

OP. NO. 04-057

**TAXATION: REAL PROPERTY TAX — TAX EXEMPT
PROPERTY.**

Federal government has exclusive jurisdiction over Interior and Exterior Posts of Fort Story. Neither Commonwealth nor any of its political subdivisions may impose property taxes on portion of military housing project to be built on leasehold interest or on Ground Lease interest located thereon. Leasehold interests are not subject to local taxation. Military Housing Privatization Initiative precludes local taxation of project's Ground Lease interests.

The Honorable Philip J. Kellam
Commissioner of the Revenue for the City of Virginia Beach
July 21, 2004

Issues Presented

You ask several questions regarding the proposed construction of military family housing at the United States Army base at Fort Story under the Military Housing Privatization Initiative contained in the 1996 Defense Authorization Act.

Background

You inquire regarding the ability of the City of Virginia Beach to impose real property taxes on certain transactions and improvements to be located at Fort Story. In connection with your request, you have submitted certain documents corroborating the information set forth below.¹

Fort Story is a 1,450-acre military installation on a federal enclave within the City of Virginia Beach. It is primarily a base for the United States Army. Approximately one-third of Fort Story is under the exclusive jurisdiction of the federal government (the "Interior Post"), and two-thirds is under the concurrent jurisdiction of the United States and the Commonwealth of Virginia (the "Exterior Post"). The present installation at Fort Story was created primarily by two grants from the Commonwealth—one in 1902² and the other in 1940.³

You relate that that the 1996 Defense Authorization Act, in particular the Military Housing Privatization Initiative, enables the military to obtain private funding for the construction of family housing, because the Department of Defense recognized that military family housing cannot be revitalized using only traditional military construction programs. The Army has awarded a project planning contract to GMH Military Housing-Hampton Roads LLC ("GMH"), a nongovernment party, to replace and upgrade 161 family housing units, and if necessary, to build approximately 250 new housing units to meet the on-post family housing requirements for personnel assigned to Fort Story.

At Fort Story and other military installations in Virginia, the Department of Defense, through the Secretary of the Army, and military housing contractors have entered into Community Development and Management Plans. To qualify for private financing, and to allow military personnel to receive a housing allowance to be used as rent, GMH and the Army plan to enter into an agreement to create a Delaware limited liability company ("GMH Family Housing"), which will be taxed as a partnership for federal income tax purposes.⁴

You advise that the Army will own at least 90% interest,⁵ and up to 100% interest, depending on the actual dollar contribution by the minority contractor member, in GMH Family Housing.⁶ The majority owner, or government member,⁷ controls the selection of the manager and the terms on which financial contributions by GMH Family Housing members will be reimbursed or paid. Thus, you conclude that the Army, as the holder of the majority interest, controls GMH Family Housing.

Two members will fund GMH Family Housing. The Army will lease the real property to GMH Family Housing, under the terms of a Ground Lease, for a period of 50 years, with a right of renewal.⁸ Although the United States will contribute a certain amount of cash, as appropriated by Congress, GMH also will be required to contribute a specified cash amount of the construction costs. You relate, however, that this contribution is limited to certain costs incurred during construction. Thus, the more efficient the construction, the lower the contribution will be.

GMH Family Housing will plan, develop and construct the 250 family units, and then manage, rent and maintain the units under the guidelines of the family housing requirements of the Department of Defense. You state that all improvements⁹ are permanent structures that will be annexed to the realty. Upon

termination of the military housing project, the Ground Lease and ownership of all improvements automatically will revert to the Army, at no consideration. You relate that 243 housing units will be built in the Interior Post and 7 units in the Exterior Post.

Applicable Law and Discussion

The 1996 National Defense Act established the Military Housing Privatization Initiative as alternative authority for the acquisition and improvement of military housing.¹⁰

A. The Interior Post

You ask whether the federal government has exclusive jurisdiction over the portion of the Interior Post where military housing will be constructed, and if so, whether the local government is prohibited from levying any form of property tax on the leasehold interest.

Article I, § 8, Clause 17 of the Constitution of the United States authorizes the federal government "[t]o exercise exclusive legislation ... over all places purchased by the consent of the legislature of the state in which the same shall be, for the erection of forts, magazines, arsenals, dock yards, and other needful buildings."¹¹ The Interior Post will hold 243 units under the terms of the Ground Lease. Pursuant to the 1902 Act, the Commonwealth ceded exclusive jurisdiction to the United States, subject only to the right of the Commonwealth to serve civil and criminal process.¹² The 1902 Act states:

1. Be it enacted by the general assembly of Virginia, That the consent of the State of Virginia is hereby given, in accordance with the seventeenth clause, eighth section, of the first article of the constitution of the United States, to the acquisition by the United States, by purchase, condemnation, or otherwise, of any land in this State required for sites for custom houses, courthouses, postoffices, arsenals, or other public buildings whatever, or for any other purposes of the government.

2. *That exclusive jurisdiction in and over any land so acquired by the United States shall be, and the same is hereby, ceded to the United States for all purposes except the service upon such sites of all civil and criminal process of the courts of this State; but the*

jurisdiction so ceded shall continue no longer than the said United States shall own such lands.

3. The jurisdiction ceded shall not vest until the United States shall have acquired the title to said lands by purchase, condemnation, or otherwise; and so long as the said lands shall remain the property of the United States when acquired as aforesaid, and no longer, the same shall be and continue exempt and exonerated from all State, county, and municipal taxation, assessment, or other charges which may be levied or imposed under the authority of this State.

4. This act shall take effect and be in force from and after its passage.^[13]

Under the terms of the Ground Lease, the United States always retains the fee interest in the property. GMH Family Housing will have a leasehold interest for a term of fifty years. Throughout the entire term, it is anticipated that the Army will be the majority and controlling owner, and will authorize all aspects of the construction, choice of tenants, and lease rates. At termination, all improvements revert to the United States, without charge.

In the absence of a clear waiver, states and their political subdivisions may not levy taxes on property belonging to the federal government.¹⁴ The immunity from local taxation applies to private property within an area of exclusive federal jurisdiction.¹⁵ "[W]here the lands are within the exclusive jurisdiction of the United States, under Article I, Section 8, Clause 17 of the Federal Constitution, they are immune from taxation by a state and even private property located thereon is not subject to taxation by a state."¹⁶ This is frequently known as the "intergovernmental tax immunity doctrine."¹⁷

Therefore, in the absence of congressional consent, neither the Commonwealth nor any of its political subdivisions may impose a leasehold interest on the project at Fort Story. No such consent applicable to this situation exists.¹⁸ As such, neither Virginia nor its political subdivisions may impose property taxes on the leased land or on improvements made to the Interior Post.

B. The Exterior Post

You ask whether the federal government has exclusive jurisdiction over the portion of the Exterior Post where military housing will be constructed.

Seven of the military housing units will be constructed on Ground Lease property lying in the Exterior Post. Although these units are subject to the United States Constitution granting the federal government the exercise of exclusive jurisdiction over all lands purchased with the consent of the state legislature,¹⁹ the property on which these units are to be located must also comply with the provision of the 1940 Act that the Commonwealth and the federal government exercise concurrent jurisdiction over crimes and offenses committed on lands acquired by the United States and used for any military purpose.²⁰ Otherwise, the federal government retains exclusive jurisdiction, subject to the right of the Commonwealth to serve civil and criminal process. The 1940 Act, however, provides the following condition under which state jurisdiction may be reasserted:

[I]n the event that the said lands or any part thereof shall be sold or leased to any *private* individual, or any association or corporation, under the terms of which sale or lease the vendee or lessee shall have the right to conduct thereon any *private industry or business*, then the jurisdiction ceded to the United States over any such lands so sold or leased shall cease and determine, and thereafter the Commonwealth of Virginia shall have all jurisdiction and power she would have had if no jurisdiction or power had been ceded to the United States. This provision, however, shall not apply to post exchanges, officers' clubs, and similar activities on lands acquired by the United States for purposes of National defense.^[21]

Therefore, once the ceded property is sold or leased to a "private" individual, association, or corporation and the terms of the sale or lease provide the buyer or lessee with the right to conduct "any private industry or business" thereon,²² Virginia would regain jurisdiction over the relevant property. It is clear, however, that the military housing project does not trigger this reversionary condition. As a threshold matter, where, as here, the federal government is engaging in a ground lease to another entity, and reserves the right to retain all improvements made thereon at no charge, the property is considered to continue to be owned by the federal government.²³ In this case, that other "entity" is not "private,"²⁴ but is a

government-controlled corporation or, in other words, an instrumentality of the federal government.

Moreover, the federal government has a long history of using publicly owned corporations, quasi-public corporations, and other government-controlled entities to achieve governmental purposes while using techniques available in the private sector.²⁵ The "privatization" contained in the Military Housing Privatization Initiative is an example of the federal government seeking to use private sector expertise to accomplish a governmental function. Indeed, there is Virginia precedent for these types of structures,²⁶ as well as for federal military housing within the Commonwealth.²⁷ Given the overwhelming preponderance of federal ownership of family housing, as well as for its authorization for all aspects of construction, its choice of tenants and establishment of lease rates, it is clear that this is not the type of "private individual, or any association or corporation ... [engaging in] any private industry or business," within the meaning of the 1940 Act.²⁸ This is government action, with a private party exercising its expertise in return for a very small minority interest. Accordingly, this is not the type of activity that would trigger a reversion of the Exterior Post to the Commonwealth. Indeed, it is merely an instrumentality of the federal government, and as such, the military housing project is entitled to intergovernmental tax immunity.²⁹

Inasmuch as the federal government retains exclusive jurisdiction over the Exterior Post for most purposes, including its immunity from state or local taxation, and in the absence of express congressional consent therefor, neither the Commonwealth nor the City of Virginia Beach has taxing jurisdiction.

C. Leasehold Taxes Under § 58.1-3203 or § 58.1-3603

Assuming exclusive jurisdiction in A and B above, you ask whether any portion of the property or leasehold interest is taxable under § 58.1-3203 or § 58.1-3603.

Finally, even assuming that the military housing project and GMH Family Housing's leasehold interest may not be exempt from state and local taxation due to the exclusive federal jurisdiction exercised over the Interior Post and the Exterior Post resulting in intergovernmental tax immunity, neither the Commonwealth nor its political subdivisions would be able to impose property taxes on the project under the express terms of the Military Housing Privatization Initiative. This prohibition is sufficient to encompass both §§ 58.1-3203 and 58.1-3603, which provide for taxation of leasehold

interests. Consistent with the governmental nature and purposes of the project, Congress specifically has provided that the government's conveyance or lease of property or facilities under the Initiative shall not be subject to the federal government's waiver of sovereign immunity to allow state and local taxation of "non-excess property" of the Department of Defense.³⁰ Accordingly, the Ground Lease interests to be created by the project are not subject to local taxation under either § 58.1-3203 or § 58.1-3603.³¹

Conclusion

Accordingly, it is my opinion that the United States government, through the Army, has exclusive jurisdiction over the Interior and Exterior Posts of Fort Story. Therefore, neither the Commonwealth nor any of its political subdivisions may impose property taxes on the portion of the military housing project to be built on the leasehold interest or on the Ground Lease interest located thereon.

I am also of the opinion that due to the exclusive jurisdiction of the United States government over Fort Story, and in the absence of an applicable waiver from the federal government, the described military housing project is not subject to taxation under § 58.1-3203 or § 58.1-3603. Moreover, even in the absence of such exclusive jurisdiction by the United States government, the operation of these local taxing provisions to the project's Ground Lease interests is specifically precluded by § 2878(d)(1) of the Military Housing Privatization Initiative.

¹I assume, for the purposes of this opinion, that the following documents are the only ones pertinent to the use of Fort Story by the United States government, except as otherwise noted in this opinion: (1) The Army's Residential Communities Initiatives under the 1996 Defense Authorization Act, setting forth the Military Housing Privatization Initiative, marked Exhibit 1; (2) two draft documents dated May 10, 2004: (a) Limited Liability Company Operating Agreement for Hampton Roads Family Housing LLC, marked Exhibit 2 [hereinafter LLC Operating Agreement], and (b) Department of the Army Ground Lease, Fort Eustis and Fort Story, Virginia Beach and Newport News, Virginia, marked Exhibit 3; and (3) letter from Colonel Robin N. Swope to Ms. Stephanie L. Hamlett regarding jurisdiction at Fort Story under Residential Communities Initiative (June 16, 2004), marked Exhibit 4, enclosing (a) February 1, 1982, map of Fort Story showing areas subject to concurrent and exclusive jurisdiction; (b) two Corps of Engineers' maps showing eastern and western portions of Fort Story; (c) Deed of Cession, dated May 11, 1978, from the Commonwealth of

Virginia to the United States, and recorded in the Clerk's Office of the Circuit Court of Virginia Beach, in Deed Book 1826, at 13; and (d) memorandum from Susan A. Bivins regarding jurisdiction at Fort Story under Residential Communities Initiative (June 16, 2004).

²1901-2 Va. Acts ch. 482, at 565; see *id.* ch. 55, at 49, 49 ("An Act inviting the government of the United States to establish a military post in Virginia, and giving the consent of the State to the purchase of land for the same."); see *also* 1918 Va. Acts ch. 382; 1922 Va. Acts ch. 390, at 657.

³1940 Va. Acts ch. 422, § 19-c-(6), at 761, 762 (creating certain reversionary provisions to Virginia for conduct of private industry or business on lands acquired by United States for purposes of national defense); *cf. id.* ch. 110, at 161 (authorizing Virginia Conservation Commission to transfer to United States certain portion of Virginia Sea Shore State Park adjoining Fort Story Military Reservation); *id.* ch. 417, at 754, 754 ("For all purposes of taxation and of the jurisdiction of the courts of Virginia over persons, transactions, matters and property on said lands, the said lands shall be deemed to be a part of the county or city in which they are situated."). Virginia's current laws pertaining to the jurisdiction of lands acquired by the United States are contained in Chapter 3 of Title 7.1, § 7.1-12, §§ 7.1-18.1 through 7.1-24, and § 7.1-25.1 (Michie Repl. Vol. 1999).

⁴It appears from the terms of the LLC Operating Agreement (see *supra* note 1) that GMH Family Housing is to be operated as a for-profit entity, at least with respect to the Agreement's nongovernment members. Accordingly, for purposes of this opinion, I assume that GMH Family Housing will not qualify as tax exempt within the purview of § 58.1-3203 or § 58.1-3603. See *Mariner's Museum v. City of Newport News*, 255 Va. 40, 495 S.E.2d 251 (1998) (affirming lower court's judgment that charitable corporation forfeits its tax-exempt status when its realty is leased for substantial revenue or profit under § 58.1-3603(A)); see *also* 2002 Op. Va. Att'y Gen. 331 (concluding that rent paid by using entity to Christian Aid Mission is source of revenue or profit and therefore taxable).

⁵Initially, the government member will have only an 80% membership interest. See LLC Operating Agreement, *supra* note 1, Ex. "C", "Initial Capital Contributions," at 43.

⁶Under certain circumstances, the Army may transfer its membership interest to (1) an agency or subdivision of the federal government; (2) an agency or subdivision of any state or local

government; or (3) any other direct or indirect holder of membership interest in GMH Family Housing, or an affiliate of the holder. See LLC Operating Agreement, *supra* note 1, § 9.1(a)-(c), at 28-29. For the purposes of this opinion, I assume that at all times relevant to the questions posed in your request, the government member's interest will be held by the Army or the Department of Defense.

⁷For purposes of this opinion, "government member" means the United States Army.

⁸See *supra* note 1. The Ground Lease referenced in this opinion will be entered into between the United States, by the Secretary of the Army, and GMH Family Housing, as lessee, for the lease of the proposed military housing project at Fort Eustis and Fort Story. See *id.*

⁹The construction of roads, infrastructure, housing units and other buildings related to the proposed project are collectively referred to as "improvements."

¹⁰See National Defense Authorization Act for Fiscal Year 1996, Pub. L. No. 104-106, 1996 U.S.C.C.A.N. (110 Stat.) 186, 544-51 (codified as amended at 10 U.S.C.A. §§ 2871-2885 (West 1998 & Supp. 2004)).

¹¹The language in the United States Constitution granting exclusive federal jurisdiction "exclude[s] all other authority than that of congress; and that no other authority can be exercised over them has been the uniform opinion of Federal and State tribunals." *Foley v. Shriver*, 81 Va. 568, 571-72 (1886) (citation omitted); see, e.g., *Offutt Housing Co. v. County of Sarpy*, 351 U.S. 253, 256 (1956) (citing *Surplus Trading Co. v. Cook*, 281 U.S. 647 (1930)) (noting that power of "exclusive legislation" has been held to prohibit state taxation of private property located on military base acquired pursuant to U.S. Constitution).

¹²See 1901-2 Va. Acts ch. 482, *supra* note 2, at 566 (citing § 2).

¹³*Id.* at 565, 566 (emphasis added).

¹⁴See *Surplus Trading Co.*, 281 U.S. at 656-57 (discussing language of Arkansas statute).

¹⁵The doctrine of federal immunity from state taxation originally was espoused by the Supreme Court in the case of *McCulloch v.*

Maryland, 17 U.S. (4 Wheat.) 316 (1819) (holding that State of Maryland, within which branch bank of United States was established, cannot tax branch, without violating Constitution).

¹⁶*Sheridanville, Inc. v. Wrightstown*, 125 F. Supp. 743, 750 (D.C.N.J. 1954) (footnote omitted) (citing *Surplus Trading Co.*, 281 U.S. at 647).

¹⁷See, e.g., *Harper v. Va. Dep't of Tax'n*, 509 U.S. 86 (1993) (applying rule announced in [*Davis v Michigan Dep't of Treasury*, 489 U.S. 803 \(1989\)](#), that state violates constitutional doctrine of intergovernmental tax immunity when state taxes retirement benefits received from United States by military retirees but does not tax benefits received by retired state and local government employees); see also *Bd. of Supvrs. v. Stanley Bender & Assocs.*, 201 F. Supp. 839, 842 (E.D. Va. 1961) ("Plaintiff overlooks the basic fact that no tax may be levied upon property owned by the United States in the absence of Congressional consent."); *County of Prince William v. Thomason Park, Inc.*, 197 Va. 861, 864, 91 S.E.2d 441, 444 (1956) ("The parties agree that upon ceding to the United States exclusive jurisdiction over the land here involved, Virginia gave up the power to impose the [real estate] taxes herein assessed.... It is a fundamental principle that a state and its [political] subdivisions are without power, in the absence of express consent of Congress, to tax property owned by the United States. Such consent, being in derogation of the sovereign power of the federal government, is found only where Congress has spoken in the clearest language.").

¹⁸It might be argued that the federal government may have waived its sovereign immunity over certain interests of lessees in non-excess military property. See 10 U.S.C.A. § 2667(e) (West 1998) ("The interest of a lessee of property leased under this section may be taxed by State or local governments."); see also *Thomason Park, Inc.*, 197 Va. at 862 n.1, 91 S.E.2d at 443 n.1 ("The lessee's interest, made or created pursuant to the provisions of [the Military Leasing] Act, shall be made subject to State or local taxation.") (quoting § 522e, predecessor to § 2667(e)). The question whether the Ground Lease at the Interior Post or the Exterior Post at Fort Story constitutes non-excess military property is irrelevant. The federal government's conveyance or lease of property or facilities under the Military Housing Privatization Initiative would not be subject to the waiver contained in § 2667(e). See 10 U.S.C.A. § 2878(d)(1) (West Supp. 2004).

¹⁹See U.S. Const. art. I, § 8, cl. 17.

²⁰ See 1940 Va. Acts, *supra* note 3, at 762 (citing § 19-c-(6)).

²¹ *Id.* (emphasis added). The May 11, 1978, Deed of Cession contains similar language as the 1940 Act.

²² 1940 Va. Acts, *supra* note 3, at 762 (quoting § 19-c-(6)).

²³ See *Thomason Park, Inc.*, 197 Va. at 867, 91 S.E.2d at 445-46 ("In the instant case, no right of removal was reserved to the lessee, but to the contrary ..., the lease contract expressly provides that the improvements shall remain on the land and be the property of the federal government without compensation. Hence, title to the improvements vested upon their erection in the United States in fee simple, and therefore the only property owned by lessee is a leasehold interest in the land and buildings for a fixed period of years."). At the time in question, neither the state nor its subdivisions were authorized to tax a leasehold. *Cf.* 2000 Op. Va. Att'y Gen. 211, 213 ("The provisions of [§ 58.1-3203] shall not apply to any leasehold interests exempted or partially exempted by other provisions of law."). *Cf. Sheridanville, Inc.*, 125 F. Supp. at 743 (holding that lands within exclusive jurisdiction of United States, as well as private property located on such lands, are not subject to state taxation).

²⁴ See *Harrison v. Day*, 202 Va. 967, 972, 121 S.E.2d 615, 618 (1961) ("If it is a governmental function and a public purpose that is to be carried out by the [Virginia State Ports] Authority, it does not become a private function and a private purpose by being let by the Authority to another to do the work."). For an example of privatization resulting in a "private" entity, see *Varicon Int'l v. Office of Personnel Mgmt.*, 934 F. Supp. 440, 446-47 (D.D.C. 1996) (bringing action against Office of Personnel Management for awarding government contract for services to U.S. Investigations Services).

²⁵ See *LeBron v. Nat'l R.R. Passenger Corp.*, 513 U.S. 374, 386-91 (1995); see also *Baltimore Gas & Elec. Co. v. United States*, 133 F. Supp. 2d 721 (D. Md. 2001) (declaring Army Secretary's implementation of privatization initiative through bid solicitation for right to operate military installation's utility system proper).

²⁶ See, e.g., *Harrison*, 202 Va. at 969, 121 S.E.2d at 616 ("Since the acquisition, development and operation of port and harbor facilities contemplated at Hampton Roads is a proper governmental function, our conclusion is that the statutes involved are not violative of § 185 of the Constitution of Virginia. It being a

governmental function, the appropriation is for a public purpose and *not a private purpose.*" (Emphasis added.) (Citation omitted)).

²⁷ See, e.g. *Stanley Bender & Assocs.*, 201 F. Supp. at 843 (stating that "'public purpose' of Wherry Act housing projects ... is to provide housing accommodations in critical defense housing areas for the military and such civilians as may be related to military activities. The fact that these housing projects are operated and maintained by quasi-private corporations under long-term lease agreements with the United States does not, in any degree, lessen the 'public purpose.'"); *Thomason Park, Inc.*, 197 Va. at 863 n.2, 91 S.E.2d at 443 n.2 (noting section of Wherry Military Housing Act that permitted state and local taxation of private lessee's interest).

²⁸ 1940 Va. Acts, *supra* note 3, at 762 (quoting § 19-c-(6)).

²⁹ While GMH Family Housing may be considered an instrumentality of the federal government for purposes of local property taxation, no opinion is expressed concerning its status for any other purpose, including, but not limited to, purposes of federal and state income taxation.

³⁰ See 10 U.S.C.A. § 2878(d)(1). In this regard, Congress has "express[ed] itself unequivocally." *Offutt Housing Co.*, 351 U.S. at 260 (noting that Congress used general language in Military Leasing Act of 1947 and Wherry Military Housing Act of 1949, regarding taxation of leasehold interests); see also *supra* note 11.

³¹ As to the operation of §§ 58.1-3203 and 58.1-3603 generally, see 1987-1988 Op. Va. Att'y Gen. 601, 602-03.

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