

Long Awaited Tech One Associates Decision Clarifies Taxation of Leasehold Interests

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In a much anticipated decision, the Pennsylvania Supreme Court in *Tech One Associates v. Board of Property Assessment, Appeals and Review of Allegheny County*, 32 WAP 2010 (April 25, 2012), held there is statutory authority to tax leasehold interests as part of the totality of the assessment. Thus an assessment can properly include the value of land, buildings, and other improvements, regardless of whether the buildings and land were put there by the landlord or the tenant. This will alter what had been confusing present practice, and will require parties to leases to carefully consider tax responsibility.

The issue before the court was the validity of a single unified assessment of both a tract of land and the buildings of a shopping center, movie theater and restaurant located on land owned by Tech One Associates. The buildings and improvements were constructed by a second entity and owned by that entity under a long term lease. The Board of Property Assessment of Allegheny County treated the land, buildings and the improvements all as real estate subject to taxation.

Tech One argued that it should be taxed on the rent paid for the ground by the lessee and the present worth of the reversionary interest in the property at the conclusion of the long term lease, reasoning that the current value of the improvements should not be included in its assessment.

After analyzing the contentions of the parties, the Court ultimately determined that leasehold interests are taxable under the phrase "All Real Estate" in 72 P.S. § 5020-201. Therefore, the Pennsylvania Supreme Court has now held that there is statutory authority to tax leasehold interests as part of the totality of the assessment.

After determining that buildings and improvements of the shopping center were real estate, the Court then determined the proper methodology for valuing the real estate. In doing so, the Court stated the following:

"The term 'actual value' as used in Section 402 means 'market value.' *In re Brooks Bldg.*, 391 Pa. 94, 97, 137 A.2d 273, 274 (1958). Market value is 'a price which a purchaser, willing but not obliged to buy, would pay an owner willing, but not obliged to sell, taking into consideration all uses[s] to which the property is adapted and might in reason be applied.' *Deitch Co. v. Bd. of Prop. Assessment, Appeals and Review*, 417 Pa. 213, 217-218, 209 A.2d 397, 400 (1965) (quoting *Buhl Found. v. Bd. Of Prop. Assessment, Appeals and Review*, 407 Pa. 567, 570, 180 A.2d 900, 902 (1962)). Thus, in an assessment appeal, '[e]vidence presented by appraisers must be directed to the market value of the property as a whole.' *Rieck Ice Cream Co. v. Bd. Of*

Prop. Assessment, Appeals and Review, 417 Pa. 249, 256, 209 A.2d 383, 387 (1965); see also *Miracle Mile Shopping Center v. Bd. Of Prop. Assessments, Appeals and Review*, 417 Pa. 243, 245, 209 A.2d 394, 395 (1965) ('The basic and controlling substantive issue in a real estate assessment appeal is the correctness of the total assessment of the property as a unit.'). The 'property as a whole' in this case, i.e., the real estate comprising the tax parcel at issue, consists of the land upon which the shopping center buildings and improvements sit, as well as the buildings and the improvements themselves; hence it is the market value of this entire parcel – land, buildings, and improvements – which Allegheny County was required to ascertain for assessment purposes."

Tech One Associates, 32 WAP 2010.

Therefore, in valuing the land owned by Tech One as the leased fee, the Court held that it was necessary to consider the impact of the ownership division and rent restrictions created by the lease on Appellant's ability to sell the land, and, in capitalizing the value of the income stream that an owner of the land could expect to receive. Likewise, in valuing the shopping center buildings and other improvements owned by Lessee as leasehold interests, it is necessary to consider the impact of the lease on the value the Lessee could expect to receive if it attempted to assign the leasehold interests to others, and, in capitalizing the value of the income stream generated by Lessee's leasehold interests, it is necessary to use the contract rent which Lessee received under the subleases which it had entered into with tenants.

This case is significant because it clarifies the taxable status of leased fee interests and leasehold interests. In short, the Court held that both the leasehold interest and the leased fee interest are taxable real estate and that their combined value must be calculated and their assessment based on the total combined value. While the Court held that both leasehold and leased fee interests are taxable, it did not make any ruling that separate tax parcels can be created but rather confined the holding to how to assess a unified tax parcel.

It is critical that drafters of leases in these types of situation be cognizant of the holding in this case, because there is nothing in this case which allows a County to create separate tax parcels for the leasehold and lease fee. Leases will have to be drafted carefully to allocate tax responsibility.

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