



State of Alabama Department of Revenue

Montgomery, Alabama 36132

GEORGE E. MINGLEDORFF III
Commissioner (Acting)

GEORGE E. MINGLEDORFF III
Assistant Commissioner

LEWIS A. EASTERLY
Secretary

ALABAMA DEPARTMENT OF REVENUE REVENUE RULING 94-003

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

TO: Company A

FROM: The Alabama Department of Revenue

DATE: July 1, 1994

RE: Additions of machinery and equipment made pursuant to a 1988 indenture and lease agreement with the Huntsville Industrial Development Board.

FACTS

Company A and the Industrial Development Board of the City of Huntsville (IDB) executed a lease agreement effective September 1, 1988, for the further development of Company A's Huntsville operation. This agreement is to expire September 30, 2003. It was supplemented as of April 1, 1990, however, this supplement did not change the original expiration date.

The project is the property of the IDB, which leases the project to Company A. The project is exempt from ad valorem taxes due to IDB ownership.

Section 6.1 of the lease agreement permits Company A to make additions, modifications, replacements and/or improvements with same becoming part of the project and subject to the terms of the lease. Equipment and machinery purchased for any addition, renewal, modification and/or improvement becomes leased equipment pursuant to §6.7(a) of the lease. Section 8.4 requires that purchases of equipment, machinery or fixtures be made by the IDB.

Company A made additions of machinery and equipment to the Huntsville project in 1992 and 1993 totalling \$11,647,340.00. These additions were made pursuant to the terms of the 1988 lease referred to above. These additions were made after May 21, 1992, the effective date of the Tax Incentive Reform Act of 1992, codified at §40-9B-1, et seq., Code of Alabama 1975.

ISSUE

Whether the 1992-1993 additions to the Company A - Huntsville project are subject to the Tax Incentive Reform Act.

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 A and the IDB was in effect prior to May 21, 1992 and remains in effect to date. Ad Valorem Tax Regulation 810-4-3-02(2) states:

The taxability provision [40-9B-7(a)(1)] will not apply if a private user was entitled to use the property pursuant to a lease or other agreement entered into before the effective date of Act 92-599 [Tax Incentive Reform Act] or would be entitled to use the 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 Regulation 810-4-3-.03(4)(B)(2), it becomes apparent that the additions to the Company A - Huntsville project are tax exempt as a result of the 1988 lease agreement. Regulation 810-4-3-.03(4)B2 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 A in 1992 and 1993 may not have been replacement equipment, to

assert that new non-replacement equipment is subject to the Tax Incentive Reform Act would be too narrow of a construction of the Act. 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 A - Huntsville 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 (The Tax Incentive Reform Act of 1992).



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