission March 1, 2011 Tip
Topic: Personal Property Reporting (Part 1)



Dear STaCy,

I'm processing the Personal Property Statements I've received and have encountered something unusual. Several taxpayers, using very similar language, have indicated that they, or a professional association to which they belong, have made a determination that the depreciable life of their personal property should be five years. They conclude that since the Section B (Table B) multipliers provide for a 15-year depreciable life, their personal property is incorrectly valued by using the Section B valuation multipliers. One taxpayer went so far as to use the phrase "grossly overstated" to describe the true cash value indication obtained from using the Section B multipliers. The items in question include such things as surgical instruments, day-care equipment, trash receptacles and trash compactors. Does the fact that they are depreciating these items over a 5-year life mean that it is incorrect to use the Section B multipliers?

Sincerely,
Deb Depreciated

Dear Deb,

Table B **does not** indicate that a 15-year useful life has been estimated. In fact, Table B is not a depreciation table at all. Instead, it translates historic cost into current true cash value for the surviving items of personal property as of any given tax day. The 5-year life which they use for financial accounting depreciation purposes is deficient for the purposes of arriving at current true cash value in several ways including the following:

- It does not take into account the possibility that there has been an increase, or decrease, in replacement cost for the items through time. If the replacement cost of an item increases by 2% a year, then over five years the aggregate 10.41% increase in replacement cost offsets part of the realized depreciation for the surviving units that are five years old. In other words, using a straight-line five-year reduction in value fails to consider the fact that the rate of depreciation, when measured against historic cost, is less for valuation purposes than it is for accounting purposes.

- It does not take into account the fact that any items which are destroyed, or lost, or simply taken out of service each year, are depreciated 100%, because they are not reported, and, therefore, are not valued at all on subsequent tax days. Assigning a 100% depreciation rate to the disposals results in a much lower effective rate of depreciation being imputed to the surviving items, even if the financial accounting overall depreciation rate for the group is correctly based on a 5-year life.

- It does not distinguish between instances where an item has exhausted its economic life (has worn out, or been retired due to inutility) and instances where the item has been lost or has broken. Just as is the case for a house that burns down on January 1, the value on

> December 31 is not impaired by the actuarial possibility that the item will be destroyed the next day, the next week or the next year. The claimed 5-year life, since it is a depreciation table, does not distinguish as to the reason that a given item has been taken out of service. This results in an overstatement in the rate of depreciation, as we assessors would use the term.

When the adjustments are made for these factors, the 5-year financial account depreciation is too short for the units still remaining as of each tax day, particularly since it is common for some items to continue in use for many years, even if many are retired in 5 or 6 years.

If you have any additional questions please feel free to contact Tim Schnelle at (517) 373-6262.