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Robert F. Corbin

May 20, 1987

Mr. C. "Hos" Hoskins, Director  
Arizona Department of Revenue  
1700 W. Washington  
Phoenix, Arizona 85007

Re: I87-069 (R87-085)

Dear Mr. Hoskins:

By letter dated May 1, 1987, you have asked for our advice on the application of Laws 1987 (1st Reg. Sess.) Ch. 96 (House Bill 2051). Section 2 of Chapter 96 modifies A.R.S. § 43-401 by increasing the statutory withholding tax rate, and by adding an election to withhold at a 25% rate. Section 4 of Chapter 96 provides that the act is effective retroactively to July 1, 1987, and that the increase in withholding rates expires from and after December 31, 1987.<sup>1/</sup>

House Bill 2051 does not contain an emergency clause. Consequently, House Bill 2051 will become effective 90 days after the Legislature adjourns. Ariz. Const., art. IV, pt. 1, § 1(3). Since the Legislature is still in session, House Bill 2051 will not become effective until some time after August 1, 1987. At that point in time however, it will be effective retroactive to July 1, 1987.

The question thus presented is whether this retroactive application is constitutionally valid, and how employers may

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<sup>1/</sup>The purpose of the increase in the withholding rate is to compensate for a decrease in federal withholding. Withholding for Arizona state income tax purposes is a percentage of the federal income tax deducted and withheld. Because the federal withholding has decreased as a result of the new tax laws, Arizona withholding has also decreased. House Bill 2051 was intended to negate this decrease in Arizona income tax withholding.

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comply with House Bill 2051 during the "window period," i.e. the period between July 1, 1987 and 90 days after the adjournment of the legislature.

Retroactive legislation is not per se unconstitutional. The legislature may pass retroactive legislation so long as such legislation does not retroactively impair any substantive rights that have vested, or that are so substantively relied upon that retroactive divestiture would be manifestly unjust. Hall v. A.N.R. Freight Systems, Inc., 149 Ariz. 130, 140, 717 P.2d 434, 444 (1986). In this case, it does not appear that increasing the withholding rate would affect a vested right. In Beaumont Company v. State, 125 Misc.2d 87, 477 N.Y.S.2d 272, 275 (1984) the New York Court stated:

No taxpayer has a vested right in the rate of taxation and so long as the proposed retroactive application is not unreasonably long, serves a public purpose and does not unreasonably disappoint the taxpayer's justified reliance on prior law, such retroactive application will not violate due process.

The court in Beaumont held constitutional a law that was enacted on April 2, 1982 which increased the rate of tax on the recording of certain mortgages which were recovered on or after February 1, 1982.

In Welch v. Henry, 303 U.S. 134, 147, 59 S.Ct. 121, 126, 83 L.Ed. 87, 93 (1938), the United States Supreme Court stated:

In each case it is necessary to consider the nature of the tax and the circumstances in which it is laid before it can be said that its retroactive application is so harsh and oppressive as to transgress the constitutional limitation.

Generally, if the taxpayer is reasonably forewarned that a tax may later be levied or increased for a given period, the imposed tax usually will not be found unjustly oppressive or void. General Expressways, Inc. v. Iowa Reciprocity Board, 163 N.W.2d 413, 425 (Iowa 1968).

Even though the legislature is still in session, it does not appear that the period of retroactivity for House Bill 2051 will be unreasonably long. Also, since House Bill 2051 was

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filed in the office of the Secretary of State on April 17, 1987, taxpayers and employers are reasonably forewarned that the withholding rate will be increased retroactively for the period July 1, 1987 to the effective date of House Bill 2051.

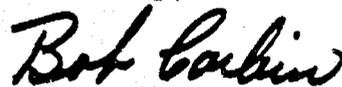
An increase in the rate of withholding is not in fact an increase in tax rate, but an acceleration of tax collection. All amounts withheld will be credited toward the employees 1987 state income tax liability. Such employees' total 1987 state income tax liability is not increased by the temporary change in the withholding rate. Consequently, we do not believe that the retroactive application of House Bill 2051 renders it unconstitutional.

The retroactive application of House Bill 2051 does present a dilemma for employers during the period of July 1, 1987 until 90 days after the legislature adjourns. During that period, the unauthorized rate of withholding is as currently set forth in A.R.S. § 43-401, even though that rate will be retroactively increased at a later date. It is our opinion that during that "window period" employers must continue withholding at the rates authorized by A.R.S. § 43-401 as there is no authority in effect to do otherwise.

Because the legislature included a retroactive provision however, it is clear that it was their intent to collect a higher withholding on earnings from and after July 1, 1987. In order to give effect to the intent of the legislature, we believe there is an implicit authorization in House Bill 2051 for employers to collect the additional withholding for the "window period" after House Bill 2051 becomes effective.

Finally, because employers cannot collect the additional withholding until after Chapter 96 becomes effective, we do not believe that any penalties or interest may be imposed for failure to withhold during the "window period." However, after Chapter 96 becomes effective, all interest and penalty provisions become applicable when the additional withholding is not collected and paid to the state.

Sincerely,



BOB CORBIN  
Attorney General