



## Common Ways to Limit the Impact of Arizona's Speculative Builder Tax

*This month's state and local tax (SALT) column addresses common ways to limit the impact of Arizona's speculative builder tax through the use of exclusions, exemptions, deductions, and more.*

Arizona cities and towns impose a privilege (sales) tax on speculative builders that operates much like a real estate transfer tax in some situations. However, as is often the case with other sales taxes, there are opportunities that limit the impact of Arizona's speculative builder tax. Many of those opportunities require planning ahead, as well as obtaining and maintaining copies of appropriate documentation — often including exemption certificates.

### Definitional Limitations

This local speculative builder tax only applies to sales of “improved real property” by “speculative builders.” As I explained in my column last month, sometimes legally planning around this tax simply involves postponing sales of certain types of property for a short time in order to avoid falling within the scope of those key terms.

### Tax Credits and Cost Shifting

When the tax does apply, it applies to 65 percent of the total selling price from the sale of the subject property after taking into account all available exclusions, deductions, exemptions, and credits.

The dollar-for-dollar tax credits identified in my column last month often are the most direct way to limit the amount of tax due. And, speculative builders who are aware of the tax can try to pass the cost of tax along to the party who purchases the property from them.

### Exclusions

While the definitional limitations, tax credits, and the idea of passing the cost of the tax along to one's buyer, if possible, apply in all Arizona cities and towns that impose speculative builder tax; exclusions from the tax vary from jurisdiction to jurisdiction.

For example, five cities or towns allow speculative builders to exclude the cost of land from their tax base, and 17 cities or towns allow speculative builders to exclude the fair market value of land from their tax base. However, most cities and towns that impose speculative builder tax do not allow speculative builders either of these exclusions.

One common exclusion available in all jurisdictions allows speculative builders that obtain the appropriate exemption certificate to shift the tax liability on residential lots or partially completed residential properties until substantial completion of the home.

Other common exclusions that are available in all jurisdictions allow speculative builders to exclude the “direct costs” of providing architectural or engineering services and to exclude the “prior value” of a property in cases of “reconstruction.”



by James G. Busby, Jr., CPA

**James G. Busby, Jr., CPA**, is a state and local tax attorney at The Cavanagh Law Firm. Busby previously worked in the SALT departments at Arthur Andersen and Deloitte & Touche. Before entering private practice, Busby was in charge of all transaction privilege (sales) tax audits at the Arizona Department of Revenue. If you have any questions, please contact the author. He can be reached at (602) 322-4146 or [JBusby@CavanaghLaw.com](mailto:JBusby@CavanaghLaw.com).

The City of Sierra Vista adapted a special exclusion for transactions located at Fort Huachuca.

### **Exemptions**

The most commonly used exemptions are for: (1) the cost of “income producing capital equipment” and tangible personal property used at a qualifying nonprofit hospital, community health center, or health care organization that is exempt or deductible from the municipal sales tax base for retailers; and (2) amounts attributable to “development fees” that are incurred in relation to the construction, development, or improvement of real property.

Exemptions also are available for contracts related to: (1) the construction of environmentally controlled facilities to raise poultry for the production of eggs; (2) the installation, assembly, repair, or maintenance of cleanrooms that are deducted from the municipal sales tax base for retailers; and (3) certain activities for persons engaged in activities regarding livestock, livestock products, crops, or crop products if the project is directly and primarily used to prevent, monitor, control, or reduce air, water or land pollution.

### **Deductions**

Arizona cities and towns allow just three deductions from the speculative builder tax. Namely, there are deductions for: (1) 35 percent of all amounts subject to tax (hence, the 65 percent tax base); (2) proceeds from installing, assembling, repairing, or maintaining “income producing capital equipment” that is deducted from the municipal sales tax base for retailers so long as the equipment does not become “permanently attached” to realty or a manufactured building; and (3) proceeds from a contract to provide and install a qualified solar energy device.

**Practice Tip!** — Speculative builders that enter into a contract to sell a property with one or more tenants in place may be able to reduce their tax base further by taking into account the portion of the sales price attributable to one or more leases that are in effect. ■