

OPINION
65-381

November 29, 1965 (OPINION)

Mr. Lloyd Omdahl

Tax Commissioner

RE: Taxation - Municipal Industrial Development - Exemption

This is in reply to your letter of November 5, 1965, requesting an opinion of this office in regard to the application of section 40-57-17 of the 1965 Supplement to the North Dakota Century Code. Said statute provides as follows:

40-57-17. Exemptions from taxation. The leasehold granted by a municipality under this chapter is hereby classified as personal property and such leasehold and all other personal property used by the lessee in connection with the project and located on the premises of the leasehold shall be exempt from personal property taxation for a period of five years from the granting of such leasehold and execution of any instrument evidencing said grant. Further, that any corporate lessee under such a leasehold referred to shall be exempt from the payment of corporate income taxes on any corporate income attributable to the business carried on by the lessee on such leasehold premises for a period of five years from the year in which the corporation lessee commenced business operations on the leased premises, provided, however, that this section shall not have the effect of exempting such corporation lessee from filing an annual income tax return."

Your first question is stated as follows:

1. If a project, such as a manufacturing or assembly plant, has already been constructed with private funds and if an expansion of that project is financed under the Municipal Industrial Development Act, chapter 40-57, N.D.C.C., do the exemptions provided by Chapter 295, S.L. 1965, extend to any part of the property acquired or built with private funds or to the income attributable to that part of the plant built with private funds?"

Under the terms of the Municipal Industrial Development Act, as a whole, we see not basis for predicating the tax exemption here concerned on the method of construction of the project in question. The Act specifically authorizes the acquisition of lands, buildings, improvements, etc. (subsection 1 of section 40-57-03 of the 1965 Supplement to the North Dakota Century Code). Thus the fact that a building was originally constructed by private funds would have no bearing on whether it could be acquired by a municipality under the Act, or could become a "project" within the meaning of the terms of the Act. The tax exemption by its terms would appear to be applicable to "* * * * * The leasehold granted by a municipality under

this chapter" and to "* * * * corporate income attributable to the business carried on by the lessee on such leasehold premises."

A leasehold necessarily implies that the lessor owns the premises and/or has the right to possession of same and that the lessee is permitted to use the lessor's premises for a given consideration. Any agreement whereby a property owner purported to lease premises owned by itself from a municipality pursuant to the terms of the Act would perhaps create an interesting subterfuge, but would hardly create a "leasehold" nor make the property owner a "lessee" within the meaning of the terms of the tax exemption statute in question. Such part of the project as was owned by the municipality and was "leased" to the "lessee", i.e., the "leasehold" of the "lessee" would qualify for the tax exemption. Such part of the project as was held by a private person or corporation by reason of the ownership of same by that person or corporation would not be a "leasehold" within the meaning of the Act and would not qualify for the tax exemption.

Your second question is stated as follows:

2. Referring to question No. 1 and assuming for the purposes of this question that the exemptions do not extend to either the property of income attributable to the part of the plant built with private funds, should the income attributable to that part of the plant financed under the Municipal Industrial Development Act be allocated in all cases according to a specific formula, or should this allocation be made by the tax commissioner, or be made by the taxpayer subject to the approval of the tax commissioner in a manner that depends upon the facts and circumstances of each case with a view to apportioning the taxable and exempt parts of the income in a fair and equitable manner?"

In reply to this question as stated and with reference to your question no. 1, there is no reason why the Act as a whole cannot apply to plants built with private funds which are later acquired by a municipality under this Act and there is therefore no reason why the tax exemption should not be applied to plants built with private funds. However, the tax exemption should be applicable only to the "leasehold" and income realized by the "lessee." On such basis, we assume that the "leasehold" would not differ greatly from other leaseholds and that the lessee's income would not differ greatly from that of other taxpayers. On such basis, where the "lessee" could claim that the "leasehold" was such a "leasehold" as exempted within the meaning of the Act and to the extent that such "leasehold" comprised a part of the whole premises assessed for tax, such lessee could claim the exemption in the same manner as other exemptions are claimed. Likewise, where and to the extent that the "corporation lessee" could show that corporate income was attributable to the business carried on by the "lessee" on such "leasehold premises", such exemption could be claimed.

Your third question is stated as follows:

3. Referring again to the facts in question no. 1, if the two exemptions provided by this amendment extend to that part

of the project built with private funds, would the five year exemption period provided in the amendment extend to a full five year period beginning from the effective date (July 1, 1965) of the amendment, or would it be reduced by the period of time that this part of the project was in existence before the effective date of the amendment?"

Looking again to the statute, the period under the statute is specified to be "for a period of five years from the granting of such leasehold and execution of any instrument evidencing said grant." and "for a period of five years from the year in which the corporation lessee commenced business operations on the leased premises." Thus, it would appear that the exemption would date from the granting of the leasehold and commencement of business operations on the leased premises rather than necessarily from the time the project was "in existence", and under the terms of the statute that should be the date from which to compute time rather than from the effective date of the statute.

Your fourth question is stated as follows:

4. If expansion of a project that was built with private funds is now contemplated, would the municipality have the power under the Municipal Industrial Development Act to purchase the project that was built with private funds, then finance the construction of the proposed expansion, and then lease both the original plant and the expanded part to the former owner of the original plant who built it?"

Subsection 1 of section 40-57-03 of the North Dakota Century Code gives authority to acquire existent plants and to extend same. Subsection 3 of said section 40-57-03 gives authority to lease such projects. There is no prohibition in the statute that would prevent leasing a plant, whether expanded or not, to a former owner of such plant.

Your fifth question is stated as follows:

5. If the answer to question no. 4 is yes, would the exemption from property taxes provided by the 1965 amendment extend to the entire leasehold interest, that is, to that part of the leasehold interest represented by the original plant built with private funds and to that part of the leasehold interest represented by the expanded part of the plant built and financed under the Municipal Industrial Development Act? If this property tax exemption applies to the entire leasehold interest, will the exemption run for the full five year period for the entire leasehold interest? Will the exemption from income tax apply to the income derived from the entire leased project, both the original part and the expanded part, and, if so, will the exemption extend for the full five years?"

We believe your fifth question is properly answered in the affirmative.

Your sixth question is stated as follows:

6. In the case of a project that was financed and constructed prior to July 1, 1965, under the provisions of the Municipal Industrial Development Act, will either the personal property tax exemption or the income tax exemption created by this 1965 amendment be applicable to such a project? If either or both of the exemptions are applicable, will they extend for five years after July 1, 1965, or will they be limited to the period of time after July 1, 1965, that will end five years after the leasing of the project to the lessee?"

We believe that your sixth question is also properly answerable in the affirmative and to the effect that they will be limited to the period of time after July 1, 1965, that will end five years after the leasing of the project to the lessee.

Your seventh question is stated as follows:

7. If the answers to question no. 6 are no and if such a plant is expanded after July 1, 1965, and the expansion is financed under the Municipal Industrial Development Act, will this expanded part of the project and the income derived from it be entitled to the exemptions provided by the 1965 amendment? If the income tax exemption applies to the income derived from the expanded part of the project, should the income from the operation of the original plant and from the operation of the expanded part of the plant be allocated under rules and regulations prescribed by the tax commissioner that are intended to fairly and equitably apportion the income between the two parts of the project?"

As you will note our answer to your question no. 6 is "yes", however, we believe the first part of your seventh question is likewise answerable in the affirmative. The latter portion of the question presents a more difficult problem. Basically it is our opinion that the allocation must properly be made under the terms of the statute, although it is our opinion that the Tax Commissioner does have authority to prescribe appropriate rules and regulations, and that proper rules may well simplify the obtention of a fair and just result in the making of such allocation.

Your eighth question is stated as follows:

8. After a municipality has leased the project to the lessee, is there any property interest in either the land or the improvements that is assessable to the lessee even though, under the 1965 amendment, the leasehold is classified as personal property and exempted from property taxes for a five year period?"

This question does present an interesting problem, although we believe it will be best determined from the actual facts and circumstances of given cases. There is nothing to indicate such property interests in the factual situations assumed to exist in questions one through seven heretofore answered, though we believe it clear that both municipalities and operators under the Act may well

draw variations on the basic theme that might well be taxable to the operator. To draw an example at random, it is conceivable that a municipality could deed a space that in actuality contains a suite of offices on the sixth floor of the plant to the operating corporate entity. Under the terms of the Act, the deeded as opposed to lease premises would obviously be taxable.

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Attorney General