

Overruled in part by N.D.A.G. 89-6

OPINION
79-267

February 12, 1979 (OPINION)

Mr. R. E. Lommen
Land Commissioner
State Land Department
State Capitol
Bismarck, North Dakota 58505

Dear Commissioner Lommen:

This is in response to your request for an opinion on the following question:

May a county levy a tax on the leasehold interest in lands under the control of the Board of University and School Lands?

Our response to your question is in the negative until such time as the Legislature specifically provides for such levy. Our reasons for this opinion follow:

I.

Section 176 of the North Dakota Constitution provides in part that:

The property of the United States and of the state, county and municipal corporations and property used exclusively for schools, religious, cemetery, charitable or other public purposes shall be exempt from taxation.

Subsections 1, 2, and 3 of Section 57-02-08, North Dakota Century Code, insofar as this discussion is concerned, also generally exempt the same property from taxation by providing:

57-02-08. PROPERTY EXEMPT FROM TAXATION. - All property described in this section to the extent herein limited shall be exempt from taxation, that is to say:

1. All property, real or personal, owned exclusively by the United States except any such property which the state and its political subdivisions are authorized by the laws of the United States to tax;
2. All property, real or personal, owned by this state, but no lands contracted to be sold by the state shall be exempt;
3. All property, real or personal, belonging to any county, city, park district, township, school district, or to any other municipal corporation, except that land purchased by counties at tax sales shall be taxed until the period of redemption from such tax sale has been terminated;

* * *

Although property owned by the United States, this state, or its political subdivisions cannot be taxed to the government unit that owns it except where Congress has waived United States immunity as provided in Section 57-02-08(1), the federal and state courts have many times rules that privately held leasehold or other possessory interests in federal, state, or local government-owned real property can be taxed by the state and its political subdivisions under statutes that so provide. See, for example, such cases as *United States v. County of Fresno*, __ U.S. __ 50 L. Ed. 2d. 683, 97 Supreme Court (1977), upholding California's taxation of possessory interests of federal employees in housing owned and furnished to them by the federal government; *Ottertail Power Co. v. Degnan*, 64 N.D. 413, 252 N.W. 619 (1934), in which Ottertail's leasehold or possessory interest in real property owned by the City of Devils Lake was held subject to property taxation by the state and its political subdivisions; *Lower Yellowstone Irrigation District No. 2 v. Nelson*, 71 N.D. 439, 2 N.W.2d. 180 (1941), in which a desert entryman's interest in federal public lands prior to acquisition by him of a complete equitable title is subject to state taxation; and *Moeller v. Gormley*, 87 P. 507 (Wash. 1906), relief on in the Ottertail case, supra, in which the Washington Supreme Court held leasehold interests in state-owned tidelands to be subject to taxation.

This office has stated in previous opinions and correspondence that a leasehold interest held by a private party in state, municipal, public school district and political subdivision-owned land is not exempt from taxation even though the fee title held by a governmental unit is exempt. (See opinions dated July 27, 1973, to Divide County State's Attorney; July 3, 1978, to Vice President, University of North Dakota; October 26, 1978, to Mountrail County State's Attorney; November 27, 1978, to Sheridan County State's Attorney, and December 29, 1978, to Logan County State's Attorney.)

In North Dakota, privately held possessory interests in governmentally owned real property are subject to property taxation because of Sections 57-02-03 and 57-02-04(1). Section 57-02-03 provides that "Except as otherwise expressly provided" all real property (as well as other property) "is subject to taxation." Subsection 1 of Section 57-02-04 defines real property for taxation purposes as including:

1. The land itself . . . and all rights and privileges thereto belonging or in any wise appertaining. . .

There is no provision in our statutes which expressly (see 57-02-03) exempts private leasehold interests in state-owned land from taxation. In this regard, in *Northern Pacific Railway Co. v. Morton County*, 32 N.D. 627 at 647, 156 N.W. 226 at 232 (N.D. 1915), the Supreme Court in considering Sections 2118, 2076 and 2075 of the 1913 Compiled Laws, now Sections 57-02-26, 57-02-04 and 57-02-03, said in reference to Section 2075, now Section 57-02-03:

Leasehold interests are not "expressly excepted" and are therefore taxable.

The following is quoted from *Ottertail Power Co.*, supra, in which the Supreme Court held Ottertail's possessory interest in buildings owned by the City of Devils Lake taxable under Section 2076 of the Compiled Laws of 1913 (now Section 57-02-04):

In *ex parte* Gaines (*Garland County v. Gaines*) 56 Ark. 227, 19 S.W. 602, it is held "that the interest of a lessee in lands leased from the United States is not exempt from assessment for taxation," and further that such interest acquired by the lease was property. To the same effect is *Outer Harbor Dock and Wharf Co. v. Los Angeles*, 49 Cal. App. 120, 193 P. 137; *Carrington v. People*, 195 Ill. 484, 63 N.E. 163; *State ex rel. Sioux County v. Tucker*, 38 Neb. 56, 56 N.W. 718. In this latter case the court held that "school lands sold by the state, but to which the equitable title of the purchaser has not been completed by full payment of the purchase money, are subject to taxation to the extent of the purchaser's interest therein."

This latter holding is based upon the broad general principle that "exemptions no matter how meritorious, are of grace, and must be strictly construed;" and "the constitution and the statutes based thereunder contemplate the taxation of all property not specifically exempted." It is true there was also a statute in Nebraska specifically providing for the taxation of the purchaser's interest in school lands, similar to one in this state, but the courts hold that independent of such statute such interest is taxable. If leasehold and possessory interests are taxable as rights and privileges appertaining to the real estate, we see no reason why the right to use of the building involved herein is not also taxable. such an eminent authority as Cooley in his work on taxation (*I Cooley on Taxation* 3d. Ed. p. 635) says: "It is entirely competent to provide for the assessment of any mere possessory right in lands whether they are owned by the government or by private individuals." 64 N.D. at 421, 252 N.W. at 621-622.

It is important to note that Ottertail's leasehold or other possessory interest in the city-owned building was held taxable in the above case under Section 2076 of the 1913 Compiled Laws which is quoted in 64 N.D. at 419, 252 N.W. at 621 as follows:

Real property, for the purpose of taxation, includes the land itself, whether laid out in town lots or otherwise, and, except as otherwise provided, all buildings, structures and improvements (except plowing and trees thereon) and all rights and privileges thereto belonging or any wise appertaining, for all mines, minerals, quarries in and under the same.

The substance of that definition is now included in subsections 1 and 2 of Section 57-02-04.

In the 1942 case of *Lower Yellowstone Irrigation District v. Nelson*, *supra*, the court, after quoting the above real property definition in Section 2076 in the opinion denying a rehearing, said:

This section expressly subjects rights and privileges appertaining to real property to taxation as such. But appellant says they may not be taxed separately but only as an adjunct to the land to which they appertain. The question as to whether or not rights or privileges, held by persons who are not exempt from taxation, in real property the fee title to which is held by one who is exempt from taxation, in real property the fee title to which is held by one who is exempt from taxation, are taxable as real property was fully and carefully considered in the case of *Ottertail Power Company v. Degnan*, 64 N.D. 413, 252 N.W. 619. In that case we held that the Ottertail Power Company's right to the use of the tax

exempt property of the city of Devils Lake was taxable as real property under the provisions of section 2076, supra. It follows that the rights and privileges in land held by the appellant in this case are taxable as real property. But appellant says that while the result in the decision is correct, the court's construction of section 2076, supra, is incorrect and the results should have been reached by a construction of section 2118, Compiled Laws of 1913. It may be that the decision could have rested upon a construction of section 2118, supra, but nevertheless we did construe section 2076 and that construction has been the settled law of this state since 1935. We think the reasoning of the decision in this case is sound and amply supported by cited authority and we therefore adhere to it. 71 N.D. at 444, 2 N.W.2d. at 183.

As already noted, Section 2076 is now Section 57-02-04, and Section 2118 is now Section 57-02-26. Section 57-02-26 and its purpose will not be considered.

II.

Section 57-02-26 provides:

57-02-26. CERTAIN PROPERTY TAXABLE TO LESSEE OR EQUITABLE OWNER. - Property held under a lease for a term of years, or under a contract for the purchase thereof, belonging to the United States or to the state or a political subdivision thereof, except such lands as have been leased for pasture or grazing purposes, or to any religious, scientific or benevolent society or institution, whether incorporated or unincorporated, or to any railroad corporation whose property is not taxed in the same manner as other property, shall be considered, for all purposes of taxation, as the property of the person holding the same.

The source note shown in the Century Code for Section 57-02-26 indicates its original source as Section 29 of Chapter 126, Session Laws 1897. Chapter 126 is shown as the original source for most of the provisions of Chapter 57-02, North Dakota Century Code. Section 29 of Chapter 126 read as follows:

Section 29. CERTAIN PROPERTY HELD TO BELONG TO LESSEE OR EQUITABLE OWNER. - Property held under a lease for a term of years, or a contract for the purchase thereof, belong to the state (except such state lands as have been leased for pasture or grazing purposes), or to any religious, scientific or benevolent society or institution, whether incorporated or unincorporated, or to any railroad company or corporation, whose property is not taxed in the same manner as other property, shall be considered, for all purposes of taxation, as the property of the person so holding the same.

Although the above-quoted Section 29 of the 1897 law is shown as the source in the Century Code for Section 57-02-26, the first session of the Legislature following statehood had enacted a revenue and taxation law that included a very similar provision in Section 27 of Chapter 132, S.L. 1889-1890, which read as follows:

Section 27. CERTAIN PROPERTY HELD TO BELONG TO LESSEE OR EQUITABLE OWNER. - Property held under a lease for a term of three or more

years, or a contract for the purchase thereof, belonging to the state, or to any religious, scientific or benevolent society or institution, whether incorporated or unincorporated, or to any railroad company or corporation whose property is not taxed in the same manner as other property, shall be considered for all purposes of taxation as the property of the person so holding the same.

These two sections of the 1889-1890 and the 1897 laws are the same except that, first, in the 1889-1890 Session Laws, a lease had to be "for a term of three or more years" whereas under the 1897 law the reference is only to a lease "for a term of years," and, second, the language "(except such state lands as have been leased for pasture or grazing purposes)" that appears in the 1897 section did not appear in the 1889-1890 section.

In the Lower Yellowstone Irrigation District case, *supra*, the court said that while it probably could have held in the Ottertail Power Company case, *supra*, that Ottertail's leasehold interest in city-owned real property was taxable under Section 2118, now Section 57-02-26, it had in fact held it taxable under Section 2076, now Section 57-02-04, and that that had become settled law to which it adhered. In this regard it is important to note that Section 57-02-26 has also always included a reference to property "held under . . . a contract for the purchase thereof, belonging to the state . . ." In the Ottertail case the court pointed out, which seemingly apparent approval, the fact that the Nebraska court in *State ex rel. Sioux County v. Tucker*, 56 N.W. 718 (Neb. 1893), held that state school land held by a purchaser under a contract for its purchase was taxable to the extent of the purchaser's interest therein and that it was taxable under the general statutes of Nebraska independent of the fact that a specific Nebraska statute provided for taxation of the purchaser's interest in school lands, which statute, as the North Dakota Supreme Court pointed out in *Ottertail*, was "similar to one in this state."

Therefore in view of the fact that the North Dakota Supreme Court regards both a privately owned leasehold interest in a state-owned real property and a privately owned interest under a contract for the purchase of state-owned property to be taxable under Sections 57-02-03 and 57-02-04, it is necessary to consider the purpose of Section 57-02-26.

It is considered that the purpose of Section 57-02-26 is to provide a method for determining how such private leasehold interests shall be valued and assessed for purposes of taxation. This section provides that such "property" held by a person under a lease or contract for its purchase "shall be considered, for all purposes of taxation, as the property of the person so holding the same." In other words, the assessed value of that person's interest shall be the same as if he were the fee owner of it. This is true not only for state-owned property, but also for property owned by a railroad that is leased for nonrailroad purposes. See: *Northern Pacific Railway Company v. Morton County*, *supra*, 32 N.D. at 645-647.

The above interpretation, however, would not apply to state-owned lands "leased for pasture or grazing purposes" due to the specific exception in Section 57-02-26. Such lands would not be valued and assessed to the lessee as though he were the fee owner of them as provided for other interests covered by Section 57-02-26; instead, a lessee of state-owned land for pasture and grazing purposes would be assessed only for the value of his leasehold interest in them, which would presumably be a lesser value than if he were assessed as though he were the fee owner.

A lessee of state-owned pasture or grazing lands would be assessed on the value of his leasehold interest. That leasehold interest in exempt land owned by the state is a right or privilege in real property that is subjected to taxation by Sections 57-02-03 and 57-02-04, as interpreted in the Ottertail and Lower Yellowstone Irrigation District cases. Furthermore, Section 57-02-26 provides that the method of valuation it prescribes does not apply to state-owned lands leased for pasture or grazing purposes.

III.

While we conclude that there are no statutory or general constitutional provisions that prohibit taxing leasehold interests in state-owned trust lands under the control of the Board of University and School Lands, we do not believe that existing statutory law provides the necessary procedures to implement such taxation. For example, see Chapter 47 of the South Dakota Session Laws for 1977. In reaching this conclusion we are aware of the fact that since statehood leasehold interests in state-owned trust lands under the control of the Board of University and School Lands have not, in practice, been assessed for the purpose of taxation and that only very recently have attempts been made by local assessing authorities to subject these leasehold interests to taxation by reliance upon the statutory and case law authority reviewed above in this opinion.

We take notice of the fact that the Board of University and School Lands manages approximately 700,000 surface acres. Neither Title 15, dealing with state-owned trust lands, nor Title 57, dealing with taxation, contain any provisions to implement this taxation. In contrast, the procedures for taxing state-owned trust lands sold under contract for deed are set forth with particularity in North Dakota Century Code Sections 15-08-12, 13, 14, 18, 18.1, 18.3, 18.6, and 19. In order to tax state-owned trust lands in accordance with North Dakota Century Code Section 57-02-26 it would be necessary to classify lands used for pasture and grazing and lands used for other than pasture and grazing. The State Land Department would have to furnish these classifications together with names and addresses of all lessees and assignees to counties on a continuing basis. Furthermore, some "pasture and grazing" lands might be used for haying; conversely, some cultivated lands might be seeded to tame grass and used for grazing. Yet, no statutes have been enacted to address these problems.

We have not addressed the special Constitutional and Enabling Act provisions that may prohibit the taxation of state-owned trust lands. Article IX of the North Dakota Constitution and Sections 11-19 of the Enabling Act do pose questions as to the legality of taxing leasehold interests in trust lands. These questions may ultimately have to be resolved in the courts should legislation be enacted specifically authorizing the taxation of leasehold interests. Given the special status of these trust land and the large acreage involved, we do not believe our opinion is inconsistent with previous opinions of this office that generally have ruled that leasehold interests in state and political subdivision property are taxable.

It is hoped that the foregoing will be of assistance.

Sincerely,

ALLEN I. OLSON
Attorney General