



COMMONWEALTH OF VIRGINIA

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April 26, 2010

The Honorable Samuel W. Swanson, Jr.
Pittsylvania County Commissioner of the Revenue
P.O. Box 272
Chatham, Virginia 24531

Dear Mr. Swanson:

I am responding to your request for an official advisory opinion in accordance with § 2.2-505 of the *Code of Virginia*.

Issue Presented

You ask whether certain deposits of clay and sand are subject to assessment as subsurface minerals for purposes of local real property taxes. If so, you ask at what point in time the assessment of such clay and sand would be appropriate. Finally, you ask whether the capitalized income strength method of valuation for assessing subsurface minerals is appropriate under §§ 58.1-3286 and 58.1-3287.

Response

It is my opinion that clay and sand that are in place, *i.e.*, beneath the surface of real property, are minerals that are subject to local taxation whether or not the property is under development. It further is my opinion that the initial discovery of a mineral generally is the time at which assessment would occur. Finally, it is my opinion that the income capitalization methodology that you describe would comply with §§ 58.1-3286 and 58.1-3287.

Background

You indicate that a brick company intends to extract clay deposits from a 1,200-acre tract of land in Pittsylvania County that the company recently purchased. You state that at the present time no mining activity has occurred. You also indicate that the owner of certain land has been dredging sand from the bed of a river located on his property. Further, you relate that the Virginia Department of Mines, Minerals, and Energy has identified this landowner as being engaged in production.

You state that you use a capitalization rate obtained from the contractor that performs Pittsylvania County's reassessments to ascertain the present value of undeveloped minerals based on projected future earnings. You indicate that you adjust this capitalization rate only in the year in which the county reassessment becomes final; however, you assess undeveloped minerals annually using the prevailing capitalization rate and year-to-year variances in the tonnage of materials reported to the Department of Mines as having been extracted.

Applicable Law and Discussion

Pursuant to Article X, § 4 of the Constitution of Virginia and § 58.1-3000, localities in Virginia have the authority to tax real estate, coal, and other mineral lands.¹ Therefore, whether a locality may impose real estate taxes on deposits of clay and sand depends on whether these substances constitute “minerals.”

A 1977 opinion of the Attorney General (“1977 Opinion”) has analyzed a similar question regarding a tract of land utilized as a stone quarry.² The 1977 Opinion concluded that stone constitutes a mineral subject to local assessment.³ Further, the 1977 Opinion concluded that when the General Assembly enacted § 58-744, it contemplated the definition of the term “mineral” that the Supreme Court of Virginia tacitly approved.⁴ In interpreting the term, the Virginia Supreme Court noted that “[t]he word “mineral,” in the popular sense, means those inorganic constituents of the earth’s crust which are commonly obtained by mining or other process for bringing them to the surface for profit.”⁵ Therefore, stone is a mineral when it is extracted from land for profit.⁶

Based on this reasoning, clay and sand deposits would also be “minerals” subject to local real property tax assessment.⁷ It is clear that the clay and sand at issue will be extracted for commercial purposes. Although Title 58.1 does not define the term “mineral,” Title 45.1, which governs mines and mining in the Commonwealth, contains several definitions of “mineral.”⁸ I note that § 45.1-161.8 specifically includes clay and sand in the definition of “mineral.”⁹ Therefore, it is my opinion that clay and sand constitute “minerals” and are subject to local assessment.

¹ See 1993 Op. Va. Att’y Gen. 221, 224, cited in 2007 Op. Va. Att’y Gen. 138, 140 n.1.

² See 1976–1977 Op. Va. Att’y Gen. 267, 267.

³ *Id.* at 268 (interpreting § 58-744, predecessor to § 58.1-3286).

⁴ *Id.* at 267-68.

⁵ *Warren v. Clinchfield Coal Corp.*, 166 Va. 524, 528, 186 S.E.2d 20, 22 (1936) (citation omitted).

⁶ See 1976–1977 Op. Va. Att’y Gen., *supra* note 2, at 268.

⁷ You also inquire whether sand that is dredged from a riverbed is subject to assessment pursuant to §§ 58.1-3286 and 58.1-3287 to the same degree as minerals that are “mined” in the traditional sense. I note that neither of these statutes expressly or impliedly draws a distinction regarding the method for mining or extraction of minerals. Furthermore, since the General Assembly intended that these statutes require the assessment of “minerals,” as defined by the *Warren* court, then it is clear that the assessment of minerals is not limited to a particular means of extraction or mining. See *supra* notes 4-5 and accompanying text. The *Warren* court endorsed a definition of “minerals” that included “inorganic constituents of the earth’s crust which are commonly obtained by mining *or other process.*” *Warren*, 166 Va. at 528, 186 S.E.2d at 22 (emphasis added) (citation omitted). Therefore, in my opinion, the sand deposits that you describe are subject to assessment.

⁸ See *Branch v. Commonwealth*, 14 Va. App. 836, 839, 419 S.E.2d 422, 425 (1992) (noting that because *Code* is one body of law, sections using same phraseology may be consulted to determine meaning of statute).

⁹ I also note that § 45.1-229 defines the term “other minerals” with the same language used by § 45.1-161.8 to define the term “mineral.” See also VA. CODE ANN. § 45.1-161.292:2 (2002) (defining “mineral” with same language as § 45.1-161.8); § 45.1-180 (2002) (defining “mineral,” related to requirement for permit for mining operations other than drilling or mining of coal, as “[o]re, rock, and any other solid homogenous crystalline chemical element of compound that results from the inorganic processes of nature other than coal”).

You next ask at what point clay, sand, and other minerals become subject to assessment. Article X, § 4 of the Virginia Constitution requires taxable real estate, including mineral lands, to be “assessed for local taxation in such manner and at such times as the General Assembly may prescribe by general law.” Sections 58.1-3286 and 58.1-3287 contain the requirements for assessing mineral lands.¹⁰ Section 58.1-3287 mandates that in any year when a locality conducts a general reassessment of real estate, the assessor must assess the fair market value of mineral lands and minerals separately from other real estate. Such assessment must be done in accordance with § 58.1-3286, which requires assessments of mineral lands to be based upon:

1. The area and the fair market value of such portion of each tract as is improved and under development;
2. The fair market value of the improvements upon each tract; and
3. The area and fair market value of such portion of each tract not under development.

In each of the years between general reassessments, § 58.1-3287 requires commissioners of the revenue (“commissioners”) to “adjust [these] assessed values in such manner as to reflect such changes as may have occurred during the preceding year, especially such changes as may have operated to increase or decrease” any of the values.

One type of change that has been recognized as potentially operating to increase or decrease the value of a parcel of real estate, within the meaning of § 58.1-3287, is the initial discovery of minerals thereon.¹¹ Thus, minerals should be separately and specially assessed upon their discovery, whether that occurs in the course of a general reassessment of real estate or in the years between general reassessments.¹² Furthermore, I note that § 58.1-3286 specifically requires commissioners to determine the “fair market value of such portion of each tract not under development.” The fact that no mining operations have occurred does not shield the minerals underlying a parcel from assessment.

Finally, you ask whether the income capitalization method that you employ to assess the value of such minerals complies with §§ 58.1-3286 and 58.1-3287. Section 58.1-3286 requires that commissioners assess mineral lands at their fair market value and to record such mineral assessments separately from the assessed fair market value of the land overlying the minerals. The only additional mandate on such assessments imposed by § 58.1-3287 is the directive that commissioners adjust the values of minerals included in general reassessments based on “such changes as may have occurred during the preceding year.”

The Virginia Supreme Court has “defined the fair market value of a property as its sale price when offered for sale ‘by one who desires, but is not obliged, to sell it, and is bought by one who is under no necessity of having it.’”¹³ I note that there are three generally accepted approaches for ascertaining the

¹⁰ See 1992 Op. Va. Att’y Gen. 178, 180.

¹¹ *Id.*

¹² See *id.* at 181 n.1.

¹³ *Keswick Club, L.P. v. County of Albemarle*, 273 Va. 128, 136, 639 S.E.2d 243, 247 (2007) (quoting *Tuckahoe Woman’s Club v. City of Richmond*, 199 Va. 734, 737, 101 S.E.2d 571, 574 (1958)).

fair market value of real property: “the cost method, the market method, and the income capitalization method.”¹⁴ The income capitalization approach to valuation is recognized as a useful method of ascertaining the fair market value of income-producing property such as mineral rights.¹⁵ Under this approach, the property’s fair market value derives from an estimate of the cash flows that the property will generate, to which a multiplier (“capitalization rate”), which is based on the average rate of return of investment from similar properties, is applied to arrive at the present capital value of the property.¹⁶ In my opinion, reliance upon the tonnage of extracted minerals reported to the Department of Mines, Minerals and Energy is a reasonable means of estimating the income that would accrue to an owner in mineral land inasmuch as the depletion of minerals beneath the land’s surface would diminish the amount of material that the owner would be able to offer for sale.

Sections 58.1-3286 and 58.1-3287 do not prescribe which valuation methodology a commissioner must employ to ascertain the fair market value of mineral lands. Similarly, I find no law that specifically requires a commissioner who employs an income capitalization approach to adjust the capitalization rate on an annual basis. Since §§ 58.1-3286 and 58.1-3287 do not mandate a specific methodology by which a commissioner is to ascertain such fair market value, it is my opinion that the method for determination is within his discretionary authority.¹⁷ Of course, any method a commissioner uses must be reasonable.¹⁸ I note, however, that the accuracy of a capitalization rate, related to calculation of the time value of money versus the compensation factor for the risk associated with a venture, contains an element of subjectivity.¹⁹ Therefore, a party aggrieved by an assessment derived from a static capitalization rate may be able to present facts that would undermine the validity of the prevailing rate based on changes in conditions that occur in years between general reassessments.²⁰

Conclusion

Accordingly, it is my opinion that clay and sand that are in place, *i.e.*, beneath the surface of real property, are minerals that are subject to local taxation whether or not the property is under development. It further is my opinion that the initial discovery of a mineral generally is the time at which assessment

¹⁴Stephen C. Gara & Craig J. Langstraat, *Property Valuation for Transfer Taxes: Art, Science, or Arbitrary Decision?*, 12 AKRON TAX J. 125, 143 (1996); *see also Keswick Club*, 273 Va. at 137, 639 S.E.2d at 248 (recognizing “the cost approach, income approach, and sales approach”).

¹⁵Gara & Langstraat, *supra* note 14, at 143.

¹⁶*See* 4 POWELL ON REAL PROPERTY § 34A.06 (Michael Allan Wolf, ed., Matthew Bender & Co., Inc., 2009) [hereinafter POWELL]; Gara & Langstraat, *supra* note 14, at 143.

¹⁷*See* Va. Beach v. Hay, 258 Va. 217, 221, 518 S.E.2d 314, 316 (1999) (holding that when legislature grants power to local government, but does not specify method of implementing power, local government’s choice regarding implementation of conferred power will be upheld, provided method chosen is reasonable); *see also* 2005 Op. Va. Att’y Gen. 147, 148 and opinions cited therein (noting that act did not specify method for compliance, but left to discretion of agency; noting also that commissioners, as constitutional officers, are vested with authority and power to administer operations of their offices in manner and to extent they see fit).

¹⁸*Hay*, 258 Va. at 221, 518 S.E.2d at 316.

¹⁹*See* 1 POWELL, *supra* note 16, at § 10B.06.

²⁰*See* VA. CODE ANN. § 58.1-3350 (2009) (providing that any person aggrieved by any assessment may apply for relief to board of assessors or to board of equalization or may apply for relief to appropriate circuit court for correction).

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would occur. Finally, it is my opinion that the income capitalization methodology that you describe would comply with §§ 58.1-3286 and 58.1-3287.

With kindest regards, I am

Very truly yours,

A handwritten signature in black ink, appearing to read "Ken Cuccinelli, II". The signature is written in a cursive style with a large initial "K" and "C".

Kenneth T. Cuccinelli, II
Attorney General