

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT

John D McLeod, Administrative Law Judge

Case No 09-ALJ-17-0532-CC

Centex International, Inc & Affiliates

Appellant,

v

South Carolina Department of Revenue

Respondent

FINAL BRIEF OF APPELLANT

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STATEMENT OF ISSUES ON APPEAL

- I DID THE ALC ERR AS A MATTER OF LAW BY CONCLUDING THAT THE CORPORATE AFFILIATES OF CENTEX WERE NOT ELIGIBLE TO CLAIM THE INFRASTRUCTURE TAX CREDIT UNDER S C CODE ANN § 12-6-3420 AS PARTNERS OF THE CENTEX HOMES PARTNERSHIP?**
- II DID THE ALC ERR IN ITS APPLICATION AND INTERPRETATION OF THE AGGREGATE AND ENTITY THEORIES OF PARTNERSHIP TAXATION BY CONCLUDING THAT THE INFRASTRUCTURE EXPENDITURES AND CONTRIBUTIONS MADE BY CENTEX REAL ESTATE CORPORATION (CREC) AS MANAGING GENERAL PARTNER OF CENTEX HOMES REMAINS ATTRIBUTABLE TO THE PARTNERSHIP?**
- III DID THE ALC ERR IN ITS CONCLUSION THAT CENTEX INTERNATIONAL, INC AND AFFILIATES ARE NOT A SINGLE TAXPAYER AND MAY NOT CLAIM THE INFRASTRUCTURE CREDIT ON ITS CONSOLIDATED TAX RETURN?**

STATEMENT OF THE CASE

This case originated when Centex International, Inc and Affiliates (hereinafter “Centex” or “Appellant”) filed amended 2002 through 2004 South Carolina corporate tax returns in December 2005 and subsequently filed its 2005 tax return claiming infrastructure tax credits totaling in all \$5 1 million. The infrastructure credits claimed for those tax years were based upon the expenditures of \$68 million made by three corporate subsidiaries of Centex, operating in South Carolina as general partners of Centex Homes. The Department of Revenue (“SCDOR”) determined that the Appellant was not entitled to claim infrastructure tax credits on the basis that the qualifying infrastructure expenses were incurred by the general partnership, rather than the Appellant directly, and disallowed the credits in a notice of proposed assessment dated

July 25, 2007 On October 23, 2007, the Appellant appealed the denial of the credit and the notice of the proposed assessment

The SCDOR issued its Final Determination on December 4, 2009, setting forth the legal basis for its denial of the claim for credits On December 7, 2009, the Appellant requested a contested case hearing before the Administrative Law Court (“ALC”) to dispute the SCDOR’s Determination The SCDOR filed a Motion for Partial Summary Judgment on the infrastructure tax credit question, to which the Appellant responded with a Cross-Motion for Summary Judgment on the same issue With both parties stipulating that no issue of fact remained on the infrastructure credit issue, a hearing was held before the Honorable John D McLeod of the ALC on March 31, 2011

On June 2, 2011, Judge McLeod granted the SCDOR’s Motion for Summary Judgment and denied Appellant’s Cross-Motion for Summary Judgment Appellant timely filed a Motion to Reconsider and/or Alter or Amend pursuant to Rule 59, SCRCP The SCDOR filed a Reply in Opposition, and a hearing was held before Judge McLeod On July 11, 2011, Judge McLeod denied Appellant’s Motion for Reconsideration and Motion to Alter or Amend

On August 3, 2011, Appellant timely filed and served its Notice of Appeal to the Court of Appeals Appellant also filed a Motion to Substitute Counsel on October 26, 2011

The relief sought by the Appellant is the issuance of an Order by the court finding that the ALC erred (1) in granting an Order ruling in favor of the Respondent’s Motion for Summary Judgment, and (2) in failing to grant the Appellant’s Cross Motion for Summary Judgment

STATEMENT OF FACTS

The facts are not in dispute in this matter. Centex Homes is a builder and developer that acquires and develops land used primarily for the purpose of developing communities and constructing new homes throughout the country. Centex Homes constructs significant infrastructure to support the areas in which it is building homes and developing communities. South Carolina has an infrastructure tax credit statute at S.C. Code Ann. § 12-6-3420 (1976) (the "Infrastructure Credit Statute") under which taxpayers may claim a credit for certain infrastructure expenses, such as roads, water lines and sewer lines, made by taxpayers that benefit the State and its residents where that infrastructure does not exclusively benefit the taxpayer, built to applicable standards, and dedicated to public use.

During fiscal years ending March 31st of 2002 through 2005, the audit years at issue in this matter (the "Audit Years"), Centex Homes spent approximately \$68 million in South Carolina developments on roads and water and sewer lines. Specifically, Centex spent approximately \$11,533,645 on water lines, \$33,028,002 on sewer lines and \$23,440,223 on roads. (R. p. 334, Par. 7) Centex Homes was one of the largest homebuilders in South Carolina during the Audit Years. (R. pp. 334-35, Par. 5) Upon completion of the developments, Centex Real Estate Corporation ("CREC"), the managing general partner of Centex Homes, dedicated the infrastructure to public use by contributing the properties to local municipalities and counties in South Carolina (at no cost to them) thus becoming public property for the benefit of this State's residents and communities.

The Appellant is a corporation subject to the South Carolina corporate income tax. Centex Homes is a general partnership with three corporate partners. All three corporations are wholly owned subsidiaries of Appellant. (R. p. 111, Par. 11) Although Centex Homes is considered a "taxpayer" as it files both a federal and state (South Carolina) partnership return, these partnership returns are for informational purposes only and Centex Homes pays no income tax. Rather, the income, deductions, and credits pass through to its corporate partners and are reflected as income, deductions, and credits on Appellant's consolidated federal and state income tax returns.

Accordingly, Appellant's South Carolina corporate tax return, filed on a consolidated basis, included the infrastructure credit for the audit years. (R. pp. 111-12, Par. 12) After reviewing Appellant's claim, one of SCDOR's most experienced auditors (R. p. 337, page 10, lines 22-24), Orville Sharpe, consulted his supervisor via an email. The e-mail precisely states the issue as follows:

This is regarding the Infrastructure credit I'm working for Centex International, Inc. & Affiliates. The credits were earned by the Partnership Centex Homes. The Partnership is owned by three different Corporate affiliates of Centex International:

AAA Holdings, Inc. (owns 80% of the partnership), Nomax Corp. (owns 18% of the partnership), Centex Real Estate Corporation (owns 2% of the Corporation). The Partnership not the corporations would have paid the infrastructure expenses. Would the Corporations be able to claim credits earned by the partnership since the partners pro rata share of the partnership's income flows to the corporations or does the infrastructure expenses have to be paid by a corporation before any resulting infrastructure credits can be claimed? Below is the Section of law dealing with infrastructure credits, it's not clear to me. (R. p. 339)

The auditor and his supervisor then consulted with SCDOR's legal department, and SCDOR subsequently denied the credits. This dispute followed:

STANDARD OF REVIEW

Tax appeals to the ALC are subject to the Administrative Procedures Act *Long Cove Home Owners' Ass'n v Beaufort Cnty Tax Equalization Bd*, 327 S C 135, 139, 488 S E 2d 857 860 (1997) Accordingly, review of the ALC decision is governed by S C Code Ann § 1-23-380(5) (Supp 2010), which states

The court may reverse or modify the decision if substantial rights of the appellant have been prejudiced because the administrative findings, inferences, conclusions, or decisions are

(a) in violation of constitutional or statutory provisions,

* * *

(d) affected by other error of law,

(e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record, or

(f) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion

As the South Carolina Supreme Court recently stated in *Media General v South Carolina Department of Revenue*, 388 S C 138, 144, 694 S E 2d 525, 27-28 (2010)

Rule 56(c) of the South Carolina Rules of Civil Procedure provides a motion for summary judgment shall be granted “if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law” Rule 56(c), SCRCP, *see also* ALC Rule 68 (stating the South Carolina Rules of Civil Procedure may be applied in proceedings before the ALC to resolve questions not addressed by the ALC rules) A reviewing court may reverse the decision of the ALC where it is in violation of a statutory provision or it is affected by an error of law S C Code Ann §1-23-610(B)(a), (d) (Supp 2009)

Questions of statutory interpretation are questions of law, which the appellate court may decide without any deference to the court below *CFRE, LLC v Greenville Co Assessor*, 395 S C 67, 74, 716 S E 2d 877, 881 (2011) (*citing City of Rock Hill v*

Harris, 391 S C 149, 152, 705 S E 2d 53, 54 (2011))

In addition, except for the reordering of several paragraphs, the ALC adopted the SCDOR's proposed order practically verbatim (*Compare* SCDOR's Proposed Order, R pp 352-68, *with* ALC Order, R pp 3-21) When a lower court adopts the prevailing party's proposed order verbatim, that order is entitled to lower deference and may be subjected to increased scrutiny on appeal *See Anderson v City of Bessemer*, 470 U S 564, 572-73 (1985), *United States v Marine Bancorporation, Inc* , 418 U S 602, 615, n 13 (1974), *Flowers v Crouch-Walker Corp* 552 F 2d 1277, 1284 (7th Cir 1977), *Bright v Westmoreland Cnty* , 380 F 3d 729, 731-2, (3d Cir 2004), and *Holsey v Armour & Co* , 683 F 2d 864, 866 (4th Cir 1982)

ARGUMENTS

I THE ALC ERRED AS A MATTER OF LAW BY CONCLUDING THAT THE CORPORATE AFFILIATES OF CENTEX WERE NOT ELIGIBLE TO CLAIM THE INFRASTRUCTURE TAX CREDIT AS PARTNERS OF THE CENTEX HOMES PARTNERSHIP

A The Clear and Plain Language of the Statute Allows the Corporate Affiliates of Centex to Claim the Infrastructure Tax Credit

1 In General

As the Supreme Court recently stated in *Media General*,

“The cardinal rule of statutory construction is to ascertain and effectuate the intent of the legislature ” “The determination of legislative intent is a matter of law ” “Where the statute’s language is plain and unambiguous, and conveys a clear and definite meaning, the rules of statutory interpretation are not needed and the court has no right to impose another meaning ” The best evidence of intent is in the statute itself “What legislature says in the text of the statute is considered the best evidence of the legislative intent or will Therefore, the courts are bound to give effect to the expressed intent of the legislature ”

388 S C at 147-48, 694 S E 2d at 529 (citations omitted) Additionally, where the Legislature defines statutory terms, those definitions “are generally binding on the court and

should prevail ” *Brown v Martin*, 203 S C 84, 26 S E 2d 317, 320 (1943)

In the context of a tax statute, it is a settled rule that ambiguities are resolved “against the government and in favor of the taxpayer ” *See Hadden v S C Tax Comm’n*, 183 S C 38, 46-47, 190 S E 249, 251 (1937) (noting that “where a tax statute is ambiguous or is reasonably susceptible of an interpretation that would exclude the person or subject sought to be taxed, any substantial doubt must be resolved against the government in favor of the taxpayer”), *see also Clark v S C Tax Comm’n*, 259 S C 161, 169, 191 S E 2d 23, 26 (1972) (“Revenue laws are generally construed in favor of the taxpayer and against the taxing authority”), and *Sutherland Statutory Construction* § 66 1 (6th ed)

Admittedly, the general rule is that tax credits and exemptions are a matter of legislative grace and are strictly construed against the taxpayer *M Lowenstein & Sons, Inc v S C Tax Comm’n* 277 S C 561 290 S E 2d 812 (1982) However, as the Supreme Court recently stated in *CFRE*

“This rule of strict construction simply means that constitutional and statutory language will not be strained or liberally construed in the taxpayer’s favor It does not mean that we will search for an interpretation in [the SCDOR]’s favor where the plain and unambiguous language leaves no room for construction ” It is “[o]nly when the literal application of the statute produces an absurd result will we consider a different meaning ”

395 S C at 74-5, 716 S E 2d at 881 (*citing State v Sweat*, 379 S C 367, 376, 665 S E 2d 645, 650 (Ct App 2008)) As discussed later, there is no absurd result with respect to the literal application of the statute’s plain language and use of the statutorily defined terms utilized within the Infrastructure Credit Statute

Moreover, the rule of strict construction is not always applied as narrowly as noted above in the general rule when the interpretation of economic tax incentive statutes

is involved (As the ALC correctly noted, the Infrastructure Credit is an economic development incentive) (R p 10) Such statutes, while granting tax credits, should not be so strictly construed against the taxpayer as to defeat or destroy the legislative intent and should further, not frustrate, the policy of rewarding investment and spurring economic development *See Arizona v Capitol Castings Inc* , 88 P 3d 159, 160 (Ariz 2004), *Sharp v Tyler Pipe Indus , Inc* , 919 S W 2d 157, 161 (Ct App Tex 1996) (terms “liberal” and “strict” as applied to statutory construction can be misleading where other principles are at work, construing tax exemption statutes too narrowly could defeat legislative purpose of economic development), *Idaho State Tax Comm’n v Haener Bros* , 828 P 2d 304, 307 (Idaho 1992), and *Amoena Corp v Strickland*, 283 S E 2d 894, 897 (Ga 1981) (construing the Georgia sales tax exemption for machinery and equipment in which the Georgia Supreme Court stated that “it is true that tax exemptions are to be strictly construed against the taxpayer and doubts resolved in favor of taxability However, this should not impinge on the other rule that a statute is to be construed in accordance with its real intent and meaning and not so strictly as to defeat the legislative purpose ” 283 S E 2d at 897)

Indeed, in its Technical Advice Memorandum (TAM) 89-14, the SCDOR stated this rule of statutory construction with regards to the Infrastructure Tax Credit

It is ambiguous whether the language “any one infrastructure project” means that only one project may qualify for the credit per year or whether the credit is merely limited to 50% or \$10,000 of expenses paid Many South Carolina cases have held that tax statutes are not to be extended beyond the clear import of their language, *and any substantial doubt as to its meaning is to be resolved in favor of the taxpayer* (*Southeastern Fire Ins Co v South Carolina Tax Commission* 253 S C 407, 171 S E 2d 355 (1969), *Deering Milliken Inc v South Carolina Tax Commission*, 257 S C 185, 184 S E 2d 711 (1971))

It therefore appears that the appropriate interpretation of this statute should be the one most favorable to the taxpayer Section 12-7-1250(A) should thus be construed to mean that a taxpayer is not limited to the number of projects which will qualify for the credit

S C TAM 89-14 (emphasis added)

The South Carolina Supreme Court has previously recognized the importance of economic development incentives in a number of sales and property tax exemption cases. In one case dealing with a sales tax exemption, the Court noted that the purpose of exempting the purchase of machinery is “to promote new industry within the State and encourage expansion of present industry” *Southeastern-Kusan, Inc v S C Tax Comm’n*, 276 S C 487, 490, 280 S E 2d 57, 59 (1981), *see also Hercules Contractors & Engineers v S C Tax Comm’n*, 280 S C 426, 435, 313 S E 2d 300, 306 (Ct App 1984), and *Anon Corp v S C Dep’t of Rev*, 99 ALJ-17-0153 (1999) (noting that “[c]ourts of other jurisdictions have recognized that construing tax exemption statutes too narrowly could defeat the legislative purpose of such statutes”)

Similarly, in *Duke Power Co v Bell*, 156 S C 299, 301, 152 S E 865, 868 (1930), a county treasurer argued that a statute providing property tax exemptions to manufacturers who located in certain South Carolina counties was unconstitutional. In rationalizing its decision, the Court stressed the importance of tax incentives for attracting manufacturing industry investment. *Id* at 303, 152 S E at 871-72. Further, the Court noted that “[t]he theory of the transaction is that a public benefit will accrue to the town and its inhabitants by the introduction of the business enterprise. The property of a town is benefitted, both in value and income, by the introduction of business, and the consequent increase of inhabitants.” *Id* at 303, 152 S E at 871-72 (quoting *Crafts v Ray*, 22 R I 179, 46 A 1043 (1900))

The SCDOR took a similar position in S C Private Letter Ruling (PLR) 95-3 regarding a similar Title 25 economic development incentive, the Job Tax Credit Act. At that time, as noted in the PLR, the Job Tax Credit was limited to a “[c]orporation” [which] means a business entity which is **subject to** South Carolina taxes as contained in Section 12-7-230 and Chapter 7, Title 38 (Emphasis in original)” S C PLR 95-3

As an S corporation, the taxpayer “paid no corporate level taxes.” *Id.* The PLR nevertheless held the taxpayer was entitled to the credit, stating

In reviewing Code Section 12-7-1220 in its entirety, the legislature intended the job tax credit to be available as an economic incentive to encourage businesses subject to corporate level taxes to expand work forces in South Carolina. Although it is rare that S corporations are subject to corporate level taxes and it is rare that S corporations convert to C corporations, S corporations may earn and carryover a job tax credit.

Id.

Similarly, at issue in S C Rev. Rul. 96-11 was whether an eligible project had to meet the requirements of four--or only one--tax credit provisions in order to be entitled to incentives found in the utility tax credit statute, Section 12-6-3490 (now codified as Section 12-20-105). The statute reads: “(A) Any company subject to a license tax under Section 12-20-100 may apply for a credit against its tax liability for amounts paid in cash to provide infrastructure for a project qualifying for income tax credits under Chapter 6 of Title 12, withholding tax credits under Chapter 10 of Title 12, income tax credits under Chapter 14 of Title 12, *and* fees in lieu of property taxes under Chapter 12 of Title 4.” (Emphasis added.)

In holding that “and” in the statute meant “or” (so that an eligible project only had to satisfy any one of the tax credit provisions), the SCDOR stated

As a general rule, the use of the word “and” within a statute connotes that

all the requirements listed must be met in order to qualify under the statute, while the use of “or” within a statute means that only one of the requirements needs be met in order to satisfy the particulars of the statute. However, when those meanings are inconsistent with the perceived intent of the legislature or the purpose of the legislation itself, “and” has been construed to mean “or”, and “or” has been construed to mean “and”

Section 12-6-3490 of the Code was enacted as part of the South Carolina Rural Development Act of 1996. The stated purposes of the Rural Redevelopment Act include promoting positive economic development momentum in rural areas of the State and encouraging significant incentives to induce capital investment and job creation within rural counties. *To read the provision of Code Section 12-6-3490(A) narrowly to require a project to meet all the requirements listed in the statute would severely limit the number of projects that could qualify and would exclude projects located in eleven of the least developed and underdeveloped counties from qualifying under the statute.*

Id. (emphasis added) (citations omitted)

The clear objective of the Infrastructure Credit Statute is to encourage and reward infrastructure investment in South Carolina. Centex, one of the largest homebuilders in South Carolina, made approximately \$68 million in such infrastructure investments, and the State has received a significant benefit from this infrastructure. Thus, the statute should be construed in a way that furthers its objectives, rewards Centex for making its investment and continues to encourage investments in the State.

2 The Infrastructure Credit Statute

1 In General

The statute at issue is not ambiguous and should be interpreted in accordance with the clear and plain meaning of the language and statutorily defined terms therein. The Infrastructure Credit Statute provides, in pertinent part

(A) *A corporation may claim a credit for the construction or improvement of an infrastructure project against taxes due under Section 12-6-530 or Section 12-11-20 for*

- (1) *expenses paid or accrued by the taxpayer,*
- (2) *contributions made to a governmental entity, or*

(3) contributions made to a qualified private entity in the case of water or sewer lines and their related facilities in areas served by a private water and sewer company

(B) *For expenses paid or accrued by the taxpayer* in building or improving any one infrastructure project

(1) the credit is equal to fifty percent of the expenses *or* contributions,

(2) the credit is limited to ten thousand dollars annually, and

(3) any unused credit, up to a total amount of thirty thousand dollars, may be carried forward three years

(C) For purposes of this section

(1) An infrastructure project includes water lines or sewer lines, their related facilities, and roads that

(a) do not exclusively benefit the taxpayer,

(b) are built to applicable standards, and

(c) are dedicated to public use

* * * *

(D) If an infrastructure project benefits more than *the taxpayer, the expenses of the taxpayer* must be allocated to the various beneficiaries and only those expenses not allocated to the taxpayer's benefit qualify for the credit

(E) The credit may be claimed before dedication or conveyance if the *taxpayer submits* with its tax return a letter of intent signed by the chief operating officer of the appropriate governmental entity or qualified private entity stating that upon completion the governmental entity or qualified private entity shall accept the infrastructure project for the appropriate use

(F) *A qualifying private entity* is not allowed the credit provided by this section for expenses it incurs in building or improving facilities it owns, manages, or operates

* * * *

(H) *A corporation which files or is required to file a consolidated return is entitled to the income tax credit allowed by this section on a consolidated basis. The tax credit may be determined on a consolidated basis regardless of whether or not the corporation entitled to the credit contributed to the tax liability of the consolidated group*

S C Code Ann § 12-6-3420 (1976) (emphasis added)

Section 12-6-3420 accordingly requires (1) a corporation to claim the credit on its corporate income tax return, (2) for expenses paid by the taxpayer, or contributions made to a governmental entity or a qualified private entity, (3) in building or improving an infrastructure project. There is no disagreement over the first and the third

requirements

The disagreement solely focuses on the second requirement. The Appellant maintains that the expenditures made by the general partnership, Centex Homes, satisfied the second requirement. (In other words, the partnership earned the credit by paying the qualifying expenditures and contributions of the resulting infrastructure projects were made allowing the corporate partners to claim the credit.) The SCDOR maintains that the expenditures must be directly made by the corporation filing the tax return which claims the credit. (In other words, the corporation must earn the credit by cutting the checks to the contractors who performed the road and sewer work in order to claim the credit.) This is the dispute.

While South Carolina has no true record of legislative intent, it is clear from the statute itself that its purpose is to encourage development and investment in the state by defraying a portion of the cost incurred by real estate developers for making public infrastructure improvements (road, water and sewer) that historically would have been borne by state (e.g., S.C. Department of Transportation) or local government (e.g., county, city, water and sewer authority). Of course, the government benefits from receiving the “free” public infrastructure and from the enhanced tax base. (And the credit is indeed partial, the appellant expended some \$68 million for public infrastructure in return for a \$5 million potential credit.) In what appears to be the only published decision on the Infrastructure Credit, *Anonymous Corporation v. South Carolina Department of Revenue*, 98-ALJ-17-0533 (1999), the ALC noted

13 The Taxpayer’s development of these subdivisions substantially contributed to Lexington’s growth, helping to increase disposable income, attract new businesses and employers and expand the property tax base

* * * *

18 The Taxpayer's infrastructure projects benefited the communities in which they were constructed by contributing to the growth of the community, thereby increasing disposable income, attracting new businesses and employers and expanding the property tax base

ii Appellant, as a Corporate Taxpayer, May Claim the Credit

The parties agree that the Infrastructure Credit Statute requires a corporation to claim the credits against corporate income taxes. It clearly so states "[a] corporation may claim" an infrastructure credit against corporate income taxes. In this case, Appellant, a corporation that owns Centex Homes, has claimed the credit in its consolidated income tax return against its South Carolina corporate income taxes thus satisfying the plain language and meaning of the statute.

iii Centex Homes, a Partnership, May Earn the Credit as a "Taxpayer" (a Statutorily Defined Term)

The Infrastructure Credit Statute provides that a corporation may claim a credit for "expenses paid or accrued by the taxpayer." S.C. Code Ann. § 12-6-3420(A)(1). The ALC's Order is premised almost entirely on its finding that "'the taxpayer' in subsection (A)(1) is limited to the 'corporation' attempting to claim the credit, as referred to in subsection (A)." (R. p. 11). The infrastructure tax credit statute, itself, however, clearly indicates this is not the case in at least one instance. Subsection (F) of Section 12-6-3420 states: "A qualifying private entity is not allowed the credit provided by this section for expenses it incurs in building or improving facilities it owns, manages, or operates." The "qualifying private entity" referred to in subsection (F) includes an electric cooperative. Section 12-20-105 provides a tax credit for entities which pay license taxes under Section 12-20-100. As the section title to Section 12-20-100 notes, this is a "[l]icense tax on

utilities and electric cooperatives ” Section 12-20-105(D) provides virtually the identical “anti-double dip” language as Section 12-6-3420(F) In addition, Section 12-20-105(G) states that “[f]or South Carolina income tax and license purposes, a company that claims the credit allowed by this section is ineligible to claim the credit allowed by [the infrastructure credit] ”

Section 12-6-3420(F) of the infrastructure credit presumably uses the words “qualifying private entity” instead of “corporation” given that cooperatives (unlike investor owned utilities) are not incorporated in the same manner as traditional corporations, *see* S C Code Ann § 33-45-10 et seq , and are subject to different tax treatment than traditional corporations under both state and federal tax law

Electric Cooperatives do not pay corporate income taxes based on Section 33-49-120 For this limitation to have any meaning it is clear that the statute is limiting a cooperative--which made expenditures on property which it manages or operates—from passing the credit onto a parent corporation with a corporate income tax liability

The term “taxpayer” was also not limited by the Administrative Law Court in the only published decision dealing with the infrastructure credit, *Anonymous Corporation v South Carolina Department of Revenue*, 98-ALJ-17-0533 (S C Admin Law Judge Div 1999) The ALC noted in it Finding of Facts

The taxpayer is a conglomerate which files a consolidated corporate tax return annually with the State of South Carolina

At all times relevant to this case, *one of the taxpayer s subsidiaries* was in the business of developing real estate for profit This business was included in the taxpayer’s consolidated return filings *For purposes of this contested case this business shall also be referenced as Taxpayer ”*

Id (emphasis added) Accordingly, it is clear that the entities making the infrastructure

expenditures were not the parent corporation filing the return (but rather they were part of the consolidated group) The SCDOR did not challenge this issue before the ALC

Title 12, Chapter 6 contains some 37 business tax credits, including the Infrastructure Credit Chapters 10, 14 and 15 contain additional business tax credits The majority of the business tax credits including the Infrastructure Credit, are found in Title 12, Chapter 6, Article 25 Article 25 starts with South Carolina's pass through statute, section 12-6-3310, which provides that unless "specifically prohibited," S corporations, LLCs and partnerships may pass through tax credits to shareholders, members and partners The word "taxpayer" (singular and plural) is used 381 times in Article 25 (Indeed, the Job Tax Credit Act, section 12-6-3360, alone uses the word "taxpayer" some 27 times)

"Taxpayer" is a statutorily defined term that "unless otherwise required by the context" means " an individual, trust, estate, *partnership*, association, company, corporation or any other entity subject to the tax imposed by this chapter or required to file a return " S C Code Ann § 12-6-30(1) (emphasis added) This definition applies with respect to reading and interpreting the statutes under Title 12

The word "taxpayer" is a term of art and was used with precise intentions by the Legislature Had it wanted to limit the entities or taxpayers that "qualify" for the credit to be just corporations, the Legislature could have and would have simply used the term "corporation" consistently throughout Section 12-6-3420 such that, for example, the first paragraph would read as follows

A corporation may claim a credit for the construction or improvement of an infrastructure project against taxes due under § 12-6-530 or § 12-11-20 for expenses paid or accrued by the taxpayer corporation,

However, the Legislature chose not to use the word "corporation" in certain

specific sections of the statute for specific reasons (and there are many reasons why it would make sense to do so)

As the Supreme Court very recently stated in *CFRE LLC v Greenville County Assessor*

However, “the statute must be read as a whole and sections which are part of the same general statutory law must be construed together and each one given effect” *S C State Ports Auth v Jasper County*, 368 S C 388, 398, 629 S E 2d 624, 629 (2006) We therefore should not concentrate on isolated phrases within the statute *Id* Instead, we read the statute as a whole and in a manner consonant and in harmony with its purpose *State v Sweat*, 379 S C 367, 376, 665 S E 2d 645, 650 (Ct App 2008), *aff’d* 386 S C 339, 688 S E 2d 569 (2010) In that vein, we must read the statute so “that no word, clause, sentence, provision or part shall be rendered surplusage, or superfluous,” *id* at 377, 665 S E 2d at 651, for “[t]he General Assembly obviously intended [the statute] to have some efficacy, or the legislature would not have enacted it into law” *id* at 382, 665 S E 2d at 654

395 S C 67, 74, 716 S E 2d 877, 881 (2011)

Additionally, a careful analysis of when and why the Legislature used “taxpayer” versus when it used “corporation” in the Infrastructure Credit Statute reveals a clear and obvious theme which is indicative of the Legislatures intentions “Corporation” is used in subsection (A) providing for the type of entity that can “claim” the infrastructure credit, and it is used again later in subsection (H) to explain that “[a] corporation which files or is required to file a consolidated return is entitled to the income tax credit allowed by this section on a consolidated basis” and that the tax credit may be determined on a consolidated basis regardless of whether or not the corporation entitled to the credit contributed to the tax liability of the consolidated group And lastly, “corporation” is used in subsection (I) to explain that unused credits can be transferred to a succeeding corporation in instances of merger, consolidation or reorganization of a corporation

where tax attributes survive

“Taxpayer,” a term with broader meaning (which includes partnership), is used by the Legislature to explain which entities qualify for the infrastructure credit and what those entities must do in order to earn (or generate) the credit. Subsection (A)(1) states that the infrastructure costs must be “paid or accrued by the taxpayer” and further explains certain limitations, in subsection (B) where the term “taxpayer” is used again, regarding the “expenses paid or accrued by the taxpayer” in building or improving any one infrastructure project. In subsections (C) and (D), the Legislature explains (again using the term “taxpayer”) that the credit is only available for expenses paid or accrued that “do not exclusively benefit the taxpayer, are built to applicable standards, and are dedicated to public use” and “[i]f an infrastructure project benefits more than the taxpayer, the expenses of the taxpayer must be allocated to the various beneficiaries and only those expenses not allocated to the taxpayer's benefit qualify for the credit.” The last phrase in subsection (D)—“only those expenses not allocated to the taxpayer's benefit qualify for the credit”—emphasizes the point made here that the Legislature clearly intended (specifically provided via its articulate use of “corporation” and “taxpayer”) that a taxpayer may **earn** by way of qualifying for the credit as provided here in subsection (D) in contrast to subsection (A) where the Legislature limited which entities could **claim** the credit stating “[a] corporation may claim a credit.”

Thus, after analyzing the placement and use of the term “taxpayer” and “corporation” throughout Section 12-6-3420, the Legislature's reason for using “taxpayer” in certain portions and “corporation” in others becomes quite obvious—it used the broader term “taxpayer” (as defined by Section 12-6-30(1)) when it needed to

focus on the entity making an expenditure or taking an action related to the project itself whereas it used “corporation” only when it needed to focus on the entity actually claiming, repaying, or transferring the credit

The ALC states that “in order for this Court to apply the definition of Section 12-6-30(1) to the infrastructure credit’s inclusion of the word ‘taxpayer,’ each of the entities enumerated therein must be a feasible substitution. This inevitably leads to absurd results, since portions of the Petitioner’s proposed interpretation of ‘taxpayer’ would be meaningless (i.e., an individual could make qualifying expenditures yet the credit could not be claimed)” (R p 35). However, applying the statutory definition of “taxpayer” as used in the infrastructure credit statute does not produce such an absurd result. While an individual or trust could make the qualifying expenditures, neither could claim the credit because neither pays tax “under Section 12-6-530 or Section 12-11-20” (as required under Section 12-6-3420). In other words, they could meet part but not all of the statutory requirements. On the other hand, a partnership can incur the qualifying expenditures and dedicate the infrastructure project to public use thereby earning or generating the credit, and then, by operation of the partnership pass-through provisions, those qualifying expenditures or the infrastructure credit itself is passed through to its corporate partners to be claimed against a corporate income tax liability under both the federal and South Carolina tax statutes.

Because the plain language of the statute expressly allows a partnership like Centex Homes (a “taxpayer”) to earn the credit and the corporate partners (or a parent company with respect to a consolidated tax return) to claim the credit, “the Court has no right to impose another meaning.” *Hodges v. Rainey*, 341 S.C. 79, 85, 533 S.E.2d 578, 581

(2000) The restrictive use or failure to use the statutory definition of the term “taxpayer” in this Statute, where there is no such restriction nor absurd results, would render it superfluous and allow for the opportunity to restrict or fail to use the statutory definition throughout the South Carolina Code

Also of relevance is S C Rev Rul 97-8 which dealt with the Economic Impact Investment Tax Credit. At issue was whether a taxpayer must be an “economic impact zone business” (which was narrowly defined in former Section 12-14-70) in order to be eligible for the economic impact zone investment tax credit under Section 12-14-60 (Such a conclusion would have greatly limited the number of businesses which qualified for the investment tax credit.) In holding it did not, the SCDOR stated

The general rule of statutory construction is that nothing can be read into a statute which is not within the intent of the legislature as gathered from the statute itself. Where the language of a statute is clear and leaves no room for doubt as to the intention of the legislature, there is no authority to add or take away from the language in the statute. Another rule of statutory construction is that a condition or restriction should not be implied if the right granted by the statute is unrestricted and *it will be presumed that the legislature did not intend to restrict the use of the statute to a particular class of persons or things when it has included in the general language of the statute a number of persons or entities without limitation*

Id. (emphasis added and citations omitted)

In this vein, the infrastructure statute uses the word “taxpayer” eight times without limitation. Incidentally, the South Carolina Supreme Court in *Media General v South Carolina Department of Revenue*, 388 S C 138, 694 S E 2d 525 (2010), very recently dealt with the definition of “taxpayer” contained in Section 12-6-30(1). The Supreme Court rejected the SCDOR’s interpretation that the statute’s reference to “corporation” (in the singular) prevented two or more corporations from filing a combined unitary return under Section 12-6-2320(A)(4). *See id.* at 148-49, 694 S E 2d at

3 **The Doctrine of *In Pari Materia* Supports Allowing Centex Homes to Pass Through Credits**

Although the Appellant believes its interpretation is clear when viewing the Infrastructure Credit Statute and the Pass-Through Statute separate and apart from one another, the Appellant's interpretation is buttressed when the statutes are read together as the doctrine of *in pari materia* requires. This doctrine provides that statutes that address the same subject matter must be construed together to achieve the intent of the Legislature. See *Grant v. City of Folly Beach*, 346 S.C. 74, 79, 551 S.E.2d 229, 231 (2001) ("It is well-settled that statutes dealing with the same subject matter are *in pari materia* and must be construed together, if possible, to produce a single harmonious result.") The SCDOR in PLR 95-3, quoted this rule in allowing an S corporation to qualify for the Job Tax Credit.

Under the rule of statutory construction of statutes *in pari materia*, statutes are not to be considered as isolated fragments of law, but as a whole, or as parts of a great, connected homogenous system. Such statutes are considered as if they constituted but one act, so that sections of one act may be considered as though they were parts of the other act, as far as this can reasonably be done. Indeed, as a general rule, where legislature dealing with a particular subject consists of a system of related general provisions indicative of a settled policy, new enactments of a fragmentary nature on that subject are to be taken as intended to fit into the existing system and to be carried into effect conformably to it, unless a different purpose is shown plainly, 73 Am Jur 2d *Statutes* Section 188.

The Infrastructure Credit Statute and the Pass-Through Statute address the same subject matter, i.e. the earning and claiming of credits in the case of the Infrastructure Credit Statute and the earning and passing through of credits in the case of the Pass-Through Statute. Thus, these statutes must be construed together to achieve the intention of the Legislature. (In addition, the incentives pass-through statute was codified as the

first section of Article 25)

As previously stated, the purpose of the Legislature in enacting the Infrastructure Credit Statute was to incentivize and reward infrastructure expenditures in South Carolina, the purpose of the Pass-Through Statute is to codify the ability of a pass-through entity to pass credits through to its partners unless a given credit statute specifically prohibits it from doing so. The Infrastructure Credit Statute states that a corporation may “claim the credit” and the Pass-Through Statute states that a partnership that “qualifies for the credit” by making qualifying infrastructure expenditures can pass through the “credit earned” to its corporate partner. The only interpretation of the wording in these statutes that is consistent both with the language therein and the purposes thereof is the phrase “expenses paid or accrued by the taxpayer” in the Infrastructure Credit Statute means expenses paid or accrued by the applicable pass-through entity, the language in the Pass-Through Statute referencing a partnership that “earned” the credit clearly indicates that a partnership can “earn” or “generate” a credit and pass it through to its partners unless the particular credit statute specifically prohibits it, and the language in the Pass-Through Statute “that qualifies for the credit” means the entity that makes the required expenditures and contributes (i.e., dedicates or conveys) the property to public use. There is no question in this case that the taxpayer, a partnership, made qualified expenditures and contributed the resulting infrastructure projects to local municipalities on behalf of its corporate partners and therefore earned the credit and that a corporation eligible to claim the credits did in fact claim them “against its taxes due under § 12-6-530.” See S.C. Code Ann. § 12-6-3420(A).

The ALC erred in its finding that the word “claim” and “generate” have identical

meanings and are used synonymously by the Legislature. It is undisputed that these words are defined differently in any dictionary. In addition, the Legislature demonstrates that these terms have different meanings by their articulate use of these terms including not only “claim” and “generate,” but also “qualifies,” “pass through” and “earned” all of which are artfully utilized in Sections 12-6-3310 and 12-6-3420.

In reaching its conclusion, the ALC mistakenly relies upon SCDOR’s assertion that it has a long-standing policy of interpreting credit statutes to require that the entity that generates the credits be the same one that claims the credits (R. p. 11).

This appeal was instituted through the issuance of a Final Agency Determination (FAD) by the SCDOR. Although the SCDOR’s FAD stated that “[a]bsent a statutory provision stating otherwise, the general rule is that tax benefits *may only be claimed by the taxpayer that generated the credit*” (Emphasis in original) (R. p. 117), it provided no citation or authority for such “general rule,” nor did it claim (unlike the ALC) that this was the SCDOR’s long standing Agency interpretation. Certainly the SCDOR has not promulgated a Regulation or issued a policy document to this effect. Indeed, in what is apparently the only written SCDOR pronouncement on the subject, the *South Carolina Tax Incentives for Economic Development Winter Edition 2009*, the rule is just the opposite. The publication states

Except as otherwise provided, a credit must be used by the taxpayer who earns it. *Exception to these rules exist* for the following: (1) taxpayers [like Centex] participating in a consolidated corporate income tax return [and] (2) pass through entities [like Centex Homes] eligible to earn and use a credit.

Id. at 21.

Again the SCDOR publication cites absolutely no authority for this “rule.” While

a Court generally gives deference to an Agency's interpretation of a statute or regulation, *Brown v Bi-Lo, Inc* 354 S C 436, 581 S E 2d 836 (2003), the SCDOR cites no statute or regulation in support of the rule. Incidentally all three SCDOR witnesses admitted that the SCDOR had no policy, written or otherwise, regarding either the infrastructure credit or the pass through of credits by a partnership (R p 338, page 40, lines 18-23 (Donovan), R p 341-42, page 69, line 8 - page 70, line 5 (Sharpe), and R p 344, page 43, line 18 - Page 44, line 19 (Swearingen)) "Secret" rules asserted by agency staff which have not been promulgated in regulations or binding policy documents are entitled to little, if any, deference. See S C Tax Comm'n Dec 93-78 (rejecting taxpayer's use of longstanding agency interpretation stating that, "we do not believe there are any generally accepted consolidation rules which exist *if they are not codified*," (emphasis added), S C Tax Comm'n Dec 94-90 (likewise rejecting the taxpayer's "longstanding administrative policy," argument, stating "it is important to note that there are no Commission decisions or Department approved policy documents which support that [Department] decision"), *Seigfried v S C Dep't of Rev* 2003 WL 24004736 (S C Admin Law Judge Div 2003), *S C Dep't of Motor Vehicles v Laquenesse* 2008 WL 1740063 (S C Admin Law Judge Div 2008), *Coastal Conservation League v S C Dep't of Health & Envtl Control*, 363 S C 67, 610 S E 2d 482 (2005), and *Clarendon Cnty Mem Hosp v S C Dep't of Health & Envtl Control*, 2006 WL 1430090 (S C Admin Law Judge Div 2006).

Additionally, the ALC decision primarily relies on *Bell Atlantic Nynex Mobile Inc v Commissioner of Revenue Services* 273 Conn 240, 869 A 2d 611 (2005), wherein corporate partners of a partnership attempted to claim a tax credit for payment of personal property taxes by the partnership on electronic data processing equipment. The ALC

Order is premised on the fact that the Connecticut statute was a “similarly worded credit provision” to the South Carolina statute (R p 17) The Connecticut Statute, however, contains two significant differences

(i) Comparison of CT vs SC statutes regarding Payment

Connecticut

“Thus the text of the statute indicates that the legislature intended to grant eligibility for the 212-217 tax credit to a ‘taxpayer’ *who has paid the personal property taxes* on the electronic data processing equipment ” 869 A 2d at 620 (Emphasis added)

South Carolina

“Expenses paid or accrued by the taxpayer”

(ii) Comparison of CT vs SC statutes regarding the definition of “Taxpayer”

Connecticut

“[A] corporation, foreign municipal electric utility [and other utility entities]”

South Carolina

“ ‘Taxpayer’ includes an individual, trust, estate, partnership, association, company, corporation, or any other entity subject to the tax imposed by this chapter or required to file a return ”

In *2004 and 2005 Connecticut Tax Law Developments*, the author, in discussing the *Bell Atlantic* case, states “To the extent it is so applied, the decision presents a trap for the taxpayer unaware that, with respect to credits, Connecticut *does not follow the general rule that partnership expenditures are those of its partners*” John R Shaughnessy, *2004 and 2005 Connecticut Tax Law Developments*, 79 Conn B J 67, 76-77 (2005) (emphasis added) The ALC erred in its application and reliance upon *Bell*

Atlantic, since the statutory definition of “taxpayer” in *Bell Atlantic* was limited to electrical utility corporations who paid personal property taxes on data processing equipment owned by it. The definition did not include partnerships, and thus, a partnership could not pass the credit through to its corporate partners as a matter of Connecticut law, which is not the case under South Carolina tax law.

The ALC Order also relied upon *L&W Construction Co., Inc. v. Wisconsin Department of Revenue*, 149 Wis. 2d 684, 439 N.W.2d 619 (1989), in which a corporation claimed an income tax credit for sales and use tax paid by a partnership in which the corporation was a partner. This case is also readily distinguishable as the Wisconsin credit statute at issue clearly stated:

(2) The tax imposed upon or measured by corporate net income may be reduced by an amount equal to the sales and use tax under ch. 77 paid by the corporation in such taxable year on fuel and electricity consumed in manufacturing tangible personal property in this state. 439 N.W. 2d at 620. *Id.* (Emphasis in original)

By contrast, the South Carolina statute does **not** read “expenses paid by the corporation,” as the SCDOR would like but rather it reads “expenses paid by the taxpayer.”

Lastly, the ALC’s reliance on *Rath v. Commissioner*, 101 T.C. 196 (1993) is misplaced. In *Rath*, an S-corporation sold securities for a loss which was not properly reported on its informational tax return as a pass through item to its shareholders. Similar to the partnership tax rules, both the “Aggregate” and “Entity” theories of taxation are applied to S corporations. That is, I.R.C. Sections 1366(a) and (b) provide that the amount and character of the S-corporation’s reportable items (e.g. income, loss, deduction or credit) is determined at the S-corporation level and, then passed through to

the shareholders as if realized directly from the source from which realized by the S-corporation. However, the individual shareholders of the S-corporation, who were aware of the stock sale transaction, reported ordinary loss on their individual income tax returns.

The individual shareholders asserted that I R C Section 1244 applied allowing them to re-characterize the capital loss to an ordinary loss. Specifically, I R C Section 1244(b) states

In the case of an individual, a loss on § 1244 stock issued to such individual or to a partnership which would (but for this section) be treated as a loss from the sale or exchange of a capital asset shall, to the extent provided in this section, be treated as an ordinary loss.

In making its decision that the individual shareholders were not entitled to report the loss as an ordinary loss, the Tax Court stated

the plain language of section 1244(a) directs that the relief provided therein is limited to individuals and partnerships. Simply stated, ordinary loss treatment is only available where section 1244 stock is issued to an individual or a partnership and then sold by that individual or partnership at a loss. Treas. Reg. 1.1244(a)-1(B).

* * * *

Moreover, where a statute is clear on its face, we require unequivocal evidence of legislative purpose before construing the statute so as to override the plain meaning of the words used therein. *Halpern v Commissioner*, 96 T.C. 895, 899 (1991), *Huntsberry v Commissioner*, 83 T.C. 742, 747-748 (1984).

Rath, 101 T.C. at 200-01.

The basis for the ALC's reliance on *Rath* is not readily apparent because the special deduction statute at issue clearly and unambiguously prohibits corporations from claiming an ordinary loss deduction, whereas a specific prohibition like that found in I R C Section 1244 is not found in the South Carolina Infrastructure tax credit. Moreover, I R C Section 1244 explicitly allows a partnership like Centex to receive

ordinary loss treatment, as characterized and determined at the partnership level, and pass through such deduction to its individual partners. Accordingly, this case supports Appellant's position that partners, who are specified as the type of taxpayer eligible to claim the credit or deduction (e.g., I.R.C. Section 1244 – individuals, S.C. Code Ann. § 12-6-3420 – corporations) may do so via pass through from their partnership investment unless the deduction or credit statute specifically prohibits the partnership, or an S corporation as in *Rath*, from earning such credit or deduction.

The ALC Order also asserts as support of its conclusions that (unlike the infrastructure tax credit) three South Carolina tax credit statutes explicitly provide for pass through provisions for partnerships (R pp 12, 15). The ALC Order cites Sections 12-6-3340, 12-6-3370 and 12-6-3560. While these Sections indeed contain explicit pass through provisions, they provide no support to the SCDOR's arguments as all three were enacted *prior* to the incentives pass through statute, 12-6-3310. Section 12-6-3310 was amended in 2003, 2003 Act No. 69, § 3N, to include partnership pass through treatment. Section 12-6-3340 and Section 12-6-3370 were enacted in 1995 Act No. 76. (Both pass through provisions serve to *limit* the amount of the credit at the partnership level rather than at the partner level (which would result in much higher deductions).) Section 12-6-3560 was enacted in 2004 Act No. 299, but as the Code Commissioner's note to the predecessor statute, Section 12-6-3510, the Section "was derived from 2000 Act No. 399." (Current Section 12-6-3560 was re-codified from Section 12-6-3510, which was "derived" from 2000 Act No. 399.)

Decisions from other authorities are to the contrary. At issue in New York Department of Taxation Advisory Opinion Petition No. C850528A (attached as **Exhibit**

1) was whether Xco, a corporation which was a partner in a partnership, was entitled to the New York investment tax credit “permitted for production equipment not only in situations where Xco directly purchases the equipment but also in situations where the cost or other basis of such equipment passes through from a partnership. Petitioner feels that this result is consistent with analogous situations, such as the treatment of shareholders of S corporations and individual partners of a partnership, and conforms with the general pattern for taxing a corporate partner on its allocable share of partnership items.” *Id*

The Department of Taxation allowed the credit, stating

[A] strict interpretation of Section 210 12(b) of the Tax Law, would deny the passthrough to the corporate partner of the principal use of the qualifying property because the partnership is using the property, not the partners

However, in *Symphony Space v Tishelman*, 60 NY2d 33 (1983), the Court of Appeals invoked statutory purpose over the doctrine that tax exemptions are to be strictly construed. It stated

While exemption statutes should be construed against the taxpayer seeking the benefit of the exemption, an interpretation so literal and narrow that defeats the exemption’s settled purpose is to be avoided. *Id* at 36

Id

In *Bordon Chemicals and Plastics, LP v Zehnder*, 726 N.E.2d 73 (2000), an operating partnership purchased certain assets which gave rise to replacement tax investment credits for years 1988 and 1989. However, the operating partnership was not entitled to an investment credit because it had no replacement tax liability, which the investment credit offset. Plaintiff, however, was subject to the Illinois personal property tax (replacement tax). Plaintiff claimed that, under these circumstances, it was entitled to use the Operating Partnership’s replacement tax investment credit. The Department

rejected this claim because the assets that generated the investment credit were owned by the Operating Partnership, not the plaintiff, which owned no assets in Illinois. As the Court noted, the tax credit section did not explicitly provide at the time whether pass through of the investment credit from partnerships to partners was allowed or disallowed, nor did the statute expressly prohibit pass through. *Id.* at 82. The Statute was silent. *Id.*

The Court held for the plaintiff, stating

Our decision comports with the rule of statutory construction that a court, in construing a statute, presumes that the legislature did not intend absurd, inconvenient or unjust results. Under the present situation in view of the subtraction modification required by section 203(D)(2)(1), the operating partnership will never incur a replacement tax liability, and can never utilize the investment credit generated by the investment in qualified property. If, in spite of the shift of the Operating Partnership's replacement taxation to the plaintiff, the plaintiff is not allowed to utilize the investment credit that leaves the credit unusable by any taxpayer. We believe such a result to be unreasonable and, not one intended by the legislature.

Id. at 83-4 (citations omitted)

4 "Qualifying Expenditures" were Paid and Infrastructure Projects were Contributed for Public Use

Centex Homes spent approximately \$68 million in South Carolina developments on roads and water and sewer lines, which CREC, the managing general partner of Centex Homes, then contributed to local municipalities. Accordingly, Centex Homes (which as just discussed is a "taxpayer" as defined within S.C. Code Ann. § 12-6-30(1) and I.R.C. § 7701(a)) and its corporate partners *qualify* for the tax credit pursuant to the Infrastructure Credit Statute by satisfying each of its requirements as follows:

- 1) Centex Homes made qualifying expenditures related to water lines, sewer lines or roads,
- 2) Said expenditures for infrastructure projects benefited the local community as a whole and were built to applicable standards, and

- 3) CREC, (as managing general partners acting on behalf of Centex Homes and the other general partners) dedicated the properties to public use by contributing the infrastructure projects to local municipalities in South Carolina

That the above requirements were met is undisputed

B The Corporate Partners of Centex are Entitled to the Infrastructure Tax Credit Based on the Application of South Carolina's Pass Through Statutes

South Carolina has two pass-through statutes or regimes which serve to pass through the expenditures made by the General Partnership, Centex Homes, to the corporate partners and then, (through South Carolina's consolidated return statute) onto the Appellant's tax return. The first of these regimes is the general taxation of partnerships in South Carolina. The second is the tax statute adopted by the General Assembly to explicitly pass through economic development tax credits. Both are discussed below, and the application of either (or both) allows the Appellant to use the Infrastructure Credits.

1 General Federal Partnership Tax Rules Adopted by State Law Allow Centex to Pass Through Earned Tax Credits to its Corporate Partners

As previously stated, it is undisputed that the Centex Homes partnership made expenditures for qualifying infrastructure projects contemplated by the Infrastructure Credit Statute. For both federal and state purposes, partnerships like Centex Homes are "pass-through" entities, meaning that they are not subject to income tax but rather their income, deductions and credits pass through the partnership to its partners. *See* I R C § 701 et seq. South Carolina adopts the I R C's provisions for determining the taxation of partnerships. *See* S C Code Ann. §§ 12-6-40 (2000 & Supp. 2010), 12-6-50 (2000 &

Supp 2010) and 12-6-600 (2000) More specifically, the SCDOR publication, *South Carolina Tax Incentives for Economic Development Winter Edition 2009* states

Partnerships are not subject to South Carolina income tax under South Carolina Code §12-6-600 The gross income, adjusted gross income, and taxable income of a partnership and its partners are determined in accordance with applicable provisions of the Internal Revenue Code Partners include in their South Carolina taxable incomes their proportionate share of the partnership's South Carolina taxable income

Id at 5

“South Carolina has adopted all of the partnership and corporate provisions (subchapters K, C and S) of the Internal Revenue Code and Internal Revenue Code Section 7701 which defines “partnership” and “corporation ”” S Barnes, J Burkhardt, R Handle, B Maybank, M McWilliams & D Merline, *South Carolina Limited Liability Companies and Limited Liability Partnerships* (S C Bar 3d ed)

Accordingly, for both federal and South Carolina income tax purposes, a partnership computes its income from an active trade or business in the same manner as other taxpayers See § 12-6-600, I R C § 702(a)¹ The net income or loss is then distributed among the partners See I R C section 704

As stated above, Appellant is a corporation which claimed the infrastructure credit on its South Carolina consolidated return The qualifying expenditures for the public infrastructure were made by a general partnership, Centex Homes, whose 3 partners were corporate subsidiaries of Centex International, Inc I R C Section 702(b) provides that the “character of any item of income, gain, loss, deduction or credit included in a

¹ I R C §§ 701 – 703 IRC § 703(a) provides that a partnership must separately compute its taxable income or loss where the computation is based upon the same principles used to calculate an individual s taxable income See I R C §61 and 162 for determination of gross income and trade or business expenses relative to computing a taxpayer s taxable business income See also Instructions to Form 1065, pp 1 15 19

partner's distributive share **shall be determined as if such item were realized directly from the source from which realized by the partnership, or incurred in the same manner as incurred by the partnership**” I R C Section 702(b) (emphasis added) South Carolina, as previously discussed, has adopted the federal rules regarding the taxation of partnerships Thus, I R C Section 702(b) dictates that the credits earned by Centex Homes (the partnership) be treated as if the corporate partners earned those credits themselves

S C Rev Rul 97-7 states

Code Section 12-6-600 addresses the taxation of partnerships and reads

An entity treated as a partnership for federal income tax purposes is not subject to tax under this chapter Each partner shall include its share of South Carolina partnership income on the partner's respective income tax return All of the provisions of the Internal Revenue Code apply to determine the gross income, adjusted gross income, and taxable income of a partnership and its partners, subject to the modifications provided in Article 9 of this chapter and subject to allocation and apportionment as provided in Article 17 of this chapter

The law provides that each partner is directly taxable on his distributive share of partnership income Items of income, such as personal service income received from a partnership performing legal or accounting services, are separately stated and passed through to the partners *Such items retain their character at the partner level and are treated as if realized by the partner directly from the source from which realized by the partnership* See *Ellis v South Carolina Tax Commission*, 280 S C 65, 309 S E 2d 761 (1983)

(Emphasis added)

Two South Carolina cases dealing with income tax deductions by partnerships are to the same effect (These cases also illustrate that our pass through statute is not exclusively “pro-taxpayer” The statute also operates to disallow deductions as well)

Dalton v S C Tax Commission, 295 S C 174, 367 S E 2d 459 (1988), and *Ellis v S C Tax Commission*, 280 S C 65, 309 S E 2d 761 (1983), both utilized the general partnership pass through statute now codified at Section 12-6-600 to disallow deductions. In *Ellis*, the Supreme Court disallowed deductions on an individual income tax return which were incurred by the taxpayers from out-of-state limited partnerships. The Court first noted that “[p]artnerships and limited partnerships are not taxed on their income or losses. Although a partnership files an informational return, the income or losses must be passed through and distributed to the individual partners for separate inclusion or deduction in their individual tax returns.” *Id.* at 68, 309 S E 2d at 762. The Court then stated:

The “pass through” rule is equally applicable to limited partnerships. Section 12-7-300 makes no distinction between a general or limited partnership. By reason of the “pass through” rule, the character of any item of income, gain, loss, deduction or credit included in a partner’s distributive share of gains and losses shall be the same as if such item was realized directly from the source from which realized or incurred by the partnership. In other words, *each item of income, gain, loss, deduction or credit is treated as if it were realized or incurred by the partner directly from the source without ever having passed through the partnership.* If this were not the case, then partners in real estate or other business ventures could not take advantage of depreciation write-offs and other operating expenses or losses.

Id. at 68, 309 S E 2d at 762-63 (emphasis added)

The Court in *Dalton* referring to the nearly identical *Ellis* decision, similarly stated: “The Court found that the loss deduction of the partnership *was treated as if it were incurred by the partners directly* from the source with the source being out-of-state income not taxable in South Carolina.” 295 S C 174, 180, 367 S E 2d 459, 462 (1988) (emphasis added). It bears repeating that the three partners of Centex Homes were corporations, which reported tax deductions for qualifying infrastructure expenditures as

well as income generated from such expenditures in a consolidated corporate income tax return

As noted on the SCDOR's website, "South Carolina taxable income of a partnership is the same as for federal partnership income tax purposes with certain South Carolina modifications. Taxable income (loss) of a partnership flows through and is taxable to the partners in the same manner as for federal partnership income purposes"²

Additionally, commentators have addressed this issue, noting

Owners of pass-through entities must learn their particular states rules with respect to the use of income tax credits generated by the entity. *In states that do not tax the entity itself [such as South Carolina] the entity's credits presumably will flow through to the owners*

The state's tax forms should be one of the first items reviewed. For example, federal Schedules K-1 indicate that income, deductions, and credits are to be taken into account by partners and S corporation shareholders. Many states [like South Carolina] have their own Schedules K-1, or comparable forms, that indicate the items to be taken into account by the pass-through entity's owners. If the form has a line to report tax credits, [as stated below South Carolina does] it is likely that the credits pass through. The forms generally reflect the state revenue department's position as to the tax treatment of a particular item. Tax forms do not carry the same authoritative weight as statutes but may have the same weight as a regulation

David A. Hughes & C. Eric Fader, *Pass-Through Entities and Tax Credits Don't Lose the Opportunity*, J. Multistate Tax'n & Incentives, June 1999, at 31 (emphasis added)

The partners of a partnership in South Carolina annually receive a SC 1065 K-1 (attached as **Exhibit 2**). As the instructions to this form state "**Lines 15 through 18** [of the form] list the partner's share of applicable South Carolina Credits" (emphasis in original)

² Corporate Income Tax, <http://www.sctax.org/Tax+Information/Corporate+Income+Tax/corpingo.htm>

South Carolina follows the general treatment of partnerships as stated in Hellerstein's State Taxation treatise

Most states follow the basic federal tax structure governing income taxation of partners and partnerships. Under the federal rules, partnerships are treated as conduits and are not themselves subject to tax, but partners are directly taxable with respect to their distributive shares of partnership items of income, gain, loss, deduction, and credit. *As under federal law, partnership items normally retain their character when passed through to the person as though realized directly by the partners from their source*

Jerome R. Hellerstein & Walter Hellerstein, *State Taxation* (3d Ed 2003) § 20.08, p. 20-134 (emphasis added)

2 The Pass-Through Statute was Enacted in Part to Accommodate the Use of Tax Credits and Eliminate Choice of Entity Issues

The Infrastructure Credit was originally passed in 1988. Many of South Carolina's modern tax incentives came into existence at this time. Most large business entities during this time period (and before) were traditional corporations who were taxed as C corporations for state and federal income tax purposes. As a result of passage of various federal tax laws, many entities were subsequently formed (or converted) to other kinds of legal entities (S corporations, partnerships and limited liability companies). The General Assembly reacted to this change by amending the various specific tax credit statutes to include other forms of entities, *see e.g.*, Job Tax Credit Act, Section 12-6-3360(k)(1). This proved to be a laborious chore because of the numerous tax credit provisions, (Title 12, Chapter 6 alone contains 37 business tax credits) and as a result, the General Assembly in 2003, 2003 Act No. 69, adopted a broad pass-through statute, Section 12-6-3310, which allows tax credits to be claimed by any entity except where "specifically prohibited."

In the *Journal of Multistate Taxation*, *supra*, the author states, at the time this

article was written (1991), that

In a majority of the states that impose a tax on partners rather than on the partnerships, the statutes do not expressly provide for a pass through of credits

Nevertheless, despite state statutes' silence as to pass-through of credits, the taxing authorities may interpret the law to allow for pass-through treatment. Such a favorable position may be reflected in regulations, tax forms or official publications

Some states have drafted credit statutes to expressly allow a pass through from partnerships to partners

David A. Hughes & C. Eric Fader, *Pass-Through Entities and Tax Credits: Don't Lose the Opportunity*, J. Multistate Tax'n & Incentives, June 1999, at 34-5 (emphasis added). South Carolina is one such state.

3 Nothing in South Carolina Code Specifically Prohibits the Pass-Through of the Infrastructure Tax Credit by Partnerships under S.C. Code Ann. § 12-6-3310

The Pass Through Statute, S.C. Code Ann. § 12-6-3310, allows Centex Homes to pass through the credits earned to its corporate partners. Note that this Section is the first code section in Article 25, which contains the Infrastructure Credit. The statute reads in part as follows:

SECTION 12-6-3310 Tax credits, time-frame for use, pass through and calculation of shareholder credit, limited liability companies

(A) Credits allowed in this article are nonrefundable and may be used only in the year generated unless otherwise provided.

(B)(1) *Unless specifically prohibited*, an "S" corporation, limited liability company taxed as a partnership, or *partnership that qualifies for a credit pursuant to this article may pass through the credit earned to each shareholder of the "S" corporation, member of the limited liability company, or partner of the partnership*

Id. (emphasis added)

The statute states that unless "*specifically prohibited*" a partnership may pass

through a credit for which it qualifies pursuant to this Article (“This Article” is Article 25, which includes the infrastructure credit) This is significant as the exact phrase “specifically prohibited” is found only twice in the state tax code and only ten times in the entire South Carolina Code Even using different versions of the phrase (e g, “specifically prohibits”), it is found only 13 times in the entire South Carolina Code Black’s Law Dictionary defines “specific” as “relating to, or designating a particular or defined thing, explicit ” Black’s Law Dictionary (9th ed 2009) A common dictionary definition similarly defines “specific” as “set forth explicitly definite ” Webster’s II New College Dictionary 1060 (2d ed 2001)

This, of course, begs the question, where does the Infrastructure Credit, explicitly or definitively, prohibit the pass through of the tax credit from a partnership to the corporate taxpayer? Simply put, there is no such specific prohibition (Indeed, there is no prohibition at all)

The SCDOR’s publication, *South Carolina Tax Incentives for Economic Development Winter Edition 2009*, discusses the pass through statute with admirable clarity The publication first states

Except as otherwise provided, a credit must be used by the taxpayer who earns it *Exceptions to these rules exist* for the following (1) taxpayers participating in a consolidated corporate income tax return, (2) pass through entities eligible to earn and use a credit, (3) limited liability companies not expressly eligible to earn a credit, (Emphasis added)

Id at 21 (emphasis added) The publication then states the rule with regards to partnerships

South Carolina Code § 12-6-3310(B) contains several provisions concerning the use of income tax credits by pass through entities These rules include

Unless specifically prohibited, an S corporation, limited liability company taxed as a partnership, or partnership that qualifies for a credit pursuant to Article 25 of Chapter 6, Title 12 may pass through the credit earned to each shareholder of the S corporation, member of the limited liability company, or partner of the partnership Note The statutory language of a particular tax credit controls whether a credit generated by an entity may be used by a partner, shareholder, or member For example, the infrastructure credit in South Carolina Code § 12-6-3420 specifically states that the credit is claimed against corporate income taxes imposed under South Carolina Code § 12-6-530 or bank taxes imposed under South Carolina Code § 12-11-20, therefore, it cannot be used by an individual against individual income taxes imposed under South Carolina Code § 12-6-510

Id (emphasis added) Again, note that the Infrastructure Credit is found in Article 25

The Pass Through Statute further provides that a corporate partner of a partnership (such as the corporate taxpayers here) may claim a credit against its corporate tax liability in proportion to its ownership interest (here 100% total for the corporate partners) More specifically, the statute states that the percentage of the corporate partner's interest in the partnership is to be “multiplied by the amount of the credit *earned* by the entity ” See S C Code Ann § 12-6-3310(B)(3) (2003) (emphasis added)

The South Carolina Pass Through Statute clearly states that a partnership qualifies for a credit and may pass through the credit earned to its partners unless specifically prohibited by another statute There is no specific prohibition regarding a partnership earning and passing the infrastructure credit through to its partners Accordingly, the Pass-Through Statute, consistent with the IRC, allows a corporate partner of a partnership to claim a credit against its corporate tax liability in proportion to its ownership interest, which in this case would mean Centex should claim 100% of the credit flowing through from its wholly owned partnership, Centex Homes, which qualified for the credits as a result of making infrastructure expenses and contributing the infrastructure project to

public use

4 A Review of the Treatment of Limited Liability Companies with Respect to the Infrastructure Tax Credit Demonstrates the Credit's Applicability to Partnerships

The SCDOR publication cited above specifically discusses limited liability companies as follows

South Carolina Code § 12-6-3310(C) contains special provisions concerning the qualification and use of credits by limited liability companies that are not organized as a legal entity that expressly qualifies for a credit in Article 25 of Chapter 6, Title 12. Note. These special provisions do not apply to credits in other Articles or Titles of the South Carolina Code, such as Chapter 14 of Title 12 containing the economic impact zone credit, or Chapter 65 of Title 12 containing the textile revitalization credit. The rules include

Limited Liability Company Taxed as a Partnership

Individual Member The limited liability company may earn and pass through any credits allowed by Article 25. The individual member will use any credits against individual income taxes imposed under South Carolina Code §12-6-510.

Corporate Member The limited liability company may earn and pass through any credits allowed by Article 25. *The corporate member will use any credits against corporate income taxes imposed under South Carolina Code §12-6-530.*

Note. South Carolina Code § 12-6-3310(c) controls over the statutory language of a particular tax credit. For example, the infrastructure credit in South Carolina Code § 12-6-3420 specifically states that the credit is claimed against corporate income taxes imposed under South Carolina Code § 12-6-530 or bank taxes imposed under South Carolina Code § 12-11-20, however an individual member of a limited liability company taxed as a partnership can use the credit against individual income taxes imposed under South Carolina Code § 12-6-510.

Id. at 22 (emphasis added). Section 12-6-3310(C) states

“ Limited liability companies taxed for South Carolina income tax purposes as partnerships shall apply the credits as provided in subsection (B)” As previously indicated, Section 12-6-3110(B)(1) provides, “Unless specifically prohibited, an “S” corporation, limited liability company taxed as a partnership, or partnership qualifies for a credit pursuant to this article

may pass through the credit earned to each shareholder of the “S” corporation, member of the limited liability company, or partner of the partnership”

Thus, an LLC (taxed as a partnership) may qualify to earn and pass through tax credits unless specifically prohibited by the applicable credit statute. The Pass Through Statute, consistent with the guidance and statutory provisions discussed below, provides that except for LLCs which elect to be taxed as corporations, the taxation of LLCs and partnerships is identical for both state and federal income tax purposes.³

As noted in S C Rev Rul 98-11

A limited liability company (LLC) is an unincorporated business association that provides its owners (members) limited liability, flexible management, and financial alternatives. It is a popular form of business entity since a properly formed LLC can provide the favorable pass-through tax treatment of partnerships, and the limited liability of corporations.

S C Rev Rul 98-11. Section 12-2-25 states for purposes of state taxation

(A) as used in this title and in other titles which provide for taxes administered by the department and unless otherwise required by the context

(1) “partnership” includes a limited liability company taxed for South Carolina income tax purposes as a partnership

(2) “partner” includes a member of a limited liability company taxed for South Carolina income tax purposes as a partnership

South Carolina Tax Incentives for Economic Development states

South Carolina follows the federal tax treatment of limited liability companies. If a limited liability company is treated as a corporation for

³ The Court would also note as consistent with its position in this case (but contrary to SCDOR's) statements made by a policy member of SCDOR in connection with a 2008 amendment to the Infrastructure Credit Statute, which specifically addressed the right of a limited liability company ("LLC") to pass through a credit earned by it to a member. SCDOR's policy section advised the taxpayer who was lobbying for this amendment that the amendment was not necessary because the statute's existing language already allowed an LLC to qualify for and pass the credits through to its members. See R. p. 397 and R. p. 179. Pars. 6-7.

federal income tax purposes it is treated as a corporation for South Carolina income tax purposes and is subject to a corporate license fee South Carolina Code §12-2-25 provides that a partnership includes a limited liability company taxed for all South Carolina income tax purposes as a partnership Accordingly, a limited liability company that is treated as a partnership for federal income tax purposes is not subject to South Carolina income tax or the corporate license fee

Id at 6

LLCs and partnerships file the same tax form with the SCDOR See, e g SCDOR

Partnership FAQ

Which tax form does a limited liability company (LLC) taxed as a partnership File? An LLC taxed as a partnership must file SC1065

See also, the instructions of the South Carolina Partnership Income Tax Return, SCDOR SC1065

Every partnership (including any multiple member LLC not taxed as a corporation), domestic or foreign, doing business or owning property in South Carolina must file SC 1065

Given that (1) partnerships and LLCs are taxed exactly the same for South Carolina tax purposes, and (2) the SCDOR publication quoted above explicitly states that LLCs taxed as partnerships may pass through the Infrastructure Credit to its members, the ALC and SCDOR's application of the statutes undoubtedly produce an absurd result Essentially, their application of the statutes results in all entities other than actual partnerships being permitted to pass through infrastructure credits (e g , S-Corporations are permitted to pass through the credits to its shareholders, LLCs taxed as partnerships would pass through the credits to their member-partners), however, a true partnership would not be permitted to do so, such as in the case Centex Homes

II THE ALC ERRED IN ITS APPLICATION AND INTERPRETATION OF THE AGGREGATE AND ENTITY THEORIES OF PARTNERSHIP TAXATION BY CONCLUDING THAT THE INFRASTRUCTURE EXPENDITURES AND CONTRIBUTIONS MADE BY CENTEX REAL ESTATE CORPORATION (CREC), AS MANAGING GENERAL PARTNER OF CENTEX HOMES, REMAIN ATTRIBUTABLE TO THE PARTNERSHIP

As mentioned previously, Section 12-6-3420 requires (1) a corporation to claim the credit on its corporate income tax return, (2) for expenses paid by the taxpayer, (3) or for contributions made to a governmental entity or a qualified private entity, (4) in building or improving an infrastructure project. Again, there is no disagreement over the first and the fourth requirements.

Based upon application of the “aggregate” and “entity” theories of partnership law as well as the fact that CREC signed the conveyance agreements, Appellant believes the corporate partners directly earned the credit with respect to requirements 2 (making the expenditures) and 3 (making contributions) above. Accordingly, the SCDOR’s position is incorrect, where they maintain that the corporate partners did not directly earn and, thus, may not claim the credit because the corporate partners did not cut the checks to the contractors who performed the road and sewer work.

A The Partners’ Expenditures at Issue Meet the Definition of “Qualifying Infrastructure Expenditures” According to the Infrastructure Tax Credit

The ALC erred in its finding that expenditures remain attributable to the partnership and, thus, the corporate partners of Centex Homes did not incur the expenditures made on infrastructure. The statutory framework for the federal income taxation and, thus, South Carolina income taxation of partners and partnerships is set forth in I R C Sections 701-777 (Subchapter K). One of the recurrent themes of

Subchapter K is the blending of aggregate and entity concepts According to the IRS

Partnership Audit Technique Guide

[t]here is a basic tension between the “Entity” and “Aggregate” Theories of partnership accounting for tax purposes Under the Entity Theory, the amount and character of partnership income is determined at the partnership level as though it was an entity separate from its partners According to the Aggregate Theory, each partner is treated as the owner of a direct and undivided interest in partnership assets, liabilities and operations Tax is actually paid at the partner level

Internal Revenue Service, Partnership - Audit Technique Guide – Overview (December 2002), *available at* www.irs.gov/businesses/partnerships/article/0,,id=134689,00.html In other words, a partnership is treated as a conduit which passes its tax attributes including income, deductions and credits through to the partners to be reported on their individual, or in this case corporate, tax returns

In *Ellis v South Carolina Tax Commission*, 280 S C 65, 309 S E 2d 761 (1983), as previously mentioned, the South Carolina Supreme Court recognized the blending of both concepts or theories in reaching its decision to disallow deductions on an individual income tax return since the deductions or expenditures were incurred by (passed through to) the individual taxpayer from out-of-state limited partnerships (stating that “each item of income, gain loss, deduction or credit is treated as if it were realized or incurred by the partner directly from the source without ever having passed through the partnership”) “Without ever passing through the partnership” precisely articulates or describes the “aggregate theory” concept or method

Under the entity theory as the ALC recognized, but misapplied, the character of a deduction or expenditure is retained at the partner level, thus, the deduction or expenditure is determined by its nature or origin as defined by the applicable tax statute

The SCDOR acknowledges that the infrastructure expenditures incurred by Centex Homes meet the definition and are of the type considered to be qualifying infrastructure expenditures as defined in Section 12-6-3420, but deny the credit solely because the checks to pay the expenditures were made by a partnership, not a corporation. However, the SCDOR fails to recognize or apply the tax law, which is clear under I R C Section 702(b) and the Supreme Court's conclusion in *Ellis*. Under the entity theory, the amount and character of partnership income and deductions including expenditures for qualifying infrastructure projects is determined at the partnership level as though it was an entity separate from its partners. Here, Centex Homes, a general partnership, incurred qualifying infrastructure expenditures and allocated the income and deductions associated with such expenditures and business activities to its corporate partners. Under the aggregate theory, the income and tax deductions, such as expenditures for qualifying infrastructure projects, retain their character (as if the partners directly realized and incurred the partnership items) passing through to the partners to be claimed on their individual, in this case corporate, income tax returns.

In Decision No. 93-78, the South Carolina Tax Commission states, "the Department's treatment of credits is consistent with the treatment of income tax deduction limitations on South Carolina consolidated returns. A credit is very similar to a deduction. Because of the similarity between deductions and credits, we find that these items should be treated in a similar manner for South Carolina consolidation purposes." S C Tax Comm'n Decision No. 93-78 (1993). Accordingly, the tax credit generated by the revenue and expenditures and reflected in the corporate partner's South Carolina taxable income should also be determined at the corporate level and, thus,

pass through to the partnership's owners (i.e., (1) the tax credit created at the partnership level receives similar pass through treatment and/or (2) the qualifying expenditures are treated as passing through and, thus, incurred directly by the corporate partner which then qualifies as earning and claiming the credit at the corporate partner level)

Since the infrastructure expenditures meet the definition of qualifying infrastructure credit expenditures as defined within Section 12-6-3420, the corporate partners are considered to have directly incurred the qualifying expenditures under the tax law

B The Corporate Partners were Directly Involved in the Contribution of Qualifying Infrastructure Projects and Thus Qualify for the Infrastructure Tax Credit

As discussed above, each partner is treated as the owner of a direct and undivided interest in partnership assets, liabilities and operations. This aggregate theory is clearly applied with respect to property ownership upon reviewing the South Carolina Partnership Return (See Line 19 of Form SC1065 and Schedule SC1065 K-1), as partners must take into account their interest of partnership property in applying the state apportionment rules (property factor) to determine their South Carolina taxable income and liability. Use of the aggregate theory for property ownership is consistent with the South Carolina Partnership Act, where an officer of CREC, the managing general partner of Centex Homes, signed the property conveyance agreements with the local municipalities in order to contribute or transfer the qualifying infrastructure projects. Since the partners are considered to own the land and qualifying infrastructure projects within Centex Homes, the execution of the conveyance agreements and contribution of the infrastructure projects are considered to have been made directly by CREC and the

other general partners

The ALC states, “ the expenditures made by a managing partner remain attributable to the partnership, and do not circumvent the determination that the individual partners of Centex Homes indirectly incurred the expenditures made on infrastructure ” (R p 30) Upon review of South Carolina partnership law and the facts of this case, the corporate partners were not investment partners of Centex Homes with an indirect or passive role with respect to business activities South Carolina partnership law views a general partnership and all of its partners as being agents of one another and liable for the acts or omissions of any partner acting in the ordinary course of the business of the partnership See S C Code Ann §§ 33-41-10 et seq (the “South Carolina Partnership Act”) That is, every partner is considered an agent of a general partnership and generally any partner can bind the partnership § 33-41-310 Each general partner is considered to have an equal amount of influence over the day-to-day operations of Centex Homes, and each partner shares equally in the profits and liabilities of the partnership §§ 33-41-370, 33-41-510 and 33-41-730 The corporate partners of Centex Homes exercise command, direction and control over the activities of Centex Homes as well as furnish the capital and bear the risk for the operations of Centex Homes Accordingly, the ALC erred in its conclusion that the corporate partners cannot claim the credit based upon their indirect involvement in the partnership’s business activity

III THE ALC ERRED IN ITS CONCLUSION THAT CENTEX INTERNATIONAL, INC AND AFFILIATES ARE NOT A SINGLE TAXPAYER AND MAY NOT CLAIM THE INFRASTRUCTURE CREDIT ON ITS CONSOLIDATED RETURN

Under South Carolina law, a consolidated corporate income tax return may be filed with respect to a parent and its substantially controlled subsidiaries S C Code Ann

§ 12-6-5020(A)(1) When such a consolidated return is filed, the entities included on that return are combined and reported on a single return for the controlled group § 12-6-5020(D) Specifically, the controlled group is **treated as a single taxpayer** for purposes of administering and claiming tax credits If a corporation that files or is required to file a consolidated return is entitled to one or more income tax credits, the income tax credits must be determined on a consolidated basis § 12-6-5020(F) Moreover, limitations on credits that refer to the income or the income tax liability of a corporation are deemed to refer to the income or income tax liability of the consolidated group, and credits shall reduce the consolidated group's tax liability regardless of whether or not the corporation entitled to the credit contributed to the tax liability of the consolidated group *Id* Additionally, the Infrastructure Credit Statute states that “a corporation which files or is required to file a consolidated return is entitled to the income tax credit allowed by this section on a consolidated basis regardless of whether or not the corporation entitled to the credit contributed to the tax liability of the consolidated group ” § 12-6-3420(H)

Also, the corporate partners of Centex Homes are considered to be the “taxpayer” with respect to filing and signing a partnership tax return *See* Instructions, Form 1065 (2010) (“U S Return of Partnership Income” (“Form 1065”)), which states, “Form 1065 is not considered to be a return unless it is signed One general partner or LLC member manager must sign the return ” Similarly, page 1 of Form SC1065 requires a signature of a general partner or LLC/LLP member Given that CREC is considered the taxpayer with respect to filing and signing the Centex Homes partnership return and it along with all of the other partners are corporations included in the Centex consolidated corporate tax return, there is, in substance, a single taxpayer reporting and paying of tax on a

consolidated basis including Centex Homes

In this case, Centex International, Inc. is the parent company owning 100% of the corporate subsidiary partners of Centex Homes, which in turn own 100% of the Centex Homes partnership. Because a single tax liability was incurred and a single corporate tax return was filed by Centex International, Inc. as the parent holding company, it is treated and viewed as the “taxpayer” and its consolidated return must include the income and deductions related to qualifying infrastructure expenditures. Since these qualifying expenditures are considered to have been accrued by the Centex consolidated group with respect to determining and reporting taxable income, such expenditures must also be considered as being incurred for purposes of administering and claiming the infrastructure tax credit.

Accordingly, the Centex Consolidated Group met the requirements of the Infrastructure Credit Statute (i.e., expenses paid or contributions made) and should be allowed to claim the credit against its consolidated tax liability subject to the limitation of the credit (i.e., 50% of the expenses or contributions or \$10,000 annually per project) as applied to the Centex Consolidated Group.

CONCLUSION

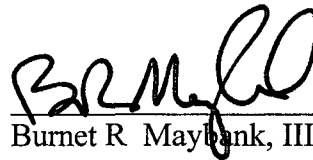
Based upon a literal reading with no absurd results of the infrastructure tax credit statute, the Appellant Centex International, Inc. & Affiliates correctly claimed a credit against taxes due under S.C. Code Ann. § 12-6-530 for expenses paid by Centex Homes, a taxpayer and contributions directly made by CREC, the managing general partner.

In addition, pursuant to case law (*Ellis* and *Dalton*) and the general pass-through statute, Section 12-6-600, treatment of partnerships in South Carolina requires that

expenditures made by the partnership are treated as if made directly by the partners. All three partners are corporations and included in Appellant's consolidated corporate tax return.

Lastly, the incentives pass-through statute, Section 12-6-3310, was codified as the first section of Article 25, which includes the infrastructure tax credit statute. It allows the pass through of any tax credit incentive except where "specifically prohibited." The infrastructure tax credit statute contains no such explicit or definite prohibition.

March 6, 2012



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**THE STATE OF SOUTH CAROLINA
In The Court of Appeals**

APPEAL FROM ADMINISTRATIVE LAW COURT

John D McLeod, Administrative Law Judge

Docket No 2009-ALJ-17-0532-CC

**Centex International, Inc
and Affiliates**

Appellant,

v

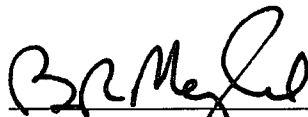
South Carolina Department of Revenue

Respondent

CERTIFICATE OF COUNSEL

The undersigned certified that this Brief of Appellant complies with Rule 211(b),
SCACR

March 6, 2012



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THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT

John D McLeod, Administrative Law Judge

Case No 09-ALJ-17-0532-CC

Centex International Inc & Affiliates,

Appellant,

v

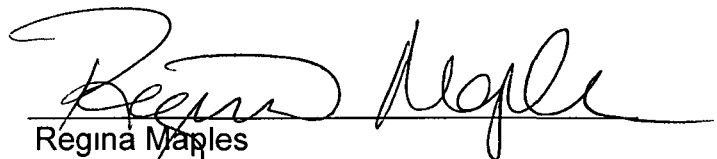
South Carolina Department of Revenue

Respondent

PROOF OF SERVICE

I certify that I have served the Final Brief of Appellant on the South Carolina Department of Revenue by mailing a copy of it, on March 6, 2012, to their attorney of record, Adam Marinelli, SC Department of Revenue, 301 Gervais Street, Columbia, SC 29201

March 6, 2012



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SC Court of Appeals