

## DECISION OF MUNICIPAL TAX HEARING OFFICER

October 20, 2014

*Taxpayer's Representative*  
*Address of Representative*

*Taxpayer - Avondale, LLC*  
MTHO #823

*Dear Representative:*

We have reviewed the evidence presented by *Taxpayer - Avondale, LLC* and the City of Avondale (Tax Collector or City) at the hearing on September 24, 2014. The review period covered was August 1, 2011 through November 30, 2013. Taxpayer's protest, Tax Collector's response, and our findings and ruling follow.

### Taxpayer's Protest

Taxpayer was assessed City of Avondale privilege tax under the commercial lease classification for the lease of real property owned by Taxpayer to *Brand-new Traditional Charter School (Brand-new)*. *Brand-new* is an Arizona non-profit corporation. Under the lease agreement *Brand-new* is required to pay the tax. Legacy is a "public education entity" and is exempt from tax under Avondale Tax Code (ATC) Section 13A-270(b). Therefore Taxpayer's lease of real property to Legacy is exempt from the City's privilege tax.

### Tax Collector's Response

The Taxpayer in this case is *Taxpayer - Avondale, LLC*, a for-profit limited liability company. The City Code imposes the tax on the lessor, not the tenant. While the lessor may pass the burden of the tax to the tenant, the lessor cannot shift its tax liability to the tenant. The City Code does not provide for an exemption to a lessor leasing real property to a charter school. ATC § 13A-270 does not exempt Taxpayer's lease of the real property to *Brand-new*. The City's assessment should be upheld.

### Discussion

Taxpayer leases real property to *Brand-new*, an Arizona charter school. The Tax Collector conducted an audit assessment of Taxpayer for the period August 1, 2011 through November 30, 2013 and issued an assessment. The Tax Collector considered Taxpayer taxable under the commercial lease classification. Taxpayer timely protested the assessment stating it was leasing the property to a charter school and that the charter school is an agency of the state. The lease is therefore exempt under ATC § 13A-270.

ATC § 13A-270 provides for an exclusion of gross income of persons deemed not engaged in business. Paragraph (a)(5) provides definitions for the purposes of the section, including "Public Educational Entity". Subsection (b) then provides:

(b) Transactions which, if conducted by any other person, would produce gross income subject to tax under this Chapter shall not be subject to the imposition of such tax if conducted entirely by a public educational entity; governmental entity, except "proprietary activities" of municipalities as provided by Regulation; or non-licensed business.

Taxpayer contends that subsection (b) intends to provide a benefit to transactions involving a public educational entity and should be read to exclude "transactions" with a public educational entity from the tax. Taxpayer contends that the City's interpretation will result in unintended consequences that will benefit taxable entities and not exempt organizations.

ATC § 13A-270 is an exemption statute. Statutes granting deductions and exemptions from tax are to be strictly construed against the deduction or exemption. If there is any doubt, the exemption does not apply. In addition, no clause, sentence, or word should be rendered superfluous, void, contradictory or insignificant. *State v. Superior Court for Maricopa County*, 113 Ariz. 248, 550 P.2d 626 (1976).

The plain language of subsection (b) exempts certain transactions conducted by a person who would be receiving income that would otherwise be subject to the privilege tax. The City privilege tax is a tax on the persons engaging in business measured by their income from the business and not a tax on the customer. Here, **Brand-new** is the lessee and pays rent. The transaction does not produce any income to **Brand-new** that might otherwise be subject to the City privilege tax.

While a business may pass the cost of the tax onto its customers, a business remains liable for the tax whether or not the cost of the tax was passed on. The business remains liable for the tax even if the customer is a governmental entity such as the state or the federal government. For example, in *City of Tempe v. Del E. Webb Corporation*, 13 Ariz.App. 597, 480 P.2d 18 (1971) the court held that a city may impose a transaction privilege tax on an independent contractor notwithstanding the construction contracts were with a state agency for construction to be performed on the campus of a state university located within the municipality. 13 Ariz.App. at 599, 480 P.2d at 20. The court stated when it overruled a prior case that had allowed a contractor an exemption for a transaction with the state Board of Regents, 13 Ariz.App. at 599, 480 P.2d at 20:

Furthermore, we are of the opinion that the rationale of Ashton is completely antithetic to the pronouncement of our Arizona Supreme Court in *Arizona State Commission v. Garrett Corporation*, supra, wherein the court, indulging in the assumption that the economic burden of the tax was upon the United States, stated:

'Regardless of where the burden rests, the decisive test under the class of taxing Acts (Business Privilege Tax) now under consideration is where does the legal incidence of the tax fall.'  
79 Ariz. at 395, 291 P.2d at 212.

Here, **Brand-new** is not the taxpayer but the lessee (customer) of Taxpayer. **Brand-new** does not receive any income from the transaction to which ATC § 13A-270 could apply. Taxpayer has not cited any authority that would exempt it from the privilege tax here. The City's assessment is therefore upheld.

Taxpayer's argument that imposing the tax results in a conclusion not contemplated by the code or is unwise does not mandate a different result. Under the clear language of ATC § 13A-270(b), an exemption could only apply if **Brand-new** were the lessor and not the lessee. It is not relevant to a determination under a statute enacted by the legislature whether the statute may be unwise or undesirable. It is for the legislature to balance the advantages and disadvantages of legislation.

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 is a limited liability company.
2. Taxpayer owned real property (Property) within the City.
3. Taxpayer leased the Property to **Brand-new**, an Arizona charter school.
4. The lease required **Brand-new** to pay the cost of any privilege tax imposed on Taxpayer as a result of the lease.
5. **Brand-new** is an Arizona a non-profit corporation.
6. Taxpayer did not pay City privilege tax on its gross receipts from the lease of the Property to **Brand-new**.
7. The Tax Collector conducted an audit assessment of Taxpayer for the period August 1, 2011 through November 30, 2013 and issued an assessment.
8. The Tax Collector considered Taxpayer taxable under the commercial lease classification.
9. Taxpayer timely protested the assessment.
10. Taxpayer believes its lease of the Property to a charter school is exempt from City privilege tax under ATC § 13A-270(b).

#### Conclusions of Law

1. Avondale Tax Code § 13A-445 imposes the city privilege tax on the business activity of renting, leasing or licensing for use real property located in the City.
2. ATC § 13A-270(b) provides that transactions which, if conducted by any other person, would produce gross income subject to tax under this Chapter shall not be subject to the imposition of such tax if conducted entirely by a public educational entity; governmental entity, except "proprietary activities" of municipalities as provided by Regulation; or non-licensed business.
3. The law will be given, whenever possible, such an effect that no clause, sentence, or word is rendered superfluous, void, contradictory or insignificant. *State v. Superior Court for Maricopa County, supra.*
4. Tax deductions and exemptions are to be strictly construed against the deduction or exemption. *Arizona Department of Revenue v. Raby*, 204 Ariz. 509, 511, 65 P.3d 458 (App. 2002).
5. Taxpayer has the burden to show he is entitled to an exemption or deduction from taxation.

- Ebasco Servs., Inc. v. Ariz. State Tax Comm'n*, 105 Ariz. 94, 99, 459 P.2d 719, 724 (1969).
6. The City privilege tax is a tax on the person engaging in business and not a tax on the customer. *See, City of Tempe v. Del E. Webb Corporation, supra*.
  7. A business may, but is not required to, pass the cost of the tax onto its customers. *City of Tempe v. Del E. Webb Corporation, supra*.
  8. A taxpayer is liable for the tax whether or not the taxpayer passes the cost of the tax onto its customers. *City of Tempe v. Del E. Webb Corporation, supra*.
  9. 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).
  10. It is not relevant to a determination under a statute enacted by the legislature whether the statute may be unwise or undesirable. It is for the legislature to balance the advantages and disadvantages of legislation. *See, Arizona Downs v. Ariz. Horsemen's Foundation*, 130 Ariz. 550, 637 P.2d 1053 (1981).
  11. Taxpayer's lease of the Property to **Brand-new** is subject to the City's privilege tax under ATC § 13A-445 and is not exempt under ATC § 13A-270.
  12. The City's privilege tax assessment against Taxpayer is upheld.

### Ruling

The protest by Taxpayer of an assessment made by the City of Avondale for the period August 1, 2011 through November 30, 2013 is denied.

The Tax Collector's Notice of Assessment is upheld.

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 Supervisor**  
Municipal Tax Hearing Office