

**North Carolina Department of Revenue
Post Office Box 25000
Raleigh, North Carolina 27640-0001**

To Registered Taxpayers:

This document lists the major changes made by the 2008 Session of the General Assembly to the taxes administered by the Sales and Use Tax Division. The document also includes rate changes authorized by the 2007 General Assembly that are effective October 1, 2008. Legislative changes supersede any information previously set forth in Sales and Use Tax Administrative Rules or Technical Bulletins relating to any subject matter of the legislation. Part I lists the changes to sales and use tax rates; Part II lists the remaining legislative changes. The changes in both Parts are cited in order of effective date. A more detailed explanation of the legislative changes is available in the 2008 Tax Law Changes, which will be available on the Department's website.

PART I: RATE CHANGES

Effective October 1, 2008

Change in State and Local Rates

The general State rate of tax will increase from 4.25% to 4.5%. The third one-half percent (0.5%) local tax under Article 44 will decrease to one-quarter percent (0.25%). These changes occur as the State continues assuming Medicaid responsibilities for the counties. The total of the State and local rates of tax does not change, and the "combined general rate" that applies only to telecommunications and ancillary services, video programming, and spirituous liquor other than mixed beverages does not change as a result of the simultaneous changes in the State and local rates.

Additional Local Sales and Use Tax in Two Counties

The additional 0.25% local sales and use tax authorized by the 2007 General Assembly is levied by Cumberland and Haywood Counties effective October 1, 2008. The increase applies to sales of tangible personal property by merchants located in those counties and to sales of tangible personal property delivered into Cumberland and Haywood Counties by merchants in other counties. While the additional levy would result in an increase in the total local sales and use tax in those counties to 2.75%, the simultaneous changes in the State and local rates, which is also effective October 1, 2008, results in the local rate remaining at 2.5% in those counties. The general State rate increases to 4.5%, resulting in a total combined State and local rate of 7% in Cumberland and Haywood Counties. The "combined general rate" that applies only to telecommunications and ancillary services, video programming, and spirituous liquor other than mixed beverages remains at 7%.

PART II: OTHER LEGISLATIVE CHANGES

Effective January 1, 2004

Refund for University Affiliated Nonprofit Organizations

G.S. 105-164.14(b) is amended to allow a refund to a university affiliated nonprofit organization that procures, designs, constructs, or provides facilities to, or for use by, a constituent institution of The University of North Carolina. For purposes of this refund provision, a nonprofit organization includes an entity exempt from taxation as a disregarded entity of the nonprofit organization. The amendment is effective retroactively to January 1, 2004 and applies to purchases made on or after that date. A refund claim for the period January 1, 2004 through December 31, 2007 will be considered timely filed if it is submitted to the Department by October 15, 2008.

Effective July 1, 2008

Privilege Tax on Purchases by Industrial Machinery Refurbishing Companies

G.S. 105-187.51B is amended to provide that the 1% privilege tax with a maximum tax of eighty dollars (\$80.00) per article applies to purchases of equipment or an attachment or repair part for equipment by an industrial machinery refurbishing company that is included in industry group 811310 of NAICS. In order to be subject to the privilege tax, the equipment (or attachment to, or repair part for) must be capitalized by the company for tax purposes under the Code, used by the company in repairing or refurbishing tangible personal property, and considered mill machinery if it were purchased by a manufacturer and used to manufacture tangible personal property.

Refund for Qualifying Nonprofit Organizations Clarified

The refund provision for certain nonprofit organizations is rewritten to clarify the types of organizations that are eligible for semiannual refunds. As rewritten, G.S. 105-164.14(b) provides that an organization is eligible for refunds if it is exempt from income tax under section 501(c)(3) of the Code and is not classified in any of the following three major group areas of the National Taxonomy of Exempt Entities: Community Improvement and Capacity Building, Public and Societal Benefit, or Mutual and Membership Benefit. The change is effective July 1, 2008 for purchases made on or after that date. Additional information will be provided prior to January 1, 2009. The provisions related to nonprofit hospitals and qualified retirement facilities are unchanged.

Refund for Solar Electricity Generating Materials Manufacturing Facility

G.S. 105-164.14(j), which authorizes annual refunds to certain industrial facilities of sales and use taxes paid on qualified building materials, building supplies, fixtures, and equipment that become a part of the real property of the eligible facility, is rewritten to add a facility that is primarily engaged in solar electricity generating materials manufacturing. The statute contains a definition of "solar energy generating materials manufacturing." In order to qualify for a refund, the owner of the facility must invest at least the required amount of private funds to construct the facility in this State, and the business must satisfy a wage standard at the facility. A refund request is due by December 31 for the prior fiscal year ending June 30; a refund applied for after the due date is barred. The provisions are effective July 1, 2008 for purchases made on or after that date and are repealed for sales made on or after January 1, 2013.

Effective July 16, 2008

New Sales Tax Holiday for Energy Star Qualified Products

G.S. 105-164.13D authorizes a new sales and use tax holiday for specific Energy Star qualified products. "Energy Star qualified product" is defined in G.S. 105-164.3(8g) as "A product that meets the energy efficient guidelines set by the United States Environmental Protection Agency and the United States Department of Energy and is authorized to carry the Energy Star label." Qualified products are exempt from all State and local sales and use taxes if sold between 12:01 A.M. on the first Friday of November and 11:59 P.M. the following Sunday. For 2008, the dates are Friday, November 7th through Sunday, November 9th. Only the following products will be exempt from tax during the holiday period: clothes washers, freezers, refrigerators, central air conditioners, room air conditioners, air-source heat pumps, geothermal heat pumps, ceiling fans, dehumidifiers, and programmable thermostats. **The exemption does not apply to rentals of qualified products and to sales of qualified products for use in a trade or business, including sales to contractors of products that will be installed in buildings or structures.** Rentals of qualified products and sales of qualified products for use in a trade or business, such as sales to contractors, are subject to sales and use tax even when rented or sold during the holiday period.

Aviation Fuel Refunds Extended

The aviation fuel refunds authorized under G.S. 105-164.14(a1) for interstate passenger air carriers and G.S. 105-164.14(l) for professional motorsports racing teams and motorsports sanctioning bodies were scheduled to expire for purchases made on or after January 1, 2009. As rewritten, the provisions are repealed for purchases made on or after January 1, 2011.

Small Business Protection Act

This new act requires the Secretary of Revenue to reduce certain sales and use tax assessments against small businesses and waive any penalties imposed when all of the following conditions are met: (1) The gross receipts of the business for the calendar year preceding the year in which the audit began, combined with the gross receipts of all related persons, do not exceed \$1,800,000. (2) The business remitted to the Department all the sales and use taxes it collected during the audit period. (3) The business had not been told by the Department in a prior audit to collect sales and use taxes in the circumstance that is the basis of the assessment, as reflected in the written audit comments of the prior audit. (4) The business made a good faith effort to comply with the sales and use tax laws and the assessment is based on the incorrect application of one of the following areas: the rate of tax that applies to prepared food; the distinction between a retailer and a performance contractor; the distinction between a service that is necessary to complete the sale of tangible personal property (taxable) and a service that is incidental to the sale of tangible personal property (not taxable); or the determination of whether a person is a manufacturer. The amount by which an assessment must be reduced is either 90%, 95%, or 98% and is determined by the average monthly gross receipts of the business for the calendar year preceding the year in which the audit period begins, combined with the average monthly gross receipts of all related persons; the reduction applies only to the amount attributable to the incorrect application of tax to one of the four areas listed above. In addition, the law pertaining to the effect of the Secretary's interpretation of revenue laws is amended to provide relief from liability as a result of erroneous verbal advice in addition to erroneous written advice, provided the Department's records establish that it provided erroneous verbal advice. The provisions pertaining to reductions of certain assessments expires January 1, 2010.

Another provision of the act, which is effective January 1, 2009, requires that, for conversations conducted by telephone or in person, the Secretary of Revenue or his representative must document advice about the application of a tax to the taxpayer in specific circumstances if requested by the taxpayer. The taxpayer must furnish the Secretary his identifying information and must request that the advice be documented in his records. A similar provision is effective July 1, 2009 and applies only to sales tax inquiries by a person who is not registered and is requesting advice as to whether he is required to be registered.

Effective July 28, 2008

Reporting Sales and Use Taxes for Simultaneous State and Local Rate Changes

New G.S. 105-164.16(e) provides that, when the State and local sales and use tax rates change on the same date because one increases and the other decreases but the "combined general rate" does not change, special rules apply for taxes payable on the gross receipts from certain periodic payments. For tangible personal property leased for a definite period of time where the agreement was entered into prior to the effective date of the rate changes, the sales and use taxes payable on the gross receipts from lease or rental payments received after the effective date of the changes are to be reported at the "new" or "changed" rates. Sales and use taxes payable on the gross receipts from installment sale payments received after the effective date of the changes by a taxpayer who reports the installment sale on a cash basis are reportable in accordance with the "new" or "changed" rates. For instance, when the simultaneous State rate increase and local rate decrease occur October 1, 2008, tax on lease/rental payments and installment sale payments will be reported using the rates in effect October 1, 2008 rather than the rates in effect prior to the simultaneous changes.

Effective August 1, 2008

Exemption for Interior Design Services Made in Conjunction with Sales

G.S. 105-164.13(59) is a new exemption for interior design services provided in conjunction with the sale of tangible personal property. In order to qualify for the exemption, the charge representing the interior design services must be separately stated from the sales price of the tangible personal property.

Exemption for Disaster Assistance Debit Purchases

G.S. 105-164.13(58) is a new exemption for tangible personal property purchased with a client assistance debit card issued for disaster assistance relief by a State agency or a federal agency or instrumentality

such as the Federal Emergency Management Administration (FEMA) or the American Red Cross. Prior to August 1, 2008, such purchases were subject to the applicable State and local sales and use tax.

Effective August 2, 2008

Distribution of Supplemental PEG Support Clarified

G.S. 105-164.44I is amended and a new section, G.S. 105-164.44J, is enacted to clarify the distribution of supplemental PEG (Public, Educational, or Governmental) channel funding. Cities or counties must certify to the Department by July 15th of each year the number of qualifying PEG channels provided for use during the preceding fiscal year by a cable service provider. The certification must include the following: (1) An identification of each channel as a public, an education, or a government channel. (2) The name and signature of the PEG channel operator. If a qualifying PEG channel has more than one PEG channel operator, the city or county must include the name of each operator of the PEG channel and a PEG channel operator may be included on the certification of only one county or city for each type of PEG channel that it operates. (3) Any other information required by the Department. For the 2008 certification, the date the certification must be submitted is September 15, 2008 instead of July 15th. In addition, a provision is added that, if a county or city certifies a PEG channel in error, it must submit a revised certification and return all funds distributed as a result of the error.

Effective August 7, 2008

Changes to Direct Mail Sourcing Principles

G.S. 105-164.4B(d)(2), which sets out an exception to the general sourcing principles for sourcing direct mail, was rewritten to correct an incorrect reference. As rewritten, when the purchaser of direct mail does not provide the seller a direct pay permit or other information to show the jurisdictions to which the direct mail is to be delivered, direct mail is sourced to the address from which it was shipped.

Effective August 9, 2008

Changes to Solid Waste Disposal Tax Provisions

Article 5G, which imposes a tax of \$2.00 per ton on the disposal of municipal solid waste and construction and demolition debris in a landfill permitted under Article 9 of Chapter 130A of the General Statutes and on the transfer of such waste and debris to a transfer station permitted under the same Article for disposal outside the State, is amended to provide that returns and payments of the tax are due quarterly. A return and payment for a calendar quarter are due by the last day of the month following the end of the quarter. The tax was effective July 1, 2008; the first return will be due October 31, 2008 for taxes due for the period July 1 through September 30. A bad debt deduction provision is also added that allows an owner or operator to recover tax paid on tonnage it received but for which it was never compensated.

Effective January 1, 2009

State Sales Tax Exemption for Baked Goods Sold by Artisan Bakeries

G.S. 105-164.13B, which provides that certain food is exempt from State sales and use tax unless it is included in one of five specific categories, is amended. New subdivision (a)(4), which provides that "prepared food" is not included in the exemption but is subject to the applicable State and local rates of tax, is rewritten. As rewritten, prepared food **other than bakery items sold without eating utensils by an artisan bakery** is subject to the applicable State and local rates of tax. Bakery items (bread, rolls, buns, biscuits, bagels, croissants, pastries, donuts, danish, cakes, tortes, pies, tarts, muffins, bars, cookies, and tortillas) sold without eating utensils by an artisan bakery are exempt from State tax and subject to only the 2% local tax applicable to sales of qualifying food. An "artisan bakery" is a bakery that derives over 80% of its gross receipts from bakery items **and** whose annual gross receipts, combined with the gross receipts of all related persons as defined in G.S. 105-163.010, do not exceed \$1,800,000.00.

Frequently asked questions with responses can be found on the Department's website at www.dornrc.com. If you have questions about the information in this document or about sales and use tax, you may contact the Taxpayer Assistance and Collection Center at 1-877-252-3052 (toll-free) or write to the Taxpayer Assistance Division, North Carolina Department of Revenue, Post Office Box 25000, Raleigh, North Carolina 27640-0001.