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Arizona Revised Statutes Section 43-1071

Credit for income taxes paid to other states; definitions

A. Subject to the following conditions, residents are allowed a credit against the taxes imposed by this chapter for net income taxes imposed by and paid to another state or country on income taxable under this chapter:

1. The credit is allowed only for taxes paid to the other state or country on income that is derived from sources within that state or country and that is taxable under its laws irrespective of the residence or domicile of the recipient.
2. The credit is not allowed if the other state or country allows residents of this state a credit against the taxes imposed by that state or country for taxes paid or payable under this chapter.
3. The credit shall not exceed the proportion of the tax payable under this chapter as the income subject to tax in the other state or country and also taxable under this title bears to the taxpayer's entire income on which the tax is imposed by this chapter.

B. If any taxes paid to another state or country for which a taxpayer has been allowed a credit under this section are at any time credited or refunded to the taxpayer:

1. The taxpayer shall immediately report that fact to the department.
2. A tax equal to the credit allowed for the taxes credited or refunded by the other state or country is due and payable from the taxpayer on notice and demand from the department.
3. Interest shall be added to and collected as a part of the tax at the rate determined pursuant to section 42-1123 from the date the credit was allowed under this chapter to the date of the notice and demand.
4. If the tax and interest are not paid within ten days after the date of notice and demand, there shall be collected as a part of the tax interest on the unpaid amount of tax and interest at the rate of twelve percent a year from the date of the notice and demand until the amount is paid.

C. The credit against the taxes imposed by this chapter for net income taxes paid to another state or country is not allowed to any taxpayer or any class of taxpayers if the allowances of the credit will result in any invalid or illegal discrimination against another taxpayer or another class of taxpayers.

D. For taxable years beginning on or after January 1, 2002 and subject to the following conditions, a resident of this state, who is also considered to be a resident of another state under the laws of the other state, is allowed a credit against the taxes imposed by this title for net income taxes imposed by and paid to that state on income taxable under this title as follows:

1. The credit is allowed only if the other state taxes the income to the resident of this state and does not allow the taxpayer a credit against taxes imposed by that state on that income for taxes paid or payable on that income under this title.
2. The credit is allowed only for the proportion of the taxes paid to the other state as the income taxable under this title and also subject to tax in the other state bears to the entire income on which the taxes paid to the other state are imposed.
3. The credit may not exceed the proportion of the tax payable under this title as the income taxable under this title and also subject to tax in the other state bears to the entire income taxable under this title.
4. For the purpose of the credit allowed under this subsection, "income taxable under this title and also subject to tax in the other state" means income that would be sourced to the other state if the other state were imposing its income tax on the taxpayer as if the taxpayer was a nonresident of that other state.

E. The taxpayer may apply the allowable credit only against Arizona income tax for the same taxable year in which the income is subject to tax in the other state.

F. An individual who participates in a composite income tax return in another state may claim a credit for taxes paid to the other state if the taxpayer meets all of the requirements of this section and the taxes paid to the other state are imposed on and paid directly by the individual taxpayer and not the entity. For the purposes of this subsection, taxes are considered to be imposed on and paid directly by the individual under one or more of the following circumstances:

1. The individual makes direct payment to the other state.
2. The individual makes direct payment to the entity filing the composite income tax return.
3. The entity charges the individual's loan account for the amount of the tax.
4. The entity reduces the individual's capital account.

G. For taxable years beginning from and after December 31, 2021, a resident taxpayer is allowed a credit against the tax otherwise due under this title for the amount of any tax that the department determines is substantially similar to the tax imposed under section 43-1014 for the taxable year and that is imposed by another state of the United States or a political subdivision of such a state, or by the District of Columbia, with respect to the direct and indirect taxable income attributable to the resident taxpayer from a pass-through entity that is also subject to tax under this title. A credit allowed pursuant to this subsection may not exceed the amount that would have been allowed if the income were taxed at the individual level and not taxed at the entity level.

H. If the taxpayer claims the credit for taxes paid to a foreign country, the taxpayer shall use the conversion rate in effect on the date the taxpayer paid the taxes to the foreign country.

I. For the purposes of this section:

1. "Composite income tax return" means a single income tax return that is filed with another state on behalf of a group of individuals who are partners or shareholders of the partnership or S corporation that filed the return on their behalf.

2. "Entire income on which the other state's or country's tax is imposed" means the other state's or country's income computed under the equivalent of section 43-1094 but does not include any exemption allowable under the equivalent of section 43-1023.

3. "Entire income on which the tax is imposed by this chapter" means Arizona adjusted gross income as defined and computed under section 43-1001 but does not include any exemption allowed under section 43-1023.

4. "Income subject to tax in the other state or country and also taxable under this title" means the portion of income that is included in entire income on which the tax is imposed by this chapter that is also included in the entire income on which the other state's or country's tax is imposed. The taxpayer shall increase or reduce the portion of income that is included in the entire income on which the tax is imposed by this chapter by any related additions under section 43-1021 and by any related subtractions under section 43-1022. The taxpayer shall increase or reduce the portion of income that is included in the entire income on which the other state's or country's tax is imposed by any related additions and subtractions under the other state's equivalent of sections 43-1021 and 43-1022, as applicable.

5. "Net income tax":

(a) Means:

(i) A tax that grants deductions or exemptions from gross income.

(ii) Any tax imposed by another country that qualifies for a credit under sections 901 and 903 of the internal revenue code and the regulations under those sections, even if withheld from income.

(b) Except as specifically included in subdivision (a) of this paragraph, does not include:

(i) A system of taxation that assesses taxes on gross income, gross receipts or gross dividends.

(ii) Taxes withheld from income.

6. "Tax payable under this chapter" means the income tax imposed by this state on the taxpayer's taxable income as defined under section 43-1001 minus any tax credit amount

claimed for the taxable year under this article but not including the credit amount allowed under this section.