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Memorandum

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to:

(Chief Counsel)

from:

(Income Tax & Accounting)

subject: Real Property Tax Deduction for Fire Prevention Fees

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent

ISSUE

May California residents deduct the Fire Prevention Fee they may pay on their federal income tax returns as a real property tax deduction under section 164 of the Internal Revenue Code and § 1.164-4 of the Income Tax Regulations?

CONCLUSION

California residents may not deduct the Fire Prevention Fee as a real property tax deduction because (i) the fee is not a tax under California or federal law (ii) the fee is not levied at a like rate, (iii) the fee is not imposed throughout the taxing authority's jurisdiction, and (iv) the fee is assessed only against specific property to provide a local benefit.

FACTS

In 2011, California enacted legislation requiring the State Board of Equalization to charge an amount not to exceed \$150 as a fire prevention fee (the fire fee) on each

structure within a state responsibility area. Cal. Pub. Res. Code § 4212(a)(1). A state responsibility area is an area of the state “in which the financial responsibility of preventing and suppressing fires has been determined by the [Board of Forestry and Fire Protection]... to be primarily the responsibility of the state.” Cal. Pub. Res. Code § 4102. The legislature gave the following reasons for enacting the legislation:

(a) Fire protection of the public trust resources on lands in the state responsibility areas remains a vital interest to California. Lands that are covered in whole or in part by a diverse plant community prevent excessive erosion, retard runoff, reduce sedimentation, and accelerate water percolation to assist in the maintenance of critical sources of water for environmental, irrigation, domestic, or industrial uses.

(b) The presence of structures within state responsibility areas can pose an increased risk of fire ignition and an increased potential for fire damage within the state’s wildlands and watersheds. The presence of structures within state responsibility areas can also impair wild land firefighting techniques and could result in greater damage to state lands caused by wildfires.

(c) The costs of fire prevention activities aimed at reducing the effects of structures in state responsibility areas should be borne by the owners of these structures.

(d) Individual owners of structures within state responsibility areas receive a disproportionately larger benefit from fire prevention activities than that realized by the state’s citizens generally.

(e) It is the intent of the Legislature that the economic burden of fire prevention activities that are associated with structures in state responsibility areas shall be equitably distributed among the citizens of the state who generally benefit from those activities and those owners of structures in the state responsibility areas who receive a specific benefit other than that general benefit.

(f) It is necessary to impose a fire prevention fee to pay for fire prevention activities in the state responsibility areas that specifically benefit owners of structures in the state responsibility areas.

Cal. Pub. Res. Code § 4210.

The legislation requires the State Department of Forestry and Fire Prevention to submit the names and addresses of those liable for the fee, and the amount of the fee, within 30 days of the legislation’s effective date and each January 1 thereafter. Cal. Pub. Res. Code § 4213(c). It empowers the State Board of Equalization to collect the fee pursuant to the Fee Collection Procedures Law in Part 30 of Division 2 of the California Revenue and Taxation Code. Cal. Pub. Res. Code § 4213(a)(1). The legislation requires an

appeals process separate and distinct from that in the Fee Collection Procedures Law in which the Department of Forestry and Fire Prevention, not the State Board of Equalization, determines whether the feepayer is liable for the fee. Cal. Pub. Res. Code §§ 4213(2), 4220. Thus, a feepayer may not file a petition for redetermination of the fee with the State Board under the Fee Collection Procedures Law as the feepayer might for other fees.

LAW AND ANALYSIS

Section 164(a)(1) of the Internal Revenue Code (“Code”) permits a deduction for real property taxes, but does not define what constitutes a real property tax. Personal property taxes may also be deductible under § 164(a), but § 164(b)(1) requires a personal property tax be an ad valorem tax to be deductible. The Code does not explicitly require the same for real property taxes. Section 1.164-4(a) of the Income Tax Regulations explains that to be deductible, a real property tax must be levied for the general public welfare at a like rate against all real property in the taxing authority’s jurisdiction. In general, an amount that is assessed only on specific property benefitted by a local benefit (such as for streets, sidewalks, and like improvements) cannot be deducted as a real property tax.

Revenue Ruling 80-121, 1980-1 C.B. 43, notes that a characteristic common to many real property taxes is that the tax is measured by the value of the real property. However, there is no statutory or regulatory requirement that a real property tax be an ad valorem tax to be deductible for federal income tax purposes. Assessments on real property owners, based other than on the assessed value of the property, may be deductible if they are levied for the general public welfare by a proper taxing authority at a like rate on owners of all properties in the taxing authority’s jurisdiction, and if the assessments are not for local benefits (unless for maintenance, repair, or interest charges).

The fire fee does not qualify as a deductible real property tax under the Code and the regulations. First, the fire fee is not a tax under California or federal law:

A tax is an enforced contribution, exacted pursuant to legislative authority in the exercise of the taxing power, and imposed and collected for the purpose of raising revenue to be used for public or governmental purposes. Taxes are not payments for some special privilege granted or service rendered and are, therefore, distinguishable from various other charges imposed for particular purposes under particular powers or functions of government.

Rev. Rul. 77-29, 197-1 C.B. 44 citing Rev. Rul. 61-152, 1961-2 C.B. 42 and Rev. Rul. 71-49, 1971-1 C.B. 103; see also Rev. Rul. 58-141, 1958-1 C.B. 101.

Article 13A, § 3(a) of the California Constitution requires a two-thirds vote of both houses of the California legislature to raise taxes, and it forbids new ad valorem taxes and sales or transactions taxes on real property. Regulatory fees require only a simple majority to be enacted into law. California Farm Bureau Federation v. State Water Resources Control Bd., 51 Cal. 4th 421, 428 (Cal. 2011). The bill enacting the fire fee into law, Assembly Bill 29 in the 2011-2012 session of the legislature, did not pass with a two-thirds vote.¹ Thus, the fire fee only has force of law as a regulatory fee.

Article 13A, § 3(b)(1) states that a tax does not include “a charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the State of conferring the benefit or granting the privilege to the payor.” The charge § 3(b)(1) refers to is a regulatory fee. In California, “a fee may be charged by a government entity so long as it does not exceed the reasonable cost of providing services necessary to regulate the activity for which the fee is charged.” Id. at 437, citing Sinclair Paint Co. v. State Bd. of Equalization, 15 Cal. 4th 866, 876 (Cal. 1997). Regulatory fees are imposed under the police power, rather than the taxing power. Id. at 875. The fire fee was imposed to “to pay for fire prevention activities in the state responsibility areas that specifically benefit owners of structures in the state responsibility areas.” Cal. Pub. Res. Code § 4210. It was not imposed to collect revenue for general governmental purposes, but to provide the specific benefit of fire prevention for certain structures in the state. It is thus a regulatory fee, like the fees assessed on manufacturers and other persons contributing to environmental lead contamination that the Supreme Court of California in Sinclair ruled were regulatory fees. Sinclair Paint Co., supra at 874-875.

Regulatory fees in California are also collected according to a different procedure than are taxes. Ad valorem real property taxes are collected under the provisions of Part 5 of Division 1 of the Revenue and Tax Code, entitled Collection of Taxes. Mello-Roos special taxes are collected under the same procedures. Cal. Gov. Code 53340(3).² But all fees charged in California under the state’s regulatory power, including the fire fee, are collected pursuant to the Fee Collection Procedures Law, Part 30 of Division 1 of the Revenue and Tax Code. See also Cal. Pub. Res. Code § 4213(a)(1); California Farm Bureau Federation, supra at 432 (fee collected according to Fee Collection Procedures Law). As noted above, the appeals process for the fire prevention fee is separate and distinct from that provided for in the Fee Collection Procedures Law, which further differentiates the fire fee from a tax. See Cal. Pub. Res. Code §§ 4213(2),

¹ The vote in the California Assembly was 52-26 in favor of the legislation and the vote in the California Senate was 23-16 (less than two-thirds voted for passage in the Senate). See http://www.leginfo.ca.gov/cgi-bin/postquery?bill_number=abx1_29&sess=PREV&house=B&author=blumenfield.

² “The special tax shall be collected in the same manner as ordinary ad valorem property taxes are collected and shall be subject to the same penalties and the same procedure, sale, and lien priority in case of delinquency as is provided for ad valorem taxes, unless another procedure has been authorized in the resolution of formation establishing the district and adopted by the legislative body.”

4220. The supermajority requirement and this disparate collection treatment for fees in California indicate that the fire fee is an ordinary regulatory fee rather than a tax.

Second, the fire fee is not levied at a like rate as § 1.164-4(a) requires. Although neither the Code nor the regulations define “like rate”, we believe that the term requires that the rate must uniformly apply based upon an independent variable, such as property value or parcel or structure size, to be considered similar or “like.” A charge of \$150 against each structure no matter how large or small is not levied at a “like” rate.

Third, the fire fee is not imposed against all real property throughout the taxing authority’s jurisdiction as § 1.164-4(a) requires. First, it is imposed only against real property containing structures, not all real property within the state. Second, it is imposed only within state responsibility areas as designated by the state Board of Forestry and Fire Prevention, not all real property throughout the taxing authority’s jurisdiction. These areas are geographically limited and do not cover the entire state of California or the entirety of the territory over which the appropriate taxing authority within the state has jurisdiction.

Fourth, the fire fee is assessed only against specific property to provide a local benefit. § 1.164-4(a) requires that a real property tax be levied for the general public welfare and not for a local benefit to be deductible. In its statement of findings, the California legislature stated that the presence of structures within state responsibility areas poses an increased risk of fire ignition and an increased potential for fire damage within the state’s wildlands and watersheds, and also impairs wild land firefighting techniques. Cal. Pub. Res. Code § 4210. It noted that “individual owners of structures within state responsibility areas receive a disproportionately larger benefit from fire prevention activities than that realized by the state’s citizens generally.” Id. It concluded that “[t]he costs of fire prevention activities aimed at reducing the effects of structures in state responsibility areas should be borne by the owners of these structures”. Id. Thus, the legislature decided that “[i]t is necessary to impose a fire prevention fee to pay for fire prevention activities in the state responsibility areas that specifically benefit owners of structures in the state responsibility areas.” Id. The legislature was explicit that the fee be levied against specific property to provide a distinctly local benefit to these properties within state responsibility areas. Thus, the fire fee fails the general public welfare requirement of § 1.164-4(a) and it is not a deductible real property tax.

I hope this information is helpful. If you have any questions, please contact me or
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