Jerry Rudibaugh

Municipal Tax Hearing Officer

DECISION OF MUNICIPAL TAX HEARING OFFICER

Decision Date: August 26, 2002

Decision: MTHO #37

Tax Collector: City of Tempe

Hearing Date: July 10, 2002

DISCUSSION

Introduction

On January 11, 2002, "Holding Company" or "Taxpayer" filed a protest of the City of Tempe ("City"). After review of the protest, the City concluded it was timely and in the proper form. On February 28, 2002, the Municipal Tax Hearing Officer ("Hearing Officer") ordered the City to file a response on or before April 15, 2002. The City filed its response on April 10, 2002. On April 22, 2002, the Hearing Officer ordered the Taxpayer to file any reply on or before May 6, 2002. Subsequently, the Taxpayer requested an extension until May 10, 2002. On May 6, 2002, the Hearing Officer granted the extension request for good cause shown. On May 10, 2002, the Taxpayer filed a reply. On April *25,* 2002, the matter was scheduled for hearing commencing on May 30, 2002. The matter was subsequently rescheduled several times until the parties agreed upon a hearing date of July 10, 2002. The City and the Taxpayer both appeared and presented evidence at the July 10, 2002 hearing. On July 11, 2002 the Hearing Officer issued a letter indicating a decision would be issued on or before August 26, 2002.

The Taxpayer is a corporation that is owned by two shareholders. The same two shareholders are partners in "Partnership", an Arizona general partnership. The Partnership owns and operates "Dealer" stores. In some cases, the Taxpayer purchases property with money from the Partnership and has a Dealer store constructed on the property. At the completion of construction, the Taxpayer transfers the improved property to the Partnership. No money exchanges hands when the property is transferred. In April 1998, the Taxpayer purchased vacant land located on XXX Road within the City, from an unrelated party. The Taxpayer constructed a building to operate a Dealer store, A certificate of occupancy was issued on June 27, 2000. In August of 2000, the Taxpayer deeded the property to the Partnership. The City concluded there was a sale and imposed a speculative builder tax pursuant to City Code Section 16-416 ("Section 416"). On August 1, 2000, the ("Bank") loaned the Partnership a total of $1.2 million on two properties. Those properties were located at AAA Road, City B, AZ and XXX Road, Tempe, AZ. Since the sale in question was for the XXX Road property, the City utilized the $1.2 million loan amount as an estimate of the fair market value of the property in making its tax assessment for taxes due pursuant to Section 416 in the amount of $8,199.44, a late filing penalty pursuant to Section 16-540 (b) (1) ("Section 540 (b) (1)") in the amount of $1,229.92, a late payment penalty pursuant to Section 16-540 (b) (2) ("Section 540 (b) (2)") in the amount of $819.94, plus interest pursuant to Section 16-540 ("Section 540").

City Position

The City concluded that the Taxpayer was an owner-builder that sold improved real property before the expiration of twenty-four months after the improvements of the real property sold were substantially complete. The City argued that Section 416

doesn't require consideration in order to impose a speculative builders tax. For that reason, the City requested the assessment be up held. The City further argued that even if consideration was required the sale was still taxable because the deed transferring the title of the property to the Partnership contained the following language: for "consideration of TEN AND NO/100 DOLLARS, and other valuable considerations". The City also asserted that it is clear in the City Code that the Taxpayer and the Partnership were distinct and separate persons and that there was a business and legal benefit in making the transfer.

The City concluded that the gross income from the transaction between the affiliated companies (Taxpayer and Partnership) was not indicative of the "market value" of the subject matter of the transaction. In those circumstances City Code Section 16-210 ("Section 210") authorizes the City to determine the "market value" which would correspond to gross income from similar transactions.

The City estimated the fair market value at $1.2 million based on the fact that the Bank loaned that amount on the property. Further, the City determined a similar property sold over a year before the transfer in question for approximately $1.2 million.

Taxpayer Position

The Taxpayer argued that a "sale" is required under Section 416 and the definition of "sale" contained in City Code Section 16-100 ("Section 100") "requires that there be consideration for the transaction. In this case, the Taxpayer transferred the property on XXX Road to a Taxpayer related entity (Partnership) without the exchange of consideration. The Taxpayer and the Partnership are both owned by the same two individuals. The Taxpayer was acting as the agent of the Partnership and no consideration was paid for the transfer of property. The Taxpayer asserted that it improved the property as the agent for the Partnership, for the benefit of the Partnership, and with the use of the funds of the Partnership. As a result, the Taxpayer requested a finding that no sale has occurred and that no tax is due in connection with the transfer. Alternatively, if a determination is made that a taxable sale has occurred, the Taxpayer disputes the City's determination of an "estimated gross sale amount" of $1.2 million. The City erroneously utilized the Bank loan amount from August of 2000 as a representative value for the XXX Road property. The Taxpayer asserted that the $1.2 million loan was made on two properties. One of those properties was the XXX Road and the other was on ma Road in City B, AZ. Further, the Taxpayer provided an affidavit from the loan officer for the Bank indicating the Bank had valued the XXX Road property at approximately $770,000. In addition, the similar sale the City relied upon was for a store with twelve bays while the property in question is a store with only seven bays and approximately 50% less square footage. The Taxpayer argued that a more representative "estimated gross sales amount" would be the actual cost of the property of $847,378.46, which is the sum of the original purchase price of the land ($365,000) and the actual cost of constructing the improvements ($482,378.46).

ANALYSIS

It is clear that the Taxpayer and the Partnership were separate and distinct entities under the provision of the City Code. It is also clear that there was a transfer from the Taxpayer to the Partnership of improved real property within twenty-four months of the issuance of a certificate of occupancy. We also conclude that the use of the word "sale" in Section 416 is controlled by the definition of "sale" contained in Section 100. Accordingly, we must conclude that consideration is a requirement for there to be a "sale" pursuant to Section 416. Under the circumstances of this case, we do not find there was a transfer of property for a consideration. While there was language contained in the deed transferring the title of the property to the Partnership regarding consideration often dollars and other valuable considerations, we do not find such language to be sufficient to conclude there was consideration for the transfer of properties. In fact, based on the evidence presented, we conclude that the Taxpayer was acting as the agent for the Partnership in acquiring the land and subsequently constructing the improvements. The Taxpayer had no funds of its own to purchase and construct the improvements, but utilized the funds of the Partnership for the purchase and improvements. We also did not find any evidence that the transaction in question was structured in a manner to attempt to avoid the plain meaning and intent of Section 416. Based on all the above, the Hearing Officer concludes there was no sale pursuant to Section 416 and thus no tax is due in connection with the transfer. Accordingly, the Hearing Officer finds the valuation issue to be moot and did not enter a decision on that issue.

FINDINGS OF FACT

1. On January 11, 2002, the Taxpayer filed a protest of the City tax assessment.

2. After review of the protest, the City concluded the protest was timely and in the proper form.
3. On February 28, 2002, the Hearing Officer ordered the City to file a response on or before April 15, 2002.
4. The City filed its response on April 10, 2002.

5. On April 22, 2002, the Hearing Officer ordered the Taxpayer to file any reply on or before May 6, 2002.

6. On May 6, 2002, the Hearing Officer granted the Taxpayer's extension request for good cause shown.

7. On May 10, 2002, the Taxpayer filed a reply.

8. On April 25, 2002, the matter was scheduled for hearing commencing on May 30, 2002.

9. The matter was subsequently rescheduled several times until the parties agreed upon a hearing date of July 10, 2002.

10. The City and Taxpayer both appeared and presented evidence at the July 10, 2002 hearing.

11. On July 11, 2002, the Hearing Officer issued a letter indicating a decision would be issued on or before August 26, 2002.

12. The Taxpayer is a corporation that is owned by two shareholders.

13. The same two shareholders are partners in the Partnership.

14. The Partnership owns and operates Dealer stores.

15. In April 1998, the Taxpayer purchased vacant land located on XXX Road within the City from an unrelated party.

16. The Taxpayer had a building constructed to operate a Dealer store on the XXX Road property.

17. The Taxpayer acted on behalf of the Partnership in purchasing the land and having a building constructed to operate a Dealer store.

18. The Taxpayer had no funds to purchase the property and construct the building but utilized the funds of the Partnership.

19. A certificate of occupancy was issued for the improved property on XXX Road on June 27, 2000.

20. In August of 2000, the Taxpayer deeded the improved property on XXX Road to the Partnership with no money changing hands.

21. The City imposed a tax assessment on the transfer from the Taxpayer to the Partnership as a speculative builder tax pursuant to Section 416.

22. The City issued an assessment for taxes due in the amount of $8,199.44, a late filing penalty pursuant to Section 540 (b) (1) in the amount of $1,229.92, a late payment penalty pursuant to Section 540 (b) (2) in the amount of $819.94, plus interest pursuant to Section 540.

23. The improved property on XXX Road was transferred from the Taxpayer to the Partnership before the expiration of twenty-four months after the real property transferred was substantially complete.

24. The deed transferring the title from the Taxpayer to the Partnership contained the following language: for "consideration of TEN AND NO/100 DOLLARS, and other valuable considerations."

25. The Taxpayer and the Partnership were distinct and separate persons pursuant to the City Code.

26. On August 1, 2000, the Bank loaned the Partnership a total of $1.2 million on two properties that were located on XXX Road and on YYY Road in City B, AZ respectively.

27. The loan officer for the Bank filed an affidavit indicating the Bank had valued the XXX Road property at approximately $770,000.

28. Approximately one year prior to the transfer of the XXX Road property, the Partnership had sold another Dealer store with twelve bays for approximately $1.2 million.

29. The XXX Road store had seven bays and approximately 50% less square footage than the Dealer store sold approximately one year earlier.

CONCLUSIONS OF LAW

1. Pursuant to ARS Section 42-6056, the Municipal Tax Hearing Officer is to hear all reviews of petitions for hearing or redetermination under the Model City Tax Code.

2. The City imposes a privilege tax on speculative builders pursuant to Section 416.

3. Section 210 authorizes the City to determine the "market value" of a transaction between related entities if the gross income from the transaction was not indicative of the "market value".

4. The use of the word "sale" in Section 416 is controlled by the definition of "sale" contained in Section 100.

5. Consideration is a requirement for there to be a "sale" pursuant to Section 416.

6. The Taxpayer received no consideration for the transfer of the improved property to the Partnership.

7. The Taxpayer acted as the agent for the Partnership in acquiring the XXX Road property and having a Dealer store constructed on the property.

8. The Taxpayer's protest should be granted.

ORDER

It is therefore ordered that the January 11, 2002, protest of Taxpayer of the tax assessment of the City of Tempe is hereby granted.

It is further ordered that the City of Tempe shall revise its tax assessment to reflect that the transfer of improved property on XXX Road from the Taxpayer to Partnership was not a taxable transaction.

It is further ordered that this decision shall be effective immediately.

Jerry Rudibaugh

Municipal Tax Hearing Officer