

# **Class 9 Treatment:**

Property Leased to Charter Schools  
and Religious Organizations

Presented August 31, 2015 by Brad Tebow

# Some Statutory Requirements

- Non-Profit Use
- Tenant is a Charter School or Religious Organization
- Used for Education or Religious Worship

# More Statutory Requirements

- Leased for entire Valuation Year
- Used Exclusively by the Charter School or Church
- Affidavits are required; **Assessor may require additional evidence**
- Reduction in property tax goes exclusively to the Charter School or Religious Organization
- The rent must be at Market or consistent with other rents at the property

# What Types of Property Might Qualify?



# Neighborhood Shopping Center



# Strip Retail Center (100% CL 1)



# Business Park



# Single-Family Residence?



# Starting a Church

(common for start-up Churches)

- Incorporate as an Arizona Non-Profit Corporation
- Regularly Scheduled Discussion Groups in a Home
- Expand with Discussion Groups and/or Worship Services in a restaurant, school, or community room
- Rent a space for a Sanctuary, Meeting Rooms, and Offices
- Raise Building Funds, Purchase Property

# Verification

- Is the School / Church Tenant the sole beneficiary?
- Is the Tenant's rent at Market or Consistent with other rents at the property?



# Sole Beneficiary of Class 9

- Excerpted from ARS Section 42-12009(A)(5): the school/church tenant “shall be the sole beneficiary of the change in property tax classification.”
- Leases Where the Entire Parcel is Class 9
  - Gross lease where property tax is included in base rent
  - Net lease where the Tenant reimburses property tax
- Leases in a Mixed Ratio Parcel
  - Gross lease where property tax is included in base rent
  - Net lease where Tenants reimburse property tax

# “Triple Net” Lease



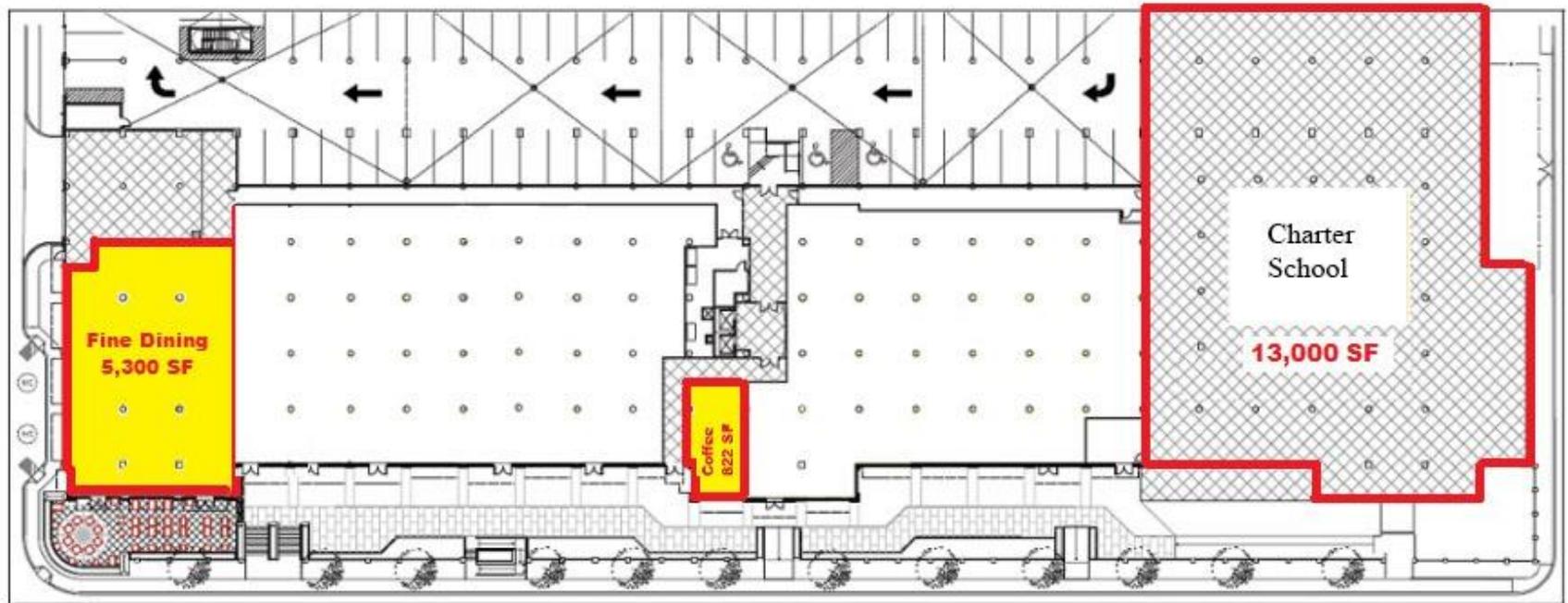
- Operating Expenses, such as property taxes, are reimbursed by tenants as additional rent on a pro-rata basis.
- Estimated monthly payments of additional rent are impounded by Landlord.
- After the end of the lease year, Landlord gives Tenant an accounting of actual expenses versus the impound collected. Any shortfalls are collected and any overages are refunded.

# Management Challenge

- Multi-tenant properties where tenants reimburse operating expenses present a challenge to owners in complying with
- Do all tenants share in any decreases in property tax under the existing leases?

# Leasing Plan: Assessor Village Shops

Charter School	13,000 SF	30.6%
Shops	29,480 SF	69.4%
Total	42,480 SF	100.0%



# Example: Assessor Village Shops Multi-Tenant Retail

- Charter School leases 13,000 sf (30.6%) on 7/1/2014
- 2015 Property Tax: \$85,000 (\$2/sf for 42,480 sf)
- Land 100% CL 1; Imps. 100% CL 1; Ratio = 18.5%
- Landlord and School apply to Assessor for Class 9 for 2015 valuation year; Assessor changes 30% to Class 9
- 2016 Property Tax: \$63,963 (\$1.51/sf for 42,480 sf)
- Land 70% CL1, 30% CL9; Imps. 70% CL1, 30% CL9
- Mixed Ratio = 12.9%

# Example: School's Pro-Rata Share

- Typical Proration in a Net Lease
  - 2015 Property Tax – 100% Class 1 for Land and Imps.
    - $\$85,000 \times 30.6\% = \$26,010$  ( $\$2.00/\text{sf}$  for 13,000 sf)
  - 2016 Property Tax – Mixed Ratio 12.9%
    - $\$63,963 \times 30.6\% = \$19,573$  ( $\$1.51/\text{sf}$  for 13,000 sf)
- Under the typical, shopping-center lease, the 2016 Property Tax would be applied to **ALL** tenants in Assessor Village at  $\$1.51/\text{sf}$ .

# Compliant Owner must separately compute tax for Class 1 and Class 9 Tenants

## Calculate Property Tax for Class 1 Portion (70%)

2016 Limited Property Value	\$4,060,881
Times Ratio 18%	<u>0.18</u>
Assessed LPV	\$ 730,959
Times aggregate Tax Rate	<u>0.1221</u>
Sub-total	\$ 89,250
Times Proportionate Share of Center (70%)	<u>0.70</u>
Property Tax owed by Class 1 Shops	\$ 62,475

## Calculate Property Tax for Class 9 Portion (30%)

2016 Limited Property Value	\$4,060,881
Times Ratio 1%	<u>0.01</u>
Assessed LPV	\$ 40,609
Times aggregate Tax Rate	<u>0.1221</u>
Sub-total	\$ 4,958
Times Proportionate Share of Center (30%)	<u>0.30</u>
Property Tax owed by Class 9 School	\$ 1,488

# Allocation of the Property Tax for Tenant Reimbursement

- School's share of property tax is \$1,488 or \$0.12/sf for 13,000 sf
- Total share for the shops is \$62,475 or \$2.12/sf for 29,480 sf
- This insures that the benefit of Class 9 goes to the School

# Application of “Sole Beneficiary” Clause

- In a multi-tenant property, verification of landlord’s compliance has two facets:
  - Verify that the school/church tenant is the sole beneficiary and
  - Verify that no other tenants or owner benefit from the property class change.

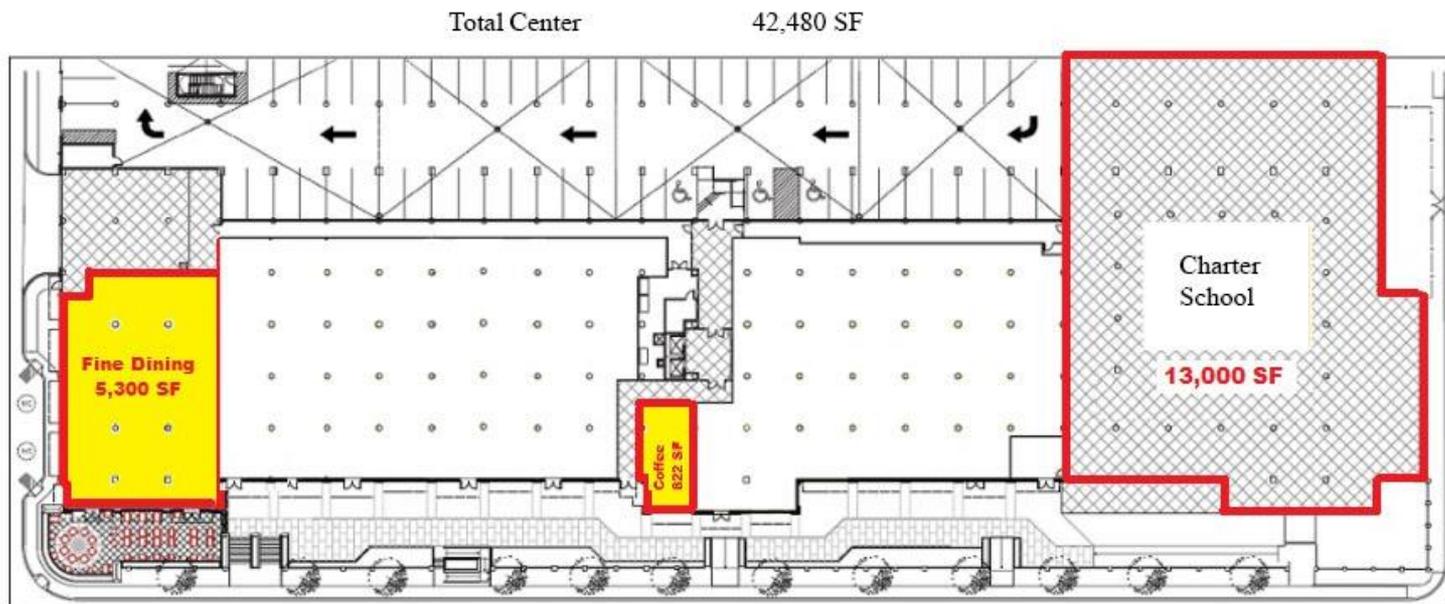
# Is the Rent too high?

- ARS § 42-12009(A)(5) “. . . the lease rate that is charged . . . is consistent with the lease rates that are charged to other tenants of the property or a fair market rate.”
- Might an Owner receive some of the tax savings by increasing the Rent?
- Might an unwilling Owner be induced to apply for Class 9 if the Tenant agrees to an increase in the Rent?



# Valuation Issues

- Example: Assessor Village Center
  - Since the Mixed Ratio is computed based upon value, should the 13,000 sf school space receive a different value per square foot than the remaining shop space?



THE END.....

- Good Bye.