



NORTH
CAROLINA
DEPARTMENT
OF REVENUE

2017 Sales and Use Tax Update Overview NCPMA



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Disclaimer

- Presentation is for general information only.
- Presentation content should not be interpreted as specific tax advice for a specific tax situation.
- Some questions may require additional facts before a response may be given.
- Some questions may require responses from other Departmental employees or employees in other agencies.
- The presentation does not take into consideration draft or future legislation.

Gross receipts – exempt from sales/use tax

- Defined* as:
 - Application of pesticides to real property.
- Pesticide defined as:
 - Any substance used to kill rats, mites, insects, fungi, and bacteria.

*Effective retroactively to January 1, 2017, for sales and purchases occurring on or after such date unless amendments increase a sales or use tax liability, then effective August 11, 2017.

NCDOR Exempt Pest Control Services

- **Exempt Transactions – Gross Receipts:**
 - Single application of pesticide to real property
 - Monthly service contract for application of pesticide to real property
 - Quarterly service contract for application of pesticide to real property
- **Taxable Items – For Pest Control Services:**
 - Purchases of:
 - Pesticides
 - Applicators
 - Traps
 - Tanks, sprayers, and other items for use in the application of pesticides.

- **Exempt Transactions – Gross Receipts**
 - Bed bug heat treatments
 - Crawlspace moisture removal (removal service such as water or condensation)
 - Removal of pests/wildlife
 - Cleaning of real property (See 3/17/17 Notice on Department’s website)
 - Removal and re-installation of existing insulation from crawlspace and application of pesticide to real property
 - Dehumidification system (provided a permanent “system” is installed) – generally a capital improvement and taxed as a real property contract
 - Drainage system (installation of permanent sump pump, piping, etc.) in crawlspace – generally a capital improvement and taxed as a real property contract
 - Pest control inspection for the sale or finance of real property

- **Repair, Maintenance, and Installation Services – Gross Receipts**
 - Removal of existing insulation from crawlspace and replacement with insulation impregnated with pesticide -100% taxable
 - Removal of existing insulation from crawlspace and replacement with insulation not impregnated with pesticide and application of pesticide to real property (pest control services), the following apply:
 - Tax applies to the gross receipts where receipts for removal and installation of new insulation and receipts for pest control services are not separately stated on the invoice or other documentation given to the purchaser at the time of the sale
 - Tax applies only to the gross receipts for removal and installation of new insulation provided the receipts for pest control services are separately stated
 - Installation of vapor/moisture barrier only to existing real property – 100% taxable
- **Portable Dehumidifiers**
 - Sale or rental to consumers – gross receipts taxable including any charges for delivery, installation, etc.)

Generally, gross receipts from services to real property are taxable* as Repair, Maintenance, and Installation Services, unless the person substantiates that the transaction is subject to sales and use tax as:

- A real property contract.
 - (e.g. obtains Form E-589CI, or maintains other records that establish it is a real property contract).
- Certain mixed transactions.
- Exempt
 - (e.g. RMI for resale where Form E-595E, Certificate of Exemption, is on file, or a service that is exempt from sales and use taxes).



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- **Repair, Maintenance, and Installation Services**
 - Generally, the location where the service to real property is performed
- **Real Property Contracts**
 - The location of the contract performed

- Acceptable Substantiation
 - Form E-589 CI
 - Other Documentation

- Liability
 - Person that issues Form E-589CI for any additional tax.
 - Recipient of Form E-589CI, no additional liability unless egregious activity or fraud.

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NCDOR Form E-589CI, Affidavit of CI

NCDOR
Web-Fill
1-17

E-589CI Affidavit of Capital Improvement



Form E-589CI, Affidavit of Capital Improvement, is generally required to substantiate that a contract, or a portion of work to be performed to fulfill a contract, is to be taxed for sales and use tax purposes as a real property contract with respect to a capital improvement to real property.

- This affidavit may not be used to purchase building materials, other tangible personal property, or digital property to fulfill a real property contract exempt from sales and use tax.
- A person who willfully attempts, or a person who aids or abets a person to attempt in any manner, to evade or defeat a tax imposed by the Sales and Use Tax Law, or the payment thereof, shall be guilty of a Class H felony. If there is a deficiency or delinquency in payment of any tax due to fraud with intent to evade the tax, there shall be assessed a penalty equal to 50% of the total deficiency.

Section I. Single Use (Complete this section to issue the affidavit for a single capital improvement.)

<p>A Owner, Tenant, or Real Property Contractor</p> <p>Address</p> <p>City State Zip Code</p>	<p>B Real Property Contractor (General Contractor or Subcontractor) <small>Must perform capital improvement</small></p> <p>Address</p> <p>City State Zip Code</p>
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Describe capital improvement to be performed:

Project Name

Project Address (where the work is to be performed) City State Zip Code

I certify that, to the best of my knowledge, this affidavit is accurate and complete and that the transaction described to be performed by the Real Property Contractor (General Contractor or Subcontractor identified in box "B") shall be treated as a real property contract with respect to a capital improvement to real property for sales and use tax purposes.

Signature of Authorized Person: _____ Title: _____ Date: _____

Section II. Blanket Use (Complete this section to execute a blanket affidavit.)

<p>C Real Property Contractor</p> <p>Address</p> <p>City State Zip Code</p>	<p>D Real Property Contractor or Subcontractor <small>Must perform capital improvement</small></p> <p>Address</p> <p>City State Zip Code</p>
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To be completed by the Real Property Contractor identified in Box C.

I certify that I am a Real Property Contractor who performs capital improvements to real property and all transactions with the real property contractor (subcontractor) identified in box "D" shall be treated as real property contracts with respect to capital improvements for real property for sales and use tax purposes.

Signature of Authorized Person: _____ Title: _____ Date: _____

NCDOR Mixed Transaction Contract*

Contract that include both a real property contract for a capital improvement and an RMI service that is not related to the capital improvement.

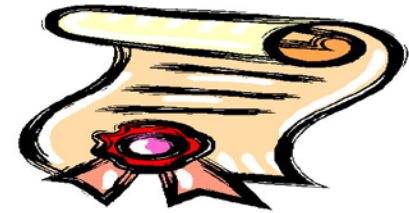
- **25% Rule** - Does the allocated price of RMI exceed 25% of the contract?
 - If no, the entire transaction is treated as a real property contract.
 - **If yes, the allocated amount for RMI is taxable.**

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A contract where the obligor under the contract agrees to maintain, monitor, inspect, repair, or provide another service included in the definition of repair, maintenance, and installation service (RMI) to digital property, tangible personal property, or real property for a period of time or some other defined measure. The term does not include a single repair, maintenance, and installation service, but does include a contract where the obligor may provide a service included in the definition of RMI as a condition of the contract.

Includes:

- Service contract for a pool, fish tank, or similar aquatic feature and a home warranty.
- **Warranty agreement** other than a manufacturer's warranty or dealer's warranty provided at no charge to the purchaser.
- Extended warranty agreement.
- Maintenance agreement.
- Repair agreement.
- Similar agreement or contract.

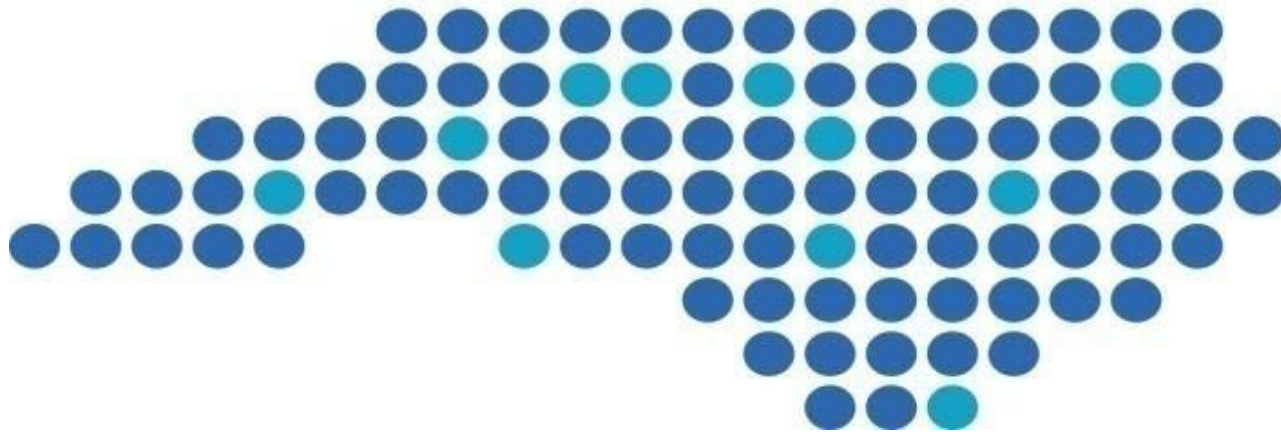


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Questions



Excerpt from 3/17/17 Important Notice



**Sales and Use Tax Division
North Carolina Department of Revenue
Post Office Box 25000
Raleigh, North Carolina 27640-0001**
www.dornc.com

**IMPORTANT NOTICE: ADDITIONAL INFORMATION REGARDING REAL PROPERTY CONTRACTS AND
RETAIL SALES OF REPAIR, MAINTENANCE, AND INSTALLATION SERVICES TO REAL PROPERTY**

The following list provides general guidance to assist with making a determination as to whether a transaction is a real property contract with respect to a capital improvement to real property; subject to tax as a retail sale of repair, maintenance, and installation services to real property; or exempt from sales and use tax. Refer to [Directive SD-16-3: Real Property Contracts](#), [Directive SD-16-4: Repair, Maintenance, and Installation Services](#), and the [Important Notice: Form E-589Cl, Affidavit of Capital Improvement](#), available on the Department's website for additional information regarding the application of the sales and use tax laws to real property contracts with respect to a capital improvement and repair, maintenance, and installation services.



Excerpt from 3/17/17 Important Notice

Disclaimer: This list is not specific tax advice. The application of sales and use tax may differ based on the facts and circumstances of a particular transaction.

Transactions by Category	<u>Capital Improvement</u> Gross Receipts are Exempt from Sales and Use Tax	<u>Repair, Maintenance, and Installation Services</u> Sales Price or Gross Receipts are Taxable Unless Exemption Applies
Commercial Refrigeration Equipment		
Replacement or installation of commercial refrigeration systems	X	
Repair or maintain commercial refrigeration systems (other than installation or replacement of systems)		Taxable
Repair, maintain, install, or replace component parts or portion of commercial refrigeration systems		Taxable
Commercial refrigeration service contracts	Important Notice: Service Contracts 11/15/16	

NCDOR Capital Improvement* Definition

One or more of the following:

New Construction - Construction of or site preparation for a permanent new building, structure, or fixture on land or an increase in the square footage of an existing building, structure, or fixture on land.

Reconstruction - Rebuild or construct again a prior existing permanent building, structure, or fixture on land and may include a change in the square footage from the prior existing building, structure, or fixture on land.

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Capital Improvement*

Definition (cont'd)

Remodeling - A transaction comprised of **multiple services** performed by one or more persons **to restore, improve, alter, or update real property** that may otherwise be subject to tax as RMI services if separately performed.

- **Includes** a transaction where the **internal structure or design** of one or more rooms or areas within a room or building are substantially **changed**.
- 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 to the true purpose of the transaction.
 - Repair of sheetrock that includes applying paint.
 - Replacement of cabinets that includes installation of caulk or molding.
 - Installation of hardwood floors that includes installation of shoe molding

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Capital Improvement* Definition (cont'd)

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 individual items that are not part of new construction, reconstruction, or remodeling.

- Underlined items are taxable as RMI services!!!

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Capital Improvement* Definition (cont'd)

- Installation of **utilities on utility owned land, right of way, or easement**, notwithstanding that charges for such may be included in the gross receipts derived from services subject to the combined general rate under G.S. 105-164.4.
- **Installation of equipment or fixture** that is attached to real property and that meets **one or more** of the following conditions:
 - Is capitalized and depreciated under Generally Accepted Accounting Principles or International Financial Reporting Standards.
 - Is depreciated under the Code.
 - Is expensed under Section 179 of the Code.

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Capital Improvement* Definition (cont'd)

- **Painting or wallpapering** of real property, except where painting or wallpapering is incidental to the RMI service.
- Replacement or installation **of a septic tank system, siding, roof, plumbing, electrical, commercial refrigeration, irrigation, sprinkler or other similar system.**
 - Does not include the repair, replacement, or installation of electrical or plumbing components, water heaters, gutters, and similar individual items that are not part of new construction, reconstruction, or remodeling.
- Replacement or installation **of a heating or air conditioning unit or a heating, ventilation, and air conditioning system.**
 - Does not include the repair, replacement, or installation of gas logs, water heaters, pool heaters, and similar individual items that are not part of new construction, reconstruction, or remodeling.
- Replacement or installation **of roads, driveways, parking lots, patios, decks, and sidewalks.**

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Capital Improvement*

Definition (cont'd)

- Services performed to resolve an issue that was part of a real property contract if the services are performed **within six months of completion** of the real property contract or, **for new construction, within 12 months** of the new structure being occupied for the first time.
- **Landscaping** – A service that modifies the living elements of an area of land.
 - Installation of trees, shrubs, or flowers on land.
 - Tree trimming.
 - Mowing.
 - The application of seed, mulch, pine straw, or fertilizer to an area of land.
 - Does not include services to trees, shrubs, flowers, and similar items in pots or in buildings.
- **Addition or alteration to real property that is permanently affixed or installed to real property and is not an activity listed in the definition of RMI services.**

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Erroneous Collection of Sales Tax – Real Property Contract

IMPORTANT NOTICE: ERRONEOUS COLLECTION OF SALES TAX ON A REAL PROPERTY CONTRACT

Session Laws 2016-94 enacted by the 2016 General Assembly included a provision that amended the language in N.C. Gen. Stat. § 105-164.4H(c) regarding the provisions of N.C. Gen. Stat. § 105-164.11(a)(2), retroactive to January 1, 2015. As amended, the provisions of N.C. Gen. Stat. § 105-164.11(a)(2) may apply to an erroneous collection of sales tax by a real property contractor or a retailer-contractor on the gross receipts of a real property contract.

N.C. Gen. Stat. § 105-164.11(a)(2) provides, in part, “[i]f the Secretary determines that a [real property contractor or retailer-contractor] who overcollected sales tax on a transaction is instead liable for a use tax on a related transaction, the Secretary may allow the [real property contractor or retailer-contractor] to offset the use tax liability with the overcollected sales tax.” The Secretary shall not allow an offset if the real property contractor or retailer-contractor has elected to receive a refund of the overcollected tax from the Department as permitted under N.C. Gen. Stat. § 105-164.11(a)(1) that requires the real property contractor or retailer-contractor to give the purchaser credit for or a refund of tax collected in error before requesting a refund from the Department.

A real property contractor or retailer-contractor, that collected and remitted sales tax on the gross receipts of a real property contract on or after January 1, 2015 in error and that also paid sales or use tax on the purchase price of tangible personal property transferred to the real property contractor’s or retailer-contractor’s customer as part of a real property contract, may be due a refund. A real property contractor or retailer-contractor who paid use tax directly to the Department on the purchase price of tangible personal property used to fulfill the real property contract and who wishes to receive credit against the use tax due for a portion of the sales tax collected on the related transaction in error, should submit a claim for refund to the Department on Form E-588, Business Claim for Refund State, County and Transit Sales and Use Taxes, and include documentation to substantiate the refund request.

A real property contractor or retailer-contractor who paid sales and use tax directly to a seller on the purchase price of tangible personal property used in fulfilling the real property contract and who also collected sales tax on the gross receipts derived from the real property contract, may either 1) request a refund of the tax paid to the seller that collected and remitted the tax to the Department or 2) refund or credit the sales tax collected in error to its customers and the provisions of N.C. Gen. Stat. § 105-164.11(a)(1) apply.

Application of Sales and Use Tax on RMI applies to:

- Tangible personal property
 - A motor vehicle
 - Digital property
 - Real property
- The term does not include services used to fulfill a real property contract taxed in accordance with N.C. Gen. Stat. 105-164.4H



*Effective retroactively to January 1, 2017, for sales and purchases occurring on or after such date unless amendments increase a sales or use tax liability, then effective August 11, 2017.

- To keep or attempt to keep property or a motor vehicle in working order to avoid breakdown and prevent deterioration or repairs. Examples include to clean, wash, or polish property.
- To calibrate, refinish, restore, or attempt to calibrate, refinish, or restore property or a motor vehicle to proper working order or good condition. This activity may include replacing or putting together what is torn or broken.
- To troubleshoot, identify, or attempt to identify the source of a problem for the purpose of determining what is needed to restore property or a motor vehicle to proper working order or good condition. **The term includes activities that may lead to the issuance of an inspection report.**
- To install, apply, connect, adjust, or set into position tangible personal property, digital property, or a motor vehicle. **The term includes floor finishing and the installation of carpet, flooring, floor coverings, windows, doors, cabinets, countertops, and other installations where the item being installed may replace a similar existing item. The replacement of more than one of a like-kind item, such as replacing one or more windows, is a single repair, maintenance, and installation service. The term does not include an installation defined as a capital improvement under G.S. 105-164.3(2c)d.**
- To inspect or monitor property or a motor vehicle, but does not include security or similar monitoring services for real property.

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- An item exempt from sales and use tax.
- The following inspections:
 - An inspection performed where the results are included in a report for the sale or financing of real property.
 - An inspection of the structural integrity of real property, provided the charge for the inspection is separately stated.
 - An inspection to a system that is a capital improvement under G.S.105-164.3(2c)f, provided the inspection is to fulfill a safety requirement and provided the charge for the inspection is separately stated.
- Services performed for a person by a related member as defined by N.C. Gen. Stat. § 105-130.7A.
- **Cleaning of real property, except . . . for a pool, fish tank, or other similar aquatic feature.**
- Pest control service.
- Motor vehicle emissions and safety inspection fee.
- Removal of waste, trash, and debris except . . . portable toilets.
- Moving services.
- **Services performed on an animal such as microchipping a pet, hoof shoeing.**

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Effective retroactively to January 1, 2017 through June 30, 2018

- If the Secretary of Revenue determines that a retailer paid sales and use taxes on a product that becomes a part of or is applied to a purchaser's property as part of a retail sale of taxable repair, maintenance, and installation services to real property that occurs on or after January 1, 2017 through June 30, 2018, the Secretary will allow the retailer to offset the sales tax liability due on the taxable repair, maintenance, and installation services by the amount of sales and use tax originally paid on the product. The retailer must be able to substantiate the amount of tax originally paid on the product by invoice or other documentation.
- Additionally, a retailer entitled to a credit for tax originally paid on a product as provided above, may reduce the taxable receipts for an applicable reporting period by the taxable purchase amount of the product on which tax was originally paid in lieu of a determination being made by the Secretary.
- The credit provision does not apply to a product stored, used, or consumed by the retailer unless the product becomes a part of or is applied to a purchaser's property as part of a retail sale of repair, maintenance, and installation services to real property.

NCDOR Service Contract Exemptions*

- G.S. 105-164.13(61a) – Contains complete list of exemptions.
- Examples:
 - Service contract for an item exempt from sales and use taxes.
 - Qualifying farm machinery, mill machinery, etc.
 - Service contract for cleaning of real property.
 - Custodial services, carpet cleaning, window washing
 - A transmission, distribution, or other network asset contained on utility-owned land, right-of-way, or easement.
 - A qualified aircraft.
 - A qualified jet engine.



*Effective retroactively to January 1, 2017, for sales and purchases occurring on or after such date

A service contract for real property that includes two or more services, one of which is subject to sales and use tax and one of which is not subject to sales and use tax.

Tax applies to the sales price of or gross receipts derived from a mixed service contract unless one of the following applies:

- Allocation. – The person determines an allocated price for the taxable portion of the service contract based on a reasonable allocation of revenue that is supported by the person's business records kept in the ordinary course of business. In this circumstance, tax applies to the allocated price of the taxable portion of the service contract.
- Ten percent (10%) test. – The allocated price of the taxable portion of the service contract does not exceed ten percent (10%) of the price of the contract.

Exceptions. – The tax imposed by this section does not apply to a any of the following:

- A security or similar monitoring contract for real property.
- A contract to provide a certified operator for a wastewater system.



Example: Service contract that provides for both custodial services for a pool house and for maintaining the pool.

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NCDOR Sales Tax Base Expansion Protection Act

- N.C. Gen. Stat. § 105-244.3 was enacted in order to allow a grace period.
- N.C. Department of Revenue shall take no action to assess any tax due for a filing period beginning on or after March 1, 2016, and ending before January 1, 2018, if one or more conditions apply and the retailer did not receive specific written advice from the Secretary of Revenue for the transactions at issue for the laws in effect for the applicable periods. However, some limitations do exist for the conditions set out in the statutes.
- To review the conditions and limitations specified within the statute refer to Session Law 2017-204 Section 2.8(c) pg. 22 at www.ncleg.net/Sessions/2017/Bills/Senate/PDF/S628v7.pdf
- Important Notice issued September 6, 2017
 - http://www.dornc.com/taxes/sales/impnotice090617_expansion_protection_act.pdf

IMPORTANT NOTICE: SALES TAX BASE EXPANSION PROTECTION ACT

The Governor signed into law S.L. 2017-204 that amended Article 9 of Chapter 105 of the General Statutes by adding a new section, N.C. Gen. Stat. § 105-244.3, Sales tax base expansion protection act. N.C. Gen. Stat. § 105-244.3 provides the following:

(a) **Grace Period.** – The Department shall take no action to assess any tax due for a filing period beginning on or after March 1, 2016, and ending before January 1, 2018, if one or more of the conditions of this subsection apply and the retailer did not receive specific written advice from the Secretary for the transactions at issue for the laws in effect for the applicable periods. The conditions are as follows:

- (1) A retailer failed to charge sales tax due on separately stated installation charges that are part of the sales price of tangible personal property or digital property sold at retail for a filing period beginning on or after March 1, 2016, and ending before January 1, 2018.
- (2) A person failed to properly classify themselves as a retailer in retail trade for the filing period beginning on or after March 1, 2016, and ending before January 1, 2017, and did not charge sales tax on all retail transactions but rather treated some transactions as real property contracts in error for sales and use tax purposes. This subdivision does not prohibit the Secretary from assessing use tax on purchases used to fulfill a transaction erroneously treated as a real property contract.
- (3) A person treated a transaction as a real property contract in error and did not collect sales tax on the transaction as a retail sale for a filing period beginning on or after March 1, 2016, and ending before January 1, 2018. This subdivision does not prohibit the Secretary from assessing use tax on purchases used to fulfill a transaction erroneously treated as a real property contract.
- (4) A person failed to collect sales tax on the sales price of a service contract for one or more components, systems, or accessories for a motor vehicle for a filing period beginning on or after March 1, 2016, and ending before January 1, 2017, where the contract was sold by a motor vehicle dealer, a motor vehicle service agreement company, or a motor vehicle dealer on behalf of a motor vehicle service agreement company.
- (5) A person failed to collect sales tax on the retail sale of a service contract for tangible personal property that becomes a part of or is affixed to real property for a filing period beginning on or after March 1, 2016, and ending before January 1, 2018.
- (6) A person failed to collect sales tax on the retail sale of a service contract for a pool, a fish tank, or similar aquatic feature for a filing period beginning on or after January 1, 2017, and ending before January 1, 2018, provided the person paid tax on any purchases used to fulfill the service contract.
- (7) A person failed to collect sales tax on the sales price of or the gross receipts derived from the retail sale of a home warranty for a filing period beginning on or after January 1, 2017, and ending before January 1, 2018, provided the warranty includes coverage for real property.
- (8) A person failed to collect sales tax on the portion of a mixed contract for repair, maintenance, and installation services that exceeds ten percent (10%) for a transaction for a filing period beginning on or after March 1, 2016, and ending before January 1, 2017. This subdivision does not prohibit the Secretary from assessing use tax on purchases used to fulfill a mixed contract.

Sales Tax Base Expansion Protection Act (Cont'd)

(9) A person treats a transaction as a real property contract for remodeling instead of the retail sale of repair, maintenance, and installation services sold at retail for a filing period beginning on or after March 1, 2016, and ending before January 1, 2018. This subdivision does not prohibit the Secretary from assessing use tax on purchases used to fulfill the transaction.

(b) **Limitations.** – This section does not prohibit the following assessments:

(1) The assessment of tax collected by a person and not remitted to the Department.

(2) The assessment of tax due on an amount included in the definition of sales price where a retailer failed to charge or remit the tax, except as allowed under subsection (a) of this section.

(3) The assessment of use tax on purchases as provided in subsection (a) of this section.

Additional Information

Various sales and use tax law changes were enacted during the 2017 General Assembly Session applicable to repair, maintenance, and installation services; real property contracts; service contracts; and other topics. The Department will publish additional information regarding the changes in the near future.

To the extent there is any change in the rate or amount of tax, change to a statute or regulation, or new case law subsequent to the date of this notice, the provisions in this important notice may be superseded or voided. To the extent that any provisions in any other notice, directive, technical bulletin, or published guidance issued prior to the date of this notice conflicts with this important notice, the provisions contained in this important notice supersede.

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Questions

