



**STATE OF NORTH CAROLINA
OFFICE OF ADMINISTRATIVE HEARINGS**

October 20, 2023

Laura Lansford, Rulemaking Coordinator
Department of Revenue
Sent via email only to: laura.lansford@ncdor.gov

Re: Objections to Department of Revenue (DOR) Rules 17 NCAC 07B .1202, .1303, .1404, .1601, .1605, .1705, .2001, .2002, .2204, .4109

Dear Ms. Lansford:

This letter will serve as the written notice of objection pursuant to G.S. 150B-21.12.

At its meeting on October 19, 2023, the Rules Review Commission (RRC) objected to 17 NCAC 07B .1202, .1303, .1404, .1601, .1605, .1705, .2001, .2002, .2204, .4109 pursuant to G.S. 150B-21.9(a). Specifically, with respect to these rules, the RRC adopted the opinions of counsel attached hereto and incorporated by reference. Please respond to these objections in accordance with the provisions of G.S. 150B-21.12.

If you have any questions regarding the Commission's actions, please let me know.

Sincerely,

/s/ Seth Ascher
Seth Ascher
Commission Counsel

CC: Andrew O. Furuseth, andrew.furuseth@ncdor.gov
Tenisha S. Jacobs, tenisha.jacobs@ncdor.gov

Donald Robert van der Vaart, Director
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RRC STAFF OPINION

PLEASE NOTE: THIS COMMUNICATION IS EITHER 1) ONLY THE RECOMMENDATION OF AN RRC STAFF ATTORNEY AS TO ACTION THAT THE ATTORNEY BELIEVES THE COMMISSION SHOULD TAKE ON THE CITED RULE AT ITS NEXT MEETING, OR 2) AN OPINION OF THAT ATTORNEY AS TO SOME MATTER CONCERNING THAT RULE. THE AGENCY AND MEMBERS OF THE PUBLIC ARE INVITED TO SUBMIT THEIR OWN COMMENTS AND RECOMMENDATIONS (ACCORDING TO RRC RULES) TO THE COMMISSION.

AGENCY: Department of Revenue

RULE CITATION: 17 NCAC 07B .1202

RECOMMENDATION DATE: October 17, 2023

RECOMMENDED ACTION:

- Approve, but note staff's comment
- Object, based on:
 - Lack of statutory authority
 - Unclear or ambiguous
- Unnecessary
 - Failure to comply with the APA
- Extend the period of review

COMMENT:

Staff recommends objection to this rule but notes that it is a particularly close question.

Note that because staff believed this rule was objectionable for fundamentally the same necessity issue as previously objected to rules, staff included this rule in a draft opinion rather than formal requests for changes. The agency's response raised legislative history unique to this rule, which necessitated a separate opinion.

G.S. 150B-21.9(a)(3) charges the Commission with determining whether a rule: "is reasonably necessary to implement or interpret an enactment of the General Assembly, or of Congress, or a regulation of a federal agency. The Commission shall consider the cumulative effect of all rules adopted by the agency related to the specific purpose for which the rule is proposed."

The department is implementing G.S. 105-164.4(a)(1), which states in relevant part: "The general rate of tax applies to the following items sold at retail: . . . The sales price of each article of tangible personal property that is not subject to tax under another subdivision in this section. A sale of a freestanding appliance is a retail sale of tangible personal property."

The Department is interpreting a law administered by the Secretary, an authority granted by G.S. 105-264(a), which reads in full:

It is the duty of the Secretary to interpret all laws administered by the Secretary. The Secretary's interpretation of these laws shall be consistent with the applicable rules.

Seth Ascher
Commission Counsel

An interpretation by the Secretary is prima facie correct. When the Secretary interprets a law by adopting a rule or publishing a bulletin or directive on the law, the interpretation is a protection to the officers and taxpayers affected by the interpretation, and taxpayers are entitled to rely upon the interpretation. If the Secretary changes an interpretation, a taxpayer who relied on it before it was changed is not liable for any penalty or additional assessment on any tax that accrued before the interpretation was changed and was not paid by reason of reliance upon the interpretation.

G.S. 105-264(a) establishes the Secretary's duty to interpret certain laws and acknowledges that such interpretations might be contained in rules, bulletins, or directives. This Department of Revenue statute does not provide guidance as to what types of interpretations should be adopted by rule or published in a bulletin directive. As a result, the APA's requirement that only "reasonably necessary" rules be approved by this Commission and put in the code would apply.

To the extent that this rule is interpreting statutory language, it appears to be stating that items purchased by an accommodation provider are "tangible personal property." This interpretation appears plain on the face of the statute as currently enacted.

The agency, however, has pointed to a session law and codified language suggesting that the General Assembly believed such a rule was necessary. To summarize: S.L. 2017-204 enacted G.S. 105-244.4, which provided a mechanism for relief from tax penalty for accommodation providers who failed to pay the appropriate tax on these purchases prior to January 1, 2018. The bill analysis noted that even with a Department bulletin in place, "some members of the vacation rental industry have incorrectly interpreted or applied the law with respect to the rental of linens as part of a vacation rental and have been assessed by the Department. This section would permit the Department to reduce an assessment by 90% under [certain] circumstances."

Assuming, arguendo, that it is proper to rely on such a bill analysis to determine legislative meaning, it appears that the legislature determined that an ambiguity existed regarding the "rental of linens as part of a vacation rental." However, the legislature did not appear to clarify the statute or rulemaking authority to address this.

Ultimately, staff recommends objection but notes that the necessity of this rule appears to be a close question. On the one hand, action by the General Assembly suggests that it believed a certain degree of ambiguity existed. On the other hand, the text of the statute currently in force seems clear in the area covered by the rule. Staff believes that the General Assembly's identification of a possible ambiguity in this case is not enough to justify the necessity of a rule, as opposed to clarification by other means available.

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AGENCY: Department of Revenue

RULE CITATION: 17 NCAC 07B .1303, .1404, .2001, .2002

RECOMMENDATION DATE: October 17, 2023

RECOMMENDED ACTION:

- Approve, but note staff's comment
- Object, based on:
 - Lack of statutory authority
 - Unclear or ambiguous
 - Unnecessary
 - Failure to comply with the APA
 - Extend the period of review

COMMENT:

Staff recommends objection to these four rules as written, but notes that resolving the clarity issues discussed in the omnibus staff opinions could also resolve the necessity issues.

Note that because staff believed that these rules are objectionable for fundamentally the same necessity issue as previously objected to rules, staff provided the agency with a draft of this opinion rather than formal requests for changes. The agency provided a written response which suggested that a rule on this subject matter may be necessary. However, it is staff's opinion that the rule as written is not necessary.

G.S. 150B-21.9(a)(3) charges the Commission with determining whether a rule: "is reasonably necessary to implement or interpret an enactment of the General Assembly, or of Congress, or a regulation of a federal agency. The Commission shall consider the cumulative effect of all rules adopted by the agency related to the specific purpose for which the rule is proposed."

The department is implementing G.S. 105-164.4(a)(1), which states in relevant part: "The general rate of tax applies to the following items sold at retail: . . . The sales price of each article of tangible personal property that is not subject to tax under another subdivision in this section. A sale of a freestanding appliance is a retail sale of tangible personal property."

As written, these rules appear to be examples of taxable items which are already covered by the plain language of G.S. 105-164.4(a)(1). However, in communication with staff regarding each of these four rules, the department has identified terms defined in G.S. 105-164.3 which may be

Seth Ascher
Commission Counsel

ambiguous under the circumstances described by these rules, thus supporting the necessity of interpretation by the department.

To summarize the four rules:

.1303: As written, the rule indicates that purchases of items to be given away by or at the direction of the purchaser are retail sales of tangible personal property. Staff believes that this, by itself, is unnecessary for reasons stated in the other staff opinions issued on 17 NCAC 07B .0115 and similar rules.

However, the department's response indicates that the rule is necessary to interpret how the terms "sales price" and "purchase price" apply to items which are given away by a retailer at the direction of a purchaser. Staff believes that a clear statement of the interpretation being made would likely resolve the necessity issue in this rule.

.1404: As written, the rule indicates that purchases of medical supplies, instruments, and equipment by "physicians, dentists, hospitals, and other consumers of medical supplies" are retail sales of tangible personal property. Staff believes that this, by itself, is unnecessary for reasons stated in the other staff opinions issued on 17 NCAC 07B .0115 and similar rules.

However, the department's response indicates that the rule is necessary to interpret that "physicians, dentists, and hospitals" are "consumers" of medical supplies and not "retailers" of medical supplies. Staff believes that a clear statement of the interpretation being made would likely resolve the necessity issue in this rule.

.2001: As written, the rule indicates that retail sales to an employee of the seller are retail sales. Staff believes that this, by itself, is unnecessary for reasons stated in the other staff opinions issued on 17 NCAC 07B .0115 and similar rules.

However, the department's response indicates that the rule is necessary to interpret that an employer who is not in business as a retailer, is a retailer if they make sales to employees. Further, such sales are not covered by the "occasional and isolated sales exception" in rule 17 NCAC 07B .0112. Staff believes that a clear statement of the interpretation being made would likely resolve the necessity issue in this rule.

.2002: As written, the rule indicates that purchases by an employer of items to provide as gifts or compensation are retail sales of tangible personal property. Staff believes that this, by itself, is unnecessary for reasons stated in the other staff opinions issued on 17 NCAC 07B .0115 and similar rules.

However, the department's response indicates that the rule is necessary to interpret that a business that purchases an item as a gift or compensation is a "consumer" of the item. Further, that a manufacturer that ordinarily does not collect sales tax on items sold for resale must pay sales tax if those items are given away as gifts or compensation. Staff believes that a clear statement of the interpretation being made would likely resolve the necessity issue in this rule.

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AGENCY: Department of Revenue

RULE CITATION: 17 NCAC 07B .1601, .1605, .1705, .2204, .4109

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COMMENT:

Staff recommends objection to these five rules for substantially the same reasons as 17 NCAC 07B .0115, .3101, and .3107. The Commission objected to those rules at its September 21, 2023, meeting. This memo summarizes those reasons and the distinctions between each rule.

Note that because staff believes these rules are objectionable for fundamentally the same necessity issue as previously objected to rules, staff provided the agency with a draft of this opinion rather than formal requests for changes. The agency provided a written response which did not change staff's recommendation.

G.S. 150B-21.9(a)(3) charges the Commission with determining whether a rule: "is reasonably necessary to implement or interpret an enactment of the General Assembly, or of Congress, or a regulation of a federal agency. The Commission shall consider the cumulative effect of all rules adopted by the agency related to the specific purpose for which the rule is proposed."

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G.S. 105-264(a) establishes the Secretary's duty to interpret certain laws and acknowledges that such interpretations might be contained in rules, bulletins, or directives. This Department of Revenue statute does not provide guidance as to what types of interpretations should be adopted by rule or published in a bulletin directive. As a result, the APA's requirement that only "reasonably necessary" rules be approved by this Commission and put in the code would apply.

To the extent that these rules are interpreting statutory language, they appear to be stating that particular objects are "tangible personal property" or that particular categories of sales are retail sales. These interpretations are plain on the face of the statute. As a result, the rule is unnecessary.

Put another way, if these rules were repealed, it appears that nothing would change about the actual sales tax implementation in this State. Given such an effect, it could not be said that this rule is "necessary to implement or interpret" an enactment of the General Assembly.

In considering the cumulative effect of rules proposed for this purpose, staff estimates that of the ninety rules currently pending from the Department of Revenue, at least half raise a similar necessity problem.

The rules appear to make the following "interpretations":

.1601: Purchases of items by nonprofit entities are subject to tax, unless purchased for retail. Note that G.S. 105-164.13(5) provides an explicit statutory exception for items purchased for resale and that G.S. 105-164.14(b) provides for the refund of certain sales and use taxes paid by nonprofit entities.

.1605: Nonprofit entities that make retail sales are retailers and such sales are subject to taxes.

.1705: Sales to housing authorities are taxable sales and housing authorities are not entitled to refunds under G.S. 105-164.14. Note that G.S. 105-164.14(c) states that it "applies only to the following governmental entities" before providing a list. Housing authorities are not on that list.

.2204: Retail sales of food by transportation companies within this state are retail sales subject to tax.

.4109: Sales of blueprints, photographs, and other items to architectural or engineering firms are retail sales of tangible personal property, unless purchased for resale. Note that G.S. 105-164.13(5) provides an explicit statutory exception for items purchased for resale.