

ARIZONA DEPARTMENT OF REVENUE

1600 WEST MONROE - PHOENIX, ARIZONA 85007-2650



JANE DEE HULL
GOVERNOR

MARK W. KILLIAN
DIRECTOR

ARIZONA CORPORATE TAX RULING CTR 02-4

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 income from foreign currency transactions 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 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 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."

Income or loss from foreign currency transactions is considered to be business income when the income results from normal business transactions of the taxpayer such as cash deposited in foreign bank accounts, accounts receivable or hedging contracts to mitigate the effects of currency fluctuations. A taxpayer may also engage in separate investments in foreign currencies and those investments may serve an operational or

ARIZONA CORPORATE TAX RULING

CTR 02-4

Page 2

investment purpose. When the investment serves an operational purpose, such as short-term investment of working capital, the gain or loss is considered business income. If the investment serves a solely passive investment purpose, the gain or loss is considered nonbusiness income.

RULING:

Gain or loss on foreign currency transactions is considered earned in the regular course of a trade or business of the taxpayer and is business income when the income results from normal business transactions of the taxpayer such as cash deposited in foreign bank accounts or accounts receivable. Gain on foreign currency transactions is considered business income when the investment in stock serves an operational purpose. Gain on foreign currency transactions is considered nonbusiness income when the investment in foreign currency transactions serves a purely passive investment purpose.

See CTR 94-10 for a discussion of business/nonbusiness income.

See CTR 99-4 for a discussion of including gross receipts from business income in the sales factor.

Mark W. Killian, Director

Signed: August 12, 2002

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.