

## COMPLYING WITH NEW JERSEY'S SALES AND USE TAX LAWS

By David L. Ferullo, CPA

The New Jersey Division of Taxation has targeted several industries over the past several years for sales and use tax audits. In addition, as part of the Division's regular audits of corporations, the sales and use tax portion of the audit continues to be a lucrative source of additional revenue for the State. Contractors need to be aware of these laws and the potential of incurring significant interest and penalties on additional taxes resulting from one of these audits.

A contractor is defined as an individual or business entity engaged in the business of constructing, improving, altering or repairing the land, buildings, or other property of others. Included under this definition are subcontractors and fabricator/contractors.

Under New Jersey's sales and use tax laws, contractors have special responsibilities. Work performed by a contractor is categorized as a capital improvement, repair or a maintenance service. Rules governing the payment and/or collection of sales tax vary under each of these categories.

For New Jersey sales tax purposes, contractors are considered to be the actual consumer of the material and supplies used in construction, improving, altering or repairing of real property or others. Therefore, they are required to pay sales or use tax to suppliers on the purchase of materials and supplies used in fulfilling contracts. An exception to this is if they are purchased for use in performing work on real property of an exempt organization, a qualified business in an Urban Enterprise Zone or a qualified housing sponsor.

Contractors are also required to pay sales tax on the purchase or rental of construction equipment for an initial contract term of 28 days or less. This even applies to equipment used on a contract with an exempt organization. The sales tax charged under this type of transaction can vary. If the equipment is rented without an operator, the amount of the rental is taxable. If rented with an operator and the invoice separately states the charge for the operator, only the charge for the equipment is taxable. If, however, the invoice does not separate the operator's charge, the entire invoice is taxable. On leases of construction equipment with an initial contract term of 28 days, the lessor (owner of the property) is liable for tax.

Many contractors conduct business outside of New Jersey. If materials, supplies and equipment are purchased in New Jersey and delivered to the out of state job site by the supplier, these purchases are not taxable. However, if the contractor accepts delivery in New Jersey, they are subject to sales tax.

One of the most overlooked taxes is the Use Tax. The Use Tax is a tax imposed on the purchase of goods and services on which sales tax was not collected, or was collected at a rate less than the New Jersey sales tax rate. Under the New Jersey Sales and Use Tax Act the contractor is required to calculate the tax on out of state purchases using the prevailing New Jersey sales tax rate at the time of purchase. If the contractor paid an out of state sales tax less than New Jersey's prevailing sales, tax he would be responsible for the difference between the rate paid and New Jersey's rate. Once the contractor determines any use tax owed, it would be included on his sales tax returns.

As indicated above, contractors who perform work for an exempt organization may purchase material and supplies for jobs without paying sales tax. To accomplish this the contractor must obtain or prepare a valid New Jersey exemption certificate. The most frequently used exemption certificates used in the construction industry are: Resale Certificate (Form ST-3), Exempt Use Certificate (Form ST-4), Exempt Organization Certificate (Form ST-5) Certificate of Capital Improvement (Form ST-8), Contractor's Exempt Purchase Certificate (Form ST-13) and Contractor's Exempt Purchase Certificate – Urban Enterprise Zone (Form ST-UZ-4).

Examples of such organizations include the State of New Jersey or any of its agencies or political subdivisions, the United States of America or any of its agencies, the United Nations or any international organization of which the United States is a member or certain nonprofit organizations which have been

granted exempt status by the Division of Taxation. These include churches, charitable organizations and fire and rescue squads.

In summary, contractors are responsible for the collection of sales tax from property owners. How the tax is determined is based upon the type of work performed. Contractors performing capital improvements to real property pay the sale tax on the purchases of materials and supplies and do not charge sales tax on labor. Work performed by a contractor in maintaining, servicing or repairing real property is taxable and the contractor is required to charge sales tax on the labor portion of the invoice. If, however, the invoice does not separately state the labor and material, the contractor must charge and collect sales tax on the entire amount of the invoice.

Every contractor should be aware of the current reporting requirements under the New Jersey Sales and Use Tax Act. Additional information may be obtained by accessing the Division's home page at [www.state.nj.us/treasury/taxation/](http://www.state.nj.us/treasury/taxation/) .

#### About the Author...

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