



North Carolina Department of Revenue

Roy Cooper
Governor

Ronald G. Penny
Secretary

October 4, 2018

Re: Request for Written Determination Ruling Regarding Tobacco Products Excise Tax

Dear [REDACTED]

The North Carolina Department of Revenue (Department) is in receipt of the request for a written determination made on behalf of [REDACTED] (Company) via letter dated December 20, 2017 along with the five hundred dollar fee. Please accept this letter as the Department's written determination in response to your inquiry whether the Company has a business nexus with the State of North Carolina and is required to obtain a license for tobacco products tax under North Carolina General Statute (N.C. Gen. Stat.) § 105-113.36. In making this written determination, the Department has considered the facts presented in your initial request as well as the supplemental information provided to the Department.

This written determination is issued under N.C. Gen. Stat. §§ 105-264 and 105-264.2 and applies the current tax law to a specific set of existing facts as furnished by the requesting Company. This written determination is applicable only to the Company addressed herein and as such has no precedential value except to the Company to whom the Department issues this determination.

The statement of facts submitted for the Department's consideration is as follows:

- ***The Company provides the following background information on their business structure:***

"The Company manufactures, sells, and distributes ENDS (Electronic Nicotine Delivery Systems) which include e-cigarettes and vaping liquids and devices. The Company's e-cigarettes and vaping liquids contain nicotine. The Company has employees in 11 states, but no employee resides in North Carolina. The Company's sales force does periodically travel to North Carolina to solicit sales.

The Company is headquartered outside of North Carolina. The Company uses a third-party warehouse to hold its inventory which is located [sic] the same state where they are headquartered (outside of North Carolina).

The Company's products are manufactured [REDACTED] and the manufacturing relationship is brokered through a third-party based [REDACTED]. The Company sends purchase orders and payments to the third-party [REDACTED] and the third-party then remits the purchase orders and money to the manufacturers.

The Company purchases the liquid components that go into their products from US vendors outside of [REDACTED]. The liquids are sent directly to a third-party who blends the liquid components into a finished e-liquid. The blender of the liquids is located outside of North Carolina.

The blended liquids are picked up at the blender's location by third-party importer/exporters who ships the liquids from [REDACTED] via air for manufacturing. The manufacturers complete the finished goods and they are sent back [REDACTED]. The first point of entry is in [REDACTED]. Upon [REDACTED] the items are shipped to the Company's third-party warehouse in a state outside of North Carolina via common carrier.

The Company sells its products to 3 types of customers:

1. **Distributors:** Products are sold to distributors who supply various grocery/convenient mart retailers. Some of The Company's distribution customers have some of their warehouses located in North Carolina. In those instances, the product is received into the distribution customer's North Carolina warehouse via common carrier direct from the Company's warehouse. From there, the products are distributed directly to retailers located both inside and outside of North Carolina.
 2. **Retailers:** The Company has no direct sales to retailers in North Carolina.
 3. **Digital:** The Company also directly sells to consumers via the Company's website. Items purchased on the website are shipped from the Company's third-party warehouse outside of North Carolina. The Company's products are shipped into North Carolina via common carrier directly to the end consumer."
- *The Company provides the following assertions and/or understanding of North Carolina requirements for tobacco product vendors:*

The Company asserts they do not have a business nexus with North Carolina, nor a requirement to obtain a license based on North Carolina's statutory provision establishing the primary liability for the excise tax on tobacco products other than cigarettes as well as the statutory definitions of a wholesale dealer, retail dealer, manufacturer, and place of business. The Company adds to this assertion by proffering that the Company ships their manufactured vapor products into North Carolina via common carriers.

- The Company indicates that if the Department agrees the Company has no business nexus, nor a requirement to obtain a license, the Company acknowledges a duty to provide the Department shipping reports to show the volume of consumable vapor products shipped into North Carolina.
- The Company asserts that if the Department determines a business nexus exists and the Company must obtain a license, then only the vaping liquid is subject to the tax, instead of the entire e-cigarette, because only the vaping liquid is consumable as per the statutory definition of consumable vapor products. In addition to the above assertion, the Company further states that if required to be licensed, it is the Company's belief that as the first wholesale/retail dealer who acquires or handles the product is liable for the tax, that sales to other wholesale/retail dealers are not exempt.

- ***The Department posed two (2) follow-up questions via email dated April 26, 2018, to which the Company provided the following responses via email dated April 27, 2018:***
 1. When asked whether sales people who travel into North Carolina on behalf of the Company bring any inventory into the State with them, the Company responded in the negative.
 2. When asked whether sales people who travel into North Carolina on behalf of the Company solicit or direct North Carolina residents to the Company's website to order products, the Company responded in the negative, indicating the Company's sales people are soliciting wholesale sales, not internet sales.

Issue(s):

1. Does the Company have nexus and a requirement to obtain a license for the Tobacco Products Tax?
2. If the Company does not have nexus and a requirement to obtain a license, do they have a reporting requirement?
3. If it is determined the Company does have nexus and a requirement to obtain a license for the purposes of the Tobacco Products Tax, the Company seeks confirmation of the following:
 - a. What e-cigarettes/vapor products are covered by the tax?
 - b. Are products containing zero milligrams of nicotine exempt?
 - c. What is the applicable tax rate for consumable vapor products?
 - d. If the Company is required to have a license, what is the amount of any associated license fee?
 - e. Are sales to other wholesale dealers or retail dealers exempt?
 - f. What are the return due dates?

Department's Response:

1. Does the Company have nexus and a requirement to obtain a license for the Tobacco Products Tax?

North Carolina levies an excise tax on tobacco products, including vapor products. See *N.C.G.S. § 105-113.35(a1)*. The excise tax on vapor products is levied upon the "consumable product" which is defined as "[a]ny nicotine liquid solution or other material containing nicotine that is depleted as a vapor product is used."

In the instant case, the Company, in its statement of facts submitted for the Department's consideration, indicates it "manufactures, sells, and distributes ENDS (Electronic Nicotine Delivery Systems) which include e-cigarettes and vaping liquids and devices." The Company further provides the following list of customers to whom the Company sells its products:

- "1. **Distributors:** Products are sold to distributors who supply various grocery/convenient mart retailers. Some of The Company's distribution customers have some of their

warehouses located in North Carolina. In those instances, the product is received into the distribution customer's North Carolina warehouse via common carrier direct from the Company's warehouse. From there, the products are distributed directly to retailers located both inside and outside of North Carolina.

2. **Retailers:** The Company has no direct sales to retailers in North Carolina.
3. **Digital:** The Company also directly sells to consumers via the Company's website. Items purchased on the website are shipped from the Company's third-party warehouse outside of North Carolina. The Company's products are shipped into North Carolina via common carrier directly to the end consumer."

Based on the information provided, the Company acknowledges they are a manufacturer of vapor products and the Company's activities are consistent with North Carolina's statutory definition of a manufacturer. See *N.C.G.S. § 105-113.4(6)*. In North Carolina, manufacturers of tobacco products other than cigarettes are deemed wholesale dealers. See *N.C.G.S. § 105-113.4(14)*. Additionally, the type of products the Company indicates they manufacture, distribute and sell, are taxable in North Carolina.

As the tobacco product the Company manufactures is taxable in North Carolina, it must be determined if the mechanisms the Company uses to sell vapor products in North Carolina creates a nexus with the State subjecting the Company to licensure and tobacco product excise tax reporting and payment requirements.

In the present case, the Company is engaged in transactions of tobacco products (i.e. vapor products) that do not currently subject the Company to state and/or local licensing and excise tax laws through the PACT Act. However, nexus generally refers to the degree and amount of business activity that must be present in a state for that business to be subject to the state's taxing authority. The amount of activity or connection with the state necessary to create a licensure and excise tax requirement is found in a state's statutes, rules, regulations, and/or case law.

North Carolina has two (2) administrative rules that are relevant to Company's inquiry regarding nexus and tobacco product licensing requirements. The rules read as follows:

"17 NCAC 04C .1402 SALES TO LICENSED DEALERS ONLY

- (a) No manufacturer may make shipments of other tobacco products directly to a person in this State not qualified and licensed as a wholesale or retail dealer of other tobacco products.
- (b) Any manufacturer of other tobacco products shipping such products to other wholesale or retail dealers who are licensed pursuant to G.S. 105-113.36 for payment of the other tobacco products excise tax is relieved of the requirement of paying the tax."

"17 NCAC 04C .1403 MANUFACTURERS ACTING AS RETAILER

A retail dealer who manufactures other tobacco products and sells those products to consumers in this State is liable for the tax except for those transactions in other tobacco products which meet exemption from the tax under G.S. 105-113.35."

Based on the above administrative rules and the Company's statement of facts, which 1) does not specify if the distributors to whom the Company sell are licensed North Carolina wholesale dealers and 2) indicates the

Company sells direct to consumers within North Carolina, the Company must obtain a North Carolina wholesale dealer license for tobacco products other than cigarettes. Licensure as a wholesale dealer will cover the Company's retail sales of tobacco products for purposes of reporting and paying of excise taxes.

In the alternative, if the Company does not choose to be a North Carolina licensed wholesale dealer, they may not sell or ship vapor products direct to customers, but rather, may only sell their vapor products to licensed North Carolina wholesale dealers. The licensed North Carolina wholesale dealer purchasing from the Company would then be responsible for reporting and paying the excise tax on the Company's vapor product brought into the State. Thereafter, the wholesale dealer may resell the product, tax-paid, to other wholesale dealers, retail dealers, and/or ultimate consumers.

Finally, in response to the U.S. Supreme Court decision in *South Dakota v. Wayfair, Inc.*, et al., 585 U.S. ____ (2018), that overruled *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), and *National Bellas Hess, Inc. v. Department of Revenue of Illinois*, 386 U.S. 753 (1967), the North Carolina Department of Revenue, Sales and Use Tax Division has issued a Directive associated with the prospective requirement for remote sellers located outside North Carolina to collect and remit North Carolina Sales and Use tax.

Beginning November 1, 2018, the Department will enforce N.C.G.S. § 105-164.8(b) concerning remote sales and applicable remote sellers having gross sales sourced to the state in excess of \$100,000 or having 200 or more separate transactions sourced to the state in the previous or current calendar year. The Directive may be found using the following link to the Department's website: https://files.nc.gov/ncdor/documents/files/sd-18-6_0.pdf

Department's Response:

2. If the Company does not have nexus and a requirement to obtain a license, do they have a reporting requirement?

As indicated above, it is the Department's determination that if the Company sells taxable vapor products to either unlicensed North Carolina wholesale or retail dealers or sells taxable vapor products directly to consumers, the Company must obtain a North Carolina wholesale dealer license. Along with licensure, the Company does have a monthly reporting requirement and must remit any excise taxes due with the monthly B-A-102 return.

In the alternative, if the Company chooses not to obtain a North Carolina wholesale dealer license, then the Company must make all sales of their vapor products to North Carolina licensed wholesale and/or retail dealers. If the Company opts not to obtain their wholesale dealer license, they must still submit shipping reports pursuant to N.C. Gen. Stat. § 105-113.37(d). Shipping reports are required of any person who transports tobacco products upon any North Carolina public highway, road, or street. Shipping reports do not have a specific due date, but are required upon demand by the Department.

Department's Response:

3. If it is determined the Company does have nexus and a requirement to obtain a license for the purposes of the Tobacco Products Tax, the Company seeks confirmation of the following:
 - a. What e-cigarettes/vapor products are covered by the tax?

The excise tax levied on vapor products pursuant to N.C. Gen. Stat. § 105-113.35(a1) is upon the consumable product. N.C. Gen. Stat. § 105-113.4(1k) defines "consumable

product” as “[a]ny nicotine liquid solution or other material containing nicotine that is depleted as a vapor product is used.” The term vapor product is defined in N.C. Gen. Stat. § 105-113.4(13a), and specifically states, the term includes “any vapor cartridge or other container of nicotine in a solution or other form” used with or in an electronic nicotine delivery system (ENDS). Thus, the tobacco products excise tax is upon the entire e-liquid solution containing nicotine used with or in an ENDS.

- b. Are products containing zero milligrams of nicotine exempt?

Consumable vapor products containing zero milliliters of nicotine are not subject to the tobacco products excise tax.

- c. What is the applicable tax rate for consumable vapor products?

Pursuant to N.C. Gen. Stat. § 105-113.35 (a1) the tax on vapor products “is levied at the rate of five cents (5¢) per fluid milliliter of consumable product.”

- d. If the Company is required to have a license, what is the amount of any associated license fee?

The Department has determined that if the Company sells vapor products to unlicensed North Carolina wholesale dealers or direct to North Carolina resident consumers, the Company must be licensed as a wholesale dealer of tobacco products other than cigarettes. N.C. Gen. Stat. § 105-113.36 states that “a wholesale dealer shall obtain for each place of business a continuing tobacco products license and shall pay a tax of twenty-five dollars (\$25.00) for the license.” Further, N.C. Gen. Stat. § 105-113.4A(b) requires applicants for tobacco products licensure to either be organized in this State or be authorized to transact business in this State by registering with the North Carolina Secretary of State.

In addition to licensure as a wholesale dealer, the Company must also post a surety bond or irrevocable letter of credit pursuant to N.C. Gen. Stat. § 105-113.38 in an amount that is two times the wholesale dealer’s average expected monthly tax liability, but may not be less than two thousand dollars (\$2,000) nor more than two million dollars (\$2,000,000).

- e. Are sales to other wholesale dealers or retail dealers exempt?

N.C. Gen. Stat. § 105-113.35 (b) provides that the wholesale dealer or retail dealer who first acquires or otherwise handles tobacco products is liable for the tax. It also states that a wholesale dealer or retail dealer who brings into this State a tobacco product made outside the State is the first person to handle the tobacco product in this State.

The only exemptions are found at N.C. Gen. Stat. § 105-113.35(a2) which indicates the taxes imposed on tobacco products other than cigarettes do not apply to tobacco products 1.) sold outside the State, 2.) sold to the federal government, and 3.) are provided as a sample and distributed without charge. The tobacco products excise tax is only collected once on the same product, thus when the wholesale dealer or retailer dealer who first

acquires or handles the product per N.C. Gen. Stat. § 105-113.35(b) pays the tax, no subsequent sales to either wholesale dealers or retail dealers are subject to the same tax.

f. What are the return due dates?

N.C. Gen. Stat. § 105-113.37 states in part “a report is due on a monthly basis. A monthly report covers sales and other activities occurring in a calendar month and is due within 20 days after the end of the month covered by the report.”

This written determination is based solely on the facts described in the statement of facts submitted to the Department for consideration of the transactions described. If the facts and circumstances described are not accurate or if there are other facts not previously disclosed that may result in the Department reaching a different conclusion, this written determination may not be relied upon. If a taxpayer relies on this written determination and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material aspect from the facts and circumstances presented for consideration, the written determination will not afford the taxpayer any protection from adverse tax consequences. A written determination is not equivalent to a Technical Advice Directive that generally affects a large number of taxpayers. A written determination has no binding effect on the Department with regard to any person other than the taxpayer who requested and received the determination. It should be noted this document shall not be cited or relied upon as precedent and that a change in statute, regulation, or case law could void this determination.

I hope this clarifies your issues regarding your client and its Excise Tax requirements under the North Carolina Tobacco Products Tax. If I can be of further assistance, please do not hesitate to let me know.

Respectfully Submitted,

[REDACTED]
[REDACTED]
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cc: [REDACTED]