ARIZONA TAX COURT

TX 2004-000593 01/05/2006

HONORABLE MARK W. ARMSTRONG

CLERK OF THE COURT
L. Slaughter
Deputy

FILED:_____

EMPIRE SOUTHWEST, LLC JAMES BUSBY

v.

ARIZONA DEPARTMENT OF REVENUE ELIZABETH S. HILL

UNDER ADVISEMENT RULING

This matter was taken under advisement after oral argument held November 15, 2005. The Court has considered the Defendant's Motion for Summary Judgment, Plaintiff's Cross-Motion for Summary Judgment and arguments of counsel.

I. THE ISSUE

The issue is whether or not Empire Southwest, LLC ("Empire") is entitled to a refund pursuant to a transaction privilege ("sales") tax exemption for sales and leases of electric-power generators. The operative statute provides a sales tax exemption for:

> Machinery, equipment or transmission lines used directly in producing or transmitting electrical power, but not including distribution. Transformers and control equipment used at transmission substation sites constitute equipment used in producing or transmitting electrical power.

See A.R.S. § 42-5061(B)(4). The Arizona Department of Revenue's ("Department's") administrative rule, A.A.C. R15-5-128 (the "Rule"), distinguishes between equipment used to transmit electrical power and equipment used to distribute electrical power based on a 34,500 volt threshold.

Empire argues that before it filed its refund claim, the Department had agreed that "engine generator sets" used "as an electric power source in institutions, hospitals, industrial commercial facilities, contractors job sites and utilities" are "exempt from the imposition of Arizona sales tax" regardless of the above stated threshold. However, the Department claims that this is not the case. The Department argues that the Rule does apply in this case and pursuant

to the Rule Empire was subject to sales tax on its proceeds from selling and leasing the subject electric-power generators because they are not capable of generating more than 34,500 volts of electricity. The Department also relies on the Legislative history of the operative statute.

II. FACTUAL BACKGROUND

Empire sells, leases and services equipment including diesel and gas powered electric-power generators. Most of the customers that purchase or lease generators from Empire are construction contractors, governmental entities or industrial companies, including utility companies, that use such electric-power generators to generate electricity.

On March 17, 2003, Empire requested a refund of transaction privilege tax in the amount of $666,008.15 for the period of February 1, 1999 through July 31, 2002 ("Refund Period") on sales and leases of electric-power generators. In June 2003, Empire modified its request for a current refund in the amount of $563,892.50, plus interest. On August 20, 2003, the Department denied Empire's refund request. Empire protested the Department's denial of its refund request.

A formal hearing was held on March 9, 2004, before the Office of Administrative Hearings. On July 8, 2004, the Administrative Law Judge issued a decision upholding the Department's denial of Empire's refund claim. Accordingly, Empire brought this action asking the Tax Court to determine that Empire is entitled to the refund that it requested along with its costs and attorneys fees.

III. ARGUMENTS OF THE PARTIES

- Arizona Department of Revenue's Arguments -

A. NO EXEMPTION WITHOUT EXPLICIT AUTHORITY.

A taxpayer may not claim an exemption without explicit authority. *See Weller v. City of Phoenix*, 39 Ariz. 148, 152, 4 P.2d 665, 667 (1931). Moreover, exemptions "must exist, if at all, within a specific statutory grant." *New Cornelia Co-op. Mercantile Co. v. Ariz. State Tax Comm'n*, 23 Ariz. App. 324, 327, 533 P.2d 84, 87 (1975).

Courts must strictly and narrowly construe a statute granting a tax exemption from taxation. *Kitchell Contractors, Inc. v. City of Phoenix*, 151 Ariz. 139, 144, 726 P.2d 236, 241 (App. 1986). A court cannot narrowly construe an exemption by interpreting the exemption's words broadly, expansively, or figuratively. *State ex rel. Ariz. Dep't of Revenue v. Capitol Castings, Inc.*, 193 Ariz. 89, 970 P.2d 443 (App. 1998).

1. The Sale And Lease Of Generators by Empire Is Not Exempt From Taxation Under Arizona Law.

Empire's business activities include the sale and rental of generators. The tax base for the retail and personal property rental classification is the gross proceeds of sales or gross income derived from the business. Arizona law presumes that all income is subject to tax. A.R.S. § 42-5023. Unless Empire explicitly establishes that its income falls within an exemption, all of its gross income is taxable.

Empire claims that it is entitled to an exemption pursuant to A.R.S. §§ 42-5061(B)(4) and 42-5071(B)(2)(b) for the sale and rental of its diesel and gas powered electric generators. The exemption, however, does not apply to the portable generators that Empire sells and rents. A.R.S. §§ 42-5061(B)(4) exempts sales of:

> Machinery, equipment or transmission lines used directly in producing or transmitting electrical power, but not including distribution. Transformers and control equipment used at transmission substation sites constitute equipment used in producing or transmitting electrical power.

A.R.S. § 42-5071(B)(2)(b) provides a comparable exemption for rentals of personal property which, if it had been purchased instead of rented, would have been exempt under A.R.S. § 42-5061(B)(4). While the above statutes exempt machinery and equipment that produce and transmit electrical power, they exclude machinery and equipment used for distribution.

A.A.C. R15-5-128 distinguishes between nontaxable production and transmission equipment versus taxable distribution equipment. The Rule states that machinery and equipment used to produce voltage up to and including 34,500 volts are part of a distribution system, and are therefore, subject to transaction privilege tax. A.A.C. R15-5-128(B)(1). None of the generators Empire sold or leased during the Refund period exceeded a capacity of 34,500 volts. By definition, the generators Empire sells and rents constitute machinery and equipment that are part of a distribution system and are subject to tax. They are expressly excluded from the statutory exemption.

2. The Legislative History Indicates The Legislature's Intent To Exempt Specific Machinery And Equipment Employed By Utilities.

Exemption of the generators sold and leased by Empire would be contrary to the statute's purpose as reflected by its Legislative history. The Legislative history of A.R.S. § 42-5061(B)(4) demonstrates that the intent of the statute is only to exempt machinery and equipment employed by utilities. The exemption set forth in A.R.S. § 42-5061(B)(4) dates back to 1968, when the Legislature added an exemption statute. 1968 Ariz. Sess. Laws, ch. 2. It sets forth various transaction privilege tax exemptions listed by business category, including manufacturing and processing, mining, telephone, electric power production and transmission, etc. *See* A.R.S. § 42-1312.01.

The initial draft of the statute included a provision that would later become the exemption at issue in this case. The draft dated June 29, 1967, provided:

> Electric Power Companies. Tangible personal property consisting of machinery and equipment used or consumed in the direct production of electrical power, including, but not limited to, generators, transformers and control equipment at the production site, but excluding dams and appurtenances thereto.

In July of 1967, an industry member of the Citizens Advisory Committee commented on the draft expressing his concern with using the term "electric power companies." Specifically, the letter stated:

> [T]his should apply to the production and sale of electricity by any organizations, such as the City of Mesa, the electrical districts, the Salt River Project Agricultural Improvement and Power District (all having status of municipalities) and the Arizona Power Authority (a body politic of the State of Arizona) and REA cooperatives. The word "companies" might be construed to be unduly restrictive.

In 1968, the following statute was enacted into law:

> Electric power production and transmission. Tangible personal property consisting of machinery, equipment or transmission lines used directly in the production or transmission of electrical power, but not including distribution and, in addition, transformers and control equipment used at transmission substation sites.

The title "electric power production and transmission" was used to include municipalities and other providers of electricity. It was not the intent of the Legislature to expand the exemption to vendors of small electric power sources such as the generators at issue in this case.

Finally, in 1988, the provision was rephrased in a recodification that resulted in the current text of A.R.S.§ 42-5061(B)(4). Ch. 161, HB 2001, 38th Leg., 2nd Reg. Sess. This rephrasing and reorganization was not a substantive change.

The history of the exemption illustrates that the Legislative intent was to exempt machinery and equipment that various businesses employed. A.R.S. § 42-5061(B)(4) applies to machinery and equipment employed by businesses engaged in the production and transmission of electricity.

3. The Department Is Not Asking This Court To Read Additional Conditions Or Requirements Into The Exemption.

Contrary to Empire's assertions, the Department is not asking this Court to read additional conditions or requirements into the exemption. Rather, the Department is asking this Court to look at the language of the exemption as a whole in conjunction with the Rule, which distinguishes between nontaxable transmission equipment and taxable distribution equipment.

The exemption and the Rule consider the overall process by which electricity is produced for transmission and distribution. The statute expressly excludes equipment used to distribute electricity from the exemption. The Rule clearly defines distribution equipment as that which produces less than 34,500 volts of electricity. The Legislature's decision to include transmission equipment and exclude distribution equipment evidences its intent not to exempt all equipment.

Empire attempts to discredit the Rule by arguing that it does not define the term "production". Determining what constitutes production, however, is unnecessary because equipment that produces less than 34,500 volts of electricity, including the generators at issue, fall within the definition of distribution equipment. Therefore, they are specifically excluded from the exemption.

Empire's contention that the exemption includes all power producing items produces an absurd result. It is absurd that the Legislature would allow an exemption for everything from batteries to solar cells that power lamps, watches, and toys. Statutes must be interpreted in a way that will not lead to absurd results. *City of Phoenix v. Superior Court*, 144 Ariz. 172, 177, 696 P.2d 724, 729 (App.1985).

In addition, it is well-settled law that an agency's interpretation of a statute it enforces, absent contrary Legislative intent, is given great weight. *Davis v. ADOR*, 197 Ariz. 527, 530, 4 P.3d 1070, 1073 (App. 2000). The Legislative history of A.R.S. §§ 42-5061(B)(4) and 42-5071(B)(2) supports the Department's interpretation.

B. THE LETTER ISSUED IN 1983 IS A RED HERRING.

The Department has consistently held that machinery and equipment producing less than 34,500 volts of electricity constitutes distribution equipment and is therefore not exempt. A.A.C. R15-5-128(B)(1). Empire notes that it received a letter from the Department issued over twenty years ago. Empire could not have relied upon the 1983 letter during the refund period given the fact that during that period, Empire reported and remitted tax on the sales of the generators. In addition, the letter responded to a letter submitted by Empire's predecessor, not Empire. Moreover, nothing in the letter indicates which exemption the author was referring to. In 1983, A.R.S. § 42-1312.01 provided various exemptions for different equipment. Therefore, the letter does not render a conclusion or final decision of the Department regarding the exemption at issue in this case.

C. THE DEPARTMENT DID NOT VIOLATE THE EQUAL PROTECTION CLAUSE

Empire's second claim is that the Department's denial of its request for refund violates the equal protection clause. The first step in a claim for an equal protection violation is demonstrating that similarly situated taxpayers are treated differently. *Brink Elec. Constr. Co. v. Arizona Dep't of Revenue*, 184 Ariz. 354, 363, 909 P.2d 421, 429 (App. 1995). To date, Empire has not provided any evidence to establish that the Department has treated Empire differently from any other taxpayer in the same business.

Empire alleges with no foundation, that the Department does not collect sales tax from other vendors.[1] Transaction privilege tax is self assessed. The Department is under no obligation to audit every taxpayer. *Tucson Mechanical Contracting, Inc. v. Arizona Dep't of Revenue*, 175 Ariz. 176, 182, 854 P.2d 1162, 1168 (App. 1992).

Empire has failed to demonstrate that any significant quantifiable disparity actually exists between it and other similarly situated vendors that have either been audited or requested a refund. The evidence in the record does not support Empire's allegation that the Department engaged in intentional or arbitrary discrimination. When making an equal protection claim, the burden is on Empire to gather this information or seek a confidentiality waiver from the vendors it believes the Department treats differently to release their tax information. To date, Empire has failed to do either. Nor has Empire established that the Department engaged in systematic conduct deliberately treating similarly situated taxpayers differently. The Department's refusal to allow Empire to claim an exemption does not deny them their equal protection rights.

- Empire Southwest, LLC's Arguments -

A. THE LEGISLATURE CLEARLY PROVIDED THAT EQUIPMENT USED DIRECTLY IN PRODUCING ELECTRICAL POWER IS NOT SUBJECT TO SALES TAX.

1. The Plain Meaning Of The Statute Should Apply.

As Arizona's Supreme Court stated, "it is especially important in tax cases to begin with the words of the operative statute." *See Arizona State Tax Commission v. Staggs Realty Corp.*, 85 Ariz. 294, 297, 337 P.2d 281, 283 (1959). Here the operative statute provides a sales tax exemption for:

[1] *See* this Court's decision in *No Time v. Arizona Department of Revenue*, TX2003-000252 (Tax Court February 12, 2004) that demonstrates that the Department consistently enforces the imposition of transaction privilege tax on the sale and lease of generators. While this decision is not binding in this matter, it illustrates that the Department is not singling out Empire.

> Machinery, equipment or transmission lines used directly in producing or transmitting electrical power, but not including distribution. Transformers and control equipment used at transmission substation sites constitute equipment used in producing or transmitting electrical power.

See A.R.S. § 42-5061(B)(4).

Thus, in clear and unmistakable words, the state Legislature provided an exemption from Arizona's sales tax for equipment used directly in producing electrical power. When the language of a statute is "clear and unambiguous," the "plain meaning" applies unless such an interpretation would result in an absurd result or a result at odds with the Legislature's intent. *See Resolution Trust Corp. v. Western Technologies, Inc.*, 179 Ariz. 195, 201, 877 P.2d 294, 300 (App. 1994). Before Empire filed its refund claim, the Department explained in a letter to Empire Machinery Company that "engine generator sets" used "as an electric power source in institutions, hospitals, industrial commercial facilities, contractors job sites and utilities" are "exempt from the imposition of Arizona sales tax."

Thus, at one time, even the Department agreed that the language of the exemption was clear and unambiguous. The question raised by the Department here is whether the plain meaning of the statute is at odds with the Legislature's intent. Like another sales tax exemption that the Arizona Supreme Court recently construed for "machinery, or equipment, used directly in, manufacturing, processing, fabricating, job printing, refining or metallurgical operations," this exemption is for "machinery [or] equipment used directly in" specified activities. *See Ariz. Dep't of Revenue v. Capitol Castings*, Inc., 207 Ariz. 445, 448, 88 P.3d 159, 162 (2004).

In *Capitol Castings*, the Court concluded that the Legislative policy supporting the "machinery and equipment" exemption is "to stimulate business investment in Arizona in order to improve the state's economy and increase revenue from other taxes, such as income and property taxes." *Id.* That, in fact, is the general purpose of sales tax exemptions. *See, e.g., id.* (citing *Ariz. Dep't of Revenue v. Blue Line Distrib., Inc.*, 202 Ariz. 266, 268, 43 P.3d 214, 216 (App. 2002) (describing the policy supporting Arizona's "machinery or equipment" exemption and citing *71 Am. Jur. 2d State and Local Taxation § 288* (2001)); *Duval Sierrita Corp. v. Ariz. Dep't of Revenue*, 116 Ariz. 200, 204, 568 P.2d 1098, 1102 (App. 1977) (same); *G.E. Solid State, Inc. v. Division of Taxation*, 132 N.J. 298, 310, 625 A.2d 468, 474 (1993). Accordingly, in *Capitol Castings*, the Court determined that its "interpretation of the statute therefore should further, not frustrate, the policy of encouraging investment and spurring economic development." *See Capitol Castings*, 207 Ariz. 445, 448, 88 P.3d 159, 162.

Likewise, because the subject statute is "clear and unambiguous" and interpreting it according to its plain meaning would not result in an absurd result or a result at odds with the Legislature's intent, this Court should interpret the statute to "further, not frustrate, the policy of encouraging investment and spurring economic development." *Id.* Therefore, the Court should

conclude that the subject electric-power generators are equipment used directly in producing electrical power.

2. Both The Rules Of Statutory Construction And The Legislative History Favor Empire.

Because the language of the statute is clear and unambiguous, the plain meaning of the statute should apply and it would not be appropriate to resort to the rules of statutory construction or to rely on Legislative history. *See, e.g., G.E. Solid State, Inc. v. Division of Taxation*, 132 N.J. 298, 307, 625 A.2d 468, 473 (1993); *State v. Dawson*, 264 Ala. 647, 649, 89 So.2d 103, 105 (1956). However, if needed to be considered, the rules of statutory construction and the Legislative history favor Empire.

a. The Rules Of Statutory Construction.

Granted, tax exemptions should be strictly construed. However, that basic precept does not support imposing unstated restrictions into the subject exemption. There simply is no language in the exemption that supports the Department's position. In fact, it seems that most of the cases that construe tax exemptions in favor of a taxpayer involve a holding that the court will not read terms into the exemption, notwithstanding the precept that exemptions should be strictly construed. *See, e.g., G.E. Solid State, Inc. v. Division of Taxation,* 132 N.J. 298, 625 A.2d 468 (1993) (although, the taxing authority had an administrative rule in place indicating that the state's exemption for manufacturing equipment did not apply unless the products manufactured were "for sale," the court held it could not read a "for sale" requirement into the statute despite narrowly construing the language); *Gulf Stevedore Corporation v. Rabren*, 286 Ala 482, 242 So.2d 386 (1970); *State of Alabama v. Television Corporation*, 271 Ala. 692, 127 So.2d 603 (1961); *State v. Reynolds Metal Company*, 263 Ala. 657, 662, 83 So.2d 709, 713 (1955); *State v. Calumet & Hecla Consol. Copper Co.*, 259 Ala 225, 66 So.2d 726 (1953).

b. The Legislative History.

The Department argues that the Legislative history of the 1968 version of the subject exemption supports it's theory that the current 1988 version of the exemption only applies to "equipment employed by utilities." The Department's argument is based on the fact that, in 1968, the Legislature enacted an exemption entitled "Electric power production and transmission" rather than an exemption entitled "Electric Power Companies." Because the current version of the subject exemption was enacted twenty years later in 1988, any Legislative history relative to the 1968 version of the exemption is irrelevant or should be given very little weight when construing the current version of the exemption. It is a different statute that was enacted by a different Legislature. Worse yet, part of the "Legislative history" that the Department cited actually involved a lobbyist's recommendations to broaden the exemption rather than a statement of the Legislature's intent.

That said, the "Legislative history" of the 1968 version of the exemption actually favors Empire's interpretation of the subject exemption rather than the Department's interpretation. While the language of both versions of the exemption suggests that the exemption applies to certain equipment employed by utilities, neither version of the exemption suggests that the Legislature intended to limit the exemption to equipment employed by utilities. To the contrary, the language of the exemption that the Legislature adopted in 1968 is broader than the language that was proposed in 1967 because, among other things, its title clearly indicated that it applied to "Electric power production and transmission" rather than to "Electric Power Companies."

Under the language of the exemption that the Legislature enacted in 1968, one did not have to be engaged in business as an electric power company in order to qualify for the exemption. That was clear because neither the title of the 1968 version of the exemption nor the language of the exemption required as much. Today, the exemption does not even include titles such as "Electric power production and transmission" and the language of the exemption still does not require one to be engaged in business as an electric power company. Rather, under the current version of the exemption, proceeds from sales of equipment used directly in producing electrical power are not subject to tax.

3. The Legislature Did Not Provide A More Restrictive Exemption.

The Department urges that the exemption for equipment used directly in producing electrical power should be more restrictive. For example, it suggests that the exemption does not apply to "portable generators," that it only applies to "equipment employed by utilities" and that it does not apply to "small electric power sources." At the administrative hearing, the Department even argued that the exemption only applies to equipment used to produce electrical power for sale by utilities. The Department, however, reads limitations into the exemption that simply do not exist. If the state Legislature intended the exemption to be more restrictive, it would have used more restrictive language like it did in so many other exemptions.

For example, the Legislature has created more restrictive sales tax exemptions for:

- Tangible personal property "sold to persons engaged in business classified under the telecommunications classification," *see* A.R.S. § 42-5061(B)(3);

- Tangible personal property "sold to a person that is subject to tax under . . . the prime contracting classification," *see* A.R.S. § 42-5061(A)(27);

- Sales of food, drink or condiments "to persons engaged in business classified under the restaurant classification," *see* A.R.S. § 42-5061(A)(5);

- Sales of "[m]ining machinery, or equipment, used directly in the process of extracting ores or minerals from the earth for commercial purposes," *see* A.R.S. § 42-5061(B)(2);

- Sales of "[m]achinery or equipment used directly to drill for oil or gas used directly in the process of extracting oil or gas from the earth for commercial purposes." *See* A.R.S. § 42-5061(B)(10).

All of these exemptions are more restrictive than the subject exemption. They demonstrate that the Legislature knows how to draft a more restrictive exemption. However, the subject exemption is not restricted to persons "engaged in business" under a particular classification, "subject to tax" under a particular classification or using equipment for "commercial purposes" like these other exemptions. Rather, in this case, the Legislature used clear and unmistakable language to create an exemption from Arizona's sales tax for equipment used directly in producing electrical power.

Equally important, the Legislature did in fact provide express limitations to the exemption by requiring that the equipment be "used directly" in "producing or transmitting," but not in distributing, electrical power. *See* A.R.S. § 42-5061(B)(4). The Legislature obviously required that the equipment at issue have a direct relationship to the actual production or transmission of electrical power. In sum, this exemption is sufficiently and carefully crafted to relate to a specific type of equipment with a specific purpose that produces a specific result (i.e., equipment used to produce or transmit electrical power but not to distribute it).

C. THE GENERATORS ARE USED IN PRODUCING ELECTRICITY RATHER THAN IN DISTRIBUTING ELECTRICITY.

The Department argues that the instant exemption does not apply to the subject electric-power generators because they are used to distribute rather than to produce or transmit electrical power. In support of its argument, the Department cited the Rule, which distinguishes between equipment used to transmit electrical power and equipment used to distribute electrical power. The Department's argument reflects a fundamental misunderstanding of the Rule and of the difference between producing, transmitting and distributing electricity.

The equipment used to produce electricity, namely an electric-power generator, is distinguishable from the equipment used to transmit or distribute electricity, like transformers. *See, e.g., Niagara Mohawk Power Corporation v. Wanamaker*, 144 N.Y.S.2d 458, 462-63, 286 A.D. 446, 450 (Sup. Ct. 1955) (transformers "are used in transmission or distribution, rather than in production" and "[a] transformer does not and cannot increase the amount of electric energy" because "[t]he maximum amount of energy has been produced when a current leaves the generator."). As explained below, the Department's Rule exists *solely* to distinguish between equipment used to transmit electrical power and equipment used to distribute electrical power. It does not define or address equipment used to produce electric power. Electric-power generators

are used to produce rather than to transmit or distribute electrical power. Therefore, the Rule is not relevant to the subject dispute involving electric-power generators that are used to produce rather than to transmit or distribute electrical power.

In *Maine Yankee Atomic Power Co v. State Assessor*, the court recognized the distinction between generating or producing electricity and the subsequent transmission and distribution of electricity. *See Maine Yankee Atomic Power Company v. State Assessor*, 1997 ME 27, 690 A.2d 497, 498 (1997). The court explained the process by which electricity is produced by generators at relatively low levels, the voltage is then stepped-up by transformers for purposes of mass transmission and subsequently stepped-down by transformers for purposes of distribution to individual customers:

> [The power company's] contract with its customers requires that electricity be delivered to the switchyard at 345,000 volts.
>
> Two phases are required to produce the electricity at the required 345,000 volts. The first phase, performed by the reactor or main generator creates or generates electricity at 22,000 volts, which has very little commercial value because it cannot be efficiently transmitted. The second phase, performed by the two transformers . . . alters the electricity received from the main generator by increasing the voltage to 345,000 and decreasing the amperage. Following this process, the electricity is in the transmittable form required by [the power company's] customers.
> . . .
>
> The customers distribute the electricity acquired by them in bulk to their own service area using downstream transformers to "step down" the high voltage electricity to lower voltages suitable to the requirements of the general public.
>
> *Id*.

In sum, the first two phases of generating and transmitting electricity involve the production of electricity at relatively low voltage levels using generators and subsequently increasing the voltage of the electricity using transformers to prepare the electricity for bulk transmission. In a third phase, which the *Maine Yankee Atomic Power Company* court and the subject exemption and Rule distinguish from production and transmission and refer to as distribution, transformers are used to "step down" the high voltage electricity to lower voltages suitable for use by the general public. Apparently because some of the same equipment, like transformers, is used both in transmission and distribution activities, the Department promulgated its Rule "to distinguish between nontaxable transmission equipment and taxable distribution equipment."

While the parties agree that the Rule exists to distinguish between equipment used to transmit electrical power and equipment used to distribute electrical power, they disagree over the Rule's effect on equipment used to produce electrical power. And, although the Rule distinguishes between equipment used in transmission activities and equipment used in distribution activities, it does not dictate, as the Department argues, that production equipment somehow becomes distribution equipment if it produces less than 34,500 volts of electricity. Quite simply: Production equipment is production equipment, transmission equipment is transmission equipment and distribution equipment is distribution equipment. The Rule exists to distinguish between transmission equipment and distribution equipment but has no bearing on equipment used to produce electricity.

Contrary to the Department's suggestion, Empire's argument that the exemption applies to the subject electric-power generators does not lead to an absurd result. Empire is not arguing that "everything from batteries to solar cells that power lamps, watches, and toys" qualifies for the exemption. Batteries do not even produce electrical power like the subject electric-power generators (batteries store power), and Empire does not sell or lease solar cells that power lamps, watches and toys. Rather, Empire believes that the electric-power generators that it sells and leases, primarily to large construction contractors, governmental entities and industrial companies, including utility companies, qualify for the exemption. At one time before Empire filed the subject refund claim, the Department agreed with Empire's position.

D. THE DEPARTMENT VIOLATED EMPIRE'S RIGHT TO EQUAL PROTECTION UNDER THE LAW.

Empire is a vendor of electric-power generators. While the Department denied Empire's refund claim for sales tax paid on its gross receipts from selling and renting electric-power generators, upon information and belief, the Department still does not collect sales tax from other vendors of electric-power generators including: General Electric, Westinghouse, Siemens, Hitachi, Allis Chalmers, Brush and Brown, Boveri & Co. Empire believes that the Department has, thereby, denied its right to equal protection under the law. *See* Ariz. Const., Art. 2, § 13; U.S. Const., Fourteenth Amendment; *Gosnell Development Corporation v. Ariz. Dep't of Revenue*, 154 Ariz. 539, 744 P.2d 451 (App. 1987). If necessary, discovery should proceed on this issue, and the taxpayer is entitled to a trial on these claims.

IV. THE COURT'S FINDINGS AND CONCLUSIONS

This was admittedly a very close case. On the face of A.R.S. § 42-5061(B)(4), the Court might well conclude Empire is entitled to a refund pursuant to the exemptions from Arizona transaction privilege tax for sales and leases of electric-power generators. However, upon the Court's review of the Legislative history and the Department's Rule, the Court must concur with the Department's arguments and the Hearing Officer's conclusions that Empire's generators are not exempt from taxation under Arizona law.

The Department's interpretation of the statute it enforces is entitled to substantial deference. The same may be said of the Department's interpretation of its implementing Rule, which the Court finds is reasonable in light of the Legislative history of the statute. Further, the Rule upon which the Department relies was promulgated 10 years after the date of the letter upon which Plaintiff relies. An agency rule is entitled to far greater weight than a much older agency letter, particularly when the context of the letter is unclear. Also, Plaintiff never relied on the letter for the tax years at issue.

Further, the Legislative history, sparse though it is, supports the Department's position that the statute was not intended for the benefit of sellers and lessors of the types of generators at issue. *See also* Judge Katz's decision in *No Time v. Arizona Department of Revenue*, TX2003-000252 (Arizona Tax Court, filed February 12, 2004).

Finally, the Court concurs with the Department that Empire's Equal Protection claim lacks merit since Empire came forward with no evidence of disparate treatment.

IT IS THEREFORE ORDERED granting the Department's Motion for Summary Judgment and denying Empire's Cross-Motion for Summary Judgment.

IT IS FURTHER ORDERED that both sides shall bear their own attorneys' fees and costs.