

## DECISION OF MUNICIPAL TAX HEARING OFFICER

December 7, 2010

*Taxpayer's Representative*  
*Representative's Address*

*Taxpayer*  
MTHO #562

*Taxpayer's Representative:*

We have reviewed the evidence and arguments presented by *Taxpayer*<sup>1</sup> and the City of Maricopa (Tax Collector or City) at the hearing on September 29, 2010 and in post-hearing memoranda. The review period covered was December 2007. Taxpayer's protest, Tax Collector's response and our findings and ruling follow.

### Taxpayer's Protest

Taxpayer purchased real property (the Property) that included a shell building in the City of Maricopa and leased it back to the seller (Tenant). The lease agreement allowed the Tenant to make improvements to the Property without Taxpayer's consent. Tenant could also repurchase the Property during the first five years of the lease. Tenant made improvements to the Property and then exercised its option to repurchase the Property in December 2007. Taxpayer was assessed City of Maricopa privilege tax under the speculative builder classification for the sale of the Property back to the Tenant because improvements were made while Taxpayer owned the Property.

Tenant did complete the shell and make tenant improvements while Taxpayer held title, but Taxpayer was not a party to any of the construction contracts for finishing the shell or for any of the tenant improvements. Because Taxpayer had no involvement in constructing the improvements, Taxpayer was not a speculative builder when it sold the property back to Tenant.

In addition, Taxpayer sold the property to Tenant more than 24 months after Taxpayer purchased it. Therefore, the sale was exempt from the speculative builder tax. Even if Taxpayer were taxable as a speculative builder, the sales price used by the City was overstated.

### Tax Collector's Response

Taxpayer owned the Property while improvements were constructed. Taxpayer provided the financing for the construction and approved payments to the contractors. Taxpayer therefore had control over the payments. The lease agreement also required that improvements be made in a good workman like manner. Taxpayer met the definition of "speculative builder" and was subject to the City's privilege tax. The tax was based on the sales price of the Property stated in

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<sup>1</sup> The *Trust* was created by *Taxpayers*. Both *Taxpayers* passed away before the assessment was issued. *Taxpayers* and the *Trust* are referred to herein as "Taxpayer".

the sales documents. The Property was sold within 24 months of substantial completion and Taxpayer was therefore not exempt from the privilege tax.

### Discussion

**Big Business Center, LLC** purchased the Property to construct a commercial real estate project. **BBC** had constructed a shell building that was about seventy percent complete. **BBC** sold the Property to Taxpayer in September 2005 to secure financing in order to finish the project by completing the shell and constructing tenant improvements. Taxpayer purchased the Property as a part of an Internal Revenue Code Section 1031 exchange.

At the same time as the sale, Taxpayer leased the Property back to **BBC**. The Lease Agreement provided that **BBC** could make improvements to the Property provided it makes them in good workman like manner. Taxpayer's consent was not required before **BBC** could make any alterations or improvements to the Property. The Lease Agreement did not require **BBC** to make any improvements. The Lease Agreement also gave **BBC** an option to repurchase the Property during the first five years of the lease.

Taxpayer had agreed to provide financing to allow **BBC** to complete the shell and build out the tenant improvements. After leasing the Property, **BBC** completed the shell and made the necessary tenant improvements. **BBC** entered into all construction contracts to complete the shell and construct tenant improvements. Taxpayer was not a party to any of the contracts to complete the shell or construct tenant improvements. Taxpayer did not direct **BBC** to enter into any of the construction contracts. Taxpayer did authorize the borrowed funds to be disbursed to contractors based on instructions from **BBC**.

**BBC** exercised its option to repurchase the Property in December 2007. At that time the shell had been completed and **BBC** was in process of leasing the Property to tenants. The sales price for the repurchase was listed in the affidavit of value as \$4,923,437. The sales price was determined by the amount of money Taxpayer provided.

The Tax Collector audited Taxpayer for the period December 2007 and issued an assessment under the speculative builder classification for city privilege tax in the amount of \$40,437.65, interest through August 2008 in the amount of \$1,752.24 and failure to file and pay penalties in the amount of \$10,109.41. The Tax Collector considered the sale of the Property back to **BBC** to be the sale of improved real property and Taxpayer to be a speculative builder because Taxpayer owned the Property while the improvements were constructed. Taxpayer was aware of the construction and authorized payments to the contractors.

Taxpayer timely protested the assessment arguing it was not a speculative builder under the City tax code. A speculative builder is defined by the code as an owner-builder who sells or contracts to sell, at anytime, improved real property prior to completion or before the expiration of twenty-four (24) months after the improvements of the real property sold are substantially complete.

Taxpayer does not dispute that it owned the Property and that the Property was improved real property. Taxpayer contends it was not an owner-builder when it sold the Property back to **BBC**

because it did not construct any of the improvements. If Taxpayer was not an owner-builder, then Taxpayer does not fall within the definition of a speculative builder.

Taxpayer is correct that to be a speculative builder, a person has to be an owner-builder. 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. Under this definition it takes more than the mere concurrence of ownership and the construction of improvements on the Property for the owner to be an owner-builder.

The fact that Taxpayer owned the Property, provided financing and was aware of the construction of improvements does not mean it was Taxpayer who constructed any improvement, by itself or by or through others. It was the Tenant who constructed the improvements. There was no evidence that the Tenant was acting for or on behalf of Taxpayer.

The Tax Collector contends that Taxpayer was an owner-builder because Taxpayer owned the Property, was aware of the construction and authorized the payments to be made to the contractors making the improvements. The Tax Collector contends that the owner does not have to be the moving force to build improvements to be an owner builder. It is enough that improvements were constructed and the owner was aware of the construction.

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). Statutes 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).

The Tax Collector's argument ignores the wording of the statute. An owner-builder is an owner who constructs any improvement to real property. While Taxpayer was the owner of the Property, Taxpayer was not the one who constructed any improvement, by itself or by or through others. Any doubt must be resolved against the Tax Collector. The Tax Collector has not shown that Taxpayer was an owner-builder and therefore a speculative builder.

Because we hold that Taxpayer was not a speculative builder, it is not necessary to address Taxpayer's other arguments.

#### Findings of Fact

1. Taxpayer purchased the Property from **Best Business Center, LLC (BBC)** in September 2005.
2. The Property is located in the City of Maricopa.
3. The Property included a shell building constructed by **BBC** that was approximately seventy percent complete.
4. **BBC** had purchased the Property in 2004 to construct a commercial real estate project.
5. **BBC** sold the Property to Taxpayer to secure financing in order to complete the project.
6. **BBC** leased back the Property in September 2005.

7. Paragraph 13 of the Lease Agreement provided that tenant **BBC** could make improvements to the Property provided it makes them in good workman like manner.
8. The consent of the landlord (Taxpayer) was not required before **BBC** could make any alterations or improvements to the Property.
9. Whether to make improvements and the nature of the improvements was at the discretion of **BBC**.
10. There were no other agreements between Taxpayer and **BBC** regarding making improvements to the Property.
11. Paragraph 21 of the Lease Agreement gave **BBC** an option to repurchase the Property at a later date for a Repurchase Price defined in Paragraph 35 of the Purchase Agreement.
12. After leasing the Property back, **BBC** completed the shell and made tenant improvements.
13. Taxpayer provided **BBC** financing to complete the shell and build out the tenant improvements.
14. **BBC** entered into all construction contracts to complete the shell and construct tenant improvements.
15. To pay contractors at the Property, **BBC** would tell Taxpayer what needed to be paid and Taxpayer would authorize the release of funds by the bank to pay the contractors.
16. Taxpayer was the owner of the property and authorized payments to be made to contractors from financing it secured.
17. Taxpayer was aware of the construction.
18. Taxpayer was not a party to any of the contracts to complete the shell or construct tenant improvements.
19. Taxpayer did not direct **BBC** to enter into any of the construction contracts.
20. **BBC** was not acting on behalf of Taxpayer.
21. **BBC** entered into lease agreements with tenants who would occupy the Property.
22. **BBC's** first tenant received its certificate of occupancy in May of 2006.
23. Taxpayer was not involved in leasing any portion of the Property to the ultimate tenants.
24. **BBC** exercised its option to repurchase the Property in December 2007.
25. The sales price for the repurchase was listed in the affidavit of value as \$4,923,437.
26. The sales price for the repurchase was determined by the amount of financing Taxpayer had secured to allow **BBC** to complete the shell and make tenant improvements.
27. **BBC** paid the purchase price by an assumption of mortgage, a loan from Taxpayer and a conventional new loan.
28. **BBC** has not paid and still owes Taxpayer \$1.25m on the loan from Taxpayer for its purchase of the Property.
29. The Tax Collector conducted an audit assessment of Taxpayer for the period December 2007.

30. The Tax Collector assessed Taxpayer for city privilege tax under the speculative builder classification in the amount of \$40,437.65, interest through August 2008 in the amount of \$1,752.24 and failure to file and pay penalties in the amount of \$10,109.41.
31. Taxpayer filed a timely Petition to protest the assessment.
32. Taxpayer's protest and supplement to protest stated that Taxpayer was not a speculative builder under the City tax code.

#### Conclusions of Law

1. A speculative builder includes an owner-builder who sells, at any time, improved real property prior to completion or before the expiration of twenty-four (24) months after the improvements of the real property sold are substantially complete. MTC § 8A-100.
2. 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. MTC § 8A-100.
3. To be a speculative builder a person has to be an owner-builder.
4. Taxpayer did not enter into and was not a party to any of the contracts with the contractors who finished the shell building or who constructed the tenant improvements on the Property.
5. **BBC** was not Taxpayer's agent and was not acting on behalf of Taxpayer in constructing the improvements to the Property.
6. 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).
7. 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).
8. Taxpayer was not the person who constructed any improvement on the Property, either by itself or by or through others.
9. Taxpayer was not an owner-builder under MTC § 8A-100.
10. Taxpayer was not a speculative builder when it re-sold the Property to MMBC in December 2007.
11. The City's privilege tax assessment against Taxpayer was not proper with respect to the sale of the Property to **BBC** in December 2007.

#### Ruling

Taxpayer's protest of the assessment dated September 2, 2008 made by the City of Maricopa is granted consistent with Conclusions of Law numbers 10 and 11.

The Tax Collector is directed to abate the assessment and to remove all taxes assessed on *Taxpayer* for the period December 2007.

Both parties have 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 Auditor*  
Municipal Tax Hearing Office