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ARIZONA TRANSACTION PRIVILEGE TAX RULING TPR 16-1 (This ruling rescinds and supersedes TPR 08-1)

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ISSUES:

1. What factors determine if an out-of-state business has a “substantial nexus” with Arizona for purposes of imposing Arizona’s transaction privilege or use taxes and municipal privilege taxes?
2. Once nexus is established, how should an out-of-state business determine the appropriate tax rate for calculating transaction privilege tax? (“sourcing” rules)

BACKGROUND:

Transaction Privilege Tax. Arizona’s transaction privilege tax (TPT) is a tax on the privilege of conducting business in the State of Arizona. TPT is levied on the business rather than the customer. The business may pass the burden of the tax on to its customer; however, the business is ultimately liable to Arizona for the tax. TPT is imposed under various types of business classifications, which are listed in Article 2, Chapter 5, Title 42 of the Arizona Revised Statutes (A.R.S.).

A business does not have to have a physical location in Arizona to be subject to TPT. An out-of-state business may be subject to TPT if the business is engaged in an activity within Arizona under one of the taxable business classifications *and* it has a “substantial nexus” with Arizona, as explained below. If a person engaged in business within Arizona does not have a substantial nexus for TPT purposes, Arizona’s use tax may apply.

Municipal Privilege Tax. Arizona municipalities levy and impose their own municipal privilege tax under the Model City Tax Code. Similar to the Arizona TPT, the municipal privilege tax is levied on the business rather than the customer. Pursuant to Title 42, Chapter 5, Article 6, Arizona Revised Statutes, the taxes imposed under the Model City Tax Code are to be administered pursuant to Title 42, Chapter 5. As such, a business that is found to have nexus for Arizona TPT purposes is deemed to have nexus for municipal privilege tax.

**ARIZONA TRANSACTION PRIVILEGE
TAX RULING TPR 16-1**

(This ruling rescinds and supersedes TPR 08-1)

Page 2

Use Tax. Arizona's use tax complements the transaction privilege tax in that both taxes are intended to reach all applicable transactions, by imposing *either* TPT on the business *or* a use tax on the purchaser/customer. Use tax is imposed on a person who stores, uses or consumes tangible personal property in Arizona that was purchased from an out-of-state business. The purchaser is generally liable for the use tax. However, an out-of-state business may be liable for collecting the tax on Arizona's behalf. A business is generally subject to the duty to collect use tax if TPT does not apply and a sufficient nexus for use tax purposes exists.

Substantial Nexus. "Nexus" refers to the connection between a state and a person or business. To have "substantial nexus" means a sufficient degree of connection exists between the two such that the state may impose its taxes on the person or business. The degree of connection required to have substantial nexus depends on various factors, as well as facts relating to the person or business and the activity sought to be taxed. A finding of substantial nexus varies from situation to situation.

Substantial nexus is a requirement under the "Dormant" (or "Negative") Commerce Clause, which prohibits state taxation from unduly burdening interstate commerce.¹ It should not be confused with the term "minimum contacts." "Minimum contacts" is a requirement under the Due Process Clause of the Fourteenth Amendment, and refers to the minimum amount of purposeful contact a nonresident person or business must have with a state in order for that state's exercise of jurisdiction over the person or business to be proper and fair. The two requirements may sound identical; however, they are not.² While the Commerce Clause is concerned about a state's interference with interstate commerce, the Due Process Clause is concerned about giving a person "fair warning" or notice regarding state jurisdiction. More importantly, the amount of contacts needed to satisfy either requirement differs from the other. This means a business's activities may satisfy the "minimum contacts" requirement but may not satisfy the substantial nexus requirement.

RULING:

A substantial nexus with Arizona must be present in order for Arizona to impose either TPT or the duty to collect use tax on an out-of-state business. For either tax, the substantial nexus requirement is generally satisfied if any person or business resides in

¹ Under the Dormant Commerce Clause, a state tax does not unduly burden interstate commerce if it: (1) "*is applied to an activity with a substantial nexus with the taxing State,*" (2) "*is fairly apportioned,*" (3) "*does not discriminate against interstate commerce,*" and (4) "*is fairly related to the services provided by the [taxing] State.*" *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977) (emphasis added).

² *Quill Corp. v. North Dakota*, 504 U.S. 298, 312 (1992) (comparing the substantial nexus requirement under the Dormant Commerce Clause with the "minimum contacts" requirement under the Due Process Clause of the Fourteenth Amendment and concluding they are not identical as they are "animated by different constitutional concerns and policies.").

**ARIZONA TRANSACTION PRIVILEGE
TAX RULING TPR 16-1**

(This ruling rescinds and supersedes TPR 08-1)

Page 3

Arizona; maintains an inventory warehouse or place of business in Arizona; or maintains an employee, independent contractor or other business representative or agent in Arizona. In all other instances, a case-by-base determination must be made.

The crucial question to ask when determining substantial nexus is whether the activities performed in Arizona for (or on behalf of) a business are significantly associated with the business's ability to establish and maintain a business market in Arizona.³ In answering this question, Arizona considers: (1) the type of activity or activities performed in Arizona for or by a business; and (2) the degree of activity (e.g., how often or for how long a certain activity occurs, and what effect an activity or a set of activities has on a business's market in Arizona, etc.).

(1) *The type of activity or activities performed in Arizona for or by a business.* The following is a general list of certain activities or factors that may, by themselves or in conjunction with others, establish a substantial nexus ("nexus factors"):

- The business has an employee present in Arizona for more than two days per year.
- The business maintains an office or other place of business, internet kiosk or a locally listed telephone number in Arizona.
- The business owns or leases real or personal property in Arizona.
- The business maintains an inventory of products in Arizona.
- The business's merchandise or goods is/are delivered into Arizona on vehicles owned or leased by the business.
- An independent contractor or other non-employee representative/agent is present in Arizona for more than two days a year, and acts on the business's behalf to promote the business's commercial interests.
- Other activities are performed in Arizona for or on behalf of the business that enable the business to establish or maintain a market in Arizona.
 - Such activities may include: soliciting sales; securing deposits on sales; collecting delinquent accounts; conducting banking activities; delivering property sold to customers; installing products; making repairs; conducting training for customers or for employees or representatives of the business; resolving customer complaints; providing consulting services; soliciting, negotiating or entering into business or other franchising agreements; maintaining or improving the business's name recognition, market share, goodwill or individual customer relationships.
 - For affiliated companies and businesses, such activities may also include: cross-promotion and advertising; marketing to promote the operations of

³ This test was applied by the Arizona Court of Appeals in two cases: *Arizona Department of Revenue v. Care Computer Systems, Inc.*, 197 Ariz. 414, 416 (Ct. App. 2000), and *Arizona Department of Revenue v. O'Connor, Cavanagh, Anderson, Killingsworth & Beshears, P.A.*, 192 Ariz. 200, 205 (Ariz. Ct. App. 1997).

ARIZONA TRANSACTION PRIVILEGE

TAX RULING TPR 16-1

(This ruling rescinds and supersedes TPR 08-1)

Page 4

the affiliated business; accepting returns or exchanging merchandise purchased from the affiliated business; selling gift cards redeemable through any affiliated business; issuing credit for returned or exchanged merchandise purchased from the affiliated business, redeemable through any affiliated business; maintaining or providing a telephone or internet kiosk through which customers may purchase merchandise or access inventories from the affiliated business; accepting orders for the affiliated business; fulfilling orders made through the affiliated business; providing a location at which the affiliated business's customers may enroll in that business's "member benefits" or other type of discount/benefits program.

An out-of-state business that sells merchandise to customers in Arizona may not be subject to tax if all of the following are true:

- None of the nexus factors above applies to the business;
- The business makes the sale from an out-of-state location; and
- The business delivers the merchandise to the customer by U.S. mail or common carrier only.⁴ This is limited to agreements that include FOB shipping point provisions.

(2) *The degree of activity.* The degree of activity performed by a business that is sufficient to satisfy the substantial nexus requirement will depend on certain factors including:

- The function or purpose of the activity.
- The frequency and duration of the activity.
- The activity's connection with or impact on the business's in-state market.

As a general matter, the more frequently an activity occurs within Arizona or the longer the activity lasts within Arizona the more likely it will have an impact on the business's in-state market, suggesting the substantial nexus requirement will be satisfied. On the other hand, if the business's activities are limited and its function or purpose is of an inconsequential or de minimis nature, they may not impact the business's in-state market nor establish a substantial nexus with Arizona.

Moreover, certain activities will have a more significant impact than others when it comes to the business's Arizona market and by themselves could satisfy the substantial nexus requirement, regardless of whether those activities occur frequently or result in sales or revenue. For example, if an out-of-state business

⁴ See *Quill Corp.*, 504 U.S. at 311, 315 (affirming the position that "a vendor whose only contacts with the taxing State are by mail or common carrier lacks the 'substantial nexus' required by the Commerce Clause" and that such vendors are free from state-imposed duties to collect sales and use taxes).

**ARIZONA TRANSACTION PRIVILEGE
TAX RULING TPR 16-1**

(This ruling rescinds and supersedes TPR 08-1)

Page 5

employs an Arizona resident to advertise the business and call potential customers in Arizona but no sales result, the advertising and calling potential customers may be enough to satisfy the substantial nexus requirement. In the same example, however, if the employee is not an Arizona resident and only comes into Arizona one day a year to advertise, the argument for substantial nexus is weakened and other business activities may need to be examined.

TPT vs. Use Tax Collection. There is no clear national standard that distinguishes between the substantial nexus requirement for TPT and the substantial nexus requirement for use tax. Arizona takes the position that a higher level of nexus is not required to impose TPT over use tax and will generally impose TPT rather than use tax if a substantial nexus is present.⁵ In determining which tax is appropriate, Arizona *may* consider whether the activities that establish a nexus are related or unrelated to the business activity sought to be taxed – this consideration is derived from the United States Supreme Court’s reasoning in *National Geographic Society v. California Board of Equalization*, 430 U.S. 551 (1977).

The taxpayer in *National Geographic* was a nonprofit society that published a national magazine and sold certain other products at retail. The taxpayer was headquartered on the east coast, but it maintained two offices in California for the sole purpose of soliciting advertising for its magazine. California imposed the duty to collect use taxes on the taxpayer for its retail sales to California residents. In response, the taxpayer argued there was no substantial nexus to impose the tax, specifically that its two California offices did not establish a nexus because those offices did not perform any activities related to the taxpayer’s *retail sales*. The taxpayer argued “in other words that there must exist a nexus or relationship not only between the seller and the taxing State, but also between the activity of the seller sought to be taxed and the seller’s activity within the State.” *Id.* at 560. The Court rejected the taxpayer’s argument.

The Court explained a state is not barred from imposing the use tax collection duty simply because there is dissociation or lack of relationship between the particular business transactions relied on by the state to establish nexus, and the local business activity sought to be taxed. Therefore, the Court’s rejection established that the substantial nexus requirement for use tax purposes may generally be satisfied through a person or business’s in-state activities even if those activities are unrelated to the business activity sought to be taxed by the state. This further means the substantial nexus requirement for the use tax collection duty could be satisfied by the unrelated in-state activities of a business partner, affiliate or subsidiary. *Id.*

⁵ See *Care Computer Sys., Inc.*, 197 Ariz. at 416 (rejecting the argument that “a retail transaction privilege tax requires a higher level of nexus with the taxing state than does a use tax.”).

**ARIZONA TRANSACTION PRIVILEGE
TAX RULING TPR 16-1**

(This ruling rescinds and supersedes TPR 08-1)

Page 6

The Court did not state whether a similar dissociation or lack of relationship would prevent a state from imposing TPT or a sales tax. As part of its rejection of the taxpayer's argument, the Court did however compare use tax collection to a "direct tax" on interstate sales (such as a sales tax), and stated: however "fatal" a showing of such a dissociation may be to a direct tax, such a dissociation does not bar the imposition of a use tax collection duty.^{6,7} Although this explanation does not mean TPT requires a greater degree of relationship than use tax, it could be interpreted to mean that, if a state seeks to impose a tax similar to a sales tax, the activities establishing nexus must more or less be related to the activity sought to be taxed. [Note: The Department has not adopted this interpretation but may consider it when making nexus determinations. Requests for nexus determinations should be sent to the Department at the address below.]

Determining the Appropriate Tax Rate ("Sourcing Rules"). If TPT applies, a business may rely on Arizona's "sourcing" rules to determine the appropriate tax rate. There are five categories of sourcing rules: (1) general retail sales; (2) sales of construction materials to be incorporated or fabricated into a prime contracting project; (3) sales of construction materials to be incorporated or fabricated into a *non*-prime contracting project; (4) sales of manufactured buildings; and (5) leasing or rental activities.

(1) *General retail sales* (sales not included under another category of sourcing rules). The tax rate is determined by where the sales order is received, not where the purchaser resides or maintains a place of business. An order is "received" when all information necessary to accept the order has been received by or on behalf of the seller, regardless of where the order is accepted or approved. See A.R.S. § 42-5040(A)–(B).

- If a seller receives the sales order at a business location in Arizona, the sale is "sourced" to that business location and the tax rate in effect at that location will apply.
- If a seller receives the sales order at a business location outside Arizona, the sale is sourced to the purchaser's location in Arizona and the tax rate in effect at that location will apply. The seller may rely on a purchaser's shipping address to determine the purchaser's location.

⁶ *National Geographic*, 430 U.S. at 560 ("However fatal to a direct tax a 'showing that particular transactions [a]re dissociated from the local business' . . . such dissociation does not bar the imposition of the use-tax-collection duty.") (internal citations omitted).

⁷ Reference to a "direct tax" is for explanatory purposes only. The U.S. Supreme Court no longer relies on the formal distinction between direct and indirect taxes when determining the constitutionality of a tax. See *Quill Corp.*, 504 U.S. at 310 ("*Complete Auto* rejected . . . [the] formal distinction between 'direct' and 'indirect' taxes on interstate commerce because that formalism allowed the validity of statutes to hinge on 'legal terminology,' 'draftsmanship and phraseology.'") (internal citations omitted).

**ARIZONA TRANSACTION PRIVILEGE
TAX RULING TPR 16-1**

(This ruling rescinds and supersedes TPR 08-1)

Page 7

- If the local jurisdiction where the transaction is sourced does not tax the transaction, the municipal tax rate is zero.
- (2) *Sales of construction materials to be incorporated or fabricated into a prime contracting project.* If the sale is made to a TPT-licensed contractor or subcontractor and no tax was assessed on the purchase price due to an exemption or deduction, the sale is sourced to the location of the construction project or job site. The rate in effect at that location for *prime contracting* will apply. See A.R.S. § 42-5008.01(A)(1).⁸
- (3) *Sales of construction materials to be incorporated or fabricated into a non-prime contracting project* (e.g., the maintenance, repair, replacement or alteration of existing property or “MRRA” projects). If the sale is made to a TPT-licensed contractor or subcontractor and no tax was assessed on the purchase price due to an exemption or deduction, the sale is sourced to the location of the construction project or job site.⁹ The tax rate in effect at that location for *retail* sales will be used to calculate the *TPT-equivalent* fee due under A.R.S. § 42-5008.01.¹⁰ However, if after purchasing the materials tax-free, the contractor cancels the TPT license and discards the materials or sells them in a manner that is not subject to tax, the activity is sourced to the location of the contractor’s principal place of business and the tax rate in effect at that location for *retail* sales will be used. See A.R.S. § 42-5008.01(A)(1).
- (4) *Sales of manufactured buildings* (under the prime contracting classification). For sales in Arizona, the tax rate is determined by whether the seller contracts to deliver the manufactured building to a setup site or to perform the setup in Arizona. See A.R.S. 42-5075(M).
- If the seller contracts to deliver the manufactured building to a setup site or to perform the setup in Arizona, the sale is sourced to the setup site. The tax rate in effect at that location will apply.
 - If the seller does not contract to deliver the manufactured building to a setup site or does not perform the setup in Arizona, the sale is sourced to the

⁸ See *City of Phoenix v. Bentley-Dille Gradall Rentals, Inc.*, 136 Ariz. 289, 291 (Ct. App. Ariz. 1983).

⁹ See *Bentley-Dille Gradall Rentals, Inc.*, 136 Ariz. at 291.

¹⁰ MRRA projects are not subject to TPT under any classification. Construction materials to be incorporated or fabricated into a MRRA project are also not subject to TPT, but are instead subject to a fee that is *equivalent* to the TPT rate for retail sales. See A.R.S. § 42-5008.01(A)(1). To calculate the TPT-equivalent fee, a contractor will use the TPT rate for retail sales that is in effect where the construction project or job site is located (or, if applicable, the contractor’s principal place of business).

**ARIZONA TRANSACTION PRIVILEGE
TAX RULING TPR 16-1**

(This ruling rescinds and supersedes TPR 08-1)

Page 8

seller's location where the building is delivered to the customer. The tax rate in effect at that location will apply.

(5) *Leasing or rental activities.* The determinative factor is whether the lessor has a business location in Arizona. See A.R.S. § 42-5040(C)–(D).

- If the lessor has a business location in Arizona, the activity is sourced to the lessor's in-state business location as it appears on the lessor's TPT license. The tax rate in effect at that location will apply.
- If the lessor does not have a business location in Arizona, the activity is sourced to the lessee's location in Arizona and the tax rate in effect at that location will apply. A lessor may rely on the lessee's residential address for this purpose or, if the lessee is a business, on the business's primary address.

A taxpayer may use this ruling to self-assess whether the substantial nexus requirement is satisfied for TPT or use tax purposes. The taxpayer may also request a nexus determination by sending a request, including *detailed* information about the taxpayer's business activities within Arizona, to:

Arizona Department of Revenue
Transaction Privilege and Use Tax Nexus Section
1600 W. Monroe, 5th Fl.
Phoenix, AZ 85007
(602) 716-6533

EXAMPLES:

1. Corporation is a mail order vendor that ships to customers across the country. Its principal place of business is in Missouri where it receives all sales orders. The only contacts Corporation X has with Arizona are that it mails its catalogues and supplemental advertising flyers to active or recent customers located in Arizona twice a year, and delivers any orders to Arizona customers via U.S. mail or a common carrier. It has no place of business, distribution or sales house or warehouse in Arizona. It has no agent, salesperson, solicitor, delivery person or other type of representative in Arizona. It does not own any property (real or personal) in Arizona, nor does the corporation advertise in Arizona. Is the substantial nexus requirement met?

Conclusion: No. Corporation's mail order activities by themselves do not satisfy the substantial nexus requirement to impose TPT or use tax. See, e.g., *Nat'l Bellas Hess, Inc. v. Illinois Dep't of Revenue*, 386 U.S. 753 (1967) (concluding that taxing state cannot impose a use tax on an out-of-state business because a nexus could

**ARIZONA TRANSACTION PRIVILEGE
TAX RULING TPR 16-1**

(This ruling rescinds and supersedes TPR 08-1)

Page 9

not be established where the business's only contacts with the state were through U.S. mail or a common carrier); *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992) (concluding that taxing state lacks a substantial nexus to impose its use tax on a business that is an out-of-state mail-order house with no physical presence or significant real property in the taxing state, nor any outlets, employees or sales representatives in the taxing state).

2. Corporation's principal place of business is in New Orleans. It owns and operates 13 department stores in various locations in Arizona. It also employs 5,000 workers and has thousands of customers in Arizona. Corporation contracts with a third-party company located outside Arizona to design, print and mail catalogs to existing and potential customers, for the purpose of advertising Corporation's business, promoting sales and instilling name recognition in future customers. As part of instructions to the company, Corporation provided a list of Arizona customers to whom the catalogs should be mailed and further instructed the company to send any undelivered catalogs back to Corporation in New Orleans. Corporation did not pay any taxes on the production or purchase of any of the catalogs distributed in Arizona. Arizona wants to impose use tax on Corporation for its purchase and use of the catalogs in Arizona. Is the substantial nexus requirement satisfied?

Conclusion: Yes. Corporation is subject to transaction privilege tax. Corporation's catalog distribution in Arizona, as well as its in-state retail locations and significant volume of in-state sales, are sufficient activity within Arizona to satisfy the substantial nexus requirement. Notably, the catalog distribution by itself is satisfactory because the catalogs were intended to improve Corporation's sales and name recognition in Arizona. Corporation also had sufficient control over the distribution process in Arizona, from ordering and paying for them, to providing the list of Arizona recipients, to retaining possession of the undelivered catalogs. See, e.g., *D.H. Holmes Co., Ltd. v. McNamara*, 486 U.S. 24 (1988) (concluding that taxing state has substantial nexus to impose its use tax on an out-of-state business that actively distributes its catalog in-state and has in-state retail locations and employees).

3. Organization owns a national magazine. It also operates a "mail-order business" that sells maps, atlases, globes and books at retail. Orders for the mail-order business are made using forms mailed to subscribers or nonprofit members of Organization's national magazine or that are provided as part of the national magazine. Completed order forms are mailed directly to Organization's headquarters in the District of Columbia, where the orders are fulfilled. Organization also maintains two offices in Arizona; those offices solicit advertising copy for the national magazine and do not perform any activities related to the mail-order business. Is the substantial nexus requirement satisfied for mail-order sales in Arizona?

Conclusion: Yes. Organization is subject to transaction privilege tax. Organization's Arizona offices establish a substantial nexus even though those offices' activities are

ARIZONA TRANSACTION PRIVILEGE

TAX RULING TPR 16-1

(This ruling rescinds and supersedes TPR 08-1)

Page 10

not related to the Organization's mail-order business. See, e.g., *Nat'l Geographic Soc. v. Cal. Bd. of Equalization*, 430 U.S. 551 (1977) (concluding that taxing state has substantial nexus to impose its use tax collection liability on an out-of-state nonprofit organization for its mail-order sales, based on that organization's in-state offices).

4. Manufacturer is in the business of manufacturing widgets. The widgets are manufactured entirely outside of Arizona but sold in large volume to customers in Arizona. Manufacturer has no office or employees in Arizona and does not own any other property in Arizona. However, Manufacturer pays an independent contractor located in Arizona to represent Manufacturer's interests in Arizona. The independent contractor provides Manufacturer with substantial information about the Arizona market, including product performances, competing products, pricing, market trends and conditions, and customer financial liability. Is the substantial nexus requirement satisfied for the widget sales in Arizona?

Conclusion: Yes. Manufacturer is subject to transaction privilege tax. The activities performed by the Arizona independent contractor for and on behalf of Manufacturer are substantial, and they are significantly associated with Manufacturer's ability to establish and maintain a market in Arizona for its widget sales. See, e.g., *Tyler Pipe Indus., Inc. v. Wash. Dep't of Revenue*, 483 U.S. 232 (1987) (concluding that taxing state has substantial nexus to impose its business and occupation tax on an out-of-state manufacturer, based on the manufacturer's in-state sales representative).

5. Washington-based Company sells computer hardware and software across the country including in Arizona. Most of Company's Arizona business is both initiated by existing customers through word-of-mouth type promotion, and conducted by mail or telefax. Company's sales are made through mail orders and delivered from the Washington office using a common carrier or U.S. mail. The only contacts Company has with Arizona is through its salesperson and training staff. The salesperson is a resident of California, but travels to Arizona on occasion to perform follow-up visits with Company's Arizona business prospects. Some sales result from these visits. Otherwise, the salesperson does not initiate sales relationships in Arizona. Company also sends staff from its Washington office to Arizona to provide in-person training to new customers on a one-time basis. Company has no inventory, no property owned or rented, no office, and no employees or agents residing in Arizona. Is the substantial nexus requirement satisfied to tax Company's sales in Arizona?

Conclusion: Yes. Company is subject to transaction privilege tax. Company's employment of a salesperson to cover Arizona is intended to and did increase Company's sales. Also, Company's dispatch of trainers to Arizona is intended to increase customer satisfaction in Arizona, as well as encourage others to buy. Thus, even if Company's volume of sales in Arizona are low, the purpose for and effect of its Arizona employees satisfies the substantial nexus requirement. See, e.g., *Ariz. Dep't of Revenue v. Care Computer Sys., Inc.*, 197 Ariz. 414 (Ariz. Ct. App. 2000)

ARIZONA TRANSACTION PRIVILEGE

TAX RULING TPR 16-1

(This ruling rescinds and supersedes TPR 08-1)

Page 11

(concluding Arizona may impose its transaction privilege tax on the in-state sales of an out-of-state computer company based on the presence of the company's sale representative and trainers in the state).

6. Manufacturer builds custom office furniture. It is located out-of-state and does not maintain any office space in Arizona, but it contracts with an independent retailer in Arizona to serve as its in-state representative on occasion. Manufacturer's only customer in Arizona is Customer. Customer initially ordered one shipment of furniture but later ordered more. All sales negotiations took place in person in Arizona or by telephone. Negotiations included Manufacturer sending its own employees to Arizona to assemble furniture prototypes for Customer to review. All furniture orders were delivered by Manufacturer's employees to the independent retailer in Arizona who then installed the furniture under the supervision of a factory representative employed by Manufacturer. Thereafter, Manufacturer sent employees to Customer on warranty claims as well as sent the independent retailer to Customer to solicit additional orders. Is the substantial nexus requirement satisfied for the furniture sales in Arizona?

Conclusion: Yes. Manufacturer is subject to transaction privilege tax. Even though Manufacturer had only one customer in Arizona, many of Manufacturer's in-state activities resulted in sales and they were essential to Manufacturer's ability to establish and maintain a market in Arizona. See, e.g., *Ariz. Dep't of Revenue v. O'Connor, Cavanagh, Anderson, Killingsworth & Beshears, P.A.*, 192 Ariz. 200 (Ariz. Ct. App. 1997) (concluding an out-of-state custom furniture business has a nexus with Arizona based on its business activities with a local customer and is therefore subject to Arizona's transaction privilege tax).

7. Out-of-state Company is in the business of leasing vending machines. One of its customers is a retailer in Arizona. Company leased 200 machines to the Arizona retailer over a period of 4 years. During the leasing period, Company employed two Arizona residents to deliver and install the machines at the retailer's designated locations in Arizona, to relocate the machines on occasion, to perform maintenance and respond to service calls, and to train retailer's personnel on the machines' use. Company had no other contacts with Arizona. Is the substantial nexus requirement satisfied for the leasing activities of Company?

Conclusion: Yes. Company is subject to transaction privilege tax. Company's in-state activities performed in connection with the leasing of its machines to the Arizona retailer were done to establish and maintain Company's market in Arizona. See, e.g., *Interlott Tech., Inc. v. Ariz. Dep't of Revenue*, 205 Ariz. 452 (Ariz. Ct. App. 2003) (concluding that an out-of-state lessor of lottery-ticket vending machines is liable for transaction privilege tax for its leasing activities in Arizona).

8. Company A is an online marketplace business that allows third party merchants to list products for sale on its website. Company A is also a retailer and sells its own

ARIZONA TRANSACTION PRIVILEGE

TAX RULING TPR 16-1

(This ruling rescinds and supersedes TPR 08-1)

Page 12

products on its website. Company A provides customer service to its own customers as well as other customers purchasing goods from third party merchants. It also provides purchasing information to all customers such as order status and shipping information. It provides payment and refund processing to all customers and also controls the fulfillment process but does not have actual possession or title to any inventory. The marketplace has a fulfillment center located in Arizona. The marketplace is considered agent for third party merchants on the site as a result of providing customer service, payment processing and being able to control the fulfillment process. Is the substantial nexus requirement met with regard to sales made on the online marketplace?

Conclusion: Yes. Company A is subject to transaction privilege tax. Company A is a retailer of tangible personal property. The location of a fulfillment center in Arizona satisfies the nexus requirements.

9. Company D is an online marketplace that provides a platform for other retailers to sell products. Company D does not sell any merchandise on its own website and so is not otherwise a retailer. It provides customer service and payment processing, but it does not have any control over the delivery/fulfillment process.

Conclusion: Company D does not have any control over the delivery/fulfillment process and is not otherwise a retailer, therefore, Company D is not considered an agent for third party retailers on its site and is not subject to Arizona TPT. The retailer who sells on the marketplace is subject to Arizona TPT.

LEGAL AUTHORITY:

A.R.S. § 42-5001(13) – Defines “retailer” to include “every person engaged in the business classified under the retail classification . . . and, when in the opinion of the department it is necessary for the efficient administration of [TPT] . . . dealers, distributors, supervisors, employers and salesmen, representatives, peddlers or canvassers as the agents of the dealers, distributors, supervisors or employers under whom they operate or from whom they obtain the tangible personal property sold by them, whether in making sales on their own behalf or on behalf of the dealers, distributors, supervisors or employers.”

A.R.S. § 42-5061 – Imposes the transaction privilege tax under the retail classification on retailers or any person selling tangible personal property at retail. Also, lists the exemptions, exclusions, or deductions available under the retail classification.

A.R.S. § 42-5154 – Imposes a duty on retailers to register with Arizona for use tax purposes. That sections states: “Every retailer shall, before selling any tangible personal property for storage, use or consumption within this state, register with the department upon forms prescribed by the department.”

**ARIZONA TRANSACTION PRIVILEGE
TAX RULING TPR 16-1**

(This ruling rescinds and supersedes TPR 08-1)

Page 13

A.R.S. § 42-5155 – Imposes the use tax on the storage, use, or consumption in this state of tangible personal property purchased from a retailer, as a percentage of the sales price.

A.R.S. § 42-5160 – Describes the liability for use tax between retailers and purchasers. That section, in part, provides as follows: “Any person who uses, stores or consumes any tangible personal property upon which a tax is imposed by this article and upon which the tax has not been collected by a registered retailer shall pay the tax. . . but every retailer and utility business maintaining a place of business in this state and making sales of tangible personal property for storage, use or other consumption in this state shall collect the tax from the purchaser or user unless the property is exempt under this article or the purchaser or user pays the tax directly to the department as provided by section 42-5167. . . .”

A.R.S. § 42-5161 – Imposes the use tax collection duty on retailers as follows: “Except as provided by section 42-5167, every retailer and utility business shall collect from the purchaser the tax imposed by this article [Use Tax] and give to such purchaser a receipt for the tax in the manner and form prescribed by the department. The tax required to be collected shall be shown separately on the invoice or other proof of sale. The tax required to be collected shall constitute a debt owed by the retailer or utility business to this state.”

A.R.S. § 42-5167 – Authorizes a person to pay use taxes directly to the Department under certain conditions.

A.R.S. § 42-5040 – Provides sourcing rules for retail sales of tangible personal property and for the leasing or renting of tangible personal property.

A.R.S. § 42-5075(M) – Provides sourcing rules for the sale of manufactured buildings.

Grant Nülle, Deputy Director

Signed: September 20, 2016

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

ARIZONA TRANSACTION PRIVILEGE

TAX RULING TPR 16-1

(This ruling rescinds and supersedes TPR 08-1)

Page 14

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.