

**IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION TWO**

DEBORAH HEWITT; JAN
MITTELSTAEDT,

Plaintiffs/Appellants

v.

BOARD OF DIRECTORS OF THE
ARIZONA COMMERCE AUTHORITY,
an agency of the State of Arizona, et al.

Defendants/Appellees.

Arizona Court of Appeals
Case No. 2 CA-CV 2025-0451
-and-
Case No. 2 CA-CV 2026-0013

Maricopa County Superior Court
Case No. CV2025-001929

APPELLANTS' REPLY BRIEF

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INTRODUCTION

This case is about whether a government program that directly subsidizes certain private film companies violates the Gift Clause. The answer is yes. The Program here seeks to foster the business of private enterprises, both by reducing their financial liabilities, and by paying them with public funds—an unambiguous example of a “subsidy” that “make[s] [a] donation or grant” to an “individual, association, or corporation,” which is constitutionally forbidden. [Ariz. Const. art. IX, § 7](#).

Defendants’ Answering Brief consists of a semantic argument—an attempt to relabel what is actually a direct subsidy as a mere “tax credit,” which they claim is constitutionally permissible under [Kotterman v. Killian](#), 193 Ariz. 273 (1999). But their argument elevates form over substance, which contradicts [Kotterman](#)’s acknowledgement that “the constitutionality of a tax benefit does not turn in any event on the label we accord it.” [Id.](#) at 279 ¶ 13 (cleaned up). Defendants’ analysis also ignores the Supreme Court’s admonition that in Gift Clause cases, courts must probe “the *reality* of the transaction,” rather than being misled by labels or formal technicalities. [Gilmore v. Gallego](#), 258 Ariz. 38, 46 ¶ 34 (2024) (emphasis added).

The transactional reality here is that participating film companies get a special benefit—the reduction of tax liabilities, and/or direct payments from the state—simply to do their business, in exchange for which the state receives exactly

zero measurable benefit. That violates the Gift Clause under the test of [*Schires v. Carlat*](#), 250 Ariz. 371, 376 ¶ 14 (2021).

Defendants claim the Gift Clause doesn't apply because "tax credits" are "not 'public money,'" and therefore tax credits can *never* "implicate the Gift Clause." [AB](#) at 10. That cannot be true. Arizona courts have already made quite clear that the elimination of liabilities—including through tax benefits—is *absolutely* subject to scrutiny under the Gift Clause. *See, e.g., Maricopa Cnty. v. State*, 187 Ariz. 275 (App. 1996); *Pimalco, Inc. v. Maricopa Cnty.*, 188 Ariz. 550 (App. 1997). Nothing in [Kotterman](#), or any other Gift Clause precedent, says otherwise, or supports Defendants' formalistic argument. If Defendants were right, the government could evade the Gift Clause, and subsidize private enterprise at will, simply by routing every subsidy through the tax code or calling those subsidies "tax credits." Under that theory, a direct \$50 million appropriation to a film studio would violate the Gift Clause—but an *economically identical* \$50 million refundable "tax credit" for operating the same studio would not. That's nonsense, because "[t]he Constitution deals with substance, not shadows"—with things, not names. [Cummings v. Missouri](#), 71 U.S. (4 Wall.) 277, 325 (1866).

Arizona's Gift Clause jurisprudence directs courts to examine the *substance* of a transaction—not being misled by "an overly technical view," [Turken v. Gordon](#), 223 Ariz. 342, 352 ¶ 47 (2010)—and determine whether the state has

conferred a subsidy on a private party. The Constitution, after all, forbids *all types* of aid to private entities, whether by “donation,” “grant,” “subsidy *or otherwise.*” [Ariz. Const. art. IX, § 7](#) (emphasis added). Here, the reality is that the government has singled out one class of businesses to receive financial aid—in many cases, direct *payment* of taxpayer funds—in just the manner the Constitution forbids. Defendants’ effort to obscure this fact with semantics cannot change things.

Defendants rely almost entirely on one sentence in [Kotterman](#) to argue that what everyone (including Defendant ADOR!) recognizes as a subsidy is exempt from the Gift Clause simply because it’s labeled a “tax credit.” But the Program here is nothing like the program in [Kotterman](#). That was an *actual* tax credit (i.e., it *only* credited taxpayers for already satisfying part of their tax liability), which didn’t give anyone public money. The opposite is true here. The Program provides direct financial aid to participating firms—both by reducing their financial liabilities, *and* by writing checks to them—in order to foster their private economic activities. That’s a subsidy, by whatever name the state chooses to give it.

In [Kotterman](#), individuals owing taxes could direct a portion of their payments to a scholarship program instead of the state. Their total liabilities weren’t lessened, and the state didn’t give anyone money. Here, by contrast, the Program results in the elimination of tax liability, as well as the *actual, direct*

*payment of public funds to private entities.*¹ The Program does *not* merely result in “foregoing collecting” tax revenue, and does *not* consist merely in “setting tax policy.” [AB](#) at 22, 32-36 (citations omitted). Instead, it reduces participants’ liabilities and/or increases their assets. It does this to foster their for-profit undertakings. Thus, unlike [Kotterman](#), this is a subsidy—which violates the Gift Clause. See [Maricopa Cnty.](#), 187 Ariz. at 280; [Pimalco](#), 188 Ariz. at 559-60; see also [Rowlands v. State Loan Bd. of Ariz.](#), 24 Ariz. 116, 123 (1922) (state reducing private party’s liabilities was a subsidy); [Puterbaugh v. Gila Cnty.](#), 45 Ariz. 557, 564 (1935) (same).

And just as “an illegal subsidy” cannot “be sheltered from scrutiny merely because it is embedded within an otherwise valid contract,” [Gilmore](#), 258 Ariz. at 44 ¶ 26, so the fact that the subsidy here occurs within the state’s tax laws cannot immunize it from the Constitution’s ban.

The Superior Court reversibly erred by dismissing the Complaint. Plaintiffs/Appellants’ (“Taxpayers”) Complaint adequately alleges both facial and as-applied challenges. The court’s decision to the contrary—and Defendants in their brief—misconstrued the law and disregarded Arizona’s liberal pleading standards.

¹ Defendants call this a “negative [tax] liability,” [AB](#) at 46, but that’s just a fancy way of admitting that the Program pays private entities.

As to the facial claim, Defendants say that because [Kotterman](#) upheld a tax credit program, “at least some (nonrefundable) applications of the Program are constitutional.” [AB](#) at 47. That misreads [Kotterman](#) and ignores the overwhelming differences between the two programs. Unlike in that case, the subsidy Program here eliminates participants’ tax liability and even sends them checks from the state’s treasury. There’s no government oversight to ensure that public purposes are served, and the state acquires nothing in return for these benefits that’s of proportionate economic value. Thus the Program *always* violates *both* prongs of the Gift Clause test for reasons entirely absent in [Kotterman](#). [OB](#) at 45-47; [ROA.1](#) ¶¶ 130-34, 137-43. At a minimum, Taxpayers have alleged sufficient facts to entitle them to proceed to discovery on these issues.

Defendants’ response to the as-applied claims fares no better. They say Taxpayers failed to allege that any pre- and/or post-approved credit will ultimately result in a refund. *See* [AB](#) at 36-37. But that isn’t necessary. First, the Program violates the Gift Clause even without such “refunds.” Second, Arizona’s notice-pleading standard only requires “short and plain statement of the claim showing that the pleader is entitled to relief,” the purpose of which is to “give the opponent fair notice of the nature and basis of the claim and indicate generally the type of litigation involved.” [Cullen v. Auto-Owners Ins. Co.](#), 218 Ariz. 417, 419 ¶ 6 (2008) (cleaned up). At this stage, all Taxpayers must do is plausibly allege their causes of

action. Taxpayers have easily satisfied that requirement. Whether any particular recipient will get a “refund” (i.e., a check from the state) can only be proven after discovery; indeed, such information is uniquely and solely within the Defendants’ possession and is unavailable to Taxpayers before discovery. [OB](#) at 50-51 & n.28.

What’s more, the government cannot shield the Program from legal review by the obscurity or complexity of the Program itself. As the Supreme Court has said, the government “may not avoid scrutiny” under the Gift Clause “by providing insufficient detail to permit valuation” of the challenged transaction. [Schires](#), 250 Ariz. at 378 ¶ 21. Since Taxpayers satisfied their pleading burden by alleging sufficient facts to place Defendants on notice of the basis of the claims, they cannot be faulted for failing to provide evidence that the government alone possesses and that can only be obtained through discovery.

It’s ironic that Defendants claim Taxpayers failed to provide sufficient allegations to warrant discovery, while at the same time arguing that, if Taxpayers prevail on appeal, Defendants should have the opportunity to develop the factual record because “this case is here on a [Rule 12\(b\)\(6\)](#) dismissal, with no answers, *no discovery*, *no findings*, and without Defendants’ having presented a defense beyond the narrow motion practice below.” [AB](#) at 66-67 (emphasis added). That’s right—discovery is indeed warranted. *See* [OB](#) at 52. But that’s just why dismissal was improper and why this Court should reverse. Whatever relevant questions there

might be regarding refunds or the valuation of consideration turn on facts both sides should be allowed to flesh out.

At the [12\(b\)\(6\)](#) stage, courts “must ... assume the truth of the well-pled factual allegations *and indulge all reasonable inferences therefrom.*” [Cullen](#), 218 Ariz. at 419 ¶ 7 (emphasis added). Dismissal is proper “only if as a matter of law plaintiffs would not be entitled to relief under *any* interpretation of the facts susceptible of proof.” [State ex rel. Brnovich v. Arizona Bd. of Regents](#), 250 Ariz. 127, 130 ¶ 7 (2020) (cleaned up, emphasis added). Because the Complaint plausibly alleges both facial and as-applied constitutional violations, the judgment should be reversed.

In the interim, this Court should exercise its appellate authority to grant preliminary injunctive relief to preserve the *status quo* pending resolution of this appeal. Because Taxpayers have standing, because this case presents a justiciable controversy, and because unlawful government expenditures are imminent under the Program, preliminary relief is appropriate and necessary.

ARGUMENT

I. *Kotterman* does not prevent Gift Clause scrutiny of the Program.

Defendants’ argument rests almost entirely on a brief passage in [Kotterman](#), wrenched out of context. See [OB](#) at 21. They argue that because the [Kotterman](#) court used the phrase “tax credit” while describing the nonrefundable charitable tax

credit at issue there, that court somehow *categorically exempted* from the Gift Clause any program, mechanism, or transaction—indeed, any subsidy whatsoever—that is called a “tax credit.” That’s wrong. Defendants ignore both the nature of the program that [Kotterman](#) actually considered, and the reasoning on which that decision rested.

[Kotterman](#) involved no private enrichment at the public’s expense. 193 Ariz. at 288 ¶ 52. This Program does. [Kotterman](#) involved no payment by the State to private parties. See [id.](#) at ¶ 36. This Program authorizes precisely that. The program in [Kotterman](#) did not ultimately reduce the total liability of participating taxpayers. Here, participants have their liabilities reduced—some even get checks from the state. [Kotterman](#) concerned the charitable redirection of private funds, whereas this Program provides targeted economic-development subsidies to private companies. [Kotterman](#) emphasized that the challenged tax credit did not involve the state transferring public funds or otherwise subsidizing private enterprise. [Id.](#) at ¶ 52. This Program does.

These differences aren’t incidental—they’re dispositive.

A. *Kotterman* did not create a categorical Gift Clause exemption for anything labeled a “tax credit.”

[*Kotterman*](#) did not hold that the Legislature can immunize a subsidy from Gift Clause scrutiny by placing it in Title 43 and calling it a “tax credit.”² Rather, [*Kotterman*](#) addressed an entirely different program, and when one grasps those differences, it becomes clear that the sentence on which Defendants hang their entire case means basically the opposite of what Defendants claim.

In the [*Kotterman*](#) program, taxpayers donated *their own* money to school tuition organizations, and could credit that against their tax liability. Their total financial liabilities were not reduced.³ They still had to pay the amount of taxes they owed—they just got to choose the recipient. 193 Ariz. at 276 ¶ 1, 288 ¶¶ 50, 52. The credit there was also *nonrefundable*—meaning they never got a check, and were not enriched with public funds.

² Nor did [*Kotterman*](#) create a new “threshold” inquiry or third prong of the Gift Clause analysis. See [AB](#) at 57. The Arizona Supreme Court has reaffirmed time and again that the Gift Clause is governed by a two-part analysis. [Gilmore](#), 258 Ariz. at 45 ¶ 30; [Turken](#), 223 Ariz. at 347-48 ¶¶ 19-20 (rejecting potential third step).

³ To clarify, the [*Kotterman*](#) court said that the program “reduces the [taxpayers’] tax liability,” 198 Ariz. at 288 ¶ 50, but what it meant was that the amount the taxpayer owed *the state* was reduced by the amount paid to the scholarship organization. The taxpayer still had to pay the full amount owed—she could just direct part of it to the organization instead of the state. Thus her *total* liability was *not* reduced. See [id.](#) at 276-77 ¶ 1 (quoting statute). Here, by contrast, Program participants have their *total* liability reduced.

The plaintiffs in [*Kotterman*](#) claimed the program was a subsidy to the schools using the scholarship funds. [*Id.*](#) at 283-84 ¶ 30. But the court said it wasn't, because the money the schools got *never passed through the government's hands*. "The decision-making process is completely devoid of state intervention or direction," it said; the "[i]mportant decisions" were not made by the government, and there was no "appropriation or application" of government funds. [*Id.*](#) at 281 ¶¶ 19-20, 287 ¶ 45. That was why the court said "[o]ne cannot make a gift of something that one does not own," [*id.*](#) at 288 ¶ 52—because nobody was getting anything from the government's pocket.

Defendants snatch that sentence out of context to make it sound like a categorical statement that tax credits are never "owned" by the state and can therefore never constitute subsidies. But that's not what the court was saying. It was saying that the schools weren't being given anything valuable from the government, because the funds *didn't come from the state*—they came from citizens who chose to send some of their owed money to a scholarship instead of the state treasury.

But here, the opposite is true. The "important decisions" are made by the *state*. The decision-making process is *entirely* a product of "state intervention or direction." [*Id.*](#) at 281 ¶ 20. The Program enriches participating businesses by giving them special privileges out of the government's pocket: it zeroes out (at least part

of) their otherwise-owed tax liabilities, and some participants even get checks from the state (i.e., the “refunds”). Private citizens *don’t* choose to send their money to film-making companies. Instead, the state either eliminates participants’ financial obligations or hands them dollars from the treasury.

In short, what the state “didn’t own” in [Kotterman](#), it *does* “own” here, and the decisions the state didn’t make in [Kotterman](#), it *does* make here. The state gives participants a valuable benefit: essentially a coupon against the tax payments to which the state has a legally enforceable right. It zeroes out those liabilities—and in some cases, actually sends participants checks. The state *does* “own” the valuable privileges it gives to the participants—so that sentence in [Kotterman](#) just doesn’t apply.

In addition to misrepresenting what [Kotterman](#) said, Defendants ignore that the court itself remarked on the differences between the program there and the Program at issue here. [Kotterman](#) observed that the Gift Clause “was historically intended to protect against the extravagant dissipation of public funds by government in subsidizing private enterprises ... in the guise of public interest. *Such evils do not exist here.*” [Id.](#) at 288 ¶ 52 (cleaned up, emphasis added). Those sentences are central to [Kotterman](#)’s disposition: no private firm was getting anything from the government—neither taxpayers, nor participating parents, nor schools, were receiving valuable benefits or special favors from the state. Here, the

reverse is true. Participating firms *do* get special financial benefits directly from the state to subsidize their operations. That’s the “evil” the Program is designed to promote.

And whereas in [Kotterman](#) the “important decisions” were made by private parties, the *state* makes those decisions under this Program. It determines eligibility, calculates the benefit by reference to private production costs, applies that valuable benefit to the recipient’s tax bill,⁴ and—if the credit exceeds that liability—pays the participant the difference. See [OB](#) at 16. Unlike in [Kotterman](#), therefore, this Program is a government-administered economic-development subsidy designed to induce a favored private industry to conduct its own for-profit activities. See [Schires](#), 250 Ariz. at 377-78 ¶¶ 16, 20 (finding promise to engage in own private business insufficient under the Gift Clause). That’s unconstitutional.

B. Refundability is a critical distinction that Defendants never address.

Amazingly, in their attempt to equate this case with [Kotterman](#), Defendants never directly address one of the most critical distinctions: namely, the differences between refundable and nonrefundable tax credits. Although both may be labeled

⁴ To emphasize—the Program doesn’t just prospectively reduce taxes across the board. Instead, it nullifies part of the participant’s tax liability—that is, it zeroes out at least part of what the participant would in fact owe. That makes this case like [Maricopa Cnty.](#) and [Pimalco](#), in which the state eliminated tax liabilities.

“tax credits,” they perform fundamentally different functions. That distinction is dispositive.

A *nonrefundable* credit merely reduces liability. A *refundable* credit, by contrast, means the State pays public money from the treasury directly to the recipient. Defendants concede this, acknowledging that when a participant’s credit exceeds taxes due, “the applicant may receive a refund.” [AB](#) at 13. The statute mandates this; the unused portion of the credit “shall be paid” to the taxpayer. [A.R.S. §§ 43-1082\(F\), 43-1165\(F\)](#).

In other words, participants get checks—checks funded with taxes collected from other taxpayers, including Appellants, *not* with “untaxed taxpayer income” belonging to the recipient. [AB](#) at 10. When the credit exceeds a participant’s tax liability, the Program doesn’t just forgive taxes; it *affirmatively expends public funds*. That obviously triggers Gift Clause scrutiny. See [Schires](#), *supra*; [Turken](#), *supra*.

Defendants claim “the state has no claim to taxpayer income before taxpayers take the credits to which they’re entitled, ... whether the credits are refundable or nonrefundable,” [AB](#) at 27, but that’s misleading for two reasons.

First, it’s inapplicable here, since the “refunds” take the form of direct payments to Program participants from funds *already* collected from *other*

taxpayers.⁵ This Program redistributes money that's under the state's ownership and control, as opposed to merely declining to collect taxes.⁶ (No such feature existed under the program in [Kotterman](#).)

That distinction, incidentally, also answers Defendants' parade of horrors: unlike deductions, TPT classifications, and traditional nonrefundable tax credits, this Program authorizes payment of previously collected public funds to private parties. The statutory text itself reflects this. Rather than simply declaring that excess credits are "refunded," the Legislature provided that "the amount of the claim not used as an offset against income taxes *shall be paid to the taxpayer* in the same manner as a refund under [§ 42-1118](#)." [A.R.S. §§ 43-1082\(F\), 43-1165\(F\)](#) (emphasis added). In other words, the Legislature recognized that these payments are not "refunds" in the ordinary sense. They're government disbursements, and therefore subject to Gift Clause scrutiny.

Secondly, however, this Program doesn't concern funds to which "the state has no claim." [AB](#) at 27. On the contrary, even where a participant isn't directly paid a "refund," the amount the participant would otherwise owe in taxes is

⁵ Defendant ADOR makes these payments directly. See [A.R.S. §§ 42-1001\(3\), 42-1118; 43-1082\(F\), 43-1165\(F\)](#). They're issued from the tax refund account created by Sections [42-1116](#) and [42-1117](#), which exists within the State General Fund, and are funded with tax revenues ADOR has already collected.

⁶ In [Kotterman](#)'s terms, it "earmarks funds from the general revenue of the state for an identified purpose or destination." 193 Ariz. at 287 ¶ 45 (cleaned up).

reduced by the “credit” it receives. The participant’s tax liability is *determined* and then *reduced* pursuant to the statutory formula. See [Stearns v. Arizona Dep’t of Revenue](#), 212 Ariz. 333, 335 ¶ 12 (App. 2006) (tax credits reduce calculated tax liability). That’s entirely different from, say, a law that prospectively reduces income taxes by ten percent, or that redefines taxable income. Such laws wouldn’t reduce an individualized, ascertainable liability, and therefore wouldn’t constitute a subsidy. Here, by contrast, the Program nullifies a portion of taxes that a narrow class of entities—the participants—would otherwise owe. And if those liabilities are less than the credit, participants get checks.

So, whereas in [Kotterman](#), the taxpayer’s total liability wasn’t reduced, here, participants’ total liabilities *are* reduced or eliminated, and if that total debt is less than the credit, they get paid. Defendants are therefore wrong to say that this Program concerns only funds to which “the state has no claim.” [AB](#) at 27. It concerns only funds to which the state *does* have a claim absent the Program. The Program *waives* such claims—which makes it a subsidy. [Rowlands](#), 24 Ariz. at 123; [Puterbaugh](#), 45 Ariz. at 564; [Maricopa Cnty](#), 187 Ariz. at 280.

In any event, Gift Clause cases don’t turn on “overly technical” details, but on the “realities” of the case. [Turken](#), 223 Ariz. at 352 ¶ 47, 345 ¶ 8. The Clause forbids gratuitous expenditures, but also forbids the state from giving private entities “other valuable advantages” without getting proportionate benefits in

return. [*Indus. Dev. Auth. of Pinal Cnty. v. Nelson*](#), 109 Ariz. 368, 372 (1973). This Program fails that test and is therefore unconstitutional.

C. The Program does not operate as mere “prospective” tax policy.

Thus, Defendants’ attempt to equate the Program to prospective tax policy, like cutting taxes for next year’s homeowners or farmers, must fail. Unlike broad tax reduction, the Program here is an *individualized, application-based* subsidy for a narrow class of businesses who would otherwise owe a certain amount in taxes. The Arizona Commerce Authority (“ACA”) reserves credits for identified, pre-approved productions; applicants submit post-approval materials; ADOR determines the credit amount; and any unused amount must be paid as a refund. [A.R.S. §§ 41-1517\(G\)-\(H\), 43-1082\(F\), 43-1165\(F\)](#). Applicants can only claim credits “after production is complete.” [AB](#) at 12 (citing [A.R.S. § 41-1517\(H\)](#)). That’s not prospective.⁷

Defendants assert that refundable credits are no different from deductions or exemptions because all merely “forego tax revenues.” [AB](#) at 32 (cleaned up). But that ignores the Program’s distinctive feature: once the credit exceeds tax liability, the State does *not* merely decline to collect taxes. It nullifies the participant’s legal

⁷ Defendants’ reliance on “income not yet earned, *by labor not yet performed*” fares no better, [AB](#) at 29 (emphasis added), because the Program requires that production be complete, and the labor already performed, before payments are approved.

obligation to pay—and transfers the remainder (state money) to the participant in the form of a “refund.”

The Complaint identifies specific pre-approved and post-approved credits, including MoPic-2023-008 (post-approved for \$394,113) and MoPic-2024-004 (pre-approved for \$1,220,624). [ROA.1 ¶¶ 116-18, 148-58](#). Those aren’t abstract tax-policy choices. They’re *quantified* benefits approved for *particular* recipients whose duty to pay their taxes is (perhaps partly, perhaps wholly) eliminated. And even if some credits are carried forward rather than immediately paid out, that carry-forward still confers a fixed, monetizable, state-created, taxpayer-funded benefit that subsidizes private enterprise. See [OB](#) at 34 n.19.

This case is therefore like [Maricopa Cnty.](#) or [Pimalco](#), where the state nullified existing tax liabilities—triggering Gift Clause analysis. Defendants say those cases are different because they involved retroactive refunds, [AB](#) at 51, but even if that were true, categorical exemption from future liability also violates the Gift Clause—as in [Texas & New Orleans Ry. Co. v. Galveston Cnty.](#), 161 S.W.2d 530, 532 (Tex. App. 1942), [aff’d](#), 169 S.W.2d 713 (Tex. 1943), where a local government “undertook to indemnify the Railroad Company against the negligence of its own operatives for 999 years” as a way of subsidizing the company.

But it’s not true. Here, the Program eliminates legally imposed tax liabilities and is therefore subject to Gift Clause analysis. At a minimum, [Maricopa Cnty.](#)

and [Pimalco](#) show that the idea that tax credits are categorically exempt from the Gift Clause is false—and that alone requires reversal.

D. The Legislature’s chosen label does not determine when the Gift Clause applies.

Defendants say anything labeled a “tax credit[]” is exempt from the Gift Clause, regardless of how it operates. *See, e.g.,* [AB](#) at 10. Nothing in the Constitution or Gift Clause jurisprudence supports such a “magic words” theory.

Defendants’ theory would empower the government to transform any unconstitutional grant to a private party into a refundable “tax credit,” place it in Title 43, and thereby insulate it from judicial review. A \$10 million donation to a private corporation could become a \$10 million refundable “tax credit,” and Defendants’ rule would immunize that subsidy from constitutional review.

The Gift Clause’s broad wording forbids that conclusion. It prohibits *any* state aid to private enterprises “by subsidy *or otherwise*.” [Ariz. Const. art. IX, § 7](#) (emphasis added). The phrase “or otherwise” was specifically added to forbid tax-exemption subsidies. Sandefur, [The Origins of the Arizona Gift Clause](#), 36 Regent U. L. Rev. 1, 38-43, 54-55 (2024). At statehood, “otherwise” meant “[i]n a different manner.” *Webster’s Practical Dictionary* 276 (1910).⁸ It retains that meaning today. *See Otherwise*, [Black’s Law Dictionary](#) (12th ed. 2024) (“In a

⁸ <https://archive.org/details/websterspractica00webs/page/276/mode/2up>.

different way; in another manner ... By other causes or means ... In other conditions or circumstances”). The phrase therefore broadens, rather than narrows, the Clause’s prohibition.

Defendants ignore that phrase, and focus instead on other words in the Clause. See [AB](#) at 28. But their analysis doesn’t change the result. Even if “gift,” “donation,” etc., mean the transfer of publicly owned resources, the refundable portion of this Program *is* paid from the treasury, and therefore *is* a gift, donation, grant, and subsidy. And the nonrefundable portions also confer state-created, “valuable advantages” given to private recipients. [Nelson](#), 109 Ariz. at 372.

In any event, the fact that the state chooses to call its expenditures “tax credits” has no legal consequence, because the Constitution forbids the subsidization of private industry *in whatever guise*. Just as “an illegal subsidy cannot be sheltered from scrutiny merely because it is embedded within an otherwise valid contract,” [Gilmore](#), 258 Ariz. at 44 ¶ 26, so an unconstitutional gift cannot be exempted from constitutional scrutiny by the fact that the state chooses to call it a “credit.”

II. Taxpayers’ Complaint satisfies Arizona’s notice pleading standards.

The Complaint satisfies Arizona’s pleading requirements. It alleges that the Program confers quantifiable *public* benefits on *private* film companies, without the constitutionally required consideration or public control. Those allegations

state facts sufficient to support both facial and as-applied Gift Clause claims. *See Schires*, 250 Ariz. at 374-75 ¶ 7.

Arizona is a notice-pleading jurisdiction, meaning a complaint must only give fair notice of the nature and basis of the claim and indicate generally the type of litigation involved. *Cullen*, 218 Ariz. at 419 ¶¶ 6-7. On a dismissal motion, courts must assume the truth of well-pleaded allegations and indulge all reasonable inferences in the plaintiff’s favor. *Id.*; *Brnovich*, 250 Ariz. at 130 ¶ 7. Dismissal is only proper if, as a matter of law, plaintiffs would not be entitled to relief under any interpretation of the facts susceptible of proof. *Id.*

A. The facial claim was adequately pleaded.

Defendants say Taxpayers’ facial claim fails because they didn’t allege that every Program credit will result in a refund. *AB* at 37-39, 56-58. That misunderstands the Complaint, the Plaintiffs’ burden, and the nature of the facial challenge.

First, Defendants’ claim isn’t really true. Taxpayers allege that *every* Program credit—whether it be the offset of a participating firm’s tax liability, or a direct “refund” payment (i.e., check from the state)—confers a valuable benefits to private parties without the constitutionally required consideration and public control. *ROA.1* ¶¶ 130-34, 137-45. Those allegations plausibly establish that the Program violates both prongs of the Gift Clause in *every* application. That’s a

facial claim, *see* [Fann v. State](#), 251 Ariz. 425, 437-38 ¶ 42 (2021), and the Complaint therefore satisfies [Rule 12\(b\)\(6\)](#).

Courts in Gift Clause cases ask whether, when the government gives a private party some quantifiable benefit, (a) its doing so serves a public purpose and (b) the public is getting something in return for that benefit that's proportionate in value (as measured by objective fair-market value). [Schires](#), 250 Ariz. at 376 ¶ 14. The Complaint alleges that the Program lacks the public control necessary to satisfy the Gift Clause, and therefore fails the public-purpose requirement, *see* [ROA.1](#) ¶¶ 129, 131-33, and that the Program obtains *no* economically valuable consideration for the public, and therefore fails the consideration requirement. *Id.* at ¶¶ 2, 135-43.⁹

These allegations state a facial claim because the alleged defects are built into the Program's statutes and apply to *every* subsidy granted. If proven, Taxpayers' allegations would entitle them to judgment in their favor. Therefore the Complaint satisfies [Rule 12\(b\)\(6\)](#).

Second, Defendants' argument to the contrary tries to add a pleading burden that Arizona law doesn't require. They effectively argue that Taxpayers must *also*

⁹ All the public gets in exchange for the benefits given to Program participants is (at most) an acknowledgment in the film's credits that it was made in Arizona. Yet the Program doesn't require that the filming be done in Arizona, *or even that the film be released*. [ROA.1](#) ¶¶ 64, 65, 87, 110. In any event, the "filmed in Arizona" credit has no market value. *Id.* ¶ 139.

plead an additional “third” prong,¹⁰ alleging that every award will be paid out as a cash “refund” to participants. But that isn’t required, because *both* the cash-payment “refunds” *and* the reduction-of-liability credits are valuable financial benefits, and are unconstitutional because they serve no public purpose and obtain no proportional public benefit. Or so, at least, Plaintiffs pleaded, and that’s all they are required to plead. [ROA.1](#) ¶¶ 93, 134-35, 143-45.¹¹ Whether those allegations can ultimately be proved up is a question for summary judgment or trial, not dismissal under [Rule 12\(b\)\(6\)](#). See [Cullen](#), 218 Ariz. at 419 ¶¶ 6-7; [Brnovich](#), 250 Ariz. at 130 ¶ 7.

B. The as-applied claims were adequately pleaded.

Defendants also contend that Taxpayers’ as-applied claims fail because they did not allege that MoPic-2023-008 or MoPic-2024-004 will ultimately result in refund payments. [AB](#) at 39-40. That argument fails for two independent reasons.

First, to reiterate, “refundability” (i.e., direct payment from the state to participants) is *not* the sole basis for Taxpayers’ as-applied challenges. Both the reduction in participants’ liabilities *and* the checks they get from the government

¹⁰ See *supra* n.2.

¹¹ The Program’s mandatory statutory language strengthens the facial challenge because defendants have no discretion to deny any particular applicant a credit or refund if the requirements are met and the statutory cap is not reached. [ROA.1](#) ¶¶ 131-33.

are valuable benefits given by the state, and subject to Gift Clause analysis—which, as explained above, the Program fails.

Taxpayers’ Complaint identifies the challenged credits by number, placement priority, amount, and approval status.¹² It alleges that the government provides MoPic-2023-008 with \$394,113, and MoPic-2024-004 with up to \$1,220,624, in quantifiable private benefits without proportionate consideration, and that the State lacks meaningful control over the transferred public resources, which is unconstitutional. [ROA.1](#) ¶¶ 116-18, 133-34, 148-58. It doesn’t matter whether the benefits these entities receive are “refunds” (i.e., checks) or reductions in tax liability—either way, they’re unconstitutional.

Second, Arizona law doesn’t require more specificity at the [12\(b\)\(6\)](#) stage. Taxpayers’ allegations easily provide fair notice of the challenged transactions and the constitutional defects alleged, which, again, is all Arizona law requires. *See Cullen*, 218 Ariz. at 419 ¶¶ 6-7. It’s improper for Defendants to demand that Taxpayers allege facts that actually consist of confidential refund information, because the relevant tax information is controlled by the government and is

¹² Even *preapproval* matters: it creates a governmental commitment under the Program (pending only statutory compliance) and creates a threat of misappropriation sufficient for taxpayer standing, even before ADOR issues a check. *See Rodgers v. Huckelberry*, 247 Ariz. 426, 429 ¶ 11 (App. 2019) (“A taxpayer has sufficient standing in an appropriate action to question illegal expenditures made *or threatened* by a public agency.” (emphasis added)).

shielded from public disclosure. Taxpayers should not be penalized for failing to plead facts that Defendants possess and withhold from the public. As [Schires](#) said, the government cannot insulate its giveaways of public resources from the Gift Clause by structuring them obscurely to withhold information and prevent valuation of the consideration exchanged. 250 Ariz. at 378 ¶ 21.

What’s more, whether a particular Program participant will ultimately get a check from the government cannot be known until the Program is administered and the relevant tax information determined. Taxpayers seek prospective relief to *prevent* the administration of the Program. It’s therefore illogical to demand that Taxpayers prove up facts that will only be determined after the unconstitutional act they seek to enjoin. Arizona’s notice-pleading standard certainly doesn’t require that.¹³

C. Appellees’ remand request confirms that dismissal was improper.

Defendants argue that, if the Gift Clause applies, this Court should remand for factfinding rather than decide the Program’s constitutionality now, because

¹³ Ironically, Defendants falsely claim that “no tax credit could guarantee a refund in all instances.” [AB](#) at 38. Sure it could. All the Legislature would have to do is create a refundable credit that they knew would exceed the taxable income of every qualifying person and prohibit it from being carried over year-to-year. *See id.* at 38-39. In fact, the Legislature could make the credit “refund” automatic, as they’ve done elsewhere. [A.R.S. § 42-1118\(B\)](#). That’s another potential way illegal subsidies could become embedded in the tax code, and another reason why the Gift Clause must apply to such circumstances.

“analyzing adequate consideration ... would likely require discovery.” [AB](#) at 67.

That confuses several issues.

For one thing, with respect to at least some of Taxpayers’ facial claims, fact-finding is not necessary. For example, Taxpayers allege that the Program fails the “public purpose” requirement because the state does not retain authority and control over the Program that the Clause requires. *See* [OB](#) at 39; [ROA.1](#) ¶ 133. This lack of oversight can be ascertained from a review of the statutes alone, requiring no discovery. Absent “control” by “public officials,” there’s no protection against “private gain or exploitation of public funds,” and that violates the public purpose requirement. [Kromko v. Arizona Bd. of Regents](#), 149 Ariz. 319, 321 (1986), That alone renders the Program unconstitutional, without any discovery being required.

Regarding the consideration requirement, Defendants are right that remand would be appropriate for determining the proportionality of the “give” and “get” under this Program. [Schires](#), 250 Ariz. at 376 ¶ 14. But there’s an important point worth clarifying: the distinction between the reduction-in-liability that participants get and the “refunds” (i.e., checks from the state) that they receive is *not* relevant to the facial/as-applied distinction in this case. The “refund” and the reduction-in-liability are the *same thing*, just viewed from different angles. A Program participant is entitled to a certain total amount of benefit from the Program (which

is calculated based on the statutory formula). If the participant's tax liability exceeds that amount, the participant offsets it against its taxes, and must pay the state only the difference between the two. If the participant's tax liability is *less* than the amount, the participant gets a check from the state. But *either way*, participants get \$X amount of benefits from the state—which is the kind of arrangement to which the Gift Clause applies. [Maricopa Cnty.](#), *supra*; [Pimalco](#), *supra*; cf. [Neptune Swimming Found. v. City of Scottsdale](#), 256 Ariz. 551, 560 ¶ 28 (2024). So whether a participant gets a check or just a tax write-off is indeed triggered by the unique circumstances of its case—but it doesn't change the fact that the participant is entitled to \$X in valuable public benefits. And the question before this Court (or the Superior Court) is whether the Program directly acquires for the public something that's proportionate to \$X and whether there's sufficient public oversight to ensure that Program funds serve the public.

In any event, one thing is clear: if factual development is necessary to evaluate the Program's operation, refundability, valuation, etc., then dismissal was improper and the decision below must be reversed. See [Cullen](#), 218 Ariz. at 419 ¶ 7; [Brnovich](#), 250 Ariz. at 130 ¶ 7.¹⁴ All that's necessary for this Court to decide is

¹⁴ Certainly Defendants cannot simultaneously argue that the Complaint fails because the factual record is undeveloped, and that additional factual development is necessary.

that [Kotterman](#) does not categorically foreclose Gift Clause review, and that the Complaint plausibly alleges both facial and as-applied Gift Clause violations.

III. Plaintiffs have taxpayer standing because the Program authorizes unlawful expenditures of public funds.

Defendants renew their argument that Taxpayers lack standing, on the theory that “tax credits are not appropriations or expenditures of public money.” [AB](#) at 71. But that argument is squarely foreclosed by longstanding precedent.

First, the Gift Clause forbids things other than expenditures of money. [Neptune](#), 256 Ariz. at 560 ¶ 28. It applies to the elimination of debts, [Rowlands](#), 24 Ariz. at 123 (“[F]orgiv[ing] [a debt] ... is a donation, a pure and simple gratuity, unsupported by any consideration” and thus unconstitutional); [Puterbaugh](#), 45 Ariz. at 564, as well as certain tax-breaks. [Maricopa Cnty.](#), 187 Ariz. at 280.

Second, tax credits—especially the “refundable” credits here—are expenditures, since qualifying participants receive direct payments from the state. [ROA.1](#) ¶¶ 92-93, 103, 144.

Third, the reason taxpayers can challenge illegal expenditures of public funds is because they ultimately bear the burden of replenishing the public treasury. *See, e.g.,* [Ethington v. Wright](#), 66 Ariz. 382, 387 (1948) (“sustaining the right of a taxpayer to question expenditure of state funds on any grounds of illegality or unconstitutionality of the enactment calling for their expenditure” (emphasis added)).

That equitable interest entitles taxpayers to sue to “enforc[e] [the law] to maximize value received” for expenditures of funds or for other grants of public resources, including the elimination of debts. [Rodgers](#), 247 Ariz. at 429 ¶ 13. Thus, in [Arizona Ctr. for L. in Pub. Int. v. Hassell](#), 172 Ariz. 356, 361, 367-69 (App. 1991), taxpayers had standing to challenge the state’s relinquishment of certain land rights at below-market rates, even though these were not “expenditures of public money.” And in [Rowlands](#), *supra*, the taxpayer had standing to sue over the state’s forgiveness of certain debts. 24 Ariz. at 119. Indeed, in [Kotterman](#), which Defendants rely on so heavily, the taxpayer plaintiffs challenged a tax-credit program, and their standing was never questioned.

For the same reason, Taxpayers have standing to challenge this Program, which not only eliminates participants’ tax liabilities, but will often result in a literal payment from the state treasury. In both situations, Taxpayers are liable to replenish the public coffers (for either the nullified taxes that participants would otherwise have paid, or for the checks participants get from the state).

Defendants’ contrary argument rests on their view that the Program is exempt from the Gift Clause because it doesn’t spend public funds. [AB](#) at 70-74. As we’ve seen, that premise is false. The Clause applies to the elimination of liabilities, including tax liabilities, and the Program mandates actual expenditures

of funds when a participant's entitlement under the Program exceeds its tax liability.

Defendants' reliance on [Welch v. Cochise County Board of Supervisors](#), 251 Ariz. 519 (2021), is misplaced. [Welch](#) did not involve a subsidy or expenditure of public funds. Rather, the plaintiff challenged the appointment of an individual to an already existing, *already funded* public office. [Id.](#) at 525 ¶¶ 19-20. The Court said that the choice of one person versus another to fill that office had no impact on the taxpayer, and he therefore lacked standing. That's nothing like this case. The Program challenged here authorizes up to \$125 million annually in tax credits, [A.R.S. § 41-1517\(D\)\(3\)](#), and as the Program operates, beneficiaries receive payments they otherwise would not receive, and their tax liabilities are extinguished which otherwise they would have to pay. [ROA.1](#) ¶¶ 92-95, 104-10, 130. Both those actions deplete public resources, and taxpayers must "replenish the public treasury for the deficiency." [Ethington](#), 66 Ariz. at 386. So, unlike in [Welch](#), the Program does have an impact on taxpayers and public funds. This is the paradigmatic taxpayer-standing case.¹⁵

¹⁵ The Superior Court did not adopt Defendants' standing theory, but appeared to treat the question as one of ripeness or justiciability under [Rule 12\(b\)\(1\)](#). [ROA.77](#) at 7. That analysis fares no better. Because Taxpayers challenge an *ongoing* statutory program that authorizes unconstitutional expenditures of public funds, the dispute is ripe, justiciable, and well within Arizona's established taxpayer-standing doctrine. *Cf.* [Rodgers](#), 247 Ariz. at 429 ¶ 11 (taxpayer has standing to challenge illegal actions that are merely "threatened.").

IV. This Court can and should issue injunctive relief pending final resolution of the merits.

This Court has ample authority to preserve the *status quo* while this litigation proceeds, [A.R.S. § 12-120.21\(A\)\(3\)](#), and it should do so. As explained in the Opening Brief, all four equitable factors for injunctive relief—likelihood of success, irreparable harm, balance of hardships, and public interest—support preliminary relief here. [OB](#) at 52-55. Such temporary¹⁶ relief is appropriate to prevent further expenditures of public funds while their legality is adjudicated. After all, once spent, those funds will be impossible or very difficult to recover. Courts in Gift Clause cases rarely undo an expenditure after the fact, even if it violates the Clause. *See, e.g., Rodgers*, 247 Ariz. at 431 ¶¶ 20-21. The best practice, therefore, is to “preserve[] the possibility of a meaningful remedy by seeking to temporarily enjoin performance of the disputed contracts pending the outcome” of the case. [Id.](#) ¶ 21.

CONCLUSION

The decision below should be *reversed*.

¹⁶ Defendants criticize Taxpayers for requesting injunctive relief without expressly labeling it “preliminary.” [AB](#) at 69. No confusion should result. As is routine in such cases, the Court should enjoin expenditures pending resolution of the merits, and if it concludes the Program is unconstitutional, permanently enjoin it—or, if the Court believes remand necessary, should prevent expenditures until the merits are resolved by the Superior Court.

Respectfully submitted this 16th day of July 2026 by:

/s/ Parker Jackson

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CERTIFICATE OF COMPLIANCE

Pursuant to Rule 14(a) of the Ariz. R. Civ. App. P., I certify that the body of the attached Plaintiffs-Appellants' Opening Brief appears in proportionally spaced type of 14 points, is double spaced using a Roman Font, and contains 6998 words, excluding the table of contents and table of authorities.

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