03-1721
Locally Assessed Property Tax
Signed 09/02/2005

BEFORE THE UTAH STATE TAX COMMISSION

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| | ) | **FINDINGS OF FACT, CONCLUSIONS** |
| PETITIONER, | ) | **OF LAW, AND FINAL DECISION** |
| | ) | |
| Petitioner,) | ) | Appeal No. 03-1721 |
| | ) | Parcel No. ##### |
| v. | ) | |
| | ) | Tax Type: Property Tax/Personal Property |
| BOARD OF EQUALIZATION | ) | |
| OF SALT LAKE COUNTY, | ) | Tax Years: 1998, 1999 |
| STATE OF UTAH, | ) | |
| | ) | Judge: Davis |
| Respondent. | ) | |

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**This Order may contain confidential "commercial information" within the meaning of Utah Code Sec. 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. The rule prohibits the parties from disclosing commercial information obtained from the opposing party to nonparties, outside of the hearing process. However, pursuant to Utah Admin. Rule R861-1A-37, the Tax Commission may publish this decision, in its entirety, unless the property taxpayer responds in writing to the Commission, within 30 days of this notice, specifying the commercial information that the taxpayer wants protected. The taxpayer must mail the response to the address listed near the end of this decision.**

**Presiding:**

G. Blaine Davis, Administrative Law Judge
Marc B. Johnson, Commissioner

**Appearances:**

For Petitioner: PETITIONER REPRESENTATIVE 1, Owner
PETITIONER REPRESENTATIVE 2, Owner

For Respondent: RESPONDENT REPRESENTATIVE 1, Deputy, Salt Lake County Attorney
RESPONDENT REPRESENTATIVE 2, from the Salt Lake County Assessor's Office
RESPONDENT REPRESENTATIVE 3, from the Salt Lake County Assessor's Office
RESPONDENT REPRESENTATIVE 4, from the Salt Lake County Assessor's Office

## STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for a Formal Hearing on January 12, 2005. Based upon the evidence and testimony presented at the hearing, the Tax Commission hereby makes its:

## FINDINGS OF FACT

1. The tax in question is property tax.

2. The years in question are 1998 and 1999, with lien dates of January 1 of each of those years.

3. The issue is the property tax on leasehold improvements imposed by Salt Lake County upon Petitioner based upon an audit of the books and records of Petitioner.

4. Based upon the audit of the books and records of Petitioner, the Salt Lake County Assessor imposed property tax on the leasehold improvements which Petitioner made to the building facilities which it leases for the operation of its business. The position of Petitioner is that those leasehold improvements are part of the building and real property which should have been assessed to the owner of the building, and not to Petitioner as the Lessee of space within that building.

5. On or about April 26, 1997, Petitioner entered into a lease for space in a building commonly known as ( X ) located at ADDRESS, CITY, Salt Lake County, State of Utah.

6. As part of its lease on the property, Petitioner was to provide its own leasehold improvements to build a restaurant facility in the space which it had leased. Petitioner did build those leasehold improvements for a total amount of approximately $$$$$, and the landlord provided

financing of approximately $$$$$ for additional improvements.

7. During the years at issue in this proceeding, those leasehold improvements were utilized by Petitioner in the operation of its restaurant business.

8. The leasehold improvements included such items as the demolition of some of the existing improvements, and construction of new plumbing, kitchen, restrooms, sheetrock, heating, ventilation and air conditioning, framing for new partitions, a new entry way, and decoration of the facilities.

9. The lease between Petitioner and the owner of the building, dated April 26, 1997, contained one paragraph relating to tenant improvements. That paragraph stated as follows:

> "3. Tenant Improvements. Promptly after the date hereof, Tenant, at Tenant's sole cost and expense, shall complete construction and installation on the Leased Premises of all such fixtures and improvements as may be reasonable necessary or appropriate for the operation of Tenant's business. However, Tenant shall not make any changes which are not generally consistent with plans and specifications to be approved by Landlord before commencement of the work, and Tenant shall not make structural or other permanent changes to the Leased Premises without the express written consent of Landlord, which shall not be unreasonably withheld. Upon termination of this Lease, Tenant shall remove the awnings on the exterior of the Leased Premises and otherwise leave the Leased Premises in good and clean condition, normal wear and tear excepted. Permanent improvements to the Leased Premises which the Tenant is not required to remove shall become the property of Landlord, unless Landlord agrees to the contrary in writing. Landlord and Tenant specifically agree, without limitation, that the new kitchen exhaust system to be installed by Tenant shall be a permanent improvement to the Leased Premises which shall become the property of Landlord upon termination of this Lease. However, Tenant's trade fixtures, equipment and furnishings shall remain the property of Tenant and may be removed by Tenant upon the termination of this Lease, provided Tenant repairs any damage to the Leased Premises caused by the removal of such trade fixtures, equipment and furnishings. Tenant shall pay in a timely

> manner all debts incurred in the construction of the improvements, shall not allow any lien or lien rights to accrue against the Leased Premises, and shall indemnify Landlord for any expense which may arise out of the payment or removal of any lien." (emphasis added)

10. It is the position of Petitioner that the taxes should not be assessed to them because they do not have control over the property after it is installed because it has become the property of the landlord. Petitioner maintains that as a tenant, it controls only the space defined by the leasehold in which it conducts its business.

## APPLICABLE LAW

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 that the value determined by Respondent. Petitioner also has the burden to establish that the leasehold improvements are not under its control.

4. To prevail, the Petitioner normally 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).

For the years 1998 and 1999, Utah Administrative Code Rule R884-24P-32 provided as follows:

> A. Leasehold improvements under the control of the lessee shall be taxed as personal property of the lessee.
> B. If not taxed as personal property of the lessee, the value of leasehold improvements shall be included in the value of the real property.

Beginning January 1, 2000, Utah Administrative Code Rule R884-24P-32 was amended to read as follows:

> 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 59-2-103(1).
> 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.

## DISCUSSION

In this matter, Petitioner maintains that it should not be assessed for taxes on the leasehold improvements which it constructed and which it uses in conformance with its lease on the property within the building. It maintains that it should not be assessed for those taxes because it does not have control of those improvements because they have become property of the Landlord.

However, the lease which they signed specifically contradicts their position. Paragraph 3 of that Lease, quoted above, contains language which says, " Upon termination of this Lease, Tenant shall remove the awnings on the exterior of the Leased Premises and otherwise leave the Leased Premises in good and clean condition, normal wear and tear excepted. Permanent improvements to the Leased Premises which the tenant is not required to remove shall become the property of Landlord, unless Landlord agrees to the contrary in writing. Landlord and Tenant specifically agree, without limitation, that the new kitchen exhaust system to be installed by Tenant shall be a permanent improvement to the Leased Premises which shall become the property of Landlord upon termination of this Lease."

Based upon the wording of the Lease, the Commission concludes that Petitioner is in full and complete control of all of the leasehold improvements until the termination of the Lease. Upon termination of the Lease, Petitioner is required to remove the awnings, but the other property would become the property of Landlord "upon termination of this Lease." Even if the Lease did not contain that language, the Commission deems that the control spoken of by Rule R884-24P-32, which was in effect as of the time or times at issue in this matter, is the right to use the improvements, and not necessarily the legal ownership to such improvements. Therefore, the Commission concludes that with or without the provisions in the Lease, Petitioner, as the user of those leasehold improvements, is the party in control of those improvements.

Petitioner also refers to a case from the Supreme Court of Utah, Crossroads Plaza Association v. Pratt, 912 P.2d 961, as authority for the proposition that the Landlord is the

responsible party to pay taxes on leasehold improvements. However, while that case did sustain the imposition of property taxes on leasehold improvements against a landlord, it only did so because the tenant who had installed the leasehold improvements had filed bankruptcy, and therefore, the taxes could not be collected against the tenant. Accordingly, the Supreme Court sustained a lien upon the real property of the landlord for the taxes on the leasehold improvements because of the provisions of a Utah Statute, Utah Code Ann. §59-2-1325. However, the Court did not say that the taxes were not a valid assessment against the tenant who had constructed the leasehold improvements.

It is noted, that effective January 1, 2000, the Utah State Tax Commission amended Rule R884-24P-32 so that after the applicable date of that change in the rule, the value of leasehold improvements were to be included in the value of the underlying real property and assessed to the owner of the underlying property. That new rule was applied by Respondent in its audit of the books and records of Petitioner, so the issue involved in this proceeding does not exist for the year 2000 and subsequent years.

## DECISION AND ORDER

Based upon the foregoing, the Tax Commission finds that the taxes on leasehold improvements installed and constructed by Petitioner was a correct and valid assessment. Those taxes would not have been appropriately assessed to the Landlord based upon the rule of the Commission in force for the dates at issue in this matter. The assessment by Respondent is therefore sustained. The Petition for Redetermination filed by Petitioner is hereby denied. It is so ordered.

DATED this _____ day of _____, 2005.

_____
G. Blaine Davis
Administrative Law Judge

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 _____, 2005.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Palmer DePaulis
Commissioner

Marc B. Johnson
Commissioner

**Notice of Appeal Rights and Payment Requirement:** 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. Failure to pay the balance resulting from this order within thirty (30) days from the date of this order may result in a late payment penalty.

GBD/ssw/03-1721