



TAXPAYER INFORMATION RULING LR10-005

Janice K. Brewer
Governor

Gale Garriott
Director

March 5, 2010

The Department issues this taxpayer information ruling in response to the ruling request on behalf of your anonymous client ("Company") dated March 2, 2009, and the additional information and documentation provided on June 24 and October 12, 2009. You request the Department to rule as to the applicability of Arizona transaction privilege tax to income derived from a motor vehicle dealer's "transfer fees," which are fees collected from potential customers for the transfer of a selected vehicle from one dealership to the dealership located closest to the customer. Pursuant to Arizona Revised Statutes ("A.R.S.") § 42-2101, the Department may issue a taxpayer information ruling to a taxpayer's representative. Arizona General Tax Procedure GTP 08-1 provides detailed information about the issuance and scope of private taxpayer rulings and taxpayer information rulings.

Statement of Facts:

The following facts are excerpted from your letter dated March 2, 2009:

The Company is a motor vehicles retailer. The Company maintains business locations in multiple states, including Arizona. Customers may purchase motor vehicles from the Company directly at the Company's business locations. On many occasions, a vehicle meeting the customer's requirements is not available at the Company store in the customer's immediate vicinity. And, as one would expect, most customers are unwilling to purchase a motor vehicle sight unseen and without a test drive.

On such occasions where a customer is interested in viewing and testing a motor vehicle not located at the nearest Company store, the Company will offer the customer the option of having that motor vehicle shipped to one of its business locations near the customer's home. This transfer is done under the terms of a specific and separate transfer agreement between the Company and the customer (hereafter the "Transfer Contract"). The Company charges its customers a "transfer fee" for this service.

The transfer / shipping process consists of six steps:

1. Customers contact the Company location closest to where they live: (fn: In larger markets, the Company may have more than one store within easy driving distance of a customer) Customers call a Company Sales Consultant or submit a Vehicle Transfer Form from a Vehicle Fact Sheet. If

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a Customer chooses to submit a form online, a Sales Consultant will contact the Customer to answer any questions about the vehicle, and to ensure that the vehicle meets their specific needs.

2. Pre-transfer inspection: The Sales Consultant inspects the car and provides answers to the Customer's questions at no charge to the Customer.
3. Confirmation: The Sales Consultant contacts the Customer to answer any additional questions. If the vehicle is not at the Customer's delivery location, the Sales Consultant will confirm the Customer's order to have the vehicle transferred.
4. Contract: The Customer is required to enter into a contract (the "Transfer Contract") calling for the transfer of the subject vehicle at a stated fee.
5. Payment of the Transfer Fee: If the Customer executes the transfer agreement, the Customer is required to either:
 - Bring a check for the full amount of the transfer fee to the Company location where the vehicle will be transferred; or
 - Pay the transfer fee over the phone using their credit card.
6. Reservation & Transfer: Once payment is received, the Sales Consultant verifies that the vehicle has been reserved and it is scheduled for transfer.

It should be noted that the Transfer Contract relates only to shipping vehicles. No other services are provided in exchange for the "transfer fee." For instance, executing the Transfer Contract does not entitle the customer to a vehicle fact sheet, on location inspection, and/or any other service. More importantly, the Transfer Contract is not dependent upon any other agreement - and in particular, is not dependent on the ultimate sale of the vehicle. Indeed, frequently a vehicle which has been transferred is not purchased by the customer who executes a Transfer Contract and the transfer fee. In such cases, the transfer fee is not refunded. Likewise, if the vehicle is purchased, that purchase is executed under a separate purchase and sale contract which neither refers to, nor incorporates by reference, the Transfer Contract. In no circumstances does either the existence of a Transfer Contract or payment of a transfer fee impact the sales price of the motor vehicle. In short, if a customer pays a transfer fee to view and inspect a vehicle, the price at which the transfer fee is not deducted from, or considered to be part of, the sales price.

The following statements are excerpted from the additional information that was provided on October 12, 2009:

Regarding whether the vehicle would be purchased from the transferring dealership or the receiving dealership, and which business location receives the transfer fee:

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If the customer decides to purchase the vehicle, the transaction will be executed at Company retail location A – closest Company retail location to the customer. The transfer is a transfer of inventory from one Company-owned retail location to another.

...

The transfer fee is paid to the Company retail location receiving the transferred vehicle; however, all retail locations are owned by the Company.

Regarding what happens if the customer decides not to purchase the vehicle:

The transferred vehicle will remain in the Company's available for-sale inventory until the vehicle is ultimately sold to a retail customer. All sales transactions are executed at the location the vehicle is transferred to. Any transferred vehicle not sold remains in the transferred location's available for sale inventory until sold or transferred to another Company location.

Regarding the amount of the transfer fee:

Fees are not dependent upon the sale of the vehicle. However, the Fee is dependent upon the distance of the transfers. In most cases, the cost associated with transferring the vehicle is greater than the Transfer Fee charged to the customer.

Issue:

Is income derived from a motor vehicle retailer's fees, charged solely for the transfer of a vehicle from one business location to another business location that is closest to a potential customer, subject to transaction privilege tax when the transfer contract is completely independent of a sales contract and is not contingent on the sale of the vehicle?

Your Position:

Your position is stated in your taxpayer information ruling request as follows:

Arizona transaction privilege tax does not apply to transfer fees charged and collected by the Company if the Customer ultimately purchases the motor vehicle transferred to the Company's place of business, because the fee does not relate to the taxable sale of the vehicle; and

Arizona transaction privilege tax does not apply to transfer fees charged and collected by the Company if the Customer ultimately does not purchase the motor vehicle transferred, because such transactions involve only the provision of a non-taxable service.

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Discussion

Arizona's transaction privilege tax differs from the sales tax imposed by most states. The transaction privilege tax is imposed on the privilege of conducting business in the State of Arizona. Differing from a true sales tax, the transaction privilege tax is levied on income derived by the *seller* or *lessor*, who is legally allowed to pass the economic expense of the tax on to the purchaser. However, the seller or lessor is ultimately liable to Arizona for the tax. The Arizona transaction privilege tax is imposed under 16 separate business classifications, including the retail classification and the transporting classification. Additionally, county excise taxes "piggyback" the imposition of the state's transaction privilege tax. All income that is subject to the transaction privilege tax is also subject to applicable county excise taxes.

A.R.S. § 42-5061 *Retail classification*, imposes the transaction privilege tax upon persons engaged in the business of selling tangible personal property at retail. The tax base is the gross proceeds of sales or gross income derived from the business. All sales of tangible personal property are subject to the transaction privilege tax under the retail classification unless specifically exempted or excluded by statute.

A.R.S. § 42-5001 provides definitions that describe the tax base:

(4) "Gross income" means the gross receipts of a taxpayer derived from trade, business, commerce or sales and the value proceeding or accruing from the sale of tangible personal property or service, or both, and without any deduction on account of losses.

(7) "Gross receipts" means the total amount of the sale, lease or rental price, as the case may be, of the retail sales of retailers, including any services that are a part of the sales, valued in money, whether received in money or otherwise, including all receipts, cash, credits and property of every kind or nature, and any amount for which credit is allowed by the seller to the purchaser without any deduction from the amount on account of the cost of the property sold, materials used, labor or service performed, interest paid, losses or any other expense. Gross receipts do not include cash discounts allowed and taken nor the sale price of property returned by customers if the full sale price is refunded either in cash or by credit.

[Emphasis added]

A.R.S. § 42-5061(A)(2) provides a deduction from the retail tax base for income derived from "[s]ervices rendered in addition to selling tangible personal property at retail." The taxpayer information ruling request attempts to portray Company's transfer of a vehicle to a more convenient business location as a distinct service provided to a potential customer, which is unrelated to a retail sale of a motor vehicle as the potential customer is not obligated to purchase the transferred vehicle. However, the transfer of a vehicle in which a

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potential customer has an expressed interest is merely a business activity aimed at increasing the retailer's sales of motor vehicles. Despite the fact that the transfer agreement is a separate transaction that may or may not result in the sale of the transferred vehicle, income derived from this activity is a part of a retailer's gross income derived from engaging in business.

In *Walden Books Co. v. Ariz. Dep't of Revenue*, 198 Ariz. 584, 12 P.3rd 809 (App. 2000), the Court addressed whether income derived from sales of memberships which were sold to customers and potential customers qualified for the retail classification deduction for "services rendered in addition to selling tangible personal property at retail." Like Company's transfer agreements at issue in the taxpayer information ruling request, Walden's memberships were sold separately from its books and merchandise. The Court found that income derived from the sale of memberships did not qualify as "services rendered in addition to selling tangible personal property at retail," as this was a service provided to increase sales. The Court stated:

Turning now to the "service" issue, we conclude that a service provided by Waldenbooks designed to encourage Program members to buy more merchandise is not a service "in addition to selling tangible personal property at retail." Waldenbooks admits that the Program is aimed at encouraging its members to purchase its merchandise. In an answer to an interrogatory, Waldenbooks stated, "The primary purpose of the program was to develop customer loyalty which in turn would increase sales by providing an incentive for customers to buy books at our stores instead of competitors' stores." Such incentives cannot rationally be characterized as separate and apart from the sale of tangible personal property at retail. Services intended to induce customers to buy more goods are not provided "in addition to" selling goods; they are "a part of the sales" of those goods, and are included in retail "gross income" via subsections 42-5001(4) and (7).

(*Walden* at 813)

Additionally, while a separately stated charge for transporting merchandise to a purchaser is generally exempt from transaction privilege tax, income derived from the cost of transporting merchandise which occurs prior to the retail sale is subject to tax. Arizona Administrative Code (A.A.C.) rule R15-5-133 states:

R15-5-133. Delivery Charges in Connection with Retail Sales

- A. A charge by a retailer for delivery from the retailer's location to the purchaser's location, if separately stated on the sales invoice, is not taxable.
- B. When the freight cost is incurred any time prior to the time of the retail sale, such cost is part of the gross sale and, therefore, subject to the tax.

(Emphasis added)

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Conclusion and Ruling

Company is subject to transaction privilege tax under the retail classification on the gross income derived from fees charged for the transfer of a vehicle from one business location to the business location that is closest to a potential customer, because this service activity is an integral part of the Company's retail business of selling motor vehicles.

The conclusions in this taxpayer information ruling do not extend beyond the facts presented in the correspondences dated March 2, June 24, and October 12, 2009.

This response is a taxpayer information ruling (TIR) and the determination herein is based solely on the facts provided in your request. The determinations are 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 information 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.

If the Department is provided with required taxpayer identifying information and taxpayer representative authorization before the proposed publication date (for a published TIR) or date specified by the Department (for an unpublished TIR), the TIR will be binding on the Department with respect to the taxpayer that requested the ruling. In addition, the ruling will apply only to transactions that occur or tax liabilities that accrue from and after the date the taxpayer receives the ruling. The ruling may not be relied upon, cited, or introduced into evidence in any proceeding by a taxpayer other than the taxpayer who has received the taxpayer information ruling. If the required information is not provided by the specified date, the taxpayer information ruling is non-binding for the purpose of abating interest, penalty or tax.