

# ARIZONA DEPARTMENT OF REVENUE

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## ARIZONA CORPORATE TAX RULING CTR 00-1

This substantive policy statement is advisory only. A substantive policy statement does not include internal procedural documents that only affect the internal procedures of the agency and does not impose additional requirements or penalties on regulated parties or include confidential information or rules made in accordance with the Arizona administrative procedure act. If you believe that this substantive policy statement does impose additional requirements or penalties on regulated parties you may petition the agency under Arizona Revised Statutes § 41-1033 for a review of the statement.

### **ISSUE:**

How does a taxpayer filing an Arizona corporate income tax return determine whether gain or loss on sale of stock is business or nonbusiness income?

### **APPLICABLE LAW:**

Title 43, Chapter 11, Article 4, consisting of A.R.S. §§ 43-1131 to 43-1150 and known as the Uniform Division of Income for Tax Purposes Act (UDITPA), sets forth the procedures for the apportionment and allocation of income.

### **DISCUSSION:**

Income on an Arizona multistate return is classified as either business or nonbusiness income. Business and nonbusiness income are specifically defined in A.R.S. § 43-1131(1). Additionally, judicial decisions provide guidance, and should be consulted, as to the proper classification of income. See *Allied Signal v. New Jersey*, 112 S. Ct. 2251 (1992); *F.W. Woolworth Co. v. Taxation and Revenue Dept. of New Mexico*, 102 S. Ct. 3128 (1982); *Asarco Inc. v. Idaho State Tax Commissioner*, 102 S. Ct. 3103 (1982); *General Motors v. Ariz. Dept. of Revenue*, 189 Ariz. 86, 938 P.2d 481 (1996).

In order to identify business or nonbusiness income, one must identify whether it is income arising from transactions and activities in the regular course of the taxpayer's trade or business.

If a transaction is within the regular course of a trade or business, the income from that transaction will be business income. If a transaction is not within the regular course of a trade or business, the income from that transaction will be nonbusiness income.

In apportioning and allocating income as business or nonbusiness, respectively, the principles of UDITPA, as set forth in A.R.S. §§ 43-1131 to 43-1150 are applied.

A.R.S. § 43-1131(1) defines business income as "income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income

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from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations."

The courts have generally held that where gain or loss on sale of stock is from a subsidiary that is part of the taxpayer's unitary business, the gain or loss is considered to be business income. In cases other than unitary subsidiaries, the courts have considered whether the investment in stock served an operational or investment purpose. When the investment serves an operational purpose, the gain is considered business income. If the investment serves a passive investment purpose, the gain is considered nonbusiness income.

Neither the Arizona statutes nor the court decisions have made a distinction between sales of stock in foreign or domestic companies. Although A.R.S. § 43-1132(A) precludes the allocation or apportionment of income of a foreign corporation to Arizona unless the foreign corporation has nexus within the state, there is no provision against apportionment or allocation of the domestic parent's income from the sale of its stock in a foreign corporation.

### **RULING:**

Gain on the sale of stock of a unitary subsidiary is considered earned in the regular course of a trade or business of the taxpayer and is business income. Gain on the sale of stock of a non-unitary company is considered business income when the investment in stock serves an operational purpose. Gain on the sale of stock of a non-unitary company is considered nonbusiness income when the investment in stock serves a passive investment purpose. These principles apply to gain or loss from sale of stock in foreign corporations as well as domestic corporations.

Mark W. Killian, Director

Signed: May 8, 2000

### **Explanatory Notice**

The purpose of a tax ruling is to provide interpretive guidance to the general public and to department personnel. A tax ruling is intended to encompass issues of law that are not adequately covered in statute, case law or administrative rules. A tax ruling is a position statement that provides interpretation, detail, or supplementary information concerning application of the law. Relevant statute, case law, or administrative rules, as well as a subsequent ruling, may modify or negate any or all of the provisions of any tax

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ruling. See GTP 96-1 for more detailed information regarding documents issued by the Department of Revenue.