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July 13, 1989

The Honorable Dave Carson
Arizona State Representative
State Capitol - House Wing
Phoenix, Arizona 85007

Re: I89-068 (R86-079)

Dear Representative Carson:

You have inquired about the legality of a city raising monies to fund a self-insurance plan through a lease-leaseback of city property entered into with a nonprofit municipal property corporation (corporation) previously created by the city.

The relevant facts are as follows. The city leased a municipally-owned building to the corporation for ten years at a lump sum rental.^{1/} The corporation, in turn, leased the facility back to the city for the same term.

The corporation funded its lump-sum lease payment by the issuance of tax-exempt municipal bonds. The principal and interest on these bonds is to be paid from the city's lease payments. The city's lease payments are backed by a pledge of all excise taxes ^{2/} which the city presently collects or may collect in the future, or which are allocated to the city from the State, except certain amounts which are allocated by law for other purposes. The city covenanted to maintain the excise taxes so that revenues received from them will equal at least three times the rental requirements due under the lease. The

^{1/} Although in the fact situation presented to us, the lease-leaseback of the municipal building is purely a financing measure, the city in the past has used the corporation to acquire property and to construct facilities.

^{2/} In fact, the pledge in the case brought to our attention includes some taxes other than excises, but for the purpose of this opinion, we presume the pledge is of excise taxes only.

transaction documents provide that the lease payments and the bonds do not constitute general obligations of the city and that the city is not liable for payments from ad valorem taxes. The official statement disseminated in connection with the bond issue shows that, for the fiscal year ending June 30, 1986, the city's ad valorem tax levy was just over \$800,000. Other major sources of general fund revenues totaled over five million dollars (city and state sales taxes and state revenue sharing). Property tax receipts, therefore, constitute a relatively small portion of the source of the city's general funds.

Your request raises the following issues:

May a city legally create and utilize a municipal property corporation?

May a city legally enter into a lease-leaseback arrangement involving municipal real property?

Finally, the basic question presented by your request is whether a municipal obligation ^{3/} secured by a general pledge of excise tax revenues which would otherwise be available for general governmental purposes constitutes an "indebtedness" under Ariz. Const. art. IX, § 8, which imposes debt limits on municipal corporations and other political subdivisions.

I. and II.

May a city legally create and utilize a municipal property corporation?

May a city legally enter into a lease-leaseback arrangement involving municipal real property?

Both the Supreme Court of Arizona and Division One of the Court of Appeals have at least assumed that a city may validly make use of a nonprofit municipal property corporation.

^{3/} The obligation in this situation is the city's obligation to make lease payments.

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Central Arizona Water & Ditching Co. v. City of Tempe, 140 Ariz. 119, 680 P.2d 820 (App. 1984) involved a contractual dispute over the construction of a water treatment plant for Tempe. The city had used a municipal property corporation very similar to the corporation involved in your request. The court said, "[i]n essence, the [municipal property] Corporation acts as a financing vehicle for the construction of the City's public improvements." 140 Ariz. at 120, 680 P.2d at 830. In a footnote to this statement, the court recognized the validity of this financing tool: "CAWDCO concedes and we agree that there is nothing illegal in this arrangement. See City of Phoenix v. Phoenix Auditorium & Convention Center Association, Inc., 100 Ariz. 101, 412 P.2d 43 (1966) (opinion on rehearing)." Id at n.1.

We think there can be no doubt that a city legally may utilize a municipal property corporation to finance improvements. The question remains, however, whether such a corporation can be used, not to finance acquisition of property or construction of improvements, but only to raise funds for other municipal purposes.

The general rule is that a charter city may do anything permitted under its charter and not prohibited by the Constitution of Arizona or by general law. Prendergast v. City of Tempe, 143 Ariz. 14, 17, 691 P.2d 726, 729 (App. 1984). We find nothing in the constitution or laws which would prohibit the use of such a corporation for fund-raising purposes.

Also, we find no constitutional or statutory prohibition against a city leasing its real property to others, if the city receives adequate consideration. City of Tempe v. Pilot Properties, Inc., 22 Ariz. App. 356, 527 P.2d 515 (1974); see Kromko v. Arizona Board of Regents, 149 Ariz. 319, 718 P.2d 478 (1986), and Prescott Community Hospital Commission v. Prescott School District No. 1, 57 Ariz. 492, 115 P.2d 160 (1941). In the situation under scrutiny here, not only is the consideration adequate, but the city will continue to have uninterrupted use of the facility through the leaseback.

Whether the city has power under its charter to lease municipal property and whether the corporation has the power under its articles of incorporation to act in this manner are issues of municipal concern which are not appropriately addressed by the Attorney General in this opinion. See Ariz. Att'y Gen. Ops. I81-086 and I80-058.

III.

Does a city's general pledge of excise tax revenues create a debt under Ariz. Const. art. IX, § 8, which in some instances would have to be referred to the people?

In City of Phoenix v. Phoenix Civic Auditorium & Convention Center Association, Inc., 99 Ariz. 270, 408 P.2d 818 (1965) (Convention Center I), the court held that Phoenix's obligations to make payments under a proposed lease constituted debt under Ariz. Const. art. IX, § 8, because the obligation might be paid in part from the "general fund" or from "general taxes." 99 Ariz. at 286, 408 P.2d at 829. Because this obligation would have caused the city to exceed its constitutional debt limitation, the court held the proposed lease invalid.^{4/}

All parties and amicus curiae the City of Tucson joined in a motion for rehearing urging the court to approve a modified lease arrangement whereby, the city's lease obligation would be payable only from convention center revenues and from a general pledge of excise tax revenues. The primary authority cited to the court in the joint motion for rehearing was the following passage from Switzer v. City of Phoenix, 86 Ariz. 121, 124, 341 P.2d 427,428 (1959):

The authorities dealing with this problem are not entirely in accord, but the weight generally is to the effect that an obligation payable from a special fund created by the imposition of fees, penalties, or excise taxes and for the payment of which the general credit of the taxing authority is not pledged is not a debt within the meaning of

^{4/} In the situation you brought to our attention, the city's debt limitation apparently would not have been exceeded, even if the lease obligation were held to be a constitutional debt. See Ariz. Const. Art. IX, § 8, which permits a city to incur debts up to six percent of its assessed valuation without an election. We note in passing, however, that indebtedness evidenced by general obligation bonds must be approved by the electorate even if the subdivision's debt limit will not be exceeded. Tucson Transit Authority v. Nelson, 107 Ariz. 246, 248, 485 P.2d 816, 818 (1971).

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constitutional debt limitations. See Stone v. City of Hobbs, 54 N.M. 237, 220 P.2d 704, and Annotation 100 A.L.R. 878; Gruen v. Tax Commission, 35 Wash.2d 1, 211 P.2d 651. We will follow the weight of authority at least to the extent where, as here, the fund from which the obligations are to be paid is created by voluntary contributions of the state to the city.

The Convention Center I parties asked the court to apply this authority more broadly and to hold that a general pledge of excise taxes does not create a constitutional debt. The court did as requested, quoting these authorities in its clarifying opinion. City of Phoenix v. Phoenix Civic Auditorium & Convention Center Association, Inc., 100 Ariz. 101, 103, 412 P.2d 43, 44 (1966) (Convention Center II).

Convention Center II is on point and requires us to find that a city's pledge of excise tax revenues does not create a debt under Ariz. Const. art. IX, § 8. This is the law in Arizona and will remain the law unless and until the holding of Convention Center II is overruled by the Supreme Court of Arizona.^{5/}

Sincerely,



BOB CORBIN
Attorney General

BC/it/pcd/ms

^{5/} We do note that the precedent in Arizona is now in the minority of those state courts who have decided the issue.