

DECISION OF MUNICIPAL TAX HEARING OFFICER

October 1, 2016

Taxpayer's POA

Address of Taxpayer's POA

Taxpayer
MTHO #907

Dear Taxpayer's POA:

We have reviewed the evidence and arguments submitted for redetermination by *Taxpayer* and the City of Tucson Tax Collector (Tax Collector or City). The refund period covered is June 1, 2012 through July 31, 2012. Taxpayer's position, Tax Collector's response and our findings and ruling follow.

Taxpayer's Position

Taxpayer sold income-producing capital equipment to an electric utility. Taxpayer also installed the equipment. Taxpayer paid City privilege tax on its receipts from the activity. Taxpayer was not subject to the privilege tax for either providing the equipment or for its installation. Taxpayer is entitled to a refund of the privilege it paid.

Tax Collector's Response

Under the agreement with Taxpayer, the utility and not Taxpayer provided the income-producing capital equipment. Also, the income-producing capital equipment Taxpayer installed appeared to be permanently attached. Taxpayer has not met its burden to show it is entitled to a refund.

Discussion

Taxpayer entered into an agreement with a utility to provide and install certain materials and equipment at a transmission substation in the City. Taxpayer reported its income and paid City privilege tax on its receipts under the construction contracting classification. Taxpayer thereafter filed a claim for refund contending that it sold and installed income-producing capital equipment and its receipts were therefore not taxable pursuant to Tucson City Code (TCC) § 19-415(b), paragraph (3) or (4). The City denied Taxpayer's claim for refund and Taxpayer protested the denial.

Taxpayer has not established entitlement to a refund pursuant to TCC § 19-415(b)(3)

TCC § 19-415(b)(3) allows a deduction to construction contractors for income attributable to the purchase of income-producing capital equipment. Income-producing capital equipment includes machinery, equipment, or transmission lines used directly in producing or transmitting electrical power, but does not include distribution. Transformers and control equipment used at

transmission substation sites constitute equipment used in producing or transmitting electrical power.

While equipment Taxpayer installed at the substation may qualify as income-producing capital equipment, the question presented is whether Taxpayer provided the equipment and has identified the portion of its receipts attributable to its purchase of the income-producing capital equipment. Under the agreement, the utility provided all steel structures, lightning arresters, switches, motors, insulators, bus and bus supports, conductors, lights, grounding wire and mats, entrance gates and distribution poles, cables and transformers. Taxpayer was required to furnish all other material for completing the work such as conduit fittings, connectors, bends, adapters, spacers, clamps, bushings boxes and all materials for use in concrete, including cement, sand and water. Much of the work appeared to involve foundations, which would not be a part of the equipment. The record before the Hearing Office does not identify specific items of income-producing capital equipment provided by Taxpayer, the cost of the equipment and what portion of the claim for refund was requested under TCC § 19-415(b)(3).

Taxpayer has not established entitlement a refund pursuant to TCC § 19-415(b)(4)

TCC § 19-415(b)(4) provides a deduction for income derived from a contract entered into for the installation, assembly, repair or maintenance of income-producing capital equipment that is not permanently attached. The deduction only applies to proceeds derived from the installation, assembly, repair or maintenance of the equipment and does not include that portion of any contracting activity which consists of the development of, or modification to, real property in order to facilitate the installation, assembly, repair, maintenance or removal of machinery, equipment or other tangible personal property. Thus the deduction does not apply to activities such as foundation work, excavation, reestablishing finished grade, trenching and the disposal of waste material. The record before the Hearing Office does not identify the specific items of income-producing capital equipment installed by Taxpayer and the amount of income attributable to such installation.

Also, the deduction does not apply if the income-producing capital equipment is permanently attached. The term "permanently attached" means at least one of the following:

- (a) the tangible personal property is incorporated into real property;
- (b) the tangible personal property is so affixed to real property that it becomes a part of the real property; or
- (c) the tangible personal property is so attached to real property that removal would cause substantial damage to the real property from which it is removed.

The existence of any one of the three factors means that the tangible personal property is permanently attached and the income derived from the installation is subject to tax under the construction contracting classification.

The above criteria requires a detailed review of the items installed, whether the items qualified as income-producing capital equipment and the manner of installation or attachment. The record before the Hearing Office does not provide sufficient information regarding the nature of the

property installed or the manner of installation to determine whether or not any of the items qualified for the deduction.

Taxpayer must present substantial credible and relevant evidence sufficient to establish that the City's denial of its claim for refund was erroneous. The record does not contain such evidence. The record does not specifically identify the income-producing capital equipment provided by Taxpayer, Taxpayer's cost of the equipment, the specific items of income-producing capital equipment installed by Taxpayer, that the equipment was not permanently attached and the portion of its receipts attributable to providing and installing the equipment as opposed to charges for other activity such as installing foundations, gates or performing excavation or waste disposal. The City's denial of Taxpayer's claim for refund is upheld.

Findings of Fact

1. Taxpayer entered into an agreement to provide and install certain materials and equipment for an electric utility at a transmission substation in the City.
2. Taxpayer's activity included replacing and constructing new transmission line structures including the replacement and installation of dead-end structures, SF6 circuit breakers, disconnect switches, rigid and wire bus and all control cable.
3. By letter dated December 3, 2015 Taxpayer filed a claim for refund for City privilege taxes of \$24,375.94 paid on its activity of providing and installing income-producing capital equipment for an electric utility. The claim for refund included a compact disc (CD) containing a detailed refund schedule, privilege tax return support and copies of invoices. The CD is not a part of the record before the Hearing Office.
4. Taxpayer's claim for refund was for the months of June 1, 2012 through July 31, 2012. Taxpayer's return for June 2012 showed gross contracting receipts of \$1,912,574, deductions of \$693,777, net taxable income of \$1,218,797 and City privilege tax of \$24,375.94.
5. The City denied Taxpayer's claim for refund because the City concluded that under the contract between Taxpayer and the utility the utility was required to provide the income-producing capital equipment and the income-producing capital equipment appeared to be permanently installed.
6. Taxpayer timely protested the City's denial of its claim for refund contending that the project was for the construction of the Vail T3 transmission substation and the project included the replacement and installation of dead-end structures, SF6 circuit breakers, disconnect switches, rigid and wire bus and all control cables.
7. The parties submitted into the record before the Hearing Office:
 - a. Copy of the Physical Construction specifications providing that:
 - i. Taxpayer was to install/assemble galvanized welded steel structures provided by the utility, including transmission poles. (§ 1.1.3.A.1.)
 - ii. Set the 345kV and 138kV breakers and connect the high voltage cables. (§ 1.1.3.B.1.b.)

- iii. Install various structures, lighting, panels, grounding terminals and mats. (§ 1.1.3.B.1.c. - h.)
 - iv. That a 345/138 kV power transformer was present on a pad. (§ 1.1.3.B.2.)
 - v. The utility was to furnish items such as all steel structures, lightning arresters, switches, motors, insulators, bus and bus supports, conductors, lights, grounding wire and mats, entrance gates and distribution poles, cables and transformers. (§ 1.2.1.A.1. - 21.)
 - vi. Taxpayer was to furnish all material for completing the work except material furnished by the utility, providing a non-exclusive list of materials such as conduit fittings, connectors, bends, adapters, spacers, clamps, bushings boxes etc. to be provided by Taxpayer. (§ 1.2.2.A.)
 - vii. Taxpayer is responsible for disposing waste material. (§ 1.3.4.)
- b. Copies of billing invoices. The invoices did not provide detail as to work completed.
 - c. Civil Construction Specifications providing that:
 - i. The work listed under the specifications included foundations, grounding, conduit and cable trench. (§ 1.1.2.)
 - ii. The work also included reestablishing finished grade within any disturbed areas. (§ 1.1. 1))
 - iii. The work also included excavation and compaction. (§ 2.2.)
 - iv. Taxpayer was required to furnish all materials for use in concrete, including cement, sand and water. (§ 3.2.)
 - d. Civil Construction Specifications - Unitized Pricing Sheet dated September 19, 2011 in the total amount of \$991,879.15 listed mainly charges for foundation work, 4,000 cubic yard of 4" A.B. finished surface and guard posts.
8. The record before the Hearing Office does not contain detailed information regarding the items of income-producing capital equipment provided by Taxpayer, the cost of the items, the method of installation and the specific receipts attributable to income-producing capital equipment not permanently attached.

Conclusions of Law

1. TCC § 19-415 imposes the City privilege tax on the business of construction contracting.
2. "Construction Contractor" means a person who undertakes to or offers to undertake to, or purports to have the capacity to undertake to, or submits a bid to, or does himself or by or through others, construct, alter, repair, add to, subtract from, improve, move, wreck, or demolish any building, highway, road, railroad, excavation, or other structure, project, development, or improvement to real property, or to do any part thereof. TCC § 19-100.

3. Taxpayer acted as construction contractor under its agreement to provide and install certain materials and equipment for the electric utility at a transmission substation, including doing foundation work, excavation, trenching and reestablishing finished grade.
4. The presumption is that an assessment of additional tax is correct. *See, Arizona State Tax Commission v. Kieckhefer*, 67 Ariz. 102, 191 P.2d 729 (1948).
5. Once the presumption of correctness attaches, the taxpayer must present substantial credible and relevant evidence sufficient to establish that the assessment was erroneous. *U.S. v. McMullin*, 948 F.2d 1188 (10th Cir.,1991); *Anastasato v. C.I.R.*, 794 F.2d 884 (3rd Cir.,1986).
6. The same presumption of correctness applies to a tax agency's determination to deny a taxpayer's claim for refund. *See, Bubble Room, Inc. v. United States*, 159 F.3d 553, 561 (Fed.Cir.1998).
7. A general denial of liability is not sufficient to overcome the presumption of correctness. *Avco Delta Corp. Canada Ltd. v. U.S.*, 540 F.2d 258 (7th Cir., 1976).
8. Taxpayer has the burden to show it is entitled to an exemption or deduction from taxation. *Ebasco Servs., Inc. v. Ariz. State Tax Comm'n*, 105 Ariz. 94, 99, 459 P.2d 719, 724 (1969).
9. TCC § 19-415(b)(3) provides a deduction to construction contractors of income attributable to the purchase of machinery, equipment or other tangible personal property that is exempt from or deductible from privilege or use tax under TCC § 19-465(g) (income-producing capital equipment).
10. TCC § 19-415(b)(4) provides a deduction for income derived from a contract entered into for the installation, assembly, repair or maintenance of income-producing capital equipment that is deducted from the retail classification pursuant to TCC § 19-465(g), that does not become a permanent attachment to a building, highway, road, railroad, excavation or manufactured building or other structure, project, development or improvement.¹
11. The deduction provided by TCC § 19-415(b)(4) does not include income from that portion of any contracting activity which consists of the development of, or modification to, real property in order to facilitate the installation, assembly, repair, maintenance or removal of the income-producing capital equipment.
12. The term "permanent attachment" in TCC § 19-415(b)(4) means at least one of the following:
 - a. to be incorporated into real property.

¹ Prior to being amended, A.R.S. § 42-5075(B)(7) provided deductions for state prime contractors identical in all material respects to the deduction provided by TCC § 19-415(b)(4). In 2013 the state legislature amended A.R.S. § 42-5075(B)(7). (H.B. 2535, Laws 2013, Ch. 153, § 1) H.B. 2535 also amended A.R.S. § 42-6004 by adding paragraph (A)(13) to require cities to be consistent with amended A.R.S. § 42-5075(B)(7). While the amendment was retroactive to taxable periods beginning after June 30, 1997, the bill required that any claim for refund under the amended language be filed with the state or a city by December 31, 2013. Since Taxpayer's claim for refund was not filed until December 2015, the provisions of H.B. 2535 are not applicable here.

- b. to become so affixed to real property that it becomes part of the real property.
 - c. to be so attached to real property that removal would cause substantial damage to the real property from which it is removed.
13. Income-producing capital equipment includes machinery, equipment, or transmission lines used directly in producing or transmitting electrical power, but not including distribution. Transformers and control equipment used at transmission substation sites constitute equipment used in producing or transmitting electrical power. TCC § 19-110(a)(4).
 14. Taxpayer has not established the amount of any income attributable to the purchase of income-producing capital equipment, the installation of income-producing capital equipment and that the equipment was not permanently attached.
 15. The record in this case does not established that Taxpayer is entitled to a refund of privilege taxes paid during the refund period.
 16. The City's denial of Taxpayer's claim for refund is upheld.

Ruling

The protest by Taxpayer of the City's denial of its claim for refund for the period June 1, 2012 through July 31, 2012 is denied.

The City's denial of Taxpayer's claim for refund for the period June 1, 2012 through July 31, 2012 is upheld.

Taxpayer has timely rights of appeal to the Arizona Tax Court pursuant to Model City Tax Code Section -575.

Sincerely,

Hearing Officer

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c: *Revenue Administrator*
Municipal Tax Hearing Office