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**ARIZONA TRANSACTION PRIVILEGE TAX PROCEDURE
TPP 15-1**

Procedure for the Annual Recognition and the Documentation of Exempt Status
of Certain Nonprofit Healthcare Organizations

(This procedure supersedes Arizona Transaction Privilege Tax Procedure TPP 99-5)

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This procedure gives information about the transaction privilege and use tax exemptions available to organizations recognized by the Department as one of the above entities, as well as the application process for obtaining an annual Exemption Letter from the Department and the documentation required for exemptions applicable to vendors, lessors, and utilities.

I. QUALIFYING HOSPITALS

A. Applicable Law:

1. Arizona Revised Statutes (A.R.S.) § 42-5001(11) defines a qualifying hospital as:
 - a) A licensed hospital which is organized and operated exclusively for charitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.
 - b) A licensed nursing care institution or a licensed residential care institution or a residential care facility operated in conjunction with a licensed nursing care institution or a licensed kidney dialysis center,

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which provides medical services, nursing services or health related services and is not used or held for profit.

c) A hospital, nursing care institution or residential care institution which is operated by the federal government, this state or a political subdivision of this state.

d) A facility that is under construction and that on completion will be a facility under subdivision (1), (2) or (3) of this paragraph.

2. Statutory Exemptions: For an organization that falls under one of the above categories of "qualifying hospitals," exemptions from the transaction privilege tax and use tax are provided by:

a) A.R.S. § 42-5061(A)(25)(a) Retail classification

b) A.R.S. § 42-5063(C)(3)(a) Utilities classification

c) A.R.S. § 42-5065(B)(2)(a) Publication classification

d) A.R.S. § 42-5066(B)(3)(a) Job printing classification

e) A.R.S. § 42-5067(B)(1) Pipeline classification

f) A.R.S. § 42-5071(B)(2)(a) Personal property rental classification

g) A.R.S. § 42-5074(B)(7) Restaurant classification

h) A.R.S. § 42-5159(A)(13)(a), (b), (c) Use Tax

B. Annual Applications for Exemption: Qualifying hospitals must apply to the Department of Revenue for an annual Exemption Letter to be eligible for the statutory exemptions.

1. Requests from a licensed hospital, licensed nursing care institution or a licensed residential care institution operated in conjunction with a licensed nursing care institution or a licensed kidney dialysis center must:

a) Be in writing.

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b) Include a copy of any of the required organization's current license(s) as issued by the Arizona Department of Health Services (ADHS). (Out-of-state institutions requesting exemption may include a copy of their current state license.)

c) Include a copy of the organization's I.R.C. § 501(c) determination letter. The I.R.S. issues a § 501(c) determination letter as of a specific date. The entity generally does not qualify as a § 501(c) organization prior to that date. The name on the I.R.S. letter must match the name of the organization seeking the Exemption Letter and the name on the license issued by the Arizona Department of Health Services. The organization may provide proof that it is operating as a subordinate organization under a group exemption.

2. Requests from a residential care facility operated in conjunction with a licensed nursing care institution (see Arizona Transaction Privilege Tax Ruling **TPR 99-8**) must:

a) Be in writing.

b) Include a copy of the organization's current nursing care institution license, as issued by the Arizona Department of Health Services.

c) Include a copy of the organization's I.R.C. § 501(c) determination letter. The I.R.S. issues a § 501(c) determination letter as of a specific date. The entity generally does not qualify as a § 501(c) organization prior to that date. The name on the I.R.S. letter must match the name of the organization seeking the Exemption Letter and the name on the license issued by the Arizona Department of Health Services. The organization may provide proof that it is operating as a subordinate organization under a group exemption.

d) Include a description of the medical, nursing or health related services provided for residents of the residential units.

e) Include verification that the residential care facility is operated in conjunction with the licensed nursing care institution. For purposes of

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this exemption, "operated in conjunction with" is generally defined to mean that the residential care facility has common ownership and common management with the licensed nursing care institution. (Examples of acceptable documentation may be found in Arizona Transaction Privilege Tax Ruling **TPR 99-8**.)

3. Requests from a hospital, nursing care institution or residential care institution which is operated by the federal government, this state or a political subdivision of this state must:

- a) Be in writing.
- b) If applicable, include a copy of the organization's current hospital, nursing care institution or residential care institution license, as issued by the Arizona Department of Health Services.
- c) Include verification that the facility is operated by the federal government, the State of Arizona or a political subdivision of the State of Arizona.

4. Requests from a facility under construction and that upon completion will be a nursing care institution, a residential care institution, a kidney dialysis center, or residential care facility must:

- a) Be in writing.
- b) Include a copy of the organization's building permits at the address of the facility under construction.
- c) Include a copy of the organization's I.R.C. § 501(c) determination letter. The I.R.S. issues a § 501(c) determination letter as of a specific date. The entity does not qualify as a § 501(c) organization prior to that date. The name on the I.R.S. letter must match the name of the organization seeking the Exemption Letter and the name on the building permits at the address of the facility under construction. The organization may provide proof that it is operating as a subordinate organization under a group exemption. This requirement may be waived if the facility under construction is

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operated by the federal government, this state or a political subdivision of this state.

C. Documentation for Exemption: A **qualifying hospital** must provide a copy of the annual exemption letter along with a properly completed Arizona Form 5000HC for each location(s) attesting that the location or satellite facility provides through an organized medical staff, inpatient beds, medical services, and continuous nursing services for the diagnosis and treatment of patients. A **licensed nursing care institution** must provide a copy of the annual exemption letter along with a properly completed Arizona Form 5000HC for each location(s) attesting that the location is a health care institution providing inpatient beds or resident beds and nursing services to persons who need nursing services on a continuing basis but who do not require hospital care or direct daily care from a physician. A **licensed residential care institution** must provide a copy of the annual exemption letter along with a properly completed Arizona Form 5000HC for each location(s) attesting that the location is a health care institution other than a hospital or a nursing care institution that provides resident beds or residential units, supervisory care services, personal care service, directed care services or health-related services for persons. A **residential care facility operated in conjunction with a licensed nursing care institution** must provide a copy of the annual exemption letter along with a properly completed Arizona Form 5000HC for each location(s) attesting that the facility provides medical, nursing, or health related services for residents of the residential units and is operated in conjunction with a licensed nursing care institution. A **licensed kidney dialysis center** must provide a copy of the annual exemption letter along with a properly completed Arizona Form 5000HC for each location(s) attesting that the location provides medical services, nursing services or health related services and is not used or held for profit.

[Note: If you have more than one location for which your organization is claiming an exemption, you may reference and attach a list of the locations to the Form 5000HC.]

D. ADHS Licensing: Organizations that **qualify** include a licensed hospital and its satellite facilities listed on the license, a nursing care institution, a residential care institution operated in conjunction with a licensed nursing care institution, or a licensed kidney dialysis center. A *residential care institution* includes an

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assisted living center, an assisted living facility, or an adult foster care home. Organizations that **do not qualify** include locations of a qualifying organization where the activities are not within the prescribed ADHS licensing. For example: 1) a licensed outpatient treatment center location is run by a licensed nursing care institution. The operation of such a treatment center is outside the operating scope of a licensed nursing care institution. The outpatient treatment center location would not qualify for the exemption. 2) A licensed hospital operates a licensed outpatient treatment center or a child day care center. The outpatient treatment center and the child day care center are not satellite facilities on the ADHS hospital license. These locations do not qualify for the exemption. 3) A health campus operates a licensed assisted living center and a licensed adult day health care. The licensed assisted living center qualifies as a residential care institution. The adult day health care does not qualify as adult foster care services included in residential care institutions since overnight beds and care are not provided as would be provided in an adult foster care home. **Note:** Hospice service agencies and other health care organizations that do not meet the requirements of a “Qualifying Hospital” may apply to qualify for an exemption letter as a “Qualifying Health Care Organization”. See the requirements for application as a Qualifying Health Care Organization below. Also, if applicable, see the requirements for application as a “Qualifying Community Health Center.”

II. QUALIFYING HEALTH CARE ORGANIZATIONS

A. Applicable Law:

1. A.R.S. § 42-5001(10) defines a qualifying health care organization as “an entity that is recognized as nonprofit under section 501(c) of the United States internal revenue code and that uses, saves or invests at least eighty per cent of all monies that it receives from all sources each year only for health and medical related educational and charitable services, as documented by annual financial audits prepared by an independent certified public accountant, performed according to generally accepted auditing standards and filed annually with the Department. Monies that are used, saved or invested to lease, purchase or construct a facility for health and

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medical related education and charitable services are included in the eighty per cent requirement.”

2. Statutory Exemptions: For an organization meeting the requirements for a “qualifying health care organization,” exemptions from the transaction privilege tax and use tax are provided by:

- a) A.R.S. § 42-5061(A)(25)(b), (c) Retail classification
- b) A.R.S. § 42-5063(C)(3)(b) Utilities classification
- c) A.R.S. § 42-5065(B)(2)(b) Publication classification
- d) A.R.S. § 42-5066(B)(3)(b) Job printing classification
- e) A.R.S. § 42-5067(B)(2) Pipeline classification
- f) A.R.S. § 42-5071(B)(2)(a) Personal property rental classification
- g) A.R.S. § 42-5074(B)(8) Restaurant classification
- h) A.R.S. § 42-5159(A)(13)(d), (e) Use Tax

3. With the exceptions of A.R.S. §§ 42-5061(A)(25)(c) and 42-5159(A)(13)(e), in order for the tangible personal property to be exempt it must be used by the organization solely to provide educational or charitable services that are health and medical related. (See section E below.)

B. Annual Application for Exemption: Qualifying health care organizations must apply to the Department of Revenue for an annual Exemption Letter to be eligible for the statutory exemptions. Requests from a qualifying health care organization must:

1. Be in writing.
2. Include a copy of the organization’s I.R.C. § 501(c) determination letter. The I.R.S. issues a § 501(c) determination letter as of a specific date. The entity does not qualify as a § 501(c) organization prior to that date. The name on the I.R.S. determination letter must match the name of the

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organization seeking the exemption or the organization must provide proof that it is operating as a subordinate organization under a group exemption.

3. Include an annual financial audit prepared by an independent certified public accountant according to generally accepted auditing standards. The annual financial audit should substantiate that 80 percent of all monies collected from all sources are used, saved or invested solely for health and medical related educational and charitable services. The end of the fiscal year covered by the audit must within one year and one day of the tax exemption period requested. For example, if the health care organization is requesting an exemption period of July 1, 2012 through June 30, 2013, the financial audit submitted must be for the fiscal year ended June 30, 2011 or later. Draft copies are not acceptable. A newly started organization may explain the unavailability of this information to the Department in its request but will be required to send the audit covering the exemption period as soon as it is available.

4. Include a copy of any current licenses issued by the Arizona Department of Health Services.

C. Documentation for Exemption: The qualifying healthcare organization must provide to a vendor or lessor a copy of the organization's annual exemption letter and a properly completed Arizona Form 5000HC for each location(s) **attesting that the tangible personal property purchased or leased by that location will be used solely in providing educational or charitable services that are health and medical related.** The qualifying healthcare organization must provide to a utility for each location a copy of the organization's annual exemption letter and a properly completed Arizona Form 5000HC for the location(s) that **attests that the location is providing educational or charitable services that are health and medical related.** Only those locations used by the qualifying organization to provide educational or charitable services that are health and medical related are exempt under the Utilities classification in A.R.S. § 42-5063(C)(3)(b).

[Note: If you have more than one location for which your organization is claiming an exemption, you may reference and attach a list of the locations to the Form 5000HC.]

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D. Discussion Regarding Exemptions and the 80% Requirement.

1. Using the required annual audit the Department will evaluate each program service performed by the organization. Under these statutory requirements it is generally acknowledged that the following types of program services **are health and medical related educational and charitable services**:

- a) Program services related to the diagnosis, treatment, or prevention of a mental or physical illness or condition.
- b) Program services dedicated to medical research.
- c) Program services dedicated to the treatment of substance or physical abuse, e.g., a substance abuse or domestic violence treatment program.
- d) Program services of peer or professional led support group programs organized for sufferers of a mental or physical illness or condition.
- e) Program services dedicated to educating the public on a mental or physical illness or condition.
- f) Program services dedicated to publishing educational health and medical literature.
- g) Program services which are licensed by the Arizona Department of Health Services, excluding child care providers.

2. Under these statutory requirements it is generally acknowledged that the following types of program services and **expenses are not health and medical related educational and charitable services**:

- a) Fundraising and marketing expenses.
- b) General and administrative expenses.
- c) Non-monetary depreciation expenses.

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d) Meeting and event expenses, unless the meeting is health and medical related and educational or charitable in nature.

(1) The health and medical related educational or charitable requirement excludes social events, fundraising related events, and certain corporate events, such as board meetings.

(2) An event that is charitable in nature means that the meeting will be attended by those people the organization was intended to serve (e.g. the disabled, the sick, or those in need of assistance).

(3) Equipment and other items purchased or leased for an event are exempt only if necessary to conduct the event or essential to the health and medical aspect of the event, and are used during the event itself.

(4) Food or beverages purchased for an event will not be exempt absent a specific showing that the food is necessary in order to conduct the event, essential to the health and medical aspect of the event, and is provided during the event itself, e.g., food provided at a blood drive to stabilize a donor's blood sugar. Food or beverages provided solely to feed the attendees of an event are not exempt.

e) Program services that provide food aid and nutritional assistance. These activities have a separate set of exemptions which are described below.

(1) A.R.S. § 42-5102(C) provides a transaction privilege tax exemption for food sold to a an organization that is tax exempt under section 501(c)(3) of the internal revenue code and which provides the articles to persons with a nominal charge or without a monetary charge. See Arizona Transaction Privilege Tax Ruling **TPR 94-11** for additional information.

(2) A.R.S. § 42-5061(A)(25)(e) provides a broad exemption from the transaction privilege tax for retail sales of "[t]angible

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personal property sold to ... [a] nonprofit charitable organization that has qualified under section 501(c)(3) of the internal revenue code and that regularly serves meals to the needy and indigent on a continuing basis at no cost.” These organizations are also eligible for tax exemptions from the Personal Property Rental and Use Tax Classifications under A.R.S. §§ 42-5071(B)(2)(a) and 42-5159(A)(13)(j), respectively. See Arizona Transaction Privilege Tax Ruling **TPR 00-4** for additional information.

f) Program services that are for training, job placement, rehabilitation or testing of mentally or physically disabled persons. These activities have a separate set of exemptions which are described below in Section III of this Procedure.

g) Program services that provide housing without the rendering of health and medical related educational or charitable services by the organization, such as support housing, transitional housing, temporary housing assistance or other subsidized housing. Organizations that provide subsidized housing may be eligible for a separate set of exemptions found in A.R.S. §§ 42-5061(A)(25)(f), 42-5071(B)(2)(a), 42-5075(B)(8)(a), 42-5075(B)(12) and 42-5159(A)(13)(l). These statutes contain exemptions for nonprofit charitable organizations that are qualified under section 501(c)(3) of the internal revenue code and that provide residential apartment housing for low income persons over sixty-two years of age in a facility that qualifies for a federal housing subsidy.

3 The Department will determine whether the A.R.S. § 42-5001(10) eighty percent (80%). requirement has been met using the organization’s most recent annual audit. The Department will evaluate each program service performed by the organization. The Department will determine which program services and related expenses are used only for health and medical related educational and charitable services. Those expenses that are only for health and medical related educational and charitable services will be added to any increase in the organization’s net assets (support, general, depreciation, administrative and fundraising expenses will not be included). If this calculation meets or exceeds at least eighty percent (80%) of all monies

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that the organization receives from all sources each year, the organization will be granted an Exemption Letter for the year. If the financial audit covers more than one entity, the organization requesting the Exemption Letter must substantiate how it meets the requirement that at least eighty per cent of all monies that it receives from all sources each year are used, saved or invested only for health and medical related educational and charitable services. Either the audit must show or the independent CPA may prepare a separate itemized breakdown of the revenues and expenses contained in the financial audit for the organization requesting the Exemption Letter. Expenses must be itemized into those allocated to program services, supporting services, and other expenses. A copy of the organization's most recently filed IRS Form 990 may be used to show the breakdown of expenses if prepared by an independent CPA. A **positive certification** by the independent certified public accountant may be provided to facilitate the Department determination attesting that the organization requesting the Exemption Letter used, saved or invested at least eighty per cent of all monies that it received from all sources during the period covered by the annual audit only for health and medical related educational and charitable services in accordance with A.R.S. § 42-5001(10). This certification must be in the form of a separate letter or an actual reference contained within the audit. **Negative confirmation letters or general purpose statements are not sufficient.**

E. Additional requirements for qualifying health care organizations dedicated to providing educational, therapeutic, rehabilitative and family medical education training for blind, visually impaired and multidisabled children from the time of birth to age 21.

1. A.R.S. §§ 42-5061(A)(25)(c) and 42-5159(A)(13)(e) respectively, provide exemptions from transaction privilege tax and use tax for retail sales to a qualifying health care organization dedicated to providing educational, therapeutic, rehabilitative and family medical education training for blind, visually impaired and multidisabled children from the time of birth to age 21.

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2. The exemptions are not limited to tangible personal property which is used by the organization solely to provide health and medical related educational and charitable services.

3. To qualify the organization must satisfy the requirements of a qualifying health care organization as stated above. In addition, it must provide documentation showing that the organization is dedicated to providing educational, therapeutic, rehabilitative and family medical education training for blind, visually impaired and multidisabled children from the time of birth to age 21.

III. REHABILITATION PROGRAMS FOR MENTALLY OR PHYSICALLY DISABLED PERSONS

A. Applicable Law:

1. The Arizona Revised Statutes provide for exemptions from the transaction privilege tax and the use tax for tangible personal property purchased or leased in this state by a nonprofit charitable organization that has qualified under section 501(c)(3) of the United States internal revenue code and that engages in and uses such property exclusively in programs for mentally or physically disabled persons if the programs are exclusively for training, job placement, rehabilitation or testing.

2. Statutory Exemptions: For an organization meeting the requirements for a rehabilitation program for mentally or physically disabled persons, exemptions from the transaction privilege tax and use tax are provided by:

- a) A.R.S. § 42-5061(A)(29) Retail classification
- b) A.R.S. § 42-5071(B)(2)(a) Personal property rental classification
- c) A.R.S. § 42-5159(A)(13)(f) Use Tax

3. In order for the tangible personal property to be exempt it must be used by the organization directly and exclusively in programs for training, job placement, rehabilitation or testing for mentally or physically disabled persons.

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B. Annual Application for Exemption: Rehabilitation programs for mentally or physically disabled persons must apply to the Department of Revenue for an annual Exemption Letter to be eligible for the statutory exemptions. The annual request must:

1. Be in writing.
2. Include a copy of the organization's I.R.C. § 501(c) determination letter. The I.R.S. issues a § 501(c) determination letter as of a specific date. The entity generally does not qualify as a § 501(c) organization prior to that date. The name on the I.R.S. determination letter must match the name of the organization seeking the exemption or the organization must provide proof that it is operating as a subordinate organization under a group exemption.
3. Include a copy of the organization's most recently filed I.R.S. Form 990 or 990-EZ, including all schedules, if the organization is required to file an annual information return. If the organization is not required to file an annual information return, the requestor must attest that the organization is not required file a return.
4. Include a copy of any current license(s) issued by the Arizona Department of Health Services.
5. Include 1) documentation substantiating and describing the organization's programs for training, job placement, rehabilitation or testing of mentally or physically disabled persons, and 2) a written statement attesting that the items purchased or leased will be used exclusively for training, job placement or rehabilitation programs or testing for mentally or physically disabled persons.

C. Documentation for Exemption: The organization must provide to the vendor or lessor a copy of the annual exemption letter along with a properly completed Arizona Form 5000HC for each location(s) attesting that **the tangible personal property is used by the organization directly and exclusively in programs for training, job placement, rehabilitation or testing for mentally or physically disabled persons.**

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[Note: If you have more than one location for which your organization is claiming an exemption, you may reference and attach a list of the locations to the Form 5000HC.]

IV. QUALIFYING COMMUNITY HEALTH CENTER

D. Applicable Law:

1. A.R.S. § 42-5001(9) defines a qualifying community health center as: An entity that is recognized as nonprofit under 501(c)(3) of the United States internal revenue code that is a community-based, primary care clinic that has a community-based board of directors and that is either the sole provider of primary care in the community, or nonhospital affiliated clinic that is located in a federally designated medically underserved area in this state.

2. For an organization meeting the requirements for a “qualifying community health center,” exemptions from the transaction privilege tax and use tax are provided by:

- a) A.R.S. § 42-5061(A)(25)(d) Retail classification
- b) A.R.S. § 42-5071(B)(2)(a) Personal property rental classification
- c) A.R.S. § 42-5159(A)(13)(i) Use Tax

E. Annual Application for Exemption: Qualifying community health centers must apply to the Department of Revenue for an annual Exemption Letter to be eligible for the statutory exemptions. Requests from a qualifying community health center must:

- 1. Be in writing.
- 2. Include a copy of the organization’s I.R.C. § 501(c) determination letter. The I.R.S. issues a § 501(c) determination letter as of a specific date. The entity generally does not qualify as a § 501(c) organization prior to that date. The name on the I.R.S. determination letter must match the name of the organization seeking the exemption or the organization must provide proof that it is operating as a subordinate organization under a group exemption.

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3. Include a copy of the organization's most recently filed I.R.S. Form 990 or 990-EZ, including all schedules, if the organization is required to file an annual information return. If the organization is not required to file an annual information return, the requestor must attest that the organization is not required file a return.

4. Include a copy of current required license(s) issued by the Arizona Department of Health Services.

5. Include documentation substantiating that the organization is a community based, primary care clinic with a community based board of directors and is either the sole provider or primary care in the community or a nonhospital affiliated clinic that is located in a federally designated medically underserved area within Arizona.

F. Documentation for Exemption: The organization must provide to the vendor or lessor a copy of the annual exemption letter along with a properly completed Arizona Form 5000HC for each location(s) attesting that the tangible personal property is used by the community health center that is either: 1) the sole provider of primary care in the community, or 2) a nonhospital affiliated clinic that is located in a federally designated medically underserved area in this state, or 3) a clinic that is being constructed as a qualifying community health center.

[Note: If you have more than one location for which your organization is claiming an exemption, you may reference and attach a list of the locations to the Form 5000HC.]

G. Discussion Regarding Qualifying Community Health Center Documentation

1. Community based requirement: Generally a community may be anything from a town/city to a group of people with a common bond or unifying trait. A community is not limited to any particular geographical area. It may be part of a larger town/city or it may extend beyond the boundaries of a town/city. A community based facility would generally be that which is indigenous to the area in which it is located and that was created to serve that community of individuals.

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2. Primary care requirement: A primary care clinic is a facility that delivers the first level of care to patients through the employment of physicians, professional nurses, physician's assistants or other health care technical and professional personnel. A clinic may range in size from one individual to a group of individuals. Primary care encompasses any one or any combination of the following four areas of medicine: internal medicine, gynecology, family practice or pediatrics. The type of services such a clinic provides include preventive, diagnostic, treatment, consultation, referral, routine associated laboratory, diagnostic radiological, and emergency health. The fact that a clinic also provides specialized medical care in addition to primary care does not prevent the clinic from qualifying as a primary care clinic. The organization should include with its request a description of the services provided at the clinic, as well as a current Arizona Department of Health Services license to operate as a medical facility.

3. Community based board of directors requirement: The organization should provide documentation with its request that the clinic has a community-based board of directors consisting of names, addresses, and occupations of board members; by-laws; or other internal governing documents. A majority of the board members of the clinic should be individuals who, as a group, are representative of the population using the center within the community in which the facility is located or the group that the facility was formed to serve.

4. If the organization is seeking qualification as the sole provider of primary care in the community, it should include in its request documentation showing that it is the sole provider of primary care in the community. Examples of acceptable documentation include a letter from the board of directors certifying that it is the sole provider of primary care in the community and a description of the area to which the clinic provides services. This documentation should also include information regarding the targeted users of the clinic.

5. If the organization is seeking qualification as a nonhospital affiliated clinic that is located in a federally designated medically underserved area in this state, the organization should include in its request verification that the clinic is not affiliated with a hospital, such as a letter from the board of

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directors certifying that it is not affiliated with any hospital. The organization must also document that it is located in federally designated medically underserved area within Arizona. Such documentation can be obtained on the United States Department of Health and Human Services website by entering the facilities address at the following web address: <http://datawarehouse.hrsa.gov/GeoAdvisor/ShortageDesignationAdvisor.aspx> (please note the report must specifically indicate the facility's address is located in a medically underserved area).

V. GENERAL INFORMATION APPLICABLE TO ALL QUALIFYING ORGANIZATIONS

A. The Deduction Under A.R.S. § 42-5075(B)(8) for Prime Contractors

Many qualifying organizations question the taxation of transactions with prime contractors. A.R.S. § 42-5075(B)(8) provides a deduction under the prime contracting classification for the gross proceeds of sales or gross income attributable to the purchase of machinery, equipment, or other tangible personal property that is exempt from or deductible from transaction privilege under A.R.S. §§ 42-5061(A)(25) or 42-5061(A)(29), A.R.S. § 42-5061(B), and the parallel use tax provisions. The deduction is only applicable for the amount of the gross proceeds of sales or gross income attributable to the prime contractor's actual purchase price of qualified machinery, equipment, or other tangible personal property purchased by the contractor. A deduction from the tax base is not provided for the gross proceeds of sales or gross income derived from the prime contracting activity to install, assemble, repair, maintain or remove the machinery or equipment. A deduction is not provided for any markup on the purchase price of the qualified machinery, equipment or other tangible personal property. This deduction is not listed on the Department Exemption Letters to the organizations because it pertains only to the prime contractors' purchase of the qualifying machinery, equipment, or other tangible personal property. A qualifying organization's documentation for exemption should include providing the prime contractor with a copy of their Department Exemption Letter along with a properly completed Form 5000HC.

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B. Applications for Exemption:

A qualifying organization must apply to the Department of Revenue for an annual Exemption Letter to be eligible for the statutory exemptions. Exemption Letter requests should be received by the Department at least thirty (30) business days prior to the beginning of the calendar or fiscal year for which the organization is requesting an exemption.

If an organization does not submit the required documentation, the Department will send a letter requesting further information within thirty (30) business days of receipt of the Exemption Letter request. An Exemption Letter will not be issued until all required documents are received by the Department. If the required documents do not substantiate the organization is eligible for an Exemption Letter, a denial will be issued that may be appealed as detailed below.

An exemption letter is valid for a period of 12 months or less unless the organization's tax exempt status changes prior to the end of the 12-month period, or the organization misrepresented or omitted material information in its exemption request.

C. Prior Year Applications

The Department will honor a request for an Exemption Letter for prior years if the organization submits all the documentation that would have been required to receive an exemption letter in that previous year. Annual financial audits and I.R.S. returns cannot be used for multiple years.

All organizations are subject to the statutory provisions in A.R.S. § 42-1106 Time limitations for credit and refund claims and A.R.S. § 42-1108 Audit; deficiency assessments.

D. Appeal of Agency's Decision

A.R.S. § 41-1092 defines "appealable agency action" as an action that determines the legal rights, duties or privileges of a party and that is not preceded by an opportunity for an administrative hearing. A denial of an Exemption Letter request by the Department is an appealable agency action.

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A party may obtain a hearing on an appealable agency action by filing a petition or notice of appeal with the agency within forty-five (45) days after receiving a denial of exemption. See Arizona Administrative Code (A.A.C.) R15-10-105(C) for further instruction on filing a petition.

Generally hearings for appealable agency actions are held within sixty (60) days after the notice of appeal is filed. (See A.R.S. § 41-1092.05.)

If requested by the appellant of an appealable agency action, the Department will hold an informal settlement conference within fifteen (15) days after receiving the written request. Procedures for informal settlement conferences are covered by A.R.S. § 41-1092.06.

David Raber, Director

Signed: June 22, 2015

Explanatory Notice

The purpose of a tax procedure is to provide procedural guidance to the general public and to Department personnel. A tax procedure is a written statement issued by the Department to assist in the implementation of tax laws, administrative rules, and tax rulings by delineating procedures to be followed in order to achieve compliance with the law. Relevant statute, case law, or administrative rules, as well as a subsequent procedure, may modify or negate any or all of the provisions of any tax procedure. See GTP 96-1 for more detailed information regarding documents issued by the Department of Revenue.