CONSTRUCTION CONTRACTING

WHO IS A CONSTRUCTION CONTRACTOR

A construction contractor is any person who undertakes to construct, alter, repair add to, subtract from, improve, move, or demolish any improvement to real property. This includes subcontractors, specialty contractors, prime/general contractors, construction managers, or any person receiving consideration for supervision or coordination of construction activity. A construction contractor who provides labor only is subject to the same provisions as someone who provides both materials and labor.

TAXABLE ACTIVITIES INCLUDE

- Construction or demolition of a structure
- Road construction
- Excavation and landscape installation
- Construction for governmental entities, including the federal government
- Construction for schools, churches and nonprofit organizations
- Home remodeling
- Painting and wallpapering
- Plumbing
- Installation of air conditioning
- Subsequent repairs of improvements to real property

GROSS INCOME

Contractors are taxed on their gross income from the contracting business. Normally, this is the total amount of the contract. The income is taxable regardless of whether it includes both labor and materials or just labor. Contractors must report on either a progress billing or cash receipts basis.

DEDUCTIONS

The following deductions from gross income are allowed in calculating taxable income:

- **Out of City** contracting income
- **Privilege taxes collected**, if separately billed
- **Privilege taxes factored**, if not separately billed
- **Subcontracting** income
- **Development and Impact** fees paid to a local government, but not permits
- The actual direct costs of **Architectural and Engineering** fees included in a contract
- A **35% Standard Deduction** after all other deductions (This is in lieu of a labor deduction.)
- Certain **Solar Energy** Devices

WHEN CONSTRUCTION CONTRACTING IS TAXABLE

Construction contracting is taxable in Tempe when the job is located in Tempe. Construction contractors must report their income from each job to the city in which the job is located, not where the contractor is based.

TAX RATE

The tax rate is 1.8% of gross income, less applicable deductions.

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Tempe
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OWNER-BUILDERS
An owner-builder is an owner of real property who, by himself or through others (such as a contractor), improves real property. An owner-builder who improves real property for his own use, normally is not subject to tax; his contractors and suppliers are. If, however, the improved property is subsequently sold, the owner-builder may be subject to tax as a **Speculative Builder**.

SPECULATIVE BUILDERS
A Speculative Builder is an owner-builder who improves real property for subsequent sale. Speculative Builders are taxed as construction contractors.

A Speculative Builder who sells improved real property within 24 months of substantial completion is subject to tax based on the gross selling price of the property. If the property is not sold with 24 months of substantial completion, the Speculative Builder is subject to tax based on construction costs.

Credits are allowed for city taxes paid by a Speculative Builder to contractors, and **no deduction is allowed for land.**

If you think you may have entered into a transaction subject to the tax on Speculative Builders, please contact the Tax & License office.

CONTACT TAX & LICENSE
Call: (480) 350-2955
Email: salestax@tempe.gov
Web Page: www.tempe.gov/salestax

OTHER MATTERS

EXEMPTIONS AVAILABLE FOR ITEMS PURCHASED
A contractor may claim an exemption from retail sales tax when he purchases materials to be incorporated into a building or improvement. This does not apply to construction equipment and tools sold or leased to a contractor or to materials not incorporated into the improvement. It also does not apply to materials purchased directly by an owner-builder.

SUBCONTRACTING EXEMPTIONS
Income from acting as a subcontractor is exempt from tax. This income must be included in gross income on the front of the return and itemized as a deduction on the back of the return. To qualify for this exemption, the subcontractor must obtain the City Privilege License number of the prime contractor, plus a written declaration from the prime contractor that he is liable for the tax. The City accepts a properly completed AZ Form 5005 as documentation of the exemption.

FACTORING SALES TAX
A factor of .050017 may be used to calculate the total tax included in gross contracting income. The factor is based on a combined state, county, and city tax rate of 8.1% and must be applied to taxable income before the 35% standard deduction, but after all other deductions.

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