



## TAXPAYER INFORMATION RULING LR 19-003

Douglas A. Ducey  
Governor

Carlton Woodruff  
Interim Director

March 18, 2019

Thank you for your letter dated January 18, 2019, requesting a taxpayer information ruling (“TIR”) on behalf of your unnamed client (“Taxpayer”). Specifically, you requested a ruling for a determination of whether the sale of four parcels of property is subject to the speculative builder tax.

Pursuant to Arizona Revised Statutes (“A.R.S.”) § 42-2101, the Arizona Department of Revenue (“Department”) may issue TIRs to taxpayers and potential taxpayers on request. Pursuant to A.R.S. 42-6005(B), when the state statutes and Model City Tax Code (“MCTC”) are the same and where the Department has issued written guidance, the Department's interpretation is binding on cities and towns. In all other situations, interpretation of the Model City Tax Code is the sole purview of Municipal Tax Code Commission or its designee.<sup>1</sup>

### ISSUE:

Whether Taxpayer's sale of four parcels of property that were not improved after purchase is subject to the speculative builder tax under the MCTC § -416.

### RULING:

#### The Department Rules as follows:

Generally, to be considered a speculative builder tax under MCTC § -416, a taxpayer must have performed either through itself or through others certain types of real property improvement subsequent to the purchase of the property. In this case, Taxpayer purchased three parcels of property in 2009 and a fourth property in 2014. Taxpayer only performed maintenance work on the properties between the time of purchase and now. Taxpayer did not subdivide or re-parcel the parcel or add any structures or other improvement to the property. It held and maintained the property in accordance with local government requirements. As a result, Taxpayer is not a speculative builder as defined in MCTC Reg. § -416(a).

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<sup>1</sup> For the purposes of this ruling, neither the state transaction privilege tax nor county excise tax is under consideration.

**SUMMARY OF FACTS:**

The following is a summary of the relevant facts based on your letter dated January 18, 2019, and subsequent correspondence with the Department on February 7, 2019:

Taxpayer is in the real estate business in Arizona. In 2009 Taxpayer purchased improved real property consisting of three (3) contiguous vacant commercial urban property ("lots") within \*\*\* in a City which has a tax pursuant to the MCTC. In 2014 Taxpayer acquired an additional contiguous parcel. The additional parcel as acquired was also existing improved real property consisting of vacant commercial urban property. No structures were added to the parcels. The parcels were not subdivided. Paving existed prior to acquisition and only weed control as required by the governmental units was performed subsequent to acquisition. Water, power and streets already existed on the lots for a very substantial time

Taxpayer may sell all of the properties in their current state in the coming months.

**DISCUSSION AND LEGAL ANALYSIS:**

The MCTC was created in order to impose and administer city privilege taxes. City privilege taxes are imposed "upon persons on account of their business activities." See MCTC § -400(a)(1). All Arizona cities generally follow the MCTC in the imposition of their privilege taxes based upon their local ordinances. However, certain options exist, allowing each city to alter or qualify the imposition of its privilege tax.

MCTC § -416(a) imposes the city privilege tax on the gross income derived from engaging in business as a *speculative builder* within a city. MCTC § -416(a)(1) provides that a speculative builder's taxable gross income includes the total selling price from the sale of "improved real property" at the time of closing of escrow or transfer of title. MCTC § -416(a)(2) defines "improved real property" as real property:

- (A) upon which a structure has been constructed; or
- (B) where improvements have been made to land containing no structure (such as paving or landscaping); or
- (C) which has been reconstructed as provided by Regulation; or
- (D) where water, power, and streets have been constructed to the property line.

MCTC § -100 defines a "speculative builder" as:

- 1) an owner-builder who sells or contracts to sell, at any time, improved real property (as provided in MCTC § -416, above) consisting of:

- a) custom, model, or inventory homes, regardless of the stage of completion of such homes; or
  - b) improved residential or commercial lots without a structure; or
- 2) an owner-builder who sells or contracts to sell improved real property, other than improved real property specified in subsection (1) above:
- a) prior to completion; or
  - b) before the expiration of twenty-four (24) months after the improvements of the real property sold are substantially complete.

MCTC § -100 defines “substantially complete” as construction contracting or reconstruction contracting where, among other things, the Certificate of Occupancy or its equivalent has been issued. MCTC § -100 also defines "owner-builder" as “an owner or lessor of real property who, by himself or by or through others, constructs or has constructed ... any improvement to real property.”

As an initial consideration, Taxpayer must be an owner-builder selling certain improved real property as defined to be held responsible under MCTC § -416(a) for the speculative builder tax.

The term owner-builder includes situations where owners perform the work themselves as well as where the owner engages contractors to do the work, i.e. where the owner does the construction work “through others.” “... [I]n ordinary English this phrase is equivalent to constructs or has someone else construct ... any improvement to real property.”<sup>2</sup> In this case, Taxpayer is not an owner-builder because although it owns the parcels of property no improvements were performed on those parcels subsequent to purchase. Taxpayer only performed maintenance work as required by local government agencies.

Taxpayer does not meet the definition of a speculative builder under the terms of subsection 1 of the definition detailed in MCTC § -100 because it is not selling custom, model or inventory homes; nor is it selling improved residential or commercial lots without a structure.

As noted, MCTC § -416(a)(2) defines “improved real property” as property:

- (A) upon which a structure has been constructed; or
- (B) where improvements have been made to land containing no structure (such as paving or landscaping); or
- (C) which has been reconstructed as provided by Regulation; or

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<sup>2</sup> *RDB Thomas Road Partnership v. City of Phoenix*, 883 P.2d 431, 434, 180 Ariz. 194, 197 (1994).

(D) where water, power, and streets have been constructed to the property line.

Such improvements must not have been completed prior to the sale of the property or must be completed within 24 months of the sale of the property to qualify as a speculative builder sale. The table below shows the condition the parcels existed in prior to and subsequent to acquisition.

<b>Lot</b>	<b>Date of purchase</b>	<b>Description of property at time of purchase</b>	<b>Activity on property subsequent to purchase</b>	<b>Subdivided ?</b>	<b>Re-parceled?</b>
#1	2009	Vacant commercial urban property	Held and maintained	No	No
# 2	2009	Vacant commercial urban property	Held and maintained	No	In 2013 moved a small strip of the property (20 feet) into adjoining property (also owned by taxpayer) then in 2017 moved the same strip back into property #2
#3	2009	Vacant commercial urban property	Held and maintained	No	No
# 4	2014	Vacant commercial urban property	Held and maintained	No	In 2017 assessor made lot line adjustments

In this case, none of the types of improvements listed in MCTC § -416(a)(2) were performed on any of the parcels and so Taxpayer appears not to be selling improved property as defined in the MCTC.

Generally, to be considered a speculative builder under MCTC. § -416, Taxpayer must have performed either through itself or through others certain types of property improvement subsequent to the purchase of the property. Taxpayer purchased three parcels of property in 2009 and a fourth property in 2014. Taxpayer only performed maintenance work on the properties between the time of purchase and now. Taxpayer did not subdivide or re-parcel the parcel or add any structures or other improvement to the property. It only held and maintained the property in accordance with local government requirements. As a result, Taxpayer is not a speculative builder as defined in MCTC Reg. § -416(a).

**This response is a taxpayer information ruling (TIR) and the determination herein is based solely on the facts provided in your request. The determinations are subject to change should the facts prove to be different on audit. If it is determined that undisclosed facts were substantial or material to the Department's making of an accurate determination, this taxpayer information ruling shall be null and void. Further, the determination is subject to future change depending on changes in statutes, administrative rules, case law, or notification of a different Department position.**

**If the Department is provided with required taxpayer identifying information and taxpayer representative authorization before the proposed publication date (for a published TIR) or date specified by the Department (for an unpublished TIR), the TIR will be binding on the Department with respect to the taxpayer that requested the ruling. In addition, the ruling will apply only to transactions that occur or tax liabilities that accrue from and after the date the taxpayer receives the ruling. The ruling may not be relied upon, cited, or introduced into evidence in any proceeding by a taxpayer other than the taxpayer who has received the taxpayer information ruling. If the required information is not provided by the specified date, the taxpayer information ruling is non-binding for the purpose of abating interest, penalty or tax.**