

# OWNER-BUILDERS AND SPECULATIVE BUILDERS

## WHO IS AN OWNER-BUILDER?

An owner or lessor who has improvements constructed on real property is an owner-builder whether he does the work himself or hires others to do the construction. (Mesa Tax Code 5-10-417)

## ARE OWNER-BUILDERS TAXED?

Owner-builders may or may not be liable for tax. Generally, owner-builders who sell property or who claim exemptions from tax during construction may be liable for tax in addition to tax paid by their contractors. Owner-builders should be aware of the circumstances that will result in a tax liability.

Transactions between related companies or persons are taxable by the City of Mesa. See Mesa City Code Section 5-10-100 for the definition of a "Person", Section 5-10-210 "Determination of gross income: transactions between affiliated companies or persons", and Section 5-10-220 "Determination of gross income: artificially contrived transactions".

## OWNERS BUILDING IMPROVEMENTS FOR THEIR OWN USE

Owner-builders who are building improvements for their own use are not normally the parties liable for the tax on construction contracting. Each of the contractors and suppliers who provide materials and/or services would be liable based on their income from the job. Such owner-builders should not claim a tax exemption from their contractors or suppliers.

## OWNER BUILDERS WHO ARE SPECULATIVE BUILDERS

A speculative builder is an owner-builder who sells or contracts to sell improved real property: (Mesa Tax Code 5-10-416)

- Prior to completion of construction, or
- Within 24 months after substantial completion of construction, or
- At any time for custom, model, or inventory homes, or
- At any time for improved residential or commercial lots without a structure

Owner-builders who are constructing improvements for sale may obtain a TPT license and claim a tax exemption from their contractors and suppliers. If the owner-builder does not claim an exemption, he may claim a credit for city taxes that have been paid to his contractors and suppliers.

An owner-builder who does not sell a property within the applicable 24 month period would owe tax in the 25th month based on the total cost of construction, less a credit for city taxes previously paid to suppliers and contractors.

## SALE OF A PERSONAL RESIDENCE

A homeowner may be exempt from the speculative

builder tax if they sell a residence they lived in for the six months prior to the offer for sale. This exemption is subject to some limitations including:

- The seller cannot have sold more than 2 such residences in the past 3 years.
- The property cannot have been rented in the past 2 years.

## TAX RATE ON SPECULATIVE BUILDERS

The Mesa tax rate is 2.0% of the taxable income.

## INCOME

The gross income is the full sales price of the improved real property at close of escrow or transfer of title, whichever occurs earlier.

## DEDUCTIONS

The speculative builder is entitled to certain deductions from gross income as noted below. The speculative builder should retain records of the tax paid during construction, and other fees, in order to document these deductions, as well as keeping copies of invoices showing tax was charged. Many contractors may not list tax as a separate charge on their invoices. As such, owners should obtain statements from their contractors stating the amount of state, county and city tax they paid on their income from the project and the period it was reported to the Department of Revenue. Any deduction may be subject to verification. A full listing of deductions and codes can be found at: <https://azdor.gov/transaction-privilege-tax/deduction-codes>

- The actual direct cost of Architectural & Engineering (A/E) Services included in a construction contract. (Deduction Code 557)
- Development (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. NOTE: Only Development/Impact fees are allowed, not other permitting fees. (Deduction Code 560)
- All state and county TPT taxes associated with the project and reported and paid to the Department of Revenue by a contractor constructing the improvements on the property (deduction Code 802)
- Effective 4/1/19, the gross proceeds of sales or gross income that is derived from the value of existing tenant leases in place at the time of the sale shall be exempt from tax imposed under this section. The value of the in-place leases shall be determined as of the close of escrow or transfer of title as prescribed per the Model City Tax Code Section 416 (<https://modelcitytaxcode.az.gov/articles/4-416.htm>). (Deduction Code 801)
- After reducing gross income by allowable deductions (State/County TPT paid by contractor,

*(continued on next page)*

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A/E fees, Development Impact Fees and any in-place lease, etc.), a city tax factor deduction is allowed prior to the 35% standard deduction (the current Mesa Speculative Builder tax factor rate for 2 % is .01283317). (Deduction Code 551)

- All amounts subject to the tax shall be allowed a deduction in the amount of 35%. This deduction should be computed after any other allowable deductions and after the sales tax factor deduction has been subtracted, as noted above. (Deduction Code 502)

## CREDITS

The speculative builder tax supplements the tax on construction contracting. The taxpayer is entitled to a credit for the city TPT tax that was paid by contractors, suppliers, and land developers during construction on the property (not the cost of land).

Taxpayers should retain records of the tax they paid during construction in order to document their credits and keep copies of invoices showing that tax was charged. Many contractors may not list tax as a separate charge on their invoices. As such, owners should obtain statements from their contractors indicating the amount of state, county and city tax paid on their income from the project and the period it was reported to the Department of Revenue. Any credit may be subject to verification.

## EXAMPLES

- An investor buys a commercial lot and hires a contractor to build a shopping center. They enter into a contract to sell the shopping center 23 months after completion of construction and close on the sale two months later. They owe tax based on the full sales price less applicable deductions and credit for tax paid by the contractor for the construction of the building and for the improvements completed by the land developer (not the cost of the land).
- The above investor does not enter into a contract to sell the property until after the 24th month of completion. They do not owe any speculative builder tax. The contractor would still owe tax on the construction contract.
- A homeowner (individual) buys a lot and hires various contractors to build a home. They move into the home and live in it for 7 months after completion. They then advertise the house for sale and it later sells. They do not owe any speculative builder tax (Refer to Mesa Regulation Section 5-10-416.1 regarding a bona fide residence) . Assuming the individual did not issue any exemption certificates, tax would be paid by the contractors on the cost plus their profit.
- The same individual above moves into the home and after one month lists the home for sale; four months later they sell the home. The individual is taxable upon the full sales price of the home, less any applicable deductions and credits for taxes

paid by the contractor(s) on the construction of the home and/or the development of the land (not the land cost) (Refer to Mesa Regulation Section 5-10 -416.1 regarding a bona fide residence).

- A Developer buys a piece of land and subdivides it into ten residential lots. They have streets and utilities built to the lot lines. They sell five lots to a construction company who provides them with an exemption certificate. The remaining lots are sold over five years to individuals to build homes. The first five lots are exempt, with the proper exemption form kept on file, since the construction company will pay on these later. The remaining five lots are taxable to the Developer regardless of how long after completion they are sold.

## REPORTING YOUR TAX LIABILITY

Speculative builders with a valid Arizona Department of Revenue TPT license may report their activity on the same tax return they report other business activities (Business Code 016). Those with no TPT license will need to obtain the proper license via the Arizona Department of Revenue (aztaxes.gov or azdor.gov) to report and pay the tax. For assistance in computing the tax, call the Mesa Tax Audit Department at (480) 644-3816.

## CITY RULES DIFFER FROM STATE RULES

The Arizona Department of Revenue’s laws do not contain the same provisions relating to speculative builders. Owner-builders should contact the Arizona Department of Revenue about the consequences of a sale for purposes of state and county taxes on construction contracting. For additional information, see the Model City Tax Code Guideline TG 2001-01 at:

<https://modelcitytaxcode.az.gov>.

*This is an informal and nonbinding communication. This publication is for general information only about Transaction Privilege (Sales) Tax on owner-builders and speculative builders. For complete details, refer to the City of Mesa 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 Mesa and is not a true sales tax.*

**TPT LICENSING Information:**  
Arizona Department of Revenue  
<https://www.aztaxes.gov>

**MESA TAX Information:**  
480.644.3816  
[salestax.info@mesaaz.gov](mailto:salestax.info@mesaaz.gov)



**MESA TAX AUDIT**  
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