

SUPERIOR COURT OF ARIZONA  
MARICOPA COUNTY

TX 2004-000657

09/26/2006

HON. THOMAS DUNEVANT, III

CLERK OF THE COURT  
S. Brown  
Deputy

ORTHOLOGIC CORP, et al.

JAMES A RYAN

v.

ARIZONA STATE DEPARTMENT OF  
REVENUE, et al.

FRANK BOUCEK III

ROBERTA S LIVESAY  
PAUL J MOONEY  
JAMES G BUSBY JR.

**UNDER ADVISEMENT RULING**

The Court has considered Maricopa County's Motion for Summary Judgment re A.R.S. § 42-11102(D) and Plaintiffs' Joint Cross-Motion for Partial Summary Judgment. All parties agree that the decision in this case, to the extent that it resolves the constitutional issue, should also be applied to TX2004-000699, TX2004-000700, and TX2004-000969, and counsel for the parties in each of those cases participated in briefing and oral argument. The Court ruling will therefore apply with equal force and effect to all four cases.

The issues

From 2003 until its repeal in 2006, A.R.S. § 42-11102(D) ("Subsection D") imposed a property tax on lessees of an agricultural improvement district. Defendant seeks what is in fact partial summary judgment that the statute was constitutional and lawfully applied to Plaintiffs. Plaintiffs seek partial summary judgment that the statute was unconstitutional, or alternatively that its enforcement was improper.

Plaintiffs allege that Subsection D violated Article IX of the Arizona Constitution, both as a violation of the uniformity clause and as an attempt to tax constitutionally exempted

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property. They further allege that it was a special law, applicable to only a small area owned by Salt River Project in Tempe, and also that the statute fails to properly identify who is liable for the tax and is therefore void for vagueness. As to its implementation, they complain that their property has been improperly classified as personal property, that it is being assessed despite the failure to properly notice its valuation on the property tax rolls, and that, if it is correctly treated as personal property, the wrong formula has been applied to it. Defendant counters that the section satisfied both the equal protection clause and the narrower Arizona uniformity clause; that the statute taxes only non-exempt property held by lessees or sublessees; that the statute properly classified property and was therefore not a special law; that imposition of the tax on the "lessee or sublessee" was not vague; and that treatment of the property as personal property was correct and properly carried out.

Equal protection

Defendant devotes a great deal of attention to the equal protection clause, both in its Motion and in the Reply, even though Plaintiffs do not address it at all in their Response/Cross-Motion. The Court agrees that equal protection analysis, as distinguished from uniformity clause analysis, is not helpful. *See In re America West Airlines, Inc.*, 179 Ariz. 528, 530-31 (1994) (Uniformity clause more restrictive than equal protection clause).

Special law

Defendant's special law argument, based on A.R.S. Const. Art IV, part 2 § 19 (there was a typographical error in Plaintiffs' Response/Cross-Motion), is unpersuasive, at least as applied to their rights in this case. If the legislature has discriminated, they are not the targets of the discrimination. Whether Salt River Project, which as the only qualifying agricultural district in the state was uniquely affected by the statute (becoming the only constitutionally exempt entity unable to take advantage of its exemption by entering into long-term commercial leases), could have objected to it is a matter not raised in this action; thus, Plaintiffs do not have standing to assert Salt River Project's interests. Applying the statute to the class of Salt River Project lessees, the class was open. It could be expected that leases would terminate and new leases would be signed; the statute in no way limited such movement. The tax applied to all members of the lessee class, and, assuming that the statute is rationally based with respect to Salt River Project, it is rationally based with respect to the lessees. The class did not become closed by repeal of the statute merely because new entry into the class became impossible after the repeal date. Were that the case, every classifying law that is repealed would retrospectively become unconstitutional, even if it satisfied all the legal requirements during its lifetime, a conclusion that would result in havoc. It is the intent of the enacting legislature that determines whether a classification is limited to one particular case and looks to no broader application in the future. *Republic Investment Fund I v. Town of Surprise*, 166 Ariz. 143, 150 (1990). There is no reason

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to believe that the 2003 legislature anticipated the statute would be repealed three years later, before the initial set of leases had a chance to expire.

That only Maricopa County assessed and attempted to collect the tax does not create special act concerns. Rather, to the extent that property covered by Subsection D could be found in other counties, it raises the question of why those counties were not enforcing the law.

The statutory language

To determine whether Plaintiffs or Defendant is right as to the subject of the tax, the Court turns to the statute itself. Subsection D read in full, “Notwithstanding subsection A, if permanent *improvements* are constructed on land owned by and leased from an agricultural improvement district established pursuant to title 48, chapter 17, and the *improvements* are not otherwise entitled to any constitutional exemption from property taxation, then the *improvements* are subject to taxation in the name of the lessee or sublessee in the same manner as other property used for similar purposes.” Careful attention to the statutory language resolves some issues, and raises others. By the express language of the statute, it is the *improvements* that are taxable, as Plaintiffs assert, not, as Defendant argues, possessory interests in the improvements. This answers the question of double taxation, as Subsection D and GPLET tax different things. See *U.S. West Communications, Inc. v. City of Tucson*, 198 Ariz. 515, 524-25 ¶¶ 31-35 (App. 2000).

However, the text conflicts with case law relating to the ownership of the improvements. The Subsection D tax does not (and cannot) apply if the improvements are exempt from property taxation, regardless of whether the GPLET can be applied to the transfer of leasehold rights. Defendant, despite its disquisition into the constitutional status of agricultural improvement districts, does not appear to contest that the property of Salt River Project is exempt from taxation pursuant to A.R.S. Const. Art. XIII § 7, which grants to such districts the rights, privileges, and exemptions granted to municipalities. Nor, the Court hopes, is Defendant arguing that the legislature may by statute override the provisions of the Arizona Constitution and subject the property of Salt River Project to taxation notwithstanding its constitutional exemption. Under long-established case law, improvements in property leased to a private firm by a government entity are the property of the government lessor, and are therefore exempt from property taxation. *Airport Properties v. Maricopa County*, 195 Ariz. 89 (App. 1999); *Cutter Aviation v. Arizona Dept. of Revenue*, 191 Ariz. 485 (App. 1997); *Maricopa County v. Novasic*, 12 Ariz.App. 551 (App. 1970). The only way a tax can be levied on the improvements, then, is if Subsection D repealed the holding of the *Novasic/Cutter/Airport Properties* trilogy and made the lessee or sublessee of the improvements, rather than the public lessor, the owner of the improvements for tax purposes. Given the facts in this case, it is not necessary to decide whether

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the legislature acted constitutionally in thus repealing the trilogy. The statute falls on other grounds.

To begin with, this position would prevent the imposition of the GPLET on Plaintiffs. A.R.S. § 42-6202(A) limits the GPLET to property for which the title of record is held by a government lessor. The constitutional exemption of such improvements from property taxation was precisely the reason the legislature enacted the GPLET to permit taxation via an excise on the acquisition of leasehold interests by taxable private parties. *See* Robert Clark, “The Government Lease Excise Tax: Challenging the Excise-Property Tax Distinction,” 29 ARIZ. ST. L. J. 871 (1997). This is not double taxation, but a more profound and unacceptable inconsistency. Defendant cannot treat Plaintiffs as simultaneously the owners of the improvements for the purpose of the Subsection D tax and as mere lessees of Salt River Project for the purpose of the GPLET.

Uniformity clause

In addition, Defendant has not shown any basis, and the Court cannot identify one, on which the tax can be properly limited to improvements on land owned by agricultural improvement districts and not be applied as well to those on land owned by other exempt governmental entities, such as municipalities. Property tax classifications may be based on a property’s “nature, use, utility, or productivity.” *America West Airlines, supra* at 535. They may also be based on public versus private ownership. *Cutter Aviation, supra* at 496. None of those factors applies here. There is no discernible difference in nature or use between improvements on Salt River Project’s land and similar improvements on other public land. Nor is there a difference in the state’s ability to tax such property. Granted that the county and state have a legitimate interest in deriving revenue from the commercial exploitation of improvements on publicly-owned land (an interest recognized as long ago as *Maricopa County v. Fox Riverside Theatre Corp.*, 57 Ariz. 407, 411-12 (1941), and reaffirmed in *Cutter Aviation, supra* at 496-97), that interest is no less legitimate when applied to municipal corporations or other constitutionally exempt owners. Because limitation of the tax to lessees of agricultural improvement districts is not based on any real difference in the property, the statute is invalid.

Vagueness

Finally, the statute fails to identify the person subject to the tax. Defendant’s Response brief identifies the problem: “The statute at issue clearly explains that lessees or sublessees are subject to the Subsection D tax.” The key word is that *or*. Fatally, the statute does not state, or provide any method for determining, whether the lessee or the sublessee is liable in any given case. Using the traditional property law metaphor of the bundle of sticks, the statute could have

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assessed a tax against both the lessee and the sublessee on the sticks each possessed, or it could have identified one stick and made the holder of that stick, whether the lessee or the sublessee, liable for the entire tax. It did neither. Instead, it left the matter to the arbitrary discretion of the assessor, who is left with nothing but his sense of whom the tax should most fairly be levied against. This fails the requirement of specificity that applies to all statutes and with special force to tax statutes. *Duhamé v. State Tax Commission*, 65 Ariz. 268, 272-73 (1947).

The prospect identified by Defendant at oral argument, that a covered lessor might avoid the tax by leasing the improvements in the first instance to another exempt entity which would in turn sublet them to a private firm, may explain the statute's vagueness but does not save it. It was the legislature's obligation to define in some way who was liable for the tax, allowing the taxpayer to arrange his affairs so as to minimize his liability within the confines of the law. It could not prevent tax planning by leaving the basis for liability so open-ended as to cover any eventuality.

The term "not otherwise entitled to any constitutional exemption" merely limits the scope of the act to those taxpayers whose property can lawfully be taxed. As such, it is not legally significant – if the property is constitutionally exempt, it may not be taxed even without this language – but it is not vague so as to invalidate the statute.

Ruling

The Court concludes that former A.R.S. § 42-11102(D), for the reasons stated, violated the Arizona Constitution.

Therefore, IT IS ORDERED granting Plaintiffs' Cross-Motion for Partial Summary Judgment and denying Defendant's Motion for Summary Judgment Re A.R.S. § 42-11102(D). Because of the Court's ruling on the constitutionality of the statute, it is not necessary to consider implementation issues relating to the valuation of the property and assessment of the tax on the Plaintiffs.

IT IS FURTHER ORDERED that the decision in this case, TX2004-000657, shall apply with equal force and effect to TX2004-000699, TX2004-000700, and TX2004-000969.