

02-1269, 02-1272, 02-1271
LOCALLY ASSESSED PROPERTY
SIGNED 12-14-2004

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER 1; PETITIONER 2; PETITIONER 3; PETITIONER 4,)	FINDINGS OF FACT, CONCLUSIONS
)	OF LAW, AND FINAL DECISION
)	
Petitioner,)	Appeal No. 02-1269, 02-1272, 02-1271
)	Parcel No.
v.)	
)	Tax Type: Property Tax/Locally Assessed
BOARD OF EQUALIZATION)	
OF SALT LAKE COUNTY,)	Tax Year:
STATE OF UTAH,)	
)	
Respondent.)	Judge: Davis

This Order may contain confidential "commercial information" within the meaning of Utah Code Ann. §59-1-404, and is subject to disclosure restrictions as set out in that section and regulation pursuant to Utah Admin. Rule R861-1A-37.

Presiding:

G. Blaine Davis, Administrative Law Judge

Appearances:

For Petitioner: PETITIONER REP

For Respondent: RESPONDENT REP 1, Deputy Salt Lake County Attorney
RESPONDENT REP 2, Salt Lake County Assessor's Office

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for a Formal Hearing on August 26, 2004. The matter was presented by way of Motions for Summary Judgments by each of the parties. Following the hearing and oral arguments on the Motions for Summary Judgment, the parties were given time in which to file post-hearing memorandums. Such additional documents were received through October 18, 2004.

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Petitioners (except PETITIONER 3 hereinafter referred to as PETITIONER 3) have each entered into a lease agreement to lease from the (X) certain land located within the (X) at the (X). Pursuant to the lease agreements, Petitioners (except PETITIONER 3) were required to build their own buildings in which they presently operate, and to pay to the (X) a lease payment for the use of the land. At the conclusion of the lease agreement, the buildings will belong to the (X). The lease agreements are, in general, for the duration of forty years, with an option for an additional ten-year period.

The buildings occupied by PETITIONER 3 are leased by PETITIONER 3 from PETITIONER 4, a Utah Limited Partnership (hereinafter referred to as "PETITIONER 4"). PETITIONER 4 leases the land from the (X). PETITIONER 4 constructed buildings on the land and both the land and the buildings are then leased to PETITIONER 3 by PETITIONER 4. The other buildings at issue are owned by PETITIONER 1 and PETITIONER 2, and were valued by Respondent as real property using the income approach. That valuation included the value of the land.

The buildings and all of what Petitioners refer to as leasehold improvements were not included on the personal property returns filed with Salt Lake County by any of the Petitioners.

The buildings constructed by Petitioners, and the land on which those buildings sit are the properties at issue in this proceeding.

Petitioners did not present any evidence that the value placed on the property by Respondent exceeded the fair market value of the subject properties.

The Petitioners do not have any right or option to purchase the land underneath their

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existing buildings either during or at the conclusion of the lease.

Respondent presented evidence that the subject property is real property. Petitioners did not present any evidence that the subject property is personal property.

PETITIONER 3 is wholly-owned by the (X), and is a for-profit component unit of the University for financial reporting purposes. In 2003, PETITIONER 3 paid approximately \$\$\$\$\$ in dividends to the (X). PETITIONER 3 is a for-profit corporation that provides (PORTION REMOVED)

Because PETITIONER 3 is a wholly-owned component of the (X), on April 6, 2001, the Internal Revenue Services issued a Private Letter Ruling that the income of PETITIONER 3 is excludible from gross income for federal income tax purposes under Section 115(1) of the Internal Revenue Code. The ruling was only prospective. In addition on May 14, 2003, the Taxpayer Services Division of the Utah State Tax Commission issued a letter determining that PETITIONER 3 is exempt from Utah sales tax under Utah Code Ann. §59-12-104(2).

APPLICABLE LAW

The Constitution of Utah, Article 12, Sec. 2 provides in relevant part:

"(1) so that each person and corporation pays a tax in proportion to the fair market value of his, her, or its tangible property, all tangible property in the state that is not exempt under the laws of the United States or under this constitution shall be:

- (a) assessed at a uniform and equal rate in proportion to its fair market value, to be ascertained as provided by law:
- (b) taxed at a uniform and equal rate."

Utah Code Ann. §59-2-103 provides, in relevant part, as follows:

(1) All tangible taxable property shall be assessed and taxed at a uniform and

equal rate on the basis of its fair market value, as valued on January 1, unless otherwise provided by law.

Utah Code Ann. §59-4-101(1)(a) imposes a privilege tax and provides as follows:

(1)(a) Except as provided in Subsections (1)(b) and (c), a tax is imposed on the possession or other beneficial use enjoyed by any person of any real or personal property which for any reason is exempt from taxation, if that property is used in connection with a business conducted for profit.

Utah Code Ann. §59-2-102 defines improvements, personal property, real estate or real property as:

(16) "Improvements" includes all buildings, structures, fixtures, fences, and improvements erected upon or affixed to the land, whether the title has been acquired to the land or not.

....

(24) "Personal property" includes:

- (a) every class of property as defined in Subsection (25) which is the subject of ownership and not included within the meaning of the terms "real estate" and "improvements";
- (b) gas and water mains and pipes laid in roads, streets, or alleys;
- (c) bridges and ferries; and
- (d) livestock which, for the purposes of the exemption provided under Section 59-2-1112, means all domestic animals, honeybees, poultry, fur-bearing animals, and fish.

(25)(a) "Property" means property that is subject to assessment and taxation according to its value.

(b) "Property" does not include intangible property as defined in this section.

....

(27) "Real estate" or "real property" includes:

- (a) the possession of, claim to, ownership of, or right to the possession of land;
- (b) all mines, minerals, and quarries in and under the land, all timber belonging to individuals or corporations growing or being on the lands of this state or the United States, and all rights and privileges appertaining to these; and
- (c) improvements.

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Utah Code Ann. §59-2-1101(2) sets forth the exemptions from property taxes in the

State of Utah as follows:

- (2) The following property is exempt from taxation:
 - (a) property exempt under the laws of the United States;
 - (b) property of the state, school districts, and public libraries;
 - (c) property of counties, cities, towns, special districts, and all other political subdivisions of the state, except as provided in Title 11, Chapter 13, Interlocal Cooperation Act;
 - (d) property owned by a nonprofit entity which is used exclusively for religious, charitable, or educational purposes;
 - (e) places of burial not held or used for private or corporate benefit;
 - (f) farm equipment and machinery;
 - (g) intangible property; and
 - (h) the ownership interest of an out-of-state public agency, as defined in Section 11-13-103, in property providing additional project capacity, as defined in Section 11-13-103, on which a fee in lieu of ad valorem property tax is payable under Section 11-13-302.

Utah Administrative Code Rule R884-24P-32 provides for leasehold improvements as follows:

R884-24P-32. Leasehold Improvements Pursuant to Utah Code Ann. §59-2-303.

A. The value of leasehold improvements shall be included in the value of the underlying real property and assessed to the owner of the underlying real property.

B. The combined valuation of leasehold improvements and underlying real property required in A. shall satisfy the requirements of Section 59-2-1101.

C. The provisions of this rule shall not apply if the underlying real property is owned by an entity exempt from tax under Section 59-2-1101.

D. The provisions of this rule shall be implemented and become binding on taxpayers beginning January 1, 2000.

Utah Administrative Code Rule R884-24P-33 sets forth the method for valuing personal property as follows:

- B. Each year the Property Tax Division shall update and publish percent good schedules for use in computing personal property valuation.
1. Proposed schedules shall be transmitted to county assessors and interested parties for comment before adoption.
 2. A public comment period will be scheduled each year and a public hearing will be scheduled if requested by ten or more interested parties or at the discretion of the Commission.
 3. County assessors may deviate from the schedules when warranted by specific conditions affecting an item of personal property. When a deviation will affect an entire class or type of personal property, a written report, substantiating the changes with verifiable data, must be presented to the Commission. Alternative schedules may not be used without prior written approval of the Commission.
 4. A party may request a deviation from the value established by the schedules for a specific item of property if the use of the schedule does not result in the fair market value for the property at the retail level of trade on the lien date, including any relevant installation and assemblage value.

With respect to Leasehold Improvements, Utah Administrative Code Rule R884-24P-33.22 provides:

22. Class 24 – Leasehold Improvements.

- a) This class includes leasehold improvements to real property installed by a tenant. The Class 24 schedule is to be used only with leasehold improvements that are assessed to the lessee of the real property pursuant to Tax Commission rule. Leasehold improvements include:
- (1) walls and partitions;
 - (2) plumbing and roughed-in fixtures;
 - (3) floor coverings other than carpet;
 - (4) store fronts;
 - (5) decoration;
 - (6) wiring;
 - (7) suspended or acoustical ceilings;
 - (8) heating and cooling systems; and
 - (9) iron or millwork trim.

(b) Taxable value is calculated by applying the percent good factor against the cost of acquisition, including installation.

1. The Tax Commission is required to oversee the just administration of property taxes to ensure that property is valued for tax purposes according to fair market value. Utah Code Ann. §59-1-210(7).

2. Any person dissatisfied with the decision of the county board of equalization concerning the assessment and equalization of any property, or the determination of any exemption in which the person has an interest, may appeal that decision to the Tax Commission. In reviewing the county board's decision, the Commission may admit additional evidence, issue orders that it considers to be just and proper, and make any correction or change in the assessment or order of the county board of equalization. Utah Code Ann. §59-2-1006(3)(c).

3. Petitioner has the burden to establish that the market value of the subject property is other than the value determined by Respondent.

4. To prevail, the Petitioner must (1) demonstrate that the County's original assessment contained error, and (2) provide the Commission with a sound evidentiary basis for reducing the original valuation to the amount proposed by Petitioner. *Nelson V. Bd. Of Equalization of Salt Lake County*, 943 P.2d 1354 (Utah 1997), *Utah Power & Light Co. v. Utah State Tax Commission*, 530 P.2d. 332 (Utah 1979).

DISCUSSION

The overriding principle in property taxation is that all tangible taxable property in this state should be taxed at its fair market value, and that value should be determined uniformly with

other property of a similar or like kind.

Petitioners have argued two different theories in this case. The first theory is a unique theory to attempt to have the real property of the Petitioners taxed based upon a percent good table as established by the Commission for personal property. However, those percent good tables are established as a surrogate for fair market value of personal property. If the Commission determines that the fair market value of personal property is either greater than or less than the amounts set forth in the tables, then the fair market value prevails because that is the constitutional and statutory standard to be applied to all property.

In this matter, Petitioners did not present any evidence regarding the fair market value of the property, nor did they present any evidence that the values determined under the personal property schedules would be equal to or within a reasonable range of the fair market value of the property at issue. In fact, the Petitioners have a lease for forty years, with a ten year option, indicating the property likely has a life of forty to fifty years. If the theory of Petitioners was accepted, it would reduce the value of the property to 30% of its cost after a period of ten years. The personal property tables were designed for properties with a much shorter life than forty or fifty years. Leasehold improvements for which table 22 was intended, such as those that are installed in stores and offices, are normally changed, refurbished, or replaced much sooner than forty or fifty years.

Although Petitioners have argued that their properties should be taxed as personal property pursuant to the tables set forth in Rule R884-24P-33, the properties are not personal property, but they are real property. Utah Code Ann. §59-2-102(27), provides:

- (27) "Real estate or property" includes:
- (a) the possession of, claim to, ownership of, or right to the possession of land;
 - (b) all mines, minerals, and quarries in and under the land, all timber belonging to individuals or corporations growing or being on the lands of this state of the United States, and all rights and privileges appertaining to these; and
 - (c) improvements. (emphasis added.)

Based upon the statute, the property at issue in this proceeding is real estate. This property is not personal property. Personal property is "every class of property . . . which is the subject of ownership and not "real estate" and "improvements." "The subject property is "improvements" which "includes all buildings, structures, fixtures, fences, and improvements erected upon or affixed to the land. . . ." It is also "the possession of . . . or right to the possession of land."

Although Utah Administrative Code Rule R884-24P-33 does provide that walls and partitions, plumbing and roughed-in fixtures and other items may be leasehold improvements, the rule clarifies that is when they are "assessed to the lessee of the real property." Thus, if a lessee of space in a shopping mall or an office building adds walls or plumbing to the fixed structure, those items may be assessed and taxed to the tenant as leasehold improvements. However, in these appeals, the walls, plumbing, etc., that are sought to be taxed as leasehold improvements are all part of the primary construction of the buildings. Therefore, pursuant to the percent good tables of Rule 33, those walls, plumbing, etc., are real property.

Even if the Commission were to accept the Petitioner's distorted theory in this case, the Commission would still not rule in favor of Petitioner. There has been a failure to meet the burden of proof in this proceeding. There is no evidence that the value placed on the property by

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Respondent is erroneous, no evidentiary basis for reducing the original value to the amount proposed by Petitioner, no specific value was proposed by Petitioner, no evidence that the method proposed by Petitioner would comply with generally accepted appraisal methodology, and no evidence that the method proposed by Petitioner would result in a value that was within a reasonable range of the fair market value of the property.

Accordingly, the Commission determines that the first theory argued by Petitioners is not applicable. The rule was not intended to determine that full buildings are leasehold improvements just because the land is being leased and the building has been constructed thereon. These buildings are real property and should be taxed accordingly as real property owned by Petitioners pursuant to the privilege tax provisions of Utah Code Ann. §59-4-101, et. seq. The methods proposed by Petitioners would not tax the subject property at its fair market value, and would therefore violate the overriding principles and statutes governing property taxation, and would further violate the Utah Constitution. Petitioner's proposed interpretation of the statutes and rules is a distorted and illegal interpretation of those statutes and rules.

Petitioner's second theory is that the land and buildings leased by PETITIONER 3 from PETITIONER 4, and occupied by PETITIONER 3, are exempt from taxation pursuant to Article XIII, Section 3 of the Utah Constitution, and Utah Code Ann. §59-2-1101 as property of the state or a political subdivision of the state.

In this matter, the land is owned by a political subdivision of the state (the (X)) and leased to a private entity (PETITIONER 4). PETITIONER 4 has constructed buildings upon the land and then has subleased the land and leased the buildings to another political subdivision of the state

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(PETITIONER 3).

Respondent determined that PETITIONER 4 was the owner of the buildings which are real property, and PETITIONER 4 also had the beneficial use of the land, which was exempt from taxation, and that use of the land was in connection with a business conducted for profit. Therefore, Respondent imposed regular property taxes, pursuant to Utah Code Ann. §59-4-101, et. Seq., on the land. Those taxes were assessed to PETITIONER 4.

The representative of Petitioners has argued that it is necessary to combine the property rights of the (X) with the property rights of PETITIONER 3 to determine that the majority of the incidents of ownership are with the state and its political subdivisions. It is accordingly argued that as property of the state or its political subdivisions, the land and the buildings are exempt from taxes.

In making the above arguments, the representative of Petitioners has ignored the role of PETITIONER 4 and has far overestimated the role of PETITIONER 3 in this situation. The tax is imposed by Respondent on PETITIONER 4. PETITIONER 3 is just a tenant of PETITIONER 4. Although PETITIONER 3 may be required to reimburse PETITIONER 4 for any property taxes, the taxes are not imposed on PETITIONER 3 by Respondent. Whether PETITIONER 3 is a governmental agency or a for-profit business is not material to a determination of whether the properties are exempt from taxes. The critical entity for purposes of determining the possible exemption from taxes is PETITIONER 4. PETITIONER 4 is a business which attempts to make a profit, and the "property is used in connection with a business conducted for profit." Therefore, the land is subject to the privilege tax imposed by Utah Code Ann. §59-4-101, et. seq.

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PETITIONER 4, is also the owner of the buildings notwithstanding that ownership of the buildings will transfer to the (X) upon the termination of the lease. PETITIONER 4 built the buildings, depreciates them on its income tax returns, and attempts to make a profit by leasing the buildings to tenants. Therefore, PETITIONER 4 is the owner of buildings that are subject to property tax.

DECISION AND ORDER

Based upon the foregoing, the Commission determines that the property at issue in this proceeding should not be taxed pursuant to the personal property schedules set forth in Utah Administrative Code, Rule R884-24P-33(22). The land should be taxed to PETITIONER 4 based upon its fair market value by the application of the privilege tax as set forth in U.C.A. 59-4-101, et. seq. The buildings should be taxes to PETITIONER 4 as real property pursuant to the provisions of Utah Code Ann. §59-2-103. Petitioner's Motion for Summary Judgment is hereby denied, and Respondent's Motion for Summary Judgment is hereby granted. It is so ordered.

DATED this _____ day of _____, 2004.

G. Blaine Davis
Administrative Law Judge

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BY ORDER OF THE UTAH STATE TAX COMMISSION:

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this _____ day of _____, 2004.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Palmer DePaulis
Commissioner

Marc B. Johnson
Commissioner

Notice of Appeal Rights: You have twenty (20) days after the date of this order to file a Request for Reconsideration with the Tax Commission Appeals Unit pursuant to Utah Code Ann. §63-46b-13. A Request for Reconsideration must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Reconsideration with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code Ann. §§59-1-601 and 63-46b-13 et. seq.

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