

ARIZONA SUPREME COURT

SAN DIEGO GAS & ELECTRIC
COMPANY,

Plaintiff/Appellee,

v.

ARIZONA DEPARTMENT OF
REVENUE, et al.,

Defendants/Appellants.

No. CV-23-0283-PR

Court of Appeals
No. 1 CA-TX 21-0008

Arizona Tax Court
No. TX2019-001758

DEFENDANTS/APPELLANTS' SUPPLEMENTAL BRIEF

Kristin K. Mayes
Attorney General
Firm State Bar No. 14000
Jerry A. Fries
State Bar No. 011788
Assistant Attorney General
2005 North Central Avenue
Phoenix, AZ 85004
Telephone: (602) 542-8385
Tax@azag.gov
Attorneys for Defendants/Appellants

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INTRODUCTION

Defendants-Appellants (“Defendants”) will answer the Court’s two questions in reverse order.

ARGUMENT

I. Did the Court of Appeals Incorrectly Hold that the Accumulated Excess Depreciation Cannot Offset the Value of Unrelated Property, Otherwise Known as Construction Work in Progress?

The court of appeals correctly held that accumulated excess depreciation cannot be applied to the valuation of construction work in progress (“CWIP”) because doing so would conflict with the Legislature’s clear, unequivocal valuation formula for CWIP.

Under [A.R.S. § 42-14154](#), the Department values two distinct components of a company’s Arizona transmission and distribution assets using two different and unrelated methods. Section 42-14154(G)(1) states that CWIP is property that is under construction and that is not in service on the valuation date. Under this statute, CWIP is valued at “fifty per cent of the amount spent and entered on the taxpayers’ accounting records as of December 31 of the preceding calendar year.”

[A.R.S. § 42-14154\(C\)](#). Unlike what occurs with plant in service, there is no further reduction in value because of depreciation—whether its own or otherwise—or because of any other factor.

All of San Diego's CWIP for the subject tax year is within Yuma County and within the Yuma County School District. A full cash value must be placed on the Yuma County tax roll for that CWIP. San Diego reported CWIP of \$7,296,049 as of December 31, 2018. The value that should be placed on the Yuma County tax roll is \$3,648,000 because that is fifty percent (rounded) of \$7,269,049. The statute could not be any clearer. This Court recently stated as follows:

It is a foundational rule of statutory construction “that courts will not read into a statute something which is not within the manifest intention of the legislature as gathered from the statute itself,” and similarly the “court will not inflate, expand, stretch or extend a statute to matters not falling within its expressed provisions.”

Roberts v. State, [253 Ariz. 259, 266](#), ¶ 20 (2022) (quoting *City of Phoenix v. Donofrio*, [99 Ariz. 130, 133](#) (1965)).

When the Legislature wishes to value property or a particular property component using a straight-line depreciation or another depreciation regimen, it makes that clear, as it did with transmission and distribution plant in service in [A.R.S. § 42-14154\(B\)\(2\)\(a\)](#). *See also* [A.R.S. § 42-14254\(B\)\(3\)](#) (statutory valuation of flight property); [A.R.S. § 42-14403\(B\)](#) (telecommunications property); [A.R.S. § 42-13203](#) (shopping centers); [A.R.S. § 42-13353](#) (personal property of manufacturers, assemblers, and fabricators).

When the Legislature, per the Opinion, created a valuation regimen for transmission plant in service that could occasionally result in excess depreciation

for the company's entire plant, it could have provided that the statutory value of CWIP properties, assuming that any existed for that year, would be reduced by such excess depreciation. It did not do so. In contrast to the statute governing the valuation of plant in service, there is no reference to depreciation in the CWIP statute. Hence, there is no legal basis for applying the excess depreciation associated with San Diego's plant in service to the statutory CWIP valuation, and the full cash value of the CWIP on the Yuma County tax roll should be affirmed at \$3,648,000.

If a court were to find that an office building had a full cash value of -\$25,000,000, that value could not be used to eliminate the \$10,000,000 full cash value of a different office building down the street that the same owner owned, much less the full cash value of an office building in a different county. Similarly, the -\$25,000,000 could not be used to eliminate the statutory full cash value of vending machines and other taxable personal property in the negatively valued building, which would all be personalty that is valued and taxed pursuant to [A.R.S. § 42-15051](#). There is no case law on this issue since a negative value for ad valorem tax purposes is without any known precedent. But there is ample statutory support for the proposition that all taxable property must be valued at its market or statutory value, including, among others, [A.R.S. § 42-11001\(6\)](#).

II. Did the Court of Appeals Incorrectly Hold that the Accumulated Excess Depreciation Cannot Reduce the Full Cash Value of Plant in Service to a Negative Number?

Initially, Defendants note that Plaintiff did not ask for a negative value for its plant in service before either the tax court or the court of appeals. It has therefore waived whatever “right” it has to such relief. *N. Valley Emergency Specialists, L.L.C. v. Santana*, 208 Ariz. 301, 302 n.2, ¶ 6 (2004) (finding that an issue that was not raised in the trial court or in the court of appeals was waived). As Defendants note in subsection II(B) *supra* pp. 11-12, however, if there are no consequences to Defendants arising out of a negative value, then Defendants can think of no objection to setting the plant in service full cash value at a negative number.

A. A Negative Valuation for Transmission and Distribution Property Is Unconstitutional and Unsupported by the Statute.

As with the CWIP question, this is an issue of first impression because to Defendants’ knowledge, no known legislative body the world over has ever legislated negative property values for ad valorem tax purposes.

The court of appeals’ Opinion declined to reach the argument that Defendants again raised in their Petition for Review (“Petition”)—that a \$0 or negative value for taxable Arizona property is an unconstitutional exemption in

violation of the Exemptions Clause.¹ (*See* Opinion n.3, ¶ 23; Petition at 17.)

Nevertheless, Defendants will expand on that argument here because it is responsive to the Court’s question regarding whether San Diego’s plant in service can have a negative value.

Since statehood, the few cases on point as discussed below have all held that the Legislature is precluded from exempting taxable property from taxation given the limitation in the Exemptions Clause providing that “[a]ll property in this state that is not exempt under the laws of the United States or under this section is subject to taxation as provided by law.” [Ariz. Const. art. IX, § 2](#). Section [42-11002](#) reiterates the constitutional language, providing that “[a]ll property in this state is subject to taxation except as provided in article IX, Constitution of Arizona, and article 3 of this chapter [of Title 42].” Transmission properties are not exempt under either federal or state law; indeed, the Legislature specifically stated that they must be valued and taxed under [A.R.S. § 42-14154](#). Quite simply, as taxable property, they must be taxed and cannot be exempted.²

¹ [Ariz. Const. art. IX, § 2](#).

² Even assuming that the total accumulated depreciation of a transmission company’s property does not exceed the plant’s total cost, Exemption Clause violations still exist with respect to all plant components (such as a transmission tower) whose combined accumulated straight-line depreciation of plant and cost of removal reserve monies exceed plant cost. All such plant is valued at \$0, with the excess depreciation used to lower the statutory values of newer plant. A \$0 value for any plant in service component violates the Exemptions Clause.

In *Recreation Centers of Sun City, Inc. v. Maricopa County*, [162 Ariz. 281](#) (1989), this Court vacated a court of appeals opinion holding that a residential common area property owned by a nonprofit homeowners' association and "burdened" by a nonprofit deed restriction had no value for tax purposes. In addition to rejecting the taxpayer's argument that a not-for-profit deed restriction destroyed the property's value (*id.* at 288), this Court rejected the taxpayer's implicit claim that it was exempt from taxation by virtue of the property's alleged unmarketability. Citing [Article IX, § 2](#), this Court stated that only specific property could be exempted from taxation given the Constitution's purpose in ensuring that all property in the state bears "its just burden of the taxes." [162 Ariz. at 284](#). In that regard, the Court stated as follows:

Our constitution states that "[t]he power of taxation shall never be surrendered, suspended, or contracted away." [Ariz. Const. art. 9, § 1](#). Such power is to be exercised for the public good. *Id.* Indeed, "the object of taxing property is to produce the revenues with which to conduct the business of the state...." *State v. County of Maricopa*, [38 Ariz. 347, 350, 300 P. 175, 176](#) (1931). Accordingly, only specific property may be exempt from taxation. [Ariz. Const. art. 9, §§ 2, 2.1, 2.2, and 2.3](#). The purpose of these constitutional provisions is to ensure that all property in the state bears "its just burden of the taxes." *Brophy v. Powell*, [58 Ariz. 543, 554, 121 P.2d 647, 652](#) (1942).

Legislative tax exemptions that force other taxpayers to bear increased tax burdens must foster legitimate social goals and comply with constitutional provisions. *See Comment, Real Property Exemptions in Arizona*, Law & Soc. Order 241 (1972). Therefore, the legislature may not exempt from *ad valorem* tax any property or class of property not specified in the constitution, and any law exempting property from taxation is to be strictly construed. *Kunes v. Samaritan Health Serv.*,

[121 Ariz. 413, 590 P.2d 1359](#) (1979). The legislature’s policy is that “all property in this state shall be taxed, excepting only the classifications permitted by the constitution.” See [A.R.S. § 42–271\(A\)\(1\) to \(17\)](#). Rec Centers’ property does not fall within any of the permitted exceptions.

(*Id.*) The Court reiterated these sentiments in *In re America West Airlines, Inc.*, [179 Ariz. 528, 535](#) (1994), where it held that “[u]nder our constitution, the power to classify and impose differing taxation rates is legislative, but the responsibility to enforce the constitution’s limits is judicial.”

In addition to the constitutional implications, nothing in [A.R.S. § 42-14154](#) or the related valuation statutes, [A.R.S. §§ 42-14151 to -14153](#), allows for a negative valuation of a plant in service. (Opinion, ¶ 21.) All constitutional, statutory, and case authorities compel the taxation of all of San Diego’s transmission property and forbid its exemption from taxation. Moreover, as the Opinion notes, courts should seek to avoid absurd results. (*Id.*) A violation of the Exemption Clause occurs with respect to any portion³ of the company’s property that is valued at a negative number, a facially absurd result independent of the Exemptions Clause.

³ There is no legal support for the proposition that if some of a person’s taxable property in Arizona (here, San Diego’s CWIP in Yuma County) owes tax, then other parts of its taxable property or properties can be exempted. If the Legislature were to tax a person’s first home in Arizona and exempt from taxation all other homes or property that the person owned in the same county or elsewhere in the state, that would violate the Exemptions Clause, as well as the Uniformity Clause found in [Arizona Constitution article IX, § 1](#).

B. Defendants Have No Objection to a Negative Value for Plant in Service if There Are No Payment Consequences.

The only perceptible reason to discuss the merits of a negative value relative to a zero value would be if the negative value somehow had taxation implications. Presumably, those tax implications would be something along the lines of the various taxing jurisdictions—school districts, fire districts, and community college districts—owing money to the property owner arising out of the negative valuation. There is no sense to this and no statutory or other basis for it.

Title 42 has hundreds of statutes relating to the valuation and taxation of property, the payment of taxes by property owners, and the payment of refunds of taxes paid to taxpayers under certain circumstances. There are no provisions that obligate the several taxing authorities to pay monies to property owners whose taxable properties have negative values.

If the several Maricopa County taxing jurisdictions that a negative plant full cash value could potentially impact will owe no monies to San Diego arising out of negative property values, then the question regarding negative plant in service values appears to be of no consequence. Determining whether the property's full cash value is \$0, -\$2,000,000, or -\$200,000,000 is meaningless if the result under all three scenarios is simply that the property owner owes no taxes on its property.

CONCLUSION

For the foregoing reasons, this Court should affirm the Opinion's CWIP value of \$3,648,000. And if there are no payment or other consequences to any taxation jurisdiction arising out of a negative value for plant in service, then Defendants can think of no objection to having the tax year 2020 full cash value set at a negative number. If there are payment or other unknown consequences, Defendants object because there is no statutory basis for any such relief.

Respectfully submitted this 25th day of March, 2024.

Kristin K. Mayes
Attorney General

/s/ Jerry A. Fries _____
Jerry A. Fries
Assistant Attorney General
Attorneys for Defendants/Appellants