

NEXUS IN ARIZONA

To better serve you, the Arizona Department of Revenue offers online assistance and filing of your business taxes. To file your taxes online or to register to use the website go to www.aztaxes.gov.

The purpose of this brochure is to provide general guidance. The brochure is intended to help define the meaning of "nexus" and to provide a general guideline for determining whether nexus exists within the state of Arizona. The law of nexus as explained in this brochure may change due to actions by the United States or Arizona courts, the U S Congress or the Arizona legislature.

Definitions

"Nexus" is the connection required to exist between a state and a potential taxpayer such that the state has the constitutional right to impose a tax. The United States Constitution limits the states' right to tax through the Due Process Clause and the Commerce Clause.

Due Process Clause

The Due Process Clause of the Fourteenth Amendment requires some definite link, some minimum connection between a state and the person, property, or transaction it seeks to tax. The most minimal connections will satisfy this requirement. The connection need not include physical presence in the state. Due Process also requires that the income attributed to the State for tax purposes must be rationally related to values connected with taxing state. This last requirement is rarely a bar to enforcement of tax.

Commerce Clause

The Commerce Clause of the Constitution (Article 1, Section 8, C13) gives to congress the power to regulate commerce among the states. Therefore, a state may not impermissibly affect interstate commerce without congressional authorization. The U.S. Supreme Court held in *Complete Auto Transit* (430 US 274 (1976)) that a state does not impermissibly affect interstate commerce if it meets each of four tests:

1. The taxed activity has a substantial nexus to the taxing state.
2. The tax is fairly apportioned among states.
3. The tax does not discriminate against interstate commerce.
4. The tax is fairly related to services provided by the taxing state.

The area of greatest confusion in this four-part test is what constitutes "substantial nexus" for purpose of the *Complete Auto* test. The issue of nexus most commonly arises with regard to either the transaction privilege and use tax or the income tax.

Transaction Privilege and Use Tax

The tax commonly referred to as a "sales tax" is in reality two distinct taxes. The first is the Transaction Privilege Tax, which is a tax on the privilege of doing business in Arizona. It is measured by the value of tangible personal property sold by the vendor in Arizona. The vendor is liable for the tax, even though the vendor may pass on the tax to the consumer. The second is the Use Tax. The Use Tax is a tax on any tangible personal property bought from an out-of-state vendor that is stored, used, or consumed in Arizona on which no tax was paid to the state of sale. The consumer is liable for the Use Tax, however the vendor is responsible for collecting and remitting the tax to the state as long as nexus is established. If a lesser amount of tax was paid to the state of sale than would have been paid had the property had been purchased in Arizona, the consumer is liable for the difference. For more information on what activities create nexus for out-of-state vendors, see Transaction Privilege Tax Ruling (TPR) 08-01.

Corporate Income & Individual Income Tax

In addition to the limitations imposed by the Due Process and Commerce Clause, the Congress of the United States created an additional protection from nexus for certain potential taxpayers. Public Law 86-272 (15 USC 381-384) provides that no state may impose a tax on net income where the only contact between the taxpayer and the state is the solicitation of orders for the sale of tangible personal property and where orders, if approved, are shipped from a point outside the state. Out-of-state companies that limit their activities in Arizona to the solicitation of sales and shipment of tangible goods from a point outside the state therefore have no nexus to Arizona for income tax purposes, even if they engage in other in-state activities that would otherwise create nexus, such as maintaining an employee in the state. So long as its activities are limited to the solicitation of sales, an independent contractor (such as a salesperson or broker) will not create nexus for the out-of-state entity even though it engages in activities in Arizona that would otherwise create nexus, such as maintaining an office or owning property.

Determining Nexus within Arizona

The following is a general guideline of activities that, if engaged in, may exceed the minimum threshold of nexus and subject the business to the Transaction Privilege Tax, or Use Tax requirements of Arizona:

- Employee present in the state for more than two days per year.
- Ownership or lease of real or personal property in Arizona.

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- Maintenance of an office or place of business in Arizona.
- Delivery of merchandise into Arizona on vehicles owned or leased by the taxpayer.
- Independent contractors or other non-employee representatives present in Arizona for more than two days per year for the purpose of establishing and maintaining a market for the taxpayer. Examples of establishing and maintaining a market include: soliciting sales; making repairs; collecting delinquent accounts; delivering property sold to customers; installing products; conducting training for employees or representatives of the company or customers; resolving customers complaints; providing consulting services; soliciting, negotiation, or entering into franchising agreements.

Examples of types of activities that can subject a company to income taxation can be found in Arizona Corporate Tax Ruling (CTR) 99-5.

These items are examples only and should not be considered exhaustive or conclusive. If you have any specific questions about business activity or nexus that are not answered above, please contact:

Arizona Department of Revenue
Nexus Unit—5th floor
1600 W Monroe St.,
Phoenix AZ 85007
602-716-6453
602-716-6403

Or you may contact us at: nexus@azdor.gov

Voluntary Disclosure Program

The voluntary disclosure program is available to all businesses that want to come into compliance with Arizona Transaction Privilege Tax, Use Tax, and Corporate Tax Laws. In most instances, this process is initiated by a company's representative and submitted on an anonymous basis. Terms and conditions are negotiated on an individual, factual basis.

Taxpayers interested in this program may contact the department at the appropriate address above.

Taxpayers interested in pursuing voluntary disclosures for states in addition to Arizona may do so by contacting the:

National Nexus Program
Multistate Tax Commission
444 North Capital Street N.W.
Washington, DC 20001
202-508-3800