



# CITY OF TUCSON

## A GUIDE TO UNDERSTANDING BUSINESS TAXES AND LICENSES

### REAL PROPERTY RENTALS AND LEASES BROCHURE

*This brochure is intended to help entities leasing or renting real property understand the business privilege (sales) tax laws that apply to their business. This information is based on the City of Tucson Business Privilege Tax Code in effect on October 1, 2011. In case of inconsistency or omission, the Tucson Tax Code will prevail.*

#### ARE REAL PROPERTY RENTALS AND LEASES TAXABLE?

Generally, gross income from the business activity of leasing or renting *commercial real property* is taxable at the rate of 2%. The entity leasing or renting to the tenant in actual possession is the one responsible for the tax. This includes renting to a tenant business in which you have a proprietary interest. Example: Your personal lease to a corporation you own is taxable. **Effective July 29, 2010:** Rental of commercial property between corporations if one owns at least 80% of the other corporation is exempt. The exemption includes a third corporation if it owns 80% of both the landlord and the lessor corporations, and treats a “reciprocal insurer” as if it were a corporation.

#### WHAT IS COMMERCIAL REAL PROPERTY?

Commercial real property is real property used, or to be used, for income-producing purposes. It is **not** residential real property.

#### EXEMPTIONS AVAILABLE TO LESSORS OF COMMERCIAL REAL PROPERTY

The rules regarding the taxability of commercial real property rentals and leases do not include real property that provides short-term (transient) lodging, such as hotels, motels, or RV parks. The providers of these kinds of rentals, even though they involve commercial real property, are subject to tax under the “transient rental” section of the occupational tax code. **Do be aware** that if the rental of a room is for something other than lodging, such as for a meeting or banquet, the income is subject to the commercial real property rental tax.

Additionally, if a business holds items in trust for others and restricts their customers’ access to them, the transaction is considered “bailment”. Bailment income is exempt from tax. Examples of bailment include:

- fur storage
- furniture being stored at a moving company’s warehouse
- vehicles held in a storage area

Income from public storage facilities is **not** considered bailment, and is taxable. A public storage facility allows a customer to rent a specific area of the premises, provide their own lock for that area, and restrict the owner of the facility from access to the customer’s items.

Rental income received **from** certain customers, and **by** certain lessors, is also exempt from tax. Commercial real property rental income is exempt if a tenant is:

- a qualifying hospital, community health center, or health care organization, *or*
- renting property located on Davis-Monthan Air Force base, *or*
- subletting the property to a third party (the one directly leasing to the tenant is responsible for the tax)

**Note: Rental income received from schools and churches, or federal, state, or other governmental agencies, is not exempt from tax.**

Similarly, the following entities do not owe tax on real property rental income. Those entities include:

- health-care businesses
- prisons
- 501(c)(3) organizations (certain non-profit organizations designated by the federal government)  
A word of caution: If the non-profit entity has a mortgage on the property, the rental income **is** considered taxable.

Finally, there is no exemption from tax if the lessor leases to a related lessee, or if the lessor only owns one real property rental.

### **IS ANY OTHER COMMERCIAL REAL PROPERTY RENTAL INCOME TAXABLE?**

When the landlord of a commercial property wants to guarantee a certain amount of income each month, without regard for expenses such as repairs and property taxes, a lease arrangement known as a “carefree lease” or “triple net lease” is sometimes negotiated. In this type of arrangement, the tenant sends one check to the landlord, and assumes all other expenses directly, including the Business Privilege tax due the City of Tucson. The gross income for the rental shown on the landlord’s tax return must include all expenses paid by the tenant to, or on behalf of, the landlord. These expenses may include (but are not limited to):

- mortgage payments made on behalf of the property owner in lieu of rent
- property taxes
- pet fees
- security and/or cleaning deposits (these become taxable at the time they are forfeited by the lessee)
- telecommunications and utilities, if not separately metered
- homeowner’s association dues
- common area maintenance fees
- repairs or improvements
- late charges

FOR MORE INFORMATION ABOUT...

Taxes –Audit Section: City of Tucson – Tax Audit Section - (520) 791-4681  
255 W. Alameda - Second Floor,  
P.O. Box 27210, Tucson, Arizona , 85726-7210

Licenses –License Section: City of Tucson - License Section - (520) 791-4566  
255 W. Alameda - First Floor  
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Hearing impaired: TDD (520) 791-2639

Visit the City of Tucson Web Page at: <http://www.tucsonaz.gov>

To read more about the business privilege tax: <http://www.tucsonaz.gov/finance/BusInfo.html>

**The City of Tucson prepared this brochure. It does not provide comprehensive explanations of Tucson tax laws, rules, or regulations. Specific questions should be addressed to the City of Tucson Tax Audit Section. Rev. 10-11**