LEGAL ALERT

PA Supreme Court Rules that Real Estate Interests Must Be Valued as Whole for Taxation

April 30, 2012 – Late last week the PA Supreme Court settled a long-simmering debate in Pennsylvania as to how to value real estate that is leased. In its opinion in Tech One Associates v. Board of Property Assessment Review and Appeals of Allegheny County, 32 WAP 2010 (2012), the Court ruled that both the leased fee (landlord's position) and the leasehold (tenant's position) must be valued in order to achieve constitutional uniformity of taxation. Thus, in order to assess a leased property, both the leased fee interest (value to the landlord), and the leasehold interest (value to the tenant) must be determined. Once these values are determined, the two interests are to be merged for assessment purposes.

Previously, Pennsylvania's lower courts interpreted the Supreme Court's 1992 decision in Marple Springfield to mean that, for leased real estate, just the leased fee interest should be valued for tax assessment purposes. Last week's decision clarifies that the market value of the whole must be determined, and that, "in conducting this valuation, the impact of the lease on the market value of the real estate owned as the leased fee and, also, on the market value of the real estate owned as a leasehold interest must be considered."

In Tech One, the landowner leased land to a developer for fifty years at a flat $660,000 per year for the entire 50-year term. The developer then a constructed a large strip-style shopping center on the site.

At trial, the landowner argued that only the landlord's interest, the leased fee, should be valued and introduced evidence that the leased fee value was $9 Million. The landowner argued that it did not own the buildings and received no income from the buildings, and, thus, under the Marple Springfield decision, the "economic reality" was that it should only be taxed on the real estate income it received under the lease. While the taxing districts agreed that the leased fee value was about $9 Million, they argued that both land and buildings are subject to taxation and just because different parties own them is an insufficient basis to tax them differently. Accordingly, the taxing districts entered evidence of both the leased fee and the leasehold interests, and argued that the aggregate of those interests – approximately $25 Million – was the correct assessment for the property.

The Supreme Court agreed that for leased real estate, both the leased fee and leasehold interests must be valued. To rule otherwise, the Court held, would be to allow a situation where a tenant under a long-term lease "could build a Taj Mahal and the structure would be wholly exempt from taxation merely because it was owned as a leasehold." Rather, the Court decided, the market value of the real estate must include both the leased fee and leasehold interests to achieve uniformity of taxation.

Sharon F. DiPaolo, Esquire
J. Kieran Jennings, Esquire
Siegel, Siegel, Johnson & Jennings, Co., L.P.A.
2912 Wildwood Road Extension
Pittsburgh, PA 15101
(412) 486-2848 (office)
(412) 486-2858 (fax)
sdipaolo@siegeltax.com