

## DECISION OF MUNICIPAL TAX HEARING OFFICER

September 30, 2010

*Taxpayer's Representative*

*Taxpayer's Representative's Address*

*Taxpayer*  
MTHO #586

*Dear Taxpayer's Representative:*

We have reviewed the evidence submitted for redetermination by *Taxpayer* and the City of Flagstaff (Tax Collector or City). The review period covered was October 2006 through June 2009. Taxpayer's protest, Tax Collector's response, and our findings and ruling follow.

### Taxpayer's Protest

Taxpayer was assessed City of Flagstaff privilege tax under the speculative builder classification for the transfer of four homes constructed by Taxpayer in the City. Construction loans were due on the homes and the only means to refinance was to transfer the homes to Taxpayer's Managing Member. Any monies from the sale of the homes, whether a gain or a loss, will be passed on to Taxpayer. The transaction was not an arms-length transaction and is not a qualified tax transaction as far as the City is concerned.

### Tax Collector's Response

Taxpayer is a limited liability company and transferred four townhouses to its Managing Member. Taxpayer is a separate person from its Managing Member. Sale of improved real property is subject to tax at the closing of escrow or transfer of title. The County has recorded the transfer of title, sale dates and the sale prices for the sales of the four townhomes. The recorded sales prices and sale dates were used for the privilege tax assessment. The recorded sales price amounts were similar to other sales made by Taxpayer. Taxpayer is liable for the tax that was assessed.

### Discussion

Taxpayer had constructed four townhomes in the City. Taxpayer had sold other townhomes in the City, and taxes were paid on those sales. The four townhomes at issue were transferred to Taxpayer's Managing Member by warranty deeds. No privilege taxes were paid on the four townhomes when they were transferred to the Managing Member.

The Tax Collector conducted an audit assessment of Taxpayer for the period October 2006 through June 2009 and issued an assessment to Taxpayer under the speculative builder classification. The Tax Collector considered the transfer of the four townhomes to the Managing Member sales of improved real property subject to the City's privilege tax. Taxpayer timely protested the assessment. Taxpayer contended that the four townhomes were purchased by the Managing Member for Taxpayer's benefit and no taxes were owed.

The Flagstaff City Code (FCC) governs whether and to what extent a person is taxable. Taxpayer was assessed as a speculative builder. A speculative builder is defined by the code as including an owner-builder who sells, at any time, improved real property. There was no question that Taxpayer was a speculative builder. The question here is whether Taxpayer sold the improved real property when it transferred the townhomes to its Managing Member.

Sale of improved real property includes any form of transaction which in substance is a transfer of title of improved real property. When Taxpayer executed warranty deeds transferring the townhomes to its Managing Member, Taxpayer transferred title to the townhomes. By transferring title, Taxpayer sold the townhomes to its Managing Member.

A member or manager of a limited liability company may transact business with the limited liability company and has the same rights and obligations with respect to those transactions as a person who is not a member or manager. Taxpayer and its Managing Member are separate persons for purposes of the city privilege tax.

The Tax Collector based the assessment on the sales price stated in the Affidavits of Value recorded with the sales. The Tax Collector stated in its Response that those amounts were similar to other sales made by Taxpayer. The Tax Collector basing the assessment on the sales price stated in the Affidavits of Value was reasonable. Taxpayer presented no evidence that the Tax Collector's method was unreasonable.

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 on which it built townhomes.
3. Taxpayer has sold townhomes in the City and privilege taxes were paid on those sales.
4. Taxpayer transferred title to four townhomes by warranty deed to its Managing Member.
5. Privilege taxes were not paid on the transfer of the four townhomes.
6. Affidavits of Value were recorded for the transfer for each townhome.
7. Each Affidavit of Value specified the sale price of the townhome.
8. The sales price amounts in the Affidavits of Value were similar to other sales of townhomes made by Taxpayer.
9. The Tax Collector conducted an audit assessment of Taxpayer for the period October 2006 through June 2009 and issued an assessment for city privilege tax under the speculative builder classification in the amount of \$14,454.02, interest through April 30, 2010 in the amount of \$1,404.64 and penalties in the amount of \$1,445.40.
10. The Tax Collector based the assessment on the sale price specified in the Affidavit of Value for each of the four townhomes.
11. Taxpayer timely protested the assessment and requested a redetermination.

#### Conclusions of Law

1. A speculative builder includes an owner-builder who sells, at any time, improved real property consisting of custom, model or inventory homes regardless of the stage of completion. FCC § 3-5-100.
2. Improved real property includes any real property upon which a structure has been constructed. FCC § 3-5-416(a)(2)(A).
3. The four townhomes were improved real property.
4. Taxpayer was the owner of the property on which the townhomes were constructed.
5. Taxpayer was a speculative builder.
6. Sale of improved real property includes any form of transaction which in substance is a transfer of title of improved real property. FCC § 3-5-416(a)(3).
7. Taxpayer transferred title to the townhomes to its Managing Member by warranty deeds.
8. Taxpayer sold improved real property when it transferred title to the four townhomes to its Managing Member.
9. Person means an individual, firm, partnership, joint venture, association, corporation, estate, trust, receiver, syndicate, broker, the Federal Government, this State, or any political subdivision or agency of this State. FCC § 3-5-100.
10. A person is considered a distinct and separate person from any general or limited partnership or joint venture or other association with which such person is affiliated. FCC § 3-5-100.
11. A member or manager of a limited liability company may transact business with the limited liability company and has the same rights and obligations with respect to those transactions as a person who is not a member or manager. A.R.S. § 29-608.
12. Taxpayer and its Managing Member were properly treated as separate persons for City privilege tax purposes.
13. The Tax Collector used the sale price of each townhome reflected in the Affidavit of Value to determine the tax due.
14. The Tax Collector's method for determining the market value of the transfer by Taxpayer was reasonable.
15. It is the responsibility of the taxpayer to prove that the Tax Collector's estimate of fair market value is not reasonable and correct. FCC § 3-5-545(b).
16. Taxpayer did not prove that the Tax Collector's estimate is not reasonable and correct.
17. Taxpayer's sales of the townhomes were subject to the tax on speculative builders.
18. The City's privilege tax assessment against Taxpayer was proper.

### Ruling

Taxpayer' protest of an assessment made by the City of Flagstaff for the period October 2006 through June 2009 is denied.

The Tax Collector's Notice of Assessment to Taxpayer for the period October 2006 through June 2009 is upheld.

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: Interim Tax, Licensing and Revenue Administrator  
Municipal Tax Hearing Office