

BEFORE THE ARIZONA DEPARTMENT OF REVENUE

In the Matter of	)	DECISION OF
	)	HEARING OFFICER
[REDACTED]	)	
	)	Case No. 201000170-O
UTI # [REDACTED]	)	
_____	)	

A hearing was held on September 28, 2010 in the matter of the protest of [REDACTED] and [REDACTED] (Taxpayers) to an assessment of income tax and interest by the Individual Income Tax Audit Section (Section) of the Arizona Department of Revenue (Department) for tax year 2005.

This matter is now ready for ruling.

FINDINGS OF FACT

1. Taxpayers timely filed their Arizona income tax return for tax year 2005.
2. Taxpayers claimed an income tax credit pursuant to Arizona Revised Statutes (A.R.S.) § 43-1086 in the amount of \$[REDACTED].
3. Taxpayers' Arizona income tax liability for tax year 2005 was \$[REDACTED] before applying the credit under A.R.S. § 43-1086.
4. The credit was based on Taxpayers' purchase of a neighborhood electric vehicle (NEV) in tax year 2000 from [REDACTED].
5. [REDACTED] was located in [REDACTED], Arizona.
6. Taxpayers' purchase order for the NEV was dated March 27, 2000.
7. The invoice for the NEV was dated June 6, 2000.
8. The total purchase price of the NEV was \$[REDACTED].
9. Taxpayers paid the full purchase price of the NEV by check dated June 15, 2000.
10. The check was deposited by [REDACTED] and was posted on June 19, 2000.
11. The dealer pre-delivery checklist was dated June 21, 2000.

12. The NEV was delivered to the dealer on June 22, 2000.
13. The Title and Registration Application was completed in June of 2000.
14. The NEV existed prior to June 30, 2000.
15. The NEV was stored at the dealer until Taxpayers took possession of the NEV on August 10, 2000.
16. Taxpayers were part-year residents during tax year 2000.
17. Taxpayers were residents of [REDACTED] on and before June 30, 2000.
18. Taxpayers became Arizona residents in July of 2000.
19. Taxpayers registered and used the NEV in Arizona.
20. Taxpayers took a credit under A.R.S. § 43-1086 for tax year 2000 in the amount of \$[REDACTED].
21. During tax years 2000 through 2004 Taxpayers took credits under A.R.S. § 43-1086 in the total amount of \$[REDACTED].
22. The Section reviewed Taxpayers' 2005 return and issued a proposed assessment dated October 15, 2009 disallowing Taxpayers' claimed credit of \$[REDACTED] and allowing a credit in the amount of \$[REDACTED].
23. The assessment included interest but no penalties.
24. The Section's position in the assessment was that Taxpayers were only allowed a maximum credit of fifty percent of the purchase price of the NEV.
25. Because of the credits taken in prior years, it was the Section's position that the maximum credit Taxpayers could take in tax year 2005 was \$[REDACTED].
26. Taxpayers timely protested the assessment.
27. It was Taxpayers' position that they purchased the NEV before June 30, 2000 and were therefore not limited to a maximum credit of fifty percent of the purchase price.
28. The Section also argued that Taxpayers would be entitled to no credit if they purchased the NEV while they were non-residents of Arizona.

## CONCLUSIONS OF LAW

1. For tax year 2000, Arizona taxpayers could take a credit for the purchase of a NEV for use in Arizona. A.R.S. § 43-1086(A) and (P)(2)(b).<sup>1</sup>
2. Taxpayers purchased and registered the NEV in Arizona for use in Arizona.
3. A.R.S. § 43-1086(B)(13) provided that notwithstanding any other paragraph of subsection (B), the maximum allowable credit for a new NEV that is purchased on or after July 1, 2000 is fifty per cent of the cost of the vehicle or one thousand dollars, whichever is more.
4. For a new NEV purchased before July 1, 2000, the maximum allowable credit was one hundred percent of the cost of the vehicle. A.R.S. § 43-1086(B)(5) and (M).
5. If the allowable credit exceeds the taxes otherwise due on a return, the credit not used to offset Arizona income taxes may be carried forward to the next five consecutive taxable years as a credit against subsequent years' income tax liability. A.R.S. § 43-1086(G)(2).
6. The last year to which Taxpayers could carry forward unused credits under A.R.S. § 43-1086 was tax year 2005. A.R.S. § 43-1086(G)(2).
7. The deductions and credits provided for in title 43, A.R.S., are to be taken for the taxable year in which "paid or accrued" or "paid or incurred", dependent upon the method of accounting upon the basis of which the taxable income is computed. A.R.S. § 43-905.
8. In determining the meaning of a word in a statute, the cardinal principle of statutory construction is to follow the plain and ordinary meaning of the word. *Dearing v. Arizona Dep't of Economic Security*, 121 Ariz. 203, 589 P.2d 446

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<sup>1</sup> Statutory references are to A.R.S. § 43-1086 as amended by Laws 2001, Ch. 179, Sec. 2, retroactive to taxable years beginning from and after December 31, 1999.

(App. 1978); State Tax Comm'n v. Peck, 106 Ariz. 394, 476 P.2d 849 (1970); A.R.S. § 1-213.

9. Taxpayers were subject to Arizona income tax for tax year 2000.
10. Taxpayers had an income tax liability to Arizona for tax year 2000 before the application of any credits.
11. A taxpayer is any person subject to a tax imposed by title 43, A.R.S. A.R.S. § 43-104(23).
12. Taxpayers were taxpayers within the meaning of A.R.S. § 43-104 for tax year 2000.
13. During the tax year in which a taxpayer changes from a nonresident to a resident, Arizona taxable income includes all income and deductions earned in Arizona or derived from Arizona sources prior to the time the taxpayer became a resident of Arizona. A.R.S. § 43-1097(B)(2).
14. A deduction and a credit are similar in that they each reduce a taxpayer's tax liability, either by reducing the taxpayer's taxable income or by directly reducing his tax liability, based on the expenditure of monies for a specified purpose.
15. Taxpayers' credit for the purchase of the NEV was derived from Arizona sources prior to the time they became residents.
16. Taxpayers were entitled to the credit provided by A.R.S. § 43-1086 for purchasing a NEV before July 1, 2000.
17. Taxpayers were entitled to a carryover of their credit under A.R.S. § 43-1086 in the amount of \$[REDACTED] for tax year 2005.
18. The Section's disallowance of Taxpayers' credit of \$[REDACTED] was not proper.
19. The proposed assessment issued by the Section for tax year 2005 must be vacated.

## DISCUSSION

Taxpayers moved to Arizona from [REDACTED] in August of 2000. Before they were Arizona residents, Taxpayers purchased a NEV in Arizona in tax year 2000. The NEV was ordered, paid for and delivered to the dealer in Arizona prior to June 30, 2000. The NEV was stored at the dealer's business until Taxpayers took possession in August of 2000 when they moved to Arizona. Taxpayers thereafter used the NEV in Arizona. For tax year 2000, Taxpayers filed a part-year return and took a credit under A.R.S. § 43-1086 for the purchase of the NEV earlier in the year.

Taxpayers were not able to use the total credit in tax year 2000 but they were able to carry the credit forward to the next five years. The final year of the carry forward period was tax year 2005. For tax year 2005, Taxpayers offset their total tax liability of \$[REDACTED] to the state using the credit carried over from tax year 2000. In the end Taxpayers used a little more than one-half of the cost of the NEV as credits between 2000 and 2005.

For tax year 2000, A.R.S. § 43-1086 allowed a credit for the total cost of the NEV if it was purchased before July 1, 2000. For any NEV purchased on or after July 1, 2000, the allowable credit was fifty percent of the cost. The Section audited Taxpayers' 2005 tax return and limited Taxpayers' available credit to fifty percent of the NEV's cost. The Section reasoned that Taxpayers did not purchase the NEV until they took possession from the dealer in August of 2000. Therefore the total available credit was limited to fifty percent of the cost and the credit amount over fifty percent was disallowed.

The Section also argued that if Taxpayers did purchase the NEV before July 1, 2000, Taxpayers would have been entitled to no credit because they were not residents of Arizona at the time of purchase. The Section reasoned Taxpayers would not have been "taxpayers" within the meaning of A.R.S. § 43-1086.

Taxpayers protested arguing that they purchased the vehicle in June 2000 when they paid the full purchase price, the NEV was delivered to the dealer and the application for title and registration was completed. Taxpayers had made an arrangement with the dealer to store the NEV until Taxpayers were able to pick it up.

**Was the NEV purchased before July 1, 2000?**

The first issue is to determine when the NEV was purchased. A.R.S. § 43-1086(B)(13) does not define a “purchase” for purposes of paragraph (13). In determining what the Arizona Legislature intended by the word “purchase”, we look to the plain and ordinary meaning of the word. *Dearing v. Arizona Dep't of Economic Security, supra*; *State Tax Comm'n v. Peck, supra*; A.R.S. § 1-213. We find that a reasonable person would understand the plain and ordinary meaning of the word “purchase” would include payment in full for an item that was delivered to the selling dealer and was being held by the dealer as an accommodation to the purchaser. All this occurred prior to July 1, 2000. Therefore, Taxpayers purchased the NEV before July 1, 2000.

**May Taxpayers take the credit even though they were non-residents when they purchased the NEV?**

With respect to a NEV, A.R.S. § 43-1086 allows a credit against taxes imposed by Title 43 to each taxpayer who purchases or leases one or more new original equipment manufactured alternative fuel vehicles for use in Arizona. The term “taxpayer” is defined as any person subject to a tax imposed by title 43. By allowing the credit to a taxpayer who purchases a NEV, did the legislature intend to not allow the credit if the person was a nonresident at the time the NEV was purchased. We do not believe the legislature intended such a hyper-technical definition of the word taxpayer.

The statutes encouraging the purchase of alternative fuel vehicles were part of a broad tax and regulatory program to improve Arizona's air quality. *Baker v. Arizona Department of Revenue*, 209 Ariz. 561, 105 P.3d 1180 (App. 2005). The program to

improve Arizona's air quality is more dependent on where the NEV is used, not by the person who purchases and uses the NEV. Limiting the credit to persons who were residents, or had Arizona source income when they purchased the NEV would not further the intent of the program. In contrast, denying the credit to a person because the NEV was purchased before he became an Arizona resident and had Arizona source income, even though he became an Arizona resident in the year of purchase and used the NEV in Arizona, would tend to frustrate the purpose of the statutes.

Title 43 does not specifically discuss entitlement to credits in the context of changes in residency. However, when a taxpayer changes from a nonresident to a resident, A.R.S. § 43-1097 does address including in Arizona taxable income deductions earned in Arizona or derived from Arizona sources prior to the time the taxpayer became a resident. A.R.S. § 43-1042 allows a taxpayer to take the amount of itemized deductions allowable for the taxable year pursuant to the Internal Revenue Code. By allowing a nonresident to take deductions available to taxpayers for periods prior to becoming a resident, it is clear the legislature did not intend to limit the term "taxpayer" to residents or to those who had Arizona source income at the time the deduction was earned.

A credit is similar to a deduction in that they each reduce a taxpayer's tax liability, either by reducing the taxpayer's taxable income or by directly reducing his tax liability, based on the expenditure of monies for a specified purpose. Under the facts of this case, if A.R.S. § 43-1086 had provided a deduction for the purchase of a NEV instead of a credit, A.R.S. § 43-1097 would have allowed Taxpayers the deduction. There is no reason why the credit should be treated differently.

The Arizona income tax is based on a year period. While deductions and credits are to be taken in the year they were incurred, there is no provision dictating the order or the time at which deductions and credits must be incurred. Any available credit or

deduction incurred during the taxable year is available for use when a taxpayer files his return irrespective of when during the taxable year he earned income.

Based on the foregoing, the Taxpayers' protest of the Section's assessment dated October 15, 2009 is granted.

DATED this 18th day of November, 2010.

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  
Individual Income Tax Audit Section