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ARIZONA TRANSACTION PRIVILEGE TAX RULING TPR 95-20

(This Ruling Supersedes Arizona Transaction Privilege Tax Ruling TPR 93-8)

Note: On May 12, 2021 footnotes were added. No substantive changes were made.

ISSUE:

The imposition of transaction privilege tax on sales and leases of new agricultural equipment under the retail classification and the personal property rental classification.

APPLICABLE LAW:

A.R.S. § 42-1310.01.B.13¹ provides an exemption from transaction privilege tax under the retail classification for the gross proceeds of sales of new machinery and equipment used for the commercial production of agricultural, horticultural, viticultural and floricultural crops and products in this state.

A.R.S. § 42-1310.01.B.13(b)² states that "self-powered implements" includes machinery and equipment that is electric powered.

A.R.S. § 42-1310.11.B.2³ provides an exemption from transaction privilege tax under the personal property rental classification for the gross proceeds derived from leases of tangible personal property which would have been exempt under A.R.S. § 42-1310.01.B⁴ if purchased. However, lease income is not exempt from taxation if equipment is leased for less than two years.

BACKGROUND:

Laws 1991, Chapter 158, Section 12, amended A.R.S. § 42-1310.01.B⁵ to provide a definition of "new machinery and equipment" which is exempt from taxation if used for the commercial production of agricultural, horticultural, viticultural and floricultural crops.

¹ Since this ruling was issued A.R.S. § 42-1310.01(B)(13) was renumbered to A.R.S. § 42-5061(B)(13).

² Since this ruling was issued A.R.S. § 42-1310.01(B)(13)(b) was renumbered to A.R.S. § 42-5061(B)(13)(b).

³ Since this ruling was issued A.R.S. § 42-1310.11(B)(2) was renumbered to A.R.S. § 42-5071(B)(2).

⁴ Since this ruling was issued A.R.S. § 42-1310.01(B) was renumbered to A.R.S. § 42-5061(B).

⁵ See footnote number 4.

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"New machinery and equipment" is defined as a piece of machinery or equipment which has never been sold at retail except pursuant to leases or rentals which do not total two years or more.

Laws 1992, Chapter 135, Section 1, also amended A.R.S. § 42-1310.01.B⁶ to technically correct the language used in the statutory provision.

Laws 1995, Chapter 138, Sections 1 and 2, amended A.R.S. §§ 42-1310.01.B.13⁷ and 42-1409.B.13⁸ to provide that the exemption from transaction privilege and use tax for new machinery and equipment used for the production of agricultural crops includes machinery and equipment that are necessary for extracting milk and for cooling milk and livestock. The amendments also clarified that the term "self-powered implements" includes machinery and equipment that is electric powered. This legislation is retroactive to April 17, 1985.

Laws 1991, Chapter 158, Section 13, amended A.R.S. § 42-1310.11⁹ to provide that the rental of agricultural machinery or equipment for a period of two years or more is exempt from taxation under the personal property rental classification. However, the gross proceeds of a lease of new equipment which is being leased for a period of less than two years is not exempt from taxation under the personal property rental classification.

As a result of these amendments, the exemption under the retail classification for sales of new machinery and equipment used for the commercial production of agricultural, horticultural, viticultural and floricultural crops now includes machinery and equipment which has been leased or rented for a period of time not to exceed two years as well as machinery and equipment which has never been sold at retail.

The amendments were enacted by the Legislature in order to provide a definition of new agricultural machinery and equipment which corresponds with the practices of the agricultural machinery and equipment industry.

A dealer in agricultural machinery and equipment commonly allows potential customers to use equipment, for demonstration purposes, for a short period of time to determine if it is suitable for their needs. If the customer does not purchase the equipment but returns it to the dealer, it will be sold as "new" equipment in spite of the fact that it has been used for a short period of time.

⁶ See footnote number 4.

⁷ See footnote number 1.

⁸ Since this ruling was issued A.R.S. § 42-1409(B)(13) was renumbered to A.R.S. § 42-5159(B)(13).

⁹ Since this ruling was issued A.R.S. § 42-1310.11 was renumbered to A.R.S. § 42-5071.

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In addition, occasionally a dealer will loan or lease equipment to a customer as a temporary replacement for equipment which has broken down. Because the nature of agriculture requires that a crop must be planted or harvested at a certain time, letting a customer use equipment on a short term loan or under a lease agreement allows a dealer to demonstrate the capabilities of the equipment.

DISCUSSION:

The statute specifies that the exemption is limited to tractors, tractor-drawn implements, self-powered implements, machinery and equipment that are necessary for extracting milk, and for cooling milk and livestock and drip irrigation lines which are used in commercial production of agricultural, horticultural, viticultural and floricultural crops in this state¹⁰.

Agriculture consists of agricultural crop production as well as the breeding, feeding and raising of livestock and fowl, the production of feed for such animals, and milk production.

Examples of the types of agricultural machinery and equipment which qualify for the exemption are:

Tractors

Tractor Drawn Implements:

Land Planes

Plows

Discs

Harrows

Self or Electric Powered Implements:

Cotton Pickers

Combines

Fertilizer Sprayers

Bailers

Milking Machines

Milk Cooling Systems and Storage Tanks

¹⁰ Since this ruling was issued this section was amended to include agricultural aircraft.

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Fans used to cool livestock
Misting Systems used to cool livestock

QUESTIONS AND ANSWERS:

Following are some questions and answers regarding the taxation of agricultural machinery and equipment under the retail classification and under the personal property rental classification.

Q: If equipment is leased more than once, with the cumulative leases totaling less than two years, does the equipment qualify for the retail exemption when sold?

A: Yes. Because the total lease time is less than two years, the equipment is considered "new" agricultural machinery and equipment under the retail classification.

Q: If equipment is leased more than once, with the cumulative leases totaling less than two years, is any one lease subject to tax under the personal property rental classification?

A: Yes. Leases must be for two years or more to be exempt from taxation under the personal property rental classification.

Q: Is a three-year lease of new equipment, as defined in the statute, exempt under the personal property rental classification?

A: Yes. A lease of two years or more is exempt from transaction privilege tax under the personal property rental classification as a long-term lease of new equipment.

Q: Is new equipment which is leased for a period of one year and eleven months and then sold at retail, exempt under the retail exemption? What if the equipment is then immediately released for another lease period of one year and eleven months and then sold at retail? Is the lease exempt under the personal property rental classification?

A: A sale of the equipment following the first lease for a period of one year and eleven months is exempt under the retail classification. A sale of the equipment following the second lease is not exempt under the retail classification because the total lease time totaled two years or more. Both leases are taxable under the personal property rental classification.

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Q. Is a three-year lease of agricultural equipment which has previously been leased for a period of less than two years subject to tax under the personal property rental classification?

A. A three-year lease of agricultural equipment which qualifies as new because it has not previously been sold at retail or leased for a period of two years or more is exempt from tax under the personal property rental classification.

Q: How are lease-purchase transactions taxed?

A: If the lease-purchase agreement is for new equipment and for a period of two years or more, the gross proceeds or gross income from leasing are exempt from transaction privilege tax under the personal property rental classification.

Q: What is the effect of a conversion (sale) on a lease-purchase agreement prior to the two years elapsing? After two years have elapsed?

A: In general, when a lease-purchase is converted to a sale, the transaction is considered to be a retail sale at the time of the conversion. For information on the taxation of payments received after the lease is converted to a sale, see Arizona Administrative Code (A.A.C.) R15-5-1512.

If the conversion occurs prior to two years elapsing, the transaction is the sale of new equipment and exempt under the retail classification. However, if the lease was for less than two years at the time of the conversion, the lease income becomes subject to transaction privilege tax. If the conversion occurs after two years have elapsed, the resulting sale is of used equipment and is subject to tax.

RULING:

Under the retail classification, the gross proceeds from the sale of new agricultural machinery or equipment are exempt from tax. "New" agricultural machinery and equipment is that which has never been sold at retail. In addition, agricultural machinery and equipment which has never been sold at retail but has been leased for an aggregate period of less than two years is considered to be new and qualifies for the exemption. However, machinery and equipment which has been previously sold at retail or which has been leased for a period of two years or more, is used equipment and is not exempt from transaction privilege tax under the retail classification.

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The following leases of agricultural equipment and machinery are taxable under the rental of personal property classification:

1. A lease of new machinery and equipment which is for less than two years.
2. Successive leases of new machinery and equipment which do not total two years or more.
3. A lease of machinery and equipment which has previously been sold at retail.
4. A lease of machinery and equipment which has previously been leased for a total of two years or more.

Harold Scott, Director

Signed: December 20, 1995

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.