



Sales and Use Tax

2000-2002

SUMMARY

QUESTION: Are payments made to a lessor by a lessee for "tenant improvements" subject to sales tax when: 1) the governing lease agreement indicates that the "reimbursements" are to be considered rent payments, 2) the tenant is required to make such "reimbursements" in order to continue to occupy the premises, 3) the existence of the reimbursements was a factor in pricing the lease, and 4) the "tenant improvements" will ultimately transfer to the lessor.

ANSWER - Based on the Facts Below: Yes. The "tenant improvement" payments made by lessee are part of the "total rent or license fee" paid to lessor for the privilege of remaining in possession of the subject property. Accordingly, such payments are taxable under s. 212.031, F.S.

Apr 15, 2002

Re: Technical Assistance Advisement 02A-020
Sales and Use Tax -- Tenant Improvements/Part of Total Rent

Statutes: Sections 212.031(1)(a)8., 212.02(10)(i), F.S.

Rules: Rule 12A-1.070(1)(a) 7., F.A.C.

XXX ("Lessor")

FEI #: XX

XXX ("Lessee")

FEI #: XX

Dear :

This is in response to your request for a Technical Assistance Advisement (TAA) regarding the taxability of real property improvement charges classified as additional rent.

Facts

Lessor leases approximately 16.6 acres of its property to Lessee. Lessee uses the premises for offices, warehouse and distribution facilities, and other maritime-related purposes. According to Addendum IV of the lease agreement (Special Conditions, 1. Improvements to the Premises Financed by the Authority), Lessee was provided with an Improvement Allowance of

up to \$1,000,000 to be used to finance improvements such as fencing, pavement restoration, lighting and other miscellaneous repairs or improvements necessary to make the premises suitable for Lessee's authorized use.

Lessee was under no specific contractual obligation to use the \$1,000,000. Lessee was obligated to repay any portion of the allowance it elected to use back to Lessor, plus interest, by commencing monthly payments amortized over 10 years upon completion of the subject improvements. Lessee elected to use the full amount of the improvement allowance. Under Addendum IV of the lease agreement the reimbursements are styled Additional Consideration, and must be paid directly to lessor as part of the monthly rental consideration.

Requested Advisement

Whether payments included as a part of monthly rental payments, styled "additional consideration" in the governing agreement, are taxable rental payments when such payments are made as reimbursements under a provision for a tenant improvement allowance.

Applicable Law and Discussion

Section 212.031(1)(a), F.S., provides that it is the legislative intent that every person is exercising a taxable privilege who engages in the business of renting, leasing, letting, or granting a license for the use of any real property, with certain enumerated exceptions. A "license" to use real property is defined in section 212.02(10)(i), F.S., as "... the granting of a privilege to use or occupy a building or a parcel of real property for any purpose."

Section 212.031(1)(c), F.S., provides in part:

For the exercise of such privilege, a tax is levied in an amount equal to 6 percent of and on the total rent or license fee charged for such real property by the person charging or collecting the rental or license fee. The total rent or license fee charged for such real property shall include payments for the granting of a privilege to use or occupy real property for any purpose and shall include base rent, percentage rents, or similar charges....

Determination

The consideration paid by Lessee for the right to use and occupy the premises is apportioned in the Lease as "Rent" and "Additional Rent." Addendum IV provides that the tenant improvement reimbursements should be styled "Additional Consideration." Section II B. of the Lease provides, in pertinent part:

Whenever under the terms of this lease any sum of money is required to be paid by Tenant in addition to the Rent set forth herein... such sum shall be deemed "Additional Rent" if not paid when due, and shall be collectible as such with

the first installment of Rent falling due thereafter. Said sum shall be deemed Additional Rent regardless of whether it is herein described as Additional Rent or a provision is made for the collection of such sum as Additional Rent.

Under the Lease and Addendum IV, the reimbursements are "Additional Rent," paid directly to lessor as part of the monthly rental consideration. Thus, the lease agreement itself contemplates that the money paid for the specified improvements is rent paid for the use of the property.

The Department does not agree with Lessee's characterization of the tenant improvement allowance as a loan. Lessor did not provide a short-term loan to cover construction costs and did not pass on Lessee's payments to another entity. Lessor was the terminus for the payments made by Lessee. The lease agreement itself specifically provides that certain necessary improvements, such as fencing, pavement repairs, and lighting, are to be agreed upon by both parties during a 60-day "due diligence" period. The obligation to pay rent does not commence until substantial completion of the improvements agreed to during the due diligence period, provided such improvements are substantially completed on or before May 15, 2000. Otherwise, rental payments commence May 15, 2000. If the tenant fails to make improvements, or fails to pay for such improvements, then the Lessor can re-enter the property and take possession of the leased premises. The making of the improvements, the cost of which is to be borne fully by the tenant, is a condition precedent to occupancy. The making of the improvements is not optional for the tenant. X

At the termination of the lease, all improvements become the property of the Lessor. These improvements are of a nature that would benefit any tenant of the Lessor's property, not just the Lessee. The Lessee has no claim to the improvements at the termination of the lease. Thus, the Lessor clearly receives an economic benefit from the improvement. The fact that the improvements benefit the property in general is reflected in the schedule of lease payments. During early years of the lease, when the improvements are required to be made, the lease payments are significantly lower (20% - 25%) than those in later years. The fact that significant leasehold improvements were to be made at the tenant's expense was taken into consideration in pricing the base rent for the first few years of the lease.

Section 212.031(1)(c), F.S., imposes sales tax on the total rent or license fee charged for the use or occupancy of real property. Rule 12A-1.070(4)(b), F.A.C., describes the tax as levied on all "considerations" paid by the tenant. While the rule does not define "consideration," Black's Law Dictionary (Sixth Ed. 1990), defines such term as follows:

[I]nducement to a contract... Some right, interest, profit, or benefit accruing to one party....

In this situation, the lease agreement itself specifically indicated that the reimbursements for the improvements were to be considered rent payments. The Lessor is required to make such reimbursements in order to retain occupancy of the

premises. The Lessor receives an economic benefit from the reimbursements, as they represent amounts paid by the Lessee for improvements that ultimately transfer to the Lessor for the Lessor's use with respect to future tenants. And, the existence of such reimbursements was a factor in pricing the lease. Due to the economic value of the improvements that would ultimately be received by the Lessor, the Lessor substantially reduced the base rental payment for the first few years of the lease, when the improvements needed to be made. Accordingly, the Department must construe the tenant improvement reimbursements as part of the total rent paid by Lessee for the use and occupancy of the premises rather than as payments made pursuant to a loan for construction services.

This response constitutes a Technical Assistance Advisement under s. 213.22, F.S., which is binding on the Department only under the facts and circumstances described in the request for this advice as specified in s. 213.22, F.S. Our response is predicated on those facts and the specific situation summarized above. You are advised that subsequent statutory or administrative rule changes or judicial interpretations of the statutes or rules upon which this advice is based may subject similar future transactions to a different treatment than expressed in this response.

You are further advised that this response, your request and related backup documents are public records under Chapter 119, F.S., and are subject to disclosure to the public under the conditions of s. 213.22, F.S. Confidential information must be deleted before public disclosure. In an effort to protect confidentiality, we request you provide the undersigned with an edited copy of your request for Technical Assistance Advisement, the backup material and this response, deleting names, addresses and any other details which might lead to identification of the taxpayer. Your response should be received by the Department within 15 days of the date of this letter.

Sincerely,

Case A. Bodiford
Attorney
Control # 46875

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Sales and Use Tax

2000-2002

SUMMARY

QUESTION 1: Whether payments included as a part of monthly rental payments, payable directly to a landlord as part of the base rent under the governing agreement, are taxable rental payments when such payments are made as reimbursements under a provision for the construction of tenant improvements.

ANSWER 1- Based on the facts below: Yes, payments included as a part of monthly rental payments payable directly to a landlord as part of the base rent under the governing agreement are taxable rental payments when such payments are made as reimbursements under a provision for the construction of tenant improvements.

QUESTION 2: Whether a purchaser of real property will become liable for any sales and use tax which has not been paid by the seller of such property, when seller failed to collect sales tax on tenant improvement reimbursements taxable as rental consideration.

ANSWER 2- Based on the facts below: Yes, a purchaser of a business, such as commercial rental property, for consideration will become liable for any sales and use tax which has not been paid by the seller with respect to that business.

Aug 28, 2002

Re: Technical Assistance Advise ment 02A-034
 Sales and Use Tax - Real Property Improvement/Additional
 Rent
 Statutes: Sections 212.031(1)(a) and (c), F.S
 Rules: 12A-1.070(4)(b), F.A.C.
 XXX ("Buyer")
 FEI #: XX
 XXX ("Seller/Lessor")
 FEI #: XX

Dear :

This is in response to your request for a Technical Assistance
 Advise ment (TAA) regarding the taxability of real property
 improvement charges classified as additional rent.

Facts

Seller/Lessor entered into an industrial lease agreement with XXX ("Lessee") for the rental of a XX square foot warehouse bay on or about XX. Under paragraph 29 of the lease agreement, entitled "As is," the Seller/Lessor undertook, at his sole cost and expense, to perform certain work ("Landlord's Work") to make the premises suitable for the Lessee. This work was described in Schedule A of the lease agreement, and it included the construction of a XXX. The cost of constructing these improvements was amortized over a ten-year period, with a five-year balloon of all principal, unless the lender extended for another five years.

Seller/Lessor and Lessee entered into an addendum to the lease to reflect the increase in Base Rent due to the amortization of the cost of the improvements. Lessee was required to pay Seller \$XX in sixty equal monthly payments of \$XX from XXX, through XXX. If Lessee elected to exercise its option to extend the lease term an additional five years, it was required to pay Seller/Lessor an additional \$XX in sixty equal monthly payments of \$XX. If Lessee did not elect to extend the lease an additional five years, it was required to pay Seller/Lessor a final payment of \$XX, due on XX.

I. Tenant Improvement Reimbursements

Requested Advisement

Whether payments included as a part of monthly rental payments, payable directly to a landlord as part of the base rent under the governing agreement, are taxable rental payments when such payments are made as reimbursements under a provision for the construction of tenant improvements.

Applicable Law and Discussion

Section 212.031(1)(a), F.S., provides that it is the legislative intent that every person is exercising a taxable privilege who engages in the business of renting, leasing, letting, or granting a license for the use of any real property, with certain enumerated exceptions.

Section 212.031(1)(c), F.S., provides in part:

For the exercise of such privilege, a tax is levied in an amount equal to 6 percent of and on the total rent or license fee charged for such real property by the person charging or collecting the rental or license fee. The total rent or license fee charged for such real property shall include payments for the granting of a privilege to use or occupy real property for any purpose and shall include base rent, percentage rents, or similar charges....

The improvement reimbursements paid by Lessee to Seller/Lessor for the right to use and occupy the premises are apportioned in paragraph 29 of the lease and Addendum 1 as "Base Rent." The

reimbursements are included as a line item in the monthly rental invoices, and are paid as a component part of each monthly rental payment made directly to Seller/Lessor. Thus, the lease agreement itself contemplates that the money paid for the specified improvements is rent paid for the use of the property.

The Department does not agree that the reimbursements are properly construed as loan payments for construction services. Seller/Lessor did not provide a short-term loan to cover construction costs and did not pass on Lessee's payments to another entity. Seller/Lessor was the terminus for the payments made by Lessee. The obligation to pay rent does not commence until substantial completion of the Landlord's Work in paragraph 29. If Lessee fails in its obligation to pay for such improvements (beginning with Lessee's obligation to commence payment of Base Rent under paragraph 2. following substantial completion of the Landlord's Work), Seller/Lessor can, subject to the timing and notice restrictions contained in paragraphs 17. and 18., re-enter the property and take possession of the leased premises. The making of the improvements, the cost of which is to be borne fully by the tenant, is a condition precedent to occupancy. The making of the improvements is not optional for the tenant.

At the termination of the lease, all improvements become the property of the Lessor. These improvements are of a nature that would benefit any tenant of the Lessor's property, not just the Lessee. The Lessee has no claim to the improvements at the termination of the lease. Thus, the Lessor clearly receives an economic benefit from the improvement.

Section 212.031(1)(c), F.S., imposes sales tax on the total rent or license fee charged for the use or occupancy of real property. Rule 12A-1.070(4)(b), F.A.C., describes the tax as levied on all "considerations" paid by the tenant. While the rule does not define "consideration," Black's Law Dictionary (Sixth Ed. 1990), defines such term as an "... inducement to a contract.... Some right, interest, profit, or benefit accruing to one party...."

In this situation, the lease agreement itself specifically indicated that the reimbursements for the improvements were to be considered rent payments. The Lessee is required to make such reimbursements in order to retain occupancy of the premises. The Seller receives an economic benefit from the reimbursements, as they represent amounts paid by the Lessee for improvements that ultimately transfer to the Seller for the Seller's use with respect to future tenants. Accordingly, the Department must construe the tenant improvement reimbursements as part of the total rent paid by Lessee for the use and occupancy of the premises rather than as payments made pursuant to a loan for construction services.

Response

Yes, payments included as a part of monthly rental payments payable directly to a landlord as part of the base rent under the governing agreement are taxable rental payments when such

payments are made as reimbursements under a provision for the construction of tenant improvements.

II. Transferee Liability

Requested Advisement

Whether a purchaser of real property will become liable for any sales and use tax which has not been paid by the seller of such property, when seller failed to collect sales tax on tenant improvement reimbursements taxable as rental consideration.

Applicable Law & Discussion

Section 212.10(1), F.S., provides the following:

(1) If any dealer liable for any tax, interest, or penalty levied hereunder shall sell out his or her business or stock of goods, the dealer shall make a final return and payment within 15 days after the date of selling the business; the dealer's successor, successors, or assigns shall withhold a sufficient portion of the purchase money to safely cover the account of such taxes, interest, or penalties due and unpaid until such former owner shall produce a receipt from the department showing that they have been paid or a certificate stating that no taxes, interest, or penalty are due. If the purchasers of a business or stock of goods shall fail to withhold a sufficient amount of the purchase money as above provided, he or she shall be personally liable for the payment of the taxes, interest, and penalties accruing and unpaid on account of the operation of the business by any former owner, owners, or assigns. Any receipt or certificate from the department does not, without an audit of the selling dealer's books and records by the department, guarantee that there is not a tax deficiency owed the state from operation of the seller's business. To secure protection from transferee liability under this section, the seller or purchaser may request an audit of the seller's books and records. The department may contract with private auditors pursuant to s. 213.28 to perform the audit. The department may charge the cost of the audit to the person requesting the audit.

Section 212.10(1) F.S., applies to voluntary transfers of a business between a buyer and seller where the buyer either pays for the business or assumes liability and debt as consideration for the "buying out of the business or stock of goods." The failure of the buyer to withhold a sufficient amount of that payment, in accordance with Section 212.10(1) F.S., would make the buyer personally liable for payment of the taxes, interest, and penalties accruing and unpaid by the seller. Accordingly, if Buyer is either paying for the business of Seller or assuming liability and debt as consideration for buying out the business or stock of Seller's goods, Buyer must withhold a sufficient amount of that payment to cover the taxes, interest, and penalties accruing and unpaid by Seller. The taxes, interest, and penalties accruing and unpaid by Seller would include the sales tax Seller failed to collect on tenant improvement

reimbursements paid by Lessee.

Response

Yes, a purchaser of a business, such as commercial rental property, for consideration will become liable for any sales and use tax which has not been paid by the seller with respect to that business.

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Control # 50722

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Aug 28, 2002

Re: Technical Assistance Advisement 02A-034

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Rent

Statutes: Sections 212.031(1)(a) and (c), F.S

Rules: 12A-1.070(4)(b), F.A.C.

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completion of the Landlord's Work), Seller/Lessor can, subject to the timing and notice restrictions contained in paragraphs 17. and 18., re-enter the property and take possession of the leased premises. The making of the improvements, the cost of which is to be borne fully by the tenant, is a condition precedent to occupancy. The making of the improvements is not optional for the tenant.

At the termination of the lease, all improvements become the property of the Lessor. These improvements are of a nature that would benefit any tenant of the Lessor's property, not just the Lessee. The Lessee has no claim to the improvements at the termination of the lease. Thus, the Lessor clearly receives an economic benefit from the improvement.

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improvements that ultimately transfer to the Seller for the Seller's use with respect to future tenants. Accordingly, the Department must construe the tenant improvement reimbursements as part of the total rent paid by Lessee for the use and occupancy of the premises rather than as payments made pursuant to a loan for construction services.

Response

Yes, payments included as a part of monthly rental payments payable directly to a landlord as part of the base rent under the governing agreement are taxable rental payments when such payments are made as reimbursements under a provision for the construction of tenant improvements.

II. Transferee Liability

Requested Advisement

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stock of goods, the dealer shall make a final return and payment within 15 days after the date of selling the business; the dealer's successor, successors, or assigns shall withhold a sufficient portion of the purchase money to safely cover the account of such taxes, interest, or penalties due and unpaid until such former owner shall produce a receipt from the department showing that they have been paid or a certificate stating that no taxes, interest, or penalty are due. If the purchasers of a business or stock of goods shall fail to withhold a sufficient amount of the purchase money as above provided, he or she shall be personally liable for the payment of the taxes, interest, and penalties accruing and unpaid on account of the operation of the business by any former owner, owners, or assigns. Any receipt or certificate from the department does not, without an audit of the selling dealer's books and records by the department, guarantee that there is not a tax deficiency owed the state from operation of the seller's business. To secure protection from transferee liability under this section, the seller or purchaser may request an audit of the seller's books and records. The department may contract with private auditors pursuant to s. 213.28 to perform the audit. The department may charge the cost of the audit to the person requesting the audit.

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Response

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Sincerely,

Case A. Bodiford
Attorney

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