



**MEMORANDUM Management Services Department – Council Memo No. MS 13-001**

**DATE:** DECEMBER 13, 2012

**TO:** MAYOR AND COUNCIL

**THRU:** RICH DLUGAS, CITY MANAGER *RD*  
DAWN LANG, MANAGEMENT SERVICES DIRECTOR *DL*  
MATT DUNBAR, REVENUE & TAX MANAGER *MD*

**FROM:** LEE GRAFSTROM, TAX AUDIT SUPERVISOR *LG*

**SUBJECT:** REQUEST FOR INTRODUCTION AND TENTATIVE ADOPTION OF ORDINANCE NO. 4376

**RECOMMENDATION:** Staff recommends introduction and tentative approval of Ordinance No. 4376 of the City Council of the City of Chandler, Arizona, amending Sections 62-410, 62-422, and 62-445 and Regulation 62-415.3 of Chapter 62, Code of the City of Chandler, and establishing effective dates thereof, relating to conforming changes to the Chandler Tax Code.

**BACKGROUND:** Arizona allows incorporated cities and towns to have a separate tax base for their transaction privilege and use taxes, more commonly referred to as the City’s sales and use tax. Arizona’s Model City Tax Code (“MCTC”) is the document that standardizes the taxes a municipality can choose to levy, however the State does preempt cities and towns from taxing certain activities and transactions.

The MCTC was created in response to concerns about differences in local transaction privilege tax codes and the resulting compliance difficulties. The MCTC provides uniformity while at the same time retaining the right of each municipality to choose the activities that are taxed and the exemptions that are granted, thereby leaving the determination of the local sales tax base up to the individual city council. While some city charters require a vote of the citizens to establish a city’s tax rates, Chandler’s transaction privilege and use tax rates are set by a simple majority vote of Mayor and Council for all classifications, except Real Property Rental.

Each city chooses which activities are taxable under the MCTC; however, if they choose to tax a particular activity it must be done in accordance with the MCTC. The code itself consists of standard language, referred to as “model” language, along with Local Options and Model Options. The options provide alternatives for a particular code section that any city or town can choose to incorporate in place of model language. Generally, Local Options add or substitute language in a given section, while Model Options remove model language. These options are

the means by which the city can fine-tune its tax code to match its economic environment.

The final piece of the MCTC is a collection of city-based exceptions that are commonly referred to as “green page” items. A green page item replaces the standard model or option code language with alternative language that applies only to that specific city. Although common when the MCTC was first created, there has been considerable pressure by taxpayer advocates and the Legislature to eliminate these differences whenever possible, and to discourage the creation of any new green page exceptions.

All changes to the MCTC require the prior approval of the Municipal Tax Code Commission (“Commission”), and all municipalities that have adopted the code must adopt all changes approved by the Commission. The Commission is comprised of nine mayors or city council members appointed by the Governor, Senate President, and Speaker of the House, along with the Director of the Department of Revenue, as an ex-officio member.

Following each legislative session, Arizona cities and towns acting collectively through the Unified Audit Committee (“UAC”), review new laws to determine those areas of the MCTC that require adjustment to maintain or achieve conformity with State law. The UAC also meets with taxpayer advocates and business representatives to draft tax code changes, which are then forwarded to the Commission for approval. Any changes to the MCTC that are approved by the Commission must be adopted by the City Council, unless the change is a Local Option or Model Option, which the Council may choose to select or reject as they see fit.

**DISCUSSION:** In addition to three miscellaneous technical corrections to the Amusements classification, Jet Fuel Classification, and Regulations, there is one substantive tax code change in this action – the addition of a new preemption in the Real Property Rental classification. For ease of incorporation, all of these changes are effective from and after July 20, 2011 to coincide with the effective date of the new State preemption under Section 445.

62-410 – Amusements, exhibitions, and similar activities

Section I of the ordinance corrects an inadvertent error that left out two lines from the MCTC in subsection (a). This error had no substantive impact, as the MCTC is governing whenever there is an unauthorized difference between the MCTC and a city tax code. This section also corrects two minor typographical errors.

62-422 – Jet fuel sales

Section II of the ordinance eliminates an obsolete reference to a code section that was repealed several years ago. The former Section 567 dealt with determining which city had priority when two or more cities could claim sufficient nexus to tax a particular transaction. That section was eliminated several years ago when its concepts were incorporated elsewhere in the MCTC, most notably through the addition of subsection 460(e) under Retail.

62-445 – Rental, leasing, and licensing for use of real property

Section III of the ordinance adds new subsection 445(t) to incorporate a legislative preemption, A.R.S. §42-6004(A)(12). This preemption allows an exemption from the tax when both the

Landlord Corporation and the Tenant Corporation are owned by the same shareholders in a third party entity, regardless of which type of legal entity the third party owner is. This allows an individual or LLC to own both the Landlord Corporation and the Tenant Corporation and have the rents paid between the entities be exempt from the tax. Note that subsection (s) is almost identical to this exemption, except that the third party owner must also be a Corporation. This change does not allow an exemption if either the Landlord or the Tenant are an LLC, because an LLC is a form of partnership rather than a corporation. Also in this section of the ordinance, we are clarifying subsection (s) by adding the phrase “is exempt”.

62-415.3 – Construction contracting; tax rate effective date

Section IV of the ordinance replaces a portion of the existing language with the correct final wording that was actually approved and adopted by the Municipal Tax Code Commission. This is merely an aesthetic change being made to conform to the official version of the Model Code. This alteration has no effect on the substance of the Regulation or its implementation.

**FINANCIAL IMPLICATIONS:** There are no financial impacts related to the technical corrections in Sections I, II, and IV of the ordinance. The impact of Section III related to the new exemption for commercial leases between related corporations is deemed negligible because the number of qualifying entities is very limited.

**PROPOSED MOTION:** Move to introduce and tentatively approve Ordinance No. 4376 of the City Council of the City of Chandler, Arizona, amending Sections 62-410, 62-422, and 62-445 of Chapter 62, Code of the City of Chandler, and establishing the effective dates thereof, relating to conforming changes to the Chandler Tax Code.

cc: Pat McDermott, Assistant City Manager

ORDINANCE NO. 4376

AN ORDINANCE OF THE CITY COUNCIL OF THE CITY OF CHANDLER, ARIZONA, AMENDING SECTIONS 62-410, 62-422, AND 62-445 AND REGULATION 62-415.3 OF CHAPTER 62, CODE OF THE CITY OF CHANDLER, AND ESTABLISHING THE EFFECTIVE DATES THEREOF, RELATING TO CONFORMING CHANGES TO THE CHANDLER TAX CODE.

BE IT ORDAINED by the City Council of the City of Chandler, Arizona, that the Code of the City of Chandler is hereby amended as follows:

SECTION I: That Section 62-410 of Chapter 62, Code of the City of Chandler is hereby amended as follows:

**62-410. Amusements, exhibitions, and similar activities.**

(a) The tax rate shall be at an amount equal to one and one-half (~~1.5~~) percent (1.5%) of the gross income from the business activity upon every person engaging or continuing in THE BUSINESS OF PROVIDING AMUSEMENT THAT BEGINS IN THE CITY OR TAKES PLACE ENTIRELY WITHIN THE CITY, WHICH INCLUDES the following type or nature of businesses:

(1) Operating or conducting theaters, movies, operas, shows of any type or nature, exhibitions, concerts, carnivals, circuses, amusement parks, menageries, fairs, races, contests, games, billiard or pool parlors, bowling alleys, skating rinks, tennis courts, golf courses, video games, pinball machines, public dances, dance\_halls, sports events, jukeboxes, batting and driving ranges, animal rides, or any other business charging admission for exhibition, amusement, or entertainment.

(2) Health spas, fitness centers, dance studios, or other persons who charge for the use of premises for sports, athletic, other health-related activities; or instruction, whether on a per-event use, or for long-term usage, such as membership fees.

(b) Deductions or exemptions. The gross proceeds of sales or gross income derived from the following sources is exempt from the tax imposed by this Section:

(1) (Reserved).

(2) Amounts retained by the Arizona Exposition and State Fair Board from ride ticket sales at the annual Arizona State Fair.

(3) Income received from a hotel business subject to tax under section 62-444, if all of the following apply:

(A) The hotel business receives gross income from a customer for the specific business activity otherwise subject to amusement tax.

(B) The consideration received by the hotel business is equal to or greater than the amount to be deducted under this subsection.

(C) The hotel business has provided an exemption certificate to the person engaging in business under this Section.

(4) Income that is specifically included as the gross income of a business activity upon which another ~~section~~ Section of this ~~article~~ Article imposes a tax, that is separately stated to the customer and is taxable to the person engaged in that classification not to exceed consideration paid to the person conducting the activity.

(5) Income from arranging transportation connected to amusement activity that is separately stated to the customer, not to exceed consideration paid to the transportation business.

(c) The tax imposed by this Section shall not include arranging an amusement activity as a service to a person's customers if that person is not otherwise engaged in the business of operating or conducting an amusement themselves or through others. This exception does not apply to businesses that operate or conduct amusements pursuant to customer orders and send the billings and receive the payments associated with that activity, including when the amusement is performed by third party independent contractors. For the purposes of this paragraph, "arranging" includes billing for or collecting amusement charges from a person's customers on behalf of the persons providing the amusement.

SECTION II: That Section 62-422 of Chapter 62, Code of the City of Chandler is hereby amended as follows:

**62-422. Jet fuel sales.**

(a) The tax rate shall be at an amount of ~~\$.023~~ 2.3 cents (\$0.023) per gallon sold from the business activity upon every person engaging or continuing in the business of selling jet fuel.

(1) Gallons sold includes all gallons sold, bartered, exchanged, included as part or whole of a trade-out, or similar transactions regardless of the type or form of payment.

(2) For purposes of this Section the following terms are substitutable in Articles III and V of this ~~chapter~~ Chapter, and corresponding regulations:

(A) "gallons" for "gross income"

(B) "gallon(s)" for "amount(s)."

(b) The burden of proving that a sale of jet fuel is not a taxable sale shall be upon the person who made the sale.

(c) ~~Except as provided in Section 567, when~~ When this ~~City-city~~ and another Arizona ~~City-city~~ or ~~Town-town~~ with an equivalent excise tax could claim nexus for taxing a jet fuel sale, the ~~City-city~~ or ~~Town-town~~ where the permanent business location of the seller at which the order was received shall be deemed to have precedence, and for the purposes of this ~~chapter-Chapter~~ such ~~City-city~~ or ~~Town-town~~ has sole and exclusive right to such tax.

(d) The appropriate tax liability for any jet fuel sale where the order is received at a permanent business location of the seller located in this ~~City-city~~ or in any Arizona ~~City-city~~ or ~~of-town~~ that levies an equivalent excise tax shall be at the rate of the ~~City-city~~ or town of such seller's location.

(e) Exemptions. Notwithstanding Section 62-400(d), the exemptions in Section 62-465(a), (b) and (d) through (z) will apply to sales of jet fuel taxed under this Section.

SECTION III: That Section 62-445 of Chapter 62, Code of the City of Chandler is hereby amended as follows:

**62-445. Rental, leasing, and licensing for use of real property.**

(a) The tax rate shall be at an amount equal to one and one-half ~~(1.5)~~-percent (1.5%) of the gross income from the business activity upon every person engaging or continuing in the business of leasing or renting real property located within the City for a consideration, to the tenant in actual possession, or the licensing for use of real property to the final licensee located within the City for a consideration including any improvements, rights, or interest in such property; provided further that:

(1) Payments made by the lessee to, or on behalf of, the lessor for property taxes, repairs, or improvements are considered to be part of the taxable gross income.

(2) Charges for such items as telecommunications, utilities, pet fees, or maintenance are considered to be part of the taxable gross income.

(3) However, if the lessor engages in telecommunication activity, as evidenced by installing individual metering equipment and by billing each tenant based upon actual usage, such activity is taxable under Section 62-470.

(b) If individual utility meters have been installed for each tenant and the lessor separately charges each single tenant for the exact billing from the utility company, such charges are exempt.

(c) Charges by a qualifying hospital, qualifying community health center or a qualifying health care organization to patients of such facilities for use of rooms or other real property during the course of their treatment by such facilities are exempt.

(d) Charges for joint pole usage by a person engaged in the business of providing or furnishing utility or telecommunication services to another person engaged in the business of providing or

furnishing utility or telecommunication services are exempt from the tax imposed by this Section.

(e) (Reserved).

(f) (Reserved).

(g) (Reserved).

(h) (Reserved).

(i) (Reserved).

(j) Exempt from the tax imposed by this Section is gross income derived from the activities taxable under Section 62-444 of this Code.

(k) (Reserved).

(l) (Reserved).

(m) (Reserved).

(n) Notwithstanding the provisions of Section 62-200(b), the fair market value of one (1) apartment, in an apartment complex provided rent free to an employee of the apartment complex is not subject to the tax imposed by this Section. For an apartment complex with more than fifty (50) units, an additional apartment provided rent free to an employee for every additional fifty (50) units is not subject to the tax imposed by this Section.

(o) Income derived from incarcerating or detaining prisoners who are under the jurisdiction of the United States, this State or any other state or a political subdivision of this State or of any other state in a privately operated prison, jail or detention facility is exempt from the tax imposed by this Section.

(p) Charges by any hospital, any licensed nursing care institution, or any kidney dialysis facility to patients of such facilities for the use of rooms or other real property during the course of their treatment by such facilities are exempt.

(q) Charges to patients receiving "personal care" or "directed care", by any licensed assisted living facility, licensed assisted living center or licensed assisted living home as defined and licensed pursuant to Chapter 4 Title 36 Arizona Revised Statutes and Title 9 of the Arizona Administrative Code are exempt.

(r) Income received from the rental of any "low-income unit" as established under Section 42 of the Internal Revenue Code, including the low-income housing credit provided by IRC Section 42, to the extent that the collection of tax on rental income causes the "gross rent" defined by IRC Section 42 to exceed the income limitation for the low-income unit is exempt. This exemption also applies to income received from the rental of individual rental units subject to statutory or regulatory "low-income unit" rent restrictions similar to IRC Section 42 to the extent that the collection of tax from the tenant causes the rental receipts to exceed a rent restriction for

the low-income unit. This subsection also applies to rent received by a person other than the owner or lessor of the low-income unit, including a broker. This subsection does not apply unless a taxpayer maintains the documentation to support the qualification of a unit as a low-income unit, the "gross rent" limitation for the unit and the rent received from that unit.

(s) The gross proceeds of sales or gross income derived from a commercial lease in which a reciprocal insurer or a corporation leases real property to an affiliated corporation IS EXEMPT. For the purposes of this paragraph:

(1) "*Affiliated corporation*" means a corporation that meets one (1) of the following conditions:

(A) The corporation owns or controls at least eighty (80) percent of the lessor.

(B) The corporation is at least eighty (80) percent owned or controlled by the lessor.

(C) The corporation is at least eighty (80) percent owned or controlled by a corporation that also owns or controls at least eighty (80) percent of the lessor.

(D) The corporation is at least eighty (80) percent owned or controlled by a corporation that is at least eighty (80) percent owned or controlled by a reciprocal insurer.

(2) For the purposes of subsection (1), ownership and control are determined by reference to the voting shares of a corporation.

(3) "*Reciprocal insurer*" has the same meaning as prescribed in A.R.S. Section 20-762.

(T) THE GROSS PROCEEDS OF SALES OR GROSS INCOME DERIVED FROM A COMMERCIAL LEASE IN WHICH A CORPORATION LEASES REAL PROPERTY TO A CORPORATION OF WHICH AT LEAST EIGHTY PER CENT OF THE VOTING SHARES OF EACH CORPORATION ARE OWNED BY THE SAME SHAREHOLDERS IS EXEMPT.

SECTION IV: That Regulation 62-415.3 of Chapter 62, Code of the City of Chandler is hereby amended as follows:

**Reg. 62-415.3. Construction contracting; tax rate effective date.**

(a) In the event of a tax rate change, the rate imposed on gross income from construction contracting shall be computed based upon the rate in effect when the contract was executed, subject to the "enactment date" as defined in this section. Gross income from a contract executed prior to the enactment date shall not be subject to the tax rate change, provided the contract contains no provision that entitles the contractor to recover the amount of a ~~THE~~ tax increase from a purchaser.

(b) IN THE EVENT OF A RATE INCREASE, ~~IN~~ IN order to qualify for a lower rate, the CONSTRUCTION contractor shall, upon request, provide sufficient documentation, in a manner and form prescribed by the ~~tax~~ Tax collector/Collector, to verify that a contract was ~~executed~~ ENTERED INTO before the enactment date.

(c) ~~For purposes of this section, "enactment date" shall be: the date of election or date of final adoption by the mayor and council, whichever is earlier.~~

(1) IN THE EVENT AN ELECTION IS HELD, THE DATE OF THE ELECTION.

(2) IN THE EVENT NO ELECTION IS HELD, THE DATE OF FINAL ADOPTION BY THE MAYOR AND COUNCIL.

(3) NOTWITHSTANDING THE ABOVE, NOTHING IN THIS SECTION SHALL BE CONSTRUED TO PREVENT THE CITY FROM ESTABLISHING A LATER ENACTMENT DATE.

SECTION V: The provisions of this ordinance shall be effective from and after July 20, 2011.

INTRODUCED AND TENTATIVELY APPROVED by the City Council of the City of Chandler, Arizona, this 13<sup>th</sup> day of December, 2012.

ATTEST:

\_\_\_\_\_  
CITY CLERK

\_\_\_\_\_  
MAYOR

PASSED AND ADOPTED by the Mayor and Council of the City of Chandler, Arizona, this 10<sup>th</sup> day of January, 2013.

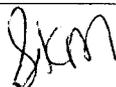
ATTEST:

\_\_\_\_\_  
CITY CLERK

\_\_\_\_\_  
MAYOR

Approved As To Form:

\_\_\_\_\_  
CITY ATTORNEY



**CERTIFICATION**

I HEREBY CERTIFY that the above and foregoing Ordinance No. 4376 was duly passed and adopted by the City Council of the City of Chandler, Arizona, at a regular meeting held on the 10<sup>th</sup> day of January, 2013, and that a quorum was present thereat.

\_\_\_\_\_  
CITY CLERK

Published: