

Arizona's Sometimes Stealth Use Tax Reporting Requirements

by James G. Busby Jr.



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In this article, Busby explains how and why Arizona taxpayers should comply with their use tax obligations — noting the requirements that are unique to the state.

Similar to other states with sales and use taxes, Arizona imposes both transaction privilege (sales) tax and use tax, and most 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 that is stored, used, or consumed in the state.¹

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 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 subject to tax in another state.²

Essentially, the use tax is meant to complement the sales tax such that every retail transaction involving tangible personal property that is stored, used, or consumed in Arizona is subject to tax, unless a deduction or exemption applies.

Common Use Tax Applications

The most common Arizona use tax liability triggers include:

- purchases from out-of-state retailers without nexus in Arizona that cannot be required to collect taxes;
- purchases from out-of-state retailers that collect tax for another state at a rate lower than Arizona's use tax rate; and
- 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 performs sales tax audits on those businesses, it also determines whether they paid use tax on all of their transactions subject to use tax.

Stealth Use Tax Reporting Requirement

Although most Arizona businesses — and hardly any Arizona citizens — are licensed to collect and remit sales tax, 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.³

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

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

¹A.R.S. section 42-5155.

²A.R.S. section 42-5159(A)(1) and (2).

³A.R.S. section 42-5152.

laws, those who make sizable purchases of tangible personal property from out-of-state retailers that do not collect sales tax should heed that liability because the DOR can assess penalties that quickly add up to at least 25 percent of the tax, plus interest, when it conducts audits. In fact, the DOR'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 those 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 DOR may not be required to limit audits of those businesses and individuals to standard four-year audit periods.⁴

Practice Tip

Tax professionals should make sure that their employers and clients are aware of Arizona's use tax and help them

⁴A.R.S. section 42-1104(B)(1)(b).

comply. Businesses and individuals that are not licensed to collect and remit sales tax in Arizona but regularly incur 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. ☆

CORRECTION

The SALT From My Saddle column in the September 21 edition of *State Tax Notes* contained an error. In "5 Important Changes to 4 Arizona Tax Credits," the second sentence in the first paragraph under Credit for Contributions to Public Schools on p. 1017 should read:

This dollar-to-dollar credit is good for up to \$200 for single taxpayers and up to \$400 for married taxpayers filing jointly.

Tax Analysts regrets the error. ☆