



NC SALES TAX REVIEW & UPDATE



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Jack Schmoll

- 33 years in state and local taxation
- 9 years with the Washington State Department of Revenue
- Started own firm in 2012
- Works with wide variety of businesses in NC and across the country and world
- Works with CPA firms across the country on SALT issues



Objectives

- Taxable Sales
- Bundled Transactions
- Repair, maintenance, and installation
 - Lots of audits!
 - Property management
- Exemptions
 - Important case
- **Pain Points!**



Sales and Use in General

- Sales Tax
 - “Privilege Tax”
- Use Tax
 - Storage, use, or consumption
 - Samples and give aways



Taxable Sales

- Tangible personal property
- Digital property
- Software
- Taxable services



Tangible Personal Property

- Can be seen, weighed, measured, felt, or touched.
Includes:
 - water,
 - gas,
 - steam,
 - electricity, and
 - prewritten computer software



Digital Goods

- Audio work (including streamed)
- Audio visual work (including streamed) – Uncertainty
- Book, magazine, newspaper, report, etc.
- Photograph – **Pain Point!**
- Greeting card



Software

- Canned or Custom
- Taxable, except
 - Custom
 - Enterprise server operating system
 - Sold to cable, telecom, or video programming services and used for cable, ISP, telecom., or video programming
 - SaaS, ASP



Taxable Services

- Laundry and dry-cleaning
- Telecommunications
- Fabrication labor
- Non-separately stated charges
- Certain services necessary for the sale
- RMI (repair, maintenance, & installation)
- Service contracts

- * not an inclusive list



Leases and Rentals

- Purchases for resale
- Intervening use
- Related party lease
- Lease with operator
- Vehicles
 - Long term – 3%
 - Short term – 7%



Bundled Transactions

- 50% Test – Exempt food; drug; medical devices, equipment, or supplies
 - 50%+ of food – 2%
 - 50%+ of prescription drugs - Exempt
- Allocation – Only if includes a service
 - Service contract exceptions
- 10% test – Not taxable if taxable items do not exceed 10%



RMI

- Definition of RMI
- Excluded and exempt
- Capital improvements
- Waivers



Tax Application

- RMI Job

Tax collection from customer	Yes
Tax due on materials	No

- Capital Improvement Job

Tax collection from customer	No
Tax due on materials	Yes



RMI Definition

- TPP, motor vehicle, digital property, real property (other than real property contract)
 - Keep or attempt to keep in working order
 - Calibrate, refinish, restore or attempt to
 - Troubleshoot source of problem with purpose of fixing
 - Install, apply, connect, adjust, set into place
 - Inspect or monitor (excludes real property)



RMI Exemptions

- Real property contract – Capital Improvement
- RMI of exempt property
- Resale of RMI services
- Cleaning real property - mold
- Services on roads, driveways, parking lots, sidewalks
- Landscaping – living elements
- Pest control – application



RMI Exemptions

- RMI purchased by a contractor as part of fulfilling capital improvement contract
- Vehicle safety and emissions inspection
- Performed by related member
- Removal of waste (not portable toilet septage)
 - Asbestos
- Alteration and repair of clothing
- Self and limited-service car wash
- Real property monitoring service
- Moving service



RMI Exemptions

- Real property contract follow up – w/in 6 months
- RMI of certain aircraft
- Funeral-related services
- Services performed on animals
- Monitoring of real property (security, fire)
- Providing operator for wastewater system



Capital Improvements

Capital improvements must relate to ***REAL PROPERTY***

General Assembly provided a list of ways a project can be a capital improvement.



Capital Improvements Includes

- New construction,
- Reconstruction, or
- Remodeling



Remodeling

- ***Multiple services*** performed by one or more persons to restore, improve, alter, or update real property
- Does not include a single RMI service
- Does not include a transaction where the true purpose is a RMI service no matter that another RMI service is performed that is incidental
- ***COLLECT AN E-589CI***



Capital Improvements Includes

- Permit required by ***state building code*** except replacing electrical components, gas logs, water heater, and similar
- Installation of utilities on utility land
- Painting or wallpapering
- Entire systems of roofing, septic tank, plumbing, electrical, commercial refrigeration, irrigation, sprinkler system, or other similar
- HVAC unit or system



Capital Improvements Includes

- Replace or install roads, driveways, parking lots, sidewalks, patios, decks
- Landscaping
- Fixture attached to real property and that is capitalized for IRC, GAAP, IFRS
- Certain services to resolve real property contract 6 months old/12
- Addition or alteration to real property that is permanently affixed or installed & is not RMI – Huh???



E-589C1

- **Pain Point!**
- Shifts burden
- Single use
- Blanket use
- New form at each level
- Reluctance of customers to sign
- Alternative documentation



Mixed contract

- RMI < 25%
 - Bathroom remodel - \$20,000
 - Replace garden window in kitchen - \$5,000
 - Treat all as CI

- RMI > 25%
 - Bathroom remodel - \$20,000
 - Replace front door - \$10,000
 - Separate line items, tax door replacement RMI



Retailer/Contractor

- A person that acts as a retailer for TPP and RMI sales and a real property contractor when it performs real property contracts
- Determining if you are a retailer or a contractor
- Tax paid on RMI materials
 - Credit allowed
 - Reduce taxable receipts



Tax Paid on Materials Example

- \$10,000 taxable repair performed
- Customer charged \$10,000 plus \$700 of tax
- Contractor purchased \$3,000 of taxed materials and paid \$210 of tax
- \$7,000 of taxable sales on tax return
- \$490 of tax paid with return



Waiver of Tax

- Secretary can compromise for 3/1/16 – 12/31/22 if:
 - Best interests of the state and
 - Good faith effort
- SB 628, 3/1/16 – 12/31/18 Grace period
 - Much Broader waiver
 - Department will take no action



Property Management

- Perform specific services (see SUTB 75-6)
- Taxable and nontaxable services
- 25% time test
- Allocation of revenue
- Taxation of additional services based on service performed
- Substantiation is problematic



Exemptions

- Resale
- Manufacturers – Significant court case
- Government
- Nonprofits are **NOT** exempt

(note that this presentation does not cover all of the exemptions available)



Resale Exemption

- Sellers responsibility
 - Collect certificate
 - Verify purchase is typical
- Buyers responsibility
- Finished goods
- Raw materials
- Containers and labels



Exemptions – Manufacturers

- Three principal activities of “manufacturing industries or plants:”
 - Administration
 - Distribution
 - Production
 - From the movement of raw materials to production
 - To the movement of finished goods to storage



Exemptions - Manufacturers

- Production
 - Processing and refining
 - Conditioning, treating
 - Assembling
 - Movement through process
 - Movement into storage or shipping areas
 - R&D
 - QC



Exemptions - Manufacturers

- What is mill machinery?
 - Used in production 50% or more
- ~~1% and \$80 max per article of mill machinery~~
 - **Expired 7/1/2018!!**
- Sales of mill machinery and equipment
- Sales of mill machinery and equipment to contractors
- Printers are manufactures



Exemptions - Manufacturers

- **NC DOR v. FSC II, LLC**
 - State Supreme Court case
 - Who is a “manufacturing industry or plant”
 - 50% rule is invalid
 - Not an insignificant amount
- DOR uncertainty



Sales to Government Entities

- US Government or any of its agencies or instrumentalities, including:
 - Federal credit unions
 - Farm credit banks and federal land banks
 - Documentation
 - Government PO
 - Document government credit card used
- North Carolina state agencies – exempt
- Local NC governments – taxable



Nonprofit, Charitable & Religious

- Purchases – taxable – **Pain Point for vendors!**
- Sales – taxable with some exceptions
 - Short-term annual fund raisers
 - Delivered in 60 days from order
 - Church food sales
- Refunds



Pain Points

- Contractors, contractors, contractors
 - Remodeling
 - Disaster recovery
 - Flooring
 - Crawl space encapsulating
 - Electrical
 - HVAC
- Photography
- Convenience Stores
- Unregistered Businesses



Thank You!



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