



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Amended:	08/09/10	Bill No:	SB 1250
Tax:	Property	Author:	Ducheny
Related Bills:			

BILL SUMMARY

Related to the property tax exemption on possessory interests available to private contractors that develop and operate military housing projects, this bill would:

- Expand its provisions to include military housing projects for single, unaccompanied, or married service members without dependents.
- Exclude its provisions from applying to any individual units rented to an unaffiliated member of the general public, as defined, and require the private contractor to annually report to the assessor any units rented to such persons as well as be responsible for any property taxes on those particular units.

SUMMARY OF AMENDMENTS

Since the last analysis, the amendments specify that Section 107.4 does not apply to units rented to unaffiliated members of the general public, as defined. In addition, the amendments specify that any property taxes on such units would be the responsibility of the private contractor.

ANALYSIS

CURRENT LAW

Section 107.4 of the Revenue and Taxation Code provides that a private contractor's interest in rental military *family* housing is not subject to property taxation as a taxable possessory interest, provided certain requirements and conditions are met.

PROPOSED LAW

Property Type. This bill would amend Section 107.4 to delete the word “family” throughout its text. Thus, the exemption could also apply to the privatization of unaccompanied housing (i.e., housing for enlisted service members without dependents).

Property Tenants. This bill adds subdivision (b) to Section 107.4 to provide that this section does not apply to a military housing unit managed by a private contractor that is rented to a tenant who is an “unaffiliated member of the general public,” which is defined to mean “a person who is not a current member of the military.” It further provides that a housing unit that is rented to, or occupied by, a person employed as management or maintenance personnel for the military housing property is not to be considered a unit rented to an unaffiliated member of the general public.

Private Contractor: Reporting and Property Tax Responsibility. This bill adds Section 107.4(b)(2) to require the private contractor to annually notify the assessor by February 15 of any units that had been rented to unaffiliated members of the general public on January 1. Any property taxes levied on those units would be the responsibility of the private contractor.

In GENERAL

In certain instances a property tax assessment may be levied when a person or entity uses publicly-owned real property that, with respect to its public owner, is either immune or exempt from property taxation. These uses are commonly referred to as “taxable possessory interests” and are typically found where an individual or entity leases, rents or uses federal, state or local government property.

Revenue and Taxation Code Section 107 sets forth the three essential elements that must exist to find that a person’s or entity’s use of publicly-owned tax-exempt property rises to a level of a taxable possessory interest. The use must be independent, durable and exclusive of rights held by others in the property.

Section 107 defines “independent” to mean “the ability to exercise authority and exert control over the management or operation of the property or improvements, separate and apart from the policies, statutes, ordinances, rules, and regulations of the public owner of the property or improvements. A possession or use is independent if the possession or operation of the property is sufficiently autonomous¹ to constitute more than a mere agency.”

Property Tax Rule 20(c)(8), a regulation, additionally requires that a possessor derive a “private benefit” from the use of the property. “Private benefit” means “that the possessor has the opportunity to make a profit, or to use or be provided an amenity, or to pursue a private purpose in conjunction with its use of the possessory interest. The use should be of some private or economic benefit to the possessor that is not shared by the general public.”

Section 107.4 provides a possessory interest exemption for a private contractor’s interest in rental military *family* housing, by stating that the contractor’s interest in the property is not “independent” when certain criteria are met. Thus, if qualified, these interests will not be deemed to be a *taxable* possessory interest.

LEGISLATIVE HISTORY

In 2004, Senate Bill 451 (Ch. 853, Ducheny) added Section 107.4 to provide that a possession or use of land or improvements is *not* independent if that possession or use is pursuant to a contract, including, but not limited to, a long-term lease, for the private construction, renovation, rehabilitation, replacement, management, or maintenance of housing for active duty military personnel and their dependents, if specific criteria are met. An interest that is not independent fails to meet one of the three necessary elements for the interest to be subject to property tax. Thus, a private contractor’s interest in military housing meeting the eligibility criteria of Section 107.4 would be exempt from property tax.

In 2006, Senate Bill 1400 (Ch. 251, Kehoe) added subdivision (o) to Section 107.4 to define the phrase “military housing under military control” as a military base that “restricts public access to the military base.” SB 1400 clarified that privately-developed military housing not located on a military base does not qualify for the military housing possessory interest tax exemption. Shortly after enactment of Section 107.4, concern arose that the statute might not adequately define the term “military housing under

¹Property Tax Rule 20(c)(5) specifies that “[t]o be ‘sufficiently autonomous’ to constitute more than a mere agency, the possessor must have the right and ability to exercise significant authority and control over the management or operation of the real property, separate and apart from the policies, statutes, ordinances, rules, and regulations of the public owner of the real property.”

military control," and that more expansive interpretations of the military housing possessory interest exemption might be advanced by developers of off-base military housing. The definition refinement was made to avoid an interpretation that Section 107.4 exempts all privatized military housing from the possessory interest tax by creating the bright line test of restricted public access. San Diego County sponsored the legislation because they have a number of privatized military housing projects, some of which are eligible for exemption and others which are not.

Last year AB 1332 (Salas) would have also expanded the exemption available to private contractors that operate military family housing projects to those that operate housing projects for single enlisted service members. In addition, it would have also refined and expanded upon the requirement that the property tax savings from the exemption inure solely to the benefit of the residents of the military housing projects. Furthermore, it would have detailed the documentation and information that the assessor may request from the private contractor to administer the exemption. This San Diego County sponsored bill was held in Assembly Appropriations.

Also in 2009, AB 1344 (Fletcher) would have expanded the taxable possessory interest property tax exemption available to private contractors that operate military family housing projects to those that operate housing projects for single enlisted service members. It would have also modified various provisions that require that the property tax savings from the exemption extended to the private contractor to inure solely to the benefit of the residents of the military housing projects. That bill was held in the Assembly Revenue and Taxation Committee.

BACKGROUND

Congress established the Military Housing Privatization Initiative (MHPI) in 1996 as a tool to help the military improve the quality of life for its service members by upgrading the condition of their housing. The MHPI was designed and developed to attract private sector financing, expertise and innovation to provide necessary housing faster and more efficiently than traditional military construction processes would allow. The military enters into agreements with private developers selected in a competitive process to own, maintain and operate family housing via a fifty-year lease. The Department of Defense maintains an extensive website on the [MHPI program](#).

In 2003, Congress authorized the Department of the Navy to undertake up to three pilot projects for the privatization of unaccompanied housing. The various services call unaccompanied housing by different names, such as bachelor enlisted quarters, barracks and dormitories. The Navy selected Clark Pinnacle to redevelop Naval Station San Diego as part of the first large-scale public-private venture to provide housing for single military personnel. The Clark Pinnacle proposal was selected through competitive bidding. Clark Pinnacle is a partnership between Clark Realty Capital, a real estate and construction company headquartered in Bethesda, Md., and Pinnacle, a real estate investment management firm headquartered in Seattle. Construction broke ground in January 2007 and was substantially completed in March 2009.

The first pilot project, Pacific Beacon LLC, privatized 258 units of Navy-owned unaccompanied housing units (Palmer Hall) and provides for the construction of 941 apartments at Naval Station San Diego (Pacific Beacon). The LLC owns, operates, and manages the project for 50 years.

A March 26, 2009, press release states: “The Department of the Navy and Clark Realty Capital celebrated the grand opening of Pacific Beacon today at Naval Base San Diego. As the nation’s first large-scale privatized housing community for unaccompanied military personnel, Pacific Beacon sets a new tradition in excellence by offering luxury living to single service members stationed in the San Diego metro area. The three luxury high-rise residences will serve as home to over 1,800 unaccompanied service members stationed in the San Diego metro area. Developed through a public-private venture between the Department of the Navy and Clark Realty Capital, Pacific Beacon opened its first building to residents in December of 2008. The entire project achieved substantial completion on March 12, 2009. The community constructed by Clark Construction Group and Clark Builders Group features 941 dual master suites and unique, resort-style amenities that rival any luxury high-rise apartment building in San Diego. The units are all priced at or below the Basic Allowance for Housing (BAH) rates of qualified residents.” www.pacificbeacon.com

COMMENTS

1. **Sponsor and Purpose.** This bill is sponsored by San Diego County “to allow military housing (both single and family) provided under a long-term lease held by a private contractor to be exempt from possessory interest classification for annual property tax assessments if the tax savings from the housing projects are applied towards improvements for the housing residents above and beyond the contract requirements.”
2. **Amendments.** The **August 9, 2010** amendments (1) specify that Section 107.4 does not apply to units rented to unaffiliated members of the general public, as defined; (2) specify that any property taxes on such units would be the responsibility of the private contractor and (3) delete the June 2 amendment adding the word “solely” -- that the housing be used “solely” for active duty personnel or their dependents. The amendments relating to unaffiliated members were made to address concerns expressed by the Senate Appropriations Committee that the property tax exemption provided by this bill should not apply to individual units being rented out to the general public in the event that there is insufficient rental demand from members of the military. The word “solely” was deleted due to concerns from the private contractor that some units are occupied by its employees who manage and maintain the housing project such as the leasing manager, etc. which might make the project ineligible for the exemption. The **June 2, 2010** amendments deleted provisions making this bill retroactive. This amendment was made because Section 107.4 is no longer necessary in order to exempt the Pacific Beacon project from the property tax as a result of a recent legal opinion on the project issued by the Board’s legal department. The June 2 amendments also specified that the possessory interest exemption for military housing set forth in Section 107.4 must be *solely* for active duty military personnel and their dependents.
3. **Pacific Beacon.** To date, Pacific Beacon is the only privatized housing for unaccompanied service members located in California. Board legal staff has opined that the private contractor in this project does not have a taxable possessory interest under Section 107, which is the general taxable possessory interest statute. It was determined that the contractor’s interest in this particular case is not independent because the contractor is serving as an agent of the government. Thus, the amendments made by this bill to Section 107.4, which is the possessory interest statute explicitly related to military housing projects, are not needed to exempt this particular project from the property tax.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board’s formal position.

4. **Supporters note that the need for affordable quality military housing exists for all military service men and women regardless of whether they have a family.** By removing the designation of “family” housing, any housing project for military service members that otherwise qualifies under Section 107.4 would benefit from the possessory interest tax exemption.

COST ESTIMATE

The Board would incur insignificant costs (less than \$10,000) to inform and advise county assessors, the public, and staff of the change in law.

REVENUE ESTIMATE

This bill does not have a revenue impact since the Pacific Beacon project is not subject to the property tax under existing law. To date, the Pacific Beacon is the only privatized housing for unaccompanied service members located in California. Depending on the success of the pilot unaccompanied housing privatization projects, Congress may decide to authorize the privatization of other unaccompanied housing quarters as well. We are not aware of any other projects on the horizon – but should there be such a project in the future (that is not structured like the fact pattern in this particular project) then this bill might have some future, unknown revenue impact.

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