

STATE OF ARIZONA

Department of Revenue
Office of the Director
(602) 716-6090



Janet Napolitano
Governor

Gale Garriott
Director

CERTIFIED MAIL [REDACTED]

The Director's Review of the Decision
of the Hearing Officer Regarding:

[REDACTED]

FEIN [REDACTED]

ORDER

Case No. 200500075-C

On August 4, 2005 the Hearing Officer issued a decision regarding the protest of [REDACTED] ("Taxpayer"). Taxpayer appealed this decision on August 30, 2005. As the appeal was timely, the Director of the Department of Revenue ("Director") issued a notice of intent to review the decision.

In accordance with the notice given the parties, the Director has reviewed the Hearing Officer's decision and now issues this order.

STATEMENT OF CASE

Taxpayer filed a request for refund of corporate income taxes on October 15, 2003 for tax years 1996 through 2002. The request was based on claimed tax credits for pollution control equipment pursuant to A.R.S. § 43-1170. The Corporate Income Tax Audit Section of the Audit Division ("Division") denied Taxpayer's refund request. Taxpayer protested the denial, and the Hearing Officer denied the protest. On appeal, Taxpayer argues that it is entitled to a credit for the construction of storm water retention areas and sewer systems because they constitute pollution control equipment. The Division argues that storm water retention areas and sewer systems, including costs for items such as landscaping, drainage piping, drywell installation, engineering and excavation do not qualify for the credit because such property is not directly used, constructed or installed for the purpose of meeting or exceeding pollution related requirements of the Environmental Protection

Agency or the Department of Environmental Quality. In addition, the Division argues that various claimed expenses were not substantiated by Taxpayer.

FINDINGS OF FACT

The Director makes the following findings of fact:

1. Taxpayer is engaged in the [REDACTED] business in Arizona.
2. Taxpayer has developed [REDACTED] facilities throughout Arizona and a corporate center in [REDACTED], Arizona.
3. Taxpayer installed certain storm water retention areas and sewers, including landscaping, drainage piping, drywell installation, engineering and excavation, on properties owned by Taxpayer. Land costs made up the largest part of the claimed expenses.
4. The purpose of the installed items was to channel storm water runoff and waste water from the properties.
5. The storm water retention areas and the sewer systems serve public health and safety purposes.
6. The primary purpose of the installed items is not pollution control.
7. On October 15, 2003 Taxpayer submitted a request for refund of corporate income tax in the amount of \$ [REDACTED] plus interest for tax years 1996 through 2002.
8. On December 22, 2004 Taxpayer amended its refund request to \$ [REDACTED] for the same period.
9. On May 3, 2005 Taxpayer amended its refund request to \$ [REDACTED], less required depreciation adjustments plus accrued interest for tax years 1997 through 2002. Taxpayer withdrew its refund request for the 1996 tax year.

10. The request for refund results from claimed income tax credits for pollution control equipment pursuant to A.R.S. § 43-1170.
11. The Section denied Taxpayer's refund request.
12. Taxpayer protested the denial.

CONCLUSIONS OF LAW

1. Corporations with a business situs in Arizona are subject to Arizona income tax on income which is the result of activity from sources within the state. A.R.S. § 43-102(A)(5).
2. Arizona allows credits against a taxpayer's Arizona income tax liability for pollution control equipment pursuant to A.R.S. § 43-1170.
3. Tax credits are a matter of legislative grace and not a matter of taxpayer right. Tax statutes are construed strictly against a party who claims a credit. *Arizona Department of Revenue v. Raby*, 204 Ariz. 509, 511, 65 P.3d 458 (App. 2002); *Davis v. Arizona Department of Revenue*, 197 Ariz. 527, 4 P.3d 1070 (App. 2000).
4. A cardinal principle of statutory construction is to follow the plain and ordinary meaning of a word. *Dearing v. Arizona Department of Economic Security*, 121 Ariz. 203, 589 P.2d 446 (App. 1978).
5. Statutes are to be given, whenever possible, such an effect that no clause, word or sentence is rendered superfluous, contradictory, void or insignificant. *State v. Deddens*, 112 Ariz. 425, 542 P.2d 1124 (1975).
6. To qualify for the credit provided by A.R.S. § 43-1170, the property must be directly used, constructed or installed in Arizona for the purpose of meeting or exceeding rules or regulations adopted by the United States environmental protection agency, the department of environmental quality or a political subdivision of this state to prevent, control, monitor or reduce air, land or water pollution. A.R.S. § 43-1170.B.

7. Taxpayer's property does not qualify for the credit under A.R.S. § 43-1170.
8. The Division properly denied Taxpayer's credit request.

DISCUSSION

The issue to be decided is whether the Section properly denied Taxpayer's request for refund. Taxpayer's request is based on claimed tax credits for pollution control equipment pursuant to A.R.S. § 43-1170 for expenses related to the installation of sewer systems and the construction of storm water retention areas on properties owned by Taxpayer. In the refund request, Taxpayer lists expenses such as land costs, landscaping, drainage piping, drywell installation, engineering and excavation, on properties owned by Taxpayer.

A.R.S. § 43-1170, as it existed for the years at issue, provides in pertinent part:

A. A credit is allowed against the taxes imposed by this title for expenses that the taxpayer incurred during the taxable year to purchase real or personal property that is used in the taxpayer's trade or business in this state to control or prevent pollution. The amount of the credit is equal to ten per cent of the purchase price.

B. Property that qualifies for the credit under this section includes that portion of a structure, building, installation, excavation, machine, equipment or device and any attachment or addition to or reconstruction, replacement or improvement of that property *that is directly used, constructed or installed in this state for the purpose of meeting or exceeding rules or regulations adopted by the United States environmental protection agency, the department of environmental quality or a political subdivision of this state to prevent, monitor, control or reduce air, water or land pollution.* The credit allowed pursuant to this section does not apply to the purchase of any personal property that is attached to a motor vehicle. (Emphasis added.)

Credits are a matter of legislative grace and not a matter of taxpayer right. *Keyes v. Chambers*, 209 Or. 640, 307 P.2d 498 (1957)(Credits must be strictly construed against the taxpayer and in favor of the taxing authority); *Davis v. Arizona Department of Revenue*, 197 Ariz. 527, 4 P.3d 1070 (App. 2000)(Tax statutes are construed strictly against a party

who claims a credit.) It is also well settled that statutes are to be given, whenever possible, such an effect that no clause, word or sentence is rendered superfluous, contradictory, void or insignificant. *State v. Deddens*, 112 Ariz. 425, 542 P.2d 1124 (1975).

The legislature made a clear statement in A.R.S. § 43-1170.B. that in order to qualify for the credit the property must be directly used, constructed or installed in Arizona for the purpose of meeting or exceeding rules or regulations adopted by the United States environmental protection agency, the department of environmental quality or a political subdivision of this state to prevent, control, monitor or reduce air, land or water pollution. This legislative requirement must be given meaning.

The storm water retention areas and the sewer systems serve a public health and safety purpose. The storm water retention areas and the sewer systems are not directly used, constructed or installed in Arizona for the purpose of meeting or exceeding rules or regulations adopted by the United States environmental protection agency, the department of environmental quality or a political subdivision of this state to prevent, control, monitor or reduce air, land or water pollution. Therefore, the Director agrees with the Hearing Officer that the Division's denial of Taxpayer's refund request was proper under A.R.S. § 43-1170.

ORDER

The Hearing Officer's decision is affirmed.

This decision is the final order of the Department of Revenue. Taxpayer may contest the final order of the Department in one of two manners. Within 60 days of the receipt of the final order, Taxpayer may file an appeal to the State Board of Tax Appeals, 100 North 15th Avenue, Suite 140 Phoenix, AZ 85007 or, if the amount in dispute is greater than five thousand dollars, Taxpayer may bring an action in Tax Court (125 West Washington, Phoenix, Arizona 85003). For appeal forms and other information from the Board of Tax Appeals, call (602) 364-1102. For information from the Tax Court, call (602) 506-3763.

Dated this 12th day of February, 2007.

ARIZONA DEPARTMENT OF REVENUE

Gale Garriott
Director

Certified original of the foregoing
mailed to:

[REDACTED]

Copy of the foregoing mailed to:

[REDACTED]

GG:st

cc: Corporate Income Tax Appeals Section
Corporate Income Tax Audit Section
Audit Division