

# SALES TAX ESSENTIALS FOR NC CPAS

DECEMBER 3, 2024

BDO USA, P.C., a Virginia professional corporation, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms.



# Our Agenda Today

- ▶ Nexus
- ▶ Sales Tax vs Use Tax
- ▶ Sales Price/Tax Base
- ▶ Sourcing
- ▶ Services
- ▶ Exemptions
- ▶ Industries
- ▶ Documentation to Keep on Audit



# With you Today



**BARBARA BARGER**  
SALT Manager

704-887-4202  
bbarger@bdo.com



**CHRIS LEJA**  
SALT Senior Manager

704-887-4179  
cleja@bdo.com

# Nexus

## What is nexus?

- The minimum activity, or connection, in a state that creates a tax reporting and payment responsibility.
- Nexus describes the minimum amount of business activity that must be present before a state can tax an entity's income.

## What creates nexus?

- Physical presence - having property or employees located in the state.  
Could include sporadic or temporary presence.
  - Warehouses, inventory, trade-show visits, independent representatives could also establish physical presence.
- Economic nexus - exceeding specific thresholds set by the states.
  - Thresholds can be either a dollar amount and/or number of transactions.
- Other forms of nexus (affiliate nexus, click-through nexus, etc.)

# Sales Tax

- Sales tax is a transactional tax imposed on the retail sale of tangible personal property (TPP) and specifically enumerated services.
- Sales tax is a “trust fund” tax, *i.e.*, the seller collects tax from the customer on behalf of the jurisdiction and remits it to the taxing authority.
- A retail sale is any sale, lease, or rental for any purpose other than for resale, sublease or sub-rent.

# Use Tax

- Use tax is a transaction tax that is imposed on the privilege of ownership, consumption, possession, storage and/or use of tangible personal property.
- Use tax is considered complementary to sales taxes
  - Intended to capture taxable transactions upon which no sales tax was paid.
- Use tax applies to transactions made under an exemption and then used in a taxable manner.
  - Samples
  - Donations
  - Converted Inventory

# What's Included in the Sales Price?

- Check the definition or imposition section of the statute - always read
- Sales price equals total amount of consideration, including cash, credit, property and services without deduction for:
  - Cost of property
  - Cost of materials, labor or services
  - Charges for services used to complete the transaction, other than delivery and installation charges
- Sales price may include:
  - Delivery charges incurred or to be incurred before the completion of the transfer of ownership
  - Installation charges incurred or to be incurred before the completion of the transfer of ownership
  - Value of exempt property bundled with taxable property
  - Credit for any trade-in

# Sourcing for Sales of TPP

## How are sales sourced?

- Origin-based vs. destination-based
- Very limited origin-based states
- For a remote seller, sales will generally be destination-based

## Streamlined Sales and Use Tax Agreement - Section 310

1. Received at a business location of the seller - sale is sourced to that location
2. Where receipt by the purchaser takes place
3. Address of customer maintained by the seller in the normal course of business
4. Address obtained at point of sale, including address of the purchaser's payment instrument (e.g., credit card)
5. Address where TPP is shipped from or location digital good was first available for transmission by the seller



# Taxability of Services

- **Services - usually specifically enumerated**
  - Many states tax some services, range from low of 1 to high of 160 taxable services
- **Most commonly taxed services**
  - Printing services
  - Repairs or maintenance of tangible personal property
  - Installation services
  - Information services
- **Separately-stated versus “bundled”**
  - Nontaxable services if “bundled” with tangible personal property may become taxable

# Taxability of Services - Continued

- For mixed transactions, many states use a "True Object" test
  - If the "True Object" is a nontaxable service - Excluded
  - If the "True Object" is a sale of TPP - Taxable
- "True Object" Test Examples
  - Educational Software
    - Example 1: License to a non-programmable educational software program?
    - Example 2: License to an education platform that provides interactive courses and personalized learning plans?
  - Photography
    - Photography service or sale of photos?
- "De Minimis" Exception
  - When the taxable component of a mixed bundle is minimal, some states allow for the transaction to be non-taxable.

# North Carolina Examples of Taxable SUT Transactions:

- The general NC sales & use tax rate is 4.75%\* and is levied on the sales price of or the gross receipts derived from the following items sold at retail (unless a statutory exemption or exception applies):
  1. Articles of tangible personal property, other than a boat, including tangible personal property sold at a specialty market or other event.
  2. Leases or rentals of tangible personal property other than a boat.
  3. Free standing appliances.
  4. Manufactured homes.
  5. Modular homes.
  6. Qualified jet engines.
  7. Admission charges to an entertainment activity.
  8. Aircraft: maximum tax is two thousand five hundred dollars (\$2,500) per aircraft.

\*NC's local SUT rates generally range from 2.00% - 2.75% depending on the county.

## North Carolina Examples of Taxable SUT Transactions (Cont'd):

- The general NC sales & use tax rate is 4.75%\* and is levied on the sales price of or the gross receipts derived from the following items sold at retail (unless a statutory exemption or exception applies) (cont'd):
  9. Certain digital property
  10. Dry cleaning or laundry services.
  11. Prepaid meal plans
  12. Prepaid telephone calling services.
  13. Rentals of accommodations.
  14. Repair, maintenance, and installation services.
  15. Satellite digital audio radio services.
  16. Service contracts.

\*NC's local SUT rates generally range from 2.00% - 2.75% depending on the county.

# Taxable Goods and Services - Digital Goods

## Digital Products

- Electronically transferred/accessed (not delivered) products.
- Taxing jurisdictions are struggling to keep up with technology; sales and use tax statutes and concepts were designed for tangible personal property
  - Issues being considered by taxing jurisdictions
    - Sale of software license?
    - Electronic delivery?
    - Where to source?
    - Information service or database access?
    - Other enumerated taxable/non-taxable service?
    - Warranties, installation, configuration, testing, maintenance agreements

# Digital Goods - NC as an Example

- The general NC state & local sales & use tax rates apply to the sales price of “certain digital property” sold at retail and sourced to this State.
- “Certain digital property” includes “specified digital products” and “additional digital goods.”
- The tax applies regardless of whether the purchaser of the property has the right to use it permanently or to use it without making continued payments.
- The sale at retail or the use, storage, or consumption in this State of a digital code is treated the same as the sale at retail or the use, storage, or consumption in this State of certain digital property for which the digital code relates.
- “Additional digital goods” - All of the following if transferred electronically:
  - A magazine, a newspaper, a newsletter, a report, or another publication.
  - A photograph.
  - A greeting card.
- “Specified digital products” - NC includes “digital audio works,” “digital audiovisual works,” and “digital books.”

# Exemptions - Exempt vs Excluded

**Excluded Sale** - a transaction or some element of the transaction that is not included in the tax imposition statute.

- Outside scope of imposition statute therefore not taxable
- “Non-taxable”, “Excluded” (*e.g. intangibles and real property*)
- Burden of proving taxability is generally on the government

**Exempt Sale** - a transaction that is not subject to tax because of specific statutory exemption.

- Inside scope of imposition statute, but statutorily excluded (*e.g. sales for resale*)
- Burden of proving exemption is generally on the taxpayer

# Exemptions - Entity Exemptions

## Entity-Based Exemptions

- IRC Section 501(c)(3)
- Religious, Charitable, Educational
- Government Contractors
- Federal Government
- State and Local Government



# Exemptions - Product Exemptions

- Food and Groceries
- Clothing
- Prescription Drugs
- Medical Devices
- Educational Material
- Renewable Energy Equipment

# Exemptions - Use Exemptions

- Sales for Resale
- Occasional, Isolated or Casual Sales
  - The sale of all or substantially all of the assets of a trade or business in a single transaction is generally exempt.
    - Does not apply to inventory, motor vehicles, airplanes.
  - Sale of used assets such as equipment may also be exempt; however, it is limited to the number of transactions per year.
- Manufacturing
  - Machinery and equipment used to manufacture or process tangible personal property for resale; must generally be used directly and exclusively in the manufacturing process
  - Tangible personal property that becomes an ingredient or component part of the product produced for sale (i.e., raw materials)
  - Tangible personal property used or consumed during the manufacturing process (e.g., chemicals)

# Exemptions - Certificates (Exemption / Resale)

**Exemption certificates are given and kept “in good faith”**

- Types of Exemption Certificates
  - Single
  - Blanket
- Certificates vary by State

**The resale exemption is important to customers who purchase for sale to others; it avoids pyramiding of the tax**

- Sales for resale must be properly documented with resale certificates
  - Sales tax registration generally needed to issue
  - Good faith acceptance
  - Certificate needed at time of transaction; generally good for multiple transactions over a few years
  - Lost or misplaced certificates can create exposure
- Also applies to purchases of items for lease

# E-595E Streamlined Sales and Use Tax Certificate of Exemption



**Do not send this form to the Streamlined Sales Tax Governing Board or the NC Department of Revenue. Send the completed form to the seller and keep a copy for your records.** This is a multi-state form for use in the states listed. Not all states allow all exemptions listed on this form. The purchaser is responsible for ensuring it is eligible for the exemption in the state it is claiming the tax exemption from. Check with the state for exemption information and requirements. **The purchaser is liable for any tax and interest, and possible civil and criminal penalties imposed by the state, if the purchaser is not eligible to claim this exemption.**

**1**  Check if this certificate is for a single purchase. Enter the related invoice/purchase order #

**2** A. Purchaser's name

B. Business address  City  State  Country  Zip code

C. Name of seller from whom you are purchasing, leasing, or renting

D. Seller's address  City  State  Country  Zip code

**3** **Purchaser's type of business.** Check the number that describes your business.

- |  |  |
|--|--|
| <input type="checkbox"/> 01 Accommodation and food services              | <input type="checkbox"/> 11 Transportation and warehousing       |
| <input type="checkbox"/> 02 Agricultural, forestry, fishing, and hunting | <input type="checkbox"/> 12 Utilities                            |
| <input type="checkbox"/> 03 Construction                                 | <input type="checkbox"/> 13 Wholesale trade                      |
| <input type="checkbox"/> 04 Finance and insurance                        | <input type="checkbox"/> 14 Business services                    |
| <input type="checkbox"/> 05 Information, publishing, and communications  | <input type="checkbox"/> 15 Professional services                |
| <input type="checkbox"/> 06 Manufacturing                                | <input type="checkbox"/> 16 Education and health-care services   |
| <input type="checkbox"/> 07 Mining                                       | <input type="checkbox"/> 17 Nonprofit organization               |
| <input type="checkbox"/> 08 Real estate                                  | <input type="checkbox"/> 18 Government                           |
| <input type="checkbox"/> 09 Rental and leasing                           | <input type="checkbox"/> 19 Not a business <input type="text"/>  |
| <input type="checkbox"/> 10 Retail trade                                 | <input type="checkbox"/> 20 Other (explain) <input type="text"/> |

**4** **Reason for exemption.** Check the letter that identifies the reason for the exemption.

- |  |   |
|--|---|
| <input type="checkbox"/> A Federal government (department) <input type="text"/>              | <input type="checkbox"/> H Agricultural production # <input type="text"/>             |
| <input type="checkbox"/> B State <input type="text"/> government (name) <input type="text"/> | <input type="checkbox"/> I Industrial production/manufacturing # <input type="text"/> |
| <input type="checkbox"/> C Tribal government (name) <input type="text"/>                     | <input type="checkbox"/> J Direct pay permit # <input type="text"/>                   |
| <input type="checkbox"/> D Foreign diplomat # <input type="text"/>                           | <input type="checkbox"/> K Direct mail # <input type="text"/>                         |
| <input type="checkbox"/> G Resale # <input type="text"/>                                     | <input type="checkbox"/> L Other (explain) <input type="text"/>                       |

Please print

### UNIFORM SALES & USE TAX CERTIFICATE—MULTIJURISDICTION

The below-listed states have indicated that this form of certificate is acceptable, subject to the notes on pages 2 - 4. The issuer and the recipient have the responsibility of determining the proper use of this certificate under applicable laws in each state, as these may change from time to time.

Issued to Seller: \_\_\_\_\_

Address: \_\_\_\_\_

I certify that: \_\_\_\_\_ is engaged as a registered

Name of Firm (Buyer): _____	Wholesaler	_____
	Retailer	_____
Address _____	Manufacturer	_____
_____	Seller (California)	_____
_____	Lessor (see notes on pages 2 - 4)	_____
_____	Other (Specify)	_____

and is registered with the below listed states and cities within which your firm would deliver purchases to us and that any such purchases are for wholesale, resale, ingredients or components of a new product or service<sup>1</sup> to be resold, leased, or rented in the normal course of business. We are in the business of wholesaling, retailing, manufacturing, leasing (renting) the following:

Description of Business: \_\_\_\_\_

General description of tangible property or taxable services to be purchased from the seller: \_\_\_\_\_

State	State Registration, Seller's Permit, or ID Number of Purchaser	State	State Registration, Seller's Permit, or ID Number of Purchaser
AL <sup>2</sup>	_____	MN <sup>12</sup>	_____
AR	_____	MO <sup>4</sup>	_____
AZ <sup>22</sup>	_____	NE	_____
CA <sup>3</sup>	_____	NV	_____
CO <sup>1</sup>	_____	NJ	_____
CT <sup>4</sup>	_____	NM <sup>1,15</sup>	_____
DC <sup>5</sup>	_____	NC <sup>25</sup>	_____
FL <sup>23</sup>	_____	ND <sup>16</sup>	_____
GA <sup>6</sup>	_____	OK <sup>17</sup>	_____
HI <sup>1,7</sup>	_____	RI	_____
ID <sup>1,8</sup>	_____	SC <sup>18</sup>	_____
IL	_____	SD	_____

# Direct Pay

- “Direct payment permit” means a permit issued by a taxing authority that allows a holder of such permit to accrue and pay state & local taxes directly to the state(s).
- Application for Permit. Applicants for a direct payment permit must apply in writing to each state.
- Qualification Process and Requirements.
  - Applicants for a direct payment permit shall demonstrate the applicant's ability to comply with each state’s sales & use tax laws and reporting and payment requirements. The applicant must provide a description of the accounting system(s) which will be used by the applicant and demonstrate that the accounting system(s) will reflect the proper amount of tax due.
  - Applicants must establish a business purpose for seeking a direct payment permit and must demonstrate how direct payment will benefit tax compliance.
  - The state(s) will review all permit applications.

# Industries - Retail

## Tax Base x Tax Rate = Tax Amount

- What is it and how it is taxed?
- Are there Sales Tax Holidays?
- Are the Sales in-store, buy online/pick-up in-store, shipped out of state?

## Complications

- Are there exemptions or exclusions?
- Do we have accurate rate tables or taxability tables?
- Do we have a drop shipment scenario?
- Has documentation been received if needed (i.e. exemption certificates)?
- How are coupons and/or discounts treated?

# Industries - Manufacturing

## Sales to Customers

- Where has nexus been established?
- What is the proper taxability of the products being sold?
- Has the proper documentation (exemption certificates) been collected?

## Purchases

- Does the state have manufacturing exemptions?
  - Machinery and equipment used directly and predominately
- What are the manufacturing process start and end points?
- Are utilities used in the manufacturing process?
- Is there proper documentation in place to distinguish administrative tasks vs. manufacturing operations?



# Industries - Software

## Type of Software

- “Canned” Software
- Custom Software
- Software as a Service (“SaaS”)

## Method of Delivery

- Tangible Form
- Load and Leave
- Electronically Downloaded

## Services

- Modifications
- Maintenance Agreements
- Remote Services

# Industries - Construction

## Must be a Construction Contract

- Real Property 3-prong test
  - Attached/affixed to real property
  - Causes substantial damage
  - Intended to be permanent

## Complications

- Type of Contract
  - Lump-Sum
  - Separated
- Customer of Contract
  - Exempt Entity

# North Carolina - Repair, Maintenance, & Installation

## RMI - TPP, motor vehicle, digital property, real property

Included activities:

- Keep or attempt to keep property from breaking down and prevent deterioration
- Calibrate, refinish, restore property (or attempt) to good condition
- Troubleshoot source of problem with purpose of determining what is needed to restore property.
- Install, apply, connect, adjust, set in to place TPP or digital property.
- Inspect or monitor TPP or digital property

## Exemptions from RMI

- Resale
- Exempt Property
- Capital Improvement

# North Carolina - Capital Improvement

## Capital Improvement Includes:

- New construction, Reconstruction, or Remodeling
- Painting or wallpapering
- Replacement or installation of entire system related to septic tank, roofing, plumbing, electrical, refrigeration, irrigation, HVAC, or similar
- Performance of work that requires the issuance of a permit under the State Building Code, other than repair or replacement of electrical components, gas logs, water heater, and similar
- Installation of transmission, distribution, or other network asset on utility owned land
- Replace or install roads, driveways, parking lots, sidewalks, patios, decks
- Landscaping
- Fixture attached to real property and that meets one or more of the following:
  - Capitalized and depreciated under GAAP or IFRS
  - Depreciated under the IRC
  - Expensed under Section 179 of the IRC
- Certain services to resolve real property contract (6 or 12 months old)
- Addition or alteration to real property that is permanently affixed or installed & is not RMI

# Documentation to Keep on Audit

- Every retailer, wholesale merchant, facilitator, real property contractor, and consumer must keep records that establish their sales and use tax liability.
- Have good documentation / record retention of purchase orders, invoices, other accounting records
- Exemption certificate documentation
- Burden of proof is on the taxpayer
- Statute of Limitations?



## Barb Barger, CPA

STATE AND LOCAL TAX MANAGER

Direct: 704-887-4202 | Mobile: 803-747-1974 | [bbarger@bdo.com](mailto:bbarger@bdo.com)

615 S College St, Suite 1200, Charlotte, NC 28202

Tel: 704-887-4236 | Fax: 704-887-4290

### Experience

Barb is a Manager in BDO's State and Local Tax Practice and focuses predominately on Sales and Use Tax Services. Barb has since been employed with BDO after she earned her M.S. in Accountancy at College of Charleston. Barb has worked with clients in various industries including financial services, manufacturing, and technology on a multitude of state and local tax issues including nexus determinations, taxability determinations, reverse audits, outsourced engagements, and voluntary disclosure agreements.

### Education

- ▶ M.S., Accountancy, College of Charleston
- ▶ B.S., Accounting and Business Administration, College of Charleston

### Professional Affiliations

- ▶ American Institute of Certified Public Accountants
- ▶ North Carolina Association of Certified Public Accountants



## Chris Leja, CPA

SENIOR MANAGER - STATE AND LOCAL TAX

Direct: 704-887-4179 | Mobile: 248-719-9974 | cleja@bdo.com

615 S College St, Suite 1200, Charlotte, NC 28202

Tel: 704-887-4236 | Fax: 704-887-4290

### Experience

Chris is a Senior Manager in BDO's State and Local Tax Practice. Chris has been working in public accounting since 2017 after getting his M.S. in Accounting at Michigan State University.

Chris has worked with clients and managed engagements in countless industries including financial services, manufacturing, healthcare, telecommunications, technology, and many other industries across a multitude of state and local tax issues. Chris has assisted his clients in identifying tax opportunities, navigating the complexities and nuances of state and local tax, and/or mitigating risk across nearly every state. Chris has assisted his clients in countless state and local tax engagements, including but not limited to the following: multi-state tax planning, state tax audit controversy, voluntary disclosure agreements, negotiated incentives, tax credits, litigation support, state income tax sourcing analyses, sales & use tax taxability and exemption certificate reviews.

### Education

- ▶ M.S. in Accounting, Michigan State University
- ▶ B.S. in Accounting, Michigan State University

### Professional Affiliations

- ▶ North Carolina Association of Certified Public Accountants
- ▶ NCACPA Tax Education and Tax Resource Committees



## About BDO USA

At BDO, our purpose is helping people thrive, every day. Together, we are focused on delivering exceptional and sustainable outcomes – for our people, our clients and our communities. Across the U.S., and in over 160 countries through our global organization, BDO professionals provide assurance, tax and advisory services for a diverse range of clients.

BDO is the brand name for the BDO network and for each of the BDO Member Firms. BDO USA, P.C, a Virginia professional corporation, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms.

[www.bdo.com](http://www.bdo.com)

Material discussed is meant to provide general information and should not be acted on without professional advice tailored to your needs.

© 2023 BDO USA, P.C. All rights reserved.

