



## Testimony—

### Political Subdivision Taxation Interim Committee

### Fiscal Impact of Sales Tax Exemption on Construction Contracts with Exempt Entities

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The schedule on page 3 estimates the total reduction in both state and local sales taxes for the 2017-19 biennium if all material used in construction contracts with exempt entities were exempt from sales and use taxes. An exempt entity is defined as an entity that has been issued a sales and use tax exemption certificate by the Tax Commissioner's Office and is exempt from paying sales and use taxes on purchases made on its own behalf. The schedule is the same information presented on March 1 except it includes additional information regarding local sales and use taxes.

Local sales and use taxes on construction contracts are difficult to estimate for the following reasons:

- The 137 city and 7 county sales and use taxes imposed in North Dakota are levied at various rates ranging from ½ to 3 percent. In addition, some contracts apply to areas where no local taxes exist.
- Most (but not all) local sales and use tax ordinances limit the amount of tax that may be imposed on a single transaction (invoice). Maximum tax amounts range from \$12.50 to \$50 on any single invoice.

The following facts and assumptions were used to estimate local sales and use taxes that would be imposed on construction contracts with tax exempt entities for the 2017-19 biennium:

- Local sales taxes collected during fiscal year 2015 were 18 percent of state taxes. Total state sales tax collections were \$1.409 billion and total local tax collections were \$258.1 million. ( $\$258.1\text{M} / \$1.409\text{B} = 18.3\%$ )
- Local sales taxes are frequently limited to roughly \$2,500 of purchase price regardless of how large the purchase may be. Common local sales tax caps range from \$25 to \$50 depending on the tax rate. This is not true in all cases, but is the norm. The bulk of material purchases made for large construction contracts are made in very large purchases that are capped by the local tax ordinances.
- For purposes of this estimate, we assumed that local tax caps reduce the local tax due on construction contracts to half of the state-wide average rate, or 9 percent.
- Because state highway projects are frequently outside of local taxing jurisdictions, we reduced the local tax rate on highway projects to 4.5 percent of state tax collections, or one-half of the rate applied to all other types of construction projects.

In summary, this estimate of local taxes assumes that the local tax due on construction contracts is 4.5 percent of the state tax amount for highway contracts and 9 percent of the state tax on all other contracts.

**Summary of Fiscal Impact - Sales Tax Exemption  
Construction Contracts with Exempt Entities**

(millions of dollars)

Category of Contracts	Annual Estimated Contracts	Total Biennium Contracts	Estimated Material Cost (30 %)	ND State Sales Tax	Local Sales Tax	Impact
North Dakota estimated highway project contracts	\$ 800	\$ 1,600	\$ 480	\$ 24.00	\$ 1.08	Revenue lost to state and political subdivision. Reduced state project costs. Reduced state appropriations to offset state revenue loss. <sup>1</sup>
Higher education facility estimated project contracts	68	136	41	2.05	0.18	
Other state agency facility estimated project contracts	40	80	24	1.20	0.11	
Subtotal				\$ 27.25	\$ 1.37	
County, city and township road, street, water, sewer, light estimated contracts	200	400	120	6.00	0.54	Revenue lost to state and political subdivision. Reduced project costs for political subdivision. Reduced local taxes for North Dakota taxpayers. <sup>1</sup>
Primary and secondary school estimated contracts	190	380	114	5.70	0.51	
Subtotal				\$ 11.70	\$ 1.05	
Federal government contracts in North Dakota	126	252	76	3.80	0.34	Revenue lost to state and political subdivisions. No direct offsetting benefit to North Dakota taxpayers in state or local taxes.
Hospital, nursing homes, intermediate care, basic care, assisted living, and emergency service provider estimated contracts	50	100	30	1.50	0.14	
Subtotal				\$ 5.30	\$ 0.48	
				<u>\$ 44.25</u>	<u>\$ 2.90</u>	

<sup>1</sup> Assumes state appropriations or local property tax is reduced by the amount of sales tax savings.