



2016 CAI-NC Community Law Day

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This 2016-17 State Budget includes several new sales tax provisions intended to clarify the application of sales and use tax on certain repair, maintenance and installation services and provides a grace period for under-collection of that tax by contractors in 2016. These new provisions will be important to individuals and companies who provide repair, maintenance and installation services to real property. For example, as opposed to current sales and use tax law, these new provisions will treat similar transactions the same regardless who performs the service. This bill removes the distinction and provides that all businesses that provide taxable repair, maintenance and installation services will be treated the same. As a practical matter, this will have the effect of taxing many more repair and maintenance services to real property.

New Sales Tax on RMI begins on January 1, 2017

1. Reflects a Shift in Philosophy on State Taxes
2. Specific Guidance Document from NC Department of Revenue on November 15, 2016
3. 2015 State Tax Law started the sales tax on repair labor.

Separate treatment to real property contractors vs. retail/real property contractors –
Former had tax free labor, later had taxable labor

4. “RMI” – Repairs, Maintenance and Installation
5. 2016 – Sales Tax on RMI
 - A. Real property contractor – one who does construction, reconstruction, remodeling of a capital improvement
vs.
 - B. Retailer – anyone who does only RMI
 - C. Construction – new or increase square footage
 - D. Reconstruction – rebuild building or fixture on land
 - E. Remodeling – replacement vs. repair
6. Many service contracts will be taxable, such as most monitoring services involving real property
7. The new sales and use tax provisions in the 2016 budget bill would do the following important things:
 - A. Exclude capital improvements – Installations into real property, and some significant repairs, would not be taxable if the service is a “capital improvement”. Factors to consider in

determining whether a contract is for the performance of a capital improvement to real property are:

1. The method of attachment for the property installed.
2. The degree of customization of the property installed.
3. The value added by or the useful life of the property installed.

B. The bill specifically identifies the following as capital improvements, and the installation and construction of these items would not be subject to sales tax:

- o New construction and enlargement of an existing structure.
- o Removal of items from real property, such as asbestos and construction material.
- o Performance for work that requires a permit under the State Building Code.
- o Installation of equipment that is attached to real property so that the removal of the item would cause physical, function or economic damage to the property;
- o Installation of roofing, septic tank, plumbing, electrical, commercial, refrigeration, irrigation and sprinkler systems.
- o Installation of an HVAC unit or system.
- o Installation of roads, driveways, parking lots and sidewalks.
- o Landscaping services.

8. An Affidavit of Capital Improvement will be developed to document the capital improvement.

9. Mixed Transaction Contracts – Contracts that include both a real property contract for a capital improvement and repair, maintenance and installation services.

- O 10% Rule – Does RMI Exceed 10% of the contract?
 - If no, it is treated as a real property contract
 - If yes, the allocated amount for RMI is taxable.

10. Clarify the taxability of certain RMI services with respect to tangible personal property – The bill would exempt the following services with respect to tangible personal property:

- o Car Washes
- o Clothing Alterations
- o Towing Services
- o Storage of a motor vehicle

11. Exempt Certain RMI Services from Tax – The following services, which otherwise fall within the definition of “repair, maintenance, and installation services”, would be exempt from tax:

- o A fee or charge for an inspection required by law. For example, a fee imposed to have a motor vehicle inspected.
- o Service performed by a related member. A person is a related member if at least 50% of its value is owned by the entity for which it is providing the RMI service; in this instance, the service is more analogous to a service provided by an employee than a retailer.
- o Service performed to resolve an issue that was part of a capital improvement if the services are performed within six months of the completion of the improvement or within 12 months of a new structure being occupied for the first time. This exemption would include

repair services a contractor may have to provide for “punch list” items required of a purchaser of a new structure.

- o RMI service for roads, parking lots and sidewalks. This exemption would treat the repair and maintenance of these items the same as the construction of them. These items are most often State or county-owned in nature and commercial property.
- o Removal of items from real property that may be provided on an as-needed basis rather than under a real property contract. Examples include garbage, grease and debris.
- o Home inspections in preparation for sale of property.
- o House cleaning and janitorial services.
- o Building cleaning services.
- o Landscaping services.
- o Car washes.
- o Alteration services.
- o Pest Control.

Most of these new sales tax changes will become effective January 1, 2017.

12. Conclusion: 4 Takeaways From The Presentation Today:

1. May be the first of many new taxes on services
2. No one can give definitive answers to every single hypothetical question. We must develop a logic to help us answer many questions.
3. Most reputable repair contractors will resolve any doubt by collecting the tax on their service
4. Plan now to add to your repair and maintenance budget for 2017.