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JANICE K. BREWER
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CHAPTER 196

SENATE BILL 1389

AN ACT

AMENDING SECTIONS 42-1001, 42-1106, 43-105, 43-1021, 43-1022, 43-1121 AND 43-1122, ARIZONA REVISED STATUTES; RELATING TO TAXATION.

(TEXT OF BILL BEGINS ON NEXT PAGE)

Be it enacted by the Legislature of the State of Arizona:

Section 1. Section 42-1001, Arizona Revised Statutes, is amended to read:

42-1001. Definitions

In this title, unless the context otherwise requires:

1. "Board" or "state board" means either the state board of tax appeals or the state board of equalization, as applicable.

2. "Court" means the tax court or superior court, whichever is applicable.

3. "Department" means the department of revenue.

4. "Director" means the director of the department.

5. "Internal revenue code" means the United States internal revenue code of 1986, as amended and in effect as of January 1, ~~2003~~ 2004, including those provisions that became effective during ~~2002~~ 2003 with the specific adoption of their retroactive effective dates but excluding all changes to the code enacted after January 1, ~~2003~~ 2004.

Sec. 2. Section 42-1106, Arizona Revised Statutes, is amended to read:

42-1106. Time limitations for credit and refund claims

A. The period within which a claim for credit or refund may be filed, or credit or refund may be allowed or made if no claim is filed, is the period within which the department may make an assessment under section 42-1104.

B. If the total amount withheld under section 43-401 exceeds the amount of the tax on the employee's entire taxable income as computed under title 43, no refund, credit or offset may be made to the employee unless the employee files a return, in respect of which the tax withheld might be credited, within four years from the due date of the original return.

C. IF A REFUND OR CREDIT OF ANY OVERPAYMENT OF TAX RESULTING FROM THE AMENDMENTS MADE TO SECTION 121(d)(9) OF THE INTERNAL REVENUE CODE BY THE MILITARY FAMILY TAX RELIEF ACT OF 2003 (P.L. 108-121) IS PREVENTED BY THE OPERATION OF ANY LAW OR RULE OF LAW, INCLUDING RES JUDICATA, AT ANY TIME BEFORE THE CLOSE OF THE ONE YEAR PERIOD BEGINNING ON NOVEMBER 11, 2003, THE REFUND OR CREDIT MAY NEVERTHELESS BE MADE OR ALLOWED IF THE CLAIM IS FILED BEFORE THE CLOSE OF THIS PERIOD.

~~C.~~ D. The failure to begin an action for refund or credit within the time specified in this section is a bar against the recovery of taxes by the taxpayer.

Sec. 3. Section 43-105, Arizona Revised Statutes, is amended to read:

43-105. Internal revenue code; definition; application

A. FOR PURPOSES OF COMPUTING INCOME TAX PURSUANT TO THIS TITLE, FOR TAXABLE YEARS BEGINNING FROM AND AFTER DECEMBER 31, 2003 THROUGH DECEMBER 31, 2004, "INTERNAL REVENUE CODE" MEANS THE UNITED STATES INTERNAL REVENUE CODE OF 1986, AS AMENDED, IN EFFECT ON JANUARY 1, 2004, INCLUDING THOSE PROVISIONS THAT BECAME EFFECTIVE DURING 2003 WITH THE SPECIFIC ADOPTION OF ALL FEDERAL

RETROACTIVE EFFECTIVE DATES, BUT EXCLUDING ANY CHANGE TO THE CODE ENACTED AFTER JANUARY 1, 2004.

~~A.~~ B. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 2002 through December 31, 2003, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 2003, including those provisions that became effective during 2002 with the specific adoption of all federal retroactive effective dates~~, but excluding any change to the code enacted after January 1, 2003~~ AND INCLUDING THOSE PROVISIONS OF THE JOBS AND GROWTH TAX RELIEF RECONCILIATION ACT OF 2003 (P.L. 108-27), THE MILITARY FAMILY TAX RELIEF ACT OF 2003 (P.L. 108-121) AND THE MEDICARE PRESCRIPTION DRUG, IMPROVEMENT, AND MODERNIZATION ACT OF 2003 (P.L. 108-173) THAT ARE RETROACTIVELY EFFECTIVE DURING TAXABLE YEARS BEGINNING FROM AND AFTER DECEMBER 31, 2002 THROUGH DECEMBER 31, 2003.

~~B.~~ C. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 2001 through December 31, 2002, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on March 9, 2002, including those provisions that became effective during 2001 with the specific adoption of all federal retroactive effective dates~~, but excluding any change to the code enacted after March 9, 2002~~ AND INCLUDING THOSE PROVISIONS OF THE JOBS AND GROWTH TAX RELIEF RECONCILIATION ACT OF 2003 (P.L. 108-27) AND THE MILITARY FAMILY TAX RELIEF ACT OF 2003 (P.L. 108-121) THAT ARE RETROACTIVELY EFFECTIVE DURING TAXABLE YEARS BEGINNING FROM AND AFTER DECEMBER 31, 2001 THROUGH DECEMBER 31, 2002.

~~C.~~ D. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 2000 through December 31, 2001, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 2001, including those provisions that became effective during 2000 with the specific adoption of all federal retroactive effective dates and including those provisions of the economic growth and tax relief reconciliation act of 2001 (P.L. 107-16), ~~and~~ the job creation and worker assistance act of 2002 (P.L. 107-147) AND THE MILITARY FAMILY TAX RELIEF ACT OF 2003 (P.L. 108-121) that are retroactively effective during taxable years beginning from and after December 31, 2000 through December 31, 2001.

~~D.~~ E. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 1999 through December 31, 2000, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 2000, including those provisions that became effective during 1999 with the specific adoption of all federal retroactive effective dates and including those provisions of the community renewal tax relief act of 2000 (P.L. 106-554), the installment tax correction act of 2000 (P.L. 106-573), FSC repeal and extraterritorial income exclusion act of 2000 (P.L. 106-519), the trade and development act of 2000

(P.L. 106-200), the economic growth and tax relief reconciliation act of 2001 (P.L. 107-16), ~~and~~ the job creation and worker assistance act of 2002 (P.L. 107-147) AND THE MILITARY FAMILY TAX RELIEF ACT OF 2003 (P.L. 108-121) that are retroactively effective during taxable years beginning from and after December 31, 1999 through December 31, 2000.

~~E.~~ F. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 1998 through December 31, 1999, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 1999, including those provisions that became effective during 1998 with the specific adoption of all federal retroactive effective dates and including those provisions of the miscellaneous trade and technical corrections act of 1999 (P.L. 106-36), the ticket to work and work incentives improvement act of 1999 (P.L. 106-170), the community renewal tax relief act of 2000 (P.L. 106-554), ~~and~~ the installment tax correction act of 2000 (P.L. 106-573) AND THE MILITARY FAMILY TAX RELIEF ACT OF 2003 (P.L. 108-121) that are retroactively effective during taxable years beginning from and after December 31, 1998 through December 31, 1999.

~~F.~~ G. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 1997 through December 31, 1998, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 1998, including those provisions that became effective during 1997 with the specific adoption of all federal retroactive effective dates and including those provisions of the IRS restructuring and reform act of 1998 (P.L. 105-206), the tax and trade relief extension act of 1998 (P.L. 105-277), the surface transportation revenue act of 1998 (P.L. 105-178), ~~and~~ the miscellaneous trade and technical corrections act of 1999 (P.L. 106-36) AND THE MILITARY FAMILY TAX RELIEF ACT OF 2003 (P.L. 108-121) that are retroactively effective during the taxable years beginning from and after December 31, 1997 through December 31, 1998.

~~G.~~ H. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 1996 through December 31, 1997, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 1997, including those provisions that became effective during 1996 with the specific adoption of all federal retroactive effective dates and including the provisions of the taxpayer relief act of 1997 (P.L. 105-34), the IRS restructuring and reform act of 1998 (P.L. 105-206), ~~and~~ the tax and trade relief extension act of 1998 (P.L. 105-277) AND THE MILITARY FAMILY TAX RELIEF ACT OF 2003 (P.L. 108-121) that are retroactively effective during taxable years beginning from and after December 31, 1996 through December 31, 1997.

~~H.~~ I. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 1995 through December 31, 1996, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 1996, including those

provisions that became effective during 1995 with the specific adoption of their retroactive effective date and including those provisions of the small business job protection act of 1996 (P.L. 104-188; 110 Stat. 1755), the health insurance portability and accountability act of 1996 (P.L. 104-191; 110 Stat. 1936), the personal responsibility and work opportunity reconciliation act of 1996 (P.L. 104-193; 110 Stat. 2105), the taxpayer relief act of 1997 (P.L. 105-34), the IRS restructuring and reform act of 1998 (P.L. 105-206) and the tax and trade relief extension act of 1998 (P.L. 105-277) that are retroactively effective during taxable years beginning from and after December 31, 1995 through December 31, 1996.

~~I.~~ J. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 1994 through December 31, 1995, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 1995, including those provisions that became effective during 1994 with the specific adoption of their retroactive effective date and including those provisions of the small business job protection act of 1996 (P.L. 104-188; 110 Stat. 1755), the health insurance portability and accountability act of 1996 (P.L. 104-191; 110 Stat. 1936), the personal responsibility and work opportunity reconciliation act of 1996 (P.L. 104-193; 110 Stat. 2105), the taxpayer relief act of 1997 (P.L. 105-34), the IRS restructuring and reform act of 1998 (P.L. 105-206) and the tax and trade relief extension act of 1998 (P.L. 105-277) that are retroactively effective during taxable years beginning from and after December 31, 1994 through December 31, 1995.

~~J.~~ K. For purposes of computing income tax pursuant to this title, for taxable years beginning from and after December 31, 1993 through December 31, 1994, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 1994, including those provisions that became effective during 1993 with the specific adoption of their retroactive effective date and including those provisions of the small business job protection act of 1996 (P.L. 104-188; 110 Stat. 1755), the health insurance portability and accountability act of 1996 (P.L. 104-191; 110 Stat. 1936), the personal responsibility and work opportunity reconciliation act of 1996 (P.L. 104-193; 110 Stat. 2105), the taxpayer relief act of 1997 (P.L. 105-34), the IRS restructuring and reform act of 1998 (P.L. 105-206) and the tax and trade relief extension act of 1998 (P.L. 105-277) that are retroactively effective during taxable years beginning from and after December 31, 1993 through December 31, 1994.

~~K. Except as provided in section 43-106, for purposes of computing income tax pursuant to this title for taxable years beginning from and after December 31, 1992 through December 31, 1993, "internal revenue code" means the United States internal revenue code of 1986, as amended, in effect on January 1, 1993, including those provisions that became effective during 1992 with the specific adoption of their retroactive effective date and including those provisions of the small business job protection act of 1996 (P.L.~~

~~104-188; 110 Stat. 1755), the health insurance portability and accountability act of 1996 (P.L. 104-191; 110 Stat. 1936), the personal responsibility and work opportunity reconciliation act of 1996 (P.L. 104-193; 110 Stat. 2105), the taxpayer relief act of 1997 (P.L. 105-34), the IRS restructuring and reform act of 1998 (P.L. 105-206) and the tax and trade relief extension act of 1998 (P.L. 105-277) that are retroactively effective during taxable years beginning from and after December 31, 1992 through December 31, 1993.~~

Sec. 4. Section 43-1021, Arizona Revised Statutes, is amended to read:

43-1021. Additions to Arizona gross income

In computing Arizona adjusted gross income, the following amounts shall be added to Arizona gross income:

1. A beneficiary's share of the fiduciary adjustment to the extent that the amount determined by section 43-1333 increases the beneficiary's Arizona gross income.

2. An amount equal to the "ordinary income portion" of a lump sum distribution that was excluded from federal adjusted gross income pursuant to section 402(d) of the internal revenue code.

3. The amount of interest income received on obligations of any state, territory or possession of the United States, or any political subdivision thereof, located outside the state of Arizona, reduced, for tax years beginning from and after December 31, 1996, by the amount of any interest on indebtedness and other related expenses that were incurred or continued to purchase or carry those obligations and that are not otherwise deducted or subtracted in arriving at Arizona gross income.

4. Annuity income received during the taxable year to the extent that the sum of the proceeds received from such annuity in all taxable years prior to and including the current taxable year exceeds the total consideration and premiums paid by the taxpayer. This paragraph applies only to those annuities with respect to which the first payment was received prior to December 31, 1978.

5. The excess of a partner's share of partnership taxable income required to be included under chapter 14, article 2 of this title over the income required to be reported under section 702(a)(8) of the internal revenue code.

6. The excess of a partner's share of partnership losses determined pursuant to section 702(a)(8) of the internal revenue code over the losses allowable under chapter 14, article 2 of this title.

7. The amount by which the adjusted basis of property described in this paragraph and computed pursuant to the internal revenue code exceeds the adjusted basis of such property computed pursuant to this title and the income tax act of 1954, as amended. This paragraph shall apply to all property which is held for the production of income and which is sold or otherwise disposed of during the taxable year, except depreciable property used in a trade or business.

8. The amount of depreciation or amortization of costs of any capital investment that is deducted pursuant to section 167 or 179 of the internal revenue code by a qualified defense contractor with respect to which an election is made to amortize pursuant to section 43-1024.

9. The amount of gain from the sale or other disposition of a capital investment which a qualified defense contractor has elected to amortize pursuant to section 43-1024.

10. The amount of depreciation or amortization of costs of child care facilities deducted pursuant to section 167 or 188 of the internal revenue code for which a credit is taken under section 43-1075, subsection A, paragraph 1.

11. Amounts withdrawn from the Arizona state retirement system, the corrections officer retirement plan, the public safety personnel retirement system, the elected officials' retirement plan or a county or city retirement plan by an employee upon termination of employment before retirement to the extent they were deducted in arriving at Arizona taxable income in any year.

12. That portion of the net operating loss included in federal adjusted gross income which has already been taken as a net operating loss for Arizona purposes or which is separately taken as a subtraction under the special net operating loss transition rule.

13. Any nonitemized amount deducted pursuant to section 170 of the internal revenue code representing contributions to an educational institution which denies admission, enrollment or board and room accommodations on the basis of race, color or ethnic background except those institutions primarily established for the education of American Indians.

14. The amount paid as taxes on property in this state with respect to which a credit is claimed under section 43-1078.

15. Amounts withdrawn from a medical savings account by the individual during the taxable year computed pursuant to section 220(f) of the internal revenue code and not included in federal adjusted gross income.

16. Any amount of agricultural water conservation expenses that were deducted pursuant to the internal revenue code for which a credit is claimed under section 43-1084.

17. The amount by which the depreciation or amortization computed under the internal revenue code with respect to property for which a credit was taken under section 43-1080 exceeds the amount of depreciation or amortization computed pursuant to the internal revenue code on the Arizona adjusted basis of the property.

18. The amount by which the adjusted basis computed under the internal revenue code with respect to property for which a credit was claimed under section 43-1080 and which is sold or otherwise disposed of during the taxable year exceeds the adjusted basis of the property computed under section 43-1080.

19. The amount by which the depreciation or amortization computed under the internal revenue code with respect to property for which a credit was taken under either section 43-1081 or 43-1081.01 exceeds the amount of depreciation or amortization computed pursuant to the internal revenue code on the Arizona adjusted basis of the property.

20. The amount by which the adjusted basis computed under the internal revenue code with respect to property for which a credit was claimed under either section 43-1081 or 43-1081.01 and which is sold or otherwise disposed of during the taxable year exceeds the adjusted basis of the property computed under section 43-1081 or 43-1081.01, as applicable.

21. The deduction referred to in section 1341(a)(4) of the internal revenue code for restoration of a substantial amount held under a claim of right.

22. The amount by which a net operating loss carryover or capital loss carryover allowable pursuant to section 1341(b)(5) of the internal revenue code exceeds the net operating loss carryover or capital loss carryover allowable pursuant to section 43-1029, subsection F.

23. Any amount deducted pursuant to section 170 of the internal revenue code representing contributions to a school tuition organization or a public school for which a credit is claimed under section 43-1089 or 43-1089.01.

24. Any amount deducted in computing Arizona gross income as expenses for installing solar stub outs or electric vehicle recharge outlets in this state with respect to which a credit is claimed pursuant to section 43-1090.

25. Any wage expenses deducted pursuant to the internal revenue code for which a credit is claimed under section 43-1087 and representing net increases in qualified employment positions for employment of temporary assistance for needy families recipients.

26. Any amount deducted for conveying ownership or development rights of property to an agricultural preservation district under section 48-5702 for which a credit is claimed under section 43-1081.02.

27. The amount of any ~~special~~ depreciation allowance allowed pursuant to section ~~168(k)~~ 167(a) of the internal revenue code TO THE EXTENT NOT PREVIOUSLY ADDED.

28. WITH RESPECT TO PROPERTY FOR WHICH AN EXPENSE DEDUCTION WAS TAKEN PURSUANT TO SECTION 179 OF THE INTERNAL REVENUE CODE, THE AMOUNT IN EXCESS OF TWENTY-FIVE THOUSAND DOLLARS.

Sec. 5. Section 43-1022, Arizona Revised Statutes, is amended to read:

43-1022. <u>Subtractions from Arizona gross income</u>

In computing Arizona adjusted gross income, the following amounts shall be subtracted from Arizona gross income:

1. The amount of exemptions allowed by section 43-1023.

2. Benefits, annuities and pensions in an amount totaling not more than two thousand five hundred dollars received from one or more of the following:

(a) The United States government service retirement and disability fund, retired or retainer pay of the uniformed services of the United States, the United States foreign service retirement and disability system and any other retirement system or plan established by federal law.

(b) The Arizona state retirement system, the corrections officer retirement plan, the public safety personnel retirement system, the elected officials' retirement plan, an optional retirement program established by the Arizona board of regents under section 15-1628, an optional retirement program established by a community college district board under section 15-1451 or a retirement plan established for employees of a county, city or town in this state.

3. A beneficiary's share of the fiduciary adjustment to the extent that the amount determined by section 43-1333 decreases the beneficiary's Arizona gross income.

4. The amount of any distributions from an individual retirement account as provided for in section 408 of the internal revenue code or from a qualified retirement plan of a self-employed individual as provided for in section 401 of the internal revenue code to the extent that total adjustments made pursuant to this paragraph in all tax years do not exceed the total of all contributions made by the taxpayer to such plans prior to December 31, 1975, which were included in computing Arizona taxable income.

5. The amount of income on an installment receivable which is recognized pursuant to the internal revenue code and which has already been recognized on the death of the taxpayer for purposes of this title for tax years ending before January 1, 1990.

6. Interest income received on obligations of the United States, less any interest on indebtedness, or other related expenses, and deducted in arriving at Arizona gross income, which were incurred or continued to purchase or carry such obligations.

7. The amount of any income tax refunds which were received from states other than Arizona and which were included as income in computing federal adjusted gross income.

8. Annuity income included in federal adjusted gross income pursuant to section 72 of the internal revenue code if the first payment with respect to such annuity was received prior to December 31, 1978.

9. The excess of a partner's share of income required to be included under section 702(a)(8) of the internal revenue code over the income required to be included under chapter 14, article 2 of this title.

10. The excess of a partner's share of partnership losses determined pursuant to chapter 14, article 2 of this title over the losses allowable under section 702(a)(8) of the internal revenue code.

11. The amount by which the adjusted basis of property described in this paragraph and computed pursuant to this title and the income tax act of 1954, as amended, exceeds the adjusted basis of such property computed pursuant to the internal revenue code. This paragraph shall apply to all

property which is held for the production of income and which is sold or otherwise disposed of during the taxable year other than depreciable property used in a trade or business.

12. The amount allowed by section 43-1024 for amortization, by a qualified defense contractor certified by the department of commerce under section 41-1508, of a capital investment for private commercial activities.

13. The amount of gain included in federal adjusted gross income on the sale or other disposition of a capital investment that a qualified defense contractor has elected to amortize pursuant to section 43-1024.

14. The amount allowed by section 43-1025 for contributions during the taxable year of agricultural crops to charitable organizations.

15. The portion of any wages or salaries paid or incurred by the taxpayer for the taxable year that is equal to the amount of the federal work opportunity credit, the empowerment zone employment credit, the credit for employer paid social security taxes on employee cash tips and the Indian employment credit that the taxpayer received under sections 45A, 45B, 51(a) and 1396 of the internal revenue code.

16. The amount of prizes or winnings less than five thousand dollars in a single taxable year from any of the state lotteries established and operated pursuant to title 5, chapter 5, article 1, except that all such winnings before March 22, 1983, including periodic distributions from such winnings made after March 22, 1983, may be subtracted.

17. The amount of exploration expenses that is determined pursuant to section 617 of the internal revenue code, that has been deferred in a taxable year ending before January 1, 1990 and for which a subtraction has not previously been made. The subtraction shall be made on a ratable basis as the units of produced ores or minerals discovered or explored as a result of this exploration are sold.

18. The amount included in federal adjusted gross income pursuant to section 86 of the internal revenue code, relating to taxation of social security and railroad retirement benefits.

19. To the extent not already excluded from Arizona gross income under section 112 of the internal revenue code, compensation received for active service as a member of the armed forces of the United States for any month during any part of which the member served in a combat zone as determined under section 112 of the internal revenue code or in an area given the same treatment as a combat zone for purposes of section 112 of the internal revenue code.

20. The amount of unreimbursed medical and hospital costs, adoption counseling, legal and agency fees and other nonrecurring costs of adoption not to exceed three thousand dollars. In the case of a husband and wife who file separate returns, the subtraction may be taken by either taxpayer or may be divided between them, but the total subtractions allowed both husband and wife shall not exceed three thousand dollars. The subtraction under this paragraph may be taken for the costs that are described in this paragraph and

that are incurred in prior years, but the subtraction may be taken only in the year during which the final adoption order is granted.

21. The amount authorized by section 43-1027 for the taxable year relating to qualified wood stoves, wood fireplaces or gas fired fireplaces.

22. With respect to a medical savings account established pursuant to section 43-1028:

(a) An eligible individual may subtract:

(i) The amount of contributions made by the individual's employer during the taxable year to the individual's medical savings account pursuant to section 43-1028 to the extent that the employer contributions are included in the individual's federal adjusted gross income.

(ii) The amount deposited by the individual in the account during the taxable year to the extent that the individual's contributions are included in the individual's federal adjusted gross income.

(b) The individual's employer may subtract the amount of contributions made by the employer to a medical savings account established on the individual's behalf to the extent that the contributions are not deductible under the internal revenue code.

23. The amount by which a net operating loss carryover or capital loss carryover allowable pursuant to section 43-1029, subsection F exceeds the net operating loss carryover or capital loss carryover allowable pursuant to section 1341(b)(5) of the internal revenue code.

24. Any amount of qualified educational expenses that is distributed from a qualified state tuition program determined pursuant to section 529 of the internal revenue code and that is included in income in computing federal adjusted gross income.

25. Any item of income resulting from an installment sale that has been properly subjected to income tax in another state in a previous taxable year and that is included in Arizona gross income in the current taxable year.

26. The amount authorized by section 43-1030 relating to holocaust survivors.

27. The amount authorized by section 43-1031 for constructing an energy efficient residence.

28. ~~With respect to property for which the depreciation allowance pursuant to section 168(k) of the internal revenue code was added under section 43-1021, paragraph 27,~~ An amount equal to ~~three-sevenths of~~ the ~~amount of~~ depreciation ~~allowed~~ ALLOWABLE pursuant to section 167(a) of the internal revenue code ~~as~~ FOR THE TAXABLE YEAR computed ~~on the adjusted basis provided pursuant to section 168(k)(1)(B) of the internal revenue code~~ AS IF THE ELECTION DESCRIBED IN SECTION 168(k)(2)(C)(iii) OF THE INTERNAL REVENUE CODE HAD BEEN MADE FOR EACH APPLICABLE CLASS OF PROPERTY IN THE YEAR THE PROPERTY WAS PLACED IN SERVICE.

29. With respect to property that is sold or otherwise disposed of during the taxable year by a taxpayer that complied with section 43-1021, paragraph 27 with respect to that property, the amount of depreciation that

~~would have~~ HAS been allowed pursuant to section 167(a) of the internal revenue code ~~computed without regard to section 168(k) of the internal revenue code~~ to the extent that the amount has not already reduced Arizona taxable income in the current or prior taxable years.

30. WITH RESPECT TO PROPERTY FOR WHICH AN ADJUSTMENT WAS MADE UNDER SECTION 43-1021, PARAGRAPH 28, AN AMOUNT EQUAL TO ONE-FIFTH OF THE AMOUNT OF THE ADJUSTMENT PURSUANT TO SECTION 43-1021, PARAGRAPH 28 IN THE YEAR IN WHICH THE AMOUNT WAS ADJUSTED UNDER SECTION 43-1021, PARAGRAPH 28 AND IN EACH OF THE FOLLOWING FOUR YEARS.

Sec. 6. Section 43-1121, Arizona Revised Statutes, is amended to read:

43-1121. Additions to Arizona gross income; corporations

In computing Arizona taxable income for a corporation, the following amounts shall be added to Arizona gross income:

1. The amounts computed pursuant to section 43-1021, paragraphs 3 through 9, 13, ~~and~~ 27 AND 28.

2. The amount of dividend income received from corporations and allowed as a deduction pursuant to sections 243, 244 and 245 of the internal revenue code.

3. Taxes which are based on income paid to states, local governments or foreign governments and which were deducted in computing federal taxable income.

4. Expenses and interest relating to tax-exempt income on indebtedness incurred or continued to purchase or carry obligations the interest on which is wholly exempt from the tax imposed by this title. Financial institutions, as defined in section 6-101, shall be governed by section 43-961, paragraph 2.

5. Commissions, rentals and other amounts paid or accrued to a domestic international sales corporation controlled by the payor corporation if the domestic international sales corporation is not required to report its taxable income to this state because its income is not derived from or attributable to sources within this state. If the domestic international sales corporation is subject to article 4 of this chapter, the department shall prescribe by rule the method of determining the portion of the commissions, rentals and other amounts which are paid or accrued to the controlled domestic international sales corporation and which shall be deducted by the payor. "Control" for purposes of this paragraph means direct or indirect ownership or control of fifty per cent or more of the voting stock of the domestic international sales corporation by the payor corporation.

6. Federal income tax refunds received during the taxable year to the extent they were deducted in arriving at Arizona taxable income in a previous year.

7. The amount of net operating loss taken pursuant to section 172 of the internal revenue code.

8. The amount of exploration expenses determined pursuant to section 617 of the internal revenue code to the extent that they exceed seventy-five thousand dollars and to the extent that the election is made to defer those expenses not in excess of seventy-five thousand dollars.

9. Amortization of costs incurred to install pollution control devices and deducted pursuant to the internal revenue code or the amount of deduction for depreciation taken pursuant to the internal revenue code on pollution control devices for which an election is made pursuant to section 43-1129.

10. The amount of depreciation or amortization of costs of child care facilities deducted pursuant to section 167 or 188 of the internal revenue code for which an election is made to amortize pursuant to section 43-1130.

11. Arizona state income tax refunds received, to the extent the amount of the refunds is not already included in Arizona gross income, if a tax benefit was derived by deduction of this amount in a prior year.

12. The amount paid as taxes on property in this state by a qualified defense contractor with respect to which a credit is claimed under section 43-1166.

13. The loss of an insurance company that is exempt under section 43-1201 to the extent that it is included in computing Arizona gross income on a consolidated return pursuant to section 43-947.

14. The amount by which the depreciation or amortization computed under the internal revenue code with respect to property for which a credit was taken under section 43-1169 exceeds the amount of depreciation or amortization computed pursuant to the internal revenue code on the Arizona adjusted basis of the property.

15. The amount by which the adjusted basis computed under the internal revenue code with respect to property for which a credit was claimed under section 43-1169 and which is sold or otherwise disposed of during the taxable year exceeds the adjusted basis of the property computed under section 43-1169.

16. The amount by which the depreciation or amortization computed under the internal revenue code with respect to property for which a credit was taken under either section 43-1170 or 43-1170.01 exceeds the amount of depreciation or amortization computed pursuant to the internal revenue code on the Arizona adjusted basis of the property.

17. The amount by which the adjusted basis computed under the internal revenue code with respect to property for which a credit was claimed under either section 43-1170 or 43-1170.01 and which is sold or otherwise disposed of during the taxable year exceeds the adjusted basis of the property computed under section 43-1170 or 43-1170.01, as applicable.

18. The deduction referred to in section 1341(a)(4) of the internal revenue code for restoration of a substantial amount held under a claim of right.

19. The amount by which a capital loss carryover allowable pursuant to section 1341(b)(5) of the internal revenue code exceeds the capital loss carryover allowable pursuant to section 43-1130.01, subsection F.

20. Any amount deducted in computing Arizona taxable income as expenses for installing solar stub outs or electric vehicle recharge outlets in this state with respect to which a credit is claimed pursuant to section 43-1176.

21. Any wage expenses deducted pursuant to the internal revenue code for which a credit is claimed under section 43-1175 and representing net increases in qualified employment positions for employment of temporary assistance for needy families recipients.

22. Any amount of expenses that were deducted pursuant to the internal revenue code and for which a credit is claimed under section 43-1178.

23. Any amount deducted for conveying ownership or development rights of property to an agricultural preservation district under section 48-5702 for which a credit is claimed under section 43-1180.

24. The amount of any deduction that is claimed in computing Arizona gross income and that represents a donation of a school site for which a credit is claimed under section 43-1181.

Sec. 7. Section 43-1122, Arizona Revised Statutes, is amended to read:

43-1122. Subtractions from Arizona gross income; corporations

In computing Arizona taxable income for a corporation, the following amounts shall be subtracted from Arizona gross income:

1. The amounts computed pursuant to section 43-1022, paragraphs 8 through 15, 28, ~~and~~ 29 AND 30. For purposes of this paragraph "federal adjusted gross income" as used in section 43-1022 means "federal taxable income".

2. The amount of Arizona capital loss carryover as defined in section 43-1124 in an amount not to exceed one thousand dollars.

3. With respect to a financial institution as defined in section 6-101, expenses and interest relating to tax-exempt income disallowed pursuant to section 265 of the internal revenue code.

4. Dividends received from another corporation owned or controlled directly or indirectly by a recipient corporation. "Control" for purposes of this paragraph means direct or indirect ownership or control of fifty per cent or more of the voting stock of the payor corporation by the recipient corporation. Dividends shall have the meaning provided in section 316 of the internal revenue code. This subtraction shall apply without regard to the provisions of section 43-961, paragraph 2 and article 4 of this chapter. A corporation that has its commercial domicile, as defined in section 43-1131, in this state may subtract the full amount of the dividends. A corporation that does not have its commercial domicile in this state may subtract:

(a) For its taxable year beginning in 1990, an amount equal to one-half of the dividends.

(b) For taxable years beginning in 1991 and thereafter, the full amount of the dividends.

5. Interest income received on obligations of the United States.

6. The amount of dividend income from foreign corporations.

7. The amount of net operating loss allowed by section 43-1123.

8. The amount of any state income tax refunds received which were included as income in computing federal taxable income.

9. The amount of expense recapture included in income pursuant to section 617 of the internal revenue code for mine exploration expenses.

10. The amount of deferred exploration expenses allowed by section 43-1127.

11. The amount of exploration expenses related to the exploration of oil, gas or geothermal resources, computed in the same manner and on the same basis as a deduction for mine exploration pursuant to section 617 of the internal revenue code. This computation is subject to the adjustments contained in section 43-1121, paragraph 8 and paragraphs 9 and 10 of this section relating to exploration expenses.

12. The amortization of pollution control devices allowed by section 43-1129.

13. The amount of amortization of the cost of child care facilities pursuant to section 43-1130.

14. The amount of income from a domestic international sales corporation required to be included in the income of its shareholders pursuant to section 995 of the internal revenue code.

15. The income of an insurance company that is exempt under section 43-1201 to the extent that it is included in computing Arizona gross income on a consolidated return pursuant to section 43-947.

16. The amount of contributions by the taxpayer during the taxable year to medical savings accounts established on behalf of the taxpayer's employees as provided by section 43-1028, to the extent that the contributions are not deductible under the internal revenue code.

17. The amount by which a capital loss carryover allowable pursuant to section 43-1130.01, subsection F exceeds the capital loss carryover allowable pursuant to section 1341(b)(5) of the internal revenue code.

Sec. 8. Retroactivity

Sections 43-1021, 43-1022, 43-1121 and 43-1122, Arizona Revised Statutes, as amended by this act, apply retroactively to taxable years beginning from and after December 31, 1999.

Sec. 9. Retroactive recognition of change in depreciation methods

A. With respect to tax returns for taxable periods ending before December 31, 2003 that were prepared pursuant to sections 43-1021 and 43-1022, Arizona Revised Statutes, or sections 43-1121 and 43-1122, Arizona Revised Statutes, before the retroactive amendments by this act, a taxpayer may elect to recognize the entire cumulative effect of the retroactive change

of depreciation methods on the tax return for the first taxable year ending on or after December 31, 2003 instead of retroactively recognizing those changes on those prior returns.

B. To qualify for this election, all returns prepared pursuant to the prior law must be filed by the due dates for those returns, including extensions, or April 15, 2004, whichever is later.

C. Any adjustment computed under this election shall be treated as either an addition to or a subtraction from Arizona gross income.

Sec. 10. Emergency

This act is an emergency measure that is necessary to preserve the public peace, health or safety and is operative immediately as provided by law.

APPROVED BY THE GOVERNOR MAY 5, 2004.

FILED IN THE OFFICE OF THE SECRETARY OF STATE MAY 5, 2004.