

STATE OF NORTH CAROLINA
COUNTY OF WAKE

BEFORE THE
SECRETARY OF REVENUE

IN THE MATTER OF:

The Denial of Refund of Sales and Use Tax)
for the Period January 1, 2003 through)
June 30, 2003 by the Secretary of Revenue)
of North Carolina)
)
vs.)
)
[Taxpayer])

FINAL DECISION
Docket No. 2005-134

This matter was heard before the Assistant Secretary of Revenue, Eugene J. Cella, in the City of Raleigh on August 17, 2005, upon an application for hearing by the Taxpayer, wherein Taxpayer protested the denial of refund of Sales and Use Tax for the period January 1, 2003 through June 30, 2003. The hearing was held by the Assistant Secretary of Revenue under the provisions of N.C. Gen. Stat. § 105-260.1 and was attended by W. Timothy Holmes, Assistant Director, Sales and Use Tax Division; Amy McLemore, Administration Officer, Sales and Use Tax Division; and Gregory P. Roney, Assistant Attorney General, N.C. Department of Justice. Taxpayer was represented by [Vice President & CFO of Taxpayer Entity]; [Representatives of Accounting Firm for the Taxpayer], and [Director and Representatives of a Tax Service Firm].

The evidentiary record was held open for 30 days after the hearing. By letter dated September 15, 2005, Taxpayer requested an additional 60 days to submit a brief and material into the record for consideration. The Taxpayer's request was granted, and the record was held open until November 15, 2005. The Department was also given 30 days to respond to Taxpayer's additional submissions.

ISSUE

The issue to be decided in this matter is as follows:

Is Taxpayer one of the types of nonprofit entities listed in N.C. Gen. Stat. § 105-164.14(b) and, therefore, eligible to receive semiannual refunds of the sales and use taxes paid on direct purchases of tangible personal property for use in carrying on charitable operations?

EVIDENCE

The following items were introduced into evidence at the hearing:

1. Memorandum dated May 16, 2001, from the Secretary of Revenue to the Assistant Secretary of Administrative Hearings, designated Exhibit E-1.
2. Copy of Form E-585, Nonprofit and Governmental Entity Claim for Refund State and County Sales and Use Taxes, dated July 24, 2003, for the semiannual period January 1, 2003 through June 30, 2003, designated Exhibit E-2.
3. Copy of letter dated October 7, 2003, from the Central Examination Division to the Taxpayer, designated Exhibit E-3.
4. Copy of letter dated October 13, 2003, from the Taxpayer to the Central Examination Division, and the attached copy of the Taxpayer's Articles of Incorporation and its Bylaws, designated Exhibit E-4.
5. Copy of letter dated January 16, 2004, from the Central Examination Division to the Taxpayer, designated Exhibit E-5.
6. Copy of letter dated February 16, 2004, from the Taxpayer's representative to the Sales and Use Tax Division, designated Exhibit E-6.
7. Copy of letter dated February 24, 2004, from the Sales and Use Tax Division to the Taxpayer's representative, designated Exhibit E-7.
8. Copy of letter dated March 5, 2004, from the Taxpayer's representative to the Sales and Use Tax Division, and the following exhibits:
 - A. Copy of October 7, 2003 letter from the Central Examination Division to the Taxpayer, designated Exhibit E-8 A.
 - B. Copy of October 13, 2003 letter from the Taxpayer to the Central Examination Division, designated Exhibit E-8 B.
 - C. Copy of the Taxpayer's Articles of Incorporation dated May 28, 2002, designated Exhibit E-8 C.
 - D. Copy of the Taxpayer's Bylaws, designated Exhibit E-8 D.
 - E. Copy of January 16, 2004 letter from the Central Examinations Division to the Taxpayer, designated Exhibit E-8 E.
 - F. Copy of the Taxpayer's Articles of Restatement dated October 10, 2002, designated Exhibit E-8 F.
 - G. Copy of November 6, 2002 letter from the Internal Revenue Service to the Taxpayer, designated Exhibit E-8G.
9. Copy of letter dated November 4, 2004, from the Sales and Use Tax Division to the Taxpayer's representative, designated Exhibit E-9.

10. Copy of Federal Form 1023, Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code, received from the Taxpayer's representative by facsimile on December 6, 2004, designated Exhibit E-10.
11. Copy of Exhibits B-H of the Taxpayer's Federal Form 1023, received from the Taxpayer's representative by facsimile on January 4, 2005:
 - B. List of the Taxpayer's activities, designated Exhibit E-11 B.
 - C. List of the Taxpayer's sources of financial support, designated Exhibit E-11 C.
 - D. List of the Taxpayer's officers and directors, designated Exhibit E-11 D.
 - E. Explanation of the Taxpayer's relationship to other organizations, designated Exhibit E-11 E.
 - F. Explanation of the Taxpayer's lease agreement with [nonprofit corporation from which Taxpayer was spun off], designated Exhibit E-11 F.
 - G. List of services rendered by the Taxpayer and the associated fees received, designated Exhibit E-11 G.
 - H. List of the Taxpayer's operating expenses, designated Exhibit E-11 H.
12. Copy of letter dated February 23, 2005, from the Sales and Use Tax Division to the Taxpayer's representative, designated Exhibit E-12.
13. Copy of letter dated March 7, 2005, from the Taxpayer's representative to the Sales and Use Tax Division, designated Exhibit E-13.
14. Copy of letter dated April 5, 2005, from the Assistant Secretary of Revenue to the Taxpayer's representative, designated Exhibit E-14.
15. Copy of letter dated April 15, 2005, from the Sales and Use Tax Division to the Taxpayer's representative, designated Exhibit E-15.
16. Copy of letter dated May 9, 2005, from the Taxpayer's representative to the Sales and Use Tax Division, designated Exhibit E-16.
17. Copy of letter dated June 20, 2005, from the Assistant Secretary of Revenue to the Taxpayer's representative, designated Exhibit E-17.
18. Copy of letter dated July 18, 2005, from the Assistant Attorney General to the Assistant Secretary of Revenue, designated Exhibit E-18.
19. Copy of letter dated July 27, 2005, from the Assistant Secretary of Revenue to the Taxpayer's representative, designated Exhibit E-19.

20. Copy of the Taxpayer's Articles of Incorporation dated May 28, 2002, designated Exhibit E-20.
21. Copy of the Taxpayer's Articles of Restatement dated October 9, 2002, designated Exhibit E-21.
22. Copy of the Taxpayer's Articles of Restatement dated May 12, 2005, designated Exhibit E-22.
23. Copy of [Newspaper] article dated March 15, 2005, designated Exhibit E-23.
24. Copy of [Newspaper] article dated April 5, 2005, designated Exhibit E-24.
25. Copy of [Taxpayer's] web site home page, printed on June 14, 2005, designated Exhibit E-25.
26. Copy of news release printed from [a web site] on June 14, 2005, designated Exhibit E-26.
27. Copy of venture funding information printed from [Taxpayer's] web site on June 14, 2005, designated Exhibit E-27.
28. Copy of press release dated April 26, 2005, printed from [Taxpayer's] web site, Exhibit E-28.
29. Listings of the Boards of Directors for [Taxpayer] and [nonprofit corporation from which Taxpayer was spun off], printed from their respective web sites, designated Exhibit E-29.
30. Copy of [Taxpayer's] web site printed on June 15, 2005, designated Exhibit E-30.
31. Copy of the Taxpayer's overview and history printed from [Taxpayer's] web site on June 15, 2005, designated Exhibit E-31.
32. Copy of the Taxpayer's brochure, designated Exhibit E-32.
33. Copy of the history and general information regarding [nonprofit corporation from which Taxpayer was spun off] printed from the [nonprofit corporation's] web site on June 15, 2005, designated Exhibit E-33.
34. Copies of Certificates of Assumed Name issued to [nonprofit corporation from which Taxpayer was spun off] by the Register of Deeds of Durham County on November 13, 2003, designated Exhibit E-34.

35. Copy of the Taxpayer's Federal Form 990, Return of Organization Exempt From Income Tax, for Tax Year 2002, designated Exhibit E-35.
36. Copy of the Taxpayer's Federal Form 990, Return of Organization Exempt From Income Tax, for Tax Year 2003, designated Exhibit E-36.
37. Copy of the Taxpayer's Form CD-405, C Corporation Tax Return 2003, designated Exhibit E-37.
38. Copy of [nonprofit endowment corporation's] Form 990, Return of Organization Exempt From Income Tax, for Tax Year 2002, designated Exhibit E-38.
39. Copy of [nonprofit endowment corporation's] Form 990, Return of Organization Exempt From Income Tax, for Tax Year 2003, designated Exhibit E-39.
40. Copy of Form 990, Return of Organization Exempt From Income Tax, for Tax Year 2002, for [nonprofit corporation from which Taxpayer was spun off], designated Exhibit E-40.
41. Copy of Form 990, Return of Organization Exempt From Income Tax, for Tax Year 2003, for [nonprofit corporation from which Taxpayer was spun off], designated Exhibit E-41.
42. Copy of Articles of Organization for [venture capital LLC owned by Taxpayer], dated September 30, 2002, and its annual reports for years ending December 31, 2002, December 31, 2003, and December 31, 2004, designated Exhibit E-42.
43. Copy of Secretary's Decision for Docket Number 2001-289, dated December 21, 2001, designated E-43.
44. Copy of brochure from [Taxpayer's customer], designated Exhibit E-44.
45. Copy of Form 990, Return of Organization Exempt From Income Tax, for Tax Year 2003, for [the nonprofit corporation Taxpayer's activities currently support], designated Exhibit E-45.
46. Copy of memorandum from the Assistant Attorney General to Sales and Use Tax Division dated August 3, 2005, designated Exhibit E-46.
47. Copy of Form D-403, 2002 Partnership Income Tax Return, for [venture capital limited partnership owned by Taxpayer], designated Exhibit E-47.
48. Copy of Form D-403, 2003 Partnership Income Tax Return, for [venture capital limited partnership owned by Taxpayer], designated Exhibit E-48.

49. Copy of letter dated August 3, 2005, from the Taxpayer's representative to the Assistant Secretary of Revenue, designated Exhibit E-49.
50. Copy of letter dated August 5, 2005, from the Assistant Secretary of Revenue to the Taxpayer's representative, designated Exhibit E-50.
51. Copy of letter from the Taxpayer to the Assistant Attorney General, received August 12, 2005, designated Exhibit E-51.
52. Copy of Exhibit A in support of the Taxpayer's letter to the Assistant Attorney General, received August 12, 2005, designated Exhibit E-52.
53. Copy of the Taxpayer's Incurred Cost Submission for Fiscal Year 2003 (only copy given to the Assistant Secretary of Revenue), designated Exhibit E-53.
54. Copy of the Taxpayer's Incurred Cost Submission for Fiscal Year 2004 (only copy given to the Assistant Secretary of Revenue), designated Exhibit E-54.
55. Comparison of customer and contract information contained in Exhibits E-13, E-51, and E-52, designated Exhibit E-55.
56. Copies of Forms Gen-58, Power of Attorney and Declaration of Representative, for the Taxpayer, [the venture capital LLC and venture capital limited partnership owned by Taxpayer], all dated August 16, 2005, designated Exhibit E-56.

Evidence presented by the Taxpayer at the hearing consisted of:

57. Binder of materials submitted by Taxpayer at the Hearing including duplicate copies of correspondence (Taxpayer's Exhibits 1-19), I.R.C. § 501(c)(3) (Taxpayer's Exhibit 20), G.S. 105-164.14 (Taxpayer's Exhibit 21), Tax Review Board Administrative Decision No. 389 (Taxpayer's Exhibit 22), and duplicate copies of Forms Gen-58 (Taxpayer's Exhibit 23), designated Exhibit TP-1.

Evidence presented by the Taxpayer, the Sales and Use Tax Division, and the Office of the Attorney General consisted of:

58. Letter dated September 15, 2005, from the Taxpayer's representative to the Assistant Secretary of Revenue, designated Exhibit TP-2.
59. Copies of Forms Gen-58, Power of Attorney and Declaration of Representative, for the Taxpayer, [the venture capital LLC and venture capital limited partnership owned by Taxpayer], all dated September 16, 2005, designated Exhibit TP-3.
60. Letter dated September 16, 2005, from the Assistant Attorney General to the Assistant Secretary of Revenue, designated Exhibit E-57.

61. Letter dated September 19, 2005, from the Assistant Secretary of Revenue to the Taxpayer and the Assistant Attorney General, designated Exhibit E-58.
62. Letter dated November 14, 2005, from the Taxpayer's representative to the Assistant Secretary of Revenue transmitting the following:
 - A. Brief of Taxpayer formerly [former Taxpayer name] in Support of Its Request for a Sales and Use Tax Refund Pursuant to North Carolina General Statute § 105-164.14, designated Exhibit TP-4 A.
 - B. Copy of N.C. Attorney General's Opinion dated June 3, 1980, designated Exhibit TP-4 B.
 - C. Copy of Final Decision of the Secretary of Revenue dated July 9, 2001, designated Exhibit TP-4 C.
 - D. Copy of Tax Review Board Administrative Decision No. 389, designated Exhibit TP-4 D.
 - E. Copy of IRS Private Letter Ruling 200537038, designated Exhibit TP-4 E.
 - F. Affidavit of [member of Taxpayer's board of directors], designated Exhibit TP-4 F.
 - G. Affidavit of [former North Carolina Governor], designated Exhibit TP-4 G.
 - H. Affidavit of [Taxpayer's president and CEO], designated Exhibit TP-4 H.
 - I. Affidavit of [representative of accounting firm representing the Taxpayer], designated Exhibit TP-4 I.
63. Memorandum from the Assistant Attorney General to the Assistant Secretary of Revenue responding to the Taxpayer's Brief, designated Exhibit E-59.

FINDINGS OF FACT

Based on the foregoing evidence of record, the Assistant Secretary makes the following findings of fact:

1. [Taxpayer] ("Taxpayer") is a corporation located in Research Triangle Park, North Carolina.
2. On July 24, 2003, Taxpayer filed a Nonprofit and Governmental Entity Claim for Refund of state and county sales and use taxes (Form E-585) ("Claim for Refund") for the period of January 1, 2003 through June 30, 2003.
3. The Taxpayer's claimed basis for the refund is that the Taxpayer is one of the types of nonprofit entities listed in N.C. Gen. Stat. § 105-164.14(b) and, therefore, eligible to receive semiannual refunds of the sales and use taxes paid on direct purchases of tangible personal property.

4. On January 16, 2004, the Department notified the Taxpayer in writing that the Taxpayer was not eligible to receive a refund of the sales and use taxes paid for the period in question.
5. By letter dated February 16, 2004, the Taxpayer's representative objected to the denial of the Claim for Refund and requested a hearing before the Secretary of Revenue.
6. By a post-hearing Brief, Taxpayer asserted federal and State constitutional challenges to the denial of the Claim for Refund.
7. The Taxpayer was incorporated May 28, 2002, and has since amended its Articles of Incorporation to change its name, along with various other changes, as follows: [Former Taxpayer Name] (used 5/28/2002 - 9/30/2002), [Former Taxpayer Name] (used 9/30/2002 - 9/11/2003), [Former Taxpayer Name] (used 9/11/2003 - 5/12/2005), [Former Taxpayer Name] (used on web site and brochure), and [Current Taxpayer Name] (used 5/12/2005 – present).
8. Taxpayer applied to the Internal Revenue Service ("IRS") to be recognized as a federally tax-exempt entity under section 501(c)(3) of the Internal Revenue Code ("I.R.C.") by an application dated July 3, 2002.
9. Taxpayer represented to the IRS that the Taxpayer would act as a supporting organization to another tax-exempt entity, [Supported Organization], and that the Taxpayer and [Supported Organization] would have overlapping purposes, activities, and boards of directors.
10. [Taxpayer] is also known as: [(former corporate name)], [(Certificate of Assumed Name)], [(Certificate of Assumed Name)], and [(name used on web sites)].
11. Based on the information the Taxpayer supplied the IRS and representations made by the Taxpayer, the IRS granted the application by letter dated November 6, 2002.
12. The Taxpayer's original Articles of Incorporation and each of two Restated Articles of Incorporation completely prohibit lobbying.
13. Taxpayer conducts lobbying activities. Exhibit E-35; Exhibit E-36.
14. Taxpayer paid one lobbying firm, [a lobbying company], \$352,865 in its 2002 fiscal year and \$290,439 in its 2003 fiscal year.
15. During its 2003 fiscal year, the Taxpayer's president devoted 10% to 20% of his time to lobbying activities.

16. Taxpayer does not currently have a board of directors which overlaps with [nonprofit corporation from which Taxpayer was spun off] as the Taxpayer represented to the IRS.
17. Only one board member is shared by Taxpayer and [nonprofit corporation from which Taxpayer was spun off].
18. Taxpayer received its assets from [nonprofit endowment corporation] during the 2002 fiscal year as reported on the 2002 IRS Form 990 filed by the [nonprofit endowment corporation] and 2002 IRS Form 990 filed by the Taxpayer.
19. Taxpayer was not created strictly as a result of the separation of [nonprofit corporation from which Taxpayer was spun off] into two entities but received assets and funding from other sources.
20. One source of Taxpayer's assets was [nonprofit endowment corporation] Endowment.
21. On May 12, 2005, the Taxpayer restated its Articles of Incorporation, dropping [nonprofit corporation from which Taxpayer was spun off] as the supported organization and naming the [nonprofit corporation Taxpayer's activities currently support] as the supported organization.
22. During the period at issue in the Claim for Refund, Taxpayer conducted two primary businesses: (1) venture capital investing ("VC") and (2) research and development ("R&D") under contracts to design or construct computer software systems and electronic systems.
23. Taxpayer is not a hospital described in N.C. Gen. Stat. § 105-164.14(b)(1).
24. Taxpayer is not an educational institution described in N.C. Gen. Stat. § 105-164.14(b)(2).
25. Taxpayer is not a qualified retirement facility described in N.C. Gen. Stat. § 105-164.14(b)(4).
26. Taxpayer owns and manages two venture capital funds: (1) [venture capital, LLC], (100% owned by Taxpayer) and (2) [venture capital limited partnership], (owned approximately 49% by the Taxpayer, 50% by [nonprofit corporation from which Taxpayer was spun off] and 1% by [venture capital, LLC]).
27. Taxpayer acts as the management company for both entities, and the Taxpayer's activities include the management of both entities.
28. Taxpayer's VC investing is not limited to any geographic area and is not limited to any charitable class.

29. The VC activities are dedicated to profitability where the Taxpayer, like any for-profit investor, will invest money, take preferred stock or convertible preferred debt, and seek a profitable exit opportunity.
30. Taxpayer's VC investing is a for-profit operation investing in the same businesses as other for-profit corporations and providing "traditional" VC funding.
31. Taxpayer conducts commercial VC investing.
32. Taxpayer competes with other for-profit companies for VC funding opportunities.
33. Taxpayer's R&D services were purchased by many for-profit, corporate customers.
34. Taxpayer is not conducting and disseminating fundamental research for public benefit.
35. Taxpayer's R&D services serve commercial and industrial operations to design, construct, and commercialize products.
36. For its 2003 fiscal year, Taxpayer admits some of its revenue is unrelated to its claimed charitable purpose and filed a C Corporation Tax Return with the State (Form CD-405) and an Exempt Organization Business Income Tax Return with the IRS (Form 990-T).
37. For its 2002 fiscal year which would have included the period of the Claim for Refund (i.e., January 1, 2003 through June 30, 2003), Taxpayer did not file a corporate income tax return.
38. For its 2002 fiscal year, Taxpayer provided a schedule detailing its revenues which reported \$3,113,629 gross revenue from private research contracts unrelated to its claimed exempt purpose for federal income tax purposes.
39. On its 2003 income tax returns, the Taxpayer claims an unreported, carryover net economic loss of \$167,255 for its 2002 fiscal year.
40. This carryover net economic loss reported on Taxpayer's 2003 returns represents commercial activities for the period of the Claim for Refund during Taxpayer's 2002 fiscal year.
41. Taxpayer's corporate income tax returns document Taxpayer's commercial activity which were reported as unrelated trade or business income and therefore were not related to any charitable purpose.

42. Taxpayer's R&D operations are commercial and have the goal to produce commercial products.
43. Taxpayer competes with other for-profit companies for R&D contracts.
44. Taxpayer's grant program is no more extensive than charitable gifts by for-profit companies.
45. Taxpayer's internship and co-op program providing internship and co-op opportunities in VC and R&D for an average of 5 students per year from local universities is no more extensive than internship programs by for-profit companies.
46. After the period in the Claim for Refund, Taxpayer sold all of its R&D operations for approximately \$5 million, effective March 14, 2005. The VC activities were not included in the sale.
47. Taxpayer's sale of its R&D operations occurring after the period in the Claim for Refund demonstrates that these operations were not essential to Taxpayer's claimed charitable purpose and could be sold.
48. Taxpayer's abandonment of [nonprofit corporation from which Taxpayer was spun off] as its supported organization after the period in the Claim for Refund and selection of [nonprofit corporation from which Taxpayer was spun off] as its supported organization demonstrates that Taxpayer's operations were not essential to Taxpayer's claimed charitable purpose to support [nonprofit corporation Taxpayer's activities currently support].
49. After the sale, the Taxpayer's only remaining activity is VC investing.
50. Taxpayer sold its R&D operations to focus on more profitable opportunities in its VC funding business.

CONCLUSIONS OF LAW

Based on the foregoing findings of fact, the Assistant Secretary makes the following conclusions of law:

1. Taxpayer filed a timely protest to the denial of refund of Sales and Use Tax and requested a hearing before the Secretary of Revenue.
2. The State imposes a sales tax at the applicable rate on a retailer's net taxable sales of tangible personal property. N.C. Gen. Stat. § 105-164.4. An additional local sales tax is levied on sales of tangible personal property subject to the

general State rate of tax. N.C. Gen. Stat. §§ 105-467; 105-483; 105-498; 105-519.

3. The State imposes a use tax on the storage, use, or consumption in this State of tangible personal property purchased inside or outside the State for storage, use, or consumption in this State. N.C. Gen. Stat. § 105-164.6. An additional local use tax is levied on the use of tangible personal property subject to the general State rate of tax. N.C. Gen. Stat. §§ 105-468; 105-483; 105-498; 105-519.
4. Certain nonprofit entities are eligible to receive semiannual refunds of the sales and use taxes paid on direct purchases of tangible personal property for use in carrying on charitable operations. N.C. Gen. Stat. § 105-164.14(b).
5. North Carolina law controls this matter. Federal determinations based on different facts and federal law do not involve the issue presented in this matter.
6. Taxpayer cannot raise constitutional arguments in the current administrative review because constitutional challenges must be brought in the original jurisdiction of the trial court under N.C. Gen. Stat. § 105-267. Gulf Oil Corp. v. Clayton, 267 N.C. 15, 20, 147 S.E.2d 522, 526 (1966) (“The law does not contemplate that administrative boards shall pass upon constitutional questions.”).
7. Taxpayer has the burden to establish all facts to show an entitlement to the refund. Southminster, Inc. v. Justus, 119 N.C. App. 669, 459 S.E.2d 793 (1995).
8. Taxpayer does not qualify for a refund of sales and use tax as a hospital under N.C. Gen. Stat. § 105-164.14(b)(1).
9. Taxpayer does not qualify for a refund of sales and use tax as an educational institution under N.C. Gen. Stat. § 105-164.14(b)(2).
10. Taxpayer does not qualify for a refund of sales and use tax as a qualified retirement facility under N.C. Gen. Stat. § 105-164.14(b)(4).
11. Taxpayer claims to be a charitable organization under N.C. Gen. Stat. § 105-164.14(b)(3).
12. The terms “charitable institution” and “charitable organization” are not defined within Article 5 of Chapter 105 of the North Carolina General Statutes which contains the sales and use tax provisions. N.C. Gen. Stat. §§ 105-164.1 through 105-164.44G; Southminster, Inc. v. Justus, 119 N.C. App. 669, 459 S.E.2d 793 (1995).
13. Other statutory sections define a charitable purpose as follows: “A charitable purpose is one that has humane and philanthropic objectives; it is an activity that

benefits humanity or a significant rather than limited segment of the community without expectation of pecuniary profit or reward.” N.C. Gen. Stat. §§ 105-278.3(d)(2) (quoted); 105-278.6(b) (same); 105-278.7(f)(4) (same); 105-278.8(c) (same).

14. These statutory definitions of charitable purpose require: (1) a humane and philanthropic objective, (2) a broad charitable class, and (3) no expectation of commercial gain.
15. A charitable purpose for N.C. Gen. Stat. § 105-164.14(b) also requires: (1) a humane and philanthropic objective, (2) a broad charitable class, and (3) no expectation of commercial gain.
16. N.C. Gen. Stat. § 105-164.14 specifically requires the tangible personal property be used to carry on the charitable work of the nonprofit entity and not be used for purposes unrelated to charitable work.
17. Taxpayer’s objective is to create profitable, commercial products with its R&D activities or make profitable VC investments.
18. Taxpayer did not use its tangible property to carry on a charitable purpose because Taxpayer had a commercial, profit-driven purpose.
19. Taxpayer lacks a humane and philanthropic objective.
20. Taxpayer’s VC activities benefit the commercial businesses that receive funding from Taxpayer.
21. Taxpayer’s R&D activities benefit the commercial businesses that employ Taxpayer to help commercialize their products.
22. Neither the R&D nor the VC investing benefit a broad charitable class.
23. Taxpayer operates both VC and R&D to maximize commercial gain.
24. The North Carolina Court of Appeals gave the following definition: “Generally defined, a charitable institution is [1] an organization or other entity engaged in the relief or aid to a certain class of persons, [2] a corporate body established for public use, or [3] a private institution created and maintained for the purpose of dispensing some public good or benevolence to those who require it.” Southminster, Inc. v. Justus, 119 N.C. App. 669, 459 S.E.2d 793 (1995)(quotations and citations omitted).
25. This definition recognizes three types of charitable organizations which either: (1) benefit a charitable class, (2) offer a facility for public use, or (3) deliver a benefit upon the public.

26. The statute authorizing refunds to charitable organizations, N.C. Gen. Stat. § 105-164.14(b), is more restrictive than federal income tax concepts of charitable activity and requires a charitable class unless the organization maintains a public building or directly dispenses a benefit to the public.
27. A generalized benefit to society at large does not benefit an identifiable charitable class and is, therefore, insufficient to support a Claim for Refund.
28. Taxpayer's VC funding benefits private companies and competes with other sources of financing for private businesses.
29. Taxpayer's R&D activities are conducted for compensation, focus on research contracts to design and build commercial products, and the results are not freely disseminated.
30. Taxpayer's lobbying activities are not charitable.
31. Taxpayer does not offer its facilities for public use.
32. Taxpayer's primary activities do not provide a public benefit.
33. Taxpayer operates like a private business seeking to make profits from VC and R&D activities.
34. Taxpayer, like many private businesses, provides some benefit to the community with a few, small charitable grants and a few internship opportunities.
35. The level of charitable activity required to meet the definition of a charitable organization under North Carolina law exceeds that found among the general population of commercial businesses which often make efforts to help the community.
36. A charitable organization must primarily operate to further its charitable purpose and not substantially operate to further non-charitable purpose.
37. Taxpayer's VC, R&D, and lobbying activities are substantial, while its grant making and educational activities are insubstantial.
38. Any incidental benefits to the community from the Taxpayer's VC or R&D activities are not sufficient to satisfy the definition of a charitable organization.
39. Taxpayer's primary activities of VC funding and R&D are not charitable and are commercial.
40. Taxpayer has not carried its burden to show its activities were charitable.

41. Taxpayer does not qualify for a refund of sales and use tax as a charitable organization under N.C. Gen. Stat. § 105-164.14(b)(3).

DECISION

Taxpayer cites its purposes and history as justification for its operations. The Department denied the sales and use tax refund due to Taxpayer's actual conduct of research and development ("R&D") and venture capital investing ("VC") as commercial businesses. Taxpayer has the burden to establish all facts to show an entitlement to the refund. Southminster, Inc. v. Justus, 119 N.C. App. 669, 459 S.E.2d 793 (1995). The critical facts are those surrounding Taxpayer's actual operations and not historical facts regarding Taxpayer's formation. Throughout the administrative review process, hearing, and post-hearing process, Taxpayer was given an ample amount of time to produce evidence demonstrating that Taxpayer had charitable purposes. However, the evidence establishes the fact that Taxpayer is a commercial business, not a charitable one.

North Carolina law controls this matter. Federal determinations based on different facts and federal law do not involve the issue presented in this matter. For example, the IRS determination letter issued to Taxpayer was issued before the period of the Claim for Refund, and the activities the Department found to be commercial in nature had not occurred. Taxpayer also made many representations to the IRS which do not reflect Taxpayer's actual conduct. The Findings of Fact contain findings contrary to Taxpayer's representations to the IRS.

By filing the North Carolina corporate income tax return, Taxpayer itself reported that some R&D activities were unrelated to its charitable function. Thus, the Department and the Taxpayer are arguing about the extent - not the existence - of the commercial R&D operations. The R&D activities and VC funding are Taxpayer's two, primary activities. The R&D was conducted to produce commercial products, competed with other commercial businesses, and aided the purchasers of the R&D services – not

a charitable class. The VC funding was expressly conducted in a “traditional” and commercial manner to make a profit. Like the R&D, the VC funding activities competed with other commercial businesses and aided the commercial businesses receiving the VC investment – not a charitable class.

Taxpayer cannot raise constitutional arguments in the current administrative review because constitutional challenges must be brought in the original jurisdiction of the trial court under N.C. Gen. Stat. § 105-267. Gulf Oil Corp. v. Clayton, 267 N.C. 15, 20, 147 S.E.2d 522, 526 (1966) (“The law does not contemplate that administrative boards shall pass upon constitutional questions.”).

No interpretation of N.C. Gen. Stat. § 105-164.14(b)(3) allows a refund of sales and use tax where the organization acts as a commercial business. The Findings of Fact and evidence in the record document the nature and extent of Taxpayer’s commercial activities. Therefore, the denial of Taxpayer’s Claim for Refund is sustained in its entirety.

Made and entered this 15th day of March, 2006.

Eugene J. Cella
Administrative Hearings Officer
Assistant Secretary of Revenue