

## DECISION OF MUNICIPAL TAX HEARING OFFICER

May 17, 2010

*Taxpayer*  
*123 Corn Cob Drive*  
*Orangewood, XX, 12345-6789*

*POA (Power of Attorney for Taxpayer)*  
*12345 E. Mountain Drive*  
*City, AZ 12345*

*Taxpayer*  
MTHO # 543

Dear Mr. *Taxpayer* and *POA for Taxpayer*:

We have reviewed the evidence presented by *Power of Attorney for Taxpayer* and the City of Scottsdale (Tax Collector or City) at the hearing on April 14, 2010. The review period covered was February 2007. Taxpayer's protest, Tax Collector's response, and our findings and ruling follow.

### Taxpayer's Protest

Taxpayer was assessed City of Scottsdale privilege tax under the speculative builder classification for the sale of a home Taxpayer had constructed in the City. Taxpayer does not dispute that some taxes are due, but believes another party is liable for at least a part of the tax, and believes the market value used by the Tax Collector to calculate the tax was too high.

### Tax Collector's Response

Taxpayer was the sole owner of record to the Property on which the home was constructed and thus Taxpayer was the only person who met the definition of a speculative builder. No interest in the Property had been transferred to another party until after the construction of the home was completed. The Tax Collector cannot assess the tax against a person who is a not speculative builder under the city code. Therefore Taxpayer is liable for the total amount of the assessment. The Tax Collector's estimate of market value was based on a sale of the Property immediately after the taxable transaction. The estimate of market value used by the Tax Collector was reasonable.

## Discussion

Taxpayer purchased a vacant lot (the Property) in *Scottsdale Estate* in May 2005. **Construction Developer** was the developer of *Scottsdale Estate*. Taxpayer held sole title to the Property. Taxpayer contracted with **Builder LLC** to build the home on the Property. The building permit for the construction of the home was issued August 25, 2005. A certificate of occupancy was issued January 16, 2007. By January 16, 2007 the home was already constructed on the Property. Taxpayer was the sole owner of the Property during the time the home was being constructed by **Builder LLC**.

On February 6, 2007 Taxpayer signed a warranty deed transferring title to the Property to **POA for Taxpayer** as to an undivided 59% interest and to **Taxpayer** as to an undivided 41% interest. The warranty deed stated that the Property was subject to existing taxes, assessments, liens, encumbrances, covenants, conditions, restrictions, rights of way and easements of record.

No contract sales price was stated in the deed. Taxpayer did not have a written agreement with **POA for Taxpayer** regarding the transfer of the Property other than the deed transferring title to **POA for Taxpayer** and **Taxpayer**.

**POA for Taxpayer** and **Taxpayer** then transferred the Property to **Final Purchaser**, the final purchaser, for a contract sales price of \$2,800,000.00. The settlement date of the sale to the final purchaser was February 7, 2007.

The Tax Collector conducted an audit assessment of Taxpayer for the period February 2007 and issued a Notice of Assessment on July 21, 2009 to Taxpayer for city privilege tax under the speculative builder classification. The Tax Collector thereafter issued two modifications to allow available credits and deductions and a reduction for development fees paid. The second modification was dated February 17, 2010 and assessed privilege tax in the amount of \$21,752.95, interest through January 31, 2010 in the amount of \$3,973.14 and license fees and license fee penalties in the amount of \$223.50.

The Tax Collector considered Taxpayer to be a speculative builder when he transferred title to the Property to **POA for Taxpayer** and **Taxpayer**. The Tax Collector based the assessment on the estimated fair market value of the Property at the time of the transfer from Taxpayer to **POA for Taxpayer** and **Taxpayer**. The Tax Collector used the contract sales price of \$2,800,000.00 to the final purchaser as its estimate of the Property's fair market value.

Taxpayer protested the assessment stating other parties were liable for at least a part of the tax. Taxpayer stated he was holding title to the property as an accommodation party for **Construction Developer** and was acting as a constructive trust for the principals of **Construction Developer**. **Construction Developer** could not get financing to build the homes because it already had loans outstanding. Therefore **Construction Developer** sought accommodating parties who would hold title and get the construction loan, and profit from the sale of the house would be split with the accommodating party.

Whether and to what extent a person is taxable is governed by the Scottsdale City Code. Taxpayer was assessed as a speculative builder. A speculative builder is defined by the code as including an owner-builder who sells, at any time, improved real property consisting of custom homes regardless of the stage of completion. To be a speculative builder, a person has to be an owner-builder.

An owner-builder is defined as including an owner or lessor of real property who, by himself or by or through others, constructs or has constructed or reconstructs any improvement to real property. Only Taxpayer meets this definition. Taxpayer had title to the Property and had an improvement constructed on the Property while he owned it (held title). *POA for Taxpayer* was not an owner of the Property while the house was being constructed. Taxpayer purchased the Property before any construction and did not sell the Property to *POA for Taxpayer* and *Taxpayer* until after construction of the home was completed.

When Taxpayer executed the warranty deed to *POA for Taxpayer* and *Taxpayer*, he transferred title to the Property. Sale of improved real property includes any form of transaction which in substance is a transfer of title of improved real property. Taxpayer therefore sold improved real property when he transferred title to the Property to *POA for Taxpayer* and *Taxpayer*.

Only Taxpayer met the definition of a speculative builder. *POA for Taxpayer* was not an owner-builder and was therefore not a speculative builder with respect to the Property. Since Taxpayer was a speculative builder, he was subject to tax under the speculative builder classification.

The warranty deed did not specify a contract sales price. The Tax Collector therefore based its assessment on the market value of the Property at the time of the transfer. The Tax Collector's estimate of market value was based on the contract sales price of the Property to the final purchaser.

The sale to the final purchaser took place almost immediately after the sale by Taxpayer to *POA for Taxpayer* and *Taxpayer*. The contract sale price of the Property to the final purchaser was therefore a reasonable estimate of the fair market value of the Property when Taxpayer transferred title to *POA for Taxpayer* and *Taxpayer*.

Taxpayer argued that the gross receipts from the sale of the property should be less than the amount used by the Tax Collector. The existence of another reasonable basis of estimation does not invalidate the Tax Collector's estimate. It is the responsibility of the taxpayer to prove that the Tax Collector's estimate is not reasonable and correct. Taxpayer did not present evidence showing that the Tax Collector's estimate was not reasonable. The amount of the assessment was therefore proper.

Taxpayer argued that he was holding title to the Property as an accommodation party, and was acting as a constructive trust for the members of *Construction Developer*. The reason Taxpayer chose to hold title to the Property does not change the outcome.

An accommodation party is one who signs a commercial paper for the purpose of lending his name and credit to another party to the document, the accommodated party, to help that party

obtain a loan or an extension of credit. An accommodation party is liable to the person or business that extended credit to the accommodation party.

An arrangement to be an accommodation party is an agreement between the accommodation party and the accommodated party. It is a private agreement. It does not relieve the accommodation party of liability. Even if Taxpayer were an accommodation party, contracts between a taxpayer and a third party regarding payment of taxes cannot shift the legal incidence of the tax as between the city and the taxpayer. Here the incidence of the tax fell on Taxpayer because he was the speculative builder.

A constructive trust is a trust created by operation of law against one who by actual or constructive fraud, by duress or by abuse of confidence, or by commission of wrong, or by any form of unconscionable conduct, or other questionable means, has obtained or holds legal right to property which he should not, in equity and good conscience, hold and enjoy. The existence or non-existence of a constructive trust between Taxpayer and the principals of *Construction Developer* has no impact on Taxpayer's liability for the City's privilege tax.

Based on all the above, we conclude Taxpayer's protest should be denied. The City's privilege tax assessment against Taxpayer was proper.

#### Findings of Fact

1. Taxpayer purchased *Lot A* in *Scottsdale Estate* in May 2005.
2. *Construction Developer* was the developer of *Scottsdale Estate*.
3. *Lot A* (the Property) was vacant land at the time Taxpayer purchased it.
4. Taxpayer entered into a new home construction agreement with *Builder LLC* to build a single family home on the Property.
5. The building permit for the construction of the home was issued August 25, 2005.
6. A Certificate of Occupancy was issued January 16, 2007.
7. Taxpayer was the sole owner of the Property during the time the home was being constructed by *Builder LLC*.
8. On February 6, 2007 Taxpayer executed a warranty deed transferring title to the Property to *POA for Taxpayer* as to an undivided 59% interest and to *Taxpayer* as to an undivided 41% interest.
9. The warranty deed stated that the Property was subject to existing taxes, assessments, liens, encumbrances, covenants, conditions, restrictions, rights of way and easements of record.
10. No contract sales price was stated in the deed.
11. Taxpayer did not have a written agreement with *POA for Taxpayer* regarding the transfer of the Property other than the deed transferring title to *POA for Taxpayer* and *Taxpayer*.
12. Construction of the home was completed when Taxpayer executed the warranty deed on February 6, 2007.

13. ***POA for Taxpayer*** and ***Taxpayer*** transferred the Property to ***Final Purchaser***, for a contract sales price of \$2,800,000.00.
14. The settlement date of the sale to the final purchaser was February 7, 2007.
15. The Tax Collector conducted an audit assessment of Taxpayer for the period February 2007 and issued a Notice of Assessment on July 21, 2009 to Taxpayer for city privilege tax under the speculative builder classification.
16. The Tax Collector thereafter issued two modifications to allow available credits and deductions and a reduction for development fees paid.
17. The second modification was dated February 17, 2010 and assessed privilege tax in the amount of \$21,752.95, interest through January 31, 2010 in the amount of \$3,973.14 and license fees and license fee penalties in the amount of \$223.50.
18. No other penalties were assessed in the second modification.
19. The assessment included all applicable credits, exemptions and deductions.
20. The Tax Collector based the assessment on the estimated fair market value of the Property at the time of the transfer from Taxpayer to ***POA for Taxpayer*** and ***Taxpayer***.
21. The Tax Collector used the contract sales price of \$2,800,000.00 to the final purchaser as its estimate of the Property's fair market value.
22. Taxpayer timely protested the assessment.

#### Conclusions of Law

1. An owner-builder is defined as an owner or lessor of real property who, by himself or by or through others, constructs or has constructed or reconstructs any improvement to real property. Sec. 100.
2. Taxpayer had title to the Property and had an improvement constructed on the Property by ***Builder LLC***.
3. Taxpayer was an owner-builder.
4. ***POA for Taxpayer*** did not have title to the Property (***Lot A***) during the period the improvement was being constructed.
5. ***POA for Taxpayer*** was not an owner-builder.
6. A speculative builder includes an owner-builder who sells, at any time, improved real property consisting of custom homes regardless of the stage of completion. Sec. 100.
7. Improved real property includes any real property upon which a structure has been constructed. Sec. 416(a)(2)(A).
8. The Property was improved real property.
9. Sale of improved real property includes any form of transaction which in substance is a transfer of title of improved real property. Sec. 416(a)(3).
10. Taxpayer sold improved real property when he transferred title to the Property to ***POA for Taxpayer*** and ***Taxpayer***.

11. Taxpayer was a speculative builder during the audit period.
12. Because *POA for Taxpayer* was not an owner-builder, *POA for Taxpayer* was not a speculative builder with respect to the Property (*Lot A*).
13. The warranty deed from Taxpayer to *POA for Taxpayer* and *Taxpayer* did not specify a contract sales price for the Property.
14. Section 210 requires transactions in circumstances where the relationship between the parties is such that the gross income from the transaction is not indicative of the market value of the subject matter of the transaction to be subject to tax based on market value.
15. The Tax Collector used the sale of the subject Property to the final purchaser immediately after the transfer by Taxpayer to *POA for Taxpayer* and *Taxpayer* to determine the market value of the transfer by Taxpayer.
16. The Tax Collector's method for determining the market value of the transfer by Taxpayer to *POA for Taxpayer* and *Taxpayer* was reasonable.
17. It is the responsibility of the taxpayer to prove that the Tax Collector's estimate is not reasonable and correct. Sec. 545(b).
18. The existence of another reasonable basis of estimation does not, in any way, invalidate the Tax Collector's estimate. Sec. 545(b).
19. Taxpayer failed to meet his burden of proving the Tax Collector's estimate of market value for Taxpayer's transfer to *POA for Taxpayer* and *Taxpayer* was not reasonable. Sec. 545(b).
20. An accommodation party is one who signs a commercial paper for the purpose of lending his name and credit to another party to the document, the accommodated party, to help that party obtain a loan or an extension of credit. West's Encyclopedia of American Law, edition 2. Copyright 2008.
21. An accommodation party is liable to the person or business that extended credit to the accommodation party. West's Encyclopedia of American Law, edition 2. Copyright 2008.
22. Contracts between a taxpayer and a third party regarding payment of taxes cannot shift the legal incidence of the tax as between the state (here the City) and the taxpayer. *Continental Inn of Albuquerque, Inc. v. New Mexico Tax. & Rev. Dept.*, 113 N.M. 588, 829 P.2d 946 (1992).
23. The incidence of the tax fell on Taxpayer because he was the speculative builder.
24. A constructive trust is a trust created by operation of law against one who by actual or constructive fraud, by duress or by abuse of confidence, or by commission of wrong, or by any form of unconscionable conduct, or other questionable means, has obtained or holds legal right to property which he should not, in equity and good conscience, hold and enjoy. West's Encyclopedia of American Law, edition 2. Copyright 2008.
25. The existence or non-existence of a constructive trust between Taxpayer and the principals of *Construction Developer* has no impact on Taxpayer's liability for the City's privilege tax.
26. The City's privilege tax assessment against Taxpayer was proper.

Ruling

Taxpayer's protest of the assessment for the period February 2007 made by the City of Scottsdale is denied.

The Taxpayer has timely rights of appeal to the Arizona Tax Court pursuant to Model City Tax Code Section -575.

Sincerely,

Hearing Officer

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c: ***Tax Audit Manager***  
Municipal Tax Hearing Office