SUPREME COURT OF ARIZONA

SAN DIEGO GAS & ELECTRIC COMPANY, a California corporation, Plaintiff/Appellee, vs. ARIZONA DEPARTMENT OF REVENUE, an agency of the State of Arizona; MARICOPA COUNTY, and YUMA COUNTY, each of which is a political subdivision of the State of Arizona, Defendants/Appellants.	**No. CV-23-0283-PR** Court of Appeals Case No. 1 CA-TX 21-0008 Arizona Tax Court No. TX 2019-001758

PLAINTIFF/APPELLEE'S SECOND SUPPLEMENTAL BRIEF

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INTRODUCTION

Pursuant to this Court's Order dated November 7, 2024, Plaintiff/Appellee, San Diego Gas & Electric Company ("SDG&E") files its Second Supplemental Brief on the following two-part question: "What is the relationship between [Sections] 42-14154, 42-15147 (sic),[1] and 42-15001,[2] and what consequence, if any, does a negative [or][3] reduced plant in service cost have on the allocations provided for in [Section] 42-14157?" The short answers – in this case – are: (1) These statutes are not related to each other; and (2) a reduced plant in service cost under Section 42-14154 does not implicate the allocations described in Section 42-14157.

Accordingly, for the reasons already set forth at length in SDG&E's prior briefing, its Cross-Petition should be granted and the tax court's Judgment setting the 2020 full cash value of SDG&E's Arizona property at $1,019,473 – which was calculated exactly as A.R.S. §42-14154 mandates – should be reinstated.

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[1] This is an apparent transposition, as no such statute exists. SDG&E believes the Court intended to refer to Section 42-14157, so it will address that statute herein.

[2] SDG&E presumes this reference is correct, but this statute is not in dispute here.

[3] SDG&E assumes the Court meant to insert the conjunction "or" between the words "negative" and "reduced" in reference to the "plant in service cost" (as defined in Section 42-14154), because that is what the record establishes. The "plant in service cost" portion of the full cash value was "reduced" by the "accumulated provision for depreciation" (which both lower courts correctly ruled includes cost of removal). The result of that calculation here is $1,043,402, which is not a negative number. The statute also requires that CWIP be added. A.R.S. §42-14154(C). Lastly, "land rights" are not "plant" and must be "excluded." A.R.S. §42-14154(G)(8). Thus, while the plant in service cost is reduced, it is not negative as this question implies.

LEGAL ARGUMENT

I. In this Case, Section 42-14154 is Not Related to Either Statute.

In its Order, this Court has asked how Section 42-14154 relates to two other statutes in Title 42; namely, Sections 42-14157 and 42-15001. The short answer is neither statute is related to Section 42-14154 on the facts of this case.

The question about Section 42-15001 is the easiest to explain. It requires an understanding of the definitions used in the property tax portion of Title 42. These are found in Chapter 11. In Arizona, all property is first valued at its "full cash value." A.R.S. §42-11001(6). In this case, the first sentence of that definition is the only portion relevant to this valuation appeal: "Full cash value … means the value determined as prescribed by statute." *Id*. The remainder of the definition only comes into play if no statutory valuation method is prescribed. *Id*. In this case, Section 42-14154 is the statutorily-prescribed method. This method was expressly upheld in *Ariz. Dep't of Revenue v. Trico Elec. Coop., Inc.*, 151 Ariz. 544 (1986).

Once determined, full cash value is multiplied by an assessment percentage based on its legal class, which is called the "assessed value." A.R.S. §42-11001(1). It is undisputed here that SDG&E owns Class 1 property. A.R.S. §42-12001(3). Pursuant to A.R.S. §42-15001, the percentage for Class 1 property is 18%. A.R.S. §42-15001(11). There is no dispute here about the classification or this percentage. Most importantly, neither issue affects how the full cash value is determined.

Turning to Section 42-14157, based on what is owned by SDG&E in Arizona, it does not apply to this case. The full cash value for SDG&E in tax year 2020 was undeniably determined by ADOR using Section 42-14154. SDG&E filed this tax appeal to challenge that full cash value due to ADOR's misconstruction of the statutory valuation method on the issue of whether "cost of removal" is part of the "accumulated provision for depreciation" as defined by FERC. Both lower courts ruled correctly in SDG&E's favor on this issue, and reduced the full cash value. And although this value was later apportioned by ADOR to Maricopa and Yuma counties, that fact does not implicate the "allocation" described in Section 42-14157.

This conclusion is evident from the plain language of Section 42-14157. Its first sentence states: "The value of property computed under sections 42-14154 [investor-owned utilities], 42-14156 [electric generation assets] and 42-14159 [non-profit utilities known as "distribution cooperatives"] shall be allocated among the various taxing jurisdictions as follows: . . .." What follows is a three-step process for utilities and distribution cooperatives that also own generation properties valued under Section 42-14156 to allocate their total full cash values using a ratio of their respective values to the original plant in service costs. A.R.S. §42-14157(A).[4]

[4] Section 42-14157 was added in 2003. It followed the Legislature's deregulation of electric generation property, which is now valued under A.R.S. §42-14156. So, when an investor-owned utility or an electric cooperative also owns generation property, this statute provides a way to "allocate" the total value of the "combined" properties. In 2013, renewable energy was added to such combinations. A.R.S. §42-14157(D).

Construing Section 42-14157 as a whole, the clear reason Section 42-14157 does not apply here is because SDG&E does not own any electric generation property that is valued under the provisions of Section 42-14156 (or renewable energy equipment valued under Section 42-14155). Instead, SDG&E owns only electric transmission property. The statute requires the values computed under either §42-14154 (utilities) or §42-14159 (cooperatives), be "combined" with the separate values of electric generation properties (calculated under §§42-14156 or 42-14155), if all are commonly-owned or part of a "combined group." A.R.S. §42-14157(E). Because SDG&E does not own any generation properties, and it is not part of any "combined group," there is no "combined" value to be allocated under the method prescribed by A.R.S. §42-14157. Therefore, this statute does not apply here.

This case is before this Court now due to ADOR's appeal from the tax court's ruling in favor of SDG&E on its appeal of the full cash value determined by ADOR for its electric transmission property in tax year 2020. Both lower courts ruled ADOR's valuation contravened the method prescribed by the Legislature in Section 42-14154, because ADOR added-back arbitrary figures for "cost of removal" that are part of the "accumulated provision for depreciation" reported by SDG&E to FERC. This case is SDG&E's sole recourse to appeal its full cash value. No statute authorizes an appeal of only a portion of the full cash value, or how it was allocated. *See, Transamerica Development Co. v. County of Maricopa*, 107 Ariz. 396 (1971).

In summary, neither of the statutes referenced in this Court's question are related to Section 42-14154. That statute prescribes the method used to determine SDG&E's full cash value, which is the sole issue in this appeal. A.R.S. §42-16204.[5]

II. SDG&E's Reduced Plant in Service Cost is Part of its Full Cash Value.

The second-part of this Court's question asks whether there is any consequence to the fact SDG&E's plant in service cost is "negative [or] reduced" (*see* Note 3, *supra*), for purposes of "the allocation provisions in Section 42-14157." In one sense, SDG&E's answer to the first-part of this Court's question answers the second-part of the question, but there are additional reasons why that is true.

First and foremost, allocation provisions such as the one found in Section 42-14157 have nothing to do with valuation. As noted in an earlier brief, the purpose of such statutes is to "allocate" the total value of unitary operating properties to the different jurisdictions where it operates. *See, Adams Express Co. v. Ohio State Auditor*, 165 U.S. 194 (1897) (referring expressly to what were known as "express" companies and railroads). Most of the law in this area has arisen in cases where the taxpayer owns property that crosses state lines (*e.g.*, railroads, pipelines, utilities and telecommunications companies). *See, e.g.*, *Mississippi Tax Comm'n v. ANR Pipeline Co.*, 806 So.2d 1081 (Miss. 2002). In fact, the property at issue in this case (electric

[5] This is also why neither side ever referenced either A.R.S. §§42-14157 or 42-15001 in the extensive briefing of cross-motions for summary judgment in the tax court, or in any of the multiple briefs filed with the court of appeals or this Court.

transmission facilities), also falls into this category because the majority of that property is located in California. But, there is no dispute here about the value of SDG&E's Arizona transmission property vis-à-vis its property in California. That is because this "allocation" took place when SDG&E filed its Arizona tax return.[6] Since that was never in dispute here, there is no "allocation" issue in this case.

Again, the plain language of Section 42-14157 reinforces this proposition. The statute talks about "the value" (singular) determined under Section 42-14154 (and two other statutes). A.R.S. §42-14157(A). These separate, individual full cash values – as computed under each statute – are then combined together before they are "allocated" under Section 42-14157. Notably, this process does not alter the individual full cash values determined under each separate statute. Instead, it merely specifies how values already determined under those statutes are combined when there are also electric generation assets involved. In most cases, this is done on the basis of the "combined" original costs. That is the sole purpose of subsections A, B, D and E of Section 42-14157. As for subsection C, when read as a whole it merely forbids combining CWIP with any EPF costs for allocation purposes.[7]

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[6] ADOR's reporting form for property valued pursuant to A.R.S §42-14154 (Property Tax Form 82054) requires owners of such property to report system-total information alongside Arizona-only information, so no "allocation" is required.

[7] One reason CWIP may be allocated differently is because CWIP is not taxable under Section 42-14156 until it is placed into service. A.R.S. §42-14156(A)(7). Also, it is undisputed here that SDG&E has never reported any EPF costs to ADOR.

In this case, there is no dispute that SDG&E's CWIP was included in the calculation of its full cash value under Section 42-14154. Moreover, since SDG&E reported no EPF, Section 42-14157(C) does not apply. Indeed, nothing in Section 42-14157 changes how SDG&E's full cash value was determined by ADOR.

Finally, any confusion about what Section 42-14157 means here is due to a related determination that is required whenever property like SDG&E's transmission lines is physically located in separate taxing jurisdictions. That is why SDG&E named both Maricopa and Yuma counties as defendants. They are required parties in a tax appeal because both counties collect and distribute taxes based on the full cash value determined by ADOR under Section 42-14154. Tax practitioners refer to this process as "apportionment," which (like allocation) is a calculation made separately from determining full cash value – and also done after the value is set.[8]

In the case of utilities (investor-owned or cooperatives), the Legislature enacted Section 42-14157 to ensure that the apportionment of any taxes that are later assessed on the values determined for each of the separate properties owned by utilities would include any values that resulted from deregulation of electric

[8] A good illustration is how railroad property in Arizona is taxed. First, it is valued at its full cash value under Section 42-14351, *et seq*. This involves determining the value of the entire railroad and then "allocating" a portion to Arizona. A.R.S. §42-14355(A)(4) and (B)(1). Because each railroad crosses multiple tax jurisdictions in Arizona, the full cash value must then be "apportioned." *See*, A.R.S. §42-14357(C); *see also*, A.R.S. §§42-14404(A)(1) (telecommunications). When either allocation or apportionment is required, it happens after the full cash value is already determined.

generation property. A.R.S. §42-14156 (and later, §42-14155 renewable energy). No doubt, this was done to avoid shifting large portions of a utility's total value. Because power plants are often located in remote areas, concerns about shifting of assessed values frequently arise with utilities that own such property. *See, e.g., Tucson Electric Power Co. v. Apache County, et al.*, 185 Ariz. 9, 13-14 (Ct. App. 1995).

Those concerns are not present here. SDG&E's Arizona electric transmission property (high-voltage transmission lines and towers) is located between the Palo Verde Nuclear Generating Station and the California border. Here, ADOR's value was apportioned to Maricopa and Yuma counties and the taxes were paid. The issue of how ADOR apportioned SDG&E's full cash value to both counties has nothing to do with the only issue raised in SDG&E's tax appeal. *See*, A.R.S. §42-16207.

Thus, the answer to the second part of this Court's question about Section 42-14157 is it does not have anything to do with the issue presented by this case, which is: What is the full cash value of SDG&E's property under A.R.S. §42-14154? The tax court answered that question correctly, so its judgment should be affirmed.

III. Courts Should Not Resolve Issues that Are Not Before Them.

As noted earlier, no party to this litigation ever raised the applicability of Sections 42-14157 or 42-15001 in this case. Neither statute was referenced in the complaint or in the parties' extensive cross-motions for summary judgment before the tax court. Similarly, they were not mentioned in any of the briefs filed with the

court of appeals. They were also not raised in either the Petition or Cross-Petition for Review, or the responses to each. Finally, neither statute was referenced or cited by either side in the supplemental briefing that preceded this Second Supplemental Brief. The first (and only) time this statute has been mentioned before now was in questioning during oral argument before this Court on SDG&E's Cross-Petition.

If this argument was raised by either of the parties at this late stage of the litigation, SDG&E has no doubt the Court would follow the general rule relating to such arguments, which is to find them waived. *N. Valley Emergency Specialists, L.L.C. v. Santana*, 208 Ariz. 301, 302 n.2, ¶6 (2004) (finding an issue not raised in the trial court or court of appeals was waived). And, while the doctrine of waiver does not apply to courts, there are other principles governing the exercise of judicial power that do, including the doctrines of judicial review and restraint.

In particular, it is well known that courts do not (and should not) provide what are known as "advisory" opinions. *See*, *Mills v. Ariz. Bd. of Technical Registration*, 253 Ariz. 415, 423, ¶23 (2022) (Arizona courts do not give advisory opinions); *see also*, *Arizona Creditors v. State of Arizona*, 549 P.3d 205, ¶22 (Ct. App. 2024).

In addition, it is clear that notwithstanding the broad grant of jurisdiction in Article 6, §1, there are limits set forth in Article 3 of the Constitution on a court's jurisdiction when reviewing legislative action. Article 9, §11 also imposes specific limits on review of tax legislation. *See*, *Trico*, *supra*. This Court stated many years

ago in a property tax valuation case: "The right to appeal is statutory and the method provided by the Legislature is exclusive." *Pima County v. Cyprus-Pima Mining Co.*, 119 Ariz. 111, 113 (1978) (citing, *County of Pima v. State Dept. of Revenue*, 114 Ariz. 275, 560 P.2d 793 (1977) and *Williams v. Bankers Nat. Ins. Co.*, 80 Ariz. 294, 297 P.2d 344 (1956).). These principles are still the law in Arizona.

As noted, no party in this case has ever claimed Section 42-14157 alters the valuation method prescribed by A.R.S. §42-14154. That statutory full cash value was the sole issue SDG&E raised in this tax appeal. It was also the sole issue decided by the tax court when it ruled on cross-motions for summary judgment below. It was the main focus of the court of appeals' opinion affirming the tax court's ruling that ADOR had no legal right to add-back the "cost of removal" reported by SDG&E. SDG&E's Cross-Petition was focused primarily on paragraph 21 of the lower court's opinion, where it acknowledged that nothing in Section 42-14154 contradicts the tax court's interpretation of the statute, but it nonetheless vacated the judgment.[9]

Respectfully, this Court should not decide an issue that is not before it. SDG&E has not found any case ever decided by this Court that goes outside the scope of the issues raised by the parties, unless it was necessary to ensure the Arizona

[9] Paragraph 21 states: "Nothing in the plain language of A.R.S. §42-14154 … expressly provides for or precludes a negative full cash valuation of a plant in service." Based solely on its erroneous conclusion that the plant in service cost portion of SDG&E's full cash value under Section 42-14154 was negative, the court vacated the tax court's judgment. SDG&E's Cross-Petition challenged this holding.

Constitution was not violated. That is the essence of the doctrine of judicial review. No party here has made such an argument. More importantly, no court has ever suggested the method mandated by Section 42-14154 violates the Constitution.[10]

To reiterate, the full cash value determined by the tax court's judgment in this case is a positive number – $1,019,473. It was calculated by applying all of Section 42-14154, as written. Hence, this Court should reinstate that Judgment.[11]

CONCLUSION

For the foregoing reasons – and those stated previously – SDG&E asks this Court to vacate the portion of the court of appeals' opinion that reversed the tax court's Judgment and affirm the correct full cash value under Section 42-14154.

RESPECTFULLY SUBMITTED this 29th day of November, 2024.

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[10] In *Trico*, this Court expressly held the predecessor to this statute constitutional. Although numbered differently, the statutes are textually identical on this issue.

[11] It is worth remembering this case presents only a one-year issue. The lower full cash value for SDG&E in tax year 2020 was an isolated occurrence resulting from the timing of the CWIP reported for tax year 2020. CWIP is valued at only 50% of cost. A.R.S. §42-14154(C). In 2021, 100% of it became "plant in service cost." So, the issue presented here has not recurred for SDG&E (or any other taxpayer valued under §42-14154) in subsequent tax years. SDG&E knows this because ADOR's add-backs for cost of removal that gave rise to this case continued in tax years 2021, 2022, 2023 and 2024, but not the "negative value" issue. *See, e.g.*, TX2020-001125.