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State and local tax services

## Arizona legislation phases-in single sales factor apportionment election, decreases corporate income tax rate

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Arizona legislation signed into law on February 17, 2011, includes a phased-in single sales factor apportionment election and a scheduled decrease in the corporate income tax rate. The legislation also provides businesses with economic development incentives, such as tax credits for new jobs created, and establishes the Arizona Commerce Authority. [H.B. 2001, enacted 2/17/11; effective 6/30/11.]

### **Phase-in of single sales factor apportionment election**

Currently, taxpayers elect to apportion all business income to Arizona using one of two methods: a double-weighted sales factor formula, or a fraction equal to the property factor plus the payroll factor plus eight times the sales factor, divided by ten (*i.e.*, an 80% sales factor formula). For taxable years beginning after December 31, 2013, the legislation provides for a phase-in of a single sales factor election. Under the legislation, taxpayers may elect to apportion Arizona business income as follows:

- For tax years beginning after December 31, 2013, but on or before December 31, 2014: by either a double-weighted sales factor formula, or a fraction equal to seven and one-half times the property factor plus seven and one-half times the payroll factor plus 85 times the sales factor, divided by 100 (*i.e.*, an 85% sales factor formula);
- For tax years beginning after December 31, 2014, but on or before December 31, 2015: by either a double-weighted sales factor formula, or a fraction equal to five times the property factor plus five times the payroll factor plus 90 times the sales

factor, divided by 100 (*i.e.*, a 90% sales factor formula);

- For tax years beginning after December 31, 2015, but on or before December 31, 2016: by either a double-weighted sales factor formula, or a fraction equal to two and one-half times the property factor plus two and one-half times the payroll factor plus 95 times the sales factor, divided by 100 (*i.e.*, a 95% sales factor formula);
- For tax years beginning after December 31, 2016: by either a double-weighted sales factor formula or a single sales factor formula.

### **Reduction of corporate income tax rates**

Currently, the corporate income tax rate is 6.968%. Under the legislation, for tax years beginning after December 31, 2013, the corporate income tax rate is reduced as follows:

- For tax years beginning after December 31, 2013, but on or before December 31, 2014, the corporate income tax rate will be 6.5%;
- For tax years beginning after December 31, 2014, but on or before December 31, 2015, the corporate income tax rate will be 6%;
- For tax years beginning after December 31, 2015, but on or before December 31, 2016, the corporate income tax rate will be 5.5%;
- For tax years beginning after December 31, 2016, the corporate income tax rate will be 4.9%.

### **Other economic development/business incentives**

In addition to broad tax reforms, the legislation includes targeted business incentives focused on job creation and business growth and development. Effective for taxable years beginning on or after December 31, 2013, capital gains on income derived from investments in small businesses with assets up to \$10 million will be excluded from Arizona gross income.

While the legislation ends the state's enterprise zone program, which offered tax breaks to select businesses, and certain other economic development programs, Arizona will now provide businesses located within the state prior to July 1, 2017, a \$9,000 tax credit for each qualifying new job created (\$3,000 per job, per year for three years, up to 400 jobs). Further, Arizona taxpayers can now take advantage of an additional 10% research and development tax credit for university-related research, and a 5% acceleration of depreciation for business personal property, among other benefits afforded by the legislation.

Of note is the law's replacement of the Arizona Department of Commerce with the Arizona Commerce Authority (the "Authority"), a public-private economic development agency charged with the responsibility of recruiting and retaining quality businesses in Arizona. The Authority is to have a \$25 million dollar deal-closing fund to assist it in achieving its charge, and is set to expire on July 1, 2016.

### **PwC observes**

"This legislation represents the culmination of several years of effort put forth by Governor Brewer to reduce the corporate tax burden on Arizona businesses," says Joe Motola, PwC SALT Director in Phoenix.

"In line with the political environment in Arizona, the intent is that this package will give out-of-state businesses, especially those in the renewable energy and defense contracting industries, as well as those that spend heavily on research and development activities, incentive to look at Arizona as a place to consider during expansion. It also encourages development of small business enterprises."

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