



PEORIA GIFT CLAUSE CASE—BACKGROUND

Executive Summary

The Goldwater Institute is suing the City of Peoria to prevent it from giving away more than \$2.5 million to private businesses.

In July 2015, Peoria entered into an agreement to give up nearly \$2 million in taxpayer money to Huntington University (“HU”), a private business. To get the money, Huntington doesn’t have to do a thing for Peoria’s taxpayers. It simply has to get accredited, offer classes, and enroll students—things it would do anyway if it wants to open its doors and run a successful university.

Peoria is also giving \$738,000 in taxpayer money to Huntington’s landlord, a private real-estate investment firm, to renovate property the landlord owns. But that doesn’t benefit taxpayers; it only benefits Huntington and the landlord, which will profit from the lease. Rather than letting customers decide whether a business has what it takes to succeed, the government tries to manipulate the outcome.

Essentially, Peoria is paying a private business to do what it would do anyway. The city gets nothing in return for the taxpayer money. It would be wrong for government to hand taxpayer money to Starbucks just to serve the coffee it’s already serving, or to pay McDonald’s to sell hamburgers. But that’s exactly what government is doing with Peoria taxpayers’ dollars.

Those handouts are illegal. Arizona’s Constitution, like those of 46 states, forbids the government from giving or lending taxpayer money to private businesses simply to benefit those businesses. While the government can spend money on public projects, and can provide certain kinds of incentives to encourage business growth, it can’t simply give away the money it takes from taxpayers in order to enrich private companies—whether they be restaurants, tourism companies, or private colleges.

Peoria taxpayers at large do not benefit from the city giving away their money. They don’t get lower tuition or admission preference at Huntington University, for example, and they don’t get to use the property the way they get to use public parks or roads that the government pays for. But even though they’re forced to subsidize a private company, the taxpayers are still forced to bear all the risks. If Huntington fails—the way St. Xavier University in Gilbert recently did—taxpayers are stuck with the bill, and students are left with no school, while Huntington can walk away from its debt.

Unlawful deals like this discourage businesses from shouldering risks responsibly and instead encourage them to get favors from lawmakers who can dip into taxpayers’ wallets. Then, if the venture succeeds, the company keeps the profits, but if it fails, the costs fall on taxpayers. Peoria’s willingness to lavish private businesses with public money creates an elite group of private businesses that get special government treatment—and a disfavored class of businesses whose owners compete fairly, often risking their own money, credit, and good names, and don’t go asking for handouts of government cash.

\$738,000 or \$2 million might seem like a drop in the bucket to a city or county, but all the subsidies officials give away to private business all over the state and the nation add up to a tremendous amount of money, spent to prop up businesses that can't—or won't—compete fairly. That's money that could have been left in the hands of the taxpayers who earned it, to spend on the education of their choice or however else they see fit. And the risks are real. This summer, St. Xavier University, also a private institution with stellar credentials, had to shut its doors, less than a year after opening even though the Town of Gilbert gave it millions of taxpayer dollars to help launch it. Not only did taxpayers lose, but students were left in the lurch.

Even if the countless examples of taxpayer-funded businesses folding aren't enough to keep lawmakers out of citizens' pockets, the law should be. Arizona's constitutional prohibition on gifts of public money means that government may not spend taxpayer money unless the expenditure serves a *public* purpose—not a private one—and only if it yields an adequate return for taxpayers. In this case, Peoria taxpayers are not served by the private university, nor do taxpayers receive adequate value for their money. Instead, the government is funding a private business that's set up to serve paying customers—all at real financial risk. That isn't fair to the hard-working people whose earnings the city taxes—and whose rights the Constitution protects.

The Problem

Peoria is giving away taxpayer money to private businesses; in return, the businesses merely have to do what they would have done even if they hadn't received a subsidy: operate.

In July 2015, the City of Peoria decided it would spend taxpayer money on a “targeted”—but private—industry to achieve its “economic development goals.”¹ Specifically, the City Council agreed to give Huntington University, a private business, up to \$1.875 million for completing certain “performance thresholds,” which include submitting a marketing plan to the City, receiving accreditation, offering coursework, and enrolling students. Essentially, taxpayers will pay nearly \$2 million for the privilege of making sure Huntington does what it must do anyway.

A month later, the city approved a new scheme, the P83 District Building Reuse Program, allowing commercial property owners to receive taxpayer money for “commercial reinvestment activities.”² This new program sweetened the deal for Huntington by offering nearly \$738,000 to the school's new landlord, Arrowhead Equities, to renovate the building Huntington will use as its campus. And Arrowhead, rather than having to pay for its own renovations like other commercial development firms, gets a windfall in the form of a government handout *plus* the rent it will receive from Huntington.

What do Peoria taxpayers get for their money? Not lower tuition or admission preferences—or even good jobs. In fact, hasn't promised to give any jobs to local residents and most of the jobs Huntington would create are low-paying, part-time adjunct faculty positions. The only thing the taxpayers really get for their money is a new business. But new businesses are supposed to go to the bank for a start-up loan—not get a government handout.

Giving taxpayer money to private businesses is risky for taxpayers and students alike. In 2015, the Town of Gilbert entered into an economic development agreement with St. Xavier University, also a private institution with stellar credentials, on the expectation that it would boost the town's economy and transform the downtown area. Less than a year after opening its doors, however, the university announced it would be shutting those

¹ Economic Development Activities Agreement between the City of Peoria, Arizona, and Huntington University, July 7, 2015.

² Minutes of the Peoria City Council, August 26, 2015; Economic Development Activities Agreement between the City of Peoria and Arrowhead Equities LLC, March 15, 2016.

doors for good, due to uncertainty in future funding. Taxpayers and students were left in the lurch.³ City officials expressed surprise,⁴ but they shouldn't be. After all, failure is always a possibility on the private market—which is one reason taxpayers shouldn't be forced to become investors against their will.

In fact, these types of subsidies aren't just unwise; they're illegal. The Arizona Constitution forbids the government from giving or lending taxpayer money to private enterprises.

The Law

The Gift Clause of the Arizona Constitution provides that “[n]either 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, or become a subscriber to, or a shareholder in, any company or corporation, or become a joint owner with any person, company, or corporation. . . .”⁵

This language is absolute. Over the years, however, the Arizona Supreme Court has ruled that government can spend taxpayer money on private undertakings, under certain limited circumstances. First, the expenditure must be for a public purpose. And second, the government must receive adequate “consideration” in return—that is, some specific asset or benefit of equal benefit—rather than some indirect social benefit, or mere good will.⁶ Subsidizing or donating money to a private company violates this rule.

Arizona Courts have explained that the reason government must receive something of adequate value in return for taxpayer money is that otherwise an expenditure “might so greatly exceed the consideration received in return as to amount to a subsidy to a private entity.”⁷ In the seminal case, *Turken v. Gordon*, the state Supreme Court explained that “a city’s purchase of a garbage truck would undoubtedly serve a public purpose. Purchasing the truck for twenty times its fair value, however, would constitute a subsidy to the seller.”⁸

But Peoria isn’t purchasing *any* product or service *at all* with the money it’s giving to Huntington. Instead, taxpayers are merely paying for reassurance that Huntington is doing what it already intends to do: open its doors to students. True, Peoria hopes the deal will bring economic benefits to the city, but these are merely *indirect* benefits, not contractual obligations, and the Arizona Supreme Court has said that indirect benefits do not count as consideration under the Gift Clause.⁹

As to Huntington’s landlord, Arrowhead Equities, taxpayers get absolutely nothing in exchange for their money. The purpose of the District Reuse Program “is to encourage a more diverse use of existing vacant buildings in the District to include professional office, entertainment and retail tenants as an alternative to continuing to add restaurant users that have a historical failure rate in the District.”¹⁰ So, in exchange for \$738,000, of public money, all Arrowhead promises is that it will renovate the building to *Huntington’s* liking –

³ Sonja Holler, *Saint Xavier University to Close Gilbert Campus Less than a Year after Opening*, THE REPUBLIC (June 1, 2016), <http://www.azcentral.com/story/news/local/gilbert/2016/05/31/gilberts-saint-xavier-university-close/85207474/>.

⁴ Shelley Ridenour, *Saint Xavier to Close Gilbert Campus*, EAST VALLEY TRIBUNE (June 10, 2016), http://www.eastvalleytribune.com/arizona/article_417c73d8-2d09-11e6-ae28-23552d6be3fb.html.

⁵ ARIZ. CONST. ART. IX, § 7 (emphasis added).

⁶ See *Turken v. Gordon*, 223 Ariz. 342 (2010). However, indirect benefits—such as increased sales taxes or expected job creation—are not consideration under the Gift Clause. *Id.*

⁷ *Id.* at 347.

⁸ *Id.*

⁹ *Id.* at 350.

¹⁰ City of Peoria P83 District Building Reuse Program Amendment 1, March 2016.

so it can lease its building for profit. The building won't belong to the taxpayers, and they'll have no legal right to use it, the way they would have the right to use a community center or a park.

Not only does the Huntington handout fail the "consideration" test, but the agreement also doesn't serve a public purpose because not all Peoria taxpayers benefit from a private university. To be considered public, an expenditure of taxpayer money "must be primarily to satisfy the need, or contribute to the convenience, of the people of the city at large."¹¹ Examples include the "maintenance of an adequate police department," "opening, maintaining, and paving a system of public streets," and "providing a system for the disposal of sewage, thus protecting the public health."¹² But Huntington and its landlord are getting money simply to run the businesses they're already running.

In short, both contracts lack the adequate consideration required by the Arizona Constitution. Peoria taxpayers at large do not benefit from this gift of taxpayer money; only Huntington and its landlord do. Unlawful deals like this discourage businesses from shouldering risks and instead encourage them to look to lawmakers who can dip into taxpayers' wallets. If Huntington's efforts are successful, the university reaps the reward. But if the venture fails, the taxpayers and the students—not the university—take the fall.

Case Logistics

The plaintiffs in this case are Darcie Schires, Andrew Akers, and Gary Whitman, Peoria residents and taxpayers. The defendants are Peoria city officials acting in their official capacities.

The case was filed in the Superior Court of Arizona in Maricopa County on October 12, 2016.

The Legal Team

Christina Sandefur is Executive Vice President at the Goldwater Institute. She also develops policies and litigates cases advancing healthcare freedom, free enterprise, private property rights, free speech, and taxpayer rights. Christina has won important victories for property rights in Arizona and works nationally to promote the Institute's Private Property Rights Protection Act, a state-level reform requires government to pay owners when regulations destroy property rights and reduce property values. She is also a co-drafter of the Right to Try initiative, now law in over half of the states, which protects terminally ill patients' right to try safe investigational treatments that have been prescribed by their physician but are not yet FDA approved for market.

Christina is the co-author of the book *Cornerstone of Liberty: Private Property Rights in 21st Century America* (2016). She is a frequent guest on national television and radio programs, has provided expert legal testimony to various legislative committees, and is a frequent speaker at conferences. Christina is a graduate of Michigan State University College of Law and Hillsdale College.

Veronica Thorson is a staff attorney at the Goldwater Institute's Scharf-Norton Center for Constitutional Litigation. Veronica earned her JD with pro bono distinction from the Sandra Day O'Connor College of Law at ASU, where she was an associate editor for the Arizona State Law Journal and a member of the Federalist Society. During law school, she completed an internship and a clerkship with the Goldwater Institute. Before law school, Veronica received an MFA in creative writing from ASU, where she was awarded an inaugural Virginia C. Piper Summer Fellowship for her fiction. She earned her BA in English from New Mexico State University, graduating with Distinction in University Honors.

¹¹ *City of Tombstone v. Macia*, 30 Ariz. 218, 224 (1926).

¹² *Id.* at 22.