

DECISION OF MUNICIPAL TAX HEARING OFFICER

Decision Date: May 17, 2007
Decision: MTHO #341
Taxpayer: *Taxpayer*
Tax Collector: City of Mesa
Hearing Date: March 14, 2007

DISCUSSION

Introduction

On October 20, 2006, *Taxpayer* (“Taxpayer”) filed a protest of a tax assessment made by the City of Mesa (“City”). After review, the City concluded on December 28, 2006, that the protest was timely and in the proper form. On January 3, 2007, the Municipal Tax Hearing Officer (“Hearing Officer”) classified the matter as a redetermination and ordered the City to file a response to the protest on or before February 20, 2007. On January 15, 2007, Taxpayer requested this matter be reclassified as a hearing. On January 20, 2007, the Hearing Officer reclassified this matter as a hearing. On February 2, 2007, the City filed a response. On February 6, 2007, the Hearing Officer ordered Taxpayer to file any reply on or before February 27, 2007. On February 12, 2007, a Notice of Tax Hearing (“Hearing”) scheduled the matter for hearing commencing on March 14, 2007. Both parties appeared and presented evidence at the March 14, 2007 hearing. On March 15, 2007, the Hearing Officer indicated the parties had agreed to the following schedule: Taxpayer would provide documentation to the City on or before April 13, 2007 to support taxes paid to the General Contractor; the City would review the documentation and provide any recommendations on or before April 27, 2007; and, Taxpayer would file any reply on or before May 4, 2007. On April 25, 2007, the City filed recommended adjustments. On April 30, 2007, Taxpayer filed a reply. On May 3, 2007, the Hearing Officer indicated the record was closed and a written decision would be issued on or before June 18, 2007.

City Position

The City performed an audit of the Taxpayer for the month of October 2003. The City concluded Taxpayer consisted of a husband and wife engaged in speculative builder activity. The City taxed Taxpayer’s sale of a home located at **Property 123** (“Property”) pursuant to City Code Section 5-10-416 (“Section 416”). The City assessed Taxpayer for taxes due of \$8,342.66, penalties for failing to timely file and timely pay totaling \$2,085.67, and interest up through October 31, 2006 of \$2,504.95. According to the City, Taxpayer had a house built on the Property with a certificate of occupancy (“Certificate”) issued on July 11, 2002. The City indicated Taxpayer entered into an Exclusive Right to Sell contract on January 8, 2003. The Property was sold on October 29, 2003. As a result,

the City concluded Taxpayer was a speculative builder as defined in City Code Section 5-10-100 (“Section 100”) since the Property was sold before the expiration of twenty-four months after the improvements were substantially complete. The City noted that City Regulation 5-10-416.1 (“Regulation 416.1”) provides for a homeowner’s bona fide non-business sale of a family residence. A sale would be a non-taxable sale pursuant to Regulation 416.1 if “ the property was actually used as the principal place of family residence or vacation residence by the immediate family of the seller for the six (6) months next prior to the offer for sale”.... In this case, the offer for sale occurred less than six months after the Certificate was issued. Accordingly, the City concluded the Regulation 416.1 exemption did not apply.

In response to Taxpayer, the City argued Taxpayer was in “business” when they sold the Property since the sale was entered into with the object of benefit or advantage. Based on testimony from Taxpayer, the Property would have been foreclosed if it hadn’t been sold. The City noted a business activity did not have to have a profit objective.

The City reviewed additional documentation provide by Taxpayer after the hearing that demonstrated contractors working on the construction of the Property had been paid taxes by Taxpayer. As a result, the City recommended a City tax credit as well as a deduction for state/county taxes which reduced the original tax assessed from \$8,342.66 to \$6,166.92. The City also made corresponding adjustments to penalties and interest resulting in a total amount due as of October 31, 2006 of \$9,618.41.

Taxpayer Position

Taxpayer protested the entire assessment amount. Taxpayer indicated the sale of the Property was the sale of their personal residence. Taxpayer asserted they hired a General Contractor to supervise construction of the home and then due to a financial hardship, Taxpayer indicated they had to sell the Property. Taxpayer argued that the sale was absolutely not a speculative sale. According to Taxpayer, the City ordinance was written for people whose business is to build and sell homes. Taxpayer asserted they were not in that business but were forced to sell the Property rather than have it being foreclosed on. Section 100 defines “business” as “all activities or acts, personal or corporate, engaged in and caused to be engaged in with the object of gain, benefit, or advantage, either direct or indirect, but not causal activities of sales.” Taxpayer argued they were not engaged in business as they had no profit motive and recognized no gain on the sale of the Property.

Taxpayer asserted that if they were in the business of building speculative homes, they would have simply waited a couple of days to sign a contract to sell the Property after the full “six months” set forth in Regulation 416.1 had expired. Taxpayer argued the “six month” period was vague as to what it actually meant as far as the number of days. According to Taxpayer, the Certificate was actually issued on July 10, 2002 which meant Taxpayer lived in the home for 180 days prior to offering the home for sale. It is not clear that the term “six months” was meant “date X of month 1 to the same date of the sixth month from such date”.

ANALYSIS

Taxpayer had a home constructed on property located at *Property 123*. Based on the Certificate, the improvements were completed on July 11, 2002. The improved real property was sold on October 29, 2003. As a result, Taxpayer was a speculative builder pursuant to Section 100. Section 416 provides for a tax on every person engaging in “business” as a speculative builder in the City. “Business” is broadly defined in Section 100 as all activities engaged in with the object of gain, benefit, or advantage, either direct or indirect, but not casual activities or sales. While there was no evidence that Taxpayer entered into the sale for a profit, we do conclude there was a benefit or advantage, either direct or indirect, to Taxpayer to sell the Property. It is also clear from the definition of “casual sale” that a sale of real property can not be considered as a casual sale. While it may not have been Taxpayer’s intent to enter into a speculative builder activity, we conclude the sale of the property was a taxable speculative builder sale pursuant to Section 416. We also find it was proper for the City to reduce the tax assessment to \$6,166.92 after review of additional documentation provided by Taxpayer.

The next issue was whether or not the sale of the Property would not be subject to the tax as a “homeowner’s bona fide non-business sale”. We think not. We conclude the Property was used as a principal place of family residence commencing on the July 11, 2002 date the Certificate was issued. Since Regulation 416.1 referred to a six month period and not a period of 180 days as used in other parts of the City Code, we conclude Taxpayer would have had to offer the Property for sale on or after January 11, 2003 in order to meet the requirements set forth in Regulation 416.1. The contract to offer the Property for sale occurred on January 8, 2003. As a result, Taxpayer did not qualify for the exempt “homeowner’s bona fide non-business sale”.

Since Taxpayer failed to timely file a report or timely pay taxes, the City was authorized to assess penalties pursuant to City Code Section 5-10-540 (“Section 540”). Those penalties may be waived when a taxpayer demonstrates “reasonable cause” for failing to timely file and timely pay. We find Taxpayer was unaware of the speculative builder tax and as a result has demonstrated “reasonable cause” to have the penalties waived. Accordingly, all penalties are waived in this matter.

FINDINGS OF FACT

1. On October 20, 2006, Taxpayer filed a protest of a tax assessment made by the City.
2. After review, the City concluded on December 28, 2006, that the protest was timely and in the proper form.
3. On January 3, 2007, the Hearing Officer classified the matter as a redetermination and ordered the City to file any response on or before February 20, 2007.

4. On January 15, 2007, Taxpayer requested the matter be reclassified as a hearing.
5. On January 20, 2007, the Hearing Officer reclassified the matter as a hearing.
6. On February 2, 2007, the City filed a response to the protest.
7. On February 6, 2007, the Hearing ordered Taxpayer to file any reply on or before February 27, 2007.
8. On February 12, 2007, a Notice scheduled the matter for hearing commencing on March 14, 2007.
9. On March 8, 2007, Taxpayer filed a reply.
10. Both parties appeared and presented evidence at the March 14, 2007 hearing.
11. On March 15, 2007, the Hearing Officer indicated the parties had agreed to the following schedule: Taxpayer would provide documentation to the City by April 13, 2007 to support taxes paid to the General Contractor; the City would review the documentation and provide any recommendations on or before April 27, 2007; and, Taxpayer would file any reply on or before May 4, 2007.
12. On April 25, 2007, the City filed recommended adjustments.
13. On April 30, 2007, Taxpayer filed a reply.
14. On May 3, 2007, the Hearing Officer indicated the record was closed and a written decision would be issued on or before June 18, 2007.
15. The City performed an audit of Taxpayer for the month of October 2003.
16. The City concluded Taxpayer consisted of a husband and wife engaged in speculative builder activity.
17. The City taxed Taxpayer's sale of the Property.
18. The City assessed Taxpayer for taxes due of \$8,342.66, penalties for failing to timely file and timely pay totaling \$2,085.67, and interest up through October 31, 2006 of \$2,504.95.
19. Taxpayer had a house built on the Property with a Certificate issued on July 11, 2002.
20. Taxpayer entered into an Exclusive Right to Sell contract on January 8, 2003.

21. The Property was sold on October 29, 2003.
22. Taxpayer hired a General Contractor to supervise construction of the home.
23. The General Contractor had paid some City taxes and some state/county taxes on the construction of the home.
24. After review of additional documentation provided by Taxpayer, the City recommended a City tax credit in the amount of \$2,087.55 and a deduction for state/county taxes paid which reduced the original tax assessment from \$8,342.66 to \$6,166.92.
25. The City made corresponding adjustments to penalties and interest resulting in a total amount due as of October 31, 2006 of \$9,618.41.
26. Due to financial hardships, Taxpayer had to sell the Property.
27. Taxpayer was unaware of the speculative builder tax or the “six month safe harbor” period set forth in Regulation 416.1

CONCLUSIONS OF LAW

1. Pursuant to ARS Section 42-6056, the Municipal Tax Hearing Officer is to hear all reviews of petitions for hearing or redetermination under the Model City Tax Code.
2. During the audit period, Taxpayer was a speculative builder pursuant to Section 100.
3. Taxpayer engaged in “business” as a speculative builder pursuant to Section 100 and Section 416.
4. Taxpayer’s sale of the Property did not constitute a “homeowner’s bona fide non-business sale” pursuant to Regulation 416.1.
5. The City was authorized to assess penalties pursuant to Section 540 for failing to timely file and timely pay.
6. Taxpayer demonstrated “reasonable cause” to have the penalties waived.
7. It was proper for the City to reduce the assessment by allowing a tax credit and deduction for taxes paid by the General Contractor.
8. Taxpayer’s protest should be partly granted and partly denied, consistent with the Discussion, Findings, and Conclusions, herein.

ORDER

It is therefore ordered that the October 20, 2006 protest of *Taxpayer* of a tax assessment made by the City of Mesa is hereby partly granted and partly denied, consistent with the Discussion, Findings, and Conclusions, herein.

It is further ordered that the City of Mesa shall revise its assessment to include the proposed adjustments set forth in the City's April 25, 2007 letter.

It is further ordered that the City of Mesa shall waive all penalties assessed in this matter.

It is further ordered that this Decision is effective immediately.

Jerry Rudibaugh
Municipal Tax Hearing Officer