

## ARIZONA TRANSACTION PRIVILEGE TAX RULING

TPR 02-2

### 4" Pipe

This substantive policy statement is advisory only. A substantive policy statement does not include internal procedural documents that only affect the internal procedures of the agency and does not impose additional requirements or penalties on regulated parties or include confidential information or rules made in accordance with the Arizona administrative procedure act. If you believe that this substantive policy statement does impose additional requirements or penalties on regulated parties you may petition the agency under Arizona Revised Statutes § 41-1033 for a review of the statement.

#### ISSUES:

1. Whether gross income from the sale of pipe 4" or larger in diameter used to transport sewage qualifies for the deductions from the tax base under the retail classification and the use tax for 4" or larger pipe used to transport oil, natural gas, artificial gas, water or coal slurry.
2. Qualification of certain types of pipe, 4" or larger, for the deduction under A.R.S. § 42-5061(B)(6).

#### APPLICABLE LAW:

Arizona Revised Statutes (A.R.S.) § 42-5061 imposes the state's transaction privilege tax on the business of selling tangible personal property at retail. The tax base for the retail classification is the gross proceeds of sales or gross income derived from the business. All sales of tangible personal property are subject to tax unless a deduction is provided by statute.

A.R.S. § 42-5061(B)(6) provides a deduction from the tax base for "[p]ipes or valves four inches in diameter or larger used to transport oil, natural gas, artificial gas, water or coal slurry."

A.R.S. § 42-5155(A) imposes Arizona's use tax on the purchase of tangible personal property that is used, stored, or consumed in Arizona.

A.R.S. § 42-5159 provides specific deductions from the use tax for certain purchases of tangible personal property.

A.R.S. § 42-5159(B)(6) provides a deduction from the tax base for "[p]ipes or valves four inches in diameter or larger used to transport oil, natural gas, artificial gas, water or coal slurry."

## DISCUSSION:

### Purpose and Use of the Pipe

A.R.S. §§ 42-5061(B)(6) and 42-5159(B)(6) (the "Statutes") allow income from the sale of "[p]ipes or valves four inches in diameter or larger used to transport oil, natural gas, artificial gas, water or coal slurry" to be deducted from the tax base. The issue has arisen as to whether the gross proceeds of sale or the gross income derived from the sale of pipes four inches or larger in diameter that transport sewage may be deducted under the Statutes.

In analyzing the Statutes, one must look at the specific purpose for which the four-inch pipe ("pipe") is being used. It is both the purpose for which the pipe is used and the substance being transported through the pipe that is at the heart of the deduction allowed by the Statutes.

For example, pipe used to transport water from a municipal water source to a factory qualifies for the deduction. The purpose of the pipe is to transport water. This is differentiated from a pipe used to transport sewage from a factory to a municipal sewage treatment plant. The purpose of the pipe is to transport sewage. Any water used in the transportation of the sewage is a medium of transportation; the pipe is not used for the purpose of transporting water. Income from the sale of pipe used for the purpose of transporting sewage is not deductible because the Statutes do not provide a deduction for the transportation of sewage. Thus, the gross proceeds of sales or the gross income derived from the sale of pipes four inches or larger in diameter that transport sewage may not be deducted under the Statutes.

This same reasoning can be seen by applying the Statutes' exemption for coal slurry. The Statutes specifically exempt coal slurry, which is a mixture of water and coal mining by-products. Coal slurry is similar to sewage in that both substances are mixtures of water, solid and semi-solid compounds. The Legislature specifically exempted coal slurry while remaining silent on other mixtures of water and solid or semi-solid compounds. Thus, it can be determined that mixtures of water and other compounds, such as sewage, was not intended by the Legislature to be exempt. If the Legislature intended to exempt sewage, they would have listed such an exemption in the Statutes, as they did with coal slurry.

### Definition of the Term "Water"

In the alternative, it has been suggested that because the Statutes do not clearly define the terms "water" or "sewage", "sewage" could be considered under the definition of the term "water". Neither the terms "sewage" nor "water" are defined under the Statutes.

There are instances where other Arizona legal resources have defined the terms "sewage" and "water". These definitions, however, cannot be used to provide guidance as to the definition of the terms "sewage" and "water" under the Statutes. Arizona courts have held that definitions which pertain to statutes serving another purpose and having nothing to do with the subject of the statute in question

are not persuasive in interpreting the statute. Thus, in interpreting the definition of the terms "sewage" and "water" in the Statutes, using definitions found in sources outside of the Statutes will not be held persuasive by Arizona courts.

How then are the terms "sewage" and "water" to be defined? Unless the Legislature clearly expresses an intent to give a term a special meaning, Arizona courts will give the words used in statutes their plain and ordinary meaning. In determining the ordinary meaning of a term, Arizona courts will refer to an established and widely used dictionary.

*Webster's Third New International Dictionary* 2581 (3d ed. 1993) defines water as "an odorless, tasteless, very slightly compressible liquid oxide of hydrogen H<sub>2</sub>O which appears bluish in thick layers, freezes at 0° C and boils at 100° C." Sewage is defined by *Webster's Dictionary* as "refuse liquids or waste matter carried off by sewers." *Id.* It is clear from the above definitions that sewage cannot be considered water under the plain definition of the term "water".

## RULING:

Pipes or valves four inches in diameter or larger used to transport sewage will not qualify for a deduction under the Statutes.

The following is a non-exhaustive list of examples of 4" or larger pipe and the taxability of the gross proceeds from sales or purchases of the pipe under A.R.S. §§ 42-5061(B)(6) or 42-5159(B)(6):

<u>Pipe Use</u>	<u>Taxability</u>
• Storm water drainage system flowing to retention basins, waterbeds or washes	Not Taxable
• Irrigation system	Not Taxable
• Transporting from water reclamation/treatment facility to irrigation system	Not Taxable
• Transporting from water reclamation/treatment facility to retention location, recharging facility	Not Taxable

• Potable water distribution system for residential and business customers	Not Taxable
• Sewage, waste or sanitary collection systems for residences, businesses or commercial enterprises	Taxable

Mark W. Killian, Director

Signed: June 12, 2002

#### Explanatory Notice

The purpose of a tax ruling is to provide interpretive guidance to the general public and to department personnel. A tax ruling is intended to encompass issues of law that are not adequately covered in statute, case law or administrative rules. A tax ruling is a position statement that provides interpretation, detail, or supplementary information concerning application of the law. Relevant statute, case law, or administrative rules, as well as a subsequent ruling, may modify or negate any or all of the provisions of any tax ruling. See GTP 96-1 for more detailed information regarding documents issued by the Department of Revenue.