STATE OF ARIZONA
Department of Revenue

TAXPAYER INFORMATION RULING LR11-002

Janice K. Brewer
Governor

Gale Garriott
Director

March 14, 2011

This taxpayer information ruling is in response to your August 19, 2009 taxpayer information ruling request as supplemented by the October 30, 2009, February 24, 2010 and April 7, 2010 correspondence, in which you, ("Representatives"), request that the Arizona Department of Revenue ("Department"), rule on behalf of your client on the application of Arizona transaction privilege and use tax to the "Ice . . ." and "Ice . . ."

Statement of Facts

Your request for a taxpayer information ruling provides in part the following information:

> [W]e submit this request for a Taxpayer Information Ruling on behalf of our client (the "Company") on the question of whether the ice making machinery it sells to Arizona businesses, or itself uses in-state, qualifies for the machinery and equipment deduction under [Arizona Revised Statutes (A.R.S.)] A.R.S. § 42-5061(B)(1) (retail classification) or the use tax deduction under A.R.S. § 42-5159(B)(1).
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> * * *
>
> The Company is an Arizona-based dealer of several different types of fully-automated, free-standing machines that manufacture ice for sale. The Company sells these machines to entrepreneurs who set them up and operate them throughout the state, generally at convenience or grocery stores. The Company also owns a few ice machines that it has set up around the state and operates itself.
>
> As a basic overview, the Company's machines do not merely freeze water into ice like an ice maker found inside a refrigerator. Rather, they intake water, which then undergoes a process of filtration, conditioning and treatment inside the machines. After this process is complete, the water is then further processed by the machines into cubes of fresh ice for purchase by customers. Unlike many other ice machines or vendors, the Company's ice is not made elsewhere then trucked in for sale. Rather, the ice is made fresh by the machines themselves. As a result, the ice is of the highest quality and purity, having never been touched by human hands.
>
> A customer desiring to purchase ice from the Company's machine operates a kiosk at the front of the machine and inserts coins or

swipes a credit card for payment. The customer selects the desired amount of ice, and may also opt to receive the ice in a bag or without a bag (filled directly into the customer's cooler or other container). The machine then dispenses ice in the form requested by the customer. Because the Company's machines are fully automated, customers may purchase ice at any time during the day, 365 days out of the year.

The Company's ice machines come in . . . different models, which for purposes of this ruling request we will call the "Ice . . .", [and] the "Ice . . ."

Ice . . . : The Ice . . . is a large, 200 square foot facility capable of producing 280 to 800 sixteen-pound bags of ice per day, depending on the model and options purchased. At any given time, it is capable of storing at the required temperature to prevent thawing 375 bags of ice made by the machine.

Ice . . . : The Ice . . . is a smaller, 86 square foot version of the Ice Machine. It is cable of producing 125 to 280 sixteen-pound bags of ice per day, depending on the model and options purchased. It stores at the required temperature to prevent thawing around 100 bags of ice.

* * *

In this case, the Company's machines are essential to creating the finished product, because they perform the entire function from beginning to end that results in the production of ice for sale. Likewise, the ice machines contribute to maintaining a harmonious integrated synchronized system, because they perform all functions necessary to convert raw water into ice and maintain the ice in marketable form until sold. Stated another way, the machines, taken as a whole, constitute the entire synchronized system of making ice: they input water, filter, condition and treat it, freeze the water into ice, and maintain the ice in marketable form until sold.

* * *

Generally, no modification to real property is necessary as a result of the installation or removal of the "Ice . . ." [and Ice . . .]." Rather, the "Ice . . ." [and Ice . . .] is merely assembled on-site and connected to public utilities such as water, sewer and electricity. As a result of the

> connection to public utilities, the “Ice . . .” [and Ice . . .] requires a building permit.
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> * * *
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> [T]he “Ice . . .” [and Ice . . .] is manufactured at an off-site location and subsequently assembled and installed on-site.
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> * * *
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> The outside sub-structure of the “Ice . . .” [and Ice . . .] is considered a factory-built building. . . . Also, as a note of clarification, the letter attached . . . is a copy of the manufacturer’s factory-built building license. It’s not our client’s license.
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> * * *
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> The “Ice . . .” [and Ice . . .] is readily removable from the site and can be removed without causing any damage to the ice machine or the site where it is located. You will note that . . . [the] “units are affixed to property on concrete piers and anchored to ground or concrete foundations.”

The April 7, 2010 correspondence provides that the Company was issued a license as a D-10 retailer of factory-built buildings by the Arizona Department of Fire, Building and Life Safety, Office of Administration.

Issue

Are the gross proceeds or gross income from the sale of the Ice . . . and the Ice . . . exempt under A.R.S. § 42-5061(B)(1) and A.R.S. § 42-5159(B)(1)?

Your Position

The Representatives’ position as stated in the August 19, 2009 ruling request:

> The Company’s ice machines [Ice . . . and Ice . . .] constitute machinery and equipment used in manufacturing or processing. As a result, the sale or use of the Company’s ice machines is deductible from transaction privilege tax under A.R.S. § 42-5061(B)(1) and exempt from use tax A.R.S. § 42-5159(B)(1).

Law

A.R.S. § 42-5061(B)(1) provides a deduction under the retail classification for "[m]achinery, or equipment, used directly in manufacturing, processing, fabricating, job printing, refining or metallurgical operations. The terms "manufacturing", "processing", "fabricating", "job printing", "refining" and "metallurgical" as used in this paragraph refer to and include those operations commonly understood within their ordinary meaning."

A.R.S. § 42-5159(B)(1) exempts from Arizona use tax "[m]achinery, or equipment, used directly in manufacturing, processing, fabricating, job printing, refining or metallurgical operations. The terms "manufacturing", "processing", "fabricating", "job printing", "refining" and "metallurgical" as used in this paragraph refer to and include those operations commonly understood within their ordinary meaning."

A.R.S. § 42-5075(A) provides that the prime contracting classification is comprised of the business of prime contracting and dealership of manufactured buildings.

A.R.S. § 42-5075(O)(3) defines "dealership of manufactured buildings" as a dealer who either:

> (a) Is licensed pursuant to title 41, chapter 16 and who sells manufactured buildings to the final consumer.
>
> (b) Supervises, performs or coordinates the excavation and completion of site improvements, setup or moving of a manufactured building including the contracting, if any, with any subcontractor or specialty contractor for the completion of the contract.

A.R.S. § 42-5075(O)(4) defines a "manufactured building" as "a manufactured home, mobile home or factory-built building, as defined in section 41-2142."

A.R.S. § 42-5155(A) imposes Arizona's use tax on purchases of tangible personal property from out-of-state retailers that are used, stored, or consumed in Arizona.

A.R.S. § 42-5155(A) imposes Arizona use tax on "[a] manufactured building purchased outside this state and set up in this state is subject to tax under this section and in this case the percentage is sixty-five per cent of the sales price."

A.R.S. § 42-5160 provides that "[i]n the case of a manufactured building that is purchased from a dealer outside this state and brought into this state, any person who is hired to set up the manufactured building and who is licensed pursuant to title 41, chapter 16, article 4 shall collect the tax from the owner and remit the tax with any tax that is due under the prime contracting classification."

A.R.S. § 41-2142(9) defines "dealer" as "any person who sells, exchanges, buys, offers or attempts to negotiate or acts as an agent for the sale or exchange of factory-built buildings,

subassemblies, manufactured homes or mobile homes except as exempted in section 41-2178.

A.R.S. § 41-2142(14) defines a "factory-built building" as "a residential or nonresidential building including a dwelling unit or habitable room thereof which is either wholly or in substantial part manufactured at an off-site location to be assembled on-site, except that it does not include a manufactured home, recreational vehicle or mobile home as defined in this section."

A.R.S. § 41-2142(37) defines "unit" as "a manufactured home, mobile home, factory-built building, subassembly or accessory structures."

A.R.S. § 41-2194(4) provides that it is unlawful for any person to engage in the business of contracting to sell any new or used unit or subassemblies regulated by this article or otherwise act in the capacity of a dealer or broker unless such person is licensed as a dealer or broker by the office.

"[I]t is presumed that all gross proceeds of sales and gross income derived by a person from business activity classified under a taxable business classification comprise the tax base for the business until the contrary is established." A.R.S. § 42-5023.

Arizona Administrative Code R4-34-203(3) states that a D-10 license is required for retailers of factory-built buildings based on certain listed activities within the scope of a D-10 license including, for example, a retailer that buys, sells, or exchanges new or used factory-built buildings.

In *Brink Electric Construction Co. v. Arizona Department of Revenue*, 909 P.2d 421 (Ariz. Ct. App. 1995), the Arizona Court of Appeals held that a prime contractor that installs electrical equipment at electric substations does not sell tax-exempt equipment at retail but performs taxable construction work.

Discussion

The Ice . . . and Ice . . . are buildings "either wholly or in substantial part manufactured at an off-site location", outside of Arizona, and then "assembled on-site" within Arizona. A.R.S. § 41-2142(14). The Ice . . . and Ice . . . are factory-built buildings as defined in A.R.S. § 41-2142(14). Therefore, the Ice . . . and Ice . . . are also manufactured buildings. A.R.S. § 42-5075(O)(4).

The Company is a licensed dealer pursuant Title 41, Chapter 16, to sell manufactured buildings and sells the Ice . . . and Ice . . . to final Arizona consumers. Therefore, the Company's business consists of the dealership of manufactured buildings. A.R.S. § 42-5075(A); A.R.S. § 42-5075(O)(3); A.R.S. § 41-2142(9).

The prime contracting classification is comprised of the business of prime contracting and dealership of manufactured buildings. A.R.S. § 42-5075(A). The prime contracting classification provides that the tax base is 65% of the gross proceeds of sales or gross income derived from the business. A.R.S. § 42-5075(B).

When the Company sells the Ice . . . and Ice . . . to final consumers within Arizona, the Company is in the business of the dealership of manufactured buildings, and the Company is not in the business of selling tangible personal property at retail. Therefore, the deduction under the retail classification provided by A.R.S. § 42-5061(B)(1) is not applicable to the Company's sale to final Arizona consumers of the Ice . . . and Ice . . . *Brink Electric Construction Co. v. Arizona Department of Revenue*, 909 P.2d 421 (Ariz. Ct. App. 1995)

Use tax is levied on "the storage, use or consumption in this state of tangible personal property purchased from a retailer or utility business, as a percentage of the sales price." On the other hand, use tax is specifically levied on "manufactured buildings purchased out of state and set up in this state" and the percentage is at 65% of the sales price, similar to the tax base for the prime contracting classification. The language of A.R.S. § 42-5155(A) that relates to the manufactured buildings is different than the language relating to tangible personal property. From this difference in language it is apparent that the Legislature considers manufactured buildings as different from "tangible personal property" for purposes of the use tax.

The exemption from use tax provided by A.R.S. § 42-5155(B)(1) is applicable to certain categories of "tangible personal property." Because manufactured buildings are not "tangible personal property," this exemption is not applicable to manufactured buildings. When the Company purchases manufactured buildings from outside of Arizona and sets them up in to Arizona, it is subject to use tax, unless otherwise provided by A.R.S. § 42-5160 (which relates to use tax liability of a third party setting up a manufactured building brought into Arizona.) The Company is liable for tax on 65% of the sales price of the manufacture buildings. A.R.S. § 42-5155(A).

Conclusion and Ruling

The Company is subject to Arizona transaction privilege tax under A.R.S. § 42-5075(A) on the gross proceeds or gross income from the sale to final consumers within Arizona of the manufactured buildings, the Ice … and Ice …. The exemption provided by A.R.S. § 42-5061(B)(1) is not applicable to the proceeds from Company's sales of the Ice … and Ice ….

Ice … and Ice … owned and operated by the Company which are purchased outside of Arizona and set up in Arizona are subject to Arizona use tax on 65% of the purchase price,

unless otherwise provided by A.R.S. § 42-5160. A.R.S. § 42-5155(A). The exemption provided by A.R.S. § 42-5159(B)(1) is not applicable to manufactured buildings.

The conclusions in this taxpayer information ruling do not extend beyond the facts presented in your correspondence dated August 19, 2009, October 30, 2009, February 24, 2010, and April 7, 2010, respectively.

This response is a taxpayer information ruling (TIR) and the determination herein is based solely on the facts provided in your request. The determinations are subject to change should the facts prove to be different on audit. If it is determined that undisclosed facts were substantial or material to the Department's making of an accurate determination, this taxpayer information ruling shall be null and void. Further, the determination is subject to future change depending on changes in statutes, administrative rules, case law, or notification of a different Department position.

If the Department is provided with required taxpayer identifying information and taxpayer representative authorization before the proposed publication date (for a published TIR) or date specified by the Department (for an unpublished TIR), the TIR will be binding on the Department with respect to the taxpayer that requested the ruling. In addition, the ruling will apply only to transactions that occur or tax liabilities that accrue from and after the date the taxpayer receives the ruling. The ruling may not be relied upon, cited, or introduced into evidence in any proceeding by a taxpayer other than the taxpayer who has received the taxpayer information ruling. If the required information is not provided by the specified date, the taxpayer information ruling is non-binding for the purpose of abating interest, penalty or tax.

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