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NOTICE 15-02

RECENT LEGISLATION INCREASES THE KANSAS STATE SALES AND USE TAX RATE FROM 6.15% TO 6.5% EFFECTIVE JULY 1, 2015

June 22, 2015

The Kansas state sales and use tax rate will increase from 6.15% to 6.5% on July 1, 2015. This Notice explains how the rate increase affects the collection and reporting of sales and use tax by Kansas retailers. The department will issue a separate notice that explains other changes to Kansas tax laws made this session. Please review our website periodically for these updates.

The new law contains a transition provision for binding written construction contracts entered into before May 1, 2015. When applied for and properly documented before July 10, 2015, the transition provision allows the 6.15% rate to apply to material purchases and labor service charges for a qualifying construction contract made after the July rate increase.

Notice 15-03 explains adjustments that certain retailers will need to make to correctly report taxable retail sales billed to customers at the 6.15% rate that are being reported on their July return (due date August 25, 2015).

When this Notice indicates the 6.15% or 6.5% state tax rate applies, retailers are required to charge customers a combined tax rate that equals the sum of the appropriate state rate *plus* all applicable local tax rates. When used in this notice, "goods" means "tangible personal property" as defined in K.S.A. 79-3602(pp). "Services" means services that are taxable under K.S.A. 79-3603. *K.S.A. 79-3602(nn).*

The following guidelines apply to retail sales of goods:

- **Tangible personal property ordered before July 1, 2015 but delivered on or after July 1, 2015** - For Kansas sales tax purposes, a sale of goods is presumed to take place when and where possession of the goods sold are delivered to the buyer. When goods are ordered before July 2015 but possession is transferred to the buyer on or after July 1, the 6.5% state rate applies. This rule applies even when partial or full payment is made before July 1, 2015.
- **Leases of tangible personal property that require recurring periodic installment payments** - Kansas sales tax is imposed on leases of tangible personal property. Each lease installment is treated as a separate sale. A sales tax rate change applies to a lease installment without regard to when the lease agreement is entered into or when installment payments are made. For periodic monthly installments, the new 6.5% rate applies to the first installment period starting on or after July 1, 2015. *K.S.A. 79-3678.* The customer billing for the last installment period that starts in June and ends on or after July 1, 2015 is subject to the 6.15% state rate. This treatment also applies to leased property that is relocated to Kansas for use here.

This treatment does not apply to financing leases, which are credit arrangements that finance purchases of goods. Under such financing arrangements, sales tax is payable up front at the time of sale on the full selling price of the goods rather than on the stream of installment payments made to pay down the loan balance.

- **Rentals** - For rentals of tangible personal of 30-days or less, the date the customer first takes possession of the rental property fixes the state sales tax rate. The 6.5% state rate applies when a customer takes possession of rental property on or after July 1, 2015. When a customer takes possession before July 1, 2015, the rental charge for the last billing period that starts in June and ends on or after July 1, 2015 is subject to the 6.15% state rate. *K.S.A. 79-3678.* If the rental agreement is extended, renewed, or modified on or after July 1, 2015, the 6.5% state rate applies from that time forward.
- **Vending machines and coin-operated amusement devices** - Sales made from vending machines, amusement devices, and similar devices that accept payment for goods or services are treated as occurring when the money is removed from the machine or device. Money removed on or after July 1, 2015 is subject to the 6.5% state rate. Fees and charges, including those for placing the device at a retail location, may not be deducted from the cash receipts before sales tax is figured.

The following guidelines apply to retail charges for taxable services:

- **Admission tickets** to events in Kansas are subject to the tax rate in effect on the date the tickets are sold, regardless of when the event is held.
- **Dry cleaning** - When a dry cleaner or laundry accepts a customer's property for cleaning before July 1, 2015 and returns it on or after July 1, 2015, the charges are subject to the new 6.5% state rate.
- **Installation, application, maintenance and repair services** - Kansas sales tax is imposed on charges for installation, application, maintenance, and repair services, as well on charges for "servicing" property. *K.S.A. 79-3603(p) & (q).* Charges for labor services are sourced in the same way as sales of goods. *K.S.A. 79-3669; K.S.A. 79-3670.*

  When a mechanic, body shop, electronics shop, or other service provider accepts a customer's vehicle or other property for service or repair before July 1, 2015, and returns it to the customer on or after July 1st, all of the charges for parts and service are subject to the 6.5% state rate. Charges for parts and labor services are taxed when the vehicle or other property is returned to the customer or when the completed service work is otherwise available for use by the customer, such as when repairs are completed to a dishwasher or refrigerator in a residence. These rules apply without regard to when the service is contracted for, when payment is made, or when the labor services are performed.

  This is the same treatment that is accorded to retail sales of oil, antifreeze, repair parts, replacement parts, and similar items. It applies regardless of whether the invoice separately lists the charges for tangible personal property and services.
- **Meals or catering-service contracts** - Charges are subject to the tax rate in effect on the date of the catered event.
- **Membership dues** - Kansas sales tax is imposed on the payments of dues to country clubs and other organizations by members that allow them to use the organization’s facilities for recreation or entertainment. Dues covering any period that begins before July 1, 2015 are taxed to members at the prior rate, regardless of the date of the bill. Dues

that cover periods that begin on or after July 1st are taxed at the new rate, regardless of the date the bill is issued to or payment is made by the member. *K.S.A. 79-3678.*

- **Periodic charges for taxable water, gas, heat, and electricity utility service and for telecommunications, cable, direct satellite TV, and similar service** - Sales of natural gas, electricity, heat and water delivered though lines or pipes are exempt from *state sales tax* if they are purchased for: (1) noncommercial use at a residence; (2) agricultural use; (3) use in the severing of oil; or (4) use in buildings and property that are exempt from property tax under K.S.A. 79-201b *Second* through *Sixth.* However, *local sales tax* continues to apply to sales of natural gas, electricity, and heat delivered though lines or pipes for: (1) noncommercial use at a residence; or (2) agricultural use. The law continues to exempt utilities that are consumed in agricultural production from both state and local sales tax. See *KS-1550, Sales and Use Tax for the Agricultural Industry; K.S.A. 79-3606(n).* Water provided through pipes for residential or agricultural use has not been subject to state or local sales tax since January 1, 2006. *K.S.A. 12-189a.* Charges for commercial use of gas, electricity, heat, and water are subject to state and local sales tax unless the use qualifies as consumed in production. *See K.S.A. 79-3602(dd).*

  For monthly periodic billing, the new 6.5% state tax rate applies to the first customer billing period that starts on or after July 1, 2015. For the last billing period that starts in June and ends on or after July 1, 2015, the customer's invoice is subject to the 6.15% state rate. *K.S.A. 79-3678.* For the last billing period that starts in June and ends on or after July 1, 2015, a service provider may elect to charge the 6.5% rate for services billed as line-item charges on or after July 1, 2015, such as long-distance calls and pay-per-view television.
- **Room Occupancy** - Hotels and accommodation brokers should charge sales tax on single-day room charges for June 30th and the morning of July 1st at the lower 6.15% state rate. All taxable occupancy charges billed thereafter should be taxed at the 6.5% state rate.

  For purposes of a rate change, room rentals billed on a weekly or monthly basis are treated as day-to-day rentals if either party has the unconditional right to terminate the room rental agreement. For rental periods other than daily rentals, the overall charge can be prorated and taxed based on the length of stay before and after the rate change.

The following guidelines apply to construction contracts:

- **Construction contracts entered into before May 1, 2015 that qualify for the transition provision in the new law** - The 2015 rate increase contains a transition provision for certain binding written construction contracts that a general contractor and property owner signed before May 1, 2015. *See K.S.A. 79-3695.* It allows the 6.15% state rate to apply to charges for purchases of construction materials and the performance of taxable labor services made on or after July 1, 2015.

  To be entitled to the 6.15% state rate, the general contractor must complete an electronic application form and submit the required documentation to the department on or before July 10, 2015. The electronic application form can be found on the department's website: www.ksrevenue.org/15ratechange.html. It can also be accessed from the link entitled "2015 State Sales and Use Tax Rate Increase" listed under "Popular Items" on the department's home page.

General contractors with a KsWebTax account can access and complete the electronic application form though the link "Submit Request for Contractor Exemption Certificate," and then the link "State Rate Increase Exemption Certificate for Contractors." General contractors that do not have a KsWebTax account should access the link that allows them to open a KsWebTax account. Once the account is opened, the contractor can access and complete the "Application for State Rate Increase Exemption Certificate."

The application form allows an electronic copy of the construction contract or a KDOT contract-award notice to be attached to it. The contract must show that it was completed by the parties before May 1, 2015. In lieu of attaching an electronic copy, the contractor may mail a copy of the contract addressed to: Office of Policy & Research, Kansas Department of Revenue, 915 SW Harrison Street, Topeka, KS 66625. The application and supporting material must be received by the department by July 10, 2015.

The department will notify the general contractor by e-mail once the application is approved or denied. The e-mail will contain a link that takes the contractor back to our web site to allow the contractor to print the exemption certificate or denial letter, which will explain the contractor's appeal rights.

When an application is approved, the department issues a numbered form PR-74c, *State Rate Increase Exemption Certificate* for the qualifying contract that the general contractor should download and print. The general contractor should copy the PR-74c and distribute copies to subcontractors on the project.

The general contractor and subcontractors should fill out a separate PR-74c certificate for each of its vendor and subcontractor that bill them for materials or taxable labor services. The numbered certificate instructs the vendors and subcontractors to charge the 6.15% state rate on construction materials and labor services that are purchased for or performed on the qualifying project on or after July 1, 2015. Vendors, subcontractors, and the general contractor are required to maintain a copy of each certificate they issue or honor as part of their sales tax records.

If a vendor or subcontractor refuses to charge the 6.15% state rate instead of the 6.5% state rate, the contractor or subcontractor is required to pay the 6.5% state tax being charged and complete and submit an ST-21 refund form to request a refund of the tax that is overcharged. Contractors and subcontractors should not strike tax that is charged at the 6.5% state rate and pay tax at the reduced 6.15% state rate.

- **Other construction contracts entered into before July 1, 2015 -** Taxable services billed under a construction contract are subject to the tax rate in place when the services are performed. Contractors that perform a construction contract with taxable labor services are required to remit sales tax at the 6.5% state rate on jobs billed on or after July 1, 2015 unless the contractor can establish a reasonable allocation of services between the two rates that is clearly supported by its records and worksheets.
- **Building Materials** - State sales tax applies to building materials at the rate in place when the materials are delivered to the contractor, not when the purchase is agreed to or payment is made, unless the general contractor secured a PR-74c for the contract.
- **Progress payments -** A progress payment is a payment made to a contractor as work progresses on a construction project. Progress-payment clauses in a construction contract allow the contractor to bill the property owner at intervals, which may be based on the costs incurred by the contractor, the percentage of work completed, the stage of work completed, a payment schedule, or some other basis. Progress payments help reimburse the contractor for the costs it incurs in each progress-payment interval, such as paying

subcontractor charges and employee wages and buying building permits, construction materials, supplies, and insurance.

When a construction contract calls for billing progress payments to the property owner that include charges for taxable labor services, the contractor is required to report and remit sales tax on the taxable labor services performed during each interval covered by a progress payment. Sales tax on the labor services is required to be reported on the return for the reporting period in which each progress payment is due and payable. The 6.15% state sale tax rate applies to taxable labor services rendered before July 1, 2015 in a progress-payment interval billing. The 6.5% state sale tax rate applies to taxable labor services rendered on or after July 1, 2015 that are included in a progress-payment interval. After a project is complete and a contractor reconciles its earlier reporting of taxable labor services with its actual pay outs, receipts, and other records, the 6.5% rate applies unless the contractor can claim a reasonable allocation between the two rates that is clearly supported by its records and worksheets.

Use tax - A 6.5% state use tax, plus the applicable local use tax, is imposed on the use in Kansas of any taxable tangible personal property on which Kansas tax has not been paid. Kansas use tax law provides a credit for sales taxes lawfully paid to another state. For purposes of determining whether Kansas use tax is owed when another state's sales tax is being credited against the Kansas use tax owed, the 6.5% state rate applies if the first use of the property in Kansas occurred on or after July 1, 2015. The difference between the applicable state and local tax rates of both states is used to determine the Kansas use tax owed, if any.

When an out-of-state retailer incorrectly charges the 6.15% state rate instead of the 6.5% state rate on property delivered to a Kansas business on or after July 1, 2015, the business should report the addition .35% state use tax on its consumers' use tax return. If no Kansas tax is collected by an out-of-state retailer, the Kansas business is required to report state and local use tax on the purchase. The date the Kansas business takes delivery of its purchases determines whether the 6.15% or 6.5% state rate applies.

Reporting the tax - Most retailers will report the correct amount of state sales tax on their July return if they bill their customers in accordance with the directives set forth above and program the rate increase into their accounting software in a timely manner. The due date of the July return is August 25, 2015. Most retailers can complete their July return that applies the 6.5% state rate in the same way they completed earlier returns.

Some retailers will report some receipts on their July return from customer charges that were correctly invoiced at the 6.15% state rate. These are: (1) retailers that report tax on the cash basis and are reporting cash receipts from credit sales made before July 2015; (2) service providers that invoice customers on a month-to-month basis fixed by the starting date of service, such as utility providers, cable companies, and telecommunications providers; (3) service providers that invoice monthly membership dues based on the starting date of the membership; (4) lease or rental companies that bill installments that start before and ends on or after July 1, 2015; and (5) vendors and subcontractors that honor a form PR-74c, *State Rate Increase Exemption Certificate*, and charge sales tax at the 6.15% rate for sales made or services rendered on or after July 1, 2015.

These retailers must adjust their July return to avoid paying more sales tax than they charged and collected from their customers at the 6.15% rate. How this is done will be explained in Notice 15-03, *Instructions for Reporting Sales Tax Receipts on the Sales Tax Return Filed for*

July 2015, which will be posted under "2015 State Sales and Use Tax Rate Increase" on the department's home page.

Taxpayer Assistance. Additional copies of this Notice, and other department forms or publications, may be downloaded from our web site, **www.ksrevenue.org**. If you have questions about this rate increase and how it applies, please contact:

Taxpayer Assistance Center
Kansas Department of Revenue
915 SW Harrison St., 1st Floor
Topeka, KS 66612-1588

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