



# State of Alabama Department of Revenue

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## ALABAMA DEPARTMENT OF REVENUE REVENUE RULING 94-004

**THIS DOCUMENT MAY NOT BE USED OR CITED AS PRECEDENT. CODE OF ALABAMA 1975, §40-2A-5(a)**

TO:

FROM: Alabama Department of Revenue

DATE: July 11, 1994

SUBJECT: Additions of machinery and equipment made by Company "B" pursuant to a 1979 Indenture and Lease Agreement with the Company "A".

### FACTS

Company "A" and Company "B" are the Lessor and Lessee, respectively, of a lease agreement executed November 1, 1979, for the financing and construction of what is known as the Project. The lease term is for a period of 20 years expiring November 1, 1999.

During the 1992-1993 ad valorem tax year, Company "B" made additions to the Project of machinery and equipment in the amount of \$23,576,106.71. These additions were purchased after May 21, 1992, which was the effective date of the Tax Incentive Reform Act of 1992.

Section 6.1 of the Lease permits Company "B", at its own expense, to make any additions, alterations, improvements or modifications to the Project that it may deem desirable for its business purposes. Section 6.3 states that any such additions, alterations, improvements or modifications become the sole property of the Company "A" and a part of the lease. Section 6.4 acknowledges that under current law (1979) the Project is exempt from ad valorem taxes due to Company "A" ownership.

LAW AND ANALYSIS

Section 40-9B-7(a)(1), Code of Alabama 1975, states:

Notwithstanding any other provision of law, if a public authority or county or municipal government has title to or a possessory right

in private use property, then:

- (1) The property shall be subject to ad valorem taxes as if the private user held title to the property.

This statute taxes property that prior to its passage would have been tax-exempt. However, §40-9B-7(c), commonly referred to as the "grandfather clause," allows property to remain exempt ". . . [I]f a private user was entitled to use the property pursuant to a lease or other agreement entered into before May 21, 1992 . . . ."

The lease agreement between Company "B" and the Company "A" was in effect prior to May 21, 1992. Ad valorem tax Reg. 810-4-3-02(2) states:

The taxability provisions [§40-9B-7(a)(1)] will not apply if a private user was entitled to use the property pursuant to a lease or agreement entered before the effective date of Act 92-599 [Tax Incentive Reform Act of 1992] or would be entitled to use of property at some future time pursuant to inducement entered into before the effective date of Act 92-599.

This regulation does not speak directly to the purchase of new equipment or machinery. However, when read in conjunction with ad valorem tax Reg. 810-4-3-.03(4)(B)(2), it becomes apparent that the additions to the Company "B" Project are tax-exempt as a result of the 1979 lease agreement. Regulation 810-4-3-.03(4)(B)(2) states:

Replacement equipment acquired subject to a lease in effect prior to Act 92-599 becoming law shall be taxable only according to the provisions of the lease.

While some of the machinery and equipment purchased by Company "B" in 1992 and 1993 may not have been replacement equipment, to assert that new nonreplacement equipment is subject to the Tax Incentive Reform Act would be too narrow of a construction. The fact that new equipment is not replacing old equipment does not make the Tax Incentive Reform Act applicable if a pre-Act lease was in place at the time of purchase.

HOLDING

The purchase of manufacturing, machinery and equipment for the Company "B" project in 1992 and 1993 is either taxable or nontaxable as determined by the law in effect prior to the passage of Act No. 92-599 ( Tax Incentive Act of 1992).

  
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Acting Commissioner of Revenue

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