BEFORE THE ARIZONA DEPARTMENT OF REVENUE

In the Matter of	)	**DECISION OF HEARING OFFICER**
[REDACTED]	)	
I.D. #[REDACTED]	)	**Case No. 200800192-C**

[REDACTED] (Taxpayer) requested that this matter be resolved through the submission of written memoranda. Taxpayer and the Corporate Audit Section (Section) of the Arizona Department of Revenue (Department) timely filed their Joint Listing of Facts on May 8, 2009. Taxpayer's Opening Memorandum was timely filed on June 8, 2009. The Section timely filed its Response Memorandum on August 7, 2009. Taxpayer's Reply Memorandum was timely filed on September 8, 2009. Therefore, this matter is ready for ruling.

FINDINGS OF FACT

The evidence and the parties' Joint Listing of Facts establish the following. Taxpayer is a subsidiary of a corporation that is a [REDACTED] in providing business services [REDACTED]. On or about December 7, 2001 Taxpayer submitted amended Arizona corporate income tax returns for tax years ending December 31, 1997, December 31, 1998 and December 31, 1999 ("1997," "1998" and "1999" respectively) claiming enterprise zone credits. Taxpayer's amended returns resulted in refund requests of $[REDACTED] for 1997, $[REDACTED] for 1998 and $[REDACTED] for 1999.

On or about September 9, 2003 the Section issued a partial refund denial which resulted in additional tax due of $[REDACTED], exclusive of interest. The refund denial totaled $[REDACTED] as follows: $[REDACTED] for 1997, $[REDACTED] for 1998 and $[REDACTED] for 1999. According to the Section's Response Memorandum, the partial denial of the credit was for second- and third-year employment positions that exceeded the number allowed in the first year of employment. Taxpayer timely protested. The issue to be decided is the propriety of the Section's partial refund denial. The resolution of this issue depends on the proper interpretation of A.R.S. § 43-1161.

For tax year ending October 31, 1997 ("1996"), Taxpayer reported hiring 49 employees into qualified employment positions, 8 of whom lived within the enterprise zone on the date of hire, and that Taxpayer had a net increase in qualified employment positions of 53. Taxpayer claimed, and the Section allowed, 22 (22 x 35% = 8 residents) first-year qualified employment positions toward the enterprise zone credit or $11,000.

For 1996, Taxpayer claimed 10 employees toward the second-year portion of the pre-December 31, 1996 Enterprise Zone Credit for Qualified Employees and Dislocated Workers.

For 1997, Taxpayer reported hiring 23 employees into qualified employment positions, 2 of whom lived within the enterprise zone on the date of hire, and that Taxpayer had a net increase in qualified employment positions of 26. Taxpayer claimed, and the Section allowed, 5 (5 x 35% = 2 residents)

first-year qualified employment positions toward the enterprise zone credit or $2,500.

For 1997, Taxpayer claimed 43 employees toward the second-year portion of the 1996 enterprise zone credit. The Section allowed 22 employees. This determination resulted in the Section denying 21 employees and a refund denial of $20,346.

For 1997, Taxpayer claimed, and the Section allowed, 8 employees toward the third-year portion of the pre-1996 enterprise zone credit.

For 1998, Taxpayer reported hiring 78 employees into qualified employment positions, 7 of whom lived within the enterprise zone on the date of hire, and that Taxpayer had a net increase in qualified employment positions of 18. Taxpayer claimed, and the Section allowed, 18 first-year qualified employment positions toward enterprise zone credits or $9,000.

For 1998, Taxpayer claimed 23 employees toward the second-year portion of the 1997 enterprise zone credit. The Section allowed 5 employees. This determination resulted in the Section denying 18 employees and a refund denial of $18,000.

For 1998, Taxpayer claimed 43 employees toward the third-year portion of the 1996 enterprise zone credit. The Section allowed 22 employees. This determination resulted in the Section denying 21 employees and a refund denial of $30,643.

For 1999, Taxpayer reported hiring 21 employees into qualified employment positions, 8 of whom lived within the enterprise zone on the date of hire, and that Taxpayer had a net increase in qualified employment positions of 21. Taxpayer

claimed, and the Section allowed, 21 first-year qualified employment positions toward enterprise zone credits or $10,500.

For 1999, Taxpayer claimed 54 employees toward the second-year portion of the 1998 enterprise zone credit. The Section allowed 18 employees. This determination resulted in the Section denying 36 employees and a refund denial of $36,000.

For 1999, Taxpayer claimed 15 employees toward the third-year portion of the 1997 enterprise zone credit. The Section allowed 5 employees. This determination resulted in the Section denying 10 employees and a refund denial of $15,000.

As previously noted, the issue to be decided is the propriety of the Section's partial refund denial.

DISCUSSION-THE PARTIES' POSITIONS

In its memoranda, Taxpayer asserts that the Hearing Office should order the Department to grant the remainder of the credits it claimed because: 1) under the plain language of the 1996 amendments to the enterprise zone credit statute, the 35% residency limitation only applies in the first year, 2) the 2002 amendment to the enterprise zone credit statute applied the 35% limitation to second- and third-year employees, but it was not effective until after the tax years involved here, and it would be inappropriate to incorporate into the 1996 credit statute amendments that did not take effect until 2002 and 3) the Department's denial of the remainder of the enterprise zone credits that Taxpayer claimed violates Taxpayer's right to equal protection under the law because the Department would be singling out Taxpayer for selective enforcement.

In its Opening Memorandum, Taxpayer asserts that there are three alternative methods to calculate the enterprise zone credit under various interpretations of the 1996 amendments to the enterprise zone credit statutes. Taxpayer labels the first method as the "Forms Method." Taxpayer asserts that the Forms Method involves a calculation consistent with the pre-1996 statutory language, allowing an enterprise zone credit in year one of the program only for first-year employees and imposing a cap on the number of employees in years two and three that could be claimed based on the specific number of employees who qualified under the 35% residency limitation in year one. Taxpayer states that in the present case, the Department is arguing that the 35% residency issue should be resolved using the Forms Method of calculating the enterprise zone credit, which would result in upholding the Section's partial refund denial.

Taxpayer labels the second method as the "Statutory Method." Taxpayer states that the Statutory Method allows an enterprise zone credit in year one of the program for first-, second- and third-year employees without regard to the 35% residency limitation for second- and third-year employees. Taxpayer states that this is the method that [REDACTED] believed was justified by the 1996 amendments to the enterprise zone credit statutes and states that this method would result in the maximum amount of credits to Taxpayer. However, Taxpayer states that it is merely pursuing the calculation of its enterprise

zone credit under the third method, which Taxpayer labels the "Compromise Method."

Taxpayer states that the Compromise Method reflects an effort by [REDACTED] to provide a middle-ground calculation of the enterprise zone credit. The Compromise Method does not allow an enterprise zone credit in year one of the program for second- and third-year employees. Taxpayer states that the Compromise Method does allow an enterprise zone credit for all qualified employees in years two and three of the program because, Taxpayer asserts, the 35% residency limitation only applies to year one. Taxpayer states that this is the method that [REDACTED] began using instead of the Statutory Method after the Department approved refund claims for some of [REDACTED]'s clients using this method of calculating the enterprise zone credit. Taxpayer asserts that the Department should use this method to calculate the enterprise zone credit in this case also, which would result in Taxpayer receiving the additional credits it has claimed.

In its Response Memorandum, the Section first asserts that the enterprise zone credit is a single credit paid over a three-year period. The Section argues that the enterprise zone credit is established in the first year and that the number of qualified positions/employees cannot increase with the subsequent installment payments. The Section asserts that the credit is allowed for employees in their second and third year of continuous employment only because those positions were allowed in their first year. The Section further asserts that

any other interpretation violates the credit's purpose of providing better employment for enterprise zone residents. Second, the Section states that it is not attempting to apply the 2002 statutory change to years before 2002. The Section asserts that the portion of the 2002 amendment cited by Taxpayer relates to the change requiring that all credits be claimed on original tax returns and that current law no longer allows taxpayers to file for the credit on an amended return. The Section continues to state that if in fact the Section were attempting to apply the 2002 amendment to the years at issue, the Section would have denied the entire credit because it was claimed on amended returns. Finally, the Section argues that its position does not violate Taxpayer's right to equal protection. The Section asserts that in reality the Department would be violating other taxpayers' rights to equal protection if it granted Taxpayer a refund based on the Compromise Method because no other identically classified taxpayer was ultimately allowed the enterprise zone credit based on the Compromise Method. The Section states that there were no claims ultimately paid under the Compromise Method where the Department did not pursue all legal action available to recover the erroneous refund. The Section further states that Taxpayer is seeking relief that would result in selective enforcement because Taxpayer wants to use the Compromise Method that was not granted to other taxpayers.

CONCLUSIONS OF LAW

Laws 1987, Ch. 361 established the enterprise zone program for the purpose of encouraging new business start-ups and business expansion in certain targeted areas in Arizona. The legislation specified qualifying criteria and procedures for establishing enterprise zones in the targeted areas and created incentives for businesses, including an income tax credit. A.R.S. § 43-1161 provides the Arizona corporate income tax credit for increased employment in enterprise zones. A.R.S. § 43-1161 has been amended several times since 1987.

The dispute in this case arises from the interpretation of the 1996 amendments to A.R.S. § 43-1161. Taxpayer argues that under the plain language of the 1996 amendments to the enterprise zone credit statute, the 35% residency limitation only applies in the first year. Taxpayer argues that from the time the enterprise zone credit statute was amended in 1996 until tax year 2002, the statute specifically provided that the 35% residency limitation only applied in the <u>first year</u> of employment, employees were no longer required to be "previously qualified" in their second and third years of employment and, by this time, the focus of the enterprise zone credit statute had changed from qualifying employees to qualifying employment positions.

In Laws 1996, Ch. 344 (H.B. 2496), the Arizona Legislature made several changes to the Arizona enterprise zone credit statutes effective retroactively to taxable years beginning from and after December 31, 1995. Taxpayer focuses on the changes made by H.B. 2496 to A.R.S. § 43-1161.A and B. Prior to these

changes, A.R.S. § 43-1161.A stated in part that a credit is allowed "for net increases in employment of qualified employees by a business located in an enterprise zone . . ." (Emphasis added.) H.B. 2496 amended A.R.S. § 43-1161.A to allow a credit "for net increases in qualified employment positions of residents of this state by a business located in an enterprise zone . . ." (Emphasis added.) Prior to H.B. 2496, A.R.S. § 43-1161.A.2 provided that the amount of the credit is equal to "[o]ne-third of the taxable wages paid to each previously qualified employee, not to exceed one thousand five hundred dollars per net new employee, in the second year of continuous employment." (Emphasis added.) H.B. 2496 amended A.R.S. § 43-1161.A.2 to provide that the amount of the credit is equal to "[o]ne-third of the taxable wages paid to an employee in a qualified employment position, not to exceed one thousand dollars per qualified employment position, in the second year of continuous employment." (Emphasis added.) Prior to H.B. 2496, A.R.S. § 43-1161.A.3 provided that the amount of the credit is equal to "[o]ne-half of the taxable wages paid to each previously qualified employee, not to exceed two thousand five hundred dollars per net new employee, in the third year of continuous employment." (Emphasis added.) H.B. 2496 amended A.R.S. § 43-1161.A.3 to provide that the amount of the credit is equal to "[o]ne-half of the taxable wages paid to an employee in a qualified employment position, not to exceed one thousand five hundred dollars per qualified employment position, in the third year of continuous employment." (Emphasis added.) H.B. 2496

added A.R.S. § 43-1161.B.2 which provides that in order to qualify for the credit:

> **Thirty-five per cent of the employees with respect to whom a credit is claimed for the first year of employment must reside in an enterprise zone that is located in the same county in which the business is located on the date of hire. (Emphasis added.)**

Taxpayer asserts that the 2002 amendment to the enterprise zone credit statute changed the law to apply the 35% limitation to second- and third-year employees, but that amendment was not effective until after the years at issue. The amendment Taxpayer is referring to is set forth in Laws 2002, Ch. 237 (H.B. 2181). H.B. 2181 amended A.R.S. § 43-1161.D to read:

> **A credit is allowed for employment in the second and third year only for qualified employment positions for which a credit was allowed and claimed by the taxpayer on the original first and second year tax returns.**

Laws 2002, Ch. 237, § 15 provides that "[t]his act applies retroactively to taxable years beginning from and after December 31, 2001."

Taxpayer points out that the 1996 amendments to A.R.S. § 43-1161 changed the language of that statute by deleting the phrase "each previously qualified" from subsections A.2 and A.3. Taxpayer argues that by deleting this language, it is clear that the Arizona Legislature intended to eliminate the requirement in years two and three that employees be previously qualified for the credit. Taxpayer argues that the Arizona Legislature further clarified its intent in 1996 when it added A.R.S. § 43-1161.B.2, as noted above. Taxpayer further argues that

because the Arizona Legislature did not amend the enterprise zone credit statute to prevent taxpayers from calculating the credit using the Statutory or Compromise Methods until 2002, taxpayers clearly were entitled to calculate the credit using the Statutory or Compromise Methods prior to 2002. Taxpayer states that rather than requesting a larger refund under the Statutory Method, in this case Taxpayer is only asking the Department to calculate the enterprise zone credit using the Compromise Method, as, Taxpayer asserts, the Department already did for several other taxpayers.

As previously noted, the Section asserts that the enterprise zone credit is a single credit paid over a three-year period. The Section argues that the enterprise zone credit is established in the first year and that the number of qualified positions/employees cannot increase with the subsequent installment payments. The Section asserts that the credit is allowed for employees in their second and third year of continuous employment only because those positions were allowed in their first year.

In support of its position, the Section cites *In re Microage Corporation*, 305 B.R. 328 (Bankr. D. Ariz. 2004), which is a memorandum decision issued by the United States Bankruptcy Court for the District of Arizona. The Section states in its Response Memorandum that although this case is not binding on the Hearing Office, it gives guidance and is persuasive.

Taxpayer, however, asserts that *Microage* is not applicable because it involves a different issue and different facts and

legal arguments. Taxpayer points out that *Microage* is a memorandum decision issued by a federal Bankruptcy Court. Taxpayer strongly argues that memorandum decisions are not intended for publication in the first place, are not regarded as precedent and are not to be cited in any court, except in certain circumstances that are not applicable here. In support of its argument, Taxpayer relies on Rule 28 of the Arizona Rules of Civil Appellate Procedure, Rule 111 of the Rules of the Supreme Court of Arizona, State Bar of Arizona Ethics Opinion No. 78-4 (January 30, 1978) and *Walden Books Company v. Arizona Department of Revenue*, 198 Ariz. 584, 12 P.3d 809 (App. 2000). Taxpayer asserts that it was inappropriate for the Section to cite *Microage* and that it would be illogical and unethical to render a decision in reliance on it.

Rule 28(c) of the Arizona Rules of Civil Appellate Procedure and Rule 111(c) of the Rules of the Supreme Court of Arizona provide that memorandum decisions shall not be regarded as precedent nor cited in any court, except in certain circumstances that are not applicable here. Rule 28(a)(2) of the Arizona Rules of Civil Appellate Procedure and Rule 111(a)(2) of the Rules of the Supreme Court of Arizona define a memorandum decision to be "a written disposition of a matter not intended for publication."

In *Walden Books*, the taxpayer relied on an unpublished Tennessee memorandum decision. The Court noted in *Walden Books* that Rule 28 of the Arizona Rules of Civil Appellate Procedure makes it improper to cite unpublished decisions as authority.

The Court found no reason for out-of-state memorandum decisions to be more citable than in-state memorandum decisions and then held that Rule 28 of the Arizona Rules of Civil Appellate Procedure applies to memorandum decisions from any court.

In light of the foregoing, the key to whether *Microage* may be regarded as precedent, or even be cited, in this proceeding is whether *Microage* constitutes a memorandum decision within the meaning of Rule 28 and Rule 111. Since Taxpayer objects to the Section citing a Bankruptcy Court memorandum decision, it is necessary to review the rules and practice of various courts regarding Bankruptcy Court memorandum decisions.

At the outset, it is critical to note that *Microage* is reported and published in West's Bankruptcy Reporter at 305 B.R. 328 (2004). *Microage* is also cited in West Publishing Co.'s Arizona Revised Statutes, Annotated at A.R.S. §§ 41-1525 and 43-1161 under "Notes of Decisions."

A review of the Federal Rules of Bankruptcy Procedure and the Local Rules of Bankruptcy Procedure for the District of Arizona does not reveal specific rules regarding publication of Bankruptcy Court orders or decisions, the relevance, if any, of designating Bankruptcy Court orders or decisions as "memorandum" or any prohibition against citing Bankruptcy Court memorandum orders or decisions. However, an Internet search of unpublished Bankruptcy Court memorandum orders and decisions reveals that they are marked "Not for Publication" or "Do Not Publish." The Bankruptcy Court memorandum decision in *Microage* is not so marked and is in fact published at 305 B.R. 328 (2004).

Rule 8013-1(c) of the Rules of the United States Bankruptcy Appellate Panel of the Ninth Circuit provides that unpublished memoranda and orders have no precedential value and may not be cited, except under narrow circumstances not applicable here. In *In re Wade Cook Financial Corp.*, 375 B.R. 580 (9th Cir. BAP 2007), the United States Bankruptcy Appellate Panel of the Ninth Circuit cites *In re Microage Corporation*, 288 B.R. 842 (Bankr. D. Ariz. 2003), which is an earlier decision issued by the United States Bankruptcy Court for the District of Arizona concerning the same bankruptcy case addressed by that Court in *In re Microage Corporation*, 305 B.R. 328 (2004), the decision that Taxpayer strongly objects to being cited in the present case. Like the 2004 *Microage* decision, the 2003 *Microage* decision is a memorandum decision and is reported in West's Bankruptcy Reporter. Like the 2004 *Microage* decision, the 2003 *Microage* decision is not marked "Not for Publication" or "Do Not Publish." Clearly, Rule 8013-1(c) of the Rules of the United States Bankruptcy Appellate Panel of the Ninth Circuit does not consider this to be an unpublished memorandum decision because the Court cited the 2003 *Microage* decision in *In re Wade Cook Financial Corp.*, even though that 2003 *Microage* decision is a memorandum decision. Likewise, in *In re Costas*, 346 B.R. 198 (9th Cir. BAP 2006), the United States Bankruptcy Appellate Panel of the Ninth Circuit cites, and relies on, *In re Faulk*, 281 B.R. 15 (2002), even though *Faulk* is a memorandum opinion.

The United States Court of Appeals, Ninth Circuit, cites Bankruptcy Court memorandum decisions. In *Biltmore Associates,*

LLC v. Twin City Fire Insurance Company, **572 F.3d 663 (9th Cir. 2009), the Court, in Footnote 17, cites *Terry v. Federal Insurance Co. (In re R.J. Reynolds-Patrick County Memorial Hospital, Inc.)*, 315 B.R. 674 (2003), which is a Bankruptcy Court memorandum decision. It is important to note that *Terry v. Federal Insurance Co.* was issued by the Bankruptcy Court before January 1, 2007. *See* Rules of the United States Court of Appeals for the Ninth Circuit, Rule 36.**

As previously noted, Rule 28(a)(2) of the Arizona Rules of Civil Appellate Procedure and Rule 111(a)(2) of the Rules of the Supreme Court of Arizona define a memorandum decision to be "a written disposition of a matter not intended for publication." The foregoing review reveals that Bankruptcy Court memorandum decisions are published unless the particular Bankruptcy Court indicates that a decision is not to be published. There is no indication that the Bankruptcy Court in *In re Microage Corporation*, 305 B.R. 328 (2004) did not intend that decision to be published. That decision was in fact published. Clearly, this Bankruptcy Court decision does not fall within the definition of a "memorandum decision" within the meaning of Rule 28(a)(2) of the Arizona Rules of Civil Appellate Procedure and Rule 111(a)(2) of the Rules of the Supreme Court of Arizona because it is a published decision. Therefore, *Microage* may be cited in this proceeding.

In *In re Microage Corporation*, 305 B.R. 328 (2004), the Bankruptcy Court addressed the debtor-employer's entitlement to the Arizona enterprise zone credit for its second- and third-

year employees. The first year for which the debtor-employer sought any Arizona enterprise zone credit was for tax year 1996. The Court held that, under Arizona law, the debtor-employer was not entitled to the Arizona enterprise zone credit for second- and third-year employees for whom no such credit was sought in their first year of employment. The Court noted in Footnote 1 of its decision that the real issue is whether an Arizona enterprise zone credit can be claimed for second- and third-year employees where the employer never certified that these employees met the 35% residency requirement. The Court noted the 1989 and 1996 amendments to the Arizona enterprise zone credit statutes. The Court stated that, according to the debtor, the 1996 legislation changed the focus from "qualified employees" to "qualified employment positions." This is one of Taxpayer's arguments in the present case. In rejecting the debtor's position, the Court stated that this reading ignores the fundamental purpose of the Arizona enterprise zone credit and the clear certification requirements that have been in place statutorily since 1987. The Court stated further:

> **It is apparent from reviewing the various legislative incarnations that the legislature created a threshold residency requirement for employers that must be met before an employer can even be considered eligible for an income tax credit. Once the employer makes such a certification, the analysis turns to calculating the number of credits to which the employer is entitled and the amount of the credits. Those amounts are then paid out over a three year period. However, the payment of the credit in years two and three is inextricably**

linked to the award of the first year credit based on satisfaction of the various statutory requirements. Nothing in the statutes' transformation over the years indicates that the decision to pay the credit out over time was meant to be [sic] change the singular character of the credit. As the ADOR argued at the hearing, an employer is awarded "*a* credit" up to $3,000 payable over three years. The amount of the credit paid in years two and three depends on the amount of the employee's taxable wages and the $3,000 limit. The statute does not provide three different credits for first, second and third year employees: It is one credit essentially paid out on an installment plan.

To read the statute as Debtor urges would in effect create a third method by which an employer could claim a tax credit: An employer could claim a tax credit for an employee in a qualified employment position in his or her second or third year of employment without any threshold residency certification by the employer for that employee's first year of employment. That goes against the fundamental reason for the statute's residency certification requirement-to encourage the hiring of individuals from within the enterprise zone. Debtor's reading also ignores the fact that payment of the credit in years two and three only results because the employer was entitled to the credit in year one.

. . . There is no need for the third category Debtor urges. Such an application would result in a windfall to employers who now, in the first year under the 1996 amendment, would be able to start claiming positions/employees who were not previously allowed to be claimed, for whatever reason, and as to which there was no previous thirty-five percent certification. This makes little sense in light of the purpose of the credit and the statute's history. (Emphasis in original.) 305 B.R. at 332-333.

Contrary to Taxpayer's assertions, the issue in *Microage* is strikingly similar to the issue in the present case. Although not binding, the Bankruptcy Court's decision is instructive and persuasive in the present case. That decision clearly rejects Taxpayer's arguments and clearly supports the Section's position. In light of the reasoning in *Microage,* Taxpayer's arguments must be rejected and it must be concluded that the Section properly applied A.R.S. § 43-1161 in denying a portion of Taxpayer's refund requests.

In light of the foregoing, Taxpayer's argument regarding the 2002 amendment to the enterprise zone credit statutes, specifically the change in the language to A.R.S. § 43-1161.D which was effective for tax years after 2001, is not relevant to the resolution of the issue in the present case.

In its Reply Memorandum, Taxpayer suggests that the Arizona enterprise zone credit statutes should be broadly construed. However, it is well settled that credits are a matter of legislative grace and not a matter of taxpayer right. As such, credits must be strictly construed against the taxpayer and in favor of the taxing authority. *Keyes v. Chambers*, 209 Or. 640, 307 P.2d 498 (1957). Tax statutes are construed strictly against a party who claims a credit. *Davis v. Arizona Department of Revenue,* 197 Ariz. 527, 4 P.3d 1070 (App. 2000).

Taxpayer argues that applying the 35% residency limitation to Taxpayer's second- and third-year credit claims violates Taxpayer's right to equal protection guaranteed by the Fourteenth Amendment to the U.S. Constitution and by Article 2,

§ 13 of the Arizona Constitution. Taxpayer asserts that the Department is singling out Taxpayer for selective enforcement. Taxpayer cites *Gosnell Development Corporation v. Arizona Department of Revenue,* 154 Ariz. 539, 744 P.2d 451 (App. 1987) for the principles that under Arizona and federal law, taxing authorities that treat taxpayers in the same class differently violate their rights to equal protection under the law and that taxing authorities may not single out taxpayers for selective enforcement of tax laws which apply to all similarly situated taxpayers equally. Taxpayer argues that in the present case, as in *Gosnell*, the Department is impermissibly treating taxpayers in the same class differently. Taxpayer asserts that the Department calculated Taxpayer's enterprise zone credits for the years at issue by applying the 35% residency limitation in years two and three, consistent with the Forms Method of calculating the credit, rather than by using the Compromise Method, which does not impose the 35% residency limitation in years two and three, like the Department knowingly used for other taxpayers. Taxpayer also points out that the Arizona Court of Appeals, in *Brink Electric Construction Company v. Arizona Department of Revenue*, 184 Ariz. 354, 363, 909 P.2d 421, 430 (App. 1995) explained that the "purpose of the equal protection clause is to prevent the government from intentionally and arbitrarily discriminating against its citizens." Taxpayer argues that this is precisely what the Department is doing in the present case and is another reason why Taxpayer should be granted the remainder of the credits it claimed.

In support of its equal protection argument, Taxpayer relies on the contents of Taxpayer's Exhibit 3. Taxpayer's Exhibit 3 consists chiefly of portions of deposition testimony, exhibits and affidavits obtained in the course of litigation in *Arizona State Department of Revenue v. America West Holdings Corporation*, Arizona Tax Court Case No. TX 2004-000480. *America West Holdings* involved the enterprise zone credit claim of America West and involved issues similar to those in the present case. Apparently, *America West Holdings* was settled by the parties before the Arizona Tax Court ever issued a decision in that case.

Taxpayer asserts that the following facts are established through Taxpayer's Exhibit 3. The following summary of Taxpayer's assertions is in no way to be construed as findings of fact by this Hearing Officer. At some point in time, the Department's audit program allowed taxpayers to calculate the enterprise zone credit using the Compromise Method. The Department used the Compromise Method to calculate refunds for at least four [REDACTED] clients. Several taxpayers and their representative thought they had reached a compromise with the Department under which the enterprise zone credit would be calculated using the Compromise Method. The Department's allowance of enterprise zone credits for other taxpayers using the Compromise Method occurred after an extended series of meetings and discussions which included senior Department officials, officials from the Arizona Department of Commerce and representatives from the Governor's Office.

The Section asserts that in reality the Department would be violating other taxpayers' rights to equal protection if it granted Taxpayer a refund based on the Compromise Method because no other identically classified taxpayer was ultimately allowed the enterprise zone credit based on the Compromise Method. The Section states that there were no claims ultimately paid under the Compromise Method where the Department did not pursue all legal action available to recover the erroneous refund. The Section further states that Taxpayer is seeking relief that would result in selective enforcement because Taxpayer wants to use the Compromise Method that was not granted to other taxpayers.

In *Brink*, the Court held that the Department did not violate the taxpayers' equal protection rights. The Court noted that the good faith of government officers and the validity of their actions are presumed, and when they are assailed, the burden of proof is on the complaining party. The Court also noted in *Brink* that mere errors of judgment by government officials do not rise to the level of discrimination.

The evidence in the present case indicates that any refunds granted by the Department based on the Compromise Method were mere errors of judgment on the part of the Department. The Section has indicated that the Department pursued all legal action available to recover such erroneous refunds. As the Court noted in *Brink*, mere errors of judgment by government officials do not rise to the level of discrimination. Additionally, the Court noted in *Brink* that when the presumed

good faith of government officers and the presumed validity of their actions are assailed, the burden of proof is on the complaining party. Taxpayer has not satisfied its burden of proof to establish that the Department has violated its right to equal protection.

A refund denial, like an additional assessment of income tax, is presumed correct and the burden is on the taxpayer to overcome such presumption. *See Arizona State Tax Commission v. Kieckhefer,* 67 Ariz. 102, 191 P.2d 729 (1948). Taxpayer has failed to show that the Section's partial refund denial was improper.

Based on the foregoing, the Section properly denied a portion of Taxpayer's requests for refund. Therefore, Taxpayer's protest is denied.

DATED this 16th day of October, 2009.

ARIZONA DEPARTMENT OF REVENUE
HEARING OFFICE

[REDACTED]
Hearing Officer

Original of the foregoing sent by certified mail to:

[REDACTED]

Copy of the foregoing delivered to:

Arizona Department of Revenue
Corporate Audit Section