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February 12, 1987

Ms. Betsey Bayless, Director
Arizona Department of Revenue
State Capitol Building
Phoenix, Arizona 85007

Re: I87-029 (R86-088)

Dear Ms. Bayless:

Your predecessor in office, Mr. J. Elliott Hibbs, requested an opinion from this office concerning the application of A.R.S. § 42-144(E) relating to "construction work in progress" in the calculation of property tax levy limits under A.R.S. § 42-301(A). This question requires us to address the following sub-questions:

1. Is the entire cost of construction work in progress "subject to tax" within the meaning of art. IX, § 2 of the Arizona Constitution and A.R.S. §§ 42-144(E) and 42-301(A)(3)?

2. When a newly-completed utility plant has been placed in commercial service during the preceding tax year, should the assessed value of that plant "for the current tax year" be based upon fifty per cent of its construction cost under A.R.S. § 42-144(E) for the purpose of making the calculation in A.R.S. § 42-301(A)(3)?

It is our opinion that the answer to the first question is "yes," and the answer to the second question is "no."

In order to answer the first question, it is necessary to examine A.R.S. § 42-144, which governs the valuation of gas and electric utility property, and A.R.S. § 42-301(A), which governs the calculation of the property tax levy limit.

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A.R.S. § 42-144 was first enacted by the Legislature in 1980 as former § 42-124.01 and simplified the valuation of utility property by the Department of Revenue for ad valorem tax purposes. The statute provides that utility property in Arizona shall be valued for such purposes by a "cost-less-depreciation" formula using the utility's reported figures for "construction work in progress," "depreciation," "materials and supplies," "original plant in service cost," and other accounting categories. The constitutionality of this statutory valuation formula was recently affirmed by the Arizona Supreme Court. See Arizona Department of Revenue v. Trico Electric Cooperative, Inc., ___ Ariz. ___, 729 P.2d 898 (1986).

A.R.S. § 42-144(C)(1) defines "construction work in progress" as follows:

"Construction work in progress" means the total of the balances of work orders for an electric, gas distribution or combination electric and gas distribution plant in process of construction on the last day of the preceding calendar year exclusive of land rights and licensed vehicles.

The treatment of "construction work in progress" in the statutory formula is provided in A.R.S. § 42-144(E):

The value of construction work in progress is fifty per cent of the amount expended and entered upon the accounting records of the taxpayer as of December 31 of the preceding calendar year as construction work in progress.

(Emphasis added.)

When determining the proper construction to place upon a statute, legislative intent is controlling. State v. Weible, 142 Ariz. 113, 688 P.2d 1005 (1984). Widespread public concern for limiting local government spending and keeping property taxes at tolerable levels led to the passage of a package of constitutional and statutory amendments in 1980, including the present version of A.R.S. § 42-301. See

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generally, "State of Arizona Publicity Pamphlet and Sample Ballot, Special Election, June 3, 1980," prepared by the Arizona Secretary of State. The obvious purpose of A.R.S. § 42-301 is to impose effective, realistic levy limitations on counties, cities, towns and community college districts. The construction placed on the statutes in this opinion, therefore, must be in accordance with that legislative intent.

A.R.S. § 42-301(A) provides:

A. In addition to any other limitations that may be imposed, the counties, cities, including charter cities, towns and community college districts shall not levy primary property taxes in any year in excess of an aggregate amount computed as follows:

1. Determine the maximum allowable levy of primary property taxes for such jurisdiction for the prior tax year plus taxes for the prior year collectible pursuant to § 42-236.

2. Multiply the dollar amount determined in paragraph 1 by 1.02.

3. Determine the assessed value for the current tax year of all property in such entity that was subject to tax in the preceding tax year. The assessed value shall include the estimate of the assessed value upon which the taxes collectible pursuant to § 42-236 and included in paragraph 1 are based.

4. Divide the dollar amount determined in paragraph 3 by one hundred and then divide the dollar amount determined in paragraph 2 by the resulting quotient.

5. Determine the finally equalized valuation of all property, less-exemptions, appearing on the tax roll for the current tax year including an estimate of the unsecured property tax roll determined pursuant to § 42-304.01.

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6. Divide the dollar amount determined in paragraph 5 by one hundred and then multiply the resulting quotient by the rate determined in paragraph 4. The resulting product shall be the maximum allowable levy of primary property taxes for the current fiscal year for all political subdivisions other than a county. The resulting product shall be the maximum allowable levy of primary property taxes for the current fiscal year for a county, subject to further reduction pursuant to subsection J of this section.

(Emphasis added.)

The first question involves the proper construction of the phrase "all property in such entity that was subject to tax in the preceding tax year" (emphasis added) as used in A.R.S. § 42-301(A)(3). Art. IX, § 2 of the Arizona Constitution sets forth a variety of types and classes of property which are declared to be exempt from taxation. However, art. IX, § 2(6) specifically provides:

(6) All property in the State not exempt under the laws of the United States or under this Constitution or exempt by law under the provisions of this section shall be subject to taxation to be ascertained as provided by law.

(Emphasis added.)

It is axiomatic that in the interpretation of the language of the Arizona Constitution, and unless the context otherwise requires, the words employed are to be accorded their plain, natural and ordinary meaning. McElhaney Cattle Co. v. Smith, 132 Ariz. 286, 645 P.2d 801 (1982); County of Apache v. Southwest Lumber Mills, Inc., 92 Ariz. 323, 376 P.2d 854 (1962). The plain meaning of the language of art. IX, § 2(6) is that, unless property within the State of Arizona is specifically declared by the Constitution or by law to be exempt, it shall be subject to taxation.

Moreover, the Legislature has used virtually the same language in A.R.S. § 42-271 (enumerating exemptions from

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taxation) by stating that "[a]ll property in this state shall be subject to taxation, except" (emphasis added). That statute makes no exception for "construction work in progress" at, for example, an investor-owned utility plant. Therefore, "construction work in progress" is "subject to taxation" in its entirety, regardless of the percentage applied to its cost for purposes of valuation under A.R.S. § 42-144(E).

This conclusion is supported by the all-inclusive language of the statutory formula, which provides that "[a]ll . . . utility property . . . shall be valued as provided in this section." A.R.S. § 42-144(B) (emphasis added). "Utility property" is defined to include, without limitation, utility "plant" and "construction work in progress," among other property. A.R.S. § 42-144(C)(7). The term "plant" is defined to include

all property situated in this state used or useful for the generation, transmission or distribution of electric power or distribution of natural gas

A.R.S. § 42-144(C)(6) (emphasis added).

It is significant that, in A.R.S. § 42-144(E), the Legislature selected the term "value of construction work in progress" (emphasis added) and determined that the "value" would be measured by fifty per cent of the amounts shown for that accounting item on the company's books at year end. Thus, the fifty per cent ratio is only applied to the cost of construction in order to calculate the value of the utility plant while construction is "in progress." Once construction has been completed, the value of the utility plant will be based upon its "actual cost" of construction, not "fifty per cent" of cost. A.R.S. § 42-144(C)(5). Stated otherwise, all of the construction work in progress is subject to taxation, and only its value is calculated by application of the fifty per cent ratio.

Therefore, the entire cost, that is, one hundred per cent of "construction work in progress" at a utility plant "was subject to tax in the preceding tax year" under A.R.S. § 42-144 for purposes of making the levy limit calculation in A.R.S. § 42-301(A)(3).

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The second question concerns the proper treatment, in the levy limit calculation for the current tax year, of a recently completed utility plant that has been placed in commercial service during the previous tax year. The narrow question is whether the "assessed value for the current tax year" of such a plant should be based upon fifty per cent of its value or upon its total value for the purpose of making the calculation in A.R.S. § 42-301(A)(3).^{1/}

The answer to the second question follows from the answer to the first question, and from the last sentence of A.R.S. § 42-144(A): "The full cash value is the value determined as of January 1 of the tax year." When a new utility plant is placed in service, it is no longer valued on the basis of fifty per cent of its cost. At that point the new plant becomes "used or useful for the generation, transmission or distribution of electric power" and is valued on the basis of its "actual cost." A.R.S. §§ 42-144(C)(5) and (6) and 42-144(D). The total value of the new plant will then be reflected in the "finally equalized valuation of all property" appearing on the tax roll for the current tax year in A.R.S. § 42-301(A)(5).^{2/}

^{1/}If fifty per cent of its value is used in the calculation, then the denominator in A.R.S. § 42-301(A)(3) will be reduced, and the levy limit rate in A.R.S. § 42-301(A)(4) will be increased accordingly. If, however, the total value is used in the calculation, then the denominator will be increased, and the levy limit rate will be decreased.

^{2/}As each phase of plant construction is completed, that part of the overall project will be included in the tax base at its total cost. As a practical matter it is not necessary to establish the precise date when a utility plant is placed into commercial service in making the levy limit calculation. The actual date of service will be determined by the state or federal regulatory commission which approves the utility's rates, such as the Arizona Corporation Commission or the Federal Energy Regulatory Commission ("F.E.R.C."). When determining the value of "utility property," the Department

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Therefore, if the new plant was placed in service during the previous tax year, then the "assessed value" of the plant "for the current tax year" must be determined as of January 1

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uses the figures for "construction work in progress" and "plant in service" reported by the utility company to the F.E.R.C. as of December 31 of the preceding tax year. We believe this administrative practice is sanctioned by the plain language of A.R.S. § 42-144(I), which provides:

I. All terms and applications of terms shall be interpreted as nearly as possible, under the circumstances, as contained in the federal energy regulatory commission reports for electric and gas utilities in effect on January 1, 1979.

(Emphasis added.)

When a power plant is placed in commercial service, the company will make a bookkeeping transfer of the plant's cost from the "construction work in progress" account to the "plant in service" account. As a general rule, the company must do so before the cost of the newly-completed plant may be recovered in the utility rates charged to its customers. Thus, the figures reported for "plant in service" as of December 31 will automatically reflect the actual cost of new plant construction that was placed in commercial service during the previous year.

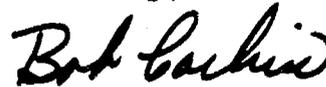
Therefore, the statutory formula contemplates that large utility plants will be completed in phases or "units" and specifically allows for the possibility that some units of the plant might be licensed for commercial operation before others. See, e.g., A.R.S. § 42-144(D)(2) concerning reductions in value when a plant loses its operating license. Thus, the valuation of a new utility plant will be based upon each phase or "unit" that has been placed in commercial service as of January 1 of the tax year, as determined by the appropriate state or federal regulatory agency. As each unit goes "on line," the total value of that unit will be reflected in the levy limit calculation.

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of the current tax year. As of January 1, the new plant is in commercial operation and is no longer under construction. Its "assessed value" as of January 1 must be based upon its total cost, not fifty per cent of its cost. A.R.S. §§ 42-144(C)(5) and 42-144(D).

Accordingly, it is our opinion that, in the tax levy limit calculation, the "assessed value for the current tax year" of a newly completed power plant that has been placed in commercial service during the previous tax year should be based upon the total cost of the new plant in accordance with A.R.S. § 42-144(D), and not upon fifty per cent of its cost pursuant to A.R.S. § 42-144(E).

Sincerely,



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