



## **COMMERCIAL PASS-THROUGH PAYMENTS**

**Commercial pass-through payments from the tenant to the landlord should NOT be included as the part of the landlord's gross income and should NOT be taxable under the revised franchise tax.**

**BACKGROUND:** Commercial leases are typically structured where the tenant pays a sum that includes base rent plus payments for the tenant's pro rata share of real estate taxes, insurance premiums and the operating expenses for the common areas of the property. The landlord holds these funds on behalf of the tenant on an escrow basis and then *passes them through* to the county tax assessor/collector, the insurance company, and the other service providers. As such, these *pass-through* payments should not be considered income or taxable to the landlord for purposes of the revised franchise tax.

### **ARGUMENTS:**

**It's a Matter of Fairness:** The revised franchise tax already excludes pass-through funds from gross income for subcontractor payments handled by a general contractor, for attorneys holding claimant's funds, and for funds mandated by law or fiduciary duty. Tenant funds held by landlords of commercial real estate should be treated no differently.

**Commercial Pass-Through Payments Provide No Financial Benefit to the Landlord:** Therefore, these payments should not be considered income for purposes of the revised franchise tax. They are simply collected as a courtesy and held in escrow to cover the tenants' pro rata share of real estate taxes, insurance, and common area maintenance fees.

**It's Double Taxation:** Funds that are remitted to insurance companies and other service providers are considered income to those entities and are taxable as such. Therefore, taxing the landlord on those same funds is double taxation. In addition, taxing the landlord on funds used to pay real estate taxes to the county tax assessor/collector is the same thing as taxing "tax dollars", not income.

**No Real Property Tax Relief to Offset:** Commercial landlords do not benefit from property tax reductions because their leases are structured in a way that requires them to pass 100% of the property tax savings through to the tenants.