

NEW LAW CLARIFIES SALES TAX ON LABOR

On August 11, 2017, the Governor signed [SB 628 \(Various Changes to the Revenue Laws\)](#) which, among other provisions, contained several clarifying changes to sales and use tax on labor applicable to residential construction. Here is a brief description of the sales tax law and the fixes which NCHBA helped bring about:

CURRENT LAW: All labor pursuant to a “real property contract” (between a real property contractor and another person to perform construction, reconstruction, or remodeling with respect to a capital improvement) is not subject to the sales or use tax. Sales tax continues to be levied on the materials. A “capital improvement” is “an alteration to real property that is new construction, reconstruction, or remodeling of a building, structure, or fixture on land that becomes part of the real property or is permanently installed in the real property”.

In short, labor charges for new construction and most remodeling activities are not subject to sales tax on labor because they will meet the definition of “capital improvement” pursuant to a “real property contract”.

SPECIFIC EXAMPLES: NCHBA fought to keep the specific exclusion of the “performance of work that requires the issuance of a permit under the State Building Code” (a residential project that costs \$15,000 or more) as a specific statutory example of a “capital improvement”. Also excluded from taxation are services performed to resolve an issue that was part of a real property contract within twelve months of the new structure being occupied for the first time (warranty call-backs). The new law also expands the definition of “capital improvement” to include patios and decks. Painting and wallpapering continue to be exempt from tax on labor except where they are “incidental” to the RMI service. NCHBA was able to expand the term “remodeling” to include “a transaction where the internal structure or design of one or more rooms or areas within a room or building are substantially changed.” However, “the term does not include a single repair, maintenance, and installation service.” Other exempt activities and are listed on the [NC Department of Revenue’s website](#).

LAW CLEARLY STATES THAT GENERAL CONTRACTOR MUST PROVIDE AFFIDAVIT (Form E-589CI) TO SUBCONTRACTOR: To notify the subcontractor that the project is a capital improvement (and therefore, exempt), the general contractor must provide the [Form E-589CI](#) to each subcontractor. However, a separate form may not be required to be supplied to the same subcontractor for each project (see “blanket use” instructions on form).

TAX ON RMI LABOR DUE WHEN NOT A CAPITAL IMPROVEMENT: A single repair, maintenance or installation (RMI) service does not qualify as a capital improvement. The replacement of a fixture in or on a building or structure is not a capital improvement unless the replacement is a part of remodeling. See RMI examples also listed on the [NC Department of Revenue’s website](#).

MIXED TRANSACTION TEST INCREASED TO 25%: Some remodeling projects may include activities which qualify as a capital improvement (no tax on labor) and activities that constitute a repair (tax on labor). However, no tax will be due on labor in these “mixed transactions” if the price of the repair, maintenance or installation (RMI) service does not exceed twenty-five percent (25%) of the contract price (was 10% under old law). If the RMI portion of the job exceeds 25% of the contract price, then sales and use tax applies only to the RMI labor portion of the contract.

ALL TYPES OF COMMERCIAL REMODELING ARE NOW EXEMPT: Under the old law, commercial remodeling done by a tenant or lessee was not defined as a capital improvement unless the project was given immediately to the owner. The new law fixes this problem and all types of commercial remodeling are now exempt from the sales tax on labor if it otherwise meets the definition of a capital improvement.

USE FORM E-595E WHEN PURCHASING ITEMS FOR AN RMI: Since the homeowner pays the sales tax on the entire sales price of an RMI project (labor, materials and any markup) for a repair, maintenance or installation, you should use the Form E-595E when purchasing items to use for that nonexempt project. This form notifies the retailer to not charge for the sales tax on the materials used. The [Form E-595E](#) is located on the DOR website.

FOR MORE INFORMATION: Contact Mike Carpenter, mcarpenter@nchba.org, or Tim Minton, tminton@nchba.org, or call NCHBA at (800) 662-7129.