Cite as Det. No. 98-208, 19 WTD 332 (2000)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of Assessment of	)	D E T E R M I N A T I O N
	)	
	)	No. 98-208
. . .	)	
	)	Registration No. . . .
	)	FY . . ./Audit No. . . .
	)	FY . . ./Audit No. . . .

[1] RULE 179; RCW 82.16.050(7): PUBLIC UTILITY TAX – DEDUCTIONS – IRRIGATION. So long as an irrigation or water district or a municipal water department supplies potable water and it segregates and separately supplies some of the water solely for nourishing plant life, as opposed to water supplied for domestic, municipal, or industrial uses, charges for such separately supplied water qualify for the deduction for water distributed through an "irrigation system, for irrigation purposes.

[2] RULE 195; RCW 82.16.010; RCW 82.16.050(1): PUBLIC UTILITY TAX – MUNICIPAL TAXES – DEDUCTIONS. Public utility taxes imposed by a municipality and received by the municipality's public utility are part of the gross income of the utility and are included in the measure of the state's public utility tax.

[3] RULE 189; RULE 251; RCW 82.04.419: B&O TAX – SEWERAGE COLLECTION BUSINESS – ENTERPRISE ACTIVITIES. A municipality's sewerage and surface water management services are not exclusively governmental in nature, and revenues from those activities are subject to the business and occupation tax.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

NATURE OF ACTION:

A City protests the denial of a tax credit with respect to: (1) a claimed irrigation deduction; (2) a claimed deduction for a municipal utility tax collected by the city's public utility; and (3) a deduction for sewerage and surface water management revenues.[1]

FACTS:

Mahan, A.L.J. – The taxpayer is the City . . . In addition to general municipal operations, it provides water distribution and sewer collection/treatment services. It also operates various golf courses and other recreational facilities.

The Department of Revenue (Department) reviewed the taxpayer's records for the January 1, 1990 through December 31, 1995 period. During this audit, the taxpayer sought a credit for public utility taxes paid on water distributed through an "irrigation system." It also requested a credit for public utility tax that was paid on the municipal utility tax portion of the city's sewer collection and water distribution revenues. The Department denied those credit requests. Following the issuance of an audit report, the taxpayer also sought a credit regarding the B&O tax that had been paid on revenues from sewer treatment and surface water management. The Department disagreed with this request and stated this issue should be included in any appeal.

With respect to the irrigation credit, the taxpayer's water department provides separate meters for certain customers, e.g., golf courses and parks. Such separately metered water is segregated at the water main on the road from water going through a meter for domestic use. The taxpayer owns all of the meters and the customer owns the system after the meters. A field inspection is generally required in order for a customer to get a separate meter for water to irrigate lawns and landscaping. The Department denied the irrigation deduction for such separately metered water, because of the Department's policy that the deduction applies only if the water is used for agricultural purposes. None of the customers for whom the deduction was claimed used the water for agricultural purposes.

With respect to the municipal utility tax credit, the taxpayer, in accordance with city ordinances, assessed business and occupation tax on public and private utility services. Those taxes are used for general governmental purposes, rather than for the direct support of the public utility business. The Department disallowed the credit because the deduction under RCW 82.16.050(1) applies only to taxes levied for the "support and maintenance" of the utility. In response, the taxpayer contends that this statutory language refers to the support and maintenance of the municipal owner, not the utility itself. In making this argument, the taxpayer concedes that it is not a "natural" reading of the statute, but one required because of a perceived ambiguity in the statute.

The taxpayer also seeks a credit for its payment of B&O taxes on storm drainage and sewerage treatment revenues. The taxpayer contends that those charges are governmental in nature and

[1] Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

not as a result of enterprise activities. In support, it cites to RCW 36.70A.020 and .030, which mandate comprehensive planning for storm drainage and sewerage facilities.

ISSUES:

1. Whether a city is entitled to deduct charges for water that is segregated from domestic water and supplied for the nourishment of plant life.

2. Whether a city is entitled to deduct a municipal utility tax from the measure of the water department's state public utility tax.

3. Whether revenues from a City's sewerage and surface water management services are exclusively governmental in nature and, therefore, not subject to the business and occupation tax.

DISCUSSION:

1. Irrigation Deduction.

[1] RCW 82.16.050(7) permits a deduction from the public utility tax for:

> Amounts derived from the distribution of water through an irrigation system, for irrigation purposes;. . .

RCW 82.16.050 has remained the same for sixty years, since enactment of the Revenue Act of 1935, Laws of 1935, c. 180, § 40, despite amendments to other parts of RCW 82.16.

The Department's administrative rule implementing the statute is WAC 458-20-179 (Rule 179). Rule 179(15)(d) is virtually identical to the statute, with the notable exception of the inclusion of the word "solely" in limiting the availability of the deduction. It provides that the deduction is available for:

> Amounts derived from the distribution of water through an irrigation system, solely for irrigation purposes.

Under this rule and the statute, the taxpayer must satisfy a two-pronged test: (1) that the water was distributed through "an irrigation system," (2) solely "for irrigation purposes." Those terms are not defined by the statute, and we must determine whether they include the various uses by the taxpayer's customers.

The goal of any statutory construction is to follow the intent of the legislature. Legislative intent is to be ascertained from the statute as a whole, and all statutes relating to the same subject matter should be considered. State v. Wright, 84 Wn.2d 645, 652, 529 P.2d 453 (1974); Clark v. Pacificorp, 118 Wn.2d 167, 176, 822 P.2d 162 (1991). A term not defined in a statute is afforded its

plain and ordinary meaning. However, when a word has no fixed, ordinary meaning, we must look to the subject matter, the context in which the word is used, and the purpose of the statute. KSLW v. Renton, 47 Wn. App. 587, 594, 736 P.2d 664 (1986).[2]

The term "irrigation" has different meanings, depending on the context in which it is used. Under ordinary usage, it is broadly defined. For example, Webster's II New Riverside University Dictionary 645 (1984) defines the term "irrigate" to mean "to supply (dry land) with water by means of ditches, pipes, or streams." In contrast, Blacks Law Dictionary 744 (5th ed. 1979) defines an "irrigation company" as one that conveys water "by means of ditches or canals through a region where it can be beneficially used for agricultural purposes." Similarly, the legislature used the term "irrigable acreage" to mean "all lands included in the district capable of being used for agricultural purposes." RCW 87.22.085 (Laws of 1929, c. 202, § 88). In 45 Am. Jur. 2d, Irrigation § 1 at 945 (1969), the term was defined as follows:

> Irrigation is defined as the artificial watering of agricultural lands in regions where rainfall is insufficient for crops. The ordinary and popular conception of the term is that it denotes the application of water to land for the production of crops; the term embraces all artificial watering of lands, whether by channels, by flooding, or merely by sprinkling.

In Det. No. 95-002, 15 WTD 106 (1996) and Det. No. 95-201, 15 WTD 166 (1996), we addressed the deduction when it was taken by water districts for water separately supplied for the purpose of watering golf courses and landscaping. In those cases we concluded that an industry specific definition, which required an agricultural component, should be used to construe the statute.

Upon further consideration of this, the Department has concluded it was error to require an agricultural component in order for the deduction to apply. Accordingly, we overrule Det. No. 91-294R, 11 WTD 487 (1991); Det. No. 95-002, 15 WTD 106 (1996) and Det. No. 95-201, 15 WTD 166 (1996), as they apply to the distribution of water through an irrigation system for irrigation purposes.[3] So long as an irrigation or water district or a municipal water department supplies potable water and it segregates and separately supplies some of the water solely for nourishing plant life, as opposed to water supplied for domestic, municipal, or industrial uses, charges for such separately supplied water qualify for the deduction for water distributed through an

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[2] On several occasions the Department has addressed the scope of the irrigation deduction. See Det. No. 91-294R, 11 WTD 487 (1991); Det. No. 95-002, 15 WTD 106 (1996); Det. No. 95-201, 15 WTD 166 (1996). The Thurston County Superior Court has reversed the Department in two cases: Alderwood Water Dist. v. Washington, Thurston County Sup. Ct. No. 91-2-02772-3 (1993) and Woodinville Water Dist. v. Department of Rev., Thurston County Sup. Ct. No. 95-2-03654-3 (1996). Although the Department sought review of the Woodinville case by Division II of the Washington State Court of Appeals, that appeal was withdrawn.

[3] In order to meet the "irrigation system" requirement, a district must demonstrate that its distribution system has turnouts or similar connections for irrigation purposes that are separate from service hookups or similar connections for domestic, industrial, or municipal uses. Under the appropriate circumstances, the use of separate meters and cross-connection or back flow devices may be evidence of such separate connections.

"irrigation system, for irrigation purposes". Accordingly, the taxpayer's petition in this regard is granted.

2. Municipal Tax Deduction.

[2] The taxpayer contends that the city utility tax should be deductible from the state tax measure, pursuant to RCW 82.16.050(1). Under that provision, the deduction is limited to:

> Amounts derived by municipally owned or operated public service businesses, directly from taxes levied for the support or maintenance thereof: PROVIDED, That this section shall not be construed to exempt service charges which are spread on the property tax rolls and collected as taxes; . . .

Where no contrary intention appears in a statute, relative and qualifying words and phrases, both grammatically and legally, refer to the last antecedent. Boeing v. Department of Licensing, 103 Wn.2d 581, 587, 693 P.2d 104 (1985); see also Davis v. Gibbs, 39 Wn.2d 481, 483, 236 P.2d 545 (1951). Under this rule of construction, the phrase "directly from taxes levied for the support or maintenance thereof" modifies the term "municipally owned or operated public service businesses." As such, in order for taxes to be deductible, they must be levied for the support or maintenance of the public service business asserting the deduction. In this case, the City's utility tax is not levied for and does not go directly to the City's water department for its support. Rather, the tax is levied in support of the City and goes directly to the City's general fund.

As a general matter, the taxes the City's public utility receives are included in the measure of the public utility tax. RCW 82.16.010 defines "gross income" by which the public utility tax is measured, as follows:

> (12) "Gross income" means the value proceeding or accruing from the performance of the particular public service or transportation business involved, including operations incidental thereto, but without any deduction on account of the cost of the commodity furnished or sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses.

(Emphasis added). See also WAC 458-20-195 (Rule 195) (state and municipal public utility taxes are not deductible from the state public utility tax.) The City's public utility tax proceeds or accrues from the water delivery business in which the taxpayer is engaged, and it is part of the cost of doing business.

The conclusion that the city's utility tax is not deductible is consistent with the Department's Excise Tax Advisory 183.16.179 (1966) (ETA 183), which reads, in relevant part:

> A public utility district was taxed under a city business and occupation tax and a Public Utility District Tax. It contended the amounts paid under the two taxes should

> have been deducted from the gross receipts taxed under Chapter 82.16 RCW, Public Utility Tax.
>
> The Commission held that the computation of the gross income (as defined by RCW 82.16.010(12)) of the power and light company properly included the amounts paid for taxes. In an appeal to the Superior Court, it was held that the city taxes were rightfully considered part of the cost of doing business and that billing the taxes as separate items could not convert them to taxes on the consumer. Thus, the proper measure of the state Public Utility Tax was the total amount billed for utility services without deduction of the amount of the city taxes

The conclusion reached by the Tax Commission, as referenced in ETA 183, was upheld by the court in Public Utility Dist. v. State, 71 Wn. 2d 211, 427 P.2d 713 (1967), where the court held:

> By the express terms of this statute [RCW 82.16.010(12)] no deduction for taxes paid or accrued is allowable in determining "gross income," since these expenses are treated as part of the cost of doing business as a franchised public utility. Therefore, the district, by billing the two taxes in question to its customers (either separately or buried in the total charge for services), adds to its "gross income" and cannot thereafter make deductions therefrom in measuring its tax liability under the public utility tax, RCW 82.16.

Accordingly, the taxpayer's petition in this regard is denied.

3. ***Sewerage and Surface Water Management.***

[3] The taxpayer's sewerage collection business is subject to public utility tax, whereas its income from the "transfer, treatment or disposal" of sewage is subject to service B&O tax. WAC 458-20-251 (Rule 251). Subsection (3)(a) of Rule 251 defines a "sewerage collection business" as follows:

> "Sewerage collection business" means the activity of receiving sewage deposited into and carried off by a system of sewers, drains, and pipes to a common point, or points, for disposal or for transfer to treatment for disposal, but does not include such transfer, treatment, or disposal of sewage.

The rule addresses the taxability of other sewerage services by stating at WAC 458-20-251(7) as follows:

> Business and occupation tax. Persons engaged in providing other sewer services, in addition to or separate from the "sewerage collection business" as defined herein, are subject to the business and occupation tax under the classification, service and other business activities. The measure of this tax is the gross income derived from such other services. It does not include any amount reported for public utility tax under the sewer collection classification.

With respect to the taxable nature of the sewerage collection and related activities, Rule 251 provides, in relevant part:

> (10) The "sewerage collection business" and many other sewer services are "enterprise activities" as defined in WAC 458-20-189, when funded over fifty percent by user fees. Thus, the amounts derived from these business activities are not exempt of tax even though they may be provided and charged for by governmental entities. (See RCW 82.04.419.)

RCW 82.04.419 provides:

> This chapter shall not apply to any county, city, town, school district, or fire district activity, regardless of how financed, other than a utility or enterprise activity as defined by the state auditor pursuant to RCW 35.33.111 and 36.40.220 and upon which the tax imposed pursuant to this chapter had previously applied. Nothing contained in this section shall limit the authority of the legislature to authorize the imposition of such tax prospectively upon such activities as the legislature shall specifically designate.

In this case, the taxpayer concedes that "storm drainage and sewer treatment activities are accounted for in proprietary funds as enterprise activities" in accordance with the state auditor's accounting requirements. However, the taxpayer contends that, under WAC 458-20-189 (Rule 189), RCW 36.70A.020(12) and .030(12), such services should be considered exclusively governmental in nature.

Rule 189(2)(d) provides:

> "Enterprise activity" means an activity financed and operated in a manner similar to a private business enterprise. The term includes those activities which are generally in competition with private business enterprises and which are over fifty percent funded by user fees. The term does not include activities, which are exclusively governmental.

The taxpayer's reference to certain sections of the Growth Management Act, RCW 36.70A, however, does not support its contention that sewerage and storm water treatment services are exclusively governmental in nature. For purposes of comprehensive planning, the taxpayer must ensure the existence of adequate "public facilities", which are defined to include "storm and sanitary sewer systems", along with roads and recreational facilities. RCW 36.70A.030(12). If the revenues at issue involved fees for comprehensive planning, such provisions might support the taxpayer's claim. There is nothing in the Act, however, to lead us to conclude that the operation of storm drainage and sewer treatment systems is exclusively governmental in nature. Indeed, if we were to accept the taxpayer's argument, other, more specific statutory provisions would be rendered mere surplusage. See, e.g., RCW 82.04.432 (which allows a B&O tax deduction for amounts paid to other municipalities on sewerage activities). Statutes should be

interpreted so as not to leave another statute mere surplusage. Schrempp v. Munro, 116 Wn.2d 929, 934, 809 P.2d 1381 (1991).

Accordingly, the taxpayer's petition in this regard is denied.

DECISION AND DISPOSITION:

The taxpayer's petition is granted in part and denied in part. It is granted with respect to the claimed irrigation deduction credit. It is denied with respect to other claims. This matter is remanded to the Audit Division for adjustment in accordance with this decision.

Dated this 30th day of November, 1998.