

Same-Parcel Property Tax Liens Defy Standard Mortgage Priority Analysis  
(Where First in Time Is No Better in Right)

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Most real estate lawyers are aware of the general features of property tax liens and grant them the respect due a super-priority lien. In the several Arizona counties however, where the treasurer sells separate certificates of purchase for separate tax years, how does the practitioner approach the priority issues among the different year tax liens held by different investors on the same tax parcel?

Does the earlier year lien holder have a right to foreclose rights of redemption of later year lien holders, and consequently wipe out those lien interests, akin to mortgage priority treatment? Do property tax liens on the same parcel have equal priority amongst themselves? Or, for public policy reasons, does the later tax year lien, if sold separately, have priority over earlier year tax liens on the same parcel?

Maricopa County is one in which the treasurer will willingly sell separate year tax certificates for the same parcel. Although at the time of this writing no appellate decision has been rendered on the issue of conflicting priorities, to the author's knowledge the issue has recently been argued in at least three actions in Maricopa County Superior Court.

Procedurally the conflict arises as follows: a tax lien holder brings a standard suit to foreclose rights of redemption, naming and serving parties with an interest in the property, including property tax lien holders of different (usually later<sup>1</sup>) year liens on the same parcel. This is proper because the other year lien holder does have a statutory right to redeem the lien in suit<sup>2</sup>, and the only protection for attorney's fees and costs in the action are prior service of process on the redeeming party<sup>3</sup>.

Assuming the defendant tax lien holder is not interested in redeeming the lien in the action (and paying the plaintiff's reasonable attorney's fees and costs), then what is the legal effect of the later year lien holder being joined to the action? Does failure to redeem before judgment is entered in the first tax lien foreclosure, as some have aggressively argued, result in the later year lien holder's interest being extinguished?

To protect their claim that the lien remains until paid, later year lien holder defendants have two alternatives: answer and move for a summary judgment declaring the protected status of the lien, or move to dismiss the complaint because the relief sought, namely foreclosure and elimination of the later year lien interest, cannot be granted.

Conflict over the issue of relative lien priority arises from an apparent ambiguity in the tax lien statutes. A.R.S. §42-18204(B)<sup>4</sup> provides that following entry of a judgment foreclosing the right to redeem, "...the parties whose rights to redeem the tax lien are thereby foreclosed *have no further legal or equitable right, title or interest in the property subject to the right of appeal and stay of execution as in other civil actions.*" (Emphasis added.)

On the other hand, A.R.S. §42-17153<sup>5</sup> provides in pertinent part that the property tax lien: "Is not satisfied or removed until one of the following occurs: (a) The taxes, penalties, charges and interest are paid. (b) The property has finally vested in a purchaser under a sale for taxes."<sup>6</sup> Further, the lien: "*Is prior and superior to all other liens and encumbrances on the property, except liens or encumbrances held by this state.*"<sup>7</sup>

While there may be some attraction to the notion that the first statute cited simply says all that needs to be said on the subject, and that a non-redeeming later-year tax lien holder made party to the tax lien foreclosure loses its investment, this simplistic conclusion is unsupported by the overwhelming weight of Arizona law and public policy of property tax liens.

### **Mortgage Priority Analysis Won't Work**

As the Arizona Supreme Court observed in 1915, although dealing with a slightly different statutory scheme, the argument that a tax interest can be purchased free from the lien for taxes for *later* years is a statutory construction leading to "manifest absurdity," which should be avoided.<sup>8</sup>

The lien sold at a tax sale is for unpaid property taxes.<sup>9</sup> Tax liens are creatures of statute, there being no such thing as a lien for taxes at common law.<sup>10</sup> The property is deemed to owe the taxes,<sup>11</sup> and the state's rights in the tax lien, as defined by the statutory scheme accrue to the tax lien buyer.<sup>12</sup> Although rights peculiar to Arizona property tax liens include high priority vis-a-vis other encumbrances on the property, the interests of which may be foreclosed,<sup>13</sup> liens for later year taxes are not on that list.<sup>14</sup> That the right to

redeem may be cut off or foreclosed “does not touch or affect the tax liens of the state on property for previous years, or for any years except those included in the foreclosure proceeding.”<sup>15</sup> Tax liens remain a lien on property until paid off or converted to tax deed.<sup>16</sup>

Thus, sale of property for taxes is subject to subsequent-accruing property taxes on the same parcel; to provide otherwise would be inconsistent with the certificate purchaser’s right to pay subsequent delinquent taxes,<sup>17</sup> and the duration and priority of the tax lien, as provided in A.R.S. § 42-17153. Thus the separate later year tax lien owes its existence solely to the foreclosing lien holder’s election not to pay the subsequent delinquent taxes on the parcel. Accordingly, it makes sense that the earlier year lien holder who succeeds in obtaining a Treasurer’s Deed through the action takes title subject to the liens for later unpaid taxes.<sup>18</sup>

The property owner should not be able to avoid payment of any years of the tax on his property (based either on equitable principles of unjust enrichment<sup>19</sup>, or Constitutional non-uniformity of taxes<sup>20</sup>). Nor should the earlier year tax lien holder who takes title escape that liability.

While traditional mortgage analysis (“first in time, first in right”) may create some comfort because of its familiarity, its application to property tax liens ignores the clear language of A.R.S. §42-17153, which allows for a lien to be removed only by payment of the taxes it secures or when it ripens into a deed to the property through one of the statutory foreclosure processes.

Proponents of the mortgage treatment analysis of tax liens (“senior” vs. “junior”) also rely on a mischaracterization of the 1930 case of *Steinfeld v. State*.<sup>21</sup> The case addressed the relative priority between property tax liens and state mortgages. The *Steinfeld* court observed that the tax lien statute in effect at the time made tax liens superior to all other liens, including the state’s mortgage lien. After the Court’s so holding, the state legislature amended what is now Section 42-17153 to modify priority of tax liens as follows: “The tax lien shall be prior and superior to all other liens and encumbrances upon the property, except liens or encumbrances held by the state.”<sup>22</sup>

The *Steinfeld* case does not address the issue of relative priorities among tax liens for different years on the same tax parcel. In any event, though, it does not stand for the proposition that liens sold to investors become private mortgages, extinguishable by the first in time. Such an interpretation is

entirely inconsistent with the other part of A.R.S. §42-17153: "The lien... is not satisfied or removed until ... [t]he taxes, penalties, charges and interest are paid[, or t]he property has finally vested in a purchaser under a sale for taxes."

If a deed issues to the holder of a certificate of purchase, he is compelled to pay the amount for which the property was sold plus accruals, in which event the taxes would actually be paid.<sup>23</sup> Nothing satisfies or removes the lien of taxes against real estate except their payment, or the sale of the property for taxes.<sup>24</sup>

**Characteristics of tax liens do not change when they are sold or assigned to private investors.**

A corollary argument that a tax lien loses the characteristics it has upon collection (namely high priority) when the state sells or assigns it, which would support a default to traditional mortgage analysis, also lacks support under Arizona law.

In *Shumway v. State*, the court held that the assignee of a state mortgage was not entitled to the same priority as the state under A.R.S. §42-17153 because after assignment, the mortgage was no longer held by the state. Thus, it concluded, a quiet-title judgment following foreclosure of the mortgage did "not estop the state or its assignee from asserting the validity of the certificate of purchase or the state's tax liens."<sup>25</sup>

These conclusions are correct for two reasons: first, the state mortgage, after assignment by the state, is enforceable and subject to the law concerning mortgages (not "state" liens); and secondly, property tax liens have characteristics specifically ascribed to them by the tax lien statutes, whether held by the state or its assignee. A distinction based on ownership of the tax lien is therefore without merit.

The weight of authority supports the conclusion that tax liens held the characteristics with which they are endowed upon creation, whether retained as unsold in the office of the county treasurer or after being sold to a private investor. As a "state" lien the claims which they represent cannot be extinguished by the foreclosure of rights of redemption by an earlier-year tax lien holder.

The common mortgage analysis simply does not apply to property tax liens<sup>26</sup>, because if it did, there would be little incentive for a tax lien investor

to pay subsequent delinquent taxes (if he could later simply wipe them out), and the threat of being wiped out would steer later year tax investors away. Were there any merit to the position, the public coffers would suffer significantly, because tax lien buyers would no longer be able to buy tax liens with all the rights defined by statute; instead, they would be offered "mortgages" - more and more junior, providing as security only equitable rights of redemption of earlier year liens on the property.

Our Supreme Court has been clear in its treatment of successors in interest to the state property tax liens:

The certificate of purchase issued to the state is in lieu of or a continuance in another form of the state's tax lien. The county treasurer is authorized to sell and transfer the state's certificate to any purchaser who will pay all the taxes, etc. (Section 31, Id.) And thereafter to issue to such purchaser a deed to the property on his compliance with the law as to notice, etc. Section 49, Id.<sup>27</sup>

Other states have accorded priority to the later year position, allowing that lien holder to extinguish all interests of earlier year lien holders once that later year lien has matured for foreclosure.<sup>28</sup> As long as multiple tax certificates are condoned or encouraged on Arizona parcels, such a provision in Arizona law might merit legislative consideration. Enactment of the later-year priority rule might go far to discourage the priority conflict issue – as it provides an incentive for paying subsequent delinquent taxes and bringing the foreclosure action as early as possible.

**Foreclosure of the right of redemption does not equate with extinguishment of a later-year tax lien.**

Terminating a right of redemption belonging to the later year lien holder is not tantamount to terminating its interest completely, because the statutes provide that the lien for taxes remains until paid. "Until foreclosed by a *senior* priority tax certificate" is not a means by which the tax lien can be extinguished.<sup>29</sup>

In *State v. Martin*, the State argued that tax lien investors whose liens were found subordinate to a foreclosed state mortgage, had an adequate remedy solely by redemption of the state's mortgage lien. The Court rejected such a restrictive view of the lienholder's rights under the circumstances:

It may be said that defendants have an adequate remedy by redemption from the foreclosure of the mortgage. It is true that they have this right, but it may well be that the accrued mortgage debt for which they were in no manner responsible is so great that it, together with the taxes paid by defendants, is far more than the land is worth. We think the trial court properly held that defendants should have the option of redeeming under the mortgage foreclosure, or recovering from the state the taxes which they had paid.<sup>30</sup>

The *Martin* case is instructive that redemption rights are not the only interest associated with the later tax lien position.

Clearly a foreclosure action affects no other tax liens than those which are the subject of the foreclosure.<sup>31</sup> Making a useful distinction, the *Linville* court wrote: "This 'right to redeem from such sale, ' Section 78-831 [now A.R.S. §42-18206], may be cut off or foreclosed, but that does not touch or affect the tax liens of the state on property for previous years, or for any years except those included in the foreclosure proceeding."<sup>32</sup>

This conclusion makes sense, and is consistent with a harmonized construction of the tax lien statutes that concern conflicting tax lien holders. *Linville* and A.R.S. § 42-17153 indicate the lien remains until paid; the earlier year lien holder suggests that because a lien holder of a different year has a right to redeem, that and all other interest in the property may be eliminated by judicial foreclosure of the tax lien. It would make sense that rights of redemption can be foreclosed, even those of tax lien holders of different years, so that there is some finality to the deed obtained in the process. Otherwise, the later year lien holder could essentially deprive the earlier year lien holder of a judgment deed by redeeming after entry of judgment, even though a treasurer's deed had been issued.

Thus although a right to redeem may be foreclosed, the foreclosure judgment cannot extinguish the later year tax lien against the property, which would be a result inconsistent with the clear provisions of A.R.S. § 42-17153 and well-established Arizona case law.<sup>33</sup>

Fundamental principles of statutory construction require sensible, harmonizing interpretations of the apparently conflicting statutes. As the Arizona Supreme Court wrote in *Hill v. Gila County*:

We think 'The several provisions of the statute should be construed together in the light of the general purpose and object of the act and so as to give effect to the main intent and purpose of the legislature as therein expressed. If possible, a statute should be so construed as to render it a consistent and harmonious whole; if different portions seem to conflict, they should, if practicable, be harmonized, that construction being favored which will render every word operative rather than one which makes some words idle and nugatory. In other words, a statute must receive such construction as will make all its parts harmonize with each other, and render them consistent with its general scope and object.' 25 R.C.L. 1007, § 247.<sup>34</sup>

The tax lien scheme clearly reflects the Legislature's intent that investor held tax claims be given the same rights as state-held tax liens, including the definite expectation that the lien lasts as long as it takes to be repaid (or turned into fee ownership through foreclosure).<sup>35</sup>

The county treasurer is the ex-officio tax collector for the state.<sup>36</sup> If liens sold to private investors were no longer to be treated as liens of the state and instead were to be treated as mortgages then there would be no reason to have the county treasurer continue to be the collection agent for taxes for private certificate holders.

## Conclusions

In a recent minute entry opinion<sup>37</sup>, Judge Michael A. Yarnell of the Maricopa County Superior Court, after thoughtfully reviewing the authorities touched on in this article, among others, wrote:

The current question may be viewed as whether or not the super priority of a tax lien ceases, or does not cease, upon the issuance of a Certificate of Purchase or only upon the issuance of the tax deed. The statutory scheme is best harmonized, the revenue to the State for delinquent taxes is best maximized, and the return of real property to the stream of commerce is best achieved by triggering the "loss of super priority for tax liens" at the latest point in time rather than an earlier point in time. This latest point in time is the issuance of the tax deed not the issuance of the Certificate of Purchase.

Therefore, this Court holds A.R.S. § 42-312 is the controlling statute for the redemption or foreclosure of tax liens and Certificates of Purchase. Tax liens and their resultant Certificates of Purchase, are superior to all other liens or encumbrances except for those held by the state and, thus, are co-equal in terms of priority. No tax lien or Certificate of Purchase may extinguish another. Tax liens and Certificates of Purchase may only be satisfied or removed through the means set forth in A.R.S. § 42-312(b).

The issuance of the tax deed based upon foreclosure of a Certificate of Purchase, however, subjects the grantee in the tax deed to foreclosure by any outstanding Certificate of Purchase. Thus, the statutory scheme is interpreted to avoid a “rush to judgment” or a “first to judgment forecloses all” approach. In order to protect their investment, Certificate of Purchase holders from tax sales must either buy (or redeem) the other out or make other arrangements prior to the issuance of any tax deed. . . .

A.R.S. § 42-452 allows any tax certificate/lien holder to foreclose the underlying property; but such foreclosure will not terminate any other prior or subsequent tax liens or Certificates of Purchase on the property. In other words, the foreclosing Certificate of Purchase holder acquires fee title subject only to prior and subsequent real property taxes, real property tax Certificates of Purchase and prior liens of the state.

If the foreclosure complaint made clear that the only purpose for joining later year lien holders was to make them liable upon redemption for attorney’s fees and costs, then the basis for their opposition to the complaint would evaporate. Of course, the final judgment would have to clearly distinguish that although their right to redeem the earlier lien was foreclosed, their tax lien interest in the property remained unaffected by the action and judgment.

This article was intended to discuss relative priorities of investor-held tax liens on the same parcel. The reader is cautioned that other peculiar priority issues and treatment concerning property tax liens may arise in contexts of bankruptcy, RICO civil forfeitures, FDIC property interests, and properties where other federal and state governmental liens have attached.

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### Endnotes:

1. The non-foreclosing lien is "usually later" because it has not yet matured for foreclosure. See A.R.S. §42-18201 (formerly A.R.S. §42-451(A); the 1997 state legislature recodified Title 42, effective January 1, 1999. Laws 1997, Ch. 150, §172)..
2. A.R.S. § 42-18151 (formerly A.R.S. § 42-421).
3. A.R.S. §42-18206 (formerly A.R.S. §42-454)
4. Formerly A.R.S. §42-452.
5. Formerly A.R.S. §42-312.
6. A.R.S. §42-17153(B)(2).
7. A.R.S. §42-17153(B)(3). (Emphasis added.)
8. *Thomas v. State*, 17 Ariz. 18, 21 147 P. 914, 915 (1915).
9. A.R.S. § § 42-18101, 18111 (formerly A.R.S. §§ 42-381(B) and 42-390(A), respectively).
10. *Ingraham v. Forman*, 49 Ariz. 29, 32, 63 P.2d 998, 999 (1937).
11. *Santos v. Simon*, 60 Ariz. 426, 429, 138 P.2d 896, 897 (1943).
12. A.R.S. § 42-18101 *et seq.*
13. A.R.S. § 42-17153 (formerly A.R.S. § 42-312).
14. *Linville v. Cheney*, 60 Ariz. 325, 137 P.2d 395 (1943).
15. *Id.*, 60 Ariz., at 329-330.
16. A.R.S. § 42-17153 (formerly A.R.S. § 42-312(B)).
17. A.R.S. § 42-18121 (formerly A.R.S. § 42-400).
18. *Linville*, 60 Ariz. at 330.

19. *State v. Martin*, 59 Ariz. 438, 130 P.2d 48 (1942).
20. *Linville v. Cheney*, 60 Ariz. 325, 137 P.2d 395 (1943).
21. *Steinfeld v. State*, 37 Ariz. 389; 294 P. 834 (1930).
22. A.R.S. §42-17153 (emphasis added); *Shumway v. State*, 63 Ariz. 400, 163 P2d 274(1945); *Conway v. Versluis*, 58 Ariz. 368, 380-381, 120 P.2d 410, 415 (1941).
23. *Shumway v. Fleishman*, 66 Ariz. 290, 296, 187 P.2d 636, 640 (1947).
24. *Maricopa County v. Bloomer*, 52 Ariz. 28, 32, 78 P.2d 993, 994 (1938).
25. *Shumway v. State*, 63 Ariz. at 410, 163 P2d at 278 (emphasis added).
26. A.R.S. 42-312(B), *Linville v. Cheney*, *supra*.
27. *Conway v. Mosher*, 55 Ariz. 307, 312, 101 P.2d 209, 211 (1940).
28. See, for example, New Jersey Statutes Annotated Section 54:5-9: recorded tax certificates constitute a first lien which is "paramount to all prior or subsequent alienations and descents of such lands or encumbrances thereon except subsequent municipal liens." See also, Pellegrino and Allocca, "Tax Certificates: A Review of the Tax Sale Law," 26 Seton Hall Law Review 1607, 1622 (and footnote 89). (Emphasis added.)
29. See A.R.S. § 42-17153.
30. 59 Ariz., at 447-448, 130 P.2d, at 52.
31. *Linville*, *supra*.
32. *Linville*, 60 Ariz. at 329-330, 137 P2d at 397(1943); see also, *Ingraham v. Forman*, 49 Ariz. at 33, 63 P.2d at 999 (1937).
33. *Linville*, *supra*, *Ingraham*, *supra*.
34. *Hill v. Gila County*, 56 Ariz. 317, 324, 107 P.2d 377, 380 (Ariz. 1940).
35. In addition to A.R.S. §42-17153, see statutory references to "purchaser" in A.R.S. §§ 42-18118 and 42-18117, (formerly §§ 42-396 and 42-397, respectively) which would necessarily include the state with respect to liens issued to it.
36. A.R.S. §42-18001 (formerly A.R.S. §42-341).
37. *Bauza Holdings, L.L.C. v. Horseman's Ranch, Inc., et al.*, Maricopa County Superior Court Case number CV95-03665, Minute Entry dated October 16, 1998.