SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2007-013766 04/02/2008

CLERK OF THE COURT
JUDGE ROBERT E. MILES K. Ballard
Deputy

MEYER TURKEN, et al. CLINT BOLICK

v.

PHIL GORDON, et al. ANDREW M FEDERHAR

LISA T HAUSER
GARY VERBURG
GREGORY W FALLS

RULING

The Court has had under advisement the City of Phoenix Defendants' (collectively, the "City") Motion for Summary Judgment, the Motion for Summary Judgment by Defendant NPP City North, LLC (the "Developer"), and Plaintiffs' Motion for Summary Judgment, and now rules as follows:

THE MOTIONS TO STRIKE

As a preliminary procedural matter, the Defendants have moved to strike the Plaintiffs' controverting statement of facts and the affidavits of Drs. Pavlov and Wells, and have also opposed the filing of an *amicus* brief by the National Federation of Independent Business Legal Foundation or, alternatively, have moved to strike portions of that brief. Plaintiffs have moved to strike the affidavit of Elizabeth DeMichael and part of the City's reply in support of its motion to strike the Pavlov and Wells affidavits. The parties are advised that the Court has reviewed all of the materials and briefs that have been filed in this action and has given them such consideration as it has deemed appropriate in light of the issues raised by the cross-motions for summary judgment. Therefore, the various cross-motions to strike are **denied**.

FACTUAL BACKGROUND

This case arises from a Parking Space Development and Use Agreement (the "Agreement") entered into between the City and the Developer relating to a massive office, residential, retail, and hotel development known as City North to be located near 56th Street and the Loop 101 Freeway in Phoenix. The Agreement was authorized and executed pursuant to an ordinance duly adopted by the Phoenix City Council (the "Ordinance").

The Agreement provides that after the Developer builds 1.2 million square feet of retail, restaurant, and hotel space at this site, and also builds parking garages in which 3,180 spaces are granted to the City for free use by the public for 45 years, including at least 200 spaces for a "park and ride" location, the City will pay an annual use fee to the Developer equal to 50% of the transaction privilege ("sales") taxes actually collected by the City from the City North project during the previous year. Thus, if the project is constructed as contemplated, the City will pay the Developer one dollar for every two dollars the City actually receives in sales tax revenue from the project. The payment period is for 11 years and 3 months or until the City has paid a maximum of $97.4 million. After that time period or payment of the maximum amount, whichever occurs first, all of the sales tax revenues from the project will remain with the City. No money will be paid by the City unless and until the Developer builds the retail space and the parking garages, and the City actually receives sales tax revenues from City North retailers.

From the City's point of view, the Agreement was designed, in large part, to assure that the project would include a very significant retail and hotel component that would generate substantial sales tax revenues for the City – by some estimates as much as one billion dollars – and would keep potential sales tax revenues from being lost to surrounding cities. The City also asserts that, in addition to the substantial sales tax revenues that will be generated, the Agreement will, among other things, promote "urban core" development, provide hundreds if not thousands of jobs, decrease pollution, and secure free and convenient parking for the public. The City Council made an express finding that, without the Agreement, the City North project would not be built in the same time, place, or manner as contemplated by the Agreement.

In contrast, the Plaintiffs argue that the Agreement is simply a mechanism to subsidize the construction of a luxury shopping mall, the beneficiary of which is just a single developer. Thus, Plaintiffs assert that the Ordinance, which likely will result in substantial payments by the City to the Developer pursuant to the Agreement, violates the Equal Privileges and Immunities Clause, the Special Law Clause, and the Gift Clause of the Arizona Constitution.

BASIC PRINCIPLES

The party challenging a law's constitutionality bears a heavy burden of establishing that it is unconstitutional. *Martin v. Reinstein*, 195 Ariz. 293, 302, 987 P.2d 779, 788 (App. 1999). Thus, legislative enactments are presumed to be constitutional and any doubts on the subject must be resolved in favor of constitutionality. *Ariz. Downs v. Ariz. Horsemen's Foundation*, 130 Ariz. 550, 554, 637 P.2d 1053, 1058 (1981); *Council of City of Phoenix v. Winn*, 70 Ariz. 316, 220 P.2d 222 (1950). However, where the facts so require, the Court will not refrain from declaring a legislative act unconstitutional. *Republic Inv. Fund I v. Town of Surprise*, 166 Ariz. 143, 148, 800 P.2d 1251, 1256 (1990).

THE EQUAL PRIVILEGES AND IMMUNITIES ("Equal Protection") CLAUSE CHALLENGE

The Arizona Constitution provides in Article 2, Section 13, that "no law shall be enacted granting to any citizen, class of citizens, or corporation other than municipal, privileges or immunities which, upon the same terms, shall not equally belong to all citizens or corporations." Where, as here, a law does not involve a suspect classification, the law may be deemed unconstitutional under this equal protection provision only if it has no conceivable rational basis to further a legitimate governmental interest. *Ariz. Downs v. Ariz. Horsemen's Foundation*, 130 Ariz. 550, 555, 637 P.2d 1054, 1058 (1981).

Setting aside for the moment the question of whether this Ordinance is a "law" within the meaning of the Equal Protection and Special Law Clauses, Plaintiffs do not mount a serious Equal Protection challenge in any event, stating only that "if" the Ordinance fails to survive rational basis scrutiny, it violates both the Equal Protection and Special Law Clauses. However, Plaintiffs fail to carry their burden of demonstrating that there is no conceivable rational basis for the City's action, *Heller v. Doe by Doe*, 509 U.S. 312, 320-21 (1993), and this Court cannot conclude that the benefits the City Council believes the Agreement carries with it, as discussed above, are not legitimate governmental interests or that the Agreement provides no rational basis to further those interests. *See, e.g., FCC v. Beach Communications, Inc.*, 508 U.S. 307, 313 (1993) ("…equal protection is not a license for courts to judge the wisdom, fairness, or logic of legislative choices."); *Vance v. Bradley*, 440 U.S. 93, 97 (1979) ("The Constitution presumes that, absent some reason to infer antipathy, even improvident decisions will eventually be rectified by the democratic process and that judicial intervention is generally unwarranted no matter how unwisely we may think a political branch has acted."). Thus, Plaintiffs' Equal Protection challenge fails.

THE SPECIAL LAW CLAUSE CHALLENGE

Plaintiffs also challenge the Ordinance as a "special law," claiming that it violates three subsections of Arizona Constitution Article 4, pt. 2, § 19.[1] Although the special law provision involves similar policies as the Equal Protection Clause, a law may withstand equal protection review, yet still be found unconstitutional as a special law. *Republic Inv. Fund I v. Town of Surprise*, 166 Ariz. 143, 149, 800 P.2d 1251, 1257 (1990).

Before undertaking the special law analysis, the Court must determine what "law" is legitimately subject to challenge. Economic development agreements, and particularly retail development tax incentive agreements like the Agreement in this case, have been expressly authorized by the legislature. A.R.S. § 9-500.11. That statute does not require a city or town to adopt an ordinance in order to enter into such an agreement. However, the Phoenix City Charter requires that all actions for the expenditure of public monies of more than $8,600.00 shall be taken by ordinance. City of Phoenix Charter, Chap. IV, Section 12; Phoenix City Code § 2-4(b).

Thus, for example, when Phoenix purchases property (as the legislature has authorized it and other cities and towns to do pursuant to A.R.S. § 9-241) from a specific seller for a price exceeding $8,600, the City Council must adopt an ordinance to effect that purchase. If these ordinances are "laws" within the meaning of the special law provision, then they would all be unconstitutional under Plaintiffs' argument because, by authorizing a specific transaction with a specific seller, they are not laws of general applicability. Rather, each individual ordinance relates to a class of one. The Court concludes that where an ordinance, like the Ordinance in this case, is merely the procedural mechanism necessary to approve and implement a specific transaction of a type that previously has been authorized by statute, the ordinance is not a "law" for purposes of the Special Law Clause and, therefore, not unconstitutional as a special law so long as the authorizing statute itself is not an unconstitutional special law.

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[1] Plaintiffs assert that the following provisions have been violated:

> No local or special laws shall be enacted in any of the following cases, that is to say:
> . . .
> 9. Assessment and collection of taxes
> . . .
> 13. Granting to any corporation, association or individual, any special or exclusive privileges, immunities, or franchises
> . . .
> 20. When a general law can be made applicable

Accordingly, the only "law" that might be subject to special law challenge in this case is A.R.S. § 9-500.11. Plaintiffs, however, have not challenged the constitutionality of that statute, and that alone is sufficient to defeat their special law argument. Moreover, because that statute does not appear to create any classification of persons, places, or things, special law analysis, which is based on whether legislative classifications are appropriate, simply does not apply to this statute. In short, Plaintiffs' special law challenge also fails.

THE GIFT CLAUSE CHALLENGE

The principal thrust of Plaintiffs' argument that the Ordinance is unconstitutional lies with the Gift Clause, which provides:

> Neither the State, nor any county, city, town, municipality, or other subdivision of the State shall ever 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…

Ariz. Const. Art. 9, § 7. In *Wistuber v. Paradise Valley Unified School Dist.,* 141 Ariz. 346, 687 P.2d 354 (1984), which the parties agree is controlling precedent, our Supreme Court established a two-prong test for analyzing transactions under the Gift Clause. First, the provision of public money to a private enterprise must serve a public purpose, *id.,* at 348; and, second, "the value to be received by the public [cannot be] far exceeded by the consideration being paid by the public." *Id*., at 349. In analyzing whether those tests have been satisfied, the Court "must give appropriate deference to the findings of the governmental body," but it must also consider "the reality of the transaction both in terms of purpose and consideration," taking a "panoptic view of the facts of each transaction." *Id*., at 349.

Public Purpose

The Agreement recites, and the City argues, that the Agreement serves various public purposes, including:

- the creation, retention, and expansion of retail uses and employment in the community;
- stimulation of economic development in Phoenix;
- generation of substantial additional sales tax revenues;
- creation of significant, free public parking, including a park and ride facility that will encourage the use of public transportation; and
- development of an urban core that will reduce congestion, traffic, and pollution.

Plaintiffs counter that argument by asserting, in essence, that these stated public purposes are illusory because the object of the Agreement is a "high-end luxury mall" and, therefore, the Agreement really provides benefits only to the Developer, not to the public.

The Court of Appeals in *City of Tempe v. Pilot Properties, Inc.*, 22 Ariz. App. 356, 527 P.2d 515 (App. 1974) has implied that the "public purpose" prong is not a difficult test for a governmental entity to meet, noting that if "a 'public purpose' was the only 'criteria by which the validity of and appropriation of public funds is to be measured, there would be hardly any limit upon the right of the state, county, city, or school districts to appropriate monies to a private corporation.'" *Id.*, at 362 (citation omitted)[2] Moreover, Plaintiffs offer no facts to dispute that the benefits the City anticipates receiving from the Agreement will not be realized.

Taken individually, any of the stated benefits standing alone would likely qualify as a public purpose. *See, e.g.*, *id.,* at 361 (stating that a public purpose can be found, for example, in making the atmosphere cleaner). Taken together, they undoubtedly do.

However, Plaintiffs also assert that because the Developer will retain ownership of the parking garages, even though the public has free use of more than 3,000 spaces within them for 45 years, the Agreement violates the Gift Clause, stating, "If the City owned the garage, it would constitute a public purpose." Plaintiffs' Reply in Support of Plaintiffs' Motion for Summary Judgment, at 6. Thus, while Plaintiffs acknowledge that the public purpose prong would be satisfied if the City owned the garage, they claim a public purpose does not exist because the City and the public only have the right to use parking spaces. The Court concludes, in the context of this case, that is not a meaningful distinction.

First, the public purpose related to the parking garages is the availability of free public parking. That parking will be no more or less available because the City has a use agreement for

[2] It is noteworthy, although not dispositive as the City argues, that the legislature apparently believed that retail development tax incentive agreements like the Agreement serve a public purpose, because it enacted A.R.S. § 9-500.11 to specifically authorize cities and town to enter into them. See *Kromko v. Ariz. Bd. of Regents*, 149 Ariz. 319, 320, 718 P.2d 478, 479 (1986) (By providing for the type of transaction at issue, the legislature had statutorily recognized its public benefit). Also noteworthy is that the legislature subsequently enacted A.R.S. § 42-6010 which, with certain exceptions, prohibits retail development tax incentive agreements by cities or towns in metropolitan areas with a population of more than two million persons. This later statute does not affect the Agreement or the Court's decision in this case because it was enacted after the Agreement was made. It does, however, reflect the legislature's changing or evolving views about tax incentive agreements, at least in major metropolitan areas. It also demonstrates that opponents of such agreements can have their policy concerns addressed effectively through the political process.

spaces in the garages as opposed to ownership of them.[3] Second, ownership cannot be an essential element to a valid transaction because cities and towns are expressly authorized to "purchase, receive, hold, lease, and convey property." A.R.S. § 9-241 (emphasis added). If Plaintiffs' argument were accepted, then every lease of property by a municipality would involve an unconstitutional gift because the municipality would not own the property.

The Court concludes that the benefits of the Agreement serve a public purpose and, therefore, the first prong of the Gift Clause analysis has been satisfied.

Fair Consideration

Even where an expenditure of public funds is for a public purpose, the Gift Clause "may still be violated if the value to be received by the public is far exceeded by the consideration being paid by the public." *Wistuber*, at 349. Here, taking a panoptic view of the transaction, the value to be received by the public is both non-monetary and monetary.

The principal non-monetary consideration is the right to use, for 45 years, over 3,000 spaces in parking garages to be built by the Developer. While Plaintiffs argue that the parking structures would have been built in any event, they do not dispute that the fair market value of that right is "in line" with the $97.4 million that is the maximum amount payable under the Agreement. The other non-monetary aspects of the Agreement – job creation, stimulation of economic growth, reduction of traffic and pollution, etc. – are, of course, more difficult to quantify, but could be substantial.[4]

The monetary value to be received by the Agreement is based on the sales tax revenues to be generated by the City North project from the 1.2 million feet of retail space that the Developer must build before it can receive any payment from the City. Once that retail space is operating, the Agreement is structured so that the City will pay the Developer one dollar for every two dollars that the City actually receives in sales taxes from the City North project, up to a maximum of $97.4 million. In other words, "the consideration being paid by the public" can never exceed "the value to be received by the public," much less "far exceed" it. Moreover, after

[3] While the use agreement may not be as valuable as ownership because it ends in 45 years, that fact goes to the consideration prong of the Gift Clause test, not to the public purpose prong.

[4] Economist Elliott Pollack has estimated that the City North project will have an annual retail economic output of $276 million, and a total annual economic impact of $1.9 billion, although these amounts would be reduced by some "leakage" of economic output from other Phoenix shopping malls and retailers. While Plaintiffs' expert, David Wells, states that Pollack's estimate of the gross economic impact "is inaccurate," he does not state what he believes the "actual" economic impact will be. Wells' criticism of the City's anticipated payments under the Agreement appears primarily aimed at the quality of the jobs to be generated by the project. The Court will not second guess the City Council's views on whether it is good policy to develop those types of jobs.

the earlier of 11 years and 3 months or the payment of $97.4 million to the Developer under the Agreement, the City is projected to receive hundreds of millions of dollars in future sales taxes to use for any public purpose it chooses. Thus, even if one ignores or substantially discounts the value of the non-monetary benefits contemplated by the Agreement, the monetary value to be received by the public will far exceed what the public will pay.

Plaintiffs' argument that the value to the public is illusory appears to be based on the speculative premise that even without the Agreement the City North project would have been built at the same place, in the same time frame, and on the same scale (including with 1.2 million square feet of retail) as is contemplated by the Agreement. The Court cannot accept that premise on faith, nor will it substitute its judgment for that of the City Council on that issue.[5] While it is likely that something would eventually have been built at this location, there is no guarantee that what would be built would contain a sales tax generating component anywhere approaching what is contemplated by the Agreement.[6] The Agreement was designed to ensure that the project that is built provides the contemplated benefits – particularly the substantial tax revenues – on a schedule and at a level that is more advantageous to the public than some other, differently configured project that might be built at the site.

The burden of demonstrating disproportionality of consideration rests with the party claiming a governmental expenditure is a gift. *Maricopa County v. State of Arizona,* 187 Ariz. 275, 281, 928 P.2d 699, 705 (App. 1996). Plaintiffs have not met that burden. Therefore, the Court concludes that the fair consideration prong of the Gift Clause analysis has also been satisfied.

Based upon the foregoing,

IT IS ORDERED granting the Motions for Summary Judgment of the City and the Developer.

IT IS FURTHER ORDERED denying the Plaintiffs' Motion for Summary Judgment.

[5] Even Plaintiffs' expert, Andrey Pavlov, candidly admitted at his deposition that he could not guarantee that the City North project would be built in the same time, place, or manner without the Agreement.

[6] Plaintiffs do not appear to dispute that non-retail construction generates more profit for developers than does retail construction.