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# ARIZONA TAX RESEARCH ASSOCIATION

## ATRA SUPPORTS SB1050

### Arizona's Constitutional Gift Clause Challenges

In 2021, the Arizona Supreme Court's historic Gift Clause decision under *Schires v. Carlat* found that the City of Peoria violated the State Constitution's Gift Clause when it promised to pay up to \$2.6 million to a private university to offer an undergraduate degree program in the city.

Arizona's Gift Clause states that a municipality may not "give or loan its credit in the aid of, or make any donation or grant, by subsidy or otherwise, to any individual, association, or corporation."

Even before the *Schires* decision, the Maricopa Superior Court found under *Englehorn v. Stanton* in 2020 that the tax subsidy under the Government Property Lease Excise Tax (GPLET) between the City of Phoenix and a developer to build a high-rise residential tower in downtown Phoenix violated the Gift Clause. Specifically, the Court ruled that the benefits to the developer over the term of the lease were "grossly disproportionate" to the amount received by the public.

To determine a Gift Clause violation, the courts rely on the *Wisturber* two-pronged test to determine whether the expenditure has a public purpose and if the consideration received by the government is grossly disproportionate to the amount paid to the private entity. In considering a violation under the second prong, only the direct payments that are bargained for in the agreement are considered and any indirect, economic benefits are not.

### What is GPLET?

In the early 1980's, some cities began to aggressively use their tax exempt status for "economic development." The Legislature responded by creating the possessory interest tax to tax private concerns on certain government properties but also exempted existing deals, which the Court ultimately struck down. The Legislature responded again in 1996 and enacted GPLET to replace the tax on possessory interests.

GPLET is an excise tax that is levied on property owned by a city, town, county or county stadium district and leased to a private concern. Under GPLET, a government lessor can offer an 8-year abatement to shield the lessee from paying both property taxes and excise tax under GPLET if the property is located in a central business district.

GPLET has been a very controversial topic at the Capitol for decades that has led to several reforms; however, the recent court decisions have made all the reforms potentially moot. It is clear that the 8-year abatement under GPLET remains the most significant problem.

In 2010, 2017, and 2018, previous Legislatures attempted to reduce GPLET's role in our public finance system. From central planners picking winners and losers and creating significant inequities across property taxpayers to cost shifting budget impacts to the state general fund, GPLET has created a myriad of policy challenges.

### **Basis for ATRA's Support**

The *Englehorn* Gift Clause challenge was the first and most significant judicial review of the GPLET structure. In ruling against the tax incentive, the lower Court questioned that "...if payments under a future GPLET agreement must more closely approximate the amount of ad valorem taxes, does the GPLET have any remaining usefulness to incent redevelopment? In other words...this judicial officer questions whether the death knell for the GPLET's usefulness has rung."

A current court case under *Paulin v. City of Phoenix (aka Garfield)* challenges the constitutionality of a \$7.9 million development agreement between the City of Phoenix and a private real estate developer to construct a high-rise luxury apartment building in the heart of downtown Phoenix. The Court of Appeals heard oral arguments in November 2024 and will rule on the questions of whether the deal violates the Gift Clause and Conveyance to Evade Taxation Clause.

These GPLET deals continue to be made and taxpayers can't be expected to legally challenge every one of them. To reduce Gift Clause challenges to future GPLET agreements, SB1050 limits the current 8-year abatement period to 4 years so that it reduces the chances that the "give" doesn't exceed the "get."

***ATRA ASKS LAWMAKERS TO VOTE YES ON SB1050!***