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NC Sales Tax on Repair, Maintenance & Installation Charges Effective March 1st

The North Carolina Department of Revenue has issued several recent directives to provide guidance related to changes that were enacted by the General Assembly which become effective March 1, 2016. This tax alert provides an overview of repair, maintenance and installation services that will be subject to sales tax at the statutory 4.75% state sales tax rate and the applicable local sales tax rate. In addition, the new laws amended the definition of “retailer” and “retail trade”.

Overview

Until March 1, 2016, installation charges were exempt from sales and use tax when the charges were separately stated on an invoice given to the purchaser at the time of sale. On and after that date, installation charges by a retailer to a purchaser as part of the retail sale of tangible personal property, certain digital property, and taxable services are subject to sales tax, regardless of whether the installation charges are separately stated by the retailer. In addition, sales and use tax applies to the sales price of repair, maintenance, and installation services sold at retail and sourced to North Carolina. The sales price from the sale or the renewal of a service contract *sold at retail* on or after March 1, 2016 is also subject to sales tax (with the exception of service contracts sold at retail for a motor vehicle).

The term “repair, maintenance, and installation services” is defined as:

- to keep or try to keep tangible personal property or a motor vehicle in working order to avoid breakdown and prevent repairs;
- to calibrate, restore, or try to calibrate or restore tangible personal property or a motor vehicle to proper working order or good condition (this may include replacing or putting together what is torn or broken);
- to troubleshoot, identify, or try to identify the source of a problem to determine what is needed to restore tangible personal property or a motor vehicle to proper working order or good condition; or

- to install or apply tangible personal property except tangible personal property installed or applied by a real property contractor pursuant to a real property contract.

Installation Charges

Effective March 1, 2016, installation charges by a retailer to a purchaser *as part of the retail sale* of tangible personal property, certain digital property and taxable services are subject to the applicable state and local tax rates, regardless of whether the charges are separately stated.

The following list, which is not all inclusive, provides examples of installation charges that are subject to the various tax rates imposed in North Carolina:

- Installation charges that are part of the sales price of tangible personal property, certain digital property, and taxable services, sold at retail, are generally subject to the general 4.75% state, applicable local (2% or 2.25%) and applicable transit (0.50%) rates of sales and use tax. Some exceptions apply.
- Installation charges that are part of the gross receipts from the lease or rental of tangible personal property are subject to the applicable rate of sales and use tax and maximum tax if any.
- Installation charges that are part of the sales price of each manufactured home or modular home sold at retail, including all accessories attached to the manufactured home or modular home when it is delivered to the purchaser, are subject to only the general 4.75% state rate of sales and use tax.
- Installation charges that are part of the sales price of each boat sold at retail, including all accessories attached to the item when it is delivered to the purchaser, are subject to the 3 percent state rate of sales and use tax, with a maximum tax of \$1,500 per article.
- Installation charges that are part of the sales price of an aircraft sold at retail, including all accessories attached to the item when it is delivered to the purchaser, are only subject to the general 4.75 % state rate of sales and use tax, with a maximum tax of \$2,500 per article.
- Installation charges by a retailer to provide telecommunications service and ancillary service, video programming service, piped natural gas and electricity are subject to the 7% combined general rate of sales and use tax.

- Installation charges by a retailer to install a new tire, sold at retail in this state, with a tire bead diameter of less than 20 inches, are subject to the 2% scrap tire disposal tax. Additionally, any installation charges by a retailer to install a new tire, sold at retail in this state, with a tire bead diameter of at least 20 inches, are subject to the 1% scrap tire disposal tax. The sales price of each new tire sold at retail or purchased for storage, use, or consumption in this state and subject to the scrap tire disposal tax is also subject to the general 4.75% state, applicable local (2% or 2.25%), and applicable transit (0.50%) rates of sales and use tax.

Repair and Maintenance Charges

Retailers engaged in business in the North Carolina are liable for the sales and use tax on the sales price or the gross receipts derived from repair and maintenance charges *sold at retail*.

A person whose only business activity is providing repair, maintenance, and installation services, where the person's activities do not otherwise meet the definition of "retail trade," is not a retailer and is not liable for sales or use tax on the sales price of or gross receipts derived from repair, maintenance and installations services on or after March 1, 2016.

A person that *solely operates as a real property contractor* is not a retailer of repair, maintenance, and installation services and is not liable for sales or use tax on the sales price of or gross receipts derived from repair, maintenance and installation services.

A person engaged in "retail trade" on or after March 1, 2016 is a retailer and must treat all sales transactions as retail sales and is liable for sales or use tax on the sales price of the items or services sold at retail, unless the retailer maintains proper records to establish a sale is exempt from sales and use tax. This applies even though the retailer may install or apply tangible personal property that becomes part of or affixed to real property. A person who meets the definition of "retail trade" cannot operate as a retailer-contractor.

A person who is a retailer-contractor prior to March 1, 2016 may be liable for sales or use tax on the sales price of or gross receipts derived from repair, maintenance and installation services on or after March 1, 2016 if the revenue from retail sales is the majority of the person's revenue.

The following list, which is not all-inclusive, provides examples

of services generally considered repair, maintenance and installation services.

- Perform a service or tune-up on the following: motor vehicle; lawnmower, trimmer, edger, leaf blower, pressure washer, generator, chainsaw, tiller, auger, or other similar small engine; boat; aircraft; ATV or dirt bike; moped; golf cart; or bicycle.
- Calibrate any of the following: watch; scale; gun or scope; medical equipment; Lasik surgery equipment; thermometer; instruments (musical or otherwise); battery; meter; or camera.
- Clean jewelry, copy machine, printer, or other tangible personal property or a motor vehicle.
- Remove dents, dings and scratches from tangible personal property or a motor vehicle.
- Restore or reupholster furniture.
- Patch or mend clothing, tires, or any type of inflatable.
- Sharpen blades.
- Polish shoes, jewelry, or silver.
- Troubleshoot a fluid leak or attempt to identify an unusual noise coming from a motor vehicle or other tangible personal property, whether or not the source of the leak or noise is located, determined, or resolved.
- Troubleshoot prewritten computer software to determine how to restore to proper working order.
- Reupholster boats.
- Re-string or re-grip tennis rackets, golf clubs, or musical instruments.
- Tune pianos or other musical instruments.
- Repair laptops, cell phones, remove viruses/malware, conduct diagnostic tests, or adjust computer settings.
- Install or apply tangible personal property which may include: clothing alterations; painting tangible personal property; embroidery; screen printing; window tinting for motor vehicles.

The following repair, maintenance and installation services

are *not* subject to sales tax under the new provisions:

- An item exempt from tax under Article 5 of Chapter 105 of the N.C. General Statutes, other than a motor vehicle. This includes items exempt from tax under N.C. Gen. Stat. § 105-164.13 and items exempt from tax under N.C. Gen. Stat. § 105-164.13E for qualifying and conditional farmers.
- An item subject to tax under Article 5F of Chapter 105 of the N.C. General Statutes. This includes mill machinery, mill machinery parts or accessories, and all items subject to the 1% privilege tax for certain machinery and equipment.
- Services provided under a security or similar monitoring contract for real property;
- Services provided for an item, other than a motor vehicle, for which a service contract on the item is exempt, as provided. Repair, maintenance and installation services provided for a motor vehicle are subject to tax, except as provided under GS 105-164.13(62a) for a manufacturer's warranty or dealer's warranty;
- Services purchased for resale; and
- Services used to maintain or repair tangible personal property or a motor vehicle pursuant to a taxable service contract if the purchaser of the contract is not charged for the item.

Service Contracts

Effective March 1, 2016, the sales price of or the gross receipts derived from the sale or the renewal of a service contract sold at retail on or after March 1, 2016, is subject to the applicable state and local rates of sales and use tax, *regardless of whether the tangible personal property covered in the service contract becomes a part of or is affixed to real property*. This reflects a change in the law effective prior to March 1 that exempted service contracts related to tangible personal property that was installed as, or would become a part of real property.

While repair, maintenance and installations charges for motor vehicles will generally be subject to tax effective March 1, the sale or renewal of a motor vehicle service contract on or after that date will be exempt from tax.

Changes to "Retailer" and "Retail Trade" Definitions

Effective March 1, 2016, a person in “retail trade,” as defined in N.C. Gen. Stat. § 105-164.3(34a), is a retailer and must treat transactions with consumers as retail sales on or after such date, no matter that such person met the definition of a real property contractor for any transactions prior to March 1, 2016. A person that meets the definition of “retail trade,” is a retailer liable for the applicable rate of sales and use tax on retail sales, unless the retailer maintains proper records to establish a sale is exempt.

A person, who meets the definition of “retail trade,” cannot operate as a “real property contractor.” A person who meets the definition of “retail trade” cannot operate as a “retailer-contractor.”

As a result the following types or similar transactions by a retailer in “retail trade” with a consumer is a retail sale: a contract or transaction to perform construction, reconstruction, installation, repair, or any other service with respect to real property; and to furnish tangible personal property to be installed or applied to real property in connection with the contract or transaction; and the labor to install or apply the tangible personal property that becomes part of real property. The retailer is liable for sales tax on the total sales price of the contract or transaction sold at retail.

Effective March 1, 2016, N.C. Gen. Stat. § 105-164.3(34a) defines “retail trade” as “trade in which the majority of revenue is from retailing tangible personal property, digital property, or services to consumers. The term includes activities of a person properly classified in NAICS sector 44-45, buying goods for resale, and rendering services incidental to the sale of merchandise. The term typically includes maintaining an inventory and may include the provision of repair, maintenance, and installation services. Not all activities provided in this subdivision are required for a trade to be considered retail trade.”

A business that is not in the retail trade sector but in another NAICS sector may meet the definition of “retail trade” for purposes of the Sales and Use Tax Act, provided the majority of the revenue is from retailing tangible personal property, digital property, or services to consumers in the state.

Effective March 1, 2016, N.C. Gen. Stat. § 105-164.3(35) is

amended and defines “retailer,” in part as “person engaged in business of delivering, erecting, installing, or applying tangible personal property for use in this state . . . unless the person is one or more of the following:

- A person that *solely* operates as a real property contractor.
- A person whose *only* business activity is providing repair, maintenance and installation services where the person’s activities do not otherwise meet the definition of a retail trade.”

As a result of these changes, a business that engages in both retail sales of tangible personal property, digital property or services to consumers, as well real property contracts, will be required to analyze their various sources of revenue in order to determine the proper method to tax certain transactions.

The directives and other guidance provided by the North Carolina Department of Revenue may assist taxpayers in making determinations based on their own fact patterns. This tax alert is intended to provide an overview of the key changes that become effective March 1. Please consult your DHG tax advisor for additional information.

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