DECISION OF MUNICIPAL TAX HEARING OFFICER

Decision Date: December 16, 2011

Decision: MTHO # 631

Taxpayer:

Tax Collector: City of Tempe

Hearing Date: September 28, 2011

DISCUSSION

Introduction

On February 28, 2011, a letter of protest was filed by ***Taxpayer*** of a tax assessment made by the City of Tempe ("City"). A hearing was commenced before the Municipal Tax Hearing Officer ("Hearing Officer") on September 28, 2011. Appearing for the City were the ***Assistant City Attorney*** and the ***Tax Audit Supervisor***. Appearing for Taxpayer was ***his representative***. At the conclusion of the hearing, the parties agreed to a briefing schedule. On November 7, 2011, the Hearing Officer indicated the record was closed and a written decision would be issued on or before December 22, 2011.

DECISION

On December 20, 2010, the Taxpayer requested a refund of City transaction privilege taxes paid on rents received for the period of November 2006 through October 2010 totaling $128,394.36. In addition, Taxpayer has protested all subsequent monthly payments to the City.

Taxpayer is the owner of real property located at ***Baseline Road*** in the City. Taxpayer purchased the property in June of 1997 with a building constructed on it. ***A Large Store*** entered into a lease agreement with Taxpayer for the facility with an initial term of fifteen years. Taxpayer and ***A Large Store*** are affiliated as both are substantially owned by ***an Out of State Limited Partnership***. ***Out of State Limited Partnership*** owns more than 80% of the voting stock of ***A Large Store*** and more than 80 % of the member interests in Taxpayer.

Taxpayer disputed the City's conclusion that it was "engaged in business" pursuant to City Code Section 16-100 ("Section 100"). Taxpayer relied on the Arizona appellate decisions in Construction Developers, Inc. v. City of Phoenix, 194 Ariz. 165, 978 P.2d 650 (App. 1999 and/or Arizona Tax Commission v. First Bank Building Corp., 5 Ariz. App. 594, 429 P.2d 481 (1967). Taxpayer argued that the mere receipt of monies and/or the relief from an obligation (e.g., payment of a mortgage or payment of ad valorem real property taxes) cannot, without more, be deemed to be in reality something it is not. As in CDI, Taxpayer asserted all the operating costs and occupancy expenses are paid by ***A Large Store*** as well as the property taxes on the property. As in CDI, Taxpayer asserted it had no full or part-time employees.

The City disputed Taxpayer's reliance on the Construction Developers case and the First Bank Building case. The City noted that Section 100 defines "business" as follows: Business means 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 casual activities or sales. The City asserted that the issue in this case was whether

Taxpayer was engaged in an activity or an act that provided it with any direct or indirect gain, benefit or advantage. The City noted that Taxpayer is a limited partnership with at least one general partnership and one or more limited partners. The City argued that it must be presumed they are involved in the limited partnership for the purposes of realizing gain or benefit from the relationship. The City asserted businesses do not engage in activities without a reason. According to the City, businesses do not incur costs that provide it with no direct or indirect advantage. The City noted that in the CDI case, the Court found: "Nothing in the record before the tax court demonstrated, much less suggested, that the taxpayer performed a single corporate act aside from challenging the City's excise tax assessment." The City indicated Taxpayer was engaged in activities, such as owning, leasing, and borrowing against real estate, that are business in nature and provide substantial gain, benefit, and advantage to both its general and limited partners. The City noted that both of the cases cited by Taxpayer involved transactions between a parent company and a wholly-owned subsidiary. In the present case, there is no direct ownership between Taxpayer and ***A Large Store***
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Taxpayer noted that on May 7, 2010, House Bill 2510 was signed into law amending A.R.S. Section 42-6004 ("Section 6004"). Taxpayer argued that the amended Section 6004 shows a legislative intent that when two companies are in a lessor/lessee relationship and both are owned at least 80% by the same company, the lessor does not have to pay taxes on its lease income. In this case, Taxpayer and ***A Large Store*** are "affiliated" as each is more than 80% owned by the same entity. Taxpayer noted that A.R.S. Section 43-104 defines corporation as follows: "Corporation" means a corporation, joint stock company, bank, insurance company, business trust or so called Massachusetts Trust, investment company or building and loan association and any other association whether incorporated or unincorporated." As a result, Taxpayer asserted that both Taxpayer and ***A Large Store*** are statutorily deemed "corporations" and Taxpayer's gross rental receipts from ***A Large Store*** are exempt from any City transaction privilege tax statute.

The City did not dispute that the amended Section 6004 exempted certain affiliated corporations from the privilege tax. However, the City argued that Taxpayer is not a corporation and so the provision is inapplicable to Taxpayer's lease. Since Section 6004 did not have any special definition for "corporation", the City asserted it must have its normal meaning. The City noted that Section 6004 states that "ownership and control are determined by reference to the voting shares of a corporation. The City argued that because "voting shares" are unique to the corporate format, the legislature intended the exemption to be available only to corporations. The City asserted that Arizona Transaction Privilege Tax Ruling TPR 93-39 ("TPR 93-39") supported the City's position. According to the City, TPR 93-39 concluded that "corporation" in ARS Section 42-5069©(5) ("Section 5069") means only corporation and not any other form of business activity. The City argued that the Department of Revenue's ("DOR") interpretation of Section 5069 is relevant because the language is virtually identical to the language of Section 6004.

Taxpayer noted that TPR 93-39 was issued in 1993. Taxpayer argued that subsequent

case law as well as statutes came into being that negated 93-39.
First, it is clear that even if Section 6004 applies in this matter, it would affect only a small portion of the refund period since the effective date was May 7, 2010. We find Section 6004 exempted certain affiliated corporations from the privilege tax. While Taxpayer has argued that corporation in Section 6004 would apply to limited partnerships, we must disagree. We agree with the City that the words of a statute are to be given their ordinary meaning. The fact Section 6004 refers to voting stock supports the City's interpretation that it does not include limited partnerships. City Code Section 360 ("Section 360") requires a taxpayer to provide adequate proof and documentation to support any claimed exemption. In this case, Taxpayer has failed to meet that burden of proof.
As noted above, "business" is broadly defined in Section 100. In this case, Taxpayer was formed as a limited partnership which then financed and purchased real property. Taxpayer then entered into a lease agreement with ***A Large Store*** and collected monthly rental payments. We concur with the City that business arrangements such as setting up the limited partnership are done for a purpose. In this case, Taxpayer is engaged in activities of financing and owning real estate and receiving lease payments which would provide substantial gain, benefit, and advantage as set forth in Section 100. We note that the Court in the Construction Developers case concluded that it could not sustain the City's assessment unless the Court could also determine that CDI leased to Dillard's for a consideration. In this case, we have such a lease in place. In fact, the June 12, 1997 lease has been amended two times. The second amendment included reference to a $8,300,000.00 loan to Taxpayer from a ***Nice Life Insurance Company***. Taxpayer has engaged in activities of financing and owning real estate and receiving lease payments which would provide substantial gain, benefit, and advantage as set forth in Section 100.

While there was no evidence of Taxpayer having an office location, the lease referred to a Post Office Box in ***California*** for which lease payments were to be sent. In the First Bank Building case, the Court concluded that the Plaintiff was organized for the purpose of doing business and was engaged in such activities by acquiring property, erecting buildings, executing leases and collecting rents. In doing so, First Bank was exercising corporate powers, taking in substantial gross receipts which benefit the corporation. The Court then considered separately whether First Bank was involved in the business of renting of office buildings and the operation of parking garages. As a result, we concur with the City that the facts in the First Bank Building case are distinguishable from this case. Clearly, Taxpayer and ***A Large Store*** were separate persons pursuant to Section 100. Consequently, the transaction between Taxpayer and ***A Large Store*** resulted in the business of leasing or renting of real property in the City pursuant to Section 445. Based on all the above, we conclude Taxpayer's protest should be denied.

FINDINGS OF FACT

1. On December 20, 2010, Taxpayer filed a request for a refund of City transaction privilege taxes paid on rents for the period of November 2006 through October 2010 totaling $128,394.36.
2. Taxpayer has protested all subsequent monthly payments to the City.
3. Taxpayer is the owner of the Baseline Property in the City.

4. Taxpayer purchased the Baseline Property in June of 1997 with a building constructed on it.
5. ***A Large Store*** entered into a lease agreement with Taxpayer for the facility with an initial term of fifteen years.
6. Taxpayer and ***A Large Store*** are affiliated as both are substantially owned by an **Out of State Limited Partnership.**
7. ***Out of State Limited Partnership*** owns more than 80% of the voting stock of ***A Large Store*** and more than 80% of the member interests in Taxpayer.
8. Taxpayer received monthly rentals from ***A Large Store*** during the period for which a refund has been requested.
9. ***A Large Store*** paid the operating costs and property taxes on the Baseline Property.
10. Taxpayer is a limited partnership with at least one general partner and one or more limited partners.
11. There is no direct ownership between Taxpayer and ***A Large Store***.
12. The June 12, 1997 lease between Taxpayer and ***A Large Store*** has been amended two times.
13. The second amendment included reference to an $8,300,000.00 loan to Taxpayer from ***Nice Life Insurance Company***.
14. The June 12, 1997 lease between Taxpayer and ***A Large Store*** referred to a Post Office Box in ***California*** for which lease payments were to be sent to Taxpayer.
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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. Section 445 imposes a tax on the gross income from the business activity of commercial rental.
3. Taxpayer and ***A Large Store*** were separate “persons” pursuant to Section 100.
4. Taxpayer was formed for a business purpose which included engaging in activities of owning real estate and receiving lease payments which would provide substantial gain, benefit, and advantage for its partners as set forth in Section 100.
5. During the assessment period, Taxpayer was in the business of leasing and renting real property within the City for a consideration pursuant to Section 445.
6. The facts in the Construction Developers and the facts in the First Bank Building case are distinguishable from the facts in this matter.
7. Section 6004 was amended on May 7, 2010 to provide an exemption for certain affiliated corporations from the privilege tax.
8. The Section 6004 exemption is only for corporations.
9. Taxpayer is a limited partnership and does not qualify as a corporation pursuant to Section 6004.
10. Taxpayer failed to provide adequate documentation to support an exemption pursuant to Section 360.
11. Taxpayer’s December 3, 2010 protest should be denied, consistent with the Discussion, Findings, and Conclusions, herein.

ORDER

It is therefore ordered that the February 28, 2011 protest by ***Taxpayer*** of a denial by the

City of Tempe of a tax refund request should be denied consistent with the Discussion, Findings, and Conclusions, herein.

Taxpayer has timely rights of appeal to the Arizona Tax Court pursuant to Model City Tax Code Section-575.

It is further ordered that this Decision is effective immediately.

Municipal Tax Hearing Officer