

Nebraska Taxation of Contractors Option 3

Overview

This guide provides an overview of the:

- ❖ Sales and use tax provisions for contractors operating under Option 3; and
- ❖ Option 3 contractor's responsibilities under the Contractor Registration Act administered by the Nebraska Department of Labor.

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Terms

Annexed. Annexed to real estate means attaching property so that: (1) the property becomes real estate, or (2) the installation or removal of the property requires specialized skills or tools and is performed or supervised by a recognized trade professional.

Building Materials. Building materials means any property that will be annexed to real estate or to an improvement on real estate. Examples include lumber, drywall, insulation, roofing materials, slope protection mulch like hay or straw, grass seed, erosion control netting, and soil retention blankets.

Building materials do **not** include tools, supplies, property, equipment, sod, live plants, and other items that will **not** be annexed to real estate.

Contractor. Contractor is any person who repairs property annexed to real estate, who annexes building materials and fixtures to real estate, or who arranges for this annexation.

A contractor who elects Option 3 is the consumer of building materials and fixtures purchased and annexed to real estate.

Demarcation point. Demarcation point is the point at which the wires, cables, and equipment that are owned and maintained by the telephone, telegraph, cable, or mobile telecommunications company are connected to the wiring or equipment dedicated to the customer's use.

Fixtures. Fixtures are items that must be annexed to a building or structure in order to properly function, yet remain identifiable as separate items. Examples include water heaters, furnaces, central air conditioners, and built-in dishwashers.

Nonresident Contractors. A nonresident contractor is a contractor who is neither domiciled in, nor maintains a place of business in, Nebraska for more than six months of a year. Nonresident contractors have the same tax responsibilities as resident contractors.

Recognized Trade Professional. A recognized trade professional includes any person required to be licensed or certified by the state to practice his or her trade, like a plumber or electrician.

Service Provider. A service provider includes a telephone, telegraph, mobile telecommunications, satellite, or community antenna television company.

Use Tax. Use tax is a complement to the Nebraska sales tax. It is imposed at the same rate and on the same transactions as the sales tax. Certain locations in Nebraska have enacted a local sales tax in addition to the state sales tax. Local use tax is due whenever Nebraska use tax is owed.

Electing a Contractor Option

All resident and nonresident contractors can elect a contractor option by completing the Nebraska Department of Labor's online Contractor/Subcontractor Registration Application located at dol.nebraska.gov.

Contractors who do not elect a contractor option will be treated as a retailer under Option 1.

The contractor/subcontractor database registration information including the contractor option is displayed in the database.

Option 3 contractors must:

- ❖ Register in the Contractor Registration Database (Database) and elect contractor Option 3. (see section titled "Contractor Registration Act - Nebraska Department of Labor" on page 7);
- ❖ Obtain a Sales Tax Permit and a Withholding Tax Certificate by filing a [Nebraska Tax Application, Form 20](#). The same Form 20 can be used to apply for the sales tax permit and the withholding certificate;
- ❖ Remit use tax on the cost of building materials and fixtures based on the rate in effect at the time and place of withdrawal from inventory;
- ❖ Collect and remit the Nebraska and local sales tax on over-the-counter sales and charges for taxable services; and
- ❖ Withhold 5% of all payments made to other contractors and subcontractors who are not registered in the Database (see section titled "Contractor Registration Act – Nebraska Department of Labor" on page 7).

Labor Charges

Option 3 contractor labor charges are not taxable. In addition, Option 3 contractors who fabricate, produce, or repair building materials that they subsequently annex to real property will not collect sales tax on these labor charges.

Option 3 contractors are not required to obtain a [Nebraska Resale or Exempt Sale Certificate, Form 13](#), from other contractors to exempt their contractor labor charges from tax.

Option 3 contractors must pay sales tax or remit use tax on fabrication, production, or repair labor performed by another person on building materials which are annexed to real estate by the Option 3 contractor. (Reg-1-082, Labor Charges.)

Building Materials and Fixtures

Option 3 contractors:

- ❖ Can purchase building materials and fixtures without paying sales tax at the time of purchase;
- ❖ Must remit use tax on all building materials and fixtures removed from inventory for annexation to real estate;
- ❖ Must collect sales tax on retail sales of building materials and other property that is not annexed.

When making tax exempt purchases of building materials and fixtures, Option 3 contractors must give their suppliers a properly completed [Form 13](#), with Section C, Block 1 filled in.

Option 3 contractors owe use tax on their cost of all building materials and fixtures purchased and annexed by them to real estate. The use tax is due at the rate in effect at the time and place the building materials and fixtures are withdrawn from tax exempt inventory, regardless of the rate in effect at the time of purchase or the rate in effect at the job site. Building materials and fixtures delivered by a supplier to the job site are taxed at the rate in effect at the job site.

Option 3 contractors are required to remit use tax on building materials and fixtures withdrawn from inventory in Nebraska for annexation to real estate in another state **unless** the building materials and fixtures were purchased from an out-of-state supplier who is not required to collect Nebraska tax.

Tools, Equipment, Supplies, and Taxable Services

Tools, equipment, and supplies used in completing a construction or repair project do not become part of the real estate, structure, or fixture. Option 3 contractors are the consumers of all tools, equipment, and supplies used in completing their construction projects, **including any project for an exempt entity**. Option 3 contractors must pay sales tax on all items purchased, rented, or leased by them for use in their construction projects – including installation, assembly, disassembly, delivery, and any other charge associated with purchasing or renting these items.

Example 1. Taxable tools, equipment, and supplies includes hammers, sandpaper, lumber to build forms, office equipment, blue prints, scaffolding, backhoes, cement mixers, and safety equipment like barriers, fences, and caution tape.

An Option 3 contractor's purchase of certain services (for example, building cleaning services, pest control services, and security services) are taxable. Each of these services is specifically taxed in statute, and persons providing these services are **not** performing contractor labor. Option 3 contractors are the consumers of these services and cannot purchase these services tax exempt for resale.

Option 3 contractors must pay sales tax or remit use tax on the equipment, tools, and services listed above even on a project performed for an exempt entity or governmental unit. Use tax is commonly due on the purchase or rental of items and services from out-of-state retailers.

Barricades and Other Items Rented or Leased to Contractors

Companies who provide barricades, high intensity lights, arrow boards, cones, and other equipment to Option 3 contractors are leasing these items. These companies are required to collect sales tax on the total amount charged for the equipment and any services included in the lease agreement to place, move, clean, maintain, remove and repair the items.

Option 3 contractors cannot use a [Form 13](#), or a [Purchasing Agent Appointment, Form 17](#), issued by an exempt entity or governmental unit to exempt the rental of these items from tax. Tax is due regardless of whether these items are required at the job site to comply with governmental or private contract specifications or to protect workers and provide traffic control.

Billing Another Contractor

Option 3 contractors will not collect tax from another contractor on any portion of their bills.

Billing the Project Owner

Option 3 general or prime contractors who bill the project owner will not collect sales tax on any portion of the invoice relating to the repair or improvement of real estate.

Example 2: An Option 3 contractor is hired to replace a kitchen sink. The invoice to the customer should state:

Materials and labor	<u>\$1,500</u>
Total amount due	\$1,500

Example 3: An Option 3 contractor is hired as a general contractor to remodel a kitchen for \$30,000. The project is located in a city with a 1.5% local tax rate for the total state and local rate of 7%. The Option 3 general contractor will provide and install new cabinets. The Option 3 general contractor hires an Option 1 electrician and an Option 2 or Option 3 plumber. The Option 1 electrician must collect sales tax from the general contractor on its **separately** stated charge for building materials.

Sample invoice from the Option 1 electrician to the Option 3 general contractor:

Labor	\$2,000
Materials (wire, lights)	600
Sales tax (\$600 x 7%)	<u>42</u>
Total amount due	\$2,642

If the Option 1 electrician chooses to charge a single amount for both its materials and labor, the total charge is taxable.

An Option 3 contractor cannot purchase annexed building materials and fixtures tax exempt for resale from an Option 1 subcontractor.

Regardless of its billing method, the Option 2 or Option 3 plumber will not collect sales tax from the general contractor on any portion of its bill as a separately stated charge. The tax previously paid by the Option 2 or Option 3 contractor should be included in its materials and labor charge.

Sample invoice from an Option 2 or Option 3 plumber to the Option 3 general contractor:

Plumbing for kitchen remodel	<u>\$3,000</u>
Total amount due	\$3,000

The Option 3 general contractor will not collect sales tax on any portion of its bill.

Sample invoice from the Option 3 general contractor to the project owner:

Materials and labor for remodeled kitchen	<u>\$30,000</u>
Total amount due	\$30,000

Contracts with Exempt Entities

Most nonprofit organizations are **not** exempt from sales tax in Nebraska. In addition, not all governmental units are exempt from Nebraska sales tax. The following Nebraska Sales and Use Tax Regulations identify those entities that are exempt from sales and use tax:

[Reg-1-072](#), United States Government and Federal Corporations;

[Reg-1-090](#), Nonprofit Organizations;

[Reg-1-091](#), Religious Organizations;

[Reg-1-092](#), Educational Institutions; and

[Reg-1-093](#), Governmental Units.

Option 3 contractors who perform work for a qualified exempt entity or an exempt governmental unit must obtain a [Purchasing Agent Appointment, Form 17](#), from the exempt project owner. The Form 17 must be completed and issued before any building materials are annexed.

Note: Except for a Nebraska irrigation or reclamation district, exempt governmental units and departments or portions of the governmental unit that provide electricity, gas, heat, or water services must pay tax on all purchases of materials, supplies, and other property or services used in providing their services. Governmental units providing these services cannot issue a Purchasing Agent Appointment, Form 17, to their contractors. Option 3 contractors must continue to remit use tax on building materials incorporated into their projects.

Exempt governmental units and departments or portions of the governmental unit that provide sewer services are exempt on all purchases of materials, supplies, and other property or services used exclusively in providing sewer services. Governmental units providing sewer services can issue a Purchasing Agent Appointment, Form 17, to their contractors.

Receipt of the Form 17 removes the use tax liability from the Option 3 contractor on any building materials and fixtures withdrawn from inventory and annexed to the specific project identified on the Form 17. The Form 17 **cannot** be used to purchase or lease tax exempt any tools, equipment, supplies, barricades, or other items that will not be annexed to real estate.

Manufacturing Machinery and Equipment

Option 3 contractors are consumers of all manufacturing machinery and equipment purchased and annexed by them. Option 3 contractors must pay tax on purchases of machinery and equipment even if the machinery and equipment will be used by a manufacturer.

Option 3 contractors who repair manufacturing machinery and equipment must pay tax on the repair or replacement parts. Option 3 contractors will not collect sales tax on charges to install, repair, or maintain qualified manufacturing machinery and equipment.

Landscaping

Landscapers performing work as a contractor must elect a contractor option and register in the Database (see section titled “Contractor Registration Act – Nebraska Department of Labor” on page 7).

Landscapers should also review the [Nebraska Sales and Use Tax Information Guide for Landscapers](#). This guide reviews the various retail sales and tax exempt services landscapers provide, in addition to performing work as a contractor.

Telecommunications Services

Telecommunications services include the installation, construction, repair, replacement, upgrading, or removal of telephone, telegraph, mobile telecommunications, or community antenna television (cable) property used in conjunction with furnishing, installing, or connecting telephone, telegraph, mobile telecommunications, satellite, and community antenna television (cable) services. Option 3 contractors must remit use tax on all of their purchases of wire, cable, outlets, and other property used to install or construct telephone, telegraph, cable, satellite, and mobile telecommunications services.

Service Provider’s Side of the Demarcation Point

Option 3 contractors who install, construct, service, repair, replace, upgrade, or remove outlets, wire, cable, satellite dishes or receivers, or any other property used in conjunction with furnishing, installing, or connecting telephone, telegraph, mobile telecommunications, satellite, or cable services on the service provider’s side of the demarcation point must collect sales tax on the total amount charged for the materials and labor even though the property is annexed to real estate.

Option 3 contractors who only perform trenching and boring services are not required to collect any sales tax on the charges provided that no materials are annexed by the Option 3 contractor.

The charge for the trenching services are not taxable even if the trenching company back-fills the trench after the materials are placed in the trench by some other company.

The amount charged by the company performing the trenching or boring services is not taxable if billed to another contractor, telephone company, mobile telecommunications company, or cable company. However, the total amount charged by the general contractor for installing, constructing, servicing, or removing property used in conjunction with furnishing, installing, or connecting telephone, telegraph, mobile telecommunications, or cable services is taxable.

Customer's Side of the Demarcation Point

Option 3 contractors hired by a telephone, telegraph, cable, or mobile telecommunication service provider who install, construct, service, repair, replace, upgrade, or remove outlets, wire, cable, or any other property on the customer's side of the demarcation point must collect sales tax on the total amount charged for the materials and labor even if the property is annexed to real estate.

Option 3 contractors hired by a company that is not a telephone, telegraph, cable, satellite, or mobile telecommunications service provider will not collect sales tax on the amount charged to install, construct, service, repair, replace, upgrade, or remove outlets, wire, cable, or any other property on the customer's side of the demarcation point.

Example 4. A telephone or cable company contracts with an Option 3 contractor to install telephone wire/cable and outlets throughout a building. The telephone wire/cable runs from the customer's side of the demarcation point to a panel and from the panel throughout the ceiling and walls to each outlet.

The Option 3 contractor will collect sales tax from the telephone company on the total amount charged for the materials and the amount charged to install the wire and outlets regardless of whether the property is annexed or remains tangible personal property.

Example 5. The owner of a building hires an Option 3 contractor to install telephone wire/cable throughout the building. The telephone wire/cable runs from the customer's side of the demarcation point to a panel and from the panel throughout the ceiling and walls to each outlet.

The Option 3 contractor will not collect sales tax from the owner of the building on the total amount charged for the materials and labor charges to install the telephone wire/cable throughout the building regardless of whether the property is annexed to the real estate.

Example 6. An electrician hires an Option 3 contractor to install coaxial cable that will only carry data from computer to computer in the same building. The wire runs through the ceiling and walls to the computer equipment.

The data lines are annexed property and the Option 3 contractor will not collect sales tax on the total amount charged to the electrician.

Other Retail Sales

Building Cleaning Services. Option 3 contractors who, in addition to their construction work, perform building cleaning services are retailers. Option 3 contractors must collect and remit sales tax on the total amount charged for the building cleaning services. Sales tax must also be paid on purchases of equipment and supplies used in performing these services.

Building cleaning services include, but are not limited to, cleaning central air conditioning units, furnaces, sewers, drains, and any property located in or attached to a building. Please refer to [Nebraska Sales and Use Tax Regulation 1-098](#), Building Cleaning and Maintenance, for additional information.

Over-the-Counter Sales. Over-the-counter sales are transactions where the terms of the sale do not require the Option 3 contractor to annex building materials or fixtures to real estate, or to arrange for the annexation.

Example 7: Customer buys a faucet, takes it home and either installs it, or makes arrangements with someone other than the Option 3 contractor to install it.

Option 3 contractors making over-the-counter sales must collect the Nebraska and applicable local sales tax on the **total** sales price, including all amounts charged to build or assemble the item sold.

Warranties, Guarantees, and Service and Maintenance Agreements. Sales of warranties, guarantees, and service or maintenance agreements that only cover the repair of buildings and fixtures are not taxable.

Example 8. Warranties, guarantees, and service and maintenance agreements that only cover repairs to a building or to fixtures, such as hot water heaters, garbage disposals, and central heating and air conditioning units are not taxable.

Option 3 contractors must pay or remit tax on their cost of the parts and materials used to replace or repair annexed property or fixtures whether or not covered by the warranty or service agreement.

If an agreement which covers both building materials, fixtures, and tangible personal property, such as appliances, is sold for one amount, the entire amount charged for the agreement is taxable. See above paragraphs for the taxability of parts used for repairs to building materials and fixtures. Sales and use tax does not apply to parts and building materials used, and services performed, in fulfilling the obligations under an agreement to repair or replace tangible personal property, provided there is not an additional charge for these items.

If an agreement that covers buildings or fixtures and building cleaning services is sold for one amount, the entire amount charged for the agreement is taxable.

Contractor Registration Act – Nebraska Department of Labor

The Nebraska Contractor Registration Act (Act) is administered by the Nebraska Department of Labor. The Act requires contractors, subcontractors, and nonresident contractors performing construction work in Nebraska to be registered with the Nebraska Department of Labor. Nonresident contractors are also required to register each project and pay the appropriate fees. Nonresident contractors are not required to post a bond to register their projects.

Who is a Contractor?

Contractors that must be registered in the contractor registration database are defined in [Neb. Rev. Stat. §§ 48-2103](#) and [77-2701.10](#) and include:

- ❖ Any person who repairs property annexed to real estate, who annexes building materials and fixtures to real estate, or who arranges for this annexation, and
- ❖ Any individual, firm, partnership, limited liability company, corporation, or other association of persons engaged in the business of the construction, alteration, repairing, dismantling, or demolition of buildings, roads, bridges, viaducts, sewers, water and gas mains, streets, disposal plants, water filters, tanks and towers, airports, dams, levees and canals, water wells, pipelines, transmission and power lines, and every other type of structure, project, development, or improvement within the definition of real property and personal property, including such construction, repairing, or alteration of such property to be held either for sale or rental. Contractor also includes any subcontractor engaged in the business of such activities and any person who is providing or arranging for labor for such activities, either as an employee or as an independent contractor, for any contractor or person.

How Does a Contractor Register?

Contractors must register in the database maintained by the Nebraska Department of Labor. Registration must be completed online at dol.nebraska.gov/LaborStandards.

What is the 5% Withholding and Reporting Requirement?

[Neb. Rev. Stat. § 77-2753](#) requires all contractors making a payment or payments to another contractor or subcontractor as defined under the heading “Who is a Contractor?,” and not listed in the database, to withhold and remit 5% of all payments made to other contractors or subcontractors including those contractors who are not required to be registered under the Act because they receive payments for construction services less than \$5,000 annually.

Example 9. A general contractor who has been hired to build a new building, hires ABC Company to demolish a building. ABC Company is a contractor as defined under the Act. The general contractor must withhold 5% of the payments made to ABC Company, unless ABC Company is registered in the database.

Reporting the 5% Income Tax Withholding. The 5% income tax withholding may be in addition to any other state income taxes withheld on payments made to employees, including nonresidents for services performed in this state.

Contractors are required to file Nebraska income tax withholding returns and remit the amount of withholding with those returns. The primary income tax withholding returns are the Nebraska Withholding Return, Form 941N, and the Nebraska Reconciliation of Income Tax Withheld, Form W-3N. In addition, Form 1099-MISC must be issued to subcontractors at the end of the year.

Who Needs to Provide the Registration Confirmation?

Either contractor. The contractor who is making the payment or payments to another contractor is required to withhold 5% of each payment made to another contractor that is not listed in the database. All contractors should locate their registration information in the database and provide it to the contractor paying them. A contractor who has not received this confirmation must verify that the contractor performing the construction work is listed in the database, which releases them from the responsibility of the 5% withholding requirement.

If you have other questions regarding the contractor registration database, please review the Department’s [Contractor FAQs](#).

General Tax Information

Use Tax. Use tax is remitted directly to the state by the purchaser when sales tax has not been collected on taxable transactions by the seller. Please refer to the [Nebraska Use Tax Information Guide](#) for more information.

Reporting and Remitting Sales and Use Tax. Option 3 contractors who have a sales tax permit can use their [Nebraska and Local Sales and Use Tax Return, Form 10](#), to remit sales tax they collect from their customers, as well as any use tax owed. Electronic filing of the Form 10 is encouraged.

Option 3 contractors who do not have a sales tax permit but have a use tax liability to report must file a [Nebraska and Local Use Tax Return, Form 2](#).

Changing Your Contractor Option. Option 3 contractors may change their contractor option by using the Department of Labor’s website at dol.nebraska.gov for contractor/subcontractor registration. Option 3 contractors cannot operate under more than one option at a time. The new contractor option applies to all contracts in progress and also to all new contracts.

Option 3 contractors with a tax-free inventory, who are changing to Option 2, which requires a tax-paid inventory, must remit tax on all building materials and fixtures in inventory at the time the change becomes effective. Documentation indicating the tax calculation and the tax payment must be sent to the Nebraska Department of Revenue when the change in its contractor option becomes effective.

Record Keeping. Contractors are required to keep all [Forms 13](#), [Forms 17](#), construction contracts, building permits, sales invoices, purchase invoices and any other information necessary to accurately describe and document the construction that was completed. Additional record keeping requirements can be found in [Sales and Use Tax Regulation 1-008](#).

Other Information. Contractors seeking additional information are encouraged to review the resources contained on the Department's website under Contractor Information. The Department also conducts educational seminars (dates are posted on the Department's website, revenue.nebraska.gov).

Resource List

Information Guides

- ❖ [Nebraska Taxation of Contractors General Information](#)
- ❖ [Nebraska Taxation of Contractors – Option 1](#)
- ❖ [Nebraska Taxation of Contractors – Option 2](#)
- ❖ [Income Tax Withholding for Nonresident Individuals Performing Personal Services in Nebraska](#)

Nebraska Sales and Use Tax Regulations

- ❖ [1-017, Contractors](#)
- ❖ [1-098, Building Cleaning and Maintenance Services](#)
- ❖ [1-100 Pest Control Services](#)

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