PRIVATE TAXPAYER RULING LR98-009

December 3, 1998

This is in response to your request for a private taxpayer ruling dated August 19, 1998, regarding ... and ... .

Statement of Facts:

... is a limited liability company of which ... are members. ... is the owner of the ... outlet mall located at the intersection of ... , Arizona. ... consists of 1,749,195 square feet, including common areas. ... has entered into numerous leases with tenants for retail, restaurant, entertainment, and other uses at ... .

... is controlled solely by The … and its affiliates. The … which are co-owners of ... , have no ownership interest in ... . entered into a … Management Agreement with ... allowing ... to operate and manage for the account of ... a kiosk and pushcart licensing program. Pursuant to this Management Agreement, ... has the authorization to execute, on behalf of ... , license agreements under which ... licenses the use of push cart or kiosk locations in the common areas of ... mall. Under the Management Agreement, ... is entitled to reimbursement of its operating costs, with the balance of the license fees received from kiosk/pushcart vendors being paid to ... .

As part of its operation and management of certain common areas under the … Management Agreement, ... , acting for and on behalf of ... , enters into License Agreements ("Agreement") between ... and various licensees which grant the licensees the right, for a fixed term (subject to unilateral termination or relocation by ... , as described below), to utilize a specified portion of the common area at ... for their retail, service, or other operations. These uses generally involve kiosks and/or pushcarts that, although movable, are required, pursuant to the Agreement; to remain at the fixed location covered by the Agreement.

The Agreement provides for a fixed "commencement date" and "ending date" and for a specific "location" and "unit number" to which the licensee will become entitled. The Agreement also provides for the payment of "minimum rent" and in most cases for payment of a "percentage rent". The Agreement provides however, that ... has the absolute right to relocate the licensee within the mall without prior notice or warning. The Agreement contains a specific "use clause" which restricts the licensee to specifically defined uses of the floor area of the mall being licensed to it.

Pursuant to the Agreements, ... provides to the Licensee either a kiosk or a pushcart, which are used to store and display the Licensee's wares. These kiosks and pushcarts, although not permanently attached to the floor of the mall, are restricted by the terms of the Agreement to the specific location in the mall to which the Agreement applies. Neither ... nor ... makes any separate charge for the kiosk or the pushcart that is segregated from the overall rent due under the Agreement. The overwhelming value for which the licensee is paying rent under the Agreement is not attributable to the cost or value of the kiosk or pushcart, but is attributable to the right to exclusive use of the space in the common areas of the mall where tremendous amounts of traffic are generated for the benefit of the licensee's business.

Your Position:

> ... is simply an agent of ... , acting on ... ' behalf, in licensing small portions of the common area of the mall to pushcart and kiosk vendors, and is not itself engaged in any taxable business activity.
>
> The license agreements between ... and the pushcart and kiosk vendors are "licenses" of the use of small portions of the mall's common area, and do not constitute the "leasing or renting" of real property.
>
> The license agreements between ... and the pushcart and kiosk vendors are "licenses" of the use of the kiosk and/or pushcart, and do not constitute the "leasing or renting" of tangible personal property.
>
> Even if the license of the pushcart or kiosk, pursuant to the same license agreement does not constitute the "leasing or renting" of real property, could be construed as the "leasing or renting" of personal property, that activity is merely incidental to the clearly primary activity of licensing real property, and is inconsequential in amount. Even though kiosks and/or pushcarts are supplied by ... to the licensees, because the fair rental value of the kiosk or pushcart is less than 3% of the total rental income being derived from the licensees, and because no separate charge is made for the kiosk and/or pushcart, ... is not "engaged in the [separate] business" of leasing tangible personal property, but the provision of the pushcarts/ kiosks is merely incidental to the licensing of real property and inconsequential in amount.

Applicable Statutory Provisions:

Arizona Revised Statutes (A.R.S.) § 42-1310.09 imposes the transaction privilege tax on the business of leasing for a consideration the use or occupancy of real property. The tax base under the commercial lease classification is the gross proceeds of sales or the gross income derived from the business. The state tax rate for the commercial lease classification is currently 0%.

A.R.S. § 42-1310.11 imposes the transaction privilege tax on the business of leasing or renting tangible personal property for a consideration. The tax base for the personal property rental classification is the gross proceeds of sales or the gross income derived from the business. The state tax rate for the commercial lease classification is currently 5%.

Discussion:

Arizona imposes a transaction privilege tax that differs from the sales tax imposed by most states. The Arizona transaction privilege (sales) tax is a tax imposed on the privilege of conducting business in the State of Arizona. This tax is levied on the ***vendor***, not the purchaser. The vendor may pass the burden of the tax on to the purchaser; however, the vendor is ultimately liable to Arizona for the tax.

According to the information provided, ... is the owner of the … mall located at the intersection of ... , Arizona. ... has an operation and management agreement with ... to manage the use of the "common areas" at ... for kiosk and pushcart vendor licensing. In turn, ... , acting for and on behalf of ... , enters into license agreements with various licensees that grant the licensees the exclusive right, for a fixed term, to use kiosks or pushcarts in certain common areas of the mall.

The fact that an agreement is called a license is not sufficient to determine the tax status of the payments received under the agreement for transaction privilege tax purposes. Transaction privilege tax is levied on the commercial lease classification by A.R.S. § 42-1310.09. The commercial lease classification consists of the business of leasing or renting the use or occupancy of real property for a consideration.

The issue of whether an agreement was a lease or a license was addressed by the Arizona Court of Appeals. A department store entered into agreements with retailers that granted the retailer the exclusive right to operate a particular type of department within the department store. The retailer was allowed to conduct only that specified type of business within the store. In consideration of the department store furnishing certain services, the retailer paid a percentage of his gross receipts with a minimum monthly payment designated. The agreements were for a definite term and were automatically renewed absent any notice of termination, but the department store could terminate the agreement at any time if the retailer was in default. Under the agreement the department store was obligated to furnish the licensee/retailer an agreeable amount of space in its store, but such space was not specifically

delineated within the agreement. In fact, the space could have been changed from time to time at the department store's direction.

The court concluded that as a matter of law the agreement between the department store and its merchant retailers did not rise to the level of a leasehold interest, but was a mere license. As such, the City of Phoenix tax on the lease or rental of real property could not be imposed on the department store. *Wenner v. Dayton-Hudson Corp.*, 123 Ariz. 203 (Ariz. App. 1979).

With regard to the use of the Mall's common areas, the agreements between ... , through its agent, ... , and its licensees are similar to the agreement between Dayton-Hudson and its retailers. ... ' license agreement does not grant the licensees an exclusive right to a specific location. "Licensor hereby grants to Licensee a non-exclusive license to occupy and use, ..." (License Agreement, paragraph 1.) In addition, the licensor retains the absolute right to cancel the agreement at any time for any reason on twelve hours notice and the absolute right to relocate the licensee within the shopping center without prior notice or warning. (License Agreement, paragraph 17.)

Concerning the issue of whether the lease of the kiosks and pushcarts is the rental of tangible personal property, the Arizona Supreme Court held that a laundromat and a car wash business were in the business of renting tangible personal property regardless of the fact that the rented equipment was used on the premises of the owner. *State Tax Commission v. Peck*, 106 Ariz. 394 (1970). *City of Phoenix v. Bentley-Dille Gradall Rentals, Inc*., 136 Ariz. App. 289, 665 P.2d 1011 (1983), acknowledged the court's holding in *State Tax Commission v. Peck,* and stated "the principal characteristic of a rental or lease is the giving up of possession to the lessee so that he, as opposed to the lessor, exercises control over and uses the leased or rented property." If control is not relinquished, the activity is not considered a rental for purposes of taxation under the personal property rental classification.

Under the agreement between ... and the kiosk/pushcart vendors, the "premise" as defined under the agreement is the pushcart or kiosk. The agreement lists the premise type as: Pushcart/RMU, Kiosk or In-line. The vendor has exclusive possession, use, and control of the pushcart/kiosk for the agreed upon period and rental amount. The fact that the pushcart/kiosk may be moved to another location without warning does not alter the vendor's ability to use the pushcart or kiosk or to preclude others from using it.

Conclusion and Ruling:

On the basis of the information provided, we rule that:

> ... is an agent of ... , acting on ... ' behalf, in licensing small portions of the common area of the mall to pushcart and kiosk vendors, and is not itself engaged in any taxable business activity.

> The license agreements between ... and the pushcart and kiosk vendors are not "licenses" of the use of small portions of the mall's common area.
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> The Agreements between ... and the pushcart and kiosk vendors constitute the "leasing or renting" of tangible personal property and are subject to tax under the personal property rental classification.
>
> The lease of the pushcart/kiosk is not merely incidental to the activity of licensing real property. The agreement lists the premise type as: Pushcart/RMU, Kiosk or In-line.

The conclusion in this private taxpayer ruling does not extend beyond the facts as presented in the letter dated August 19 1998, in the request for a private taxpayer ruling.

This response is a private taxpayer ruling and the determination herein is based solely on the facts provided in your request. The determination in this taxpayer ruling is the present position of the department and is valid for a period of four years from date of issuance except as set out herein. This determination is subject to change should the facts prove to be different on audit. If it is determined that undisclosed facts were substantial or material to the department's making of an accurate determination, this taxpayer ruling shall be null and void. Further, the determination is subject to future change depending on changes in statutes, administrative rules, case law or notification of a different department position.