

ARIZONA DEPARTMENT OF REVENUE

ARIZONA TRANSACTION PRIVILEGE TAX RULING

TPR 93-20

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:

Taxability of fees received by a utility cooperative which provides water to its owners or users.

APPLICABLE LAW:

Arizona Revised Statutes (A.R.S.) § 42-1306 levies the transaction privilege tax upon persons conducting business in Arizona.

A.R.S. § 42-1310.03 provides that the utilities classification is comprised of the business of producing and furnishing or furnishing to consumers electricity, natural or artificial gas and water.

A.R.S. § 42-1301.1 defines "business" to include activities or acts which produce a direct or indirect gain, benefit or advantage.

A.R.S. § 42-1301.12 defines "sale" to mean any transfer of title or possession of tangible personal property **or** other activities taxable under this chapter, for a consideration.

A.R.S. § 42-1301.8 provides that "person" or "company" includes an individual, firm, partnership, joint venture, association, corporation, and many other entities.

DISCUSSION:

Transaction Privilege Tax

A.R.S. § 42-1310.03 clearly imposes the transaction privilege tax upon the business of

producing and furnishing or just furnishing water to consumers. The taxation of utilities is not limited to public utilities, as evidenced by the removal of the word "public" from the title of the classification when it was transferred and renumbered by Laws 1985, Chapter 298, Sections 11 and 16.

An entity which is formed to collect fees from its owners or customers and hold legal title to the property which provides water to its members, has as its sole purpose the production and furnishing of water to consumers. This activity is taxable under the utilities classification, if the performance of this activity constitutes a business.

The issue of whether an entity which exists solely for the benefit of its members can be engaged in business, has been addressed by the Arizona courts. In *O'Neil v. United Producers and Consumers Co-operative*, 57 Ariz. 295, 113 P.2d 645 (1941), the court held that a nonprofit cooperative was engaged in business in its collection of fees from members, because the members derived benefits provided by the cooperative. Similarly, in *Tempe Life Care Village, Inc. v. City of Tempe*, 148 Ariz. 264, 714 P.2d 434 (App. 1985), the Arizona Court of Appeals concluded that regardless of whether a nonprofit *organization* derives any income or benefit from its activities, if the organization's *members* derive a gain, benefit or advantage from the activities, then the organization is engaging in business.

All receipts derived by an entity whose sole purpose is to provide water to its owners or members are considered "gross income" or "gross proceeds of sales" for purposes of the tax base under the utilities classification. Such receipts are considered to be the consideration received by the entity for the sale of water to its owners or members.

Municipal Water Delivery System Tax

An additional tax is imposed upon the operation of some water delivery systems. A.R.S. § 42-1552 levies a tax on the business of operating a "municipal water delivery system," which is defined by A.R.S. § 42-1551 as an entity that distributes or sells potable water primarily through a pipeline delivery system, which is owned by either:

1. A city or town incorporated or chartered under the constitution and laws of this state.
2. A private entity which is regulated as a public service corporation by the Arizona corporation commission under a certificate of public convenience and necessity.
3. A special taxing district established under Title 48, Chapter 6. (This statute authorizes county improvement districts.)

4. An entity which is regulated as a water supply system by the department of environmental quality.

This tax is paid to the Department of Revenue at the same time as the transaction privilege tax imposed upon businesses operating under the utilities classification.

RULING:

A utility cooperative or association whose sole purpose is to provide water to its owners or members is engaged in a business subject to tax under the utilities classification, regardless of whether any profit is realized. As such, any fees or dues paid by members or users of such a cooperative or association constitute the taxable gross proceeds of sales or gross income derived from this business. The tax upon certain municipal water delivery systems imposed by A.R.S. § 42-1552 may also be applicable to the gross proceeds of sales or gross income derived by these entities.

Harold Scott, Director
Signed April 16, 1993

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 which are not adequately covered in statute, case law or administrative rules. A tax ruling is a position statement which provides interpretation, details or supplementary information concerning the 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 92-1 for more detailed information regarding documents issued by the Department of Revenue.