

November 25, 1998

OPINION NO. 98-07

MEMORANDUM

TO: S. KALANI SCHUTTE
Deputy Director of Finance

FROM: RICHARD WURDEMAN
Corporation Counsel

RE: Taxation of Privately Occupied County Property

This is in response to your request for an opinion on the tax status of the Driving Range at the Hilo Municipal Golf Course. The range, although located on County property, is operated by a private individual, pursuant to a concession let under the provisions of Chapter 102, Hawaii Revised Statutes.

The agreement creating this relationship, entitled "Lease and Concession Agreement," encompasses both the driving range and the pro shop, which is located in the main clubhouse of the golf course. The agreement is for a term of five years, prohibits subletting and assignment without County consent, specifies the permitted hours of operation, assigns maintenance responsibilities to the concessionaire, and is otherwise quite detailed as to what the concessionaire must or cannot do, Exhibit B of the agreement delineates the boundaries of the driving range. In practice, however, on a portion of this area is an actual use. The remainder or outfield area, is mowed by the County and used as a source of sod for the golf course. In addition, the County, from time to time, stockpiled earth and other materials on the premises. These activities are conducted by the County at will, without seeking any permission from the concessionaire.

The Hawaii County Code, Section 19-84, makes real property belonging to the State or the County generally exempt from real property taxation. Excluded from this exemption, however, are cases where private persons are deemed the "owners" of the property such as when the property is

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subject to a lease, of one year or more, or when occupancy for commercial purposes, whether by lease, permit, license, or otherwise has continued for more than one year, HCC 19-84(D). Further, in cases of dual occupancy, as between the government and the tenant, the tax shall be assessed on the basis of a ratio between the space occupied by the tenant and the total floor space of the building. HCC Sec. 19-84(E).

The title given to agreements of this nature is not controlling as to how the agreement will be classified, but rather the respective rights and/or burdens assigned to the parties. *Kapiolani Park Preservation Society vs. City and County of Honolulu*, 751 P.2d 1022, 69 Haw. 569 (1988); *Robert's River Rides, Inc. vs. Steamboat Development Corp.*, 520 NW 2d, 294 (Iowa 1944); *Lee vs. North Dakota Park Service*, 262 NW2d 467 (ND 1977). A "lease" is a transfer of possession which must convey a definite space and transfer exclusive possession of the space. *Keller vs. Southwood North Medical Pavilion*, 959 P2d. 102 (Utah 1988); *Watson Pacific Ventures vs. Valley Federal Savings and Loan*, 2 F.3d 967 (9th Cir. 1993). A lease gives one the right to do any act not prohibited by its terms, a "license" only the right to carry out the purpose of the "license." *Robert's supra*. A "license" on the other hand, is merely permission to go on the lands of another to do an act or a series of acts, and is subject to management and the control of the owner. *Keller supra*.; *McCandless vs. John Li Estate*, 11 Haw. 777 (1899). Many agreements contain characteristics of both licenses and leases. In *Outdoor Media of Pensacola Inc. vs. Santa Rosa County*, 554 So.2d 613, (FL 1989), an agreement allowing the use of a county right-of-way for the placement of signs was held to be a lease. In *Keller supra*, a similar sign agreement was held to be a license.

In *In Re Fasi*, 634 P2d. 98, 63 Haw. 624 (1981), the Supreme Court was asked to employ this type of analysis to the contract for the operation of the parking lots at Honolulu Airport. Discussing the State statute applicable at the time (which is worded identically to HCC Sec. 19-84), the Court found ambiguity in the use of the words "tenant" and "occupant," denoting a lease; and "permit" and "license," in the same section. Holding that an ambiguous statute which creates an exception to an exemption should be construed in favor of the taxpayer, the Court noted that the State had retained the right to go on the land and construct improvements, as well as security and maintenance responsibilities. Thus, the State was deemed to be the true "owner" for taxation purposes, and the agreement to be an operating agreement, in which the use of the property was only an incident thereof.

Courts in other states have used similar approaches to draw the fine line between taxable and exempt properties of this nature. In *Eastern Air Lines Inc. vs. Joint City County Board of Tax Assessors, et al.*, 315 SE2d. 890, 253 Ga. 18 (1984). Florida distinguishes between governmental uses and proprietary ones, such as operating a racetrack for profit. *Volusia County vs. Daytona Beach Racing and Recreational Facilities District*, 341 So.2d 498 (FL 1976). Illinois also

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distinguishes on the basis of use by denying exemption to properties whose primary use is the production of income. *Northern Illinois University vs. Sweet*, 603 NE2d 84, 237 Ill. App. 3d 28 (1992). Utah has adopted a “significant incidents of ownership” test, considering such factors as whether improvements would be reviewed at the end of the term, maintenance responsibility and the ability to depreciate improvements for income tax purposes. *Interwest Aviation vs. County Board of Equalization*, 743 P.2d 1222 (Utah 1987).

The agreement in this case has characteristics of both lease and license. If we accept that the “central distinguishing characteristic of a lease is the surrender of absolute control of property to another person for an agreed-upon rental,” *Davis vs. Dinkins*, 206 AD2d 365, 613 HYS2d. 933 (1994), then clearly the requisite absolute control has not been so surrendered, with the exception of the office area of the driving range and the pro shop, over which the so-called lessees appears to have exclusive control. Therefore, applying the rationale of *In Re Fasi supra*, the concessionaire is not considered the “owner” for tax purposes of the open areas, and those areas remain exempt as County property.

It is puzzling that some seventeen years after the *Fasi* decision found the language which is now Section 19-84(D), HCC, to be ambiguous, that it has not been changed. One possible change would be to replace the concept of owner with that of one holding a “possessory interest,” as is done in California. Under that concept, any possession of public land is deemed taxable up to the value of the interest, leaving the reversion interest untaxed, even when some concurrent use might occur. *City of San Jose vs. Carlson*, 67 Cal. Rptr.2d 719 (Cal. App. 1997); *United States vs. County of San Diego*, 965 F2d. 691 (9th Cir. 1992); *California Revenue and Tax Code Sec.107*. Thus, HCC 19-84(D) might be re-worded to read as follows:

(D) Property in which a possessory interest is held by a non-exempt entity. A possessory interest will be found when an interest exists which results in a right of possession or exclusive use. It may consist of a leasehold estate, profit a prendre, permit, license, or any other legal or equitable right. “Exclusive use” is not destroyed by concurrent use when the use is not available to the general public, for example when two or more parties have the independent right to graze cattle on the same land.

Property taxed under this Section shall be assessed on the value of the use for the unexpired term of the interest.

See, *Lucas vs. County of Monterey*, 135 Cal. Rptr. 707 (Cal. App. 1977). (Finding a moorage in a public harbor to be taxable.) *Cal. Rev. & Tax Code Sec. 107*.

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Finally, in recognition of the fact that collection of assessments on those non-foreclosable properties is at times difficult, consideration should be given to the insertion of language such as the following at the appropriate place in the code:

Taxes on possessory interests in land and taxable improvements on land exempt from taxation which are not a lien upon the land sufficient to ensure their payment, shall act as a lien upon any other taxable property of the taxpayer located within the County.

These suggestions are merely that, and should be considered subject to any constructive suggestions from those members of our staff most familiar with the operational problems involved with the administration of the code.

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