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DATE: April 2, 1991

SUBJECT: Constitutionality of Amendment of the Definition of Real Property for Tax Purposes under LB 1115 in Light of Natural Gas Pipeline Co. v. State Bd. of Equal., 237 Neb. 357, ___ N.W.2d ___ (1991).

REQUESTED BY: Senator W. Owen Elmer
Nebraska State Legislature

WRITTEN BY: Don Stenberg, Attorney General
L. Jay Bartel, Assistant Attorney General

You have requested us to reexamine our conclusions regarding the constitutionality of the amendment of the definition of real property for tax purposes under LB 1115 reached in Attorney General Opinion No. 90007, issued on February 14, 1990, in light of the recent Nebraska Supreme Court decision in Natural Gas Pipeline Co. v. State Bd. of Equal., 237 Neb. 357, ___ N.W.2d ___ (1991).

Generally, LB 1115 would alter the current system of property taxation by exempting all personal property other than motor vehicles, and by redefining the term "real property" in Neb.Rev.Stat. § 77-103 (Reissue 1990) (as amended by 1989 Neb. Laws, 1st Spec. Sess., LB 1). The proposed redefinition of "real property" subject to taxation is contained in Section 24 of LB 1115, which provides, in pertinent part:

> (1) Real property shall include both type A and type B real property.
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> (2) Type A real property shall mean all land, including land under water, and all mines, minerals in place, quarries, sand and gravel pits, mineral springs and wells, and oil and gas wells.

> (3) Type B real property shall mean any improvement, upon or beneath type A real property, which remains, in the normal course of events, affixed upon or beneath such property for longer than twelve months. For purposes of this subsection, improvement shall mean any property that remains fixed and stationary by design in relation to the type A real property for twelve months or more, and affixed shall mean actually or constructively annexed or attached.

During a special session convened in November, 1989, the Legislature amended the definition of "real property" in §77-103 to include ". . . pipelines, railroad track structures, electrical and telecommunications poles, towers, lines, and all items actually annexed to such property, and any interest pertaining to the real property or real estate." 1989 Neb. Laws, 1st Special Session, LB 1.

We addressed at length the constitutionality of legislation amending the definition of real property in §77-103 in Attorney General Opinion No. 89071, dated November 13, 1989. In this opinion, we considered whether it was permissible for the Legislature to adopt a statutory definition of real property for tax purposes which differed from adherence to the common law standards which the Nebraska Supreme Court had found in Northern Natural Gas Co. v. State Board of Equalization and Assessment, 232 Neb. 806, 443 N.W.2d 249 (1989) ["Northern"] to be included in §77-103. Noting the general rule that "[i]t is competent for the Legislature to classify for purposes of legislation, if the classification rests on some reason of public policy, some substantial difference of situation or circumstance, that would naturally suggest the justice or expediency of diverse legislation with respect to the objects to be classified. . ." (Stahmer v. State, 192 Neb. 63, 68, 218 N.W.2d 893, 896 (1974)), we concluded the Legislature was not necessarily precluded from enacting legislation altering the definition of real property under §77-103, provided a reasonable basis could be articulated to justify any classification established by such redefinition. At the time of the issuance of our prior opinion discussing the constitutionality of Section 24 of LB 1115, we noted that no judicial determination had been made as to the constitutionality of the amendment to § 77-103 made by LB 1. Attorney General Opinion No. 90007, at 2.

Subsequent to the issuance of our two prior opinions addressing the constitutionality of legislation altering the definition of "real property" for tax purposes, the Nebraska Supreme Court issued its opinion in Natural Gas Pipeline Co. v. State Bd. of Equal., 237 Neb. 357, ___ N.W.2d ___ (1991) ["NGPL"], as well as opinions in several companion cases. You now ask us to

revisit the question of the constitutionality of the proposed redefinition of "real property" for tax purposes under LB 1115 in light of the decision in NGPL.

In reversing and remanding the 1989 action of the State Board of Equalization and Assessment ["State Board"] with respect to the equalization of the personal property of centrally assessed taxpayers, the per curiam majority in NGPL held, in part, that the redefinition of "real property" accomplished under LB 1 could not be applied to determine the equalization claims before the State Board for the 1989 tax year. Specifically, the majority held that: (1) the subject matter of LB 1 was "irrelevant to the matter of equalization;" and (2) "the application of LB 1 for the 1989 tax year would result in the commutation of a tax, in violation of Neb. Const. art. VIII, § 4." Id. at 366, ___ N.W.2d at ___. Thus, the majority in NGPL did not deal with the constitutionality of LB 1 beyond making a determination that the bill could not be applied to tax year 1989. The per curiam majority did not reach any further question as to the constitutionality of LB 1.

In a separate concurring opinion, Judge Grant, joined by Judge Fahrnbruch, went further, expressing the view that LB 1 was "unconstitutional on its face." Id. at 377, ___ N.W.2d at ___ (Grant, and Fahrnbruch, J., concurring). Citing the court's prior decisions in State ex rel. Meyer v. Peters, 191 Neb. 330, 215 N.W.2d 520 (1974), and Moeller, McPherrin and Judd v. Smith, 127 Neb. 424, 255 N.W. 551 (1934), Judge Grant stated: "Although the Legislature has broad power to define property for tax purposes, its power to define is limited, since (1) the Legislature cannot abrogate or contradict an express constitutional definition and (2) the legislative definition must be reasonable and cannot be arbitrary or unfounded." 237 Neb. at 377, ___ N.W.2d at ___. Judge Grant determined the definition in LB 1 impermissibly nullified and circumvented the Legislature's authorization under Neb. Const. art. VIII, § 2, to classify and exempt personal property, finding "the Legislature has not `classified' certain items of personal property, but has arbitrarily declared the personal property owned by an unfavored group of taxpayers to be `fixtures,' which are presumedly taxable as real estate under our decision in Northern Natural Gas Co. v. State Bd. of Equal., 232 Neb. 806, 443 N.W.2d 249 (1989)." 237 Neb. at 379, ___ N.W.2d at ___. He continued by stating that, under LB 1, "the Legislature has attempted to define and designate as a `fixture' that which is, in fact and in truth, personal property, and has gone beyond the bounds of its legitimate powers in doing so." Id. Judge Grant also concluded the classification set forth in LB 1 violated the prohibition against special legislation in Neb. Const. art. III, § 18, "because it is not based on any real and substantial difference between `machinery and equipment used for business

purposes or center pivot or other irrigation systems of a type used for agricultural or horticultural purposes' and machinery and equipment used for other purposes." Id. [1]

In another separate opinion, Judge Shanahan, concurring in part and dissenting in part, expressed his views concerning the reasonableness of the amendment to the definition of "real estate" under LB 1. Judge Shanahan, taking issue with the opinions expressed by Judge Grant as to the validity of LB 1, stated "the definition of `real estate' in L.B. 1 and the exclusion of certain property from statutorily defined `real estate'. . . have a rational basis and are, therefore, reasonable and are not arbitrary or unfounded." 237 Neb. at 392, ___ N.W.2d at ___ (Shanahan, J., concurring in part and dissenting in part). He further stated that, even if the business "machinery and equipment" provision of LB 1 were found to be unconstitutional, that provision was severable from the remainder of the bill. Id..

In summary, the following observations regarding the court's views as to the constitutionality of the Legislature's alteration of the definition of "real property" for tax purposes under LB 1 may be gleaned from the decision in NGPL: (1) A majority of the court has not expressed an opinion as to whether the redefinition of "real property" in § 77-103 accomplished by LB 1, which departs from the common law of fixtures for determining whether an item is real or personal property, is unconstitutional either on its face or as applied to tax years beyond 1990. Rather, the per curiam majority held only that the redefinition in LB 1 could not constitutionally be applied to the equalization claims for tax year 1989 pending before the court; (2) At least two members of the court (and possibly three) have expressed the opinion that the definition of "real property" in LB 1 is, in their view, unconstitutional on its face; and (3) One member of the court has stated it is his opinion that the amendment to the statutory definition of "real property" accomplished by LB 1 is constitutional, indicating the portion of the bill relating to business "machinery and equipment" may be unconstitutional but, nevertheless, severable so as to save the remainder of the bill.

In our previous opinions, we noted that several states have adopted statutory definitions of real property or real estate for tax purposes that include types of property, which, under the common law of fixtures, would likely constitute personalty, and that challenges to the constitutionality of such classifications

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[1] In a separate concurrence, Judge Caporale stated "there may be much merit in what Judge Grant has written about L.B. 1." 237 Neb. at 381, ___ N.W.2d at ___ (Caporale, J., concurring).

have been rejected in other jurisdictions. Attorney General Opinion No. 89071, November 13, 1989, at 3; Attorney General Opinion No. 90007, February 14, 1990, at 2-3. Based on such authority, we previously stated it was not inherently unreasonable for the Legislature to classify property as real or personal for tax purposes in a manner which differed from the common law tests regarding fixtures, such as contained in LB 1 and Section 24 of LB 1115, provided the classifications established were reasonable.

We did note, however, that any attempt to reclassify real and personal property by definition could well be construed as creating an arbitrary and unreasonable classification contrary to the Nebraska Constitution. Specifically, with regard to LB 1115, we stated it was possible that an owner of property subject to taxation as " type B real property" under the bill could be able to successfully argue the taxation of such property was arbitrary and unreasonable when the same or similar property was, under the definition established by the bill, classified as personal property and, therefore, exempted from taxation. Attorney General Opinion No. 90007, February 14, 1990, at 3.

The recent per curiam opinion in NGPL does not, for the reasons stated previously, provide any definitive statement of the opinion of a majority of the court as to the Legislature's authority to classify property as real or personal for tax purposes. There is case law in Nebraska, however, relied upon by the members of the court concluding LB 1 was, in their view, unconstitutional, revealing that our court has consistently taken a very restrictive view as to the Legislature's ability to classify and define terms within the confines of the State Constitution in the area of property taxation.

In Moeller, McPherrin and Judd v. Smith, 127 Neb. 424, 255 N.W. 551 (1934) ["Moeller"], the court held unconstitutional legislative action altering the taxation of tangible and intangible property accomplished by the enactment of a statute defining the term "tangible property" to include property which, by nature, was intangible. In particular, the court stated:

> May a legislature, under the guise of defining a word, do so with a definition which contravenes our Constitution, and which is not true or legal in fact? Class 2 of tangible property, as defined in House Roll No. 9, is intangible property as defined by the leading dictionaries.
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> * * *

> Can the legislature define and designate as tangible that which is, in fact and in truth, intangible? It may be admitted that the legislature has power to define words used by it, but is this an unlimited power, or is it subject to a reasonable construction? Tangible is the direct opposite of intangible; and can the legislature, under the guise of calling it two separate classes of tangible property, include all intangible property under class 2 of tangible property? In our opinion, there is a limit to the legislature's power to nullify and circumvent constitutional provisions by putting an arbitrary, but improper and unfounded, definition upon a certain word.
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> The Constitution of Nebraska clearly provides for two kinds of personal property for purposes of taxation, and the legislature has abrogated one of these by the device of calling it a class under the other. The legislature could not directly blot out a provision of the Constitution; has it not, by House Roll No. 9, attempted to do it indirectly?
>
> If the Constitution gives one definition of a legal term, and a statute another, it is the duty of a court to declare that the Constitution governs.

Id. at 433, 255 N.W. at 555-56.

Furthermore, in State ex rel. Meyer v. Peters, 191 Neb. 330, 215 N.W.2d 520 (1974) ["Peters"], the court declared unconstitutional a statute exempting from property taxation household goods, "including major appliances either attached or detached to real property," and personal effects. The legislation was assertedly enacted pursuant to Article VIII, Section 2, of the Nebraska Constitution, which provided, in part: "Household goods and personal effects, as defined by law, may be exempted from taxation in whole or in part, as may be provided by general law. . . ." (Emphasis added). In holding the phrase "household goods and personal effects, as defined by law" in Article VIII, Section 2, referred to existing law at the time of adoption of the constitutional amendment in a descriptive and limiting manner, the court stated:

> Any definitional powers given to the Legislature are prefixed and limited. The power to define household goods and personal effects necessarily is limited to those articles which ordinarily would be understood to

> be embraced within that term. Certainly, it cannot be interpreted to give the Legislature power to include air-conditioning systems, furnaces, automobiles, or real estate within the term "household goods and personal effects." Since there must be a limit to such powers, it is reasonable to find the common law concepts serve as guides.
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> * * *
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> In any event, any power to define household goods must be limited for the term "household goods" to have any meaning whatever. It is obvious that the Legislature could not be allowed to define all property in the state as household goods and personal effects. To permit it to do so would allow it to negate other parts of the Constitution.

Id. at 334-35, 215 N.W.2d at 524-25.

While it is possible to try to distinguish the situations addressed in Moeller and Peters from the one presented herein, it is clear that certain members of our Supreme Court have taken a rather narrow view of the scope of the Legislature's power to classify and define property for tax purposes in this context. The concurring opinion of Judge Grant (joined by Judge Fahrnbruch), reflecting the view that the classifications set forth in LB 1 are unconstitutional, relies heavily on the court's prior decisions in Moeller and Peters. As noted previously, at least these two members of the court (and possibly a third member) are on record as expressing their opinion that LB 1 is unconstitutional. You should recognize that there are clear similarities between the constitutional infirmities articulated by these members of the court regarding LB 1, and the proposed amendment to the definition of "real property" under LB 1115. [2]

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[2] Furthermore, in considering the constitutionality of the exemption of property classified as "personal property" by virtue of the provisions of LB 1115, it should be noted that three members of the court indicated in a concurring opinion in NGPL that the exemption of all personal property may run afoul of the Constitution, in spite of the apparent authority granted to the Legislature under Neb. Const. art. VIII, § 2, to "...exempt all personal property from taxation." In this regard, Judges White and Fahrnbruch, joined by Judge Grant, stated "[u]nder our constitutional system, all property, except household goods and property owned by nonprofit educational, charitable, horticultural, or cemetery organizations, which property is used for those purposes, must be taxed, or no property may be taxed." 237 Neb.

Five of the seven judges of the Nebraska Supreme Court must agree in order to hold a law unconstitutional. Neb. Const. art. V, § 2. It is reasonably certain that at least two judges would rule the definition of real property unconstitutional and at least one (Judge Shanahan) would likely rule the definition constitutional. Although we are of the opinion that Judge Shanahan's view is the more reasonable one, we do not know, and at this time cannot know, whether at least two of his colleagues will agree with that view.

Therefore, we cannot definitively answer the question you have raised. We, therefore, counsel caution but, at the same time, we cannot say that the definition would necessarily be ruled unconstitutional.

Finally, it is not apparent from your request whether you wish us to readdress the questions discussed in our prior opinion as to the constitutionality of certain other provisions of LB 1115. In this respect, we direct you to our earlier opinion as, upon review, we continue to adhere to the conclusions reached therein regarding the constitutionality of these provisions.

Very truly yours,

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cc: Patrick J. O'Donnell
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APPROVED BY:

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at 374, ___ N.W.2d ___ (White, and Fahrnbruch, J., concurring). In our opinion, it is unlikely that a constitutional majority of the court would accept this restrictive interpretation.