



Arizona's Sometimes Stealth Use Tax Reporting Requirements

This month's state and local tax (SALT) column explains how and why Arizona taxpayers should comply with their use tax obligations.

Similar to other states with sales and use taxes, Arizona imposes both transaction privilege (sales) tax and use tax, and most Arizona municipalities that impose sales tax also impose use tax. Arizona's use tax applies to purchases of tangible personal property from retailers and utility businesses if the property is stored, used or consumed in the state.

Arizona Use Tax Liability

Purchasers, rather than vendors, are responsible for payment of Arizona's use tax — but the tax does not apply to property sold in the state that was subject to Arizona's sales tax, whether or not the tax was paid. Likewise, purchasers are entitled to an offset against their Arizona use tax liability for excise taxes paid on property that was subjected to tax in another state.

Essentially, Arizona's use tax is meant to complement its sales tax such that every retail transaction involving tangible personal property that is stored, used, or consumed in Arizona is subject to one of these taxes, unless a deduction or exemption applies.

Common Applications of Arizona's Use Tax

The most common Arizona use tax triggers include: (1) purchases from out-of-state retailers without nexus in Arizona that cannot be required to collect Arizona taxes, (2) purchases from out-of-state retailers that collect tax for another state at a rate lower than Arizona's use tax rate, and (3) purchases of items for resale that are pulled out of inventory and stored, used or consumed in Arizona.

Use Tax Reporting and Audits

Businesses licensed to collect and remit sales tax are accustomed to paying use tax when they file their monthly, quarterly, or annual sales tax returns. And when the Arizona Department of Revenue (Department) performs sales tax audits on those businesses, it also determines whether they paid use tax on all of their transactions that were subject to use tax.

Arizona's Stealth Use Tax Reporting Requirement

Although most Arizona businesses are not licensed to remit use tax, and even though hardly any Arizona citizens are licensed to remit use tax, Arizona use tax applies to every retail transaction involving tangible personal property that is stored, used or consumed in Arizona, unless a deduction or exemption applies.

Similar to what many states have done for years, for tax year 2012 Arizona



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added a line to its individual income tax forms requiring those who stored, used or consumed property in Arizona for a nonbusiness purpose to declare the use tax due, unless sales tax was collected by a registered retailer. But after public and tax return preparer outcry, the state discontinued that requirement after just one year.

Thus, most Arizona businesses and virtually all Arizona citizens who make out-of-state purchases from retailers that do not collect sales tax are subject to Arizona use tax yet lack a convenient way to pay it. Although the Department invites those who make a single purchase subject to use tax to contact them for payment instructions, very few take them up on the invitation.

Beware of Use Tax Liability

While every conscientious business owner and citizen should consider

how they can comply with Arizona's use tax laws, those who make sizeable purchases of tangible personal property from out-of-state retailers that do not collect sales tax should heed that liability because the Department can assess penalties that quickly add up to at least 25% of the tax, plus interest, when they conduct audits. In fact, the Department's auditors routinely audit businesses and individuals that purchase automobiles, aircraft and valuables that pass through Customs to determine whether sales or use tax was paid on such items.

The Arizona use tax audit risk for businesses and individuals that do not file sales or use tax returns may be compounded by the lack of a statute of limitations for taxpayers who fail to file returns. Thus, the Department may not be required to limit audits of those businesses and individuals to standard four-year audit periods.

Practice Tip

Tax professionals should make sure that their employers and clients are aware of Arizona's use tax and help them comply with it. Businesses and individuals that are not licensed to collect and remit sales tax in Arizona but regularly incur Arizona use tax liability should register to report use tax by completing sections A, C and F of Arizona's Joint Tax Application and comparable applications for any non-program cities where they have use tax liability. However, to minimize their exposure to tax, penalties, and interest for past periods, those with significant unsatisfied use tax liabilities may be good candidates for a voluntary disclosure agreement or a managed audit before registering to report use tax. ■

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