

Department of Finance and Administration

Legislative Impact Statement

Bill: HB1266

Amendment Number: H1

Bill Subtitle: TO CREATE A SALES AND USE TAX EXEMPTION FOR CONSTRUCTION MATERIALS PURCHASED TO CONSTRUCT, REPAIR, OR REMODEL A FACILITY TO BE USED BY AN EXEMPT ENTITY.

Basic Change :

Representative Dale

House Amendment 1 - The proposal would exempt the construction materials, supplies, and other tangible personal property purchased and used in construction projects for Regional Water Distribution Districts. These Regional Water Distribution Districts are currently exempt from sales and use tax on their purchases. The exemption granted in the bill would apply to the materials purchases by construction contractors performing contracts for these districts. The Regional Water Distribution District would register the project with DFA and obtain an exemption certificate for use by the construction contractors when making project materials purchases. The construction contractor would be responsible for payment of the sales and use tax on the excess portion of materials originally purchased for use on the project. The bill does not exempt the purchase of machinery, equipment or tools used in fulfilling the construction contract.

Under current law, contractors must pay sales tax on materials and supplies they purchase for use in building a project regardless of whether the entity for which the project is constructed is exempt from sales tax on its own purchases. Under this bill, construction contractors would continue to pay sales tax on materials and supplies purchased for use in building a project for most exempt entities (e.g. U.S. Government, UAMS, Habitat for Humanity, etc.) but would not pay sales tax when purchasing materials and supplies for use in constructing a project for a Regional Water Distribution District.

Revenue Impact :

FY2014 Tax Decrease

Total Impact to State Revenues - \$.485 million

[8 months estimated reduced tax revenues]

-\$.325 million --- State General Revenue (4.5%)
-\$.063 million --- Educational Adequacy (.875% tax)
-\$.036 million --- Property Tax Relief Trust Fund (.5%)
-\$.009 million --- Conservation Tax (.125%)
-\$.036 million --- Highway Fund (.5%)
-\$ 0 million --- Educational Excellence Trust Fund
-\$ 0 million --- Educational Adequacy (GR transfer)
-\$.011 million --- State Central Services
-\$.005 million --- Constitutional Officers
Total Impact to Local Sales Tax -\$.156 million

FY2015 Tax Decrease

Total Impact to State Revenues - \$.750 million

-\$.452 million --- State General Revenue (4.5%)
-\$.098 million --- Educational Adequacy (.875% tax)
-\$.056 million --- Property Tax Relief Trust Fund (.5%)
-\$.014 million --- Conservation Tax (.125%)
-\$.056 million --- Highway Fund (.5%)
-\$.046 million --- Educational Excellence Trust Fund
-\$.004 million --- Educational Adequacy (GR transfer)

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-\$.017 million --- State Central Services

-\$.007 million --- Constitutional Officers

Total Impact to Local Sales Tax -\$.240 million

Taxpayer Impact :

Sellers of project materials would exempt eligible sales and maintain records to substantiate the exemption claims.

Resources Required :

None

Time Required :

Adequate time is allowed in the proposal

Procedural Changes :

Education of staff of provision of the law and revise the sales tax rules.

Other Comments :

Regional Water Distribution Districts would be the only entity for which construction materials may be purchased free from sales tax by a construction contractor.

Legal Analysis :

Amendment S1 creates a sales tax exemption for construction materials purchased for use by a regional water distribution district (the "exempt entity") or for use by a contractor to construct, repair, or remodel a "facility to be used by the exempt entity in the conduct of the exempt entity's regular functions and activities." The bill does not define the term facility for purposes of determining whether or not the use of the materials would qualify for exemption. This is important because the provisions of Ark. Code Ann. §26-52-466(h)(2) would make the exempt entity responsible for payment of tax on any construction materials that are incorporated into or consumed in a project or part of a project that is found not to be related to the exempt entity's functions and activities.

The amendment requires exempt entities to register eligible projects with the Department for issuance of an exemption certificate for the project; however, the bill does not require the exempt entity to provide contractors with a copy of the exemption certificate nor does it require contractors to provide a copy of the exemption certificate to suppliers of construction materials purchased for the project. In order to avoid being taxed on the materials at the point of sale, contractors will have to provide sellers with a copy of the exemption certificate.

The amendment requires contractors to return any resaleable construction materials that are not consumed or incorporated into the project to a supplier for credit, and if the materials cannot be returned for credit, then the contractor will be responsible for the tax due on the materials. From a practical standpoint, a contractor may not be able to determine if materials are resaleable. If the contractor does not perform taxable services in Arkansas, it will not be registered to report and pay sales tax and it will be difficult for the contractors to comply with reporting and remittance requirements absent creation of new forms and temporary accounts in our computer system.