

DECISION OF MUNICIPAL TAX HEARING OFFICER

Decision Date: January 14, 2013

Decision: MTHO # 723

Taxpayer:

Tax Collector: City of Phoenix

Hearing Date: September 26, 2012

DISCUSSION

Introduction

On June 1, 2012, *Taxpayer* filed a letter of protest for a tax assessment made by the City of Phoenix (“City”). A hearing was commenced before the Municipal Tax Hearing Officer (“Hearing Officer”) on September 26, 2012. Appearing for Taxpayer were their *representatives*. Appearing for the City were a *Senior Tax Auditor* and the *Assistant City Attorney*. At the conclusion of the hearing, the parties agreed to a briefing schedule. On November 29, 2012, the Hearing Officer closed the record and indicated a written decision would be issued on or before January 14, 2013.

DECISION

On April 23, 2012, the City issued an assessment to Taxpayer for additional taxes in the amount of \$516,851.73, interest up through March 2012 in the amount of \$79,887.07, penalties in the amount of \$129,213.00, and license fees in the amount of \$20.00. The audit period was from December 2006 through September 2008. The assessment was based on a speculative builder sale pursuant to City Code Section 14-416 (“Section 416”).

Taxpayer owned property which was located on a Maricopa County island parcel (“County Parcel”) known as *The Ranch*. Taxpayer was also a subsidiary of *Be More Fit, Inc.* (“*BMF*”). Taxpayer contracted with an affiliated entity, *Big Construction, LLC*, (“*BC*”) to construct a fitness center on *The Ranch*. On December 20, 2006 the Certificate of Occupancy (“COO”) was issued for the fitness center. The fitness center was leased by Taxpayer to another related entity, *The Ranch Club Operations Company* (“*TR Club*”) from December 2006 through September 2008. On September 26, 2008, Taxpayer sold the improved *The Ranch* to *The Ranch FIT (AZ-MD), LLC* (“*The Ranch Fit*”) for \$32,397,878.00. The City assessed the sale as a taxable speculative builder sale.

The City passed Ordinance No. G-4848 annexing *The Ranch* property on December 13, 2006. Pursuant to Arizona Revised Statutes Section 9-471(D) (“Section 471”), the annexation became effective thirty days after the adoption of the ordinance or January 12, 2007.

Taxpayer argued that Section 416 requires two components by the same owner-builder to occur within the City. Taxpayer asserted that the owner-builder must first improve real property and then the owner-builder must sell the improved real property within twenty-four months of substantial completion. In this case, Taxpayer indicated the improvements were made while *The Ranch* property was located in a county island and thus the sale was not taxable by the City.

The City disagreed with Taxpayer’s conclusion that Section 416 requires two components. The City asserted the sole taxable triggering event was the sale of real property. Since the sale occurred within the City, the City assessed a speculative builder tax on Taxpayer.

Section 416 provides as follows: “(a) The tax shall be equal to ----- percent of the gross income from the business activity upon every person engaging or continuing in business as a speculative builder within the City. (1) The gross income of a speculative builder considered taxable shall include the total selling price from the sale of improved real property at the time of closing of escrow or transfer of title....”

Section 416 goes on to define “improved real property” to mean real property upon which a structure has been constructed. It is clear in this case that Taxpayer had constructed a structure on *The Ranch* which constituted improved real property. It is also clear that there has been a sale of the improved real property within the City. Is that enough to authorize the City to impose a speculative builder tax on Taxpayer? We think not. The tax is imposed on the “gross income from the business activity of engaging in the business as a speculative builder within the City.” City Code Section 14-100 (“Section 100”) defines a “speculative builder” as an owner-builder who sells or contracts to sell improved real property. Section 100 further defines “owner-builder” as an owner who has constructed any improvements to real property. It’s clear from the code that a speculative builder is an owner-builder that has constructed improvements to real property. In this case, Taxpayer was a speculative builder of the fitness center at *The Ranch*. This construction of improvements to real property is the business activity of engaging in the business as a speculative builder which is referred to in Subsection (a) of 416. In turn, the Code in Subsection (a)(1) provides that the measurement of this business activity shall be the selling price of the improved real property. Normally, the business activity and the sale of improved real property both occur in the same City. This case is different because the business activity occurred in the County and the sale occurred after the property was annexed into the City. Because the business activity did not occur in the City, Subsection 416(a) does not apply to the Taxpayer’s sale of the improved *The Ranch* property. Even if we accept the City’s focus on the sale referred to in Subsection (a)(1), there is an ambiguity from Subsection (a) referring to gross income from the business activity of engaging in business as a speculative builder. It does not refer to the business activity of

sale of improved property. In fact, the City argument would make Subsection (a) not necessary as we would go directly to Subsection (a)(1) and the sale of improved real property. The law requires ambiguities in tax statutes to be resolved in favor of the taxpayer. Based on all the above, Taxpayer's protest of the speculative builder assessment should be granted, consistent with the Discussion, Findings, and Conclusions, herein.

FINDINGS OF FACT

1. On June 1, 2012, Taxpayer filed a letter of protest for a tax assessment made by the City.
2. On April 23 2012, the City issued an assessment to Taxpayer for additional taxes in the amount of \$516,851.73, interest up through March 2012 in the amount of \$79,887.07, penalties in the amount of \$129,213.00, and license fees in the amount of \$20.00.
3. Taxpayer owned property which was located on a County Parcel known as ***The Ranch***.
4. Taxpayer was a subsidiary of ***Be More Fit***.
5. Taxpayer contracted with an affiliated entity, ***Big Construction***, to construct a fitness center on ***The Ranch***.
6. On December 20, 2006, the COO was issued for the fitness center.
7. The fitness center was leased by Taxpayer to another related entity, ***TR Club***, from December 2006 through September 2008.
8. The City passed Ordinance No. G-4848 annexing ***The Ranch*** on December 13, 2006.
9. The annexation of ***The Ranch*** became effective on January 12, 2007.
10. On September 26, 2008, Taxpayer sold the improved ***The Ranch*** to ***The Ranch Fit*** for \$32,397,878.00.

11. The City assessed the sale of the improved *The Ranch* as a speculative builder sale in the City.

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. City Code Section 416 imposes a tax on the selling price from the sale of improved real property in the City.
3. Taxpayer was an owner-builder for *The Ranch* property pursuant to Section 100.
4. Since Taxpayer was an owner-builder who contracted to sell improved real property, Taxpayer was a speculative builder pursuant to Section 100.
5. The construction of improvements to real property is the business activity of engaging in the business as a speculative builder pursuant to Subsection 416(a).
6. The measurement of the business activity of engaging in the business as a speculative builder is the selling price of the improved real property pursuant to Subsection 416(a)(1).
7. The business activity of engaging in the business as a speculative builder for *The Ranch* property occurred in the county.
8. Because the business activity occurred in the county, the sale of the improved *The Ranch* property was not taxable by the City.
9. The law requires any ambiguity in tax statutes to be resolved in favor of the taxpayer.
10. Taxpayers protest of the speculative builder assessment should be granted, consistent with the Discussion, Findings, and Conclusions, herein.
11. The parties have timely appeal rights pursuant to Model City Tax Code Section 575.

ORDER

It is therefore ordered that the June 1, 2012 protest by *Taxpayer* of a speculative builder tax assessment made by the City of Phoenix is hereby granted, consistent with the Discussion, Findings, and, Conclusions, herein.

It is further ordered that the City of Phoenix shall revise the assessment by removing all speculative builder tax assessment as well as all associated penalties and interest.

It is further ordered that this Decision is effective immediately.

Municipal Tax Hearing Officer