

SC PRIVATE LETTER RULING #04-6

SUBJECT: Personal Property Leased to the Federal Government
(Property Tax)

REFERENCES: S. C. Code Ann. Section 12-37-710 (2000)
S. C. Code Ann. Section 12-37-900 (2000)
S. C. Revenue Ruling #93-11

AUTHORITY: S. C. Code Ann. Section 12-4-320 (2000)
S. C. Code Ann. Section 1-23-10(4) (Supp. 2002)
SC Revenue Procedure #03-01

SCOPE: A Private Letter Ruling is a written statement issued to a specific taxpayer by the Department to apply principles of law to a specific set of facts or a particular tax situation. **A Private Letter Ruling does not have the force and effect of law, and is not binding on the person who requested it or the public.** It is, however, the Department's opinion limited to the specific facts set forth, and is binding on agency personnel only with respect to the person to whom it was issued and only until superseded or modified by a change in statute, regulation, court decision, or advisory ruling, providing the representations made in the request reflect an accurate statement of the material facts and the transaction was carried out as proposed.

Question:

Is the personal property leased to the federal government by XYZ, LLC ("Lessor") through a "lease to own" plan, as described in the facts, subject to property taxes in South Carolina?

Conclusion:

Based on the facts given below, the personal property leased to the federal government by the Lessor through a "lease to own" plan, is not subject to property taxes in South Carolina.

Facts:

XYZ, LLC (“Lessor”) is a lessor of tangible personal property consisting of computer equipment. Lessor leases this personal property to the federal government and agencies of the federal government pursuant to the federal Lease to Ownership Plan (“LTOP”). The most significant feature of the lease agreement is that after the required lease payments have been made, title to the property automatically transfers to the federal government at the end of the lease term. During the term of the lease, the legal title to the property is held by the Lessor for security purposes although the federal government is responsible for maintaining the equipment in good condition and working order.

For federal income tax purposes, the Lessor records the lease transaction as a sale and does not depreciate the personal property for income tax purposes. The lease payments are reported as interest income and return of principal by the Lessor. Under this lease agreement, the federal government is properly treated as the income tax owner of the equipment. At the end of the lease term, title to the property is transferred to the federal government.

Discussion:

Generally, the business who has title to personal property lists the property for taxation, files property tax returns and pays the property tax for such property. See, Code Section 12-37-710. However, in South Carolina Revenue Ruling #93-11, the Department determined that the liability for the property taxes imposed upon leased property runs to the lessee if the lease is a financing arrangement for income tax purposes whereby the lessee is treated as the owner of the property.¹ In this instance, the Lessor is not treated as the owner of the property for income tax purposes. The transaction is treated as a conditional sale by the Lessor to the federal government. Since the LTOP agreement in question is a financing lease where the property is treated as owned by the federal government for income tax purposes, the property is considered owned by the federal government for property tax purposes as well.

It is well established that the United States and its agencies, instrumentalities, and property are immune from state and local taxation pursuant to the doctrine of sovereign immunity. *McCullough v. State of Maryland*, 17 U.S. (4 Wheat.) 316 (1819). At the same time, it is equally well settled that this constitutional immunity does not protect a private party that does business with the United States from a state tax that is imposed on the private party merely because part or all of the tax eventually falls on the United States. *Alabama v. King & Boozer*, 314 U.S. 1 (1941). This principle was upheld in *United States v. New Mexico*, 455 U.S. 720 (1982) in which several taxes imposed by New Mexico on contractors doing

¹For real property, SC Revenue Ruling #93-11 is no longer applicable, as Code Section 12-37-610 now provides that for real property, the person who has title to the property must pay the ad valorem property taxes on such property. However, SC Revenue Ruling #93-11 is still applicable to personal property.

business with the federal government were found not to violate the Supremacy Clause of the Constitution and in *Washington v. United States*, 460 U.S 536 (1983) which held similarly. Thus whether the property is subject to South Carolina property tax turns on whether the tax is actually assessed against the United States or its property or whether it is assessed against a private party doing business with the federal government.

In *United States v. Allegheny County*, 322 U.S. 174 (1944), the United States Supreme Court held that machines owned by the United States and leased to a private party who used the machines to manufacture guns for the government were immune from state property taxation. The Court determined that the scheme of taxation used by Pennsylvania was nothing more than the widely used ad valorem property tax which imposed the tax on the property itself. The Court held "... that Government-owned property, to the full extent of the Government's interest therein, is immune from taxation, either as against the Government itself or against one who holds it as bailee." 322 U.S. at 189.

In this instance, while the federal government is not the technical title owner of the property, it is treated as the owner of the property for South Carolina property tax purposes. The tax imposed is an ad valorem tax on the property so any tax assessed would be assessed to the federal government.² However, the principles of *McCullough v. Maryland*, supra, and *United States vs. Allegheny County*, supra, do not allow the tax to apply to the property of the federal government. Therefore, the personal property that is leased by Lessor to the federal government under a financing lease is not subject to property taxes in South Carolina.

SOUTH CAROLINA DEPARTMENT OF REVENUE

s/Burnet R. Maybank III
Burnet R. Maybank, III, Director

November 1, 2004
Columbia, South Carolina

²Note that if this were a lease where the Lessor did properly depreciate the personal property for income tax purposes, the Lessor would be treated as the owner of the property and would be subject to ad valorem property taxes on the property.