PRIVATE TAXPAYER RULING LR 20-008

July 16, 2020

Thank you for your letter dated February 21, 2020, requesting a private taxpayer ruling ("PTR") on behalf of *** ("Taxpayer"). Specifically, you requested a determination of whether providing a tower crane, mobile crane or construction hoist (hereinafter "Crane Services") with or without an operator, for a prime contractor, is subject to taxation pursuant to the Arizona transaction privilege tax ("TPT") statutes.

Pursuant to Arizona Revised Statutes ("A.R.S.") § 42-2101, the Arizona Department of Revenue ("Department") may issue private taxpayer rulings to taxpayers and potential taxpayers on request.

ISSUE:

1. Whether the gross receipts derived from the rental of a tower crane, a mobile crane, and a hoist *with* an operator are subject to TPT.
2. Whether the gross receipts derived from the rental of a tower crane, a mobile crane, and a hoist, *without* an operator are subject to TPT.
3. Whether the gross receipts derived from the rental of a tower crane, mobile crane, or hoist are subject to TPT when an operator is provided for some of the contract period but not all.

RULING:

The department rules as follows:

1. Taxpayer's gross income derived from providing a tower crane, mobile crane, and hoist *with* an operator is subject to TPT under the prime contracting classification for state TPT and county tax purposes unless otherwise exempt, or unless otherwise designated to the prime contractor using an Arizona Form 5005; and is subject to the city privilege tax as rental, leasing, and licensing for the use of tangible personal property; unless otherwise exempt. However, the installation of equipment into real property is taxable by the cities as construction contracting; unless otherwise exempt. The gross income derived from a mobile crane rental is exempt from city privilege taxes when the annual motor carrier fee has been paid.
2. Taxpayer's gross income derived from providing a tower crane, mobile crane and hoist *without* an operator is subject to TPT under the personal property rental classification for

state, county and city tax purposes; unless otherwise exempt. The gross income derived from a mobile crane is exempt from state, county and city privilege taxes when the annual motor carrier fee has been paid.

3. Taxpayer's gross income derived from providing a tower crane, mobile crane, or hoist with an operator is taxable under prime contracting. It is taxable under personal property rental when no operator is provided.

SUMMARY OF FACTS:

The following facts are a summary based on your ruling request dated February 21, 2020, as well as additional information, provided February 26, 2020, March 4, 2020, April 2, 2020, April 21, 2020, May 1, 2020, June 9, 2020 and June 12, 2020:

Taxpayer, headquartered in ***, provides tower cranes, mobile cranes and construction hoists ("hoists"), to be used on Arizona construction projects. Cranes and hoists may, or may not, be provided with an operator. Mobile cranes may be provided for mere hours to more than a year. Tower cranes and hoists are typically provided for a duration of six to eighteen months. However, certain jobs may require both Taxpayer and the contractor provide their operators and neither has exclusive control of the cranes or hoists for the full duration of the contract.

A tower crane refers to both self-erecting and top slewing tower cranes. A self-erecting tower crane is smaller and generally transported to the job site as one unit. Top slewing tower cranes are larger and used on high rise construction projects and require assembly and setup on the job site. Tower cranes are generally erected on an engineered concrete reinforced pad. However, at times a tower crane may be erected using a cross base instead of a concrete pad.[1] "A cross base is a very large piece of equipment in the shape of an x, heavily weighted down by concrete blocks, that the tower can be built on. These are seldom used because, among other reasons, the large base takes up much more of the jobsite."[2]

Mobile cranes refer to "self-propelled cranes, such as truck cranes, all-terrain cranes, rough-terrain cranes, and crawler cranes."[3] Self-propelled cranes provide a "[l]ifting apparatus which functions intermittently to lift and transport loads suspended from a hook or any other type of holding

[1] Email from ***, to ***, Arizona Department of Revenue, (May 01, 2020, 15:16 AST) (on file with author).
[2] *Id.*
[3] Letter from ***, to Arizona Department of Revenue Tax Research & Analysis (Feb. 21, 2020) (on file with author).

mechanism. It has its power and directional system or which form part of a set so capacitated, allowing for its movement on roads and building sites."[4]

Construction hoists refer to "temporary elevators used to transport personnel and materials on a construction site. Also known as man and material elevators, construction hoists are powered by an electric motor and travel vertically along with a steel tower attached to the outside of a building during construction or renovation of the building."[5]

When Taxpayer provides a crane or hoist, the following related services may be provided as well:

1. Engineering (through a third-party professional engineer) related to the crane or hoist foundation and any connections to a building;
2. Hoist plans;[6]
3. Preparing the equipment for the specific job site;[7]
4. Transporting the equipment to and from the job site;
5. Setting up and dismantling the equipment;
6. Operating the equipment; and
7. Maintaining and repairing the equipment.

Additional services which may be provided by Taxpayer are not addressed in this ruling. Contracts and invoices document each service as separate line items. Cranes on which the Arizona Motor Carrier Fees have been paid are generally only available with an operator. Engineering services make up 0.54% of the total revenue over the last three years.[8]

DISCUSSION AND LEGAL ANALYSIS:

Arizona's TPT differs from the sales tax imposed by most states. It is a tax on the privilege of conducting business in the State of Arizona. Differing from a true sales tax, the TPT is levied on income derived by the seller, who is legally allowed to pass the economic expense of the tax on to the purchaser. However, the seller is ultimately liable to Arizona for the tax. The Arizona TPT is

[4] Self-propelled mobile crane, Construction Dictionary (Online ed. 2020), http://www.diccionariodelaconstruccion.com/en/structure-raising-phase/loading-and-lifting-machinery-in-the-productive-process/self-propelled-mobile-crane (last visited Apr 13, 2020).
[5] *Id*.
[6] Mobile crane jobs frequently, but not always, include lift plans. Lift plans are completed through a software program and do not require approval by an engineer. Tower crane and hoist jobs require foundation and tie in plans. A third party licensed engineer is required for all tower crane plans. Hoists sometimes, but not always, require an engineer. See Email from ***, to Arizona Department of Revenue, (Mar. 04, 2020, 13:53 AST) (on file with author).
[7] This includes maintenance, repairs, painting, re-configuring or modifying.
[8] Email from ***, to Arizona Department of Revenue, (Apr. 20, 2020, 15:16 AST) (on file with author).

imposed under sixteen separate business classifications. A.R.S. § 42-6102(A) provides that the state's TPT provisions shall govern the imposition of county excise taxes. All sales subject to TPT are also subject to applicable county excise taxes.

Personal Property Rental Classification

A.R.S. § 42-5071 imposes TPT on the business of leasing or renting tangible personal property for a consideration. The personal property rental classification is comprised of businesses that lease or rent tangible personal property. All income received by a lessor of tangible personal property is subject to TPT unless specifically exempted or deducted by statute.

Gross income from the rental of tangible personal property further "includes charges for installation, labor, insurance, maintenance, repairs, pick-up, delivery, assembly, set-up, personal property taxes, and penalty fees," even if such charges are billed as separate items.[9] Therefore, all charges associated with the rental of tangible personal property is taxable unless a separate statutory exclusion or deduction applies.

The *State Tax Commission v. Peck* Court set out guidelines for determining whether a particular activity is considered personal property rental.[10] It resolved the question of whether the facts presented before it constituted a rental by looking at the dictionary definition of the word "rent" which was defined as "(1) to take and hold under an agreement to pay rent," or "(2) to obtain the possession and use of a place or article for rent."[11]
The court determined that:

> When customers use the equipment on the premises of the plaintiffs . . . such customers have an exclusive use of the equipment for a fixed period of time and for payment of a fixed amount of money . . . the customers themselves exclusively control all manual operations necessary to run the machines. In our view such exclusive use and control comes within the meaning of the term "renting" as used in the statute.[12]

As may be gleaned from *Peck*, actual possession of the property by its transfer to the customer is not essential for a finding of control. Control may be found through exclusive use, or the renting party's ability to operate or use rented property on their own. *See City of Phoenix v. Bentley-Dille Gradall*

[9] Ariz. Admin. Code ("A.A.C.") R15-5-1502(D) (2020).
[10] *State Tax Comm'n v. Peck*, 106 Ariz. 394, 476 P.2d 849 (1970).
[11] *Peck.* at 396, 851.
[12] *Id.*, at 396, 851.

Rentals, Inc., 665 P.2d 1011, 1014, 136 Ariz. 289, 292 (Ariz.App.,1983) (finding that taxpayer did not rent machinery when it was provided with an operator who continued to maintain sufficient control over the machinery when "all fuel, maintenance, and repairs on the cranes were performed by the taxpayers, [and] the operator of the crane determined where and how the cranes were to operate and was in physical control of the crane at all times").

Motor Carrier Fee Deduction

A.R.S. § 42-5071(B)(4) provides a deduction from the personal property rental classification for income derived from the lease of motor vehicles where the motor carrier fee has been paid pursuant to A.R.S. § 28-5852. For purposes of the motor carrier fee, a motor vehicle is defined as "a self-propelled motor driven vehicle that has a declared gross vehicle weight of more than twelve thousand pounds and that is subject to vehicle registration before lawful operation on the public highways in this state, excluding a motor vehicle that is exempt from gross weight fees pursuant to section 28-5432."[13]

The motor carrier fee can be paid by the lessor, the lessee, or a third party authorized by the lessor or the lessee.[14] To substantiate the motor carrier fee deduction, the lessor must maintain the registration documentation stipulating that the annual motor carrier fee has been paid for that specific vehicle (identified by its vehicle identification number) for all of the periods included in the lease. If *the lessor* does not maintain such documentation for the leased vehicle, TPT will apply to any lease income received by the lessor for those periods in which the motor carrier fee was not paid.[15]

Prime Contracting Classification

A.R.S. § 42-5075 imposes TPT on "the business of prime contracting." The tax base for the prime contracting classification is sixty-five percent of a prime contractor's gross receipts derived from the business. See A.R.S. § 42-5075(B). The tax base for TPT generally includes gross sales without any deductions for any business expense. Any deductions, exemptions, or exclusions from TPT must be specifically provided for in statute and they are unique to each classification; so they cannot simply be applied into another tax classification for which they are not explicitly provided.

[13] A.R.S. § 28-5851(4).
[14] Arizona Transaction Privilege Tax Ruling TPR 03-2, 4 (Ariz. Dep't of Revenue Dec. 04, 2003).
[15] A.R.S. § 42-5009(B).

The term "contracting" means "engaging in business as a contractor." A.R.S. § 42 5075(R)(3) provides the following definition for the term "contractor":

> "Contractor" is synonymous with the term "builder" and means any person or organization that undertakes to or offers to undertake to, or purports to have the capacity to undertake to, or submits a bid to, or does personally or by or through others, modify any building …

Under A.R.S. § 42-5075(R)(6) "modification" means construction, grading and leveling ground, wreckage or demolition. And under A.R.S. § 42-5075(R)(7), "modify" means to make a modification or cause a modification to be made.

A.R.S. § 42-5075(N) provides an exclusion from taxation under the prime contracting classification for the gross proceeds of sales or gross income attributable to a written contract for professional services or design phase services, executed before modification begins and with terms, conditions and pricing of all of these services separately stated in the contract from those for construction phase services, regardless of whether the services are provided sequential to or concurrent with prime contracting activities that are subject to tax.

"Professional services" are defined to mean architect services, assayer services, engineer services, geologist services, and land surveying services or landscape architect services.[16]

"Design phase services" include, but are not limited to, preparing drawings and specifications for architectural program documents, schematic design documents, design development documents, modification work documents or documents that identify the scope of or materials for the project, and preparation of any submittals or shop drawings used by the prime contractor to illustrate details of the modification work performed. [17]

A.R.S. § 42-5075(K) provides a deduction for "[t]he portion of gross proceeds of sales or gross income attributable to the actual direct costs of providing architectural or engineering services that are incorporated in a contract is not subject to tax under this section. For the purposes of this subsection, 'direct costs' means the portion of the actual costs that are directly expended in providing architectural or engineering services."

A.R.S. § 42-5075(D) provides that subcontractors and others who perform modification activities are not subject to tax if they can demonstrate that the job was within the control of a prime contractor(s)

[16] A.R.S. § 42-5075(N)(3).
[17] A.R.S. § 42-5075(N)(2).

and that the prime contractor(s) is liable for the tax on the gross income attributable to the job and from which the subcontractors or others were paid.

A.R.S. § 42-5075(E) provides that amounts received by a contractor for a project are excluded from the contractor's gross proceeds of sales or gross income derived from the business if the person who hired the contractor executes and provides a certificate to the contractor stating that the person providing the certificate is a prime contractor and is liable for the tax. Additionally, that section provides that if the person who provides the certificate is not liable for the tax as a prime contractor, that person is nevertheless deemed to be the prime contractor in lieu of the contractor and is subject to the tax.[18]

Thus, the parties to a contracting transaction may designate the party that is the taxable prime contractor and who is therefore responsible for the TPT on a project. Contractors who receive a prime contractor's certificate, which designates the person hiring them as the prime contractor on a project, will not be required to pay TPT on their gross proceeds from the project.

Pursuant to A.R.S. § 42-5075(E), the department has adopted Arizona Form 5005, Prime Contractor's Certificate. The use of a certificate other than that adopted by the department is not effective to designate which party is deemed to be the prime contractor and responsible for the payment of the tax with regard to a contracting transaction. In addition, a certificate that has been altered by the taxpayer is not valid.

Separate Line of Business

The Arizona Supreme Court held that TPT is measured by all of the business activity of a taxpayer rather than merely a part of it.[19] Nevertheless, the Court later found that a person's activities may constitute more than one business and the taxpayer would be obligated to pay the appropriate tax on each business.[20]

In 1976, the Arizona Supreme Court addressed the issue of several lines of business in *Holmes & Narver*.[21] After stating that not all business is the subject of TPT (*i.e.*, only those businesses specifically set forth in the statutes), the Court set forth the following three-part test to determine

[18]Arizona Form 5005 is not to be used in lieu of the Arizona Form 5000 exemption certificate, or the Arizona Form 5009L exemption certificate, in order to purchase contracting materials tax exempt.
[19] *Duhame v. State Tax Comm'n*, 65 Ariz. 268, 179 P.2d 252 (1947).
[20] *Trico Elec. Co-op v. State Tax Comm'n*, 79 Ariz. 293, 297, 288 P.2d 782, 784 (1955).
[21] *State Tax Comm'n v. Holmes & Narver, Inc.*, 113 Ariz. 165, 548 P.2d 1162 (1976).

when a non-taxable service is deemed to be a separate line of business from taxable activities, not part of the primary business, and therefore non-taxable:

1. The portion of the business that is the service in issue can be readily ascertained without substantial difficulty;
2. The revenues from the service, in relation to the taxable revenues of the business, are not of consequence (i.e., not inconsequential); and
3. The service is independent from (cannot be said to be incidental to) the other taxable activity.[22]

In 1995, the Arizona Court of Appeals elaborated on the *Holmes & Narver* test, noting that "when the amount involved is not minimal, when it can be easily calculated, and when the service it relates to is not an integral part of the main business, the main and ancillary services can be separated for tax purposes."[23] The court determined that income from concededly nontaxable activity (the sale of gasoline) was part of the personal property rental classification tax base for city tax purposes. In so holding, the Court of Appeals stated:

> In summary, we conclude that because every Budget car rental contract includes a refueling charge, the charge is an integral part of Budget's car rental business. Because most customers return with a full gas tank, thus avoiding the refueling charge, the charge accounts for a minimal percentage of Budget's car rental business. Accordingly, refueling charges paid to Budget are taxable as gross income from the car rental business.[24]

Generally, a taxpayer's receipts from payments for various services offered in addition to another business activity could nevertheless be considered part of the business's taxable receipts, when the services are interwoven in and are an integral part of the taxpayer's business activity.

<u>City Tax</u>

It is important to note, the imposition of city privilege taxes is separate and distinct from the state's TPT and accompanying county excise taxes. As with the state's TPT, city privilege taxes are imposed on the vendor for the privilege of engaging in business in the city. The Model City Tax Code ("MCTC") was created in order to impose and administer city privilege taxes. Similar to Arizona's TPT, city

[22] *Id*. at 168-69, 1165-66.
[23] *City of Phoenix v. Ariz. Rent-A-Car Sys*., 182 Ariz. 75, 893 P.2d 75 (1995).
[24] *Id.* at 80.

privilege taxes are imposed "upon persons on account of their business activities." See MCTC § -400(a)(1). All Arizona cities follow the MCTC in the imposition of their privilege tax based upon their local ordinances. However, certain options exist, allowing each city to alter or qualify the imposition of its privilege tax.[25]

Rental, leasing, and licensing for use of tangible personal property

Similar to A.R.S. § 42-5071, MCTC § -450 imposes the city privilege tax on the rental, leasing and licensing for use of tangible personal property. However, separately stated charges for direct customer services and "delivery, installation, repair, and/or maintenance" are not taxable for city purposes.[26] MCTC Reg. § -450.5 provides additional guidance that delivery and installation charges are exempt when the provisions of MCTC Reg. § -100.2 have been met.[27]

MCTC Reg. § -100.2(a) states that "delivery charges" only exist "when the total charges to the ultimate customer or consumer include, as separately charged to the ultimate customer, charges for delivery to the ultimate consumer, whether the place of delivery is within or without the City, and when the taxpayer's books and records show the separate delivery charges." Delivery is defined by the *Merriam-Webster Dictionary* as "the act or manner of delivering something."[28] To deliver is defined as "to take and hand over to or leave for another."[29]

MCTC Reg. § -100.2(b) states that "'[i]nstallation'…relates only to attachment to tangible personal property. Installation to real property is deemed construction contracting in this Chapter. Examples of installation relating to tangible personal property are: installing a radio in an automobile; applying sun screens on the windows of a boat; installing cabinets, carpeting, or "built-in appliances" to a camper or motorized recreational vehicle."

[25] The MCTC can be found online at https://modelcitytaxcode.az.gov.
[26] MCTC § -450.
[27] 2019 Proposed Changes to the Model City Tax Code "2019 Retail Conformity Amendment," removed MCTC Reg. -100.2 as a regulation and included it as section -100.2 if legislation was passed enacting standards for imposing economic nexus on remote sellers.
[28] Definition of DELIVERY, Merriam-webster.com (2020), https://www.merriam-webster.com/dictionary/delivery (last visited Apr 13, 2020).
[29] Definition of DELIVER, Merriam-webster.com (2020), https://www.merriam-webster.com/dictionary/delivering (last visited Apr 13, 2020).

MCTC Reg. § -100.2(d) states that direct customer services are services, other than repairs, which are rendered directly to the customer and occur after transfer of the personal property. Services provided prior to transfer of the personal property are not included in this definition.

MCTC Reg. § -450.1(a)(3) clarifies that:

> (a) Rental, leasing, or licensing of earthmoving equipment with an operator shall be deemed construction contracting activity. Rental, leasing, or licensing of any other tangible personal property (with or without an operator) or of earthmoving equipment without an operator shall be deemed rental, leasing, or licensing of tangible personal property. For example:
>
> > (1) Rental of a backhoe, bulldozer, or similar earthmoving equipment with operator is construction contracting. Rental of these items without an operator is rental of tangible personal property.
> >
> > …
> >
> > (3) Rental of pumps or cranes is rental of tangible personal property, regardless of whether or not an operator is included with the equipment rented.

MCTC Reg. § -450.3 provides that "in cases where the tangible personal property is rented, leased, or licensed with an operator provided by the lessor, the charge for the operator shall not be includable in the gross income from the rental, lease, or license of such tangible personal property if the charge for the operator and the charge for the use of the equipment are separately itemized to the lessee and separately maintained on the books and records of the lessor."

MCTC § -266(b) allows an exemption from the gross income derived from "leasing, renting or licensing a motor vehicle subject to and upon which the fee has been paid under A.R.S. Title 28, Chapter 16." This motor carrier fee deduction includes motor vehicles which weigh less than 12,000 pounds (light motor vehicles), between 12,001 and 26,000 pounds (lightweight motor vehicles), and those weighing more than 26,000 (motor vehicles).

<u>Construction Contracting</u>

MCTC § -415 (together with A.R.S. § 42-6004(A)(14)) applies to construction contractors, whose activities and taxation are generally equivalent to that of prime contractors subject to TPT at the state level, as discussed above.

MCTC § -415(a)(4) provides that the gross income, attributable to the actual direct costs of providing architectural or engineering services that are incorporated into the contract, is not taxable.

Discussion

The gross income derived from a taxable business activity is presumed subject to TPT unless otherwise exempt. A business may be engaged in more than one taxable business activity and is subject to taxation under each classification under which it does business. Crane and hoist providers are often engaged in both personal property rental and prime contracting. The distinction is important as each classification provides exemptions and deductions that applies only to that specific classification.[30]

Personal Property Rental – State & County

The courts have provided that in order for a rental of tangible personal property to be considered taxable the lessee must have exclusive control of the property for the duration of the lease or rental agreement.[31] Accordingly, the gross income derived from providing tower cranes, mobile cranes and hoists without an operator—where the lessee has exclusive use and control throughout the duration of the contract—is taxable under the personal property rental classification, unless otherwise exempt. Gross income includes charges for the use of the equipment, engineering, hoist plans, and charges for preparing, transporting, setting up or dismantling, and maintaining or repairing the tower cranes, mobile cranes or hoists.

Tower Crane, Mobile Crane (Motor Carrier Fee NOT Paid), and Hoist without an Operator			
Charges by Lessor	TPT Consequence	Classification	Legal Authority
Engineering	Taxable	Personal Property Rental	A.R.S. § 42-5071(A)
Hoist Plans	Taxable	Personal Property Rental	A.R.S. § 42-5071(A)
Preparing Equipment	Taxable	Personal Property Rental	A.R.S. § 42-5071(A)
Transport	Taxable	Personal Property Rental	A.R.S. § 42-5071(A)
Setup	Taxable	Personal Property Rental	A.R.S. § 42-5071(A)
Dismantle	Taxable	Personal Property Rental	A.R.S. § 42-5071(A)
Operating	Taxable	Personal Property Rental	A.R.S. § 42-5071(A)
Maintenance & Repairs	Taxable	Personal Property Rental	A.R.S. § 42-5071(A)

[30] *Brink Elec. Constr. Co. v. Ariz. Dep't of Revenue*, 184 Ariz. 354, 359–60, 909 P.2d 421, 426–27 (Ct. App. 1995).
[31] *State Tax Comm'n v. Peck*, 106 Ariz. 394, 476 P.2d 849 (1970).

Motor Carrier Fee Deduction. A.R.S. § 42-5071(B)(4) provides that the gross proceeds of sales or income derived from leasing or renting a motor vehicle are not taxable when the motor vehicle is subject to, and the lessor has paid (directly or indirectly), the motor carrier fee. Neither a tower crane nor a hoist are self-propelled vehicles licensed for use on the highway and thus do not satisfy the statutory definition of motor vehicle, but a truck mounted mobile crane does.[32] Accordingly, the rental of a mobile crane, on which the motor carrier fee was paid, qualifies for this deduction. The deduction includes the gross proceeds of sales derived from the lease charges for use of the crane and all additional services—including engineering, hoist plans, preparing, transporting, setting up or dismantling, maintaining or repairing the crane, and fuel surcharges.

Mobile Crane - Motor Carrier Fee Paid without an Operator			
Charges by Lessor	TPT Consequence	Classification	Legal Authority
Engineering	Exempt	Personal Property Rental	A.R.S. § 42-5071(B)(4)
Hoist Plans	Exempt	Personal Property Rental	A.R.S. § 42-5071(B)(4)
Preparing Equipment	Exempt	Personal Property Rental	A.R.S. § 42-5071(B)(4)
Transport	Exempt	Personal Property Rental	A.R.S. § 42-5071(B)(4)
Erection	Exempt	Personal Property Rental	A.R.S. § 42-5071(B)(4)
Dismantle	Exempt	Personal Property Rental	A.R.S. § 42-5071(B)(4)
Operating	Exempt	Personal Property Rental	A.R.S. § 42-5071(B)(4)
Maintenance & Repairs	Exempt	Personal Property Rental	A.R.S. § 42-5071(B)(4)
Fuel Surcharges	Exempt	Personal Property Rental	A.R.S. § 42-5071(B)(4)

Separate Line of Business. The gross income derived from the engineering services is part of the taxable gross income of the business, unless these activities are found to be a nontaxable separate line of business using the *Holmes & Narver* test.

It appears that the engineering services are readily ascertained as Taxpayer separately states and accounts for them on the books and records of the business. As well, similar to *Holmes & Narver*, Taxpayer's engineering services are not incidental to providing cranes and hoists. The primary question here is whether the revenues from the engineering services are inconsequential.

[32] A.R.S. § 25-5601(19) defines a motor vehicle as "a self-propelled vehicle required to be licensed or subject to licensing for operation on a highway."

No court has established a bright line threshold percentage to determine if the revenues are inconsequential or not. However, by way of a guideline "[i]n *Holmes & Narver*, the court considered design fees of 43% to be significant. By contrast, the percentage found by the court to be inconsequential in *Arizona Rent-A-Car Systems, Inc*. was approximately 2%. A percentage of less than 6% suggests that Taxpayer was not engaged in a separate design business."[33]

Taxpayer's total percentage of gross income derived from providing engineering services is less than 1% over the last three years. Accordingly, Taxpayer's engineering services are not a separate nontaxable line of business.

Personal Property Rental - City

For purposes of city privilege tax, tower cranes, mobile cranes or hoist rentals—*with or without operators*—are taxable as rental, leasing, and licensing for use of tangible personal property. Charges for transport, and maintenance or repair—*i.e.,* direct customer services—are not taxable if separately stated.[34] Where an operator is provided, charges for the operator are not taxable if separately stated.[35]

The MCTC provides that services or labor provided by any person prior to the transfer of tangible personal property to the customer or consumer are not included in the definition of direct customer services.[36] Preparing the equipment is a service that occurs prior to the transfer of the tangible personal property and therefore it does not fall in the definition of direct customer services.

Installation is considered a nontaxable direct customer service only when the attachment relates to tangible personal property, and "[i]nstallation to real property is deemed construction contracting."[37] Thus, erection and dismantling of the tower crane and hoist are taxable as construction contracting as setup and dismantling are only excluded when the rented property is attached, or installed, to tangible personal property. Preparing engineering and hoist plans are part of the construction contracting services.

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[33] Arizona Department of Revenue, *The Director's Review of the Decision of the Administrative Law Judge*, Case No. 200200180-S (2003).
[34] MCTC § -450.
[35] MCTC Reg. -450.3.
[36] MCTC § -100.2(d).
[37] *Id*. § -100.2(b).

Erection or setup of the mobile crane does not require installation into real property and generally requires the operator to place the outrigger pads on the ground and then drop the outriggers onto the pads.[38] Accordingly, erection and setup of a mobile crane is not construction contracting activity.

Tower Crane, Mobile Crane (Motor Carrier Fee NOT Paid), and Hoist with or without an Operator			
Charges by Lessor	TPT Consequence	Classification	Legal Authority
Engineering	See Below	Construction Contracting	MCTC § -415(a)(4)
Hoist Plans	See Below	Construction Contracting	MCTC § -100.2(d
Preparing Equipment	Taxable**	Personal Property Rental	MCTC § -450
Transport	Deductible*	Personal Property Rental	Reg. § -450.5
Erection – Mobile Crane	Deductible*	Personal Property Rental	MCTC § -450
Dismantle – Mobile Crane	Deductible*	Personal Property Rental	MCTC § -450
Setup	See Below	Construction Contracting	MCTC § -100.2(d)
Dismantle	See Below	Construction Contracting	MCTC § -100.2(d)
Operating	Deductible*	Personal Property Rental	Reg. § -450.1(a)(3)
Maintenance & Repairs	Deductible*	Personal Property Rental	MCTC § -450
* Deductible only separately stated ** Maintenance and repairs provided during the rental are deductible, however, maintenance and repair in anticipation of a rental are taxable.			

Motor Carrier Fee Deduction - City. MCTC § -266(b) provides that the gross income derived from leasing or renting a motor vehicle are not taxable when the motor carrier deduction has been paid on a light motor vehicle, lightweight motor vehicle and motor vehicle. A tower crane and hoist are not motor vehicles and do not qualify for this deduction. Accordingly, the gross income derived from a mobile crane on which the motor carrier fee includes all charges for the use of the mobile crane and all additional services—including engineering, hoist plans, preparing, transporting, erecting or dismantling, maintaining or repairing the crane, and fuel surcharges—are not taxable.

Mobile Crane - Motor Carrier Fee Paid with or without an Operator			
Charges by Lessor	TPT Consequence	Classification	Legal Authority
Engineering	Exempt	Personal Property Rental	MCTC § -266(b)
Hoist Plans	Exempt	Personal Property Rental	MCTC § -266(b)
Preparing Equipment	Exempt	Personal Property Rental	MCTC § -266(b)

[38] Smaller cranes may also require adding counterweights.

Transport	Exempt	Personal Property Rental	MCTC § -266(b)
Setup	Exempt	Personal Property Rental	MCTC § -266(b)
Dismantle	Exempt	Personal Property Rental	MCTC § -266(b)
Operating	Exempt	Personal Property Rental	MCTC § -266(b)
Maintenance & Repairs	Exempt	Personal Property Rental	MCTC § -266(b)
Fuel Surcharges	Exempt	Personal Property Rental	MCTC § -266(b)

Prime Contracting – State and County

Providing a crane *and* an operator for use on a modification construction project is contracting activity and taxable under the prime contracting classification by the state and counties.[39] The tax base for the prime contracting classification is sixty-five percent of the gross income derived from the contracting activities, unless otherwise excluded.[40] Mobile cranes with an operator are taxable under prime contracting and, unlike the personal property rental classification, there is no deduction for a mobile crane on which the motor carrier fee is paid.

The gross income derived from providing engineering and design phase services are not taxable when the terms, conditions, and pricing are separately stated and executed before the crane or hoist activities begin.[41] This deduction applies to the gross income derived from the engineering and design phase services and not their actual cost. Thus, any markup applied to the services is also deductible. Preparing hoist plans using computer-aided design ("CAD") software (or by any other method) is deductible as a design phase service.[42] However, if the terms, conditions, and costs of the engineering services, or hoist plan preparations, are not separately stated, or if the terms are executed after the crane or hoist activities have begun, then this deduction will not apply. If A.R.S. § 42-5075(N) does not apply, then the deduction in A.R.S. § 42-5075(K) may apply for the actual direct costs associated with the engineering services.

[39] *City of Phoenix v. Bentley-Dille Gradall Rentals, Inc*. 136 Ariz. 289; 665 P.2d 1011 (Ct. App. 1983) (finding that a company providing machines with operators to a construction site was contracting activity and not personal property rental).
[40] A.R.S. § 42-5075(O) exempts maintenance, replacement, repair and alteration ("MRRA") projects from the prime contracting classification. The value of alteration activities—causing a direct physical change to the property (not previously existing) or which cannot otherwise be classified as maintenance, repair or replacement—cannot exceed $750,000 on a commercial property. If the total value of the alteration activities exceed the threshold, they are then re-classified and taxable as modification under the prime contracting classification.
[41] A.R.S. § 42-5075(N).
[42] A.R.S. § 42-5075(N)(2)(c).

A.R.S. § 42-5075(K) provides that the actual direct costs (not including markup) *expended* for engineering services—including third-party engineering subcontracted costs—are not taxable.[43] To substantiate the deduction: (1) the engineering or architectural service must have been performed or approved by a licensed engineer; and (2) the income from the service must be directly attributable to providing engineering services.[44] If hoist plans are not provided by an architect or engineer then the actual direct costs for hoist plans will not qualify under A.R.S. § 42-5075(K).

Lastly, as a subcontractor, Taxpayer is not subject to TPT under the prime contracting classification if Taxpayer is able to demonstrate that the job was within the control of a prime contractor who is liable for the tax on the gross income attributable to the job. In order to demonstrate control by a prime contractor that prime contractor must provide Taxpayer with a completed AZ Form 5005.

Tower Crane, Mobile Crane (With or Without Motor Carrier Fee), and Hoist with an Operator[45]			
Charges by Lessor	TPT Consequence	Classification	Legal Authority
Engineering	Deductible*	Prime Contracting	A.R.S. § 42-5075(N) or (K)
Hoist Plans	Deductible*	Prime Contracting	A.R.S. § 42-5075(N) or (K)
Preparing Equipment	Taxable	Prime Contracting	A.R.S. § 42-5075(B)
Transport	Taxable	Prime Contracting	A.R.S. § 42-5075(B)
Setup	Taxable	Prime Contracting	A.R.S. § 42-5075(B)
Dismantle	Taxable	Prime Contracting	A.R.S. § 42-5075(B)
Operating	Taxable	Prime Contracting	A.R.S. § 42-5075(B)
Maintenance & Repairs	Taxable	Prime Contracting	A.R.S. § 42-5075(B)

[43] Expended costs could include the costs of a third party engineer or the wages associated with the time spent by an internal licensed engineer employee.

[44] "Engineering services" for purposes of A.R.S. § 42-5075(K) means professional services solely of an engineering nature that are required to be performed or approved by a person registered, licensed, or certified by state law to provide such services, including the registered, licensed, or certified person's employee or outside third-party consultant necessary for the performance of the contract's engineering services. See Arizona Transaction Privilege Tax Ruling TPR 06-2.

[45] As required by *Peck*, a customer does not have exclusive use and control of rented equipment when an operator is provided for part of the contract period. See *State Tax Comm'n v. Peck*, 106 Ariz. 394, 476 P.2d 849 (1970). Accordingly, this is not a rental for state and county purposes but rather it is classified as prime contracting activity. See *City of Phoenix v. Bentley-Dille Gradall Rentals, Inc*. 136 Ariz. 289; 665 P.2d 1011 (Ct. App. 1983). However, if the contract provides that an operator is provided for some, but not all of the rental, then as a cash basis reporter it is taxable as personal property rental during the reportable tax periods when no operator is provided. For the tax periods an operator is provided, it should then be reported as a cash basis reporter as prime contracting for state and county purposes (city privilege tax is not affected by this as with, or without, an operator it is taxable as personal property rental).

* Taxable if not separately stated and engineering and hoist plans (under A.R.S. § 42-5075(N)) must be contracted for and agreed on before the contracting activities begin. ** The prime contracting TPT liability may be assumed by the hiring contractor if an AZ Form 5005 is provided to Taxpayer, for this job type and any other which is taxable under the prime contracting classification. However, the city privilege tax liability, which is taxable under rental, leasing, and licensing for use of tangible personal property, may not be assigned to the prime contractor. ***This chart presumes the activity is modification and not exempt under A.R.S. § 42-5075(O).

Prime Contracting - City

The MCTC regulations provide that cranes (including mobile cranes) and hoist rentals are taxable as rentals (see the discussion above).[46] However, the regulations also clarify that installation of rented personal property into real property is taxable as construction contracting.[47] Accordingly, as the tower cranes and hoists are installed into the ground, or the side of the building, sixty-five percent of the gross income derived from the installation is taxable as construction contracting. The gross income derived from the engineering and preparation of hoist plans are associated with the installation—*i.e.*, contracting activity—and the engineering fees are therefore deductible from the tax base.[48] Preparing hoist plans without the use of an architect or engineer are not deductible.

Tower Crane and Hoist with or without an Operator			
Charges by Lessor	TPT Consequence	Classification	Legal Authority
Engineering	Deductible*	Construction Contracting	MCTC § -415(a)(4)
Hoist Plans	Taxable**	Construction Contracting	MCTC § -100.2(d
Erection	Taxable	Construction Contracting	MCTC § -100.2(d)
Dismantle	Taxable	Construction Contracting	MCTC § -100.2(d)
* If an architect or engineer are used these charges are deductible when separately stated. **This chart presumes the activity is modification and not exempt under A.R.S. § 42-5075(O).			

The deductions summarized and discussed in the charts above refer only to those deductions discussed in this ruling and are available for any job. This ruling does not contemplate other

[46] MCTC Reg. § -450.1(a)(3).
[47] MCTC Reg. § -100.2(d)
[48] See *Brink Elec. Const. Co. v. Arizona Dep't of Revenue*. 184 Ariz. 354, 909 P.2d 421 (Ct. App. 1995) (finding that a contractor's activities do not qualify for exemptions under other business classifications and a contractor may only claim the exemptions listed under the contracting classification).

deductions which may apply to the entire job, such as a contracting activities or rentals to qualifying hospitals, etc.

This response is a private taxpayer ruling and the determinations herein are 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 private 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.

The determinations in this private taxpayer ruling are only applicable to the taxpayer requesting the ruling and may not be relied upon, cited nor introduced into evidence in any proceeding by a taxpayer other than the taxpayer who has received the private taxpayer ruling. In addition, this private taxpayer ruling only applies to transactions that occur or tax liabilities that accrue from and after the date the taxpayer receives the ruling.