

PRIVATE TAXPAYER RULING LR00-005

July 26, 2000

The following private taxpayer ruling is in response to your request of October 15, 1999, as amended by your letter of March 31, 2000. Your letter requests a determination regarding the application of transaction privilege tax on income derived by . . . [Taxpayer] from providing vanpool services under a contract with . . .

The following is a restatement of the facts presented in your letter.

Statement of Facts:

Taxpayer is a for profit corporation that provides . . . vanpool vehicles . . . Taxpayer recently re-negotiated a contract with . . . to provide vehicles, under vehicle license agreements, for . . .'s vanpool program in . . .

. . .

Under Taxpayer's previous contract with . . ., Taxpayer paid Arizona transaction privilege tax under the personal property rental classification. The Arizona Department of Revenue audited Taxpayer while paying under that classification.

Your Position:

Taxpayer is operating outside the scope of the transaction privilege tax because it is performing a governmental function. Therefore, Taxpayer is not subject to transaction privilege tax.

The state and its political subdivisions are subject to transaction privilege tax when engaged in proprietary functions. Arizona Administrative Code (A.A.C.) R15-5-181(B). However, when engaged in governmental functions, the state and its political subdivisions are not subject to transaction privilege tax. Arizona Constitution,

article XIII, § 7; *Salt River Project Agriculture Improvement and Power Dist. v. City of Phoenix*, 129 Ariz. 398, 631 P.2d 553 (App. 1981); *City of Phoenix v. City of Goodyear*, -- Ariz. --, 851 P.2d 154 (Tax 1993); *Flowing Wells Irrigation District v. City of Tucson*, -- Ariz. --, 863 P.2d 915 (Tax 1993).

A "governmental function" is "generally recognized as one undertaken because of a duty

imposed on the [governmental unit] for the welfare or protection of its citizens." *Copper Country Mobile Home v. City of Globe*, 131 Ariz. 329, 641 P.2d 243 (App. 1981). On the other hand, a proprietary function is a "commercial activity which directly competes with other commercial activities in the city." *Book-Cellar, Inc. v. City of Phoenix*, 150 Ariz. 42, 721 P.2d 1169 (App. 1986). Proprietary functions may be funded through bonds rather than directly by state taxes, as was the case with the fairgrounds in the *Book-Cellar, Inc. v. City of Phoenix* case.

... Thus, ... is a political subdivision of the state and, as such, it is not subject to transaction privilege tax on its proceeds from governmental activities. Arizona Constitution, art. XIII, § 7; *Salt River Project Agriculture Improvement and Power Dist. v. City of Phoenix*, 129 Ariz. 398, 631 P.2d 553 (App. 1981); *City of Phoenix v. City of Goodyear*, -- Ariz. --, 851 P.2d 154 (Tax 1993); *Flowing Wells Irrigation District v. City of Tucson*, -- Ariz. --, 863 P.2d 915 (Tax 1993).

Political subdivisions of the state have the powers delegated to them "by the constitution and the general laws of the state." *City of Tempe v. Arizona Board of Regents*, 11 Ariz. App. 24, 461 P.2d 503 (App. 1969). Accordingly, ...'s board is empowered by the Legislature to ...

... Under its contract with ... , Taxpayer is providing vehicles for ...'s vanpools in behalf of ... As ...'s independent contractor, Taxpayer performs a governmental function when it fulfills its contractual obligation to ... by providing vehicles for the vanpools. Because Taxpayer is performing a governmental function, its gross proceeds, including proceeds from ... and the vanpool riders, are not subject to transaction privilege tax.

...

Applicable Statutory Provisions:

A.R.S. § 42-5001(1) defines "business" as all activities or acts, personal or corporate, engaged in or caused to be engaged in with the object of gain, benefit or advantage, either directly or indirectly, but not casual activities or sales.

A.R.S. § 42-5008 levies the transaction privilege tax, measured by the amount or volume of business transacted by persons on account of their business activities.

A.R.S. § 42-5071 imposes the transaction privilege tax on the business of leasing or renting tangible personal property for a consideration. The tax base is the gross proceeds of sales or gross income derived from the business.

Discussion:

Arizona's transaction privilege tax is a tax on the privilege of conducting business in the State

of Arizona. It is a tax on the seller, not on the purchaser. The seller may pass the burden of the tax on to the purchaser; however, the seller is ultimately liable to Arizona for the tax.

The term "business" encompasses all activities engaged in for the purpose of gain, benefit or advantage.

It is not disputed that . . . is a political subdivision of the state, and as such, is not subject to transaction privilege tax when performing governmental functions. A governmental function is generally recognized as one undertaken because of a duty imposed on the entity for the welfare or protection of its citizens or a function that is fundamentally inherent in or encompassed within the basic nature of government. *Flowing Wells Irrigation District v. City of Tucson*, -- Ariz. --, 863 P.2d 915 (Tax 1993) citing *Copper Country Mobile Home v. City of Globe*, 131 Ariz. 329, 333, 641 P.2d 243, 247 (App. 1982); *Book-Cellar, Inc. v. City of Phoenix*, 150 Ariz. 42, 44, 721 P.2d 1169, 1171 (App. 1986).

However, Taxpayer is not a government entity, and therefore, does not perform governmental functions. Taxpayer is a for profit corporation that engages in activities for the purpose of gain, benefit or advantage. Specifically, Taxpayer has entered into a contract with . . . which provides that in consideration of the compensation provided, Taxpayer agrees to furnish vehicles owned/leased by Taxpayer, and the insurance, maintenance, fleet management and administrative services for those vehicles.

The transaction privilege tax is imposed on the business of leasing or renting tangible personal property for a consideration. A lease, with reference to tangible personal property, is defined as "a contract by which one owning such property grants to another the right to possess, use and enjoy it for a specified period of time in exchange for periodic payment of a stipulated price, referred to as rent." *Black's Law Dictionary*, Sixth Edition, West Publishing Co., 1990, citing *Undercofler v. Whiteway Neon Ad, Inc.*, 114 Ga. App. 644, 152 S.E.2d 616, 618.

Conclusion and Ruling:

The following ruling is given based on the facts presented in your request.

The department rules that the gross income derived by Taxpayer from the business of providing motor vehicles for . . . is subject to transaction privilege tax under the personal property rental classification.

The conclusion in this private taxpayer ruling does not extend beyond the facts as presented in the request for a private taxpayer ruling dated October 15, 1999, and mended by your letter of March 31, 2000.

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. 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.