North Carolina Department of Revenue

Roy Cooper
Governor

Ronald G. Penny
Secretary

August 9, 2017

[redacted]

Re: [redacted]
Private Letter Ruling Request
Account ID: [redacted]
FEIN: [redacted]

Dear [redacted]:

The Department has completed its review of your request for a written determination on behalf of your client, [redacted], ("Taxpayer"). In making this written determination, the Department has considered the facts presented in your initial request as well as all supplemental information provided or available to the Department.

This private letter ruling is a written determination issued under N.C. Gen. Stat. § 105-264.2 and applies the tax law to a specific set of existing facts furnished by you on behalf of Taxpayer. This written determination is applicable only to the taxpayer addressed herein and as such has no precedential value except to the taxpayer to whom the determination is issued on behalf of the Department. Pursuant to N.C. Gen. Stat. § 105-264, "[i]t is the duty of the Secretary to interpret all laws administered by the Secretary."

## Overview and Relevant Facts

You state that Taxpayer "takes rough cut slabs and blocks of natural stone . . . and cuts, shapes, polishes, finishes . . ." to the specifications of a customer's project needs. Photograph number one shows slabs of natural stone that may be chosen by a customer of Taxpayer. The stones with which Taxpayer works include "granite, marble, soapstone, limestone, slate, semi-precious materials, onyx and other natural products."

"[S]paces for sinks, faucets and other fixtures are cut and finished. Modifications are made to the natural material for purposes of additional support and reinforcement. . . . The edges and surfaces of stones are polished or textured according to the customer's desires. Thinner materials are mitered together to make thicker pieces for walls, tubs and countertops."

In an email response to the Department's questions dated August 28, 2015, you stated Taxpayer "does have some written agreements with customers . . . [I]t is not uncommon for an order to be placed several months before [Taxpayer] can provide the requested products to the customer." Once work on a customer's order has begun, "customer orders are nonrefundable." Taxpayer's "[c]ustomers are billed for orders upon delivery of the products." Taxpayer obtains its natural stone by purchasing "slabs of stone . . . from other companies that take the stone out of the ground."

On June 20, 2016 and January 13, 2017 based on the Department's review, the Taxpayer's website at [redacted] stated that its products are "natural stone." The [redacted] webpage of Taxpayer's website states, "[redacted]." The last section of Taxpayer's [redacted] website page states: "[redacted]"

Additionally, Taxpayer's website has a [redacted] webpage which explains the [redacted] The [redacted] are described as:

1) Schedule an appointment,
2) Tour showroom,
3) Reserve stone and choose edge,
4) Schedule template,
5) Template day,
6) Fabrication, and
7) Installation.

## Issue

Should Taxpayer be classified as a "manufacturing industry" for purposes of the privilege tax imposed by N.C. Gen. Stat. § 105-187.51(a)(1) on purchases of mill machinery or mill machinery parts or accessories?

In support of your contention that Taxpayer should be classified as a "manufacturing industry," you provided an analysis that looks at two North Carolina Supreme Court cases, *Master Hatcheries, Inc. v. Coble,* 286 N.C. 518; 212 S.E. 2d 150 (1975) and *Bleacheries, Inc. v. Johnson, 266 N.C. 692, 147 S.E. 2d 177 (1966)*. *Master Hatcheries, Inc. v. Coble, supra,* involved a mass production process whereby eggs were the raw materials being hatched into baby chicks. A new and different product was produced. Likewise, *Bleacheries, Inc. v. Johnson, supra,* involved taking greige goods and converting them into five different types of finished fabrics: corduroy, plisse, crease-resistant goods, non-shrinking goods, and lawns and organdies. New and different products were produced.

You also relied on 17 North Carolina Administrative Code ("NCAC") 07B .3402, MONUMENT MANUFACTURERS: TOOLS AND SUPPLIES. As the heading states, this administrative rule

applies to "monument manufacturers." Taxpayer is not a "monument manufacturer;" thus, this rule does not apply to Taxpayer. When firms perform only slight modifications to tangible personal property, including granite, marble, and similar materials, they are not functioning as manufacturers.

## Applicable Statutes and References

Under Article 5F of the North Carolina Revenue Act ("Act")[1], N.C. Gen. Stat. § 105-187.50 *et. seq*., a privilege tax is imposed on certain industries that purchase machinery or equipment that meet certain requirements. The privilege tax rate is one percent (1%) of the purchase price of the eligible machinery, equipment, or other personal property purchased, with a maximum of eighty dollars ($80.00) per article. Id. Specifically, N.C. Gen. Stat. § 105-187.51(a)(1) provides a privilege tax is imposed on "[a] manufacturing industry or plant that purchases mill machinery or mill machinery parts or accessories for storage, use, or consumption in this State."

N.C. Gen. Stat. § 105-164.13(5a) provides an exemption from sales and use tax for "[p]roducts that are subject to tax under Article 5F of this Chapter." A taxpayer bears the burden of establishing it is eligible for an exemption from sales and use tax and entitled to the 1% privilege tax rate. *Piedmont Canteen Service, Inc. v. Johnson*, 256 N.C. 155, 123 S.E. 2d 582 (1962) (one who claims an exemption from tax has the burden of bringing itself within the exemption). Additionally, the 1% privilege tax rate set forth in Article 5F of the Act is a lesser tax rate than the generally applicable rate of sales tax set forth in N.C. Gen. Stat. § 105-164.4. For this reason, Article 5F constitutes a partial exemption from taxation and must therefore be strictly construed against the claim of partial exemption and in favor of the imposition of the higher rate of tax. *Hatteras Yacht Co. v. High*, 265 N.C. 653, 144 S.E.2d 821 (1965).

Published for the purpose of presenting the administrative interpretation and application of the Act, the Department's administrative rules and Sales and Use Tax Technical Bulletins are considered "prima facie correct." Id. The following administrative rules and referenced Sales and Use Tax Bulletin are applicable to the classification of manufacturing activities for the application of the 1% privilege tax rate:

17 NCAC 07D .0102(a) states the three principle activities of a manufacturer are production, distribution, and administration. In defining the term "production," 17 NCAC 07D .0102(a)(1) states, in part, "[p]roduction as a phase of industrial or manufacturing operations shall mean all steps performed in processing and refining rooms, and in other quarters and departments of a plant, where conditioning, treating or other operations are done on ingredient materials as an actual routine on a processing or assembly line turning out a finished product of manufacture. It shall also include the movement of raw materials or ingredients from an inventory or a stockpile located on the premises of the manufacturing facility to the assembly or processing line, the movement of goods in process along the processing line and the movement of manufactured goods from the premises of the manufacturing facility. Purchases by a manufacturing industry or plant of machinery, and parts and accessories therefore for use in production, as defined above, are classified as mill machinery and mill machinery parts and accessories."

*See also* North Carolina Sales and Use Tax Technical Bulletins, Section 57-1 Classification of Activities of Manufacturing and Industrial Processing.

[1] References to the Act and North Carolina General Statutes are based on the laws in effect as of the date of issuance of this private letter ruling.

17 NCAC 07D .0104
Purchases of tangible personal property by a manufacturer for use in its business are subject to either the sales or use tax or privilege tax.

Under Article 5 of the Act, N.C. Gen. Stat. § 105-164.1 *et. seq*., Subchapter VIII: Local Government Sales and Use Tax, and Chapter 1096 of the 1967 Session Laws, State, applicable local, and applicable transit sales and use taxes are imposed on a purchaser in the State on the purchase price of tangible personal property, certain digital property, and certain services at the percentage rates listed in subdivision N.C. Gen. Stat. § 105-164.4. N.C. Gen. Stat. §§ 105-164.3(46), 105-164.6, 105-468, 105-483, 105-498, 105-507.2, 105-509.1, and 105-537.

N.C. Gen. Stat. § 105-164.6(a) provides, in part, that "[a]n excise tax at the applicable rate set in [N.C. Gen. Stat. §] 105-164.4 is imposed on" the purchase price of "[t]angible personal property or digital property purchased inside or outside this State for storage, use, or consumption in this State, . . . [t]angible personal property or digital property leased, or rented inside or outside this State for storage, use, or consumption in this State" or "[s]ervices sourced to this State." N.C. Gen. Stat. § 105-164.6(b) states "[t]he tax imposed by this section is payable by the person who purchases, leases, or rents tangible personal property or digital property or who purchases a service. If the property purchased becomes a part of a building or other structure in the State and the purchaser is a contractor or subcontractor, the contractor, the subcontractor, and the owner of the building are jointly and severally liable for the tax. The liability of a contractor, a subcontractor, or an owner who did not purchase the property is satisfied by receipt of an affidavit from the purchaser certifying that the tax has been paid." N.C. Gen. Stat. §§ 105-164.3(14), 105-164.3(32), 105-164.3(33), 105-164.3(44), 105-164.3(49), and 105-164.6.

The term "purchase price" is defined as having "the same meaning as the term 'sales price' when applied to an item subject to use tax." N.C. Gen. Stat. § 105-164.3(33). "Sales price" is defined, in part, as "[t]he total amount or consideration for which tangible personal property, digital property, or services are sold, leased, or rented." N.C. Gen. Stat. § 105-164.3(37).

## Ruling

The Sales and Use tax statutes do not provide a definition for the term "manufacture;" therefore, the Department is guided by North Carolina State court decisions. In *Duke Power Co. v. Clayton,* 274 N.C. 505; 164 S.E.2d 289 at 295 (1968), the North Carolina Supreme Court stated "[t]he word *manufacture* 'is not susceptible of an accurate definition that is all-embracing or all-exclusive, but is susceptible of many applications and many meanings. . . . In its generic sense, 'manufacturing' has been defined as the producing of a new article of use or ornament by the application of skill and labor to the raw materials of which it is composed.' 55 C.J.S. Manufactures, § 1 at 667 and 670 (1948). *Accord*, *Bleacheries Co.,v. Johnson, Comm'r of Revenue*, [266 N.C.692] at 695-96, 147 S.E. 2d at 179; *City of Louisville v. Ewing Vol-Allmen Dairy Co*., 268 Ky. 652, 105 S.W. 2d 801 (1937). 'To make an article manufactured, the application of the labor must result in a new and different article with a distinctive name, character, or use. To make an article manufactured, the application of the labor must result in a new and different article with a distinctive name or use.' Inhabitants of *Leeds v. Maine Crushed Rock & Gravel Co*., 127 Me. 51, 56, 141 A. 73, 75 (1928). Thus, the usual connotation of *manufacturing* is the making of a new product from raw or partly wrought materials. Carbonize coal in a coke oven and a new and different product, coke, has been manufactured. Crush coal, however, and it is still merely coal."

In *Duke Power Co. v. Clayton*, *supra*, the court quoted the United States Supreme Court in *Anheuser-Busch Brewers Ass'n v. United States*, 207 U.S. 556 at 562; 28 S. Ct. 204 at 206-07 (1908), speaking through Mr. Justice McKenna, who said, "Manufacture implies a change, but every change is not manufacture, and yet every change in an article is the result of treatment, labor, and manipulation. But something more is necessary. . . . There must be a transformation; a new and different article must emerge, 'having a distinctive name, character, or use.'"

Based on the information obtained, Taxpayer does not transform natural stone into a new and different product which is no longer natural stone. Although a made-to-order granite countertop is the end result purchased by Taxpayer's customer, the granite slab used to make the countertop remains a granite slab. The character of the granite remains unchanged. Taxpayer is not producing a "new and different article" and is not classified as a "manufacturing industry" for purposes of the privilege tax imposed on purchases of mill machinery under N.C. Gen. Stat. § 105-187.51(a)(1).

Taxpayer's purchases of machinery and equipment are not subject to the 1% privilege tax rate imposed on the purchase price of mill machinery and mill machinery parts or accessories pursuant to N.C. Gen. Stat. § 105-187.51(b). Therefore, Taxpayer's purchases are not exempt from sales and use tax under N.C. Gen. Stat. § 105-164.13(5a). Taxpayer's purchases of machinery and equipment for use in completing the customization of stone products to meet customers' specifications are subject to the general 4.75% State, applicable local (2.00% or 2.25%), and applicable transit (0.50%) rates of sales and use tax.

This ruling is based solely on the facts submitted to the Department of Revenue for consideration of the transactions described. If the facts and circumstances given are not accurate, or if they change, then the taxpayer requesting this ruling may not rely on it. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material aspect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that this document is not to be cited as precedent and that a change in statute, a regulation, or case law could void this ruling.

Issued on behalf of the Secretary of Revenue
By the Sales and Use Tax Division