

HB 1302

Bill Analysis

February 25, 1997

Brief Description: Clarifying the taxation of intangible personal property.

Bill Sponsors: Representatives Pennington, Kessler, Carrell, Boldt, Thompson, Sheldon, Cairnes, Lambert, B. Thomas, Mitchell, Chandler, Talcott, Cooke, Schoesler, Robertson, Huff, Mielke, Lisk, Delvin, Wensman, Mulliken, Backlund and L. Thomas.

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Background: All property in this state is subject to property tax each year based on the value of the property, unless a specific exemption is provided by law. The state Constitution defines "property" for tax purposes as "everything, whether tangible or intangible, subject to ownership." The Constitution also states that "such property as the Legislature may by general laws provide shall be exempt from taxation."

Intangible property is property that has no physical substance and is not susceptible to being perceived by the senses. Some types of intangible property are exempt from taxation: money, mortgages, notes, accounts, certificates of deposit, tax certificates, judgments, government bonds and warrants, stocks and shares of private corporations, private nongovernmental personal service contracts, and private nongovernmental athletic or sports franchises.

Other types of intangible property are taxable, such as trademarks, trade names, brand names, patents, copyrights, trade secrets, franchise agreements, licenses, permits, agreements to not compete, customer lists, and business goodwill.

Factors that affect the market value of real property or tangible personal property, such as location, zoning, or view, are sometimes referred to as "intangibles." However, these factors are not intangible property. These are merely items that buyers and sellers take into account in determining the market value of property. In contrast, intangible property can be bought and sold completely independently of other property.

Intangible assets are often difficult to identify, locate, and value. The correct treatment of intangible assets for property tax purposes is a matter of some controversy. Recent events have sparked a new level of interest in this issue.

In the late 1980's, the Department of Revenue was sued by Burlington Northern on the grounds that the company was being discriminated against. The taxpayer believed that assessed values established by the Department tend to include the value of intangible assets held by the taxpayer, while assessed values established by county assessors did not include the value of intangible assets. This complex litigation was eventually resolved in the Department's favor.

Recently, Congress allowed the cost of some intangible assets to be amortized over a 15-year period for federal income tax purposes. This made it more likely that businesses would show intangible value on their books and that assessors would tend to tax it. Businesses began to complain about the assessment and taxation of previously untaxed property. Businesses also expressed concern that assessors would begin to further tax these and other intangible assets.

The department responded with a letter in January 1996 advising county assessors not to list and separately value intangible assets. In 1996, bills were introduced in the Legislature to exempt all intangibles from taxation, but none of these bills were enacted by the Legislature.

Summary of Bill: All intangible property is exempt from property tax. Intangible property includes, but is not limited to, the items exempt under current law and items such as trademarks, trade names, brand names, patents, copyrights, trade secrets, franchise agreements, licenses, permits, core deposits of financial institutions, noncompete agreements, clientele, customer lists, patient lists, favorable contracts, favorable financing agreements, reputation, exceptional management, prestige, good name, or integrity of a business.

For purposes of determining the market value of real property and tangible personal property, the presence of existing intangible assets is considered in determining the highest and best use of taxable property, which is defined as the functional use for which the taxable property is employed without regard to the specific identity of the user. This does not require property to be valued at current use.

The market value of real property and tangible personal property must reflect characteristics or attributes such as zoning, location, view, geographic features, easements, covenants, proximity to raw materials, condition of surrounding property, proximity to markets, and the availability of a skilled work force. The exemption is not intended to prohibit the consideration of income generated by or market information related to the property being appraised.

These provisions are effective for taxes levied for collection in 1998 and thereafter.

The act is not intended to incorporate any other state's statutory or case law.

Appropriation: None.

Fiscal Note: Available.

Effective Date: Ninety days after adjournment of session in which bill is passed.