The Role of Real Property Taxes in a Condemnation Action

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If one were to view the complexities of a condemnation suit from a lofty height, the prominent issue would be valuation. Let us say, for example, the landowner has not been persuaded that the condemning authority's price tag was reasonable. Looking closer one might see complicated leasehold questions. Barely discernible would be issues of real property taxes.

Yet in virtually every condemnation action, the County is or should be named as a party. The reason for naming the County as a defendant is elementary. The County Board of Supervisors has the duty to levy taxes on real property located within the County. Such taxes must be levied by the third Monday in August of each year. A.R.S. §§ 42-304 and 310. Once the tax is levied *eo instanti* it becomes a lien on the property. *In re Ecology Paper Products Company*, (Bkrtcy. 1982) 17B.R.281.[1]

Substantively, tax issues are a matter of direct concern for the County and the landowner. The condemning authority is not involved for its interest is in establishing value which of course does not involve liens. Notwithstanding, the condemnor should be aware of the tax lien problems and the resolution thereof for they surface often without warning during the settlement process which disposes of many cases without the travail of trial. Failure to anticipate tax liens can often endanger a wrought-out settlement that remains fragile at best.

To foresee when the question of tax liens will arise during the course of the action would be helpful for the parties involved. The ubiquitous tax issue surfaces suddenly without warning once the condemnor has circulated a stipulation for the withdrawal of the cash bond.[2]

The failure to include a provision for the payment of delinquent taxes

in the stipulation for withdrawal of funds causes undue delays and at times strains relations.

The County, a person in interest, is a necessary party to that stipulation. A.R.S. § 12-1116(H) (2). Not obtaining the approval of all interested parties to the stipulation blocks the rapid disbursement of funds. What is then required is an application for withdrawal of funds. What is then required is an application for withdrawal which is filed, objections thereto are raised, and then oral argument is calendared. With heightened anticipation for the release of funds, the application procedure is interminable.

To avoid the time-consuming practice of filing an application, one would have to redraft the stipulation to include the omitted provision for taxes and then embark on the dreaded voyage of recirculation for approval. When time is of the essence, that procedure always seems to raise the proverbial questions: Do you have the stipulation or who has it now?

An attending problem to an incomplete stipulation is one that does not state an accurate amount of accumulated interest. Interest accrues at the rate of sixteen percent per year prorated monthly as of the first day of each month. A.R.S. § 42-342.

What often happens is that the correct amount of accrued interest is obtained as of a certain month, but all too often unforeseen problems arise and the stipulation is put aside pending resolution of those problems. When it is propitious to circulate the stipulation, the tax data is likely to be outdated and the accrued interest almost certainly has become so. To avoid the confusion and delays inherent in recirculating a stipulation containing an inaccurate tax provision, renewed communication with the County before the stipulation is circulated is worth the effort.

Although the procedure touched upon for drafting an acceptable stipulation for the withdrawal of funds may seem to be unnecessary or not worthy of close attention, those negatives pale when compared to the outrage, frustration, and last minute rush which invariably ensue in the effort to obtain correct tax information and the immediate signatures of all parties. Such turmoil is expected because large sums are being withheld for no apparent justifiable reason or a substantial amount of potential daily interest is lost because the funds deposited with the Clerk of the County do not bear interest.

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In other words, knowledge of when the tax issue will arise and how to deal with it effectively and efficiently will eliminate one of the myriad problems encountered in a condemnation case. By disposing of the tax issue early in the case, there will be one less area to cause distraction from the paramount concerns of the remaining litigants.

A second nettling problem area has to do with the misconception of proration of taxes. In a sale between consenting parties, the prevailing practice is for the buyer and the seller to prorate the current year's taxes as of the close of escrow. Such a voluntary agreement fits within the normal concepts of being fair and reasonable. The full tax assessment is paid to the County and the parties are only paying for that portion of the tax year that they have actual possession.

In a condemnation case the landowner expects that the consensual apportionment practice will continue to prevail. When the landowner vacates the property after the condemning authority has obtained an order for immediate possession (§ 12-1116), he quite naturally objects to the payment of taxes on property that he no longer possesses. The wistful assumption is that there exists some mandatory mechanism for proration or that the amount accruing after he has vacated will be abated by the County.

On the other hand, the condemning authority, a tax-exempt entity such as the State, County, or City, often takes the position that proration is not applicable because tax-exempt entities do not pay taxes. Of course that theory is generally true but not always so.[3] The condemnor does not want to shoulder any tax load which also is an understandable and reasonable position.

In litigation, the position of the County is that there is no statutory basis for apportionment of the tax and the County has no authority to forgive the tax for the abatement statute is not applicable. A.R.S. § 42-521. The taxes are a lien on the property. For the condemnor to obtain clear title, those tax liens as well as any other encumbrances must be discharged by payment which comes from the final award. Since the landowner is entitled to the award less the amount of all encumbrances,

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he is the one who pays the taxes.[4]

The misconception by the landowner and by the condemning authority is an area of mutual concern for all parties because it causes unnecessary problems that surface only after a settlement figure has been reached. The condemning authority does not want to pay taxes – in essence pay more for the property – and the landowner, having agreed to accept a reasonable price for his land, does not want to receive less than the agreed upon amount. In essence, the settlement is jeopardized for neither party properly understood that taxing scheme nor foresaw the difficulties flowing therefrom.

In an effort to avoid the tax liability in order to preserve the settlement, both parties often rely upon A.R.S. § 42-342, which divides payment of the tax bill into two installments with the first half payable by October first of the current year and the second half payable by the following March first.

The payment statute is only for the convenience of the taxpayer; it has nothing to do with satisfying or voiding the lien. Yet the installment argument is a frequently advanced reason why the taxes do not have to be paid or payment can be made in accordance with the statutory payment schedule after title has passed to the condemning authority – one that passes free and clear of all liens.

Another common attempt to solve the tax dilemma is an effort to avoid opening Pandora's box is reliance upon A.R.S. § 12-1123(D). By implication, the Assessor is statutorily directed to remove the defendant's property from the tax rolls upon recordation of the order for immediate possession.

The removal argument is couched in terms of removal of the property from the tax rolls for either the entire year or so much of the taxes that can be apportioned to the period of time subsequent to the condemnor's taking possession of the property.

Neither of those arguments withstand analysis and they do nothing but protract an impasse.

The purpose of the phrase "shall immediately remove from the tax rolls," § 12-1123(D), was to eliminate an unjust situation: A property owner's parcel was still subject to a levy of tax after a condemning authority took possession but before title passed. If taxes were levied during the pendency of the lawsuit, which could be drawn out, and after possession but before title passed. If taxes were levied during the pendency of the lawsuit, which could be drawn out, and after possession was obtained but before title passed, the taxpayer's parcel was encumbered by a tax lien. The taxes did not increase the value of the property but instead decreased it by the amount of the tax lien. To alleviate this obvious injustice, § 12-1123(D) was enacted.

Statutes granting exemptions from taxation are to be strictly construed and the presumption is against a tax exemption. *State Tax Commissioner v. Graybar Electric*, 86 Ariz. 253, 344 P.2d 1008 (1959).

The phrase "shall immediately remove from the tax rolls" means that the property is exempt from future taxation. If the phrase, which is not a paragon of clarity, were interpreted to mean the removal from existing tax rolls, there would be no prohibition from deleting year upon year of delinquent taxes from the rolls. The removal language was not meant to extinguish pre-existing tax liens. The only way to extinguish a tax lien, other than by the doctrine of merger, is by paying the tax or by a tax sale. *Packard Contracting Company v. Roberts*, 70 Ariz. 411, 222 P.2d 791 (1950). To interpret the statutory language any way other than to remove from future tax rolls would give the property owner a tax exemption never authorized by the Legislature.

Therefore, if the County has levied a tax on property that the condemn-

ing authorities subsequently take possession of, the property is encumbered with a statutory tax lien that is not extinguished by recording the order for immediate possession. In this context the lien is extinguished only be payment of the taxes.

If counsel, especially for the condemning authority, would obtain the tax data before committing to a settlement figure, more settlements would not have to be renegotiated. Certainly, an understanding why taxes are not prorated, forgiven, or compromised, or the legal effect of recording the order for immediate possession as well as an awareness of the necessity to record it in the first instance will all serve everyone's interest.

In conclusion, an understanding about the role that taxes play in a condemnation case, albeit minor, will inure to the advantage of all parties for hard-fought settlements need not be excruciatingly reopened, expensive and exasperating delays can be successfully avoided, as well as frayed tempers.

As with so many aspects of life, if one had knowledge that enabled him to perceive what is foreseeable and inevitable and then to deal with that in an effective, frictionless manner, one could then devote his energies without distractions to the issues calling for vigorous action.

References

1. Though the *Ecology* case dealt with personal property taxes, real property taxes attach as liens to real estate the instant the tax is levied. Although A.R.S. § 42-312 states that the lien exists as of January 1 for the tax year, the lien is inchoate until the tax is levied. *Territory, ex rel. Devine v. Perrin*, 9 Ariz. 316, 83 P.361 (1905). The identity of the lienor and the property subject to the lien are known but the amount of the lien is unknown. *United States v. Pioneer American Insurance Company*, 374 U.S. 84, 83 S.Ct. 1651, 10 L.Ed.2d 770 (1963).

2. The condemning authority by virtue of A.R.S. § 12-1116(H) can take immediate possession of the property after obtaining an order authorizing such by posting a surety or cash bond. If a surety bond is posted, the tax issue will not arise at this juncture.

3. If the state is the condemning authority and relocation assistance is applicable, A.R.S. § 28-1845(3) requires reimbursement to the owner for "[t]he pro rata portion of real property taxes which are allocable to a period subsequent to...the effective date of the possession of such real property by the state..."

Also, if the condemnor wants to break through an impasse in settlement negotiations where taxes have become a thorny point, the offering price for the parcel can be raised to cover the newly discovered tax liability.

4. Real property taxes are not the personal obligation of the owner. *Peabody Coal Company v. Navajo County*, 117 Ariz. 335, 572 P.2d 797 (1977). Whereas personal property taxes are a debt of the owner. A.R.S. § 42-616.