

ARIZONA DEPARTMENT OF REVENUE

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ARIZONA CORPORATE TAX RULING CTR 97-1

This substantive policy statement is advisory only. A substantive policy statement does not include internal procedural documents that only affect the internal procedures of the agency and does not impose additional requirements or penalties on regulated parties or include confidential information or rules made in accordance with the Arizona administrative procedure act. If you believe that this substantive policy statement does impose additional requirements or penalties on regulated parties you may petition the agency under Arizona Revised Statutes § 41-1033 for a review of the statement.

ISSUE:

The application of the federal "check-the-box rules" on elective tax classification of business entities for Arizona income tax purposes.

APPLICABLE LAW:

Arizona Revised Statutes (A.R.S.) § 43-102(A) states the legislative intent regarding the taxation of individuals, corporations, trusts, and partnerships.

A.R.S. § 43-104 defines the terms "corporation" and "partnership" for purposes of Title 43.

A.R.S. § 29-857, as amended by Laws 1997, Ch. 282, § 40, prescribes the income tax treatment of limited liability companies under Title 43, including single member limited liability companies.

Treasury Regulation (Treas. Reg.) §§ 301.7701-1 to 301.7701-4 prescribe the "check-the-box rules" on elective tax classification of business entities.

DISCUSSION:

Treas. Reg. §§ 301.7701-1 to 301.7701-4 are generally effective on January 1, 1997. Under the new Treasury regulations, a business entity is any entity recognized for federal tax purposes (including an entity with a single owner that may be disregarded as an entity separate from its owner) that is not classified as a trust or otherwise subject to special treatment under the Internal Revenue Code. Any business entity other than a trust or an entity automatically classified as a corporation under the regulations is eligible to elect its classification. An eligible entity with two or more members may elect to be classified as either a corporation or a partnership. An eligible entity with a single owner is classified as a corporation or is disregarded as an entity separate from its owner. If the entity is not treated as an entity separate from its owner, it is considered a sole proprietorship, branch, or division of that owner. Existing entities that meet the qualifying conditions stated in the regulations may retain their current classification.

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A.R.S. § 43-102(A) provides that the legislative intent is to adopt the provisions of the Internal Revenue Code relating to the measurement of taxable income for corporations, trusts, and partnerships, to the end that taxable income reported each taxable year by a corporation, trust, or partnership to the Internal Revenue Service shall be the identical sum reported to this state, subject only to the modifications contained in Title 43 of the Arizona Revised Statutes.

Subsection A also provides that these results will be achieved by the application of the various provisions of the Internal Revenue Code relating to the definitions of income, exceptions, deductions, accounting methods, taxation of individuals, corporations, trusts, partnerships, basis and other pertinent provisions relating to gross income as defined, resulting in an amount called adjusted gross income for individuals and taxable income for corporations, trusts, and partnerships in the Internal Revenue Code.

RULING:

The legislative intent, as stated in A.R.S. § 43-102(A), requires an entity to have the same classification, i.e., corporation, trust, partnership, for Arizona tax purposes as it does for federal tax purposes to compute Arizona gross income for its taxable year. Therefore, the federal tax classification of an entity under the federal "check-the-box rules" determines the entity's classification for Arizona tax purposes.

Mark W. Killian, Director

Signed: July 22, 1997

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 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.