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Honorable Don Davis
Mobile County Probate Judge
109 Government Street
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Recordation Tax – Leases – Probate Judges
– Renewals

Lease extension options classified as automatic and automatic extensions that include the provision allowing either party the option of nonrenewal should be included in the calculation of the total consideration of the lease and taxed at the time of recordation.

When a memorandum of lease states that the lease will automatically renew for five-year terms without stating the total number of five-year term renewals, the lease may be extended to the maximum years allowed by law unless the terms of the lease state otherwise.

When a renewal option on a previously recorded memorandum of lease is being exercised and subsequently recorded, the lease consideration amount of the extension should be taxed at the rate stated in the instrument and taxed at the present value.

Exercising a nonrenewal clause before the end of the lease period is not a mistake authorizing a refund for taxes paid on automatic renewals.

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Dear Judge Davis:

This opinion of the Attorney General is issued in response to your request.

QUESTIONS

(1) Should lease extension options classified as “automatic” in the memorandum-of-lease instrument be included in the calculation of the total consideration of the lease and taxed at the time of recordation?

(2) Should automatic extensions that include the provision allowing either party the option of nonrenewal be included in the calculation of total consideration of the lease and taxed at the time of recordation?

(3) When a memorandum of lease states that the lease will automatically renew for five-year terms without stating the total number of five-year term renewals, should the lease be extended to the maximum years allowed by law?

(4) When a renewal option on a previously recorded memorandum of lease is being exercised and subsequently recorded, should the lease consideration amount of the extension be discounted to present value and taxed at the discounted rate, or should it be taxed at 100 percent of its value?

(5) If your opinion is that the automatic extensions of the lease should be included in the calculation of total consideration of the lease and taxed at the time of the initial recordation, does the taxpayer possess the right to a refund of the taxes paid that are attributable to the renewal terms in the event the lease terminates at the 25-year initial period of the leasehold?

FACTS AND ANALYSIS

These questions arise out of a document entitled Memorandum of Lease presented for recordation to your office between Evonik Corporation and Bayer CropScience LP. The effective date of the lease is April 1, 2015. The party attempting to record the document paid recordation tax with two separate checks. The taxpayer tendered one check in the amount of \$20,816.50 for payment of a 25-year lease and a second check was paid in protest in the amount of \$93,312.50. Upon receipt of the document and payment of tax, the probate court recorded the instrument and requested an opinion in response to the above-mentioned questions.

Section 40-22-1(a) of the Code of Alabama states, in pertinent part, as follows:

. . . [N]o deed, bill of sale, or other instrument of like character which conveys any real or personal property within this state or which conveys any interest in any such property shall be received for record unless the privilege or license tax is paid prior to the instrument being offered for record

ALA. CODE § 40-22-1(a) (Supp. 2015).

Under Alabama law, recordation tax is imposed on instruments offered for recording such as leases that convey an interest in property. Additionally, tax is due upon the recordation of a lease based upon the value of the interest in the property conveyed. Opinion to Honorable Bobby Day, Morgan County Judge of Probate, dated July 19, 1994, A.G. No. 94-00241. The *Day* opinion further stated that “option periods which are to be renewed automatically are tantamount to a lease term that includes any and all such option periods. Therefore, recording tax should be computed on the fixed term of a lease, plus the terms of options to renew, if renewal of the lease is automatic.” *Id.* at 2-3 (emphasis in original).

Regarding your second question, the *Day* opinion also addressed the similar issue of a provision allowing termination prior to the end of the full lease term. In concluding that tax was due on the entire term, that opinion reasoned as follows:

The [full] term is the better indication of the value of the interest conveyed by the lease, since it represents the parties’ negotiations and perceptions of that value. In fact, the lessee may choose not to terminate the lease; instead, he may continue the lease through its

full term. Accordingly, the *mere possibility of termination by a lessee is of no consequence.*

Id. at 2 (emphasis added). The same consideration is present here. Accordingly, even though the automatic extensions include the option not to renew, they should be included in the calculation of the total consideration of the lease and taxed at the time of recordation.

Regarding your third question, as stated above, option periods that are renewed automatically are tantamount to a lease term that includes any and all such option periods. Therefore, when a memorandum of lease states that the lease will automatically renew for five-year terms without stating the total number of five-year term renewals, the interest in the property will be conveyed every five years after the end of the original period in the lease. If the lease provides that the interest in the property is automatically conveyed every five years without any other terms to the contrary, it is proper to tax the lease based on the extension of the five-year periods to the maximum years allowed by law. The parties to the lease control the language of the lease. Therefore, the parties can control the amount of recordation tax due by explicitly stating the number of renewal periods and length of the periods.

Regarding your fourth question, leases offered for recordation state the length of time, including options for renewal and the consideration exchanged. The *Day* opinion also reasoned that “the recording tax should be assessed on a leasehold interest, based upon the present value of the consideration exchanged during the term of the lease.” *Id.* at 2. Consequently, when a renewal option on a previously recorded memorandum of lease is being exercised and subsequently recorded, the lease consideration amount of the extension should be taxed at the rate stated in the instrument and taxed at the present value.

Regarding your fifth question, the party offering the instrument for recordation may petition for a refund of the recordation tax overpaid by “*mistake* of fact or law.” ALA. CODE § 40-12-23(a) (2011) (emphasis added). The petition must be made within two years from the date of payment of the tax. ALA. CODE § 40-12-23(b) (2011); ALA. CODE § 40-2A-7(c)(2) (Supp. 2015) As stated above, the amount of tax is determined at the time of recordation by the terms the parties place in the instrument offered for recordation. The later exercise of a clause the parties included in a lease is not a mistake affecting the earlier payment of tax. Tax is correctly calculated based on automatic renewal options in the lease, even if the lease period is never actually renewed.

CONCLUSION

Lease extension options classified as automatic and automatic extensions that include the provision allowing either party the option of nonrenewal should be included in the calculation of the total consideration of the lease and taxed at the time of recordation.

When a memorandum of lease states that the lease will automatically renew for five-year terms without stating the total number of five-year term renewals, the lease may be extended to the maximum years allowed by law unless the terms of the lease state otherwise.

When a renewal option on a previously recorded memorandum of lease is being exercised and subsequently recorded, the lease consideration amount of the extension should be taxed at the rate stated in the instrument and taxed at the present value.

Exercising a nonrenewal clause before the end of the lease period is not a mistake authorizing a refund for taxes paid on automatic renewals.

I hope this opinion answers your questions. If this Office can be of further assistance, please contact W. William Young, Legal Division, Department of Revenue.

Sincerely,

LUTHER STRANGE

Attorney General

By:



G. WARD BEESON, III

Chief, Opinions Section

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