# DEPARTMENT OF TAXATION
# 2015 Fiscal Impact Statement

**1. Patron** John C. Watkins

**2. Bill Number** SB 1031

**House of Origin:**
_____ **Introduced**
_____ **Substitute**
_____ **Engrossed**

**Second House:**
__X__ **In Committee**
_____ **Substitute**
_____ **Enrolled**

**3. Committee** House Finance

**4. Title** Real Property Tax; Taxation of Leasehold Interests; Federal Rehabilitation Tax Credits

**5. Summary/Purpose:**

This bill would provide a real property tax exemption for a tenant's leasehold interest on tax-exempt property if the tenant is entitled to or has received rehabilitation tax credits related to the property, and the property otherwise qualifies for exemption. The bill would also extend the exemption to qualifying tenants that use the property exclusively for cultural purposes.

Under current law, a tenant's leasehold interest on real property for which the owner is exempt, is assessable for local taxation to the lessee. An exemption is available, however, for lessees that are designated as § 501(c) organizations under the Internal Revenue Code, provided the property in question is: 1) owned by the Commonwealth or its political subdivisions; 2) owned and exclusively occupied or used by churches or religious bodies; or 3) exempt from taxation by designation. In addition, the property must be used exclusively by the lessee primarily for charitable, literary, scientific, or educational purposes in order for the exemption to apply.

The effective date of this bill is not specified.

**6. Budget amendment necessary:** No.

**7. Fiscal Impact Estimates are:** Not available. (See Line 8.)

**8. Fiscal implications:**

To the extent that lessors within a locality either: a) are entitled to or have received federal rehabilitation tax credits for qualifying property within the locality; or b) are tenants that otherwise qualify for the exemption, but use such property exclusively for cultural purposes, this bill would result in a loss of local real property tax revenues in that locality. The magnitude of the local revenue loss is unknown. This bill would have no impact on state revenues.

**9. Specific agency or political subdivisions affected:**

All localities

**10. Technical amendment necessary:** No.

**11. Other comments:**

<u>Real Property Tax on Leased Property</u>

When real property is leased, the tenant may be subject to property tax on the leasehold interest if the owner is exempt. If the remaining term of the lease is 50 years or more or the tenant has the option to acquire the property for a nominal sum at the completion of the lease, the leasehold interest is assessed as if the tenant were the owner. Otherwise, the assessment is reduced by two percent for each year that the remainder of the term is less than fifty years; however, the assessment may not be reduced more than 85%.

Leasehold interests on exempt real property owned by the state or used for religious, charitable, patriotic, historical, benevolent, cultural, or public park and playground purposes, or exempt by designation under the Constitution may also be exempt if the lessee is designated as a § 501(c) organization by federal law and the property is used exclusively by the lessee primarily for charitable, literary, scientific or educational purposes.

<u>Federal Historic Preservation Tax Credit</u>

Under federal law, an investment tax credit is allowed to taxpayers for the rehabilitation of historic income-producing properties that are deemed to be certified historic structures. "Certified historic structure" includes any building, and its structural components, which is:

- Listed in the National Register; or
- Located in a registered historic district and is certified by the Secretary of the Interior as being of historic significance to the district.

The credit is equal to 20 percent of the cost of rehabilitating or preserving commercial, agricultural, industrial, or rental residential buildings that are deemed historic structures.

An additional investment tax credit equal to 10 percent of the rehabilitation expenditures is available for the rehabilitation of non-historic buildings placed in service before 1936. The credit applies only to buildings rehabilitated for non-residential uses. The rehabilitation must be substantial, exceeding either $5,000 or the adjusted basis of the property, whichever is greater. The property also must be depreciable.

Lessees are entitled to claim the rehabilitation tax credit when they incur the cost of rehabilitation and the lease term is greater than the recovery period (currently 39 years for non-residential real property and 27.5 years for residential rental).

Proposal

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The effective date of this bill is not specified.

Similar Legislation

**House Bill 1766** is identical to this bill.

cc :  Secretary of Finance

Date: 2/9/2015 KP
DLAS File Name:  SB 1031F161