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ARIZONA TRANSACTION PRIVILEGE TAX RULING TPR 98-1

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.

(Note: on 5/17/2021, the statute and rule references were updated to show their new numbers. See footnotes for details. No substantive changes were made.)

ISSUE:

The tax base under the mining classification when the selling price of the mineral product includes an amount which represents the value added by additional processing, refinement or packaging.

APPLICABLE LAW:

Arizona Revised Statutes (A.R.S.) § 42-5072¹ levies the transaction privilege tax on the business of mining, quarrying or producing for sale, profit or commercial use any nonmetalliferous mineral product. The tax base is the gross proceeds of sales or gross income derived from the business.

A.R.S. § 42-5072(B)² provides a deduction from the tax base for sales to contractors if the property sold is to be incorporated or fabricated by the contractor into any real property structure or improvement as part of the business.

A.R.S. § 42-5072(C)³ states that the tax base includes the value of the entire product mined, quarried or produced for sale, profit or commercial use in this state, regardless of the place of sale of the product or of the fact that deliveries may be made to points without this state. If the sale price of the product includes freight, the sale price shall be reduced by the actual freight paid by any person from the place of production to the place of delivery.

¹ This ruling originally cited A.R.S. § 42-1310.12 which has been renumbered as A.R.S. § 42-5072.

² This ruling originally cited A.R.S. § 42-1310.12(B) which has been renumbered as A.R.S. § 42-5072(B).

³ This ruling originally cited A.R.S. § 42-1310.12(C) which has been renumbered as A.R.S. § 42-5072(C).

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A.R.S. § 42-5072(F)⁴ states that a person who conducts a business classified under the mining classification may be deemed also to be engaged in business classified under the retail classification to the extent that the person's activities comprise business under the retail classification if the tax is paid at the rate imposed on the retail classification. If the transaction is not subject to taxation under the retail classification, the transaction shall be included in the tax base for the mining classification.

A.R.S. § 42-5072(G)⁵ defines "nonmetalliferous mineral product" as oil, natural gas, limestone, sand, gravel or any other nonmetalliferous mineral product, compound or combination of nonmetalliferous mineral products.

A.R.S. § 42-5061⁶ imposes the transaction privilege tax on the business of selling tangible personal property at retail. The tax base is the gross proceeds of sales or gross income derived from the business.

Arizona Administrative Code (A.A.C.) R15-5-902 provides that sales to retailers or others for resale are taxable under the mining classification. Sales to licensed contractors of products to be incorporated into a structure are fully exempt.

A.A.C. R15-5-904(B)⁷ states that persons who mine and process mineral products are taxable on the gross income from sales of the first marketable product.

A.A.C. R15-5-902(C)⁸ states that income derived from sales of mineral products to final consumers is taxable under the retail classification.

A.A.C. R15-5-908 provides that when the sale price includes a charge for freight, from the place of production to the place of delivery, such charge is deductible. The cost of freight must be actually incurred by the seller and paid to a carrier. Delivery of products in the seller's own conveyance does not qualify for this deduction.

LEGAL REFERENCE:

The tax applies not only to mining and quarrying, but also to producing for sale, profit or commercial use any nonmetalliferous mineral product. *State Tax Commission v. Wallapai Brick and Clay Products*, 85 Ariz. 23, 330 P.2d 988 (1958).

⁴ This ruling originally cited A.R.S. § 42-1310.12(F) which has been renumbered as A.R.S. § 42-5072(F).

⁵ This ruling originally cited A.R.S. § 42-1310.12(G) which has been renumbered as A.R.S. § 42-5072(G).

⁶ This ruling originally cited A.R.S. § 42-1310.01 which has been renumbered as A.R.S. § 42-5061.

⁷ This ruling originally cited A.A.C. R15-5-904(C) which has been renumbered as A.A.C. R15-5-904(B)

⁸ This ruling originally cited A.A.C. R15-5-906 which was repealed in 2000. However, the statement referenced was added to A.A.C. R15-5-902(C) at the same time as the old rule was repealed.

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DISCUSSION:

The mining classification is comprised of the business of mining, quarrying or producing for sale, profit or commercial use any nonmetalliferous mineral product. The tax base includes the value of the entire product mined, quarried or produced for sale, profit or commercial use. However, when the sale price includes a charge for freight, from the place of production to the purchaser, the charge is deductible from the tax base if the cost was incurred by the seller and paid to a carrier.

Sales of nonmetalliferous mineral products to retailers or others for resale are taxable under the mining classification, however, sales to final consumers are taxable under the retail classification rather than the mining classification. Also, sales to licensed contractors of products to be incorporated into a structure are not taxable.

The mining classification applies to more than just the removal of minerals from the earth. In *Wallapai Brick*, the taxpayer mined clay from which they produced bricks which were sold for use in construction. The Court found that the tax base was the receipts from the sale of the bricks.

The Court held that:

It is upon the "business" of producing mineral products "*for sale, profit or commercial use*" that the tax is imposed. It is obvious that when the clay has been refined and the process of manufacturing bricks commences there has been no "sale"; neither could there be any sale of the product upon which proceeds the tax could be imposed. It seems equally clear that the plaintiffs have realized no "profit" at this point. And, it would also seem that this raw clay has no "commercial use" as yet.

The Court pointed out that what is taxed is the "business" of producing mineral products "for sale, profit or commercial use" and the first point at which there were proceeds from that business was when the taxpayer had something they could and did sell. The Court was therefore "of the opinion that the removal of clay from the earth's surface and the fabrication thereof into finished bricks, the first marketable product produced, is a 'business' and is, as a whole, within the purview of" the tax statute.

When mineral product is sold, the tax base includes the value of the entire product sold, including the amount which represents the value added by additional processing, refinement or packaging.

EXAMPLES:

1. A sand and gravel company sells washed and graded sand at a price that is higher than that at which river-run sand is sold because of the additional processing involved. The tax base for the washed and graded sand is the gross amount received from the sale of the washed and graded sand.

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2. A person mines and processes salt for sale. The salt is sold in bulk, in bags, and is also further processed into pellets for sale in that form. The tax base for the bulk salt, the bagged salt and the pelletized salt is the respective amount received from each of the sales.

RULING:

The tax base for the mining classification is the gross income derived from the business of mining, quarrying or producing any nonmetalliferous mineral product. When minerals are mined and further processed, refined or packaged, the tax base is the gross proceeds of the sale, including any amount in the selling price which represents the value added by the additional processing or packaging.

However, when the sale price includes a charge for freight, from the place of production to the purchaser, the charge is deductible from the tax base if the cost was incurred by the seller and paid to a carrier.

Sales of nonmetalliferous mineral products to retailers or others for resale are taxable under the mining classification, however, sales to final consumers are taxable under the retail classification rather than the mining classification.

Sales to licensed contractors of products to be incorporated into a structure are not taxable.

Mark W. Killian, Director

Signed: July 17, 1998

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