

# Overview of Southwestern States Construction Sales Tax Structure

*Prepared for the Construction Financial Management Association*

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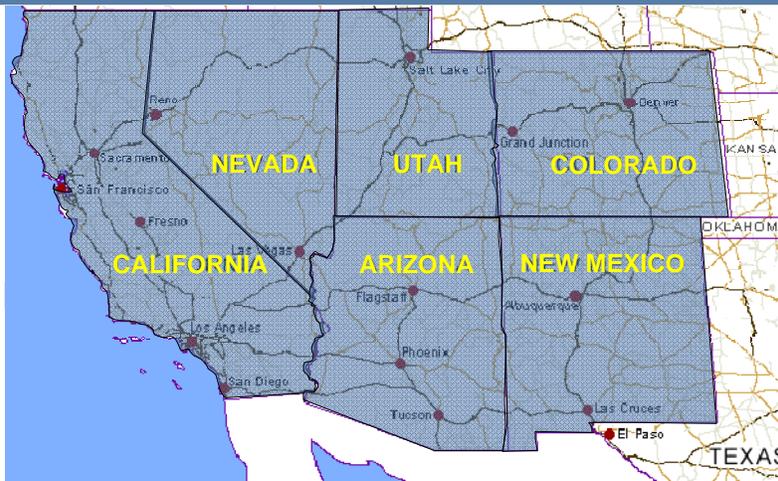
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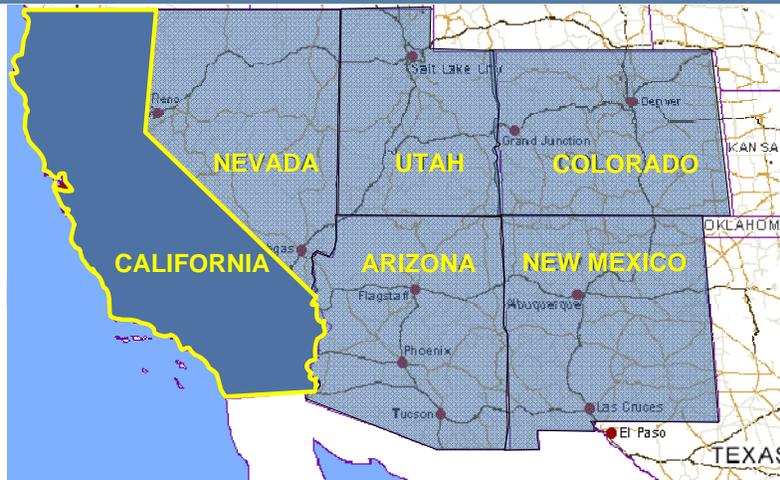
## Southwestern States Construction Sales Tax Structure



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## California Construction Sales Tax Structure



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## California Construction Sales Tax Structure

- Retail sales tax only (services not taxed)
- Tax applied to retailer's gross receipts
  - Taxpayer is the retailer, not the consumer
- For construction contracting, distinction among materials, fixtures, and machinery and equipment

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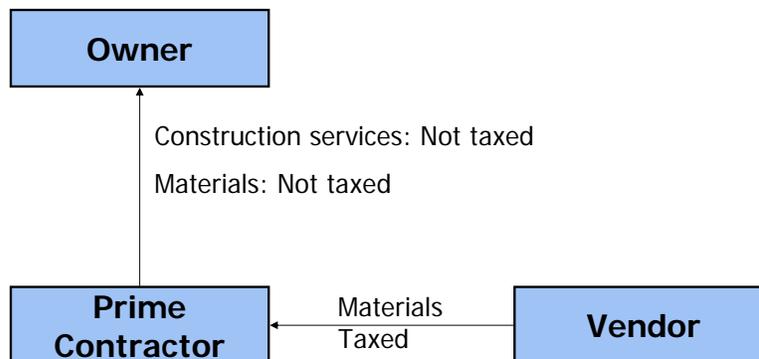
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## California Construction Sales Tax Structure

	Contractor is...	Tax based on...
<b>Materials</b>	Consumer	Contractor's purchase price
<b>Fixtures</b>	Retailer	Contractor's sales price
<b>Machinery &amp; Equipment</b>	Retailer	Contractor's sales price

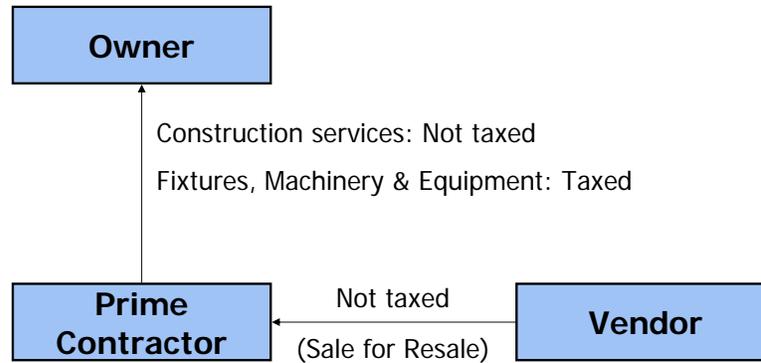
## California Normal Prime Contractor Situation - Materials

Tax generally applies to contractor's purchase



## California Normal Prime Contractor Situation - Fixtures, Machinery & Equipment

Tax generally applies to contractor's sale to owner

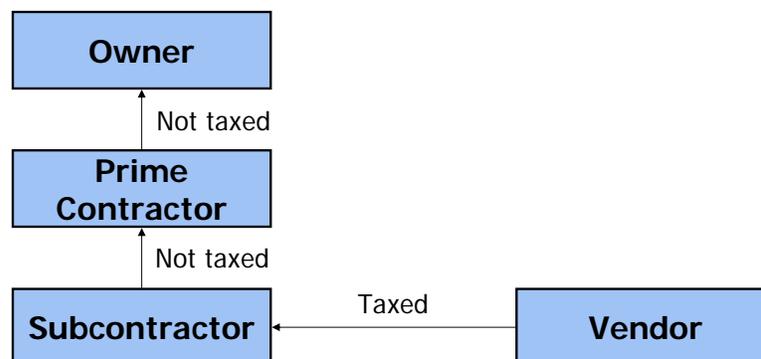


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## California Subcontractor - Materials

Tax generally applies to subcontractor's purchase

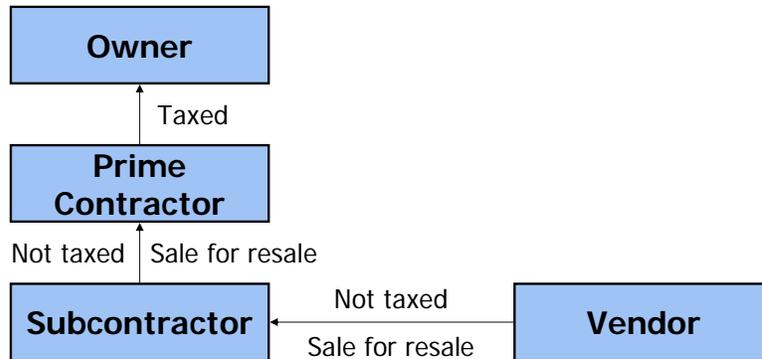


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## California Subcontractor - Fixtures, Machinery & Equipment

Tax generally applies to contractor's sale to owner

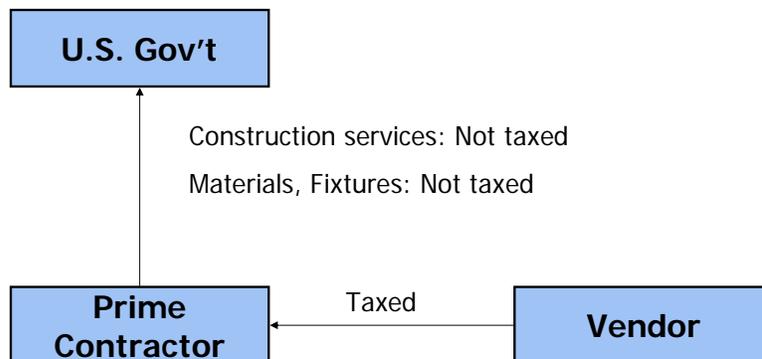


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## California Federal Government Contractor - Materials and Fixtures

Tax generally applies to contractor's purchase

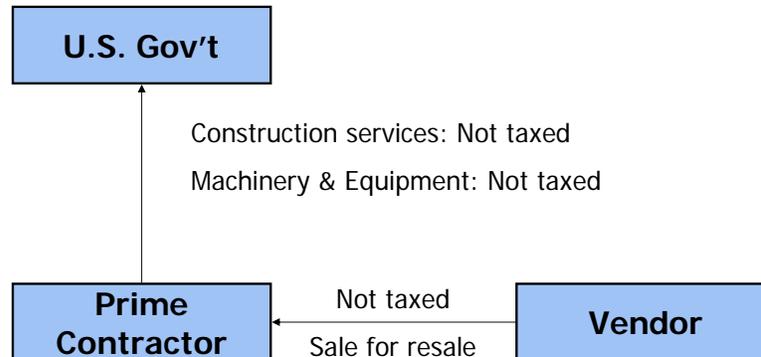


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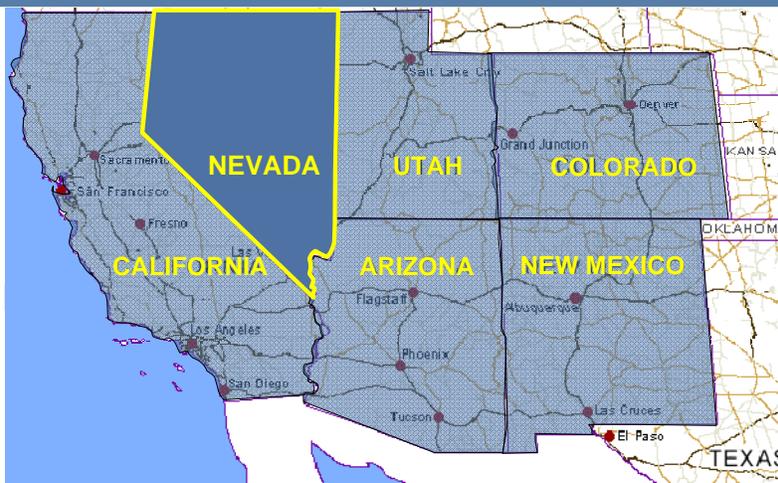
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## California Federal Government Contractor – Machinery and Equipment

Neither purchase nor sale is taxed



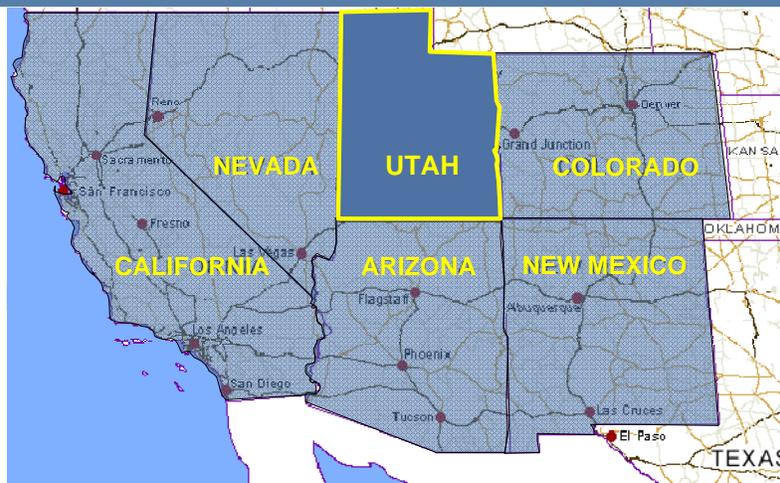
## Nevada Construction Sales Tax Structure



## Nevada Construction Sales Tax Structure

- Construction contracts not separately taxed
- Contractors are consumers of tangible personal property used in improving real property
- Sales or use tax applies to contractor's purchases of tangible personal property

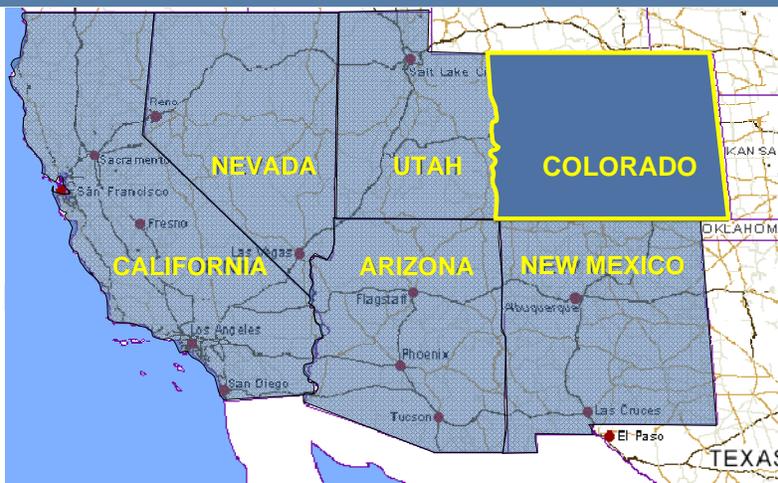
## Utah Construction Sales Tax Structure



## Utah Construction Sales Tax Structure

- Contractors' purchases of materials and other tangible personal property converted into real property generally subject to sales tax
- Contractors treated as retailers of personal property that is not permanently attached

## Colorado Construction Sales Tax Structure



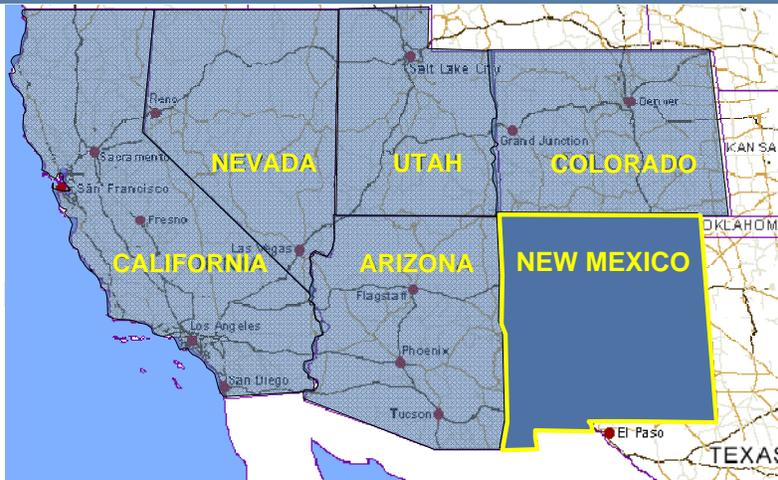
## Colorado Construction Sales Tax Structure

- Contractors generally pay sales tax on purchases of tangible personal property (materials) that becomes incorporated into the building or structure (tax paid to vendor)
- Contractors generally pay use tax on other tangible personal property used in business or on jobs if the delivery, storage, use or consumption of the property is in Colorado (tax paid directly to the state)

## Colorado Construction Sales Tax Structure

- Contractors treated as retailers of supplies or materials if purchased tax free, or if labor and materials invoiced separately
  - Sales tax applies to marked up billing price
  - Contractor's purchases exempt as resale sale

## New Mexico Construction Sales Tax Structure



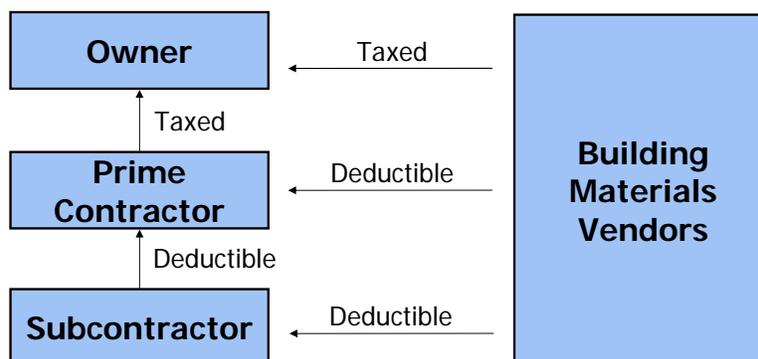
## New Mexico Gross Receipts Tax Structure

- New Mexico has gross receipts tax
  - Generally applies to seller's receipts from retail sales, leasing property, selling real property, and selling services
- Construction contracting is a taxable service
- Contractor is treated as retailer, subject to tax on gross receipts from construction

## New Mexico Subcontractors and Suppliers

- Subcontractors generally may deduct receipts for services performed on taxable projects
- Suppliers generally may deduct receipts for sales of materials that become an ingredient or component part of taxable project
- Contractor must furnish nontaxable certificate to subs and suppliers

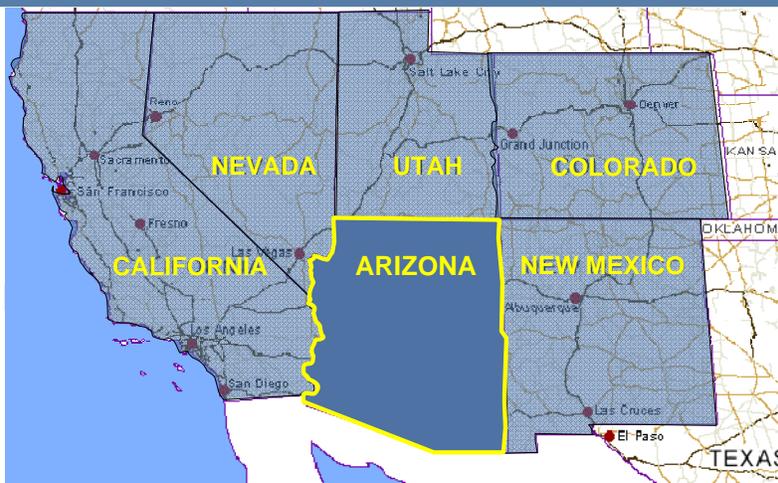
## New Mexico Subcontractors and Suppliers



## New Mexico Federal Government Contracting

- Sales of tangible personal property to United States (and New Mexico) generally exempt
- Receipts from constructing a project for a government agency are not deductible
  - Construction is taxable service
  - Contract is for services if greatest investment in performing contract is for skills and labor
- Government sales deduction unavailable even if materials billed separately

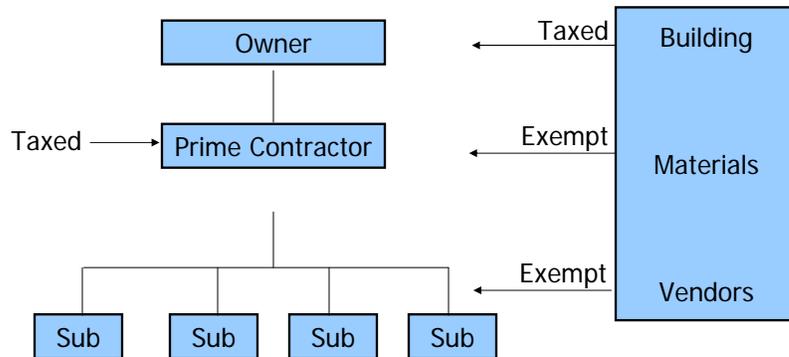
## Arizona's Complicated Scheme



## Structure Of The Arizona Contracting Sales Tax

1. The "Prime Contractor" is Taxable on 65% of Gross Receipts
2. Subcontractors are Exempt
3. Sales of Building Materials to Both Prime and Subcontractors are Exempt

## Normal General Contractor Situation



## Definition Of "Prime Contractor"

- A.R.S. § 42-5075.N.8 defines "prime contractor" to mean "the contractor who supervises, performs or coordinates the "modification" of any building, highway, road, railroad, excavation or other structure, project, development or improvement including the contracting, if any, with any subcontractors or specialty contractors and is responsible for the completion of the contract."

## House Bill 2627 (Laws 2007, Ch. 188) \*Significant Change\*

Adds following exclusion to definition of "prime contractor:"

- Excludes owners who hire one or more contractors to improve real property "regardless of the existence of a contract for sale or the subsequent sale of the real property."
- Nullifies LR05-007
- Retroactive to 1991

## Subcontractors Are Exempt

A.R.S. § 42-5075.D provides that a subcontractor is not liable for the sales tax if:

- (1) the job was within the control of a prime contractor and
- (2) the prime contractor is liable for the tax on its gross income attributable to the job and from which the subcontractors were paid

## FORM 5005



Arizona Department of Revenue  
Prime Contractor's Certificate

ARIZONA FORM  
5005

The purpose of this form is to provide a subcontractor with the validation required for tax exemption of a particular project, for a period of time, or until revoked. This certificate establishes responsibility for the transaction privilege tax; therefore, it must be completed by the prime contractor assuming the contracting transaction privilege tax liability for the contracting project(s). The asterisked (\*) items must be completed, otherwise the certificate is not valid. The Department may disregard this certificate pursuant to ARS § 42-5075.E if the certificate is incomplete or erroneous. If disregarded, the entity accepting the certificate (subcontractor) will have the burden of proving (pursuant to ARS § 42-5075.D), that it is not subject to transaction privilege tax as a taxable prime contractor.

<b>A. Prime Contractor</b>		* TRANSACTION PRIVILEGE LICENSE #:	
* NAME:		AZ Contractor License #:	
* ADDRESS:		Telephone #:	
<b>B. Subcontractor</b>		* TRANSACTION PRIVILEGE LICENSE #:	
* NAME:		AZ Contractor License #:	
* ADDRESS:		Telephone #:	
<b>C. Type of Certificate (check one and provide requested information)</b>			
<input type="checkbox"/> Single Project Certificate		<input type="checkbox"/> Blanket Certificate (check applicable box and fill in requested information).	
PROJECT DESCRIPTION	OR	<input type="checkbox"/> Period From: _____	
		Through: _____	
		<input type="checkbox"/> Until revoked	
		<input type="checkbox"/> Specific Exceptions: _____	
** (For example, Building Permit #, Address, Subdivision, Book/Map/Parcel #s, and/or Legal Description)			

I hereby certify that I have authority to sign this Certificate on behalf of Prime Contractor. I understand that by executing this Certificate, Prime Contractor is assuming the prime contracting transaction privilege tax liability applicable to the above referenced project(s).

SIGNATURE: \_\_\_\_\_ PRINT NAME: \_\_\_\_\_  
TITLE: \_\_\_\_\_ DATE SIGNED: \_\_\_\_\_

ADDER 60-2015 (4/02) This Form Supersedes All Other Form 5005's

## R15-5-602.C.1

Subcontractors are exempt provided that such persons are not acting in the capacity of prime contractors. **A subcontractor is considered to be a prime contractor, and therefore liable for the tax, if:**

- Work is performed for and payments are received from an owner-builder.
- Work is performed for and payments are received from an owner or lessee of real property.

## No Tax On Purchase Of Building Materials

Building materials are exempt if:

- Sold to prime contractors or subcontractors.
- Incorporated into the construction project.

**Note:**

- Consumable items not incorporated into structure are taxable.
- Equipment rented to contractors is taxable under the rental classification.

## Primary Deductions

1. Land Deduction (20% audit "safe harbor").
2. 35% Labor Deduction or 65% Inclusion.
3. Contractor's Deduction for State and Municipal Sales Taxes.
  - DOR Automatic Factoring Worksheet!

## Government And Indian Contracts

- Construction contracts with the U.S. Government are **taxable**.
- Likewise, contracts with the state, local governments and school districts are **taxable**.
- Contracts with an Indian Tribe are **not taxable** if the construction is on an Indian reservation and the contract is with the Indian tribe or an agency of the tribe.

## Design-Build Contracts

- Only Direct Costs Are Not Taxable.
  - Amounts paid to 3<sup>rd</sup> party are direct costs.
  - If done in-house – direct labor cost only.

*See Senate Bill 1293 (2004), A.R.S. § 42-5075.J*

## Exemption For Preconstruction Services

- H.B. 2622 (2008) exempts gross income/receipts from:
  - A separate, written “design phase” or “professional services” contract;
  - Executed before modification (construction) begins;
  - Regardless of whether the services are provided before or during construction.

*See A.R.S. § 42-5075.M*

## Exemption For Preconstruction Services

Bill defines:

- “design phase” – Not Taxable
- “construction phase” – Taxable
- “professional services” – Not taxable

## Deduction For Development And Impact Fees

Development and impact fees paid to state or local government to offset cost of infrastructure, as well as the amount of any credits against such fees.

*See* A.R.S. § 42-5075.B.21

## Differing State Treatment of Federal Projects

- California
  - Construction services are **not taxed**
  - Sales of materials & fixtures sold to prime contractors for US projects are generally **taxed**;
  - Sales of machinery & equipment to prime contractors for US projects are generally **not taxed**.
- Nevada
  - Contracting services are **not taxed**, but sales to contractor are generally **taxable**.
- Utah
  - Contracting services are **not taxed**, but sales to contractors are generally **taxable**.
- New Mexico
  - Construction services provided to US are **taxable**.
- Arizona
  - Construction services provided to US are **taxable**.

## Arizona Green Initiatives

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## Solar Energy Device Sales Tax Exemption

Exempts contract to provide and install solar energy devices.

- **"Solar energy device"** – system or series of systems designed primarily to provide heating, cooling, to produce electrical power, to produce mechanical power or any combination by collecting and transferring solar generated energy.
- Includes wind generator systems that produce electricity.

## Renewable Energy Equipment Property Tax

- Renewable Energy Equipment valued at **20%** of depreciated cost.
- Applies to electric generation, transmission & distribution, combination gas and electric transmission and distribution properties where electricity derived from solar, wind or other non-petroleum renewable resources when the power is not intended for self-consumption. ARS § 42-14155(C).

## Renewable Energy Manufacturing Businesses

### Property & Income Tax

- Incentive for “Renewable Energy Manufacturing” businesses that expand or locate manufacturing facilities or headquarters in Arizona between 2010 and 2014.
  - 10% income tax credit against total capital investment; and
  - Class 6, 5% property tax assessment ratio.
- 5 year commitment; must create new employment. Does not apply to electric generation facilities.