

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

TX 2007-000496

05/19/2010

HONORABLE DEAN M. FINK

CLERK OF THE COURT
S. Brown
Deputy

WELLS FARGO AND COMPANY AND
SUBSIDIARIES

BARBARA J DAWSON

v.

ARIZONA STATE DEPARTMENT OF
REVENUE

KIMBERLY J CYGAN

CHARLES A PULASKI JR.

MINUTE ENTRY

The Court took this matter under advisement following oral argument on April 6, 2010.

A.R.S. § 43-102(A)(1) sets forth a default rule that, unless the legislature has ordered otherwise, the provisions of the Internal Revenue Code applying to income taxation are to be followed to compute Arizona income tax. However, A.R.S. § 43-1121(7) and A.R.S. § 43-1122(7) are clear that, notwithstanding the general policy of harmonizing state and federal income tax laws, the federal allowance for net operating loss codified at I.R.C. § 172 is not extended to Arizona returns: the Section 172 allowance is to be added back to taxable income, and a net operating loss calculated pursuant to A.R.S. § 43-1123 is subtracted in its place. It would be irrational to go through this addition and subtraction if the state NOL is simply the federal NOL so that the result would necessarily be the same; the statutory language necessitates the conclusion that the legislature intended for the state to write its own rules governing net operating losses.

The I.R.C. § 381(c)(1) calculation of net operating loss carryovers for merged corporations is expressly based on the Section 172 net operating loss(es) calculated for the distributor/transferor corporation, with various specified adjustments. Construed narrowly, A.R.S. § 43-1121(7) requires that the Section 172 part, but not the Section 381 adjustments to it,

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be added back to Arizona taxable income. It seems doubtful to the Court, however, that the adjustments have any coherence except by reference to the proscribed Section 172 calculation; moreover, A.R.S. § 43-1123 envisions a comprehensive state scheme that adjustments based on an unrelated figure would mar. The Court therefore concludes that the Arizona net operating loss rules apply in lieu of the federal rules set forth in I.R.C. § 381-82.

The question thus becomes, not whether R15-2-1123 is consistent with the Internal Revenue Code, but only whether it is consistent with A.R.S. § 43-1123. (Wells Fargo's appeal to A.R.S. § 10-11106 fails. Under that statute at (A)(2), the surviving corporation is vested with "title to all real estate and other property" of the former corporation. A net operating loss is not property.) However, Wells Fargo has not shown that, beyond severing Arizona calculation of NOL from the federal rules, the legislature has spoken definitively as to how NOL is to be calculated, either in general or in the specific case of a merged corporation. Where no unambiguous mandate exists, "considerable weight should be accorded to an executive department's construction of a statutory scheme it is entrusted to administer." *Stearns v. Arizona Dept. of Revenue*, 212 Ariz. 333, 336 ¶ 17 (2006) (quoting *Arizona Water Co. v. Arizona Dept. of Water Resources*, 208 Ariz. 147, 154 ¶ 30 (2004)). Absent a sufficient showing, the regulation must be upheld.

Accordingly,

IT IS ORDERED denying Plaintiff's Motion for Partial Summary Judgment filed September 15, 2009.

IT IS FURTHER ORDERED granting Arizona Department of Revenue's Cross-Motion for Partial Summary Judgment on the Net Operating Loss Issue filed October 20, 2009.

Consistent with the Court's April 6, 2010 minute entry,

IT IS FURTHER ORDERED that within thirty days, counsel shall submit either a Stipulated Scheduling Order or a Request for Rule 16 Scheduling Conference.