

## PRIVATE TAXPAYER RULING LR02-011

May 23, 2002

The following private taxpayer ruling is in response to your request of February 25, 2002. Again, I apologize on behalf of the department for the delay in responding to your request and for any undue inconvenience caused by this delay. Your letter requests a determination whether the costs incurred in the purchase, assembly, and installation of a Cogeneration System are exempt from the Arizona transaction privilege tax under Arizona Revised Statutes ("A.R.S.") § 42-5061(B)(4), (6), and (19). . . . , also requests a ruling on whether the costs incurred in the purchase, assembly, and installation of this Cogeneration System would qualify for the income tax pollution credit as detailed in A.R.S. § 42-1170.

Based on the facts presented, . . . is not the seller of the Cogeneration System and therefore not the taxpayer for purposes of Arizona transaction privilege tax. Arizona's transaction privilege tax is a tax on the privilege of conducting business in the State of Arizona. It is a tax on the seller, not on the purchaser. The seller may pass the burden of the tax on to the purchaser; however, the seller is ultimately liable to Arizona for the tax.

Pursuant to A.R.S. § 42-2101 the department may issue private taxpayer rulings to taxpayers and potential taxpayers on request. Each request must be in writing and must be signed by the taxpayer or potential taxpayer who makes the request or by an authorized representative of the taxpayer. As stated above, based on the information provided in your request . . . is not the taxpayer. As a result, the department is not able to issue a private taxpayer ruling to . . . regarding Arizona transaction privilege tax. However, the department will issue a private taxpayer ruling regarding the credit under A.R.S. § 43-1170.

### Statement of Facts:

The following is a restatement of the facts presented in your letter.

. . . is engaged in the business of producing . . . and . . . products. One of . . . 's production facilities is located in . . . . . is considering the installation of a Cogeneration System that would produce electrical power and steam at the . . . facility ("Plant") for use as a power source for . . . 's business. The Cogeneration System has the potential to significantly reduce emissions of air pollutants specified in the rules and regulations adopted by the United States Environmental Protection Agency ("EPA") and the Arizona Department of Environmental Quality ("DEQ").

The Plant currently purchases electric power from the local utility and operates two . . . boilers to produce steam for the use in the manufacturing process. The boilers are fueled by No. 6 fuel

oil with natural gas as a backup fuel. The Plant's air operating permit is currently undergoing renewal.

The proposed Cogeneration System would involve the installation of a turbine driven electric generator to supply all electric power needed and most of the steam demand for the entire Plant. The proposed generator is powered by a natural gas . . . internal-combustion engine.

. . . has received a proposal from . . . to assemble and install the turbine engine generator and related machinery and equipment comprising the Cogeneration System. Each component of this system will be either used as an essential part of the process of either producing or transmitting electricity, or used to meet regulatory requirements for pollution control.

The expected reduction in air pollution is highlighted as follows:

NOx emission from natural gas and diesel fuel combustion in the new engine are estimated based on the predicted Emission Performance report provided by the manufacturer.

SOx emissions from natural gas combustion were estimated using emission factors from EPA's compilation of emission.

Eliminating fuel oil usage at the plant altogether, eliminating one boiler, and adding the new engine will result in a 8.64-ton/yr decrease in potential NOx emissions and a 93.79-ton/yr reduction in potential SOx emissions for this facility.

Furthermore, this project will result in the . . . plant generating less demand for electric power from Arizona Public Service. . . 's air emissions associated with this demand are expected to be reduced accordingly.

-

#### Your Position:

It is your position that the Cogeneration System would significantly reduce air pollution and therefore may qualify for the Income Tax Pollution Control Credit pursuant to A.R.S. § 43-1170.

#### Applicable Statutory Authority:

A.R.S. § 43-1170 provides a credit for expenses incurred to purchase real or personal property that is used in the taxpayer's trade or business in this state to control or prevent pollution.

## Discussion and Analysis:

A.R.S. § 43-1170 provides a credit for expenses incurred to purchase real or personal property that is used to control or prevent pollution. DEQ defines air pollution control equipment as equipment used to eliminate, reduce or control the emission of air pollutants into the ambient air. While this Plant would produce energy without producing pollution in excess of EPA standards, the equipment does not appear to be directly used for the purpose of meeting pollution control standards of the EPA but for the purpose of generating electricity. Generally, equipment that is not directly used for the purpose of meeting environmental regulations to prevent or reduce pollution would not qualify for the credit.

In addition, the reduction of pollution by . . . is irrelevant. The fact that the Cogeneration System would reduce the demand for power by . . . has no bearing on whether the Cogeneration System is entitled to the credit. . . . is not responsible for the pollution created by . . . and did not purchase the equipment to meet or exceed rules or regulations adopted by the EPA, DEQ, or a political subdivision of this state to prevent, monitor, control or reduce pollution by . . . .

Although the entire Cogeneration System does not qualify for the credit, the specific piece of equipment purchased for the purpose of controlling pollution in an industrial facility may qualify. In order to claim the credit for a specific piece of equipment . . . must be able to identify the discrete equipment and the actual price of the portion of the equipment that is used to control pollution.

## Conclusion and Ruling:

The following ruling is given based on the facts presented in your request. The department rules that the entire Cogeneration System does not qualify for the credit under A.R.S. § 43-1170. However, although the entire system does not qualify for the credit, discrete equipment purchased for the purpose of controlling pollution may qualify. To qualify and claim the credit, the specific portion of the equipment must be identified. In addition, . . . , must identify the actual purchase price of the specific piece of equipment used to control pollution.

The conclusions in this private taxpayer ruling do not extend beyond the facts as presented in the request for a private taxpayer ruling dated February 25, 2002.

This response is a private taxpayer ruling and the determinations herein are based solely on the facts provided in your request. The determinations are subject to change should the facts prove to be different on audit. If it is

determined that undisclosed facts were substantial or material to the department's making of an accurate determination, this taxpayer ruling shall be null and void. Further, the determination is subject to future change depending on changes in statutes, administrative rules, case law or notification of a different department position.

The determinations in this private taxpayer ruling are only applicable to the taxpayer requesting the ruling and may not be relied upon, cited nor introduced into evidence in any proceeding by a taxpayer other than the taxpayer who has received the private taxpayer ruling.