

THE SUPERIOR COURT OF THE STATE OF ARIZONA
IN THE ARIZONA TAX COURT

TX 2021-000388

06/06/2025

HONORABLE ERIK THORSON

CLERK OF THE COURT
A. Smith
Deputy

REBUILD THE BLOCK L L C

PAUL J MOONEY

v.

ARIZONA DEPARTMENT OF REVENUE

BENJAMIN H UPDIKE

RULING

This matter is under advisement following a bench trial held on February 10–11, 2025. After considering the witness testimony and exhibits admitted at trial as well as the Parties’ written closing arguments, proposed findings of fact and conclusions of law, and responses and objections to the same, the Court makes the following findings, conclusions, and orders.

FINDINGS OF FACT

Speculative Builder Tax

1. Defendant, Arizona Department of Revenue (the “Department”), is an agency of the State of Arizona, created and organized pursuant to A.R.S. §§42-1001, *et seq.*, charged by law with the duty to supervise audits and tax collections by Arizona cities, pursuant to A.R.S. §§42-6051, *et seq.* (Joint Pretrial Statement, filed January 24, 2025, at Uncontested Issues of Fact or Law Deemed Applicable (“JPS”) ¶2.)

2. The City of Phoenix (the “City”) imposes a privilege tax on “equal to two and three-tenths percent (2.3%) of the gross income from the business activity upon every person

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engaging or continuing in business as a speculative builder within the City.” Phoenix City Code (“City Code”) § 14-416(a).¹

3. Although the speculative builder tax is a tax under the City Code, the Department is tasked with collecting and administering the tax pursuant to A.R.S. § 42-6001(A).

4. “The gross income of a speculative builder considered taxable shall include the total selling price from the sale of improved real property at the time of closing of escrow or transfer of title.” City Code § 14-416(a)(1).

5. The City Code allows for various deductions, credits, and exemptions. *See* City Code § 14-416(b) and § 14-416(c).

Rebuild the Block, LLC

6. Nathan Anderson builds homes through his company, Rebuild the Block, LLC (“RTB”). (Defendant’s Proposed Findings of Fact and Conclusions of Law, Exh. 1 (“Day 1 Transcript”) 26:2–6.)

7. RTB is an Arizona limited liability company that holds Arizona transaction privilege tax number 21049691. (JPS ¶1.)

8. RTB has been building homes for about ten years. (Day 1 Tr. 26:13–15.)

9. RTB has built a total of about 40 to 45 homes. (Day 1 Tr. 30:18–24.)

10. RTB purchased ten previously improved parcels located in the Arcadia subdivision of Phoenix, on which it later built newer and larger homes that it sold between February of 2016 and March of 2019. (*See* JPS ¶11.)

11. RTB did not report or remit speculative builder tax on the sales of those properties.

12. The Court previously found that RTB is a speculative builder for purposes of the speculative builder tax applicable to the sales of the nine properties at issue in this case, granting the Department summary judgment on that issue. (Minute Entry, filed September 25, 2023, at 3–4.)

¹ The Court notes that amendments to the City Code were adopted March 18, 2025, in Ordinance No. G-7369. All citations to the City Code herein are to the prior version.

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History with the Department

13. The Department contacted RTB in November of 2019, requesting it to file a tax return regarding the sales of the homes between February 2016 and March 2019 that the Department believed were subject to the speculative builder tax. (JPS ¶3.)

14. Because RTB did not provide any documentation in response to the request, but instead denied taxability, the Department issued a draft assessment on December 6, 2019. (Defendant's Proposed Findings of Fact and Conclusions of Law, Exh. 2 ("Day 2 Transcript") 110:14–23; Plaintiff's Exh. 1; JPS ¶4.)

15. The Draft Assessment had a schedule attached to it that listed all ten of the separate sales of these homes between February of 2016 and March of 2019. (Plaintiff's Exh. 1.)

16. Upon receipt of the Draft Assessment, Mr. Anderson spoke multiple times with the City's Auditor assigned to this matter, Dmitry Andreyev, in an effort to understand why RTB was being assessed for its activities in tearing-down existing homes and rebuilding larger and more modern homes on the ten parcels listed in that document. (See JPS ¶5.)

17. Mr. Anderson provided a copy of Plaintiff's Exh. 3 (a one-page spreadsheet noting a Computation of Tax Due – Speculative Builder) to Mr. Andreyev in late December or early January of 2020, and Mr. Andreyev acknowledged receipt of that document. Mr. Anderson claimed he also provided Defendant's Exh. 3 (an Excel spreadsheet of costs by location) to Mr. Andreyev at the same time, but Mr. Andreyev disputed that testimony. (Day 1 Tr. 47:3–9; 51:17–23; Day 2 Tr. 181:17–24, 183:15–18.)

18. One of the permits, for the property on Earll Drive, stated the activity was an addition, and not new construction as stated in the other nine permits. As a result of this information, and lacking further information from RTB on the nature of the construction, the Department removed that home, leaving nine in the audit, where the permits stated that the constructions activities were similar. (See Day 2 Tr. 71:15–25.)

19. On January 27, 2020, the Department issued a Notice of Proposed Assessment for \$115,768.79, plus penalties and interest ("Assessment") against RTB on its sales of the nine properties as improved real properties. (Defendant's Exh. 1; JPS ¶6.)

20. The Assessment reduced the principal Draft Assessment from \$125,711.40 to \$115,768.79. (Plaintiff's Exh. 1; Defendant's Exh. 1.)

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21. In late-January or early-February of 2020, Mr. Anderson went to the City of Phoenix and spoke with Mr. Lavelle Bland, the Supervisor of Mr. Andreyev, to attempt to resolve the matter that became this case. (Day 1 Tr. 56:5–57:12.)

22. During that meeting, Mr. Anderson attempted to pay the amount calculated by his CPA (Plaintiff's Exhibit 3), but he was told he could not do so and that the amount still needed to be resolved. (Day 2 Tr. 79:15–25.)

23. At trial, Mr. Bland testified that auditors are not permitted to receive checks from taxpayers for tax payments. All payments must go through the Department's official websites or channels. (Day 2 Tr. 79:22–25.)

24. On February 5, 2020, RTB protested the Assessment and requested a meeting with the Department. (Plaintiff's Exh. 2; JPS ¶7.)

25. On July 14, 2020, RTB's counsel and Mr. Anderson met at the Department's office for an Informal Conference with representatives of the Department and the City, in an attempt to resolve the Parties' dispute about the Assessment. (JPS ¶8.)

26. During the Conference, Mr. Andreyev explained one of the original ten (10) homes included in the Draft Assessment was removed from the Assessment. (JPS ¶9; Day 1 Tr. 62:4–17.)

27. During the Conference, RTB provided evidence to the Department that the sales price indicated in the amended worksheet for the Assessment had an error in the sales price of one home (3828 N. 42nd Place). The Department verified this and adjusted the price. (JPS ¶10.)

28. Taxpayer requested and eventually received a schedule similar to the one that was attached to Plaintiff's Exhibit 1 that listed each of the properties in the Assessment. (Plaintiff's Exh. 7.)

29. The only difference between the schedule received in evidence as Plaintiff's Exh. 7 and the schedule attached to Plaintiff's Exh. 1, is the removal of the first listed home (4311 E. Earll Drive) from the Assessment.

30. On November 23, 2020, the Department issued an Amended Assessment (the "Amended Assessment") reducing the tax due from \$115,768.79 to \$114,538.85, plus interest. No penalties were included in the Amended Assessment. (Defendant's Exh. 2; JPS ¶¶10, 12.)

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31. The nine houses that were included in the Amended Assessment, the dates they were sold, and the amounts they each sold for which were stipulated in the Pretrial Statement as follows:

| <u>Address</u> | <u>Sale Date</u> | <u>Sales Price</u> |
|---------------------------|------------------|--------------------|
| a. 3828 N. 42nd Pl. | May 2016 | \$699,000 |
| b. 3709 N. 34th Pl. | Oct. 2016 | \$797,000 |
| c. 3828 E. Weldon Ave. | May 2017 | \$825,000 |
| d. 3302 E. Sells Dr. | June 2017 | \$795,000 |
| e. 3247 E. Sells Dr. | Aug. 2017 | \$825,000 |
| f. 4101 E. Indianola Ave. | Oct. 2017 | \$775,000 |
| g. 3225 E. Roma Ave. | June 2018 | \$860,000 |
| h. 3311 E. Roma Ave. | Oct. 2018 | \$1,115,000 |
| i. 4249 N. 34th St. | Mar 2019 | \$1,085,000 |

(JPS ¶11.)

RTB's Expense Spreadsheet

32. RTB provided the Department with an Excel spreadsheet of costs by location ("Spreadsheet") for various expenses related to the construction of the homes. (Defendant's Exh. 3.)

33. Mr. Anderson stated that he personally entered the data in the Spreadsheet by reconciling the amounts with bank statements from checking accounts and credit card statements. (Day 1 Tr., 48:3–20; 145:3–14.)

34. Mr. Anderson testified about how that spreadsheet was created, and how it was used by RTB in its business activities to accurately reflect all of the costs associated with constructing the ten homes the City originally inquired about in its Draft Assessment. (*See e.g.*, Day 1 Tr. 46:7–12; 47:13–20.)

35. Specifically, Mr. Anderson testified he personally entered data for each home built into the Spreadsheet three days every week (Mondays, Wednesdays and Fridays), based on his banking records, cancelled checks and business credit card statements to document payments made to contractors and purchases made for materials and supplies used in the construction of each of the homes. (Day 1 Tr. 47:21–49:15.)

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36. For each entry, the Spreadsheet contains the date, a short description, an amount, and a column indicating the check number or credit card used. (Defendant's Exh. 3.)

37. No documentation used to construct the Spreadsheet is in the record before the Court.

38. The Spreadsheet lacks information that would be found on contracts, invoices, and receipts. It lacks the scope, nature, or location of the activity or purchase, a description of the item, the parties involved, the expense amounts broken down by identified costs, and the amounts of taxes charged or paid, if any, and who would be responsible for the taxes. (Day 2 Tr. 117:15–132:17.)

The Department's Calculation of the Tax

39. The Department calculated the amount owed by first determining the total amount of income from the improved real property, and then removing the allowable deductions, and finally granting any allowable credits. (Day 1 Tr. 188:10–189:23.)

40. The Department's review of the deductions and credits potentially available to RTB resulted in a reduction of the assessment by allowing some deductions and credits that RTB could claim if RTB had produced corroborating documentation. (Day 2 Tr. 156:8–19.)

41. RTB did not record the TPT license numbers on the Spreadsheet for any of the contractors it used to construct the homes. (Day 1 Tr., 140:25–141:9.)

42. The description of the contractor on the Spreadsheet does not include anything about the type of work or activity performed. (*See* Defendant's Exh. 3.)

43. The Spreadsheet does not indicate whether or how much the contractors reported or paid in city or state taxes to the Department. (*See* Defendant's Exh. 3.)

44. The Department's settlement offer allowed the sum of \$608,804.50 of the \$1,648,776.06 for the claimed credit and deduction for taxes that contractors paid to the cities and state, disallowed the amount of \$1,039,971.56. (Defendant's Exh. 4, at 23.)

45. RTB did not provide receipts for any of its purchases from retailers for its construction materials that it claimed were incorporated into the real property. (*See* Defendant's Exh. 3; Day 1 Tr. 147:23–25; Day 2 Tr. 157:20–23.)

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46. The purchases from retailers are not described in the Spreadsheet nor the nature of the item or material that was purchased. (*See Defendant's Exh. 3.*)

47. The Spreadsheet does not indicate in which city the retailer is located. The city where the retailer is located determines the amount of tax paid, because Arizona cities impose different tax rates. (*See Defendant's Exh. 3; Day 1 Tr. 197:19–198:10.*)

48. At the time the expenses were entered into the Spreadsheet, RTB did not indicate whether, or how much, taxes were paid for any of the purchases of materials nor any other tangible personal property. (*See Defendant's Exh. 3.*)

49. Some retailers on the spreadsheet, like Amazon, sell a wide variety of items. Without a description of the nature of the item, the Department cannot verify that the item was a material that would be incorporated into a property. (*Day 2 Tr. 146:15–22.*)

50. Retailers, such as Home Depot or Lowes, sell tools and materials. Tools are not incorporated into the property so any taxes paid on their purchase would not be allowed as a deduction. (*Day 2 Tr. 16:11–24.*)

51. The description of the materials on the Spreadsheet is limited to the name of the retailer. It does not indicate the nature of the item purchased, what amounts on the purchase are materials like wood and so potentially viable for a deduction, and what is not, because it is a tool like a saw, or Gatorade. (*See Defendant's Exh. 3.*)

52. The Department's settlement offer allowed \$895,363.84 of the \$1,041,183.94 of the claimed credits for taxes paid on the purchase of materials incorporated into the projects, disallowing \$145,820.10. (*Defendant's Exh. 4, at 72.*)

53. The Department reviewed publicly available records for the plans and permits that were referenced in the Spreadsheet. It was able to verify the existence of some plan and permit fees. (*Day 2 Tr. 147:23–151:11.*)

54. Source documentation is a necessary requirement to determine which parts of the architectural and engineering expenses are direct costs, which costs are allowed, as opposed to indirect costs, and which costs are not. That required documentation was not provided. (*See Defendant's Exh. 3; Day 1 Tr. 192:15–193:19.*)

55. The Department's settlement offer allowed \$282,022.75 of the \$370,983.96 of the claimed credits for fees and permits claimed, disallowing \$89,632.46. (*Defendant's Exh. 4, at 76.*)

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56. The off-site improvements for roads, sidewalks, curb and gutter, utility connections for gas, electricity, water, sewer or telecommunications were already constructed for the previous homes on the properties when RTB purchased them to demolish and rebuild new properties. (Day 1 Tr. 98:25–99:21.)

57. RTB did not construct the offsites, or incur any costs related to off-site improvements for roads, sidewalks, curb and gutter, utility connections for gas, electricity, water, sewer or telecommunications beyond the price paid to acquire each of the lots. (Day 1 Tr. 100:2–5, 101:4–8.)

58. Based on the findings of fact set forth above, the Department requests that the Court finds the principal amount of the Amended Assessment should be reduced to \$79,992.91, plus interest. (*See* Defendant’s Proposed Conclusions of Law ¶28; *see also* Department’s Motion for Summary Judgment, filed June 7, 2024, at 15; Department’s Statement of Facts in Support of Motion for Summary Judgment, filed June 7, 2024, at ¶72.)

59. RTB requests that the principal amount of the Amended Assessment be reduced to \$56,965.55 for the nine sales at issue (\$19,870.56 if the tax only applies to three of the sales).

60. The Parties filed cross-motions for summary judgment regarding the application of speculative builder tax to the nine homes in the Amended Assessment. (JPS ¶15.)

61. The Tax Court granted the Department’s motion and denied RTB’s motion regarding the application of speculative builder tax to the nine homes but deferred its ruling on whether RTB was entitled to additional deductions, exemptions, or credits. (JPS ¶16; Minute Entry, filed September 25, 2023.)

CONCLUSIONS OF LAW

1. The presumption for City taxes is that the gross income from a business is subject to tax until the contrary is established by the taxpayer. City Code §14-400(c).

2. Any deduction, exemption, or credit is “limited to the specific activity or transaction described and not extended to include any other activity or transaction subject to the tax.” City Code §14-400(d).

3. City Code § 14-416(c)(2)(A) permits a deduction for state and county taxes associated with the project that were reported and paid to the Department by a contractor that constructed improvements on the property.

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4. City Code § 14-416(c)(3)(A) permits a tax credit for city tax paid to the City or as a separately itemized charge paid to the vendor, if the tangible personal property purchased is incorporated into the real improved property.

5. City Code § 14-416(c)(3)(B) allows a tax credit equal to the amount of taxes paid to the City or separately itemized as a charge to the taxpayer by a contractor.

6. City Code § 14-416(c)(1)(E) allows an exemption for development fees.

7. City Code § 14-416(b)(5) permits an exclusion for the “direct costs of providing architectural or engineering services that are incorporated in a contract.”

8. City Code § 14-360(a) requires that a taxpayer “preserve suitable records and such other books and accounts as may be necessary to determine the amount of tax for which [it] is liable.”

9. RTB failed to provide suitable records and books under the provisions set forth in City Code § 14-360(a) to meet its burden of proof to claim additional deductions and credits. (See Findings of Fact ¶38.)

10. City Code § 14-370(a) makes “[a]ll deductions, exclusions, exemptions, and credits . . . conditional upon adequate proof and documentation.”

11. RTB does not meet the requirement under City Code § 14-370(a) for claiming any deductions or credits because it lacks suitable documentation or any other books and records to verify and corroborate its claimed deductions or credits.

12. City code requires that tax credits related to the speculative builder tax be “documented to the satisfaction of the tax collector.” City Code §14-416(c)(3).

13. Using the information provided by RTB and the Department’s review, **THE COURT FINDS** the principal amount of the Amended Assessment should be \$79,992.91, plus interest. The Court did not find applicable the authorities that Plaintiff cited in Closing Argument, filed March 5, 2025, in support of its request that the Court abate interest.

Based on the above findings and conclusions,

IT IS ORDERED finding in favor of Defendant Arizona Department of Revenue as to the Amended Assessment in the reduced amount principal amount of \$79,992.91 plus interest.

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IT IS FURTHER ORDERED that not later than twenty (20) calendar days after the filing of these Orders by the Clerk of the Superior Court, Defendant may submit a verified application for awards of costs. Ariz. R. Civ. P. 54(f)(3) governs the response and reply timeframes.

IT IS FURTHER ORDERED that not later than twenty (20) calendar days after the filing of these Orders by the Clerk of the Superior Court, Defendant must also submit a proposed form of judgment that includes the amount awarded, including interest and costs sought. That form of judgment may incorporate by reference from this minute entry ruling along with Rule 54(c), Ariz. R. Civ. P., language. Rule 58(a)(2)(B) governs the objection and reply timeframes.