DECISION OF MUNICIPAL TAX HEARING OFFICER

Decision Date: August 24, 2004
Decision: MTHO #157
Tax Collector: Town of Fountain Hills
Hearing Date: April 20, 2004

DISCUSSION

Introduction

On October 14, 2003, ***Taxpayer*** ("Taxpayer") filed a protest of a tax assessment and denial of a refund by the Town of Fountain Hills ("Town"). After review, the Town concluded on November 19, 2003 that the protest was timely and in the proper form. On November 24, 2003, the Municipal Tax Hearing Officer ("Hearing Officer") ordered the Town to file a response to the protest on or before January 8, 2004. The Town filed a response on January 8, 2004. On January 12, 2004, the Hearing Officer ordered the Taxpayer to file any reply on or before February 2, 2004. On February 2, 2004, the Taxpayer filed a reply. On February 11, 2004, a Notice of Tax Hearing ("Notice") was issued setting the matter for hearing commencing on March 11, 2004. On February 23, 2004, the Taxpayer filed a request for a continuance of the hearing. On February 27, 2004, the Hearing Officer granted the unopposed request for a continuance. On March 8, 2004, a Notice was issued rescheduling the hearing until April 20, 2004. Both parties appeared and presented evidence at the April 20, 2004 hearing. On April 22, 2004, the Hearing Officer ordered the parties to provide a briefing schedule on or before April 23, 2004. On April 22, 2004, the parties filed a letter indicating the Taxpayer would file an opening brief on or before May 21, 2004, the Town would file a response brief on June 21, 2004, and the Taxpayer would file a reply brief on July 9, 2004. On May 20, 2004, the Taxpayer filed its opening brief. On June 21, 2004, the Town filed its response brief. On July 9, 2004, the Taxpayer filed a reply brief. On July 12, 2004, the Hearing Officer indicated the record was now closed and a written decision would be issued on or before August 26, 2004.

The Taxpayer is a developer of lots in the Town. The Town conducted an audit of the Taxpayer for the period September of 1999 through April of 2002. The Town concluded the Taxpayer had overpaid taxes in the amount of $6,839.62. The Taxpayer had previously filed a request for a refund for the period in the amount of $377,255.23 plus applicable interest. The Town denied the refund request and the Taxpayer filed a protest of that denial.

Town Position

The Taxpayer is a developer of residential real estate lots at the ***Taxpayer*** Country Club ("Country Club") in the Town. According to the Town, the development plan contemplates a prestige-gated community with golf course, clubhouse and recreational club amenities with development occurring over a seven-year period ending in the year 2005. The plan called for 379 residential lots, a golf course and clubhouse. While no homes or residences had been constructed

on the lots in question, the Town asserted there were a number of off-site improvements at the Country Club that had to be constructed prior to the first lot sale. Those improvements included the completion of _____ Drive and _____ Avenue; grading had begun on the remaining roads including ***Taxpayer*** Country Club Drive; the Guardhouse was present and sewer installation for Phase I had begun. The Town argued that under the terms of the "Declaration of Covenants, Conditions, Restrictions, and Easements for ***Taxpayer*** Country Club" ("Declarations") purchasers of lots accede to ownership interest in all of the so-called "off-site" common area improvements. The Town argued that the Declaration is clear: when a lot is purchased at ***Taxpayer***, the purchaser acquires land and rights in appurtenant lands, i.e., the easements and the roads. According to the Town, while the "lot" purchased may not have an improvement erected on it at the time of sale, that does not mean that the purchaser has not acceded to legal and/or equitable ownership estates in improved real property.

The Town argued that quite apart from the "non-contiguous" common area improvements, each of the contested lots in question had, at minimum, graded access and/or roadway bladed areas up to and/or on the actual lots prior to their sale. Further, the Town asserted that to the extent that native plant permits were obtained and pulled, with native vegetation moved, preserved and relocated following such blading and grading, that activity renders the subsequent lot sales ones of "improved real property" pursuant to the Town Tax Code Section 416(a)(2)(B) ("Section 416(a)(2)(B)"). Section 416(a)(2)(B) defines "improved real property" to mean real property where improvements have been made to land containing no structure (such as paving or landscaping). According to the Town, by use of the terms "such as", the ordinance allows for the existence of other examples in addition to those specifically identified. The Town asserted the antecedent of items in the parenthetical contained in Section 416(a)(2)(B) is the term "improvements". The Town argued that graded thoroughfares constitute just such an improvement. While the Taxpayer relied on Estancia Development Associates, LLC v. City of Scottsdale, 196 Ariz. 87, 993 P.2d 1051 (App. 1999), the Town asserted there was no decision made by the Estancia court regarding what constituted an improvement under Section 416(a)(2)(B).

Town Tax Code Section 416(a)(2)(D) ("Section 416(a)(2)(D)") defines "improved real property" as real property" where water, power, and streets have been constructed to the property line." According to the Town, there has been a longstanding administrative practice to interpret Section 416(a)(2)(D) so that the three elements are properly read in the disjunctive, rather than conjunctive, sense so that if any one of the elements is in place, then the affected real property become "improved real property." The Town further argued that the longstanding administrative practice is consistent with the legislative intent of treating the "and" in Section 416(a)(2)(D) as an "or" and thus if any one of the elements was present then the sales of lots were taxable as improved real property. The Town argued that the "legislative body", the League of Arizona Cities and Towns ("League") has clearly stated that the use of "and" instead of "or" in Section 416(a)(2)(D) was a "… grammatical oversight in the code …". According to the League, Section 416(a)(2)(D) was intended to tax all lots upon which water, power or streets had been constructed. Based on all the above, the Town requested the Taxpayer's appeal be denied and the Town's denial of the claim for refund and audit assessment be upheld.

Taxpayer Position

The Taxpayer argued that based on the recent Estancia court decision, it is entitled to a refund for taxes paid on the sale of lots during the period of September 1999 through April 2002. According to the Taxpayer, the Estancia court determined that, based on the plain and ordinary language of the Scottsdale City Tax Code Section 416, the sale of vacant parcels to which improvements were promised to be made, but had not yet been constructed, was not subject to the tax on speculative building. The Taxpayer asserts that Section 416 is identical to the statute at issue in Estancia. "Improved Real Property" is defined as any 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

The Taxpayer argued that the lots included in the refund claim had no structures, no nonstructural improvements nor reconstruction on them. For that reason, the Taxpayer's claim was focused on Subsection D on whether or not water, power and streets had been constructed to the property line.

According to the Taxpayer, there was no blading or improvement of any kind on the lots themselves. The Taxpayer also asserted that there was no evidence to demonstrate there was any movement or relocation of the native plants on the lots in question. In fact, the Taxpayer argued that the value of the lots is that they are in a native desert condition at the time of the sale. The Taxpayer did not dispute that there were common area improvements. The Taxpayer asserted there were also such improvements in the Estancia court case. The Taxpayer argued that the decision of Estancia governs this dispute and as a result the Hearing Officer must find in the Taxpayer's favor.

The Taxpayer asserts that the Town has improperly inserted words into Section 416(a)(2)(D). According to the Taxpayer, in order for there to be "improved real property" pursuant to Section 416(a)(2)(D), there must be water, power and streets constructed to the property line. The Taxpayer argued that it is clear that needs to be all three (water, power and streets) present in order for thee to be "improved real property" pursuant to Section 416(a)(2)(D). In this case, the Taxpayer argued that while there may be electrical conduit to the property line, there were no wires running through the conduit. According to the Taxpayer, only when wire is pulled through the conduit to the property line has power been "constructed to the property line". The Taxpayer agreed that if the network of main and lateral water pipes is constructed to the property line that would meet one-third of the test set forth in Section 416 (a)(2)(D). The Taxpayer asserted that if the Town had intended that any one of the three items (water, power and streets) was sufficient in order to be "improved real property", they would have said "or" and not "and". The Taxpayer also argued Section 416(a)(2)(D) is a scope issue and as a result any ambiguities must be resolved in favor of the Taxpayer.

According to the Taxpayer, the Declaration evidences the intent of the Taxpayer that the common areas were to be owned and controlled by either the ***Taxpayer*** Community Association,

Inc. ("Association"), an Arizona nonprofit corporation, or the Taxpayer. The Declaration gives very specific rights to the Association which limit the right and easement of enjoyment in and to the common areas. The Taxpayer argued that the Town has mistaken an easement for ownership. The Taxpayer asserted that none of the provisions of the Declaration anticipated that the lot owners hold, or will hold, title to any real property other than their own lots.

ANALYSIS

The first issue is whether or not the lots in question were "improved real property" pursuant to Section 416(a)(2)(B). Section 416(a)(2)(B) defines "improved real property" as any real property "where improvements have been made to land containing no structure (such as paving or landscaping) …". Clearly, there were improvements in the development such as major ingress/egress roads, the Guardhouse, and other off-site improvements that would have increased the value of the lots. However, our issue is more narrow in that we must decide whether or not the lots were "improved real property" pursuant to Section 416(a)(2)(B). In making that decision, we do not find there is any sale of common areas when a lot is sold. Instead, there is right to use common areas that attached to the sale of the lot. As we have previously concluded in other cases, we do not find that a sale of a lot, without a structure, which is part of a development with improved common areas which the lot purchaser has a right of "use and enjoyment" is a sale of "improved real property" pursuant to Section 416(a)(2)(B). The alternatives set forth in Section 416(a)(2)(B) refers to improvements on the lot such as paving or landscaping. There was no evidence to demonstrate there was any paving on the lots. Further, there was no evidence there was any landscaping on the lots. While the Town alluded that there was some movement of native plants, there was no evidence in support of that. Even if there had been some movement of native plants, it is unclear that would reach the level of constituting landscaping. Lastly, we did not find any evidence of improvements to the lots that would be similar to paving or landscaping. Accordingly, we must conclude that the Town's interpretation of Section 416(a)(2)(B) would result in a "strained construction implication" in order to tax the sale of lots in this case.

The second issue is whether or not the lots in question were "improved real property" pursuant to Section 416(a)(2)(D). Section 416(a)(2)(D) defines "improved real property" as any real property "where water, power and streets have been constructed to the property line". First, we must conclude that Section 416(a)(2)(D) is plain and unambiguous that one must have all three items (water, power and streets) constructed to the property line in order for there to be "improved real property" pursuant to Section 416(a)(2)(D). The evidence demonstrated that while some cities/towns may have construed the "and" to be an "or", there were also some cities/towns that construed the "and" to be "and" and required all three items (water, power and streets) to be constructed to the property line. In this case, we do find there was sufficient evidence to conclude there was water constructed to the property lot lines. However, we do not find sufficient evidence to conclude that there was power and streets constructed to the property line. It appears there may have been some graded access and/or roadway bladed to the lots but, we do not find that activity would reach to level of being a street constructed to the property line. Similarly, there may have been some electrical conduit constructed to the property line but there was no evidence of any power being available to provide service through such conduit. As a result, we do not find there was power constructed to the property line at the time of the lot sales.

Based on the above, we do not find the sale of Taxpayer's lots would constitute "improved real property pursuant to Section 416(a)(2)(D).

FINDINGS OF FACT

1. On October 14, 2003, the Taxpayer filed a protest of a tax assessment made by the Town.

2. After review, the Town concluded on November 19, 2003 that the protest was timely and in proper form.

3. On November 24, 2003, the Hearing Officer ordered the Town to file a response to the protest on or before January 8, 2004.

4. The Town filed a response on January 8, 2004.

5. On January 12, 2004, the Hearing Officer ordered the Taxpayer to file any reply on or before February 2, 2004.

6. On February 2, 2004, the Taxpayer filed a reply.

7. On February 11, 2004, a Notice was issued setting the matter for hearing commencing on March 11, 2004.

8. On February 23, 2004, the Taxpayer filed a request for a continuance of the hearing.

9. On February 27, 2004, the Hearing Officer granted the unopposed request for a continuance.

10. On March 8, 2004, a Notice was issued rescheduling the hearing until April 20, 2004.

11. Both parties appeared and presented evidence at the April 20, 2004.

12. On April 22, 2004, the Hearing Officer ordered the parties to provide a briefing schedule on or before April 23, 2004.

13. On April 22, 2004, the parties filed a letter indicating the Taxpayer would file an opening on or before May 21, 2004, the Town would file a response brief on or before June 21, 2004, and the Taxpayer would file a reply brief on July 9, 2004.

14. On May 20, 2004, the Taxpayer filed its opening brief.

15. On June 21, 2004, the Town filed a response brief.

16. On July 9, 2004, the Taxpayer filed a reply brief.

17. On July 12, 2004, the Hearing Officer indicated the record was closed and a written decision would be issued on or before August 26, 2004.

18. The Taxpayer is a developer of lots in the Town.

19. The Town conducted an audit of the Taxpayer for the period September 1999 through April 2002.

20. The Town concluded the Taxpayer had overpaid taxes in the amount of $6,839.62.

21. The Taxpayer had previously filed a request for a refund for the period in the amount of $377,255.23 plus applicable interest.

22. The Town denied the refund request and the Taxpayer filed a protest of that denial.

23. The Taxpayer is a developer of residential real estate lots at the Country Club in the Town.

24. The development plan contemplates a prestige gated community with golf course, clubhouse and recreational club amenities with development occurring over a seven-year period ending in the year 2005.

25. The plan called for 379 residential lots, a golf course and clubhouse.

26. No homes or residences had been constructed on the lots in question.

27. There were a number of off-site improvements at the Country Club that had to be constructed prior to the first lot sale.

28. Those improvements included completion of _____ Drive and _____ Avenue; grading had begun on the remaining roads including ***Taxpayer*** Country Club Drive, the Guardhouse was present and sewer installation for Phase I had begun.

29. There were graded access and/or roadway bladed areas up to the actual lots prior to their sale.

30. The roadways to the actual lots were not paved.

31. The Town's Transportation and Air Quality Plans require streets to be paved.

32. Water was constructed to the property line of the lots prior to their sale.

33. There was no blading or improvement of any kind on the lots themselves.

34. The lots were in a native desert condition at the time of their sale.

35. There was no power to the property line of the lots at the time of their sale.

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. The purchasers of the lots received the right to use common areas.

3. The sale of a lot, without a structure, which is part of a development with improved common areas which the lot purchaser has a right of "use and enjoyment" is not a sale of "improved real property" pursuant to Section 416(a)(2)(B).

4. There was not sufficient evidence to demonstrate that there was either paving or landscaping or a similar activity on the lots prior to their sale.

5. The Town's interpretation of Section 416(a)(2)(B) would result in a "strained construction or implication" in order to tax the sale of lots in this case.

6. There was sufficient evidence to demonstrate that there was water constructed to the property lines of the lots prior to their sale.

7. There was not sufficient evidence to demonstrate that there was either power or streets constructed to the property lines of the lots prior to their sale.

8. We find that Section 416(a)(2)(D) is clear on its face that all three elements, water, power and streets, must be constructed to the property line in order for there to be "improved real property".

9. The Taxpayer's protest should be granted.

ORDER

It is therefore ordered that the October 14, 2003 protest of ***Taxpayer*** of a tax assessment and denial of a refund by the Town of Fountain Hills is hereby granted.

It is further ordered that the Town of Fountain Hills shall grant the refund request of ***Taxpayer*** consistent with the Discussion, Findings, and Conclusions, herein.

It is further ordered that this Decision is effective immediately.

Jerry Rudibaugh
Municipal Tax Hearing Officer