SUMMARY

QUESTION: Whether Florida sales tax due in a commercial lease arrangement involving related parties, wherein it is alleged that no consideration flows directly from the occupant of the property to the owner of the property where both the occupant and owner record adjustments for rent under Internal Revenue Code s. 482 and Treas. Regs. s. 1.482-1 for federal and state income tax purposes.

ANSWER – Based on Facts Below: The amounts paid by the occupant of the property for alterations and improvements and the premiums paid by the occupant for insurance that protects the owner against liability and protects the owner against property damage are subject to Florida sales tax, because the occupant is responsible for these obligations for the benefit of the owner and the charge or responsibility for the insurance is separately stated within the Occupancy Agreement. Further, the amounts identified as rent by both the occupant and owner are subject to Florida sales tax under Section 212.031, F.S.

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July 23, 2004

Re: Technical Assistance Advisement 04A-044
Florida Sales and Use Tax
Related Entities and Commercial Real Property Rental
Section 212.031, F.S. (“Florida Statutes”)
Rule 12A-1.070, F.A.C. (“Florida Administrative Code”)

Dear :

This response is in reply to your letter dated January 17, 2004, requesting the Department’s issuance of a Technical Assistance Advisement (“TAA”) pursuant to Section 213.22, F.S., and Chapter 12-11, F.A.C., regarding related entities and commercial real property rentals. An examination of your letter has established that you have complied with the statutory and regulatory requirements for issuance of a TAA. Therefore, the Department is hereby granting your request for issuance of a TAA.

Along with your letter, you have provided the following documents: (1) a Partnership Agreement between the parties involved; (2) Articles of Incorporation for the occupant of the property in question; (3) an Occupancy Agreement between the owner of the property and the occupant of the property; and (4) the Master Loan Agreement related to the property in question.

ISSUE

Is Florida sales tax due in a commercial lease arrangement involving related parties, wherein it is alleged that no

consideration flows directly from the occupant of the property to the owner of the property where both the occupant and owner record adjustments for rent under Internal Revenue Code s. 482 and Treas. Regs. s. 1.482-1 for federal and state income tax purposes?

FACTS

Your letter provides in part:

* * *

> Applicant owns certain real property encumbered by mortgages. Applicant is responsible for the debt service payments to a commercial lender (hereinafter, "Bank"). Subject and Partners (and their spouses) have executed Guarantee Agreements with respect to the mortgages. Subject operates a multi-brand new and used retail car operation. Such operations are performed on Applicant's Premises.
>
> Applicant and Subject will enter into an Occupancy Agreement (the "Agreement") which grants Subject the right to use and occupy the Premises. The Agreement expressly states that Subject shall not be required to pay any rent to Applicant and shall not be required to pay any other consideration or compensation to or for the benefit of Applicant for the use and occupancy of the Premises. Applicant and Subject will, however, record adjustments for rent under Internal Revenue Code s. 482 and Treas. Regs. s. 1.482-1 for federal and state income tax purposes only.
>
> The Agreement calls for Subject to be liable for all costs that would be incurred to maintain the real property and improvements. The costs that will be incurred to maintain the real property and improvements include maintenance, repairs and utility charges. The Subject is also responsible for maintaining adequate insurance, agrees to indemnify the Applicant and hold it harmless from and satisfy and discharge any and all loss and liability of every kind whatsoever arising during the term of the Agreement. All payments made by Subject pursuant to the Agreement shall be paid directly by Subject to the appropriate third party payee. Subject shall not make any type of payment to Applicant under the Agreement, other than payments in the nature of indemnification or damages.
>
> The terms between Applicant, Subject, Partners, and Bank on the mortgaged property hold Applicant as primarily liable with Partners and Subject as secondarily liable in their capacity as guarantors. Partners will make capital contributions to Applicant as needed to fund Applicant's operating needs. As stated above, Applicant has no power to compel payment of any kind from Subject. Partners will determine independently whether to fund capital

> contributions to Applicant, and the amount of any such contributions.
>
> * * *

A review of the Occupancy Agreement indicates that the "owner" (a.k.a, the "Applicant") "... shall pay all real property taxes and assessments which may be levied or assessed ... against or upon the Premises." (Occupancy Agreement, para. 15) All alterations and improvements are to remain the property of the Applicant (Occupancy Agreement, para. 4) Failure by the Subject to perform any obligation under the Occupancy Agreement shall constitute default. (Occupancy Agreement, para. 19)

Based on a telephone conversation with your office, the Applicant is the entity which directly makes the mortgage payment to the lender.

TAXPAYER'S POSITION

Your letter provides in part:

> * * *
>
> It is Applicant's contention that a landlord and tenant relationship does not exist between Applicant and Subject since payment is not required for the use of the Premises. Applicant has not power to compel payment from Subject, with the exception of indemnification or damages as noted above.
>
> * * *
>
> Subject asserts that the ambiguities or doubts in the relevant tax laws governing this transaction should be resolved strongly in Subject's favor....
>
> * * *
>
> In the present instance, there is no payment due for the privilege of occupying the premises. Moreover, the privilege to use or occupy the real property is granted with only the condition that Subject assumes certain expenses of maintaining the property, none of which are payable to Applicant or a related party. Thus, there is no "rent or license fee charged" for such rental in accordance with s. 212.031(1)(c), F.S., nor can there be any "considerations due and payable by the tenant" for occupancy, as stated in Rule 12A-1.070(4)(b), F.A.C.
>
> * * *

In your letter, you cite to the following authority in support of your position: Seaboard Coastline Railroad Company v. Askew, #72-15 (Fla. Cir. Ct., 2nd Cir., Leon Co., 1972); Department of Revenue v. Ryder Systems, Inc., 406 So.2d 1299 (Fla. 1st DCA, 1981); and St. John's Trading Company, Inc. v. Department of Revenue, DOAH Case No. 84-1652 (1985). You also cite to a number of cases regarding the proper handling of ambiguities in Florida tax law (e.g., Maas Brothers, Inc. v. Dickinson, 195 So.2d 193 (Fla. 1967)).

APPLICABLE STATUTES AND RULES

Section 212.02, F.S., provides in part:

* * *

(2) "Business" means any activity engaged in by any person, or caused to be engaged in by him or her, with the object of private or public gain, benefit, or advantage, either direct or indirect....

* * *

(10) (i) "License," as used in this chapter with reference to the use of real property, means the granting of a privilege to use or occupy a building or a parcel of real property for any purpose.

* * *

(12) "Person" includes any individual, firm, copartnership, joint adventure, association, corporation, estate, trust, business trust, receiver, syndicate, or other group or combination acting as a unit and also includes any political subdivision, municipality, state agency, bureau, or department and includes the plural as well as the singular number.

* * *

Section 212.031, F.S., provides in part:

(1)(a) It is declared to be 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....

* * *

(c) 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....

* * *

(3) The tax imposed by this section shall be in addition to the total amount of the rental or license fee, shall be charged by the lessor or person receiving the rent or payment in and by a rental or license fee arrangement with the lessee or person paying the rental or license fee, and shall be due and payable at the time of the receipt of such rental or license fee payment by the lessor or other person who receives the rental or payment....

* * *

Rule 12A-1.070, F.A.C., provides in part:

* * *

(4)(b) The tax shall be paid at the rate of 5 percent prior to February 1, 1988, and 6 percent on or after February 1, 1988, on all considerations due and payable by the tenant or other person actually

occupying, using, or entitled to use any real property to his landlord or other person for the privilege of use, occupancy, or the right to use or occupy any real property for any purpose.

(c) Ad valorem taxes paid by the tenant or other person actually occupying, using, or entitled to use any real property to the lessor or any other person on behalf of the lessor, including transactions between affiliated entities, are taxable.

(d) Common area maintenance charges paid by a tenant to the lessor for the privilege or right to use or occupy real property are taxable.

(e) Utility charges paid by a tenant to the lessor for the privilege or right to use or occupy real property are taxable, unless the lessor has paid the sales tax to the utility company on such utilities consumed by the tenant, and the utilities billed by the lessor to the tenant are separately stated on the lessor's invoice to the tenant at the same or lower price as that billed by the utility company to the lessor.

* * *

(12) When a tenant or other person pays insurance for his own protection, the premium is not regarded as rental or license fee consideration, even though the landlord or other person granting the right to occupy or use such real property is also protected by the coverage. However, any portion of the premium which secures the protection of the landlord or person granting the right to occupy or use such real property and which is separately stated or itemized is regarded as rental or license fee consideration and is taxable.

* * *

(19)(a) The lease or rental of real property or a license fee arrangement to use or occupy real property between related "persons," as defined in s. 212.02(12), F.S., in the capacity of lessor/lessee, is subject to tax.

(b) The total consideration, whether direct or indirect, payments or credits, or other consideration in kind, furnished by the lessee to the lessor is subject to tax despite any relationship between the lessor and the lessee.

(c) The total consideration furnished by the lessee to a related lessor for the occupation of real property or the use or entitlement to the use of real property owned by the related lessor is subject to tax, even though the amount of the consideration is equal to the amount of the consideration legally necessary to amortize a debt owned by the related lessor and secured by the real property occupied, or used, and even though the consideration is ultimately used to pay that debt.

* * *

DISCUSSION

The issue presented is whether Florida sales tax is due in a commercial lease arrangement involving related parties, wherein it is alleged that no consideration flows from the occupant of the property to the owner of the property but both the occupant and the owner of the property record adjustments for rent under Internal Revenue Code s. 482 and Treas. Regs. s. 1.482-1 for federal and state income tax purposes.

In Florida, the renting, leasing, letting, or granting a license for the use of any real property is subject to Florida sales tax. Sales tax is due on the rental consideration paid for the right to use or occupy commercial real property. *See* Rule 12A-1.070(4) and (19), F.A.C. Rental consideration also includes the payment of premiums on insurance which protects the landlord or person granting the right to occupy real property. *See* Rule 12A-1.070(12), F.A.C.

The lease or rental of real property between related "persons" is taxable. *See* Rule12A-1.070(19), F.A.C. "Person" is defined at Section 212.02(12), F.S., and includes all types of entities including individuals and corporations. A "landlord and tenant relationship":

> ... exists where one person occupies premises of another in subordination to other's title or rights and with his permission or consent." Black's Law Dictionary 790, 791 (5th ed. 1979).

All payments made on behalf of the owner of commercial real property that benefit the owner of the commercial real property are considered "rent consideration" and are therefore subject to Florida sales tax. *See* Rule 12A-1.070 (19)(b), F.A.C., and Seaboard Coastline Railroad Company v. Askew, #72-15 (Fla. Cir. Ct., 2nd Cir., Leon Co., 1972). (Rent consideration may be payable directly to the lessor or to some other person directed by the lessor.) Finally, there need not be a written lease in order for there to be a landlord/tenant relationship. *See* Regal Kitchens, Inc. v. Department of Revenue, 641 So.2d 158 (Fla. 1st DCA, 1994).

When a business decision is made to create separate legal entities for purposes of owning and occupying real property to achieve advantages such as preferred financing, tax advantage, risk control, insurance coverage, or the like, the formalities of such arrangements are recognized for purposes of imposing Florida sales tax on transactions between those separate legal entities. *See* Seaboard Coastline Railroad Company. Courts have held that parties are not free to "...disavow the existence of the corporation for the purpose of obtaining a tax advantage." Regal Kitchens, 641 So.2d at 163. The Regal Kitchens opinion also held that: "Those who seek the protection afforded by incorporation must also accept the burdens."

Id. Finally, the Regal Kitchens court held:

> Nothing in subsection 212.02(2) Florida Statutes (1989), suggests that the term "business" is limited to those who engage in regular course of dealing with different clients or customers. A person who rents a single duplex unit is engaged in business as is the owner of an apartment who rents thousands of units. Id.

Under the facts presented, there is a "landlord and tenant relationship" because the Subject is occupying the land of another person (i.e., the Applicant). The Subject is responsible (pursuant to the Occupancy Agreement) for providing alterations and improvements and for maintaining liability and property damage insurance for the benefit of the Applicant. Ad valorem taxes and mortgage payments are directly paid by the Applicant. The Subject is directly liable for utility charges.

No payments flow directly from the Subject to the Applicant, and no third parties are paid directly by the Subject (save for the insurance premiums) on behalf of the Applicant. However, the above obligations are not optional, but contractually obligated to be performed by the Subject and failure to perform by the Subject results in default. The above obligations benefit the Applicant and are for the use and occupancy of the property. Payments made by the Subject for alterations and improvements, and payments by the Subject for maintaining liability and property insurance are subject to Florida sales tax. Both the Subject and the Applicant record adjustments for rent under Internal Revenue Code s. 482 and Treas. Regs. s. 1.482-1 for federal and state income tax purposes.

CONCLUSION

The facts show that the owner of the property is exercising a taxable privilege and is charging for use of real property and consideration is due and payable by "the tenant or other person actually occupying, using, or entitled to use" to "his landlord or other person" for the privilege of use...." The amounts identified as rent by both the Subject and Applicant are subject to Florida sales tax under Section 212.031, F.S.

The amounts paid by Subject for alterations and improvements and the premiums paid by the Subject for insurance that protects the Applicant against liability and protects the Applicant against property damage are subject to Florida sales tax, because the Subject is responsible for these obligations for the benefit of the Applicant and the charge or responsibility for the insurance is separately stated within the Occupancy Agreement. *See* Rule 12A-1.070(12), F.A.C. Further, the amounts identified as rent by both the Subject and Applicant are subject to Florida sales tax under Section 212.031, F.S.

This response constitutes a Technical Assistance Advisement

under Section 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 Section 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,

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(850) 922-4714

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