

DECISION OF MUNICIPAL TAX HEARING OFFICER

April 29, 2011

Taxpayer

Taxpayer's Address

Taxpayer
MTHO #611

Dear Taxpayer:

We have reviewed the evidence submitted for redetermination by *Taxpayer* and the City of Mesa (Tax Collector or City). The review period covered was May 2009 through November 2009. Taxpayer's protest, Tax Collector's response, and our findings and ruling follow.

Taxpayer's Protest

Taxpayer was assessed City of Mesa privilege tax under the speculative builder classification based on the trustee's sale of fifty lots Taxpayer owned in the City. A sale by the trustee is not a sale by Taxpayer. Taxpayer did not receive any funds in the sales. The sales in question resulted from foreclosure and Arizona and federal law does not recognize trustee's sales as a sale. Taxpayer was not a speculative builder under the Model City Tax Code.

Tax Collector's Response

Taxpayer was the owner of record to the lots that were sold at the trustee's sale. Taxpayer constructed improvements to the lots. Taxpayer was therefore an owner-builder. A sale includes any form of transaction which in substance is a transfer of title. When the lots were transferred by trustee's deeds, Taxpayer became a speculative builder. The tax base for the sale of the fifty lots was the bid price at auction. Taxpayer is liable for the tax that was assessed.

Discussion

Taxpayer acquired fifty-seven vacant lots in the City. Taxpayer developed the lots, paved the roads and began construction of residential structures. Taxpayer had executed Deeds of Trust on the lots. Between June 2007 and January 2009 Taxpayer sold seven of the lots and reported the sales associated with those sales.

In May, June and November of 2009 the remaining fifty lots were sold at public auction by trustee's deeds pursuant to the Deeds of Trust that had been executed by Taxpayer. The trustee's deeds provided that payment was made either entirely in cash or by the satisfaction, pro tanto, of the obligations then secured by said Deed of Trust, together with the fees, costs and expenses relative thereto. The total combined selling price of all fifty lots was \$2,506,219.

The Tax Collector conducted an audit assessment of Taxpayer for the period May 2009 through November 2009 and issued an assessment under the speculative builder classification. The assessment was based on the total combined sales prices of the lots at the trustee's sales with allowable deductions. Taxpayer timely protested the assessment.

The Mesa Tax Code (MTC) governs whether and to what extent a person is taxable. 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 and the property sold has to be improved real property.

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. Improved real property includes any real property upon which a structure has been constructed. Taxpayer owned the lots and developed the lots, paved the roads and began construction of residential structures. Taxpayer was an owner-builder.

The question presented is whether Taxpayer became a speculative builder when the lots were foreclosed and sold at Trustee's sales. The City argues that when the lots were foreclosed and sold at a Trustee's sales, title transferred from Taxpayer to the purchaser. At that point Taxpayer became a speculative builder subject to the City's privilege tax.

MTC § 5-10-416 provides that the sale of improved real property includes any form of transaction which in substance is a transfer of title of improved real property. There clearly was a transfer of title when the lots were sold at the trustee's sales. The foreclosure and sale of the lots resulted in satisfaction of some or all of Taxpayer's obligations under the Deeds of Trust. This is no different than if Taxpayer had sold the lots and used the proceeds to pay the Deeds of Trust. Taxpayer was a speculative builder and the privilege tax was measured by the amount realized at each trustee's sale.

Taxpayer's reference to definitions of the term "sale" from other sources is not applicable here. The Mesa Tax Code defines sale for purposes of the Mesa privilege tax. A statute is to be read and applied in accordance with any special statutory definitions of the terms it uses. Since the Mesa Tax Code has defined the term "sale" for purposes of the City privilege tax, that is the definition we must use.

Taxpayer also argued that it did not receive any funds in the sales. Under A.R.S. § 33-812.A.2. the proceeds of a trustee's sale are to be applied to the payment of the contract secured by the trust deed after the costs of the sale have been paid. Gross income under the Mesa Tax Code includes the reduction of indebtedness. MTC § 5-10-200(a)(3). Even if Taxpayer did not directly receive the proceeds from the trustee's sales, Taxpayer benefited by having its debt under the Deeds of Trust reduced.

Taxpayer cited the United States Supreme Court case in *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 114 S.Ct. 1757 (1994) for the proposition that a foreclosure sale is not at fair market value. In that case the Court held that the term "reasonably equivalent value" for foreclosed real property is the price in fact received at the foreclosure sale, so long as all the requirements of the State's foreclosure law have been complied with. There has been no contention that legal requirements were not followed here. In any event, the assessment was not based on the fair market value of the lots but on the sales price received at the auction. Nothing in *BFP v. Resolution Trust Corp.* would preclude the Tax Collector from basing the assessment on the sales price received at the trustee's sales.

Based on all the above, Taxpayer's protest is denied.

Findings of Fact

1. Taxpayer purchased fifty-seven vacant lots located in the City.

2. Taxpayer executed Deeds of Trust on the lots to secure financing.
3. Taxpayer developed the lots, paved the roads and began construction of residential structures.
4. Between June 2007 and January 2009 Taxpayer sold seven of the lots and reported the sales associated with those sales.
5. The remaining fifty lots were foreclosed and in May, June and November of 2009 the lots were sold at trustee's sales.
6. The trustee's deeds provided that payment was made either entirely in cash or by the satisfaction, protanto, of the obligations secured by the Deed of Trust, together with the fees, costs and expenses of the sales.
7. The total combined selling price of all fifty lots was \$2,506,219.
8. The Tax Collector conducted an audit assessment of Taxpayer for the period May 2009 through November 2009 and issued an assessment dated September 29, 2010 for city privilege tax under the speculative builder classification in the amount of \$27,606.56, penalties in the amount of \$6,591.65, interest through August 31, 2010 in the amount of \$918.45 and license fees in the amount of \$30.00.
9. The assessment was based on the lots' combined sales price of \$2,506,219 received at the trustee's sales.
10. The assessment allowed the 35% contractor deduction and deductions for factored tax and impact fees.
11. Taxpayer timely protested the assessment and requested a redetermination.

Conclusions of Law

1. 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. MTC § 5-10-100.
2. Improved real property includes any real property upon which a structure has been constructed, MTC § 5-10-416(a)(2)(A) or where water, power, and streets have been constructed to the property line, MTC § 5-10-416(a)(2)(D).
3. Taxpayer's lots were improved real property.
4. 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 § 5-10-100.
5. Taxpayer was the owner of the lots and had an improvements constructed on the lots.
6. Taxpayer was an owner-builder.
7. Sale of improved real property includes any form of transaction which in substance is a transfer of title of improved real property. MTC § 5-10-416(a)(3).
8. A statute is to be read and applied in accordance with any special statutory definitions of the terms it uses. *State v. Hazlett*, 205 Ariz. 523, 73 P.3d 1258 (App. 2003).

9. The appropriate definition of sale to be used in this case is the one found in MTC § 5-10-416(a)(3).
10. The trustee's sales transferred title to the lots from Taxpayer to the purchasers.
11. The trustee's sales were sales of improved real property.
12. Taxpayer was a speculative builder during the audit period subject to the City's privilege tax.
13. Gross income under the Mesa Tax Code includes the reduction of indebtedness. MTC § 5-10-200(a)(3).
14. The proceeds of a trustee's sale are to be applied to the payment of the contract secured by the trust deed after the costs of the sale have been paid. A.R.S. § 33-812.A.2.
15. Taxpayer received income by virtue of the trustee's sales.
16. The City's assessment of privilege tax, penalty, license fee and interest against Taxpayer was proper.

Ruling

Taxpayer's protest of an assessment of privilege tax and interest made by the City of Mesa for the period May 2009 through November 2009 is denied consistent with Conclusion of Law number 15.

The Tax Collector's Notice of Assessment to Taxpayer dated September 29, 2010 for the period May 2009 through November 2009 is upheld.

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 Administrator***
Municipal Tax Hearing Office