

ALABAMA DEPARTMENT OF REVENUE
REVENUE RULING 98-016

This document may not be used or cited as precedent. Code of Alabama 1975, §40-2A-5(a).

TO:

FROM: Commissioner of Revenue
Alabama Department of Revenue

DATE: January 4, 1999

RE: Applicability of Alabama ad valorem tax to a transaction whereby a corporation plans to replace obsolete equipment pursuant to a lease agreement between the corporation and an Alabama Public Corporation.

FACTS

The facts as stated by Requestor are as follows:

The Authority (the "Authority") is an Alabama Public Corporation. The Authority is empowered to issue its revenue bonds to secure and develop manufacturing and industrial plants and to lease or let buildings, structures and other facilities near the property operated by the Authority. A Lease Agreement (the "Lease") was entered into by and between the Authority, as Lessor, and Corporation "A", a State "X" corporation, as Lessee, in which the Authority leased to Corporation "A" certain lands, buildings, improvements and machinery. This Lease Agreement was dated November 10, 1976. On December 30, 1980, Corporation "A" assigned its rights under the Lease to Corporation "B", a State "Y" corporation. The assignment was effective on December 31, 1980.

Section 4.1 of the Lease, entitled "Agreement to Construct, Equip and Install the Building on the Leased Land" provides that the "Leased Equipment shall be the property of the Authority and subject to the terms of this Lease."

"Leased Equipment" is defined under the Lease as:

[T]hose items of machinery, equipment and related property required herein to be acquired and installed in the Building or on the Leased Land with proceeds from the sale of the Bond or the proceeds of any payment by the Lessee pursuant to Section 4.6 hereof and any item of machinery, equipment and related property acquired and installed in the Building or on the Leased Land in substitution therefor and renewals and replacements thereof....

Section 6.2 of the Lease, entitled "Removal of Leased Equipment", states in pertinent part:

In any instance where the Lessee in its sole discretion determines that any such items of Leased Equipment have become inadequate, obsolete, worn out, unsuitable, undesirable, inappropriate or unnecessary for their purposes at such time, the Lessee may remove such items from the Building and the Leased Land and (on behalf of the Authority) sell, trade-in, exchange or otherwise dispose of them (as a whole or in part) without any responsibility or accountability to the Authority or the Trustee therefor, provided that the Lessee shall:

(a) substitute...and install anywhere in the Building or on the Leased Land other machinery, equipment or related property...all of which substituted machinery, equipment or related property shall be free of all liens and encumbrances (other than Permitted Encumbrances) but shall become a part of the Leased Equipment....

These lease provisions establish that the Authority owns the Project, specified machinery and equipment and, whenever purchased, all replacements or substitutions to that machinery and equipment.

Corporation "B" desires to purchase machinery and equipment for the Project to be acquired subject to the lease which was in effect before May 21, 1992, the effective date of the Tax Incentive Reform Act of 1992 codified at ALABAMA CODE § 40-9B-1 *et seq.* (1975) (the "Reform Act"). Prior to the adoption of the Reform Act, Authority property was automatically exempt from ad valorem taxes. After passage of the Reform Act, the same property became subject to the ad valorem tax. Nevertheless, the Reform Act includes a "Grandfather Clause" that allows property to remain exempt if acquired subject to a lease in effect before the Reform Act became law.

ANALYSIS

The Tax Incentive Reform Act of 1992 (TIRA), authorizes the abatement of certain ad valorem taxes incurred in establishing or expanding industrial development within the state. TIRA also limits the abatements available through various public agencies and authorities. The Act is codified at §40-9B-1, et seq., Code of Alabama 1975. Section 40-9B-3, Code of Alabama 1975, defines several terms relevant to this ruling. “Inducement” and “private use property” are defined as follows under the Act:

INDUCEMENT. Refers to an agreement, or an “inducement agreement,” entered into between a private user and a public authority or county or municipal government and/or a resolution or other official action, an “inducement resolution,” “inducement letter,” or “official action” adopted by a public authority or county or municipal government, in each case expressing, among other things, the present intent of such public authority or county or municipal government to issue bonds in connection with the private use property therein described.

PRIVATE USE PROPERTY. Any real and/or personal property which is or will be treated as owned by a private user for federal income tax purposes even though title may be held by a public authority or municipal or county government.

Sections 40-9B-7(a)(1) and 40-9B-7(c), Code of Alabama 1975, provide as follows:

(a) 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.

(c) The rule of subsection (a)(1) shall not apply to ad valorem taxes if a private user was entitled to use the property pursuant to a lease or other agreement entered into before May 21, 1992, or would be entitled to use the property at some future time pursuant to inducement entered into or adopted before May 21, 1992, provided, however, that this subdivision shall apply only to the property and the amount of capital expenditures set out in such inducement, subject to de minimis deviations.

Ruling

Since Corporation "B" was entitled to purchase new equipment subject to the lease entered into with the Authority pursuant to the assignment of Corporation "B" by Corporation "A" on December 31, 1980, any future removal and substitution of obsolete, worn-out, etc., of Leased Equipment by Corporation "B" will continue to qualify, pursuant to the Grandfather Provision of TIRA, §40-9B-7(c), for exemption from taxation under the Industrial Development Act (IDB Act), §11-54-96, Code of Alabama 1975. This ruling is only applicable for so long as the lease and assignment shall remain valid.

ALABAMA DEPARTMENT OF REVENUE

By: _____
H.E. "Gene" Monroe, Jr.
Commissioner of Revenue

HEM:WKM