

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

TX 2017-000566
TX 2017-000567
TX 2017-001679
TX 2018-000040
TX 2018-000041
TX 2018-000736

07/27/2020

HONORABLE DANIELLE J. VIOLA

CLERK OF THE COURT
K. Cabral
Deputy

EL RANCHO AFFORDABLE HOUSING L P

DOUGLAS S JOHN

v.

MARICOPA COUNTY

ROBERTA S LIVESAY

JUDGE VIOLA

UNDER ADVISEMENT RULING

Defendant's Motions for Declaratory Judgment – Denied

The Court has received and considered Defendant's Motions for Declaratory Judgment filed December 20, 2019, Plaintiffs' Responses, and Defendant's Omnibus Reply. The Court further considered the arguments of counsel presented on May 27, 2020 and on July 22, 2020. The Court contemplated ordering supplemental briefing but has now concluded that additional briefing is not necessary.

Maricopa County asks the Court to enter declaratory relief on the issue of the correct valuation method for valuing low-income housing property encumbered by restrictions under Section 42 of title 26 of the Internal Revenue Code. The County asks the Court to declare "that property known as Low Income Tax Credit property ("LIHTC") must be valued for property tax purposes using market rent to achieve a full cash value for the fee simple estate of the property." The County asks the Court to affirm the valuation method set forth in the Arizona Department of Revenue's Subsidized Housing Valuation Guideline. Under the Guideline, the assessor must assume that a low-income housing property is unencumbered by restrictions imposed by federal and state law. According to the Guideline, assessors should use market rents as opposed to

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restricted rents for valuing the property. The Taxpayers ask the Court to deny the County's request and affirm the standard previously adopted by the Tax Court in *Cottonwood Affordable Housing v. Yavapai County*, 205 Ariz. 427 (2003).

Background

Plaintiff Taxpayers, El Rancho Affordable Housing L.P., El Rancho Affordable Housing II L.P., and Northern Gardens/Phoenix L.P. filed separate actions against Defendant, Maricopa County challenging the property valuation for their respective properties. Taxpayers operate properties that receive the LIHTC. Because of this credit, they must operate their properties according to the restrictions imposed by Congress, including restricting the amount of rent charged. The County valued the relevant properties at market rates without regard to rent restrictions.

Analysis

Arizona Revised Statutes section § 12-1831 provides that courts "within their respective jurisdictions shall have power to declare rights, status, and other legal relations. . . ." The Arizona Tax Court may issue a declaratory judgment when the action does not challenge the constitutional validity of a tax statute and if the parties have exhausted all other administrative remedies. *Estate of Bohn v. Scott*, 185 Ariz. 284 (Ariz. Ct. App. 1996). Tax valuation appeals have no requirement to exhaust administrative remedies. *Maricopa County v. TWC Chandler*, 206 Ariz. 293, 294 (Ariz. Tax. Ct. 2003). In this case, there is no challenge to the constitutional validity of a tax statute and the case has no administrative remedy requirement. Therefore, the court may issue a declaratory judgment on the question of law presented by the County.

The issue presented by the County's Motion is whether the valuation of LIHTC properties should be based on market rents or based on the restricted rents imposed by the LIHTC program. The Tax Court previously addressed the issue seventeen years ago in *Cottonwood Affordable Housing v. Yavapai County*, 205 Ariz. 427 (2003).

According to A.R.S § 42-13051, properties are to be valued according to their full cash value. Section 42-11001(6) defines full cash value as market value determined using "standard appraisal methods and techniques." When applying standard appraisal methods and techniques, current usage will be included in the determination. § 42-11054(C)(1).

Although not binding, previous decisions by this Tax Court are persuasive. The Tax Court previously decided that when valuing property in the LIHTC program, the valuation should be determined from the restricted rents imposed by the program. *Cottonwood*, 205 Ariz. at 430. The

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long-term rent restrictions placed on the property by the LIHTC program affect the marketability of the property and therefore “have a significant impact on the value. . . .” *Id.*

The Court’s analysis in *Cottonwood* is consistent with the Arizona Supreme Court decision in *Recreation Centers*. In *Recreation Centers*, the Arizona Supreme Court distinguished between deed restrictions that limited the profitability of the owner and restrictions that controlled how the property is used. *Recreation Centers of Sun City, Inc. v. Maricopa County*, 162 Ariz. 281, 290-91 (1989). In *Recreation Centers*, the Court analyzed a deed restriction requiring the owner to operate a facility on the property on a non-profit basis. The Court explained that the restrictions regarding profitability may “destroy marketability but they do not destroy value.” *Id.* at 290. In analyzing the use restrictions, the Court explained that “[t]he limitation on use does not divide value between those who have the right to use; it limits the value in use of all users.” *Id.* at 290. As the Supreme Court explained, “[t]he property cannot be valued as if it were property to be used for residences, apartments, retail stores, or industry; the land is not and cannot be so used even though it may be now properly located and zoned.” *Id.*

Here, the LIHTC restrictions, like the use restriction in *Recreation Centers*, affect and limit the value in all use of all users. Similarly, like in *Recreation Centers*, the restrictions on LIHTC properties run with the land and bind successors. See 26 U.S.C.A. § 42(j); Exhibit #2 to the El Ranch Defendants’ Motion, Recitals, § F and § 13 “Covenants Run with the Land; Successor Bound Thereby.” Similar to the facts in *Recreation Centers*, the Taxpayers cannot use the property for a non-low income housing property even though the property may be so zoned or located. In *Recreation Centers*, the Court found that “the recreational use restriction has an undoubted effect on value.” *Id.* at 290. These restrictions run with the land and new owners are subject to the same conditions. Like in *Recreation Centers*, the LIHTC program controls how the property can be used and therefore the value.¹

To the extent that the Court declines to reject the reasoning in *Cottonwood*, the County asks that the Court declare the mandatory Guideline invalid. While the *Cottonwood* decision did not expressly address the Guideline, the Tax Court explained, “[a] valuation for an LIHTC project, determined under any of the standard appraisal methods, that does not take the deed restrictions

¹ The Court notes this conclusion is consistent with the majority of states and the 2005 Appraisal Institute’s 2005 Valuation and Market Studies for Affordable Housing. See El Rancho Plaintiffs’ Response at page 9, fn. 24 and page 10, fn. 25. Other jurisdictions have explained that LIHTC restrictions constitute a governmental restriction as to use that should necessitate a reduction in the value of the property for real property tax purposes. See e.g., *Baybridge Associates Ltd. Partnership v. Dept. of Rev.*, 892 P.2d 1003 (Or. 1995); *Woda Ivy Glen Ltd P’ship v. Fayette Cnty. Bd. of Revision*, 902 N.E. 2d 984, 991 (Ohio 2009).

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into account will not result in a determination of fair market value for that property.” To the extent the Guideline related to LIHTCs was adopted before *Cottonwood*, the ruling effectively rendered the Guideline moot at least as to the proper valuation of LIHTC property.

IT IS ORDERED denying Defendant’s Motions for Declaratory Judgment filed December 20, 2019 and reaffirming the ruling in *Cottonwood* that requires the LIHTC property to be valued using restricted as opposed to market rents to achieve a full cash value.