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Court of Appeals of Arizona,
Division 1, Department T.

LEVEL 3 COMMUNICATIONS, LLC., a limited liability company, Plaintiff/Appellant,
v.
ARIZONA DEPARTMENT OF REVENUE; Cochise County; Maricopa County; Pima County; Pinal County; and Yuma County, Defendants/Appellees.

No. 1 CA–TX 08–0001.
|
July 23, 2009.
|
Review Denied April 6, 2010.

West KeySummary

1 **Taxation**
Telecommunication companies

A tax court properly determined that the Arizona Department of Revenue's valuation of a taxpayer telecommunications company's property adequately accounted for and rejected the taxpayer's claims of functional and economic obsolescence. The taxpayer asserted that it had overbuilt its network of fiber and conduit in light of a "skyrocketing demand" that had attracted the attention of suppliers and the unanticipated increase in the capacity of opto-electronic equipment. However, the taxpayer's mere erroneous business decisions and overbuilding were within its control and thus did not support its claim of economic obsolescence.

Cases that cite this headnote

Appeal from the Arizona Tax Court; Cause Nos. TX2002–000605 and TX2005–050383; The Honorable Thomas Dunevant, III, Judge. AFFIRMED.

Attorneys and Law Firms

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MEMORANDUM DECISION

THOMPSON, Presiding Judge.

*1 ¶ 1 Level 3 Communications, L.L.C. (Taxpayer) appeals a judgment rejecting its claims that the Arizona Department of Revenue's (ADOR) valuation of its property failed to adequately account for functional and economic obsolescence. For the following reasons, we affirm the tax court's ruling as to economic obsolescence.

FACTUAL AND PROCEDURAL BACKGROUND

¶ 2 Taxpayer is a telecommunications company that provides voice, data, and internet communications services through a network of fiber-optic cable running throughout North America. Its cable network consists of 18,900 intercity miles of fiberoptic cable and twenty-seven metropolitan networks. The network enters Arizona from the west through Yuma County; crosses Maricopa, Pinal, and Pima Counties; and exits to the east through Cochise County.

¶ 3 This case arises out of the valuation of Taxpayer's personal property for purposes of the Arizona property tax. Article 9, Section 11, of the Arizona Constitution requires the Arizona Legislature to prescribe "the manner, method and mode of assessing, equalizing and levying taxes in the State of Arizona." In Arizona Revised Statutes (A.R.S.) §§ 42–14401 to 42–14404, the Legislature directs ADOR to centrally value telecommunication companies' property. The property at issue includes intracity cable configurations and collation facilities, conduit (the hollow tube through which

fiber cable is pulled), and fiber-optic cable (collectively, the Property).

¶ 4 Section 42–14402(A)(7) requires the telecommunications company's chief officer in this state to file a statement under oath with ADOR by April 1 containing, among other things, a complete and correct inventory of all personal property it owned in this state on the preceding January 1, where the property was located, and its value. Section 42–14403(1) (1999) instructs ADOR value the property as follows:

> On or before August 31 of each year the department shall determine the valuation as of January 1 of the property of all telecommunications companies operating in this state at its full cash value. Real estate shall be valued at market value, and personal property shall be valued on a unitary basis at its historical cost less depreciation. For purposes of this section:
>
> 1. Depreciation is computed based on the tables adopted by the department in its personal property manual in effect on January 1, 1993 for the following categories:
>
> (a) Buildings with a twenty-five year life.
>
> (b) Cable with a fifteen year life.
>
> (c) Telecommunications equipment with a five year life.
>
> (d) Any other telecommunications property that is not included in subdivisions
>
> (a), (b) and (c) with a seven year life.

The statute defines "historical cost" as "the original cost as reported on the company's books and records." A.R.S. § 42–14403(2). The tables incorporated into A.R.S. § 42–14403 include an example permitting ADOR to value a property below the valuation stated in the table.

***2** ¶ 5 Applying the property valuation formula in A.R.S. § 42–14403 to Taxpayer's information, ADOR assessed the full cash value. Counties use such valuations to assess, levy, and collect taxes for themselves and for each taxing unit or district appearing upon their rolls.

¶ 6 To determine whether Taxpayer qualified for any additional adjustment for obsolescence, ADOR subsequently hired Stephen Barreca to identify all forms of obsolescence associated with Taxpayer's property and to develop a market value figure for the relevant tax years. These figures would allow ADOR's appraiser, David Derron, to compare Barreca's independently determined market value under the cost approach with ADOR's statutory valuation under A.R.S. § 42–14403 and decide whether Taxpayer was entitled to an additional adjustment for obsolescence.

¶ 7 Barreca studied lists of Taxpayer's property and used indices to trend the original costs to the valuation date value. He then performed a replacement-cost new analysis, assuming that three conduits would best approximate the utility of the property appraised. Barreca used the recognized cost-to-capacity model to calculate the cost of installing three conduits versus the twelve that had been originally installed. Taxpayer's expert witness conceded that the cost-to-capacity analysis is a generally accepted valuation technique that assumes that not all costs vary with size in a straight line.

¶ 8 Barreca then derived and deducted the depreciation, including all relevant forms of obsolescence, from the replacement cost new. He considered, but did not use, the income and sales comparison methods of valuation because he deemed them inappropriate. Barreca's cost valuations for each tax year, along with the full cash valuations the Department had derived from strictly applying A.R.S. § 42–14403, are as follows:

Tax Year	Barreca's Cost Valuations	ADOR's Cost Valuations
2003	$132,286,083	$116,813,012
2004	$123,860,625	$101,314,083
2005	$127,535,177	$98,772,478
2006	$131,030,571	$93,115,694
2007	$164,907,840	$90,000,000

In light of these results, ADOR determined that no further downward adjustment of the statutory valuations was warranted.

¶ 9 Taxpayer unsuccessfully appealed ADOR's valuations for tax years 2003 through 2006 to the State Equalization Board (the Board). Taxpayer then appealed to the tax court pursuant to A.R.S. §§ 42–14005, 42–16158, 42–16168, 42–16201, 42–16203, 42–16204 and 42–16207. Taxpayer contended that the ADOR and Board values were "excessive and inequitable because, among other reasons, they failed to recognize sufficient obsolescence relating to the Subject Property." The tax court consolidated these complaints.

¶ 10 Meanwhile, the Arizona Legislature amended A.R.S. § 42–14403(A) in 2006 to state: "In addition, the taxpayer may submit documentation showing the need for, and the department shall consider, an additional adjustment to recognize obsolescence using standard appraisal methods and techniques." *See* 2006 Ariz. Sess. Laws, ch. 38, § 1 (2nd Reg.Sess.). The amendment also defined obsolescence as "a reduction in the value of an asset resulting from functional or economic obsolescence." A.R.S. § 42–14403(0(2) (2006).

***3** ¶ 11 After Taxpayer sought additional obsolescence for the 2007 tax year, ADOR reduced its full cash value by $5 million based on obsolescence believed to exist in its fiber-optic cable and conduit. ADOR had based its valuation on property that Taxpayer had owned in Arizona on or before January 1, 2006, preceding the statute's effective date of September 21, 2006. ADOR then set the full cash value for the 2007 tax year at $90,000,000.[1] Taxpayer appealed that valuation directly to the tax court, where it was consolidated along with the other cases.

¶ 12 ADOR presented evidence that it had applied A.R.S. § 42–14403 to Taxpayer's data, and, in each case, the resulting values fell below the actual fair market value. ADOR consequently argued that Taxpayer was not entitled to further reductions for obsolescence below the statutory calculation.

¶ 13 Derron described ADOR's calculation of the depreciated values based upon the statutory formula in A.R.S. § 42–14403. It used the installation years and the written-down costs supplied by Taxpayer, and not the original costs, to compute depreciation.[2] The bulk of the overall value was attributable to conduit; for example, in 2003 conduit accounted for $105,495,095 of more than $133,000,000 in Arizona property.

¶ 14 In accordance with A.R.S. § 42–14403(B)(1), Derron depreciated the cable on a fifteen-year life and calculated the resulting values for all the property in tax years 2003 to 2007: 116,813,012, $101,314,083, $98,772,478, $93,115,694, and $95,011,763. Derron testified that he believed that the statutory formula precluded him from making any reductions for obsolescence. Because the resulting full cash values derived under A.R.S. § 42–14403 fell below the actual fair market value, ADOR determined that it had no discretion to allow for obsolescence below the statutory value.

¶ 15 Taxpayer introduced testimony from appraiser Jerome Weinert of AUS Consulting. Weinert based his opinion supporting an adjustment for obsolescence on replacement cost and income valuations. He did not employ the third standard appraisal technique, the market approach.

¶ 16 Weinert had no specific Arizona income data. He used the discounted cash flow (DCF), an income valuation technique, to estimate the value of Taxpayer's North American assets. A DCF analysis "recognizes the future cash outflows that are necessary to achieve the projected cash flows." Am. Soc'y of Appraisers, *Valuing Machinery and Equipment: The Fundamentals Of Appraising Machinery and Technical Assets* 180 (2d ed.2000) [hereinafter "*Valuing Machinery and Equipment* "]. The technique "measures the direct economic benefits derived from ownership, in the form of future cash inflows and outflows attributed to the property, stated at their present value." *Id.*

¶ 17 Weinert acknowledges that Taxpayer does not report any information on its revenues, expenses, or income on a statewide basis in Arizona. The economic obsolescence he found was on a national going concern basis.

***4** ¶ 18 Weinert also used the cost method to value Taxpayer's property. This entailed starting with impaired costs and making adjustments to return the values to the original costs. He then "trended" the values to calculate the "reproduction cost new," or the recreated value of Taxpayer's net worth in January of the preceding year. Next, Weinert used a methodology to determine the replacement cost new values, or the current cost of a similar new property having the nearest equivalent utility as the property being appraised, *Valuing Machinery and Equipment* 44, focusing on the cable and conduit. Weinert's replacement cost analysis

incorporated the assumption that each year eight or nine of the conduits carrying the fiber-optic cable would not be replaced. After calculating the replacement cost new, Weinert further deducted for physical depreciation and additional functional obsolescence.

¶ 19 Finally, Weinert deducted economic obsolescence from the depreciated replacement cost new results. This step entailed a comparison of the values obtained from the income and cost methods and attributed the difference to economic obsolescence. Weinert then deducted the economic obsolescence percentage from the replacement cost new less depreciation figure to arrive at the final full cash value. [3]

¶ 20 Prior to ruling, the tax court requested and received briefing on the obsolescence issue in light of our decision in *Eurofresh, Inc. v. Graham County*, 218 Ariz. 382, 187 P.3d 530 (App.2007). Neither party requested findings of fact under Arizona Rule of Civil Procedure 52(a). The tax court then ruled in favor of ADOR and entered judgment. Taxpayer appealed.

DISCUSSION

A. Economic obsolescence

¶ 21 In an appeal following a bench trial, we view the facts in the light most favorable to sustaining the judgment. *See Cimarron Foothills Cmty. Ass'n v. Kippen*, 206 Ariz. 455, 457, ¶¶ 1–2, 79 P.3d 1214, 1216 (App.2003). We review questions of law and mixed questions of law and fact de novo. *Robson Ranch Mountains, L.L.C. v. Pinal County*, 203 Ariz. 120, 125, ¶ 13, 51 P.3d 342, 347 (App.2002).

1. Taxpayer's burden

¶ 22 The valuation "as approved by the appropriate state or county authority is presumed to be correct and lawful." A.R.S. § 42–16212(B) (2006). A taxpayer can overcome the presumption with competent evidence that the valuation is excessive. *Eurofresh*, 218 Ariz. at 386, ¶ 16, 187 P.3d at 534. Evidence is competent for this purpose "when it is derived by standard appraisal methods and techniques which are shown to be appropriate under the particular circumstances involved." *Inspiration Consol. Copper Co. v. Ariz. Dep't of Revenue*, 147 Ariz. 216, 223, 709 P.2d 573, 580 (App.1985), superseded by statute on other grounds, A.R.S. § 12–348(A) (2003).

¶ 23 If the taxpayer and taxing authority employ different valuation methods, the taxpayer's evidence is not competent unless it demonstrates the appropriateness of its method under the circumstances. *Id.* at 219, 709 P.2d at 576. If the parties use the same valuation method "but differ as to the correct treatment of factors utilized in such method, the taxpayer's evidence is nevertheless competent and sufficient to overcome the statutory presumption." *Id.* Further, the tax court cannot independently value the property until the taxpayer presents competent evidence rebutting the presumption that the taxing authority's valuation is correct. *Eurofresh*, 218 Ariz. at 386, ¶ 18, 187 P.3d at 534.

***5** ¶ 24 Obsolescence is defined as a loss of value and classified as either economic or functional. *Nordstrom, Inc. v. Maricopa County*, 207 Ariz. 553, 559, ¶ 27, 88 P.3d 1165, 1171 (App.2004). Economic obsolescence is "a loss in value caused by forces external to the property and outside the control of the property owner." *Ariz. Dep't. of Revenue v. Questar S. Trails Pipeline Co.*, 215 Ariz. 577, 580, ¶ 12, 161 P.3d 620, 623 (App.2007) (*quoting Magna Inv. & Dev. Corp. v. Pima County*, 128 Ariz. 291, 293, 625 P.2d 354, 356 (App.1981)); Black's Law Dictionary 1107 (8th ed.2004) (economic obsolescence "results from external economic factors, such as decreased demand or changed governmental regulations."). More recently, this court defined economic obsolescence in *Eurofresh* as "temporary or permanent impairment of the utility or salability of an improvement or property due to negative influences outside the property." 218 Ariz. at 386, ¶ 22, 187 P.3d at 534 (quoting *Appraisal Institute, The Appraisal of Real Estate* 363 (12th ed.2001.)).

¶ 25 In *Eurofresh*, the taxpayer sought a forty-percent reduction from the agreed replacement cost value of the property based upon economic or external obsolescence. *Id.* at 383, 384 n. 3, ¶¶ 1, 8, 187 P.3d at 531, 532 n. 3. The taxpayer had asserted that "the external obsolescence evidenced by the three other greenhouse sales is market-wide and for that reason, must necessarily affect the value" of its property. *Id.* at 387, ¶ 25, 187 P.3d at 535. The taxpayer's appraiser concluded that three other greenhouses had sold for less than their adjusted replacement cost and the differential was attributable to market-wide external obsolescence. *Id.* at 384–85, ¶ 9, 187 P.3d at 532–33.

¶ 26 We adopted a three-part test that a taxpayer must meet to support a claim for external obsolescence. *Id.* at 390, ¶ 37, 187 P.3d at 538. The taxpayer must submit probative evidence

establishing: (1) the cause of the claimed obsolescence, (2) the quantity of the claimed obsolescence, and (3) that the asserted cause of the obsolescence actually affects the property. *Id.*

¶ 27 Applying this test, we held that the taxpayer had offered no probative evidence that the obsolescence observed in comparable properties also affected the property at issue. *Id.* at 392–93, ¶ 49, 187 P.3d at 540–41. Consequently, we reversed the tax court's judgment adopting the taxpayer's proposed full cash value. *Id.*

2. Taxpayer's evidence

¶ 28 Applying *Eurofresh* to this case, the tax court found that Taxpayer's evidence did not satisfy its requirements because "the loss in value of the property was not caused by obsolescence." Rather, "Level 3 simply underestimated the future supply of fiber-optic capacity. Mere erroneous business judgment does not create obsolescence." The evidence showed that the industry was in economic difficulty, but demand continued, though at a slower rate than Taxpayer had expected. Consequently, the tax court entered judgment in favor of ADOR without discussing the merits of the respective experts' opinions. Indeed, it stated that the "underlying facts" of its analysis were "not in dispute."

*6 ¶ 29 The tax court accepted Taxpayer's evidence that a "perfect storm" had struck. Taxpayer contended that the utility and salability of its property were permanently impaired as a result of having "overbuilt" its network of fiber and conduit and that installation costs for those accounts combined for eighty-five percent of its total reported costs. According to Taxpayer, "[t]hese facts illustrate why the 'historical costs' now being used by ADOR to value Level 3's property are too high and must be adjusted downward to account for obsolescence."

¶ 30 Taxpayer points out that increased competition and reduced demand, recognized external obsolescence considerations, were established here. *See Application of Putnam Theatrical Corp.*, 16 A.D.2d 413, 228 N.Y.S.2d 93, 98–99 (N.Y.App.Div.1962) (finding that a theater suffered from economic obsolescence based upon a substantial decline in attendance after the advent of television, and an office area was affected by competition from shopping centers); Black's Law Dictionary 1107 (external obsolescence "results from external economic factors, such as decreased demand"). Taxpayer also correctly points out that economic obsolescence need not be permanent. *Eurofresh*, 218 Ariz. at 386, ¶ 22, 187 P.3d at 534 (external obsolescence may be "a temporary or permanent impairment").

¶ 31 More fundamentally, however, our cases have recognized that external obsolescence is not established by a factor within the taxpayer's control. *Questar*, 215 Ariz. at 580, ¶ 12, 161 P.3d at 623 (economic obsolescence is "a loss in value caused by forces external to the property and outside the control of the property owner"); *Eurofresh*, 218 Ariz. at 386, ¶ 22, 187 P.3d at 534 (in the real property context, external obsolescence "is not usually considered curable on the part of the owner, landlord, or tenant"). Taxpayer states that it overbuilt in light of the "skyrocketing demand" that attracted the attention of suppliers and the unanticipated increase in the capacity of opto-electronic equipment. Taxpayer's business decisions and overbuilding were within its control and thus do not support its claim of economic obsolescence. As the tax court explained, "[m]ere erroneous business judgment does not create obsolescence."

¶ 32 Furthermore, as ADOR argued to the tax court in post-trial briefing, there was no evidence that Taxpayer's property had actually been affected in a meaningful way. There had been no filings for bankruptcy; indeed, Taxpayer actually had continued to acquire companies and properties and was expanding in Arizona.[4] ADOR's worksheets also reflect that Taxpayer had added new property, and the maps in Weinert's appraisal show expansion both in Arizona intercity and metro routes. This evidence supports the tax court's holding that Taxpayer failed to show any actual effect. *See generally Putnam*, 228 N.Y.S.2d at 98 (rejecting an economic obsolescence claim because "[t]he reasons advanced to show a down-grading of the area are overborne by evidence that Syracuse is the focal point of a region which has been characterized by rapid growth").

*7 ¶ 33 Alternatively, we can affirm the tax court's holding on another basis identified in *Eurofresh*. The *Eurofresh* taxpayer had incorrectly argued that the property must suffer from external obsolescence because the taxpayer's appraiser observed external obsolescence in other greenhouses. 218 Ariz. at 391–92, ¶ 45, 187 P.3d at 539–40. Taxpayer here asks us to take a similar leap of faith with Weinert's actual market transactions evidence.

¶ 34 In this case, Weinert developed a cost of replacement less depreciation indicator of value but then sought a further reduction for economic obsolescence ranging from 24.52 percent to 45.77 percent for tax years 2003 to 2007.

Weinert's calculations are based upon the North American going concern value and are not specific to Arizona. Taxpayer does not even maintain separate data on income, productivity or profitability of its Arizona property. More importantly, Weinert failed to show whether or how the market-wide obsolescence data actually affects Taxpayer's assets in Arizona.

¶ 35 At trial, Weinert produced a list of sales allegedly demonstrating that the value of telecom network facilities are deeply discounted from original cost. Yet Weinert made no adjustments for comparability, the comparison properties that he used were dissimilar in configuration and scope, and some of his comparison transactions were bankruptcy sales. These values are not comparable to Taxpayer's property, as Taxpayer has not filed for bankruptcy, and the evidence reveals that it has acquired properties and is expanding in Arizona. Indeed, the Executive Summary of Weinert's appraisal acknowledges the lack of comparability: "The market or comparable sales approach to value looks to market sales of comparable property in order to arrive at value. In this appraisal, the market approach was not utilized due to concerns over comparability." By its own expert's admission, Taxpayer's information does not pass muster under *Eurofresh*.

¶ 36 Taxpayer's lack of data specific to the income, productivity, or profitability of its Arizona tangible assets is fatal to its economic obsolescence claim. Its position seems to be that the value and associated property tax on its tangible assets in Arizona should be reduced any time Taxpayer experiences a problem somewhere else in its system. Taxpayer argues that its Arizona tangible assets experience economic obsolescence of the same type and rate as any other property in its system. Even if we take this analysis at face value, we must reject it as a matter of law because it is the type of unsupported conjecture we declined to adopt in *Eurofresh*. [5] Consequently, we affirm the tax court's rejection of economic obsolescence on this basis as well. [6]

B. Functional obsolescence

¶ 37 Taxpayer also complains that the tax court failed to account for functional obsolescence. This type of obsolescence is either "a physical element that buyers are unwilling to pay for or a deficiency that impairs the utility of property when compared to a more modern replacement, leading to a loss in value." *Nordstrom*, 207 Ariz. at 559–60, ¶ 27, 88 P.3d at 1171–72.

***8** ¶ 38 ADOR contends that the tax court addressed functional obsolescence by stating: "Since the loss in value of the property was not caused by obsolescence, it cannot be deducted. Therefore, the amount of lost value does not matter." In other words, even allowing for the unused conduits, ADOR's value was lower than the property's fair market value and the functional obsolescence claim fails.

¶ 39 We assume that the tax court considered the functional obsolescence evidence presented at trial. *See Fuentes v. Fuentes*, 209 Ariz. 51, 55–56, ¶¶ 17–18, 97 P.3d 876, 880–81 (App.2004) (explaining that an appellate court can assume that a factor was considered when a party submitted evidence pertaining to it and the evidence was admitted). The tax court implicitly rejected the functional obsolescence claim by entering judgment in favor of ADOR and the Counties.

¶ 40 Both parties' experts acknowledged that Weinert testified that ADOR should deduct nearly one-twelfth of the total cost for each unused conduit as functional obsolescence. He based this conclusion on a model using what he termed "civil construction" costs. Weinert conceded, however, that the American Society of Appraisers' treatise did not recognize his obsolescence methodology as authoritative.

¶ 41 ADOR countered this evidence with testimony from Barreca based on a cost-to-capacity model recognized by appraisal authorities. Unlike Weinert, Barreca did not find that this inutility constituted functional obsolescence. In Barreca's view, it was a matter of economic obsolescence to be factored into a particular asset or cluster of assets.

¶ 42 A former telecommunications engineer, Barreca testified that many construction costs would be incurred whether there were three conduits or twelve conduits. Consequently, any loss in value from functional obsolescence would not be nearly as severe as Weinert had projected. When Barreca factored in his value for obsolescence based upon the failure to use conduit, the gross value for all of Taxpayer's Property still exceeded the statutory value that ADOR had established.

¶ 43 Accordingly, there was already unrecognized obsolescence in the value that ADOR obtained from using the statutory formula. Because no obsolescence adjustment was necessary, the tax court properly concluded that "the amount of lost value does not matter." Taxpayer accuses the tax court of ignoring functional obsolescence and demands reversal. But as ADOR points out, a trier of fact is not bound by opinion testimony from Weinert or any other expert. *See*

Ariz. R. Evid. 702 (expert testimony is designed to assist the trier of fact). The tax court is in the best position to evaluate this testimony. *See Magna*, 128 Ariz. at 294, 625 P.2d at 357. Accordingly, the tax court was not bound to accept Weinert's characterization of this as functional obsolescence and had the discretion to disregard it. *See Crystal Point Joint Venture v. Ariz. Dep't. of Revenue*, 188 Ariz. 96, 104, 932 P.2d 1367, 1375 (App.1997) (explaining that the trier of fact may disregard expert testimony in a number of circumstances, including when it is contradicted by other expert testimony or an expert's factual predicates are disputed).

***9** ¶ 44 Moreover, the tax court was required to judge the impact of any personal property obsolescence on a unitary basis, i.e., the property as a whole. *See* A.R.S. § 42–14403(A). Although certain pieces of the Property may have been obsolete, the result was governed by the impact of that factor on the Property as a whole. In light of Barreca's evaluation, the tax court could reasonably find that Taxpayer had failed to prove that obsolescence of whatever kind had reduced the full cash value below the statutory valuation amount. *See Flood Control Dist. of Maricopa County v. Hing*, 147 Ariz. 292, 300, 709 P.2d 1351, 1359 (App.1985) (citing *State Tax Comm'n v. United Verde Extension Mining Co.*, 39 Ariz. 136, 140, 4 P.2d 395, 399 (1931)) (explaining that an appellate court will uphold a property valuation that falls anywhere between the high and low estimates so long as it is reasonable).

¶ 45 The tax court also could reject Weinert's claim based upon his failure to employ a standard appraisal technique appropriate under the circumstances for valuing the conduit and fiber costs. First, Weinert developed a replacement cost value. ADOR concedes that this is a standard step in the cost approach to value. But Weinert then developed a linear theory of deducting costs and incorrectly assumed that a backhoe would be employed to replace the conduit. This method was not appropriate under the circumstances. More globally, Weinert could not produce any authority to support using the income shortfall calculation from a system going-concern value and applying it to the Arizona tangible asset cost value. This evidence was not competent and consequently could not rebut ADOR's valuation.

CONCLUSION

¶ 46 We affirm the tax court's judgment. In addition, we deny Taxpayer's request for attorneys' fees on appeal in accordance with A.R.S. § 12–348(B) (2003).

CONCURRING: DONN KESSLER, Judge and MARGARET H. DOWNIE, Judge.

All Citations

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Footnotes

1 Derron testified that, had Barreca's report been available at this point, ADOR would not have granted the reduction.

2 Taxpayer reduced the value of its intercity cable and conduit to "fair value," or the estimate of the amount at which an asset could be bought or sold in a transaction between willing parties. Financial Accounting Standard (FAS) 157. Taxpayer based its fair value on an impairment study performed by American Appraisal in accordance with FAS 121 and 144. The FAS standards require that long-lived assets be reviewed for impairment when events or changed circumstances indicate that the asset's carrying amount may not be recoverable. FAS Statement No. 121, as amended by FAS Statement No. 144. In conducting the review, the entity should estimate the future cash flows expected to result from the asset's use and disposition. FAS Statement No. 121. If the undiscounted total future cash flow (excluding interest) is less than the carrying amount, the entity may recognize impairment loss. *Id.* The study wrote down the system-wide value of intercity conduit by about $884 million, and Taxpayer recognized a $2,364 billion impairment of certain North American assets.

3 Whereas Weinert opined that the conduit had a functional and economic life of twenty years, Barreca contended that the conduit had a forty-year depreciable life. ADOR depreciated the conduit based upon a fifteen-year life under A.R.S. § 42–14403(B)(1)(b), giving the Property even more built-in obsolescence than Weinert would have attributed to it. The accelerated depreciation would have included additional depreciation that might be attributed to obsolescence.

4 ADOR had allowed for external obsolescence in valuing the Property and maintained that position at trial. At that time, however, ADOR did not have the benefit of this court's opinion in *Eurofresh* setting a competency standard for external obsolescence evidence.

5 Two Indiana cases making an obsolescence adjustment on an income shortfall basis are distinguishable. Both *Meridian Towers East & West v. Washington Township Assessor*, 805 N.E.2d 475 (Ind. Tax Ct.2003), and *Canal Square Ltd.*

Partnership v. State Board of Tax Commissioners, 694 N.E.2d 801 (Ind. Tax Ct.1998), deal with valuations of property located all in one state. They provide no basis for calculating obsolescence on a system-wide basis and applying it to only those assets in a particular state or locale. Taxpayer's reliance on such authority is misplaced.

6 We also reject Taxpayer's request for additional obsolescence because it amounts to double counting depreciation. Taxpayer argued in a post-trial memorandum that the utility and salability of its Property is permanently impaired as a result of having "overbuilt" its network of fiber and conduit and that installation costs for those accounts account for eighty-five percent of its total reported costs. Taxpayer claimed that "[t]hese facts illustrate why the 'historical costs' now being used by ADOR to value Level 3's property are too high and must be adjusted downward to account for obsolescence." But even if we accept Taxpayer's analysis of the cause of obsolescence, it is already accounted for in the replacement cost less depreciation value of the four conduit system Weinert developed. To further deduct for obsolescence would result in double counting.

Taxpayer defends Weinert's analysis as simply a method for capitalizing income loss, which is a recognized method similar to market extraction. But ADOR points out that Weinert's circular usage of income shortfall is not an accepted capitalized loss method and has been rejected. *See United Tel. Co. v. Dep't. of Revenue,* 307 Or. 428, 770 P.2d 43, 51 (Or.1989). More fundamentally, market extraction and income capitalization measure all forms of depreciation, including external/economic obsolescence, and should not be deducted after an appraiser has already adjusted to account for obsolescence.

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