DECISION OF MUNICIPAL TAX HEARING OFFICER

August 30, 2010

Taxpayer Representative

Taxpayer
MTHO # 546

Dear **Taxpayer Representative**:

We have reviewed the evidence and arguments presented by ***Taxpayer*** and the City of Chandler (Tax Collector or City) at the hearing on April 12, 2010 and in post-hearing memoranda. The review period covered was February 2000 through November 2004. Taxpayer's protest, Tax Collector's response, and our findings and ruling follow.

Taxpayer's Protest

Taxpayer purchased real property (Property) in the City of Chandler previously used for farming. The Property included existing buildings and other farm structures. Taxpayer intended to subdivide the Property and sell individual lots to purchasers. To prepare the lots for sale, Taxpayer removed existing structures, filled in a dry pond, cleared and graded the property and installed certain off-site improvements. Other than removing existing structures, filling in the pond and grading the Property, Taxpayer did not alter or add to the lots themselves.

Taxpayer was assessed City of Chandler privilege tax under the speculative builder classification for the sale of the subdivided lots. Taxpayer contends that it did not improve any of the lots within the meaning of Chandler Tax Code (CTC) § 62-416(a)(2)(B), which imposes the privilege tax on the sale of real property where improvements have been made to land containing no structure, such as paving or landscaping. Taxpayer did not add pavement, landscaping or similar improvement to the lots prior to their sale. Therefore, none of its lot sales were subject to the City privilege tax and Taxpayer was not required to obtain a Chandler privilege tax license. The total assessment must be abated.

Tax Collector's Response

Taxpayer purchased the Property, including existing buildings and farm structures. Taxpayer intended to subdivide the Property into custom home lots. Before the sale of any lots, Taxpayer demolished the existing structures, filled in a dry pond, cleared and mass graded the Property and added a concrete slab, footing and stem walls for common areas. These improvements to the total Property constituted improvement to the individual lots within the meaning of CTC § 62-416(a)(2)(B). Improvement to the lot is not limited to paving and landscaping, but includes any activity that improves or increases the value of the lot.

In addition, some of the lots were sold after streets, water and utilities had been constructed to the lot property line. The sale of those lots were sales of improved real property within the

meaning of CTC § 62-416(a)(2)(D). At the minimum, Taxpayer is liable for the tax on lots that were sold after water, power and streets had been constructed to the property line of the lot.

Because Taxpayer was subject to the privilege tax under the speculative builder classification, Taxpayer was required to obtain a privilege tax license.

Discussion

Taxpayer is a land development company. Taxpayer purchased the Property to develop, subdivide into custom home lot sites and sell the lots. Taxpayer did not do any home construction or building on the lots.

The Property had been used for farming. To prepare the Property, Taxpayer demolished existing farm buildings and other structures, filled in a dry pond, cleared and graded the Property and added certain off-site improvements for the common areas. Taxpayer made no other changes to the building lots themselves.

After the Property had been cleared and graded, Taxpayer began selling lots. For a period of time Taxpayer continued to do off-site improvements, including streets, sidewalks and utilities, while lots were being sold.

The Tax Collector conducted an audit assessment of Taxpayer for the period February 2000 through November 2004 and assessed Taxpayer city privilege tax under the speculative builder classification. The Tax Collector considered the sale of all of the lots during the audit period to be sales of improved real property. Taxpayer timely protested contending that none of the lots sold were improved real property.

Whether and to what extent a person is taxable is governed by the Chandler City Code. Taxpayer was assessed as a speculative builder. A speculative builder is defined by the code as including an owner-builder who sells or contracts to sell, at anytime, improved real property consisting of improved residential or commercial lots without a structure. The definition of improved real property includes any real property where improvements have been made to land containing no structure, such as paving or landscaping (CTC § 62-416(a)(2)(B)) or where water, power and streets have been constructed to the property line (CTC § 62-416(a)(2)(D)).

Were the sales of the lots taxable under CTC § 62-416(a)(2)(B)?

The City first argues that all of the lots sold by Taxpayer were improved real property. Taxpayer purchased land that had been used for farming. Taxpayer demolished the farm structures, filled in a pond, cleared and mass graded the entire property and put in some common area off-site improvements. By the time first lot was sold, the existing farm structures had been removed, the land, including the lots, had been cleared, graded and leveled, and certain off-site improvements such as fence and footings for the common areas had been constructed. These activities, including clearing and grading the entire Property, improved the Property, which included the individual lots. The activities made the lots more valuable. Improvement to the lot is not limited to paving and landscaping. Therefore the lots were "improved real property" within the meaning of CTC § 62-416(a)(2)(B).

Taxpayer argues that the lots were not improved real property within the meaning of CTC § 62-416(a)(2)(B). Subparagraph (B) defines "improved real property" as real property where improvements have been made … such as paving or landscaping. It is the Taxpayer's position that the word "improvements" is limited to improvements of the same or similar nature as paving or landscaping. Both paving and landscaping have an element of adding to the land. Demolishing structures, clearing and grading the land or making general off-site improvements do not have this element of adding to the lots. Those activities are not of the same or similar nature as adding pavement or landscaping to the lots. Therefore, the lots sold by Taxpayer were not improved real property within the meaning of CTC § 62-416(a)(2)(B).

Statutes imposing taxes are to be strongly construed against the government and in favor of the taxpayer. Statues should be interpreted so that every word is given meaning. The meaning of a general term in a statute (improvements) is restricted to things that are similar to those designated by specific words that follow (such as paving or landscaping). In order for Taxpayer to be taxable as a speculative builder within the meaning of CTC § 62-416(a)(2)(B), the Tax Collector must show that improvements of the same or similar nature as paving or landscaping were made to the lots sold by Taxpayer.

Demolishing the existing farm buildings and other structures, filling in a dry pond and clearing and mass grading the Property did occur, at least in part, on areas that would be subdivided into the lots. While such activities may be improvement to real property in a general sense, the question is whether those activities are of a similar nature as adding pavement or landscaping to the lot. Construing the code strictly against the City, the answer must be no. Any other answer would effectively read the phrase "such as paving or landscaping" out of the code. Therefore, Taxpayer's sale of the lots were not sales of improved real property within the meaning of CTC § 62-416(a)(2)(B).

Was the sale of any of the lots taxable under CTC § 62-416(a)(2)(D)?

The definition of improved real property includes any real property where water, power and streets have been constructed to the property (lot) line (CTC § 62-416(a)(2)(D)). The City contends that at least some of the lots were sold after water, power and streets had been constructed to the property line. Taxpayer objects to the Tax Collector raising CTC § 62-416(a)(2)(D) for the first time at the hearing and moved to strike any discussion of paragraph (2)(D). Taxpayer also argues that the Tax Collector presented no evidence showing that water, power and streets had been constructed to the property line when any of the lots were sold.

Is the issue of taxability under CTC § 62-416(a)(2)(D) properly before the Hearing Officer?

The Tax Collector assessed Taxpayer for understated contracting (speculative builder) activity. The assessment did not specify a particular definition of "improved real property" under CTC § 62-416(a)(2). Taxpayer protested the assessment stating that while Taxpayer made off-site improvements such as making residential lots, installing utility lines and conduit up to but not into the building lots, paving streets, constructing a fence around the property and adding

amenities for the common use of those who purchase lots, Taxpayer made no improvement to the lots themselves. It only sold unimproved lots.

The Tax Collector submitted its response dated December 16, 2009 to the issues raised in the Taxpayer's protest. On page 2 of its response, the Tax Collector cited to both CTC § 62-416(a)(2)(B) and § 62-416(a)(2)(D) for the definition of improved real property. On page 3 of its response the Tax Collector argued that Taxpayer improved all of the real property in question by removing existing structures, grading the land prior to sale, and, in most cases, constructing water, power and streets to the property line. Therefore all of the sales were taxable under CTC § 62-416.

While the Tax Collector's response mainly discussed whether Taxpayer improved the lots within the meaning of CTC § 62-416(a)(2)(B), the response also argued that at least some of the lots were improved real property within the meaning of CTC § 62-416(a)(2)(D). Therefore the issue whether any of the lots sold were improved real property within the meaning of CTC § 62-416(a)(2)(D) is properly before the Hearing Officer. It is not necessary to discuss whether the Tax Collector could have raised the issue for the first time at the hearing.

Were any of the lots sold improved real property within the meaning of CTC § 62-416(a)(2)(D)?

The Tax Collector submitted aerial photographs of the Property from the Maricopa County Assessor's website dated December 30, 2000, January 22, 2002, December 8, 2002, December 10, 2003 and November 30, 2004. The aerial photographs reflected the state of the Property on those dates.

The lot sales took place between October 2001 and November 2004. The aerial photograph dated December 10, 2003 shows the completed subdivision and shows some home construction on the lots. It shows that the streets had been constructed to the property line. The subdivision has underground utilities, which were installed before the streets were paved. Water, power and streets were therefore constructed to the property line by December 10, 2003.[1] Therefore, the sales of lots on or after December 10, 2003 were sales of improved real property subject to the privilege tax on speculative builders.

Based on all the above, we conclude Taxpayer's protest should be granted in part and denied in part. The City's privilege tax assessment against Taxpayer was not proper for the sale of any lots prior to December 10, 2003. The City's assessment was proper for the sale of lots on or after December 10, 2003.

Findings of Fact

1. Taxpayer is a land development company.
2. Taxpayer purchased real property (Property) in the City of Chandler, including existing buildings and other structures.

[1] The aerial photograph dated December 8, 2002 was inconclusive regarding the construction of water, power and streets to the property line.

3. The Property had been used for farming.

4. Taxpayer intended to subdivide the Property and sell individual lots to purchasers.

5. Taxpayer does not construct homes on the individual lots.

6. Taxpayer demolished and removed the existing structures, filled in a dry pond and cleared and mass graded the Property.

7. After the Property was graded, Taxpayer made no changes to the building lots.

8. The only activity Taxpayer undertook on the lots was to demolish and remove existing structures, fill in a dry pond and clear and mass grade the Property, including the lots.

9. Taxpayer installed off-site improvements on the Property, including fencing, footings for common areas, streets, sidewalks and utilities.

10. The subdivision has underground utilities located below the streets.

11. Utilities such as power and water are installed before the streets are paved.

12. Taxpayer sold lots both before and after the streets had been paved.

13. Taxpayer did not have a privilege tax license from the City during the audit period.

14. The Tax Collector conducted an audit assessment of Taxpayer for the period February 2000 through November 2004.

15. The Tax Collector assessed Taxpayer for city privilege tax under the speculative builder classification in the amount of $126,391.39, interest through August 2009 in the amount of $69,657.29 and license fees and license fee penalties in the amount of $120.00.

16. No other penalties were assessed.

17. The Tax Collector included in the assessment all lot sales by Taxpayer during the audit period.

18. Taxpayer timely protested the assessment by Notice dated October 13, 2009.

19. Taxpayer's protest stated that that while Taxpayer made off-site improvements such as making residential lots, installing utility lines and conduit up to but not into the building lots, paving streets, constructing a fence around the property and adding amenities for the common use of those who purchase lots, it made no improvement to the lots themselves.

20. The Tax Collector responded to Taxpayer's protest relying on both CTC § 62-416(a)(2)(B) and § 62-416(a)(2)(D) in support of its assessment.

21. The Tax Collector's response also stated that in most cases (lot sales) Taxpayer had constructed water, power and streets to the property line.

22. The Tax Collector submitted aerial photographs of the Property from the Maricopa Assessor's website dated December 30, 2000, January 22, 2002, December 8, 2002, December 10, 2003 and November 30, 2004.

23. The aerial photographs reflected the state of the Property on the dates of the photographs.

24. Aerial photograph dated December 10, 2003 showed that the subdivision of the Property had been completed, the streets were paved, and home construction had started on some of the lots.

25. By December 10, 2003 water, power and streets had been constructed to the property line of each lot.

26. Lot sales took place between October 2001 and November 2004.

27. All lot sales during December 2003 occurred after December 10, 2003.

Conclusions of Law

1. A speculative builder includes an owner-builder who sells, at any time, improved real property consisting of improved residential or commercial lots without a structure. CTC § 62-100.

2. Improved real property includes any real property where improvements have been made to land containing no structure, such as paving or landscaping. CTC § 62-416(a)(2)(B).

3. Statutes imposing taxes are to be strongly construed against the government and in favor of the taxpayer. Any doubts as to the meaning of the statute are to be resolved against the tax authority. *Wenner v. Dayton-Hudson Corp.* 123 Ariz. 203, 208, 598 P.2d 1022, 1027 (App. 1979).

4. Statues should be interpreted so that every word is given meaning. *Industrial Authority of Pima v. Maricopa,* 189 Ariz. 558, 944 P.2d 73 (App. 1997).

5. The meaning of a general term in a statute is restricted to things that are similar to those designated by specific words that follow. *State v. Barnett*, 142 Ariz. 592, 691 P.2d 683 (1984).

6. Improvement to real property within the meaning of CTC § 62-416(a)(2)(B) must be of the same or similar nature as paving or landscaping.

7. Demolishing and removing existing structures, filling in a dry pond and clearing and mass grading real property are not improvements of the same or similar nature as paving or landscaping.

8. Taxpayer's sales of lots during the audit period were not sales of improved real property within the meaning of CTC § 62-416(a)(2)(B).

9. Improved real property also includes any real property where water, power and streets have been constructed to the property line. CTC § 62-416(a)(2)(D).

10. The Tax Collector properly raised the issue whether any of Taxpayer's lot sales were sales of improved real property within the meaning of CTC § 62-416(a)(2)(D).

11. Taxpayer's lots were improved real property by December 10, 2003.

12. Taxpayer's sales of lots on or after December 10, 2003 were sales of improved real property subject to the privilege tax on speculative builders.

13. The City's privilege tax assessment against Taxpayer was proper with respect to lots sold on or after December 10, 2003.

14. Taxpayer was engaged in business as a speculative builder in the City and was required to obtain a privilege tax license.

15. The City's privilege tax assessment against Taxpayer was proper with respect to the privilege tax license fees and license fee penalties.

16. The City's privilege tax assessment against Taxpayer was not proper with respect to lots sold before December 10, 2003.

Ruling

The October 13, 2009 protest by Taxpayer of an assessment made by the City of Chandler is granted in part and denied in part consistent with Conclusions of Law numbers 8 and 12 through 16.

The Tax Collector shall remove from the assessment taxable gross receipts from lot sales made before December 10, 2003.

Both parties have timely rights of appeal to the Arizona Tax Court pursuant to Model City Tax Code Section –575.

Sincerely,

Frank L. Migray
Hearing Officer

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c: ***Senior Tax Auditor***
Municipal Tax Hearing Office