

## PRIVATE TAXPAYER RULING LR95-006

July 25, 1995

The following private taxpayer ruling is in response to your letter dated April 26, 1995, requesting a private taxpayer ruling on the Arizona transaction privilege tax with regard to the sale of equipment by the ....

The following is a restatement of the facts in your letter.

Statement of facts:

... is an irrigation district and political subdivision of the state formed by a resolution and order of the Board of Supervisors, Maricopa County, Arizona on June 4, 1923. ... is a municipal corporation of the state for all purposes.

Because of its status as a municipal corporation, ... is sometimes able to purchase equipment (e.g., road graders, light duty trucks, tractors) needed to operate the irrigation district at a lower price than is available to the public.

... is contemplating the resale of heavy equipment such as road graders, light duty trucks and tractors to members of the district at the same price as ... pays for the equipment, plus incidental costs which may be incurred by ... as part of the sale. ... does not intend to profit from the sales, only to recover its costs in providing this service to all members of the irrigation district. All sales would be for cash, with no financing available to any member of the district.

The equipment purchased by ... is essential to the maintenance and repair of the district's canals, ditches, laterals, canal banks, well sites, etc., and, for that reason, is essential to ... governmental function as an irrigation district. The equipment would be used by those members to maintain and repair the irrigation ditches and laterals on their own property and may also be used for commercial farming.

It is difficult to estimate how many times in any given year ... would purchase equipment for resale to its members, in part because it is difficult to estimate the demand for this proposed service among the members of the district. The service will be offered to all members of ..., but only to members of ... and only in response to specific requests by members. If demand exists among its members, ... may purchase equipment for resale on more than an occasional basis.

Applicable statutory provisions:

Arizona Revised Statutes (A.R.S.) § 42-1301.1 defines "business" as including all activities or

acts, personal or corporate, engaged in or caused to be engaged in with the object of gain, benefit or advantage, either directly or indirectly, but not casual activities or sales.

A.R.S. § 42-1301.8 defines "person" to include an individual, firm, partnership, joint venture, association, corporation, estate or trust, this state, any county, city, town, district other than a school district, or other political subdivision, and any other group or combination acting as a unit, and the plural as well as the singular number.

A.R.S. § 42-1310.01 levies the transaction privilege tax on the business of selling tangible personal property at retail.

A.R.S. § 48-2901 provides that all irrigation districts organized under the laws of this state are declared to be municipal corporations for all purposes.

A.R.S. § 43-104.23 defines taxpayer as "any person subject to a tax imposed by this title, but in no case shall it include the United States, this state, counties, cities, towns, school districts or other political subdivisions or units of this state or the federal government."

Arizona Administrative Code (A.A.C.) R15-5-181.B provides that the gross receipts from the sale of tangible personal property by the state or its political subdivisions, when acting in a proprietary capacity are taxable unless otherwise exempt.

Discussion:

1. Is the income received from a profit realized from the sale of the equipment to its members subject to Arizona income tax?

Under Arizona law, all irrigation districts organized under the laws of this state are declared to be municipal corporations for all purposes. For purposes of the Arizona income tax, taxpayer is defined as "any person subject to a tax imposed by this title, but in no case shall it include the United States, this state, counties, cities, towns, school districts or other political subdivisions or units of this state or the federal government."

... is a municipal corporation. As a municipal corporation, it is not included in the definition of "taxpayer" for purposes of the Arizona income tax.

A.A.C. R15-5-181 provides that the gross receipts from the sale of tangible personal property by political subdivisions, when acting in a proprietary capacity, are taxable, unless otherwise exempt. The application of this rule is limited to the transaction privilege tax.

2. Is the sale of the equipment by ... to its members subject to Arizona's transaction privilege tax?

The transaction privilege tax is imposed on the privilege of conducting business within the Arizona. The tax is imposed on the seller, not the purchaser, although the purchaser may pass the burden of the tax on to the purchaser.

The transaction privilege tax is levied on the business of selling tangible personal property at retail. "Selling at retail" is defined as a sale for any purpose other than for resale. All retail sales of tangible personal property are subject to tax unless specifically exempted by statute.

The Arizona transaction privilege tax statutes specifically include within the definition of "person," this state, a county, city, town, district other than a school district, or other political subdivisions and any other group or combination acting as a unit.

The applicability of the transaction privilege tax to municipal corporations was addressed in *City of Phoenix v. State*, 53 Ariz. 28, 85 P.2d 56, 58 (1938). The court in *City of Phoenix* acknowledged that:

There is nothing ... indicating an intention to exempt municipalities that engage in an industrial pursuit, business, or enterprise from paying a tax on their products, or income, or service. It would seem that when municipalities become competitors with private enterprise they should be treated no better than others operating in the same field. The general rule is that municipalities are subject to the same liabilities as private corporations, or individuals, except when they are exercising purely governmental functions.

Municipalities and other local governing bodies are subject to the Arizona transaction privilege tax upon their business activities unless exercising purely governmental functions as opposed to proprietary functions.

The determination of whether a business activity or enterprise pursued by a local governmental body is purely governmental is essential to determine whether the activity is subject to transaction privilege tax.

In its governmental or public character, the local government acts merely as an agent of the state. The state endows the local government with certain limited and prescribed powers to be exercised primarily for the public good in behalf of the state rather than for the benefit of those only within the local community's borders.

In its proprietary or private character, the powers are exercised primarily or chiefly for the private advantage of the compact community rather than for the public good of the state at large. As to such powers, and to property acquired and contracts made thereunder, the corporation is regarded as having the rights and obligations of a private, rather than those of a

public, corporation. Proprietary or private purposes include acts or functions of a local character which are voluntarily assumed, mainly for the local community's own purposes or benefit, or those which are not within the police power. A proprietary function is "more a commercial activity which directly competes with other commercial activities...." *Book-Cellar, Inc. v. City of Phoenix*, 150 Ariz. 42, 44, 373 P.2d 1169 (App. 1986)

The sale of equipment to the members of an irrigation district is a commercial activity which directly competes with other commercial activities. Therefore, the sale of equipment is a proprietary function which may be subject to transaction privilege tax.

3. If the sale of the equipment is subject to Arizona's transaction privilege tax, is the original sale of the equipment to ... exempt from transaction privilege tax?

For a sale of tangible personal property to be a "sale for resale" the purchaser must make sales of the property in the ordinary course of business. Therefore, in order for ... to make purchases of equipment exempt from transaction privilege tax as sales for resale, ... must be engaged in the business of selling the equipment and not making casual sales.

A.A.C. R 15-5-2001 defines a casual sale as an occasional transaction of an isolated nature made by a person who is not engaged in the business of selling, within or without the state, the same type or character of property as that which was sold.

Conclusion and ruling:

The following ruling is given based on the facts presented in your request.

The department rules that ... will not be subject to Arizona income tax on the income received from the sale of equipment to its members.

The department also rules that the sale of equipment to its members would be a proprietary function rather than a governmental function. As such, if the transactions are not of an isolated nature, ... would be considered to be engaging in the business of making retail sales of the equipment to its members. Since ... will be engaged in the business of making retail sales, the purchase of equipment for resale to its members will be exempt from transaction privilege tax as a sale for resale. ... will be subject to transaction privilege tax on the gross receipts realized from the sale of the equipment to its members.

However, if the sales of the equipment to its members are casual sales, i.e., occasional transactions of an isolated nature, ... will not be considered to be engaged in the business of making retail sales. In that case, sales of the equipment to ... would not be for resale in the ordinary course of business and the vendor of the equipment would be subject to transaction privilege tax on the gross proceeds derived from the sale.

The conclusion in this private taxpayer ruling does not extend beyond the facts as presented in the letter dated April 25, 1995 in this request for a private taxpayer ruling.

This response is a private taxpayer ruling and the determination herein is based solely on the facts provided in your request. The determination in this taxpayer ruling is the present position of the department and is valid for a period of four years from the date of issuance except as set out herein. This determination is 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 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.