

# CONSTRUCTION CONTRACTING

Licensing and Tax Information: (623) 333-2001 | [salestax@avondale.org](mailto:salestax@avondale.org)

Avondale<sup>AZ</sup>



**YOU OWE CONSTRUCTION CONTRACTING TAX IF:** | You are in the construction business in the City of Avondale.

A contractor is considered to be in business in Avondale when the construction job is in Avondale. Contractors report the income from each job to the Arizona city in which the job is located, not to the city in which the contractor is based.

**TAX RATE ON CONSTRUCTION CONTRACTING** | The Avondale tax rate is 2.5% of the taxable income.

**ARE SUBCONTRACTORS TAXED?** | Income from acting as a subcontractor is exempt from the tax.

This income must be reported on the front of the tax return and taken as a deduction on the back of the tax 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 has exemption certificates available which you may use to document these exemptions. Contractors who work for a property owner, not another contractor or speculative builder will be considered a prime contractor for that job.

**ARE OWNER-BUILDERS TAXED?** | Owners who are improving real property for themselves may or may not be the party liable for paying the tax on the construction.

- ▶ A homeowner who is building his own principal residence would not normally be the liable party. Each of the contractors or suppliers who provide materials and/or services would be liable based on their income from the job.
- ▶ A "speculative builder" who is building a home or other property for sale would be liable for tax based on the property's sales price. If the property is not sold within 24 months of the date it was completed, the tax would be due based on the cost of construction. The tax on a home in a home builder's inventory is not due until the home is sold, even if it exceeds 24 months.
- ▶ Other owner-builders who are building for their own use would not normally be liable for the tax. Their contractors and suppliers would be the liable parties. However, the owner may be liable for some additional tax if he sells the property within 24 months after completion.
- ▶ Transactions between related companies or persons are taxable by the City of Avondale. See Avondale City Code Section 13A-100 for the definition of a "Person"; Section 13A-210 "Determination of gross income: transactions between affiliated companies or persons," and Section 13A10-220 "Determination of gross income: artificially contrived transactions."

## WHAT IS CONSTRUCTION CONTRACTING?

Construction contracting includes construction, remodeling, repairs, demolition, etc. to real property. There does not have to be a contract for the work. A construction contractor who provides only labor is subject to the same provisions as one who provides both materials and labor.

**Examples of taxable contracting activity include:**

- ▶ Construction or demolition of a building.
- ▶ Road construction.
- ▶ Land excavation and landscaping.
- ▶ Installation of permanently attached equipment.
- ▶ Sales and installation of floor covering.
- ▶ Home remodeling.
- ▶ Repairs to a building.
- ▶ Construction for a government agency (including the City of Avondale).
- ▶ Construction for a church or nonprofit organization.
- ▶ Painting.

**Examples of items which are not considered construction contracting:**

- ▶ Landscape maintenance, lawn mowing (exempt).
- ▶ Installation of drapes & mini-blinds (retail).
- ▶ The sale of manufactured buildings.
- ▶ Plug-in kitchen equipment (retail).

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## **GROSS INCOME** | Contractors are taxable based on their gross income from the contracting business.

Normally this will be either the total amount of the contract or the sales price of the property when it is sold. The income is taxable regardless of whether it includes both labor and materials or just labor.

Sales of improved land such as subdivision lots are taxable as contracting. The tax applies when the off-site improvements have been constructed to the property.

Contractors may report on a progressive billing basis or on a cash receipt basis. Home builders and speculative builders report the total selling price at the time of close of escrow.

## **DEDUCTIONS** | The following are typical deductions subtracted from the gross income to arrive at the taxable income:

- ▶ Exempt subcontracting.
- ▶ Out of City contracting.
- ▶ Environmental/Remediation contracting.
- ▶ Development or impact fees included in a construction or development contract for payment to the state or local government to offset governmental costs of providing public infrastructure, public safety and other public services to a development.
- ▶ The actual direct cost of Architectural & Engineering Services included in a construction contract.
- ▶ Installation costs of solar daylighting or energy devices included in a construction contract by a registered solar energy contractor with the Arizona Department of Revenue.
- ▶ Sales tax collected is deductible. If you have charged your customer sales tax separately, and it is included in gross income, you may deduct it.
- ▶ If you have not charged your customer sales tax, you may "factor" your privilege (sales) tax. This means that the total contract price includes privilege (sales) tax and you can compute the amount of tax and deduct it. Some formulas for factoring tax are included below.
- ▶ A standard 35% deduction is allowed for all income taxable as contracting. This is in lieu of an actual labor deduction. This 35% should be computed after the sales tax deduction has been deducted.
- ▶ No land deduction is allowed.

## **FACTORING SALES TAX** | The following are formulas for factoring privilege (sales) tax on contracting in Avondale.

These formulas are based on a combined state, county and city tax rate of 9.8%. They also consider that a land deduction is allowable for state and county purposes but not for Avondale purposes.

### **Factors to apply to Gross Income (GI) and Land (L):**

1. No sale of land is included in the gross income:  
Total privilege (sales) tax =  $(.05988531 \times GI)$
2. The gross income includes the sale of land:  
Total privilege (sales) tax =  $(.05988531 \times GI) - (.03891383 \times L)$
3. The sale involves only the sale of land:  
Total privilege (sales) tax =  $(.01124706 \times GI)$

## **EXEMPTIONS AVAILABLE FOR ITEMS YOU PURCHASE**

There is an exemption from the tax on retail sales for materials which a contractor purchases for incorporation into a building or improvement. This does not apply to construction equipment and tools sold or leased to a contractor. It does not apply to any other tangible personal property which is not incorporated into the actual improvements being built. It does not apply to materials purchased directly by an owner-builder.

*This publication is for general information only about Transaction Privilege (Sales) Tax on income from contracting activities. This is an informal and nonbinding communication.*

*For complete details, refer to the City of Avondale Privilege & Excise Tax Code and related regulations. In case of inconsistency or omission in this publication, the language of the Tax Code will prevail. The transaction privilege tax is commonly referred to as a sales tax, however, the tax is on the privilege of doing business in Avondale and is not a true sales tax.*



## **LICENSING OFFICE:**

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