

STATE OF NORTH CAROLINA

**BEFORE THE
SECRETARY OF REVENUE**

COUNTY OF WAKE

In the Matter of:

The Proposed Assessment of Additional Sales)
 and Use Tax for the period August 1, 1995)
 through June 30, 2001, by the Secretary of)
 Revenue of North Carolina.)
)
 vs.)
)
 Taxpayer)

FINAL DECISION
 Docket No. 2005-75

This matter was heard before the Assistant Secretary of Revenue, Eugene J. Cella, in the City of Raleigh, on July 7, 2005, upon application for hearing by the Taxpayer wherein it protested a proposed assessment of tax and interest for the period August 1, 1995 through June 30, 2001. The hearing was held by the Assistant Secretary pursuant to G.S. 105-260.1. Representing the Sales and Use Tax Division were W. Timothy Holmes, Assistant Director, and M. D. Stephenson, Administration Officer. Representing the Taxpayer were [President], President of the Corporation, and [Attorney], Attorney with the firm [Attorneys and Certified Public Accountants Firm].

Pursuant to G.S. 105-241.1, the Department mailed a Notice of Proposed Assessment to the Taxpayer on July 31, 2001 assessing additional tax, penalty and interest of \$ for the period August 1, 1995 through June 30, 2001. The Taxpayer filed a timely protest to the proposed assessment and requested a hearing before the Secretary of Revenue.

ISSUES

The issues to be decided in this matter are as follows:

- (1) Is the Taxpayer engaged in business and liable for collecting and remitting sales or use tax on sales of tangible personal property to purchasers in North Carolina?
- (2) Has the amount of the assessment been properly determined?

EVIDENCE

The Sales and Use Tax Division introduced the following items into evidence:

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 audit report for the period August 1, 1995 through June 30, 2001 dated July 27, 2001, designated Exhibit E-2.
3. Copy of Notice of Sales and Use Tax Assessment dated July 31, 2001, designated Exhibit E-3.
4. Copy of Power of Attorney and Declaration of Representative signed by the Taxpayer on August 3, 2001 and by his attorney on August 15, 2001, designated Exhibit E-4.
5. Copy of letter from the Taxpayer's attorney to the Department dated August 15, 2001, designated Exhibit E-5.
6. Copy of letter from the Sales and Use Tax Division to the Taxpayer's attorney dated September 10, 2001, designated Exhibit E-6.
7. Copy of letter from the Taxpayer's attorney to the Sales and Use Tax Division dated September 12, 2001, designated Exhibit E-7.
8. Copy of letter from the Sales and Use Tax Division to the Taxpayer's attorney dated September 19, 2001, designated Exhibit E-8.
9. Copy of letter from the Taxpayer's attorney to the Sales and Use Tax Division dated September 25, 2001, designated Exhibit E-9.
10. Copy of letter from the Taxpayer's attorney to the Department's Supervisory Auditor in Durham, North Carolina dated November 15, 2001, designated Exhibit E-10.
11. Copy of letter from the Sales and Use Tax Division to the Taxpayer's attorney dated January 22, 2002, designated Exhibit E-11.
12. Copy of letter from the Taxpayer's attorney to the Sales and Use Tax Division dated May 29, 2002, designated Exhibit E-12.
13. Copy of letter from the Sales and Use Tax Division to the Taxpayer's attorney dated June 12, 2002, designated Exhibit E-13.

14. Copy of letter from the Taxpayer's attorney to the Sales and Use Tax Division dated August 1, 2002, designated Exhibit E-14.
15. Copy of letter from the Sales and Use Tax Division to the Taxpayer's attorney dated August 15, 2002, designated Exhibit E-15.
16. Copy of letter from the Sales and Use Tax Division to the Taxpayer's attorney dated February 12, 2003, designated Exhibit E-16.
17. Copy of letter from the Taxpayer's attorney to the Sales and Use Tax Division dated March 21, 2003, designated Exhibit E-17.
18. Copy of letter from the Sales and Use Tax Division to the Taxpayer's attorney dated April 24, 2003, designated Exhibit E-18.
19. Copy of letter from the Sales and Use Tax Division to the Taxpayer's attorney dated June 5, 2003, designated Exhibit E-19.
20. Copy of the Taxpayer's invoice number 023523 dated April 26, 1995, designated Exhibit E-20.
21. Copy of the Taxpayer's invoice number 026001 dated July 1, 1996, designated Exhibit E-21.
22. Copy of the Taxpayer's invoice number 026015 dated July 22, 1996, designated Exhibit E-22.
23. Copy of the Taxpayer's invoice number 026041 dated July 22, 1996, designated Exhibit E-23.
24. Copy of the Taxpayer's invoice number 032511 dated June 4, 1999, designated Exhibit E-24.
25. Copy of the Taxpayer's invoice number 033071 dated August 10, 1999, designated Exhibit E-25.
26. Copy of the Taxpayer's invoice number 034400 dated February 18, 2000 and attachment, designated Exhibit E-26.
27. Copy of the Taxpayer's invoice number 035010 dated May 19, 2000 and attachment, designated Exhibit E-27.
28. Copy of the Taxpayer's invoice number 036235 dated October 9, 2000 and attachment, designated Exhibit E-28.

29. Copy of Expense Report issued to the Taxpayer on April 28, 2001 by its representative for the period of April 22, 2001 through April 28, 2001 and attachments, designated Exhibit E-29.
30. Copy of the Taxpayer's North Carolina Customer List for Parts Sales for 1999 through 2000, designated Exhibit E-30.
31. Copy of Form 1099 issued by the Taxpayer to its sales representative for 1999, designated Exhibit E-31.
32. Copy of Form 1099 issued by the Taxpayer to its sales representative for 2000, designated Exhibit E-32.
33. Copies of the Taxpayer's Registration for the NC-GWA continuing education and trade show for 1999, 2000, and 2001, designated Exhibit E-33.
34. Copy of the Taxpayer's sales and service representative's business card, designated Exhibit E-34.
35. Copy of envelope postmarked November 22, 2004 in which the amended sales and use tax audit report was returned to the Department undelivered, designated Exhibit E-35.
36. Copy of amended audit report for the period August 1, 1995 through June 30, 2001 dated November 23, 2004, designated Exhibit E-36.
37. Copy of Notice of Amended Sales and Use Tax Assessment dated December 7, 2004, designated Exhibit E-37.
38. Copy of letter from the Department's Supervisory Auditor in Durham to the Taxpayer's attorney dated December 2, 2004, designated Exhibit E-38.
39. Copy of *Felt & Tarrant Manufacturing Co. v. Gallagher, et al.*, 206 U.S. 62 (1939), designated Exhibit E-39.
40. Copy of *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960), designated E-40.
41. Copy of *Tyler Pipe Industries, Inc. v. Washington Dept. of Rev.*, 483 U.S. 232 (1987), designated Exhibit E-41.
42. Copy of *Columbine Systems, Inc. v. Limbach*, No. 90-Z-389 (Ohio B.T.A. 1993), designated Exhibit E-42.
43. Copy of In the Matter of *Orvis Company, Inc. v. Tax Appeals Tribunal of New York*, 654 N. E. 2d 954 (N.Y. Ct. App. 1995) and In the Matter of *Vermont Information Processing, Inc. v. Tax Appeals Tribunal of New York, et al.*, 86 N.Y.

- 2d 165 (N.Y. Ct. App. 1995) rev'g 615 N.Y. 2d 99 (3d Dep't 1994) cert. Denied (116 S. Ct. 518 (1995), designated Exhibit E-43.
44. Copy of *Realton Corporation v. Washington, Bd. Tax App.*, No. 93-38 (Wash. B.T.A. May 10, 1996), designated Exhibit E-44.
 45. Copy of *Brown's Furniture, Inc. vs. Wagner*, IL Supreme Ct, 665 NE2d 295 (1996), cert. denied, 117 S. Ct. 175 (1996), designated Exhibit E-45.
 46. Copy of letter from the Assistant Secretary of Administrative Tax Hearings to the Taxpayer's attorney dated March 4, 2005, designated Exhibit E-46.
 47. Copy of letter from the Taxpayer's attorney to the Assistant Secretary of Administrative Tax Hearings dated March 24, 2005, designated Exhibit E-47.
 48. Copy of letter from the Assistant Secretary of Administrative Tax hearings to the Taxpayer's attorney dated March 28, 2005, designated Exhibit E-48.
 49. Copy of letter from the Assistant Secretary of Administrative Tax Hearings to the Taxpayer's attorney dated April 25, 2005.

FINDINGS OF FACT

1. The Taxpayer is engaged in the business of selling well-drilling rigs in North Carolina and making repairs to the rigs in North Carolina.
2. A well-drilling rig is a vehicle to which a well-boring apparatus is permanently attached, is driven only to move between jobs, and is not designed principally to transport persons or property.
3. The Taxpayer's sales representatives solicit North Carolina well-drilling customers and take orders for sales of rigs in North Carolina.
4. The Taxpayer contracted with a North Carolina firm to complete repairs in North Carolina on its behalf.
5. The Taxpayer's employees and repair contractor/agent (hereinafter "repair representative") make repairs, including delivery of repair parts, to customers' well-drilling equipment in North Carolina.
6. The Taxpayer's corporate president attended the North Carolina Ground Water Association's annual trade show in North Carolina during February each year.

7. The Taxpayer billed its customers in North Carolina for the sale of well-drilling equipment, the sale of repair parts, installation labor, and its employees' or its repair representative's travel expenses.
8. The Taxpayer was not registered for sales and use tax purposes and did not collect and remit sales or use tax on its sales to North Carolina customers during the assessment period.
9. The Taxpayer denies that it has activities that create nexus in North Carolina and is liable for collecting sales or use taxes in North Carolina.
10. The Taxpayer withdrew the Department's access to its records during the examination process. Without access to the Taxpayer's records, the Department could not document all of the Taxpayer's activities in North Carolina or review every invoice.
11. The Department based the assessment on the best information available.
12. On July 31, 2001, the Department mailed a notice of proposed assessment to the Taxpayer covering the period August 1, 1995 through June 30, 2001.
13. On August 15, 2001, the Taxpayer notified the Department that it objected to the assessment and requested a hearing concerning the matter.
14. The audit report was amended on November 23, 2004 to adjust for additional tax due on special mobile equipment and to allow credit for Highway Use Tax paid by customers.
15. On December 7, 2004, a Notice of Amended Assessment of additional sales and use tax was issued to the Taxpayer.

CONCLUSIONS OF LAW

1. The Taxpayer is "engaged in business" in North Carolina because it sells well-drilling rigs and delivers parts in North Carolina within G.S. 105-164.3(9).
2. The Taxpayer is a "retailer" within G.S. 105-164.3(35) because it is engaged in the business of making retail sales of tangible personal property in North Carolina.
3. The North Carolina sales tax applies to retailers such as the Taxpayer under G.S. 105-164.4.

4. The Taxpayer's repair representative also acts as its repair agent or contractor. The effect of the repair representative's activities is to transact business on the Taxpayer's behalf in North Carolina. If this minimal activity were the Taxpayer's only North Carolina activity, the Taxpayer would still be subject to sales and use tax under G.S. 105-164.8(b)(3).
5. Well-drilling rigs are trucks to which a well-boring apparatus is permanently attached and constitute "special mobile equipment" under G.S. 105-164.3(41). The Taxpayer's retail sales of such special mobile equipment are subject to the general rate of State tax and applicable local tax.
6. The Taxpayer's retail sales of repair parts to well-drilling rigs are subject to the general rate of State tax and applicable local tax; however, its charges for installation labor are exempt when separately stated on invoices issued to customers under G.S. 105-164.13(49).
7. G.S. 105-164.24 provides that a retailer must keep separate records of taxable sales and non-taxable sales in a form as may be accurately and conveniently checked by the Secretary or his authorized agents. This statute also provides that unless such records are kept, the exemptions and exclusions provided by the Sales and Use Tax Law shall not be allowed and it shall be the Secretary's duty to assess a tax upon the retailer's gross sales. Further, this statute provides that if records are not kept disclosing gross sales, it is the Secretary's duty to assess a tax upon an estimation of sales based on the best information available.
8. G.S. 105-164.26 provides that it is presumed that the gross receipts of wholesalers and retailers are subject to sales tax until the contrary is established by proper records. Under this statute, it is also *prima facie* presumed that tangible personal property sold by any person for delivery in North Carolina, however made, and by carrier or otherwise, is sold for storage, use, or consumption.
9. Since the Taxpayer withdrew the auditors' access to its records, the assessment was properly completed in accordance with G.S. §§ 105-164.24 and 105-164.26.
10. The Taxpayer is liable for the tax due on its taxable retail sales and its failure to collect the tax from its customers does not affect its liability under G.S. 105-164.7.
11. The assessment of additional tax due based upon an estimate of the Taxpayer's retail sales is in order, as provided by G.S. 105-164.32, since the Taxpayer neither filed returns nor paid the tax.
12. The proposed assessment is based on the best information available and properly issued as provided by G.S. 105-241.1(a).

13. The Taxpayer's request for a hearing is within the time set by G.S. 105-241.1(e).

DECISION

The Taxpayer is located in [another state], and is in the business of selling well-drilling rigs and repairing such rigs for customers and has no office or place of business in North Carolina. Auditors with the Department observed that the Taxpayer made repeated sales of well-drilling rigs to customers in North Carolina and obtained copies of invoices showing the Taxpayer's employees and its repair representative made repairs to rigs and charged its North Carolina customers for the repair parts sold, installation labor, and travel expenses, including the cost of meals and hotel accommodations. The auditors also obtained copies of Forms 1099 issued to a local sales representative who solicited sales from North Carolina customers. They also obtained copies of applications completed by the corporation's president to attend trade shows held in North Carolina by the North Carolina Ground Water Association during February of each year. While at the Taxpayer's [another state] location reviewing its records, the Taxpayer withdrew the auditors' access to such records. The auditors completed the examination and a proposed assessment was issued on the basis of the best information available. Upon review of additional information subsequently furnished by the Taxpayer and the North Carolina Division of Motor Vehicles, the Department's auditor amended the original audit report and an amended assessment was issued. The amended assessment is based on the best information available.

The Taxpayer, citing *Quill v. North Dakota*, 504 U.S. 298 (1992), claims that its limited contacts with the State were insufficient to impose a sales and use tax collection responsibility upon it. The Taxpayer purports that the auditor obtained copies of invoices issued in the few instances when its employees or other repair representative entered North Carolina for purposes of making repairs, and that it did not enter North Carolina at other times. Additional time was extended to the Taxpayer and counsel to provide the Department with records showing the frequency of contact in North Carolina or that might allow the Department to issue a more accurate assessment. Neither the Taxpayer nor its counsel furnished any records or additional information that might affect the amended assessment. The Taxpayer's arguments raise constitutional issues which are exclusively reserved for the judicial branch and will not be addressed here. Instead, the General Statutes of North Carolina will be applied to the Taxpayer's North Carolina activities.

The Taxpayer, through its sales representatives, employees and corporate president, engages in business in North Carolina by soliciting, selling, and delivering to customers. The Taxpayer sold those customers well-drilling equipment and made repairs to such customers' equipment. Its employees and repair representative physically installed the repair parts in well-drilling rigs in North Carolina, and the Taxpayer billed customers for the repair parts, labor, and travel expenses.

Although the Taxpayer is not a mail-order retail merchant, it claims the same type of protections against responsibility for collecting and remitting sales or use tax as those

claimed by out-of-state mail-order businesses. A mail-order merchant is considered “engaged in business” within G.S. 105-164.3(9) if any of the conditions listed in G.S. 105-164.8(b) (1), (2), or (3) is met. The Taxpayer’s repair representative performs repairs on the Taxpayer’s behalf in North Carolina. As such, the repair representative “transacts business” on the Taxpayer’s behalf in North Carolina, satisfying the condition provided by G.S. 105-164.8(b)(3). If the Taxpayer were a mail-order retail merchant and had only this type of repair activity in North Carolina, it would be considered as “engaged in business” within the above statutes and responsible for collecting and remitting North Carolina sales and use tax on its retail sales in this State.

The Taxpayer’s employees and sales representatives solicit business and take orders for the sale of tangible personal property in North Carolina. Its employees deliver and install repair parts, and the Taxpayer’s repair representative “transacts business” for or on its behalf in North Carolina. Therefore, the Taxpayer is “engaged in business” in North Carolina within G.S. 105-164.3(9) and liable for collecting and remitting the applicable State and local sales or use tax on its retail sales of well-drilling rigs and repair parts in North Carolina. The Taxpayer’s failure to collect the tax from customers does not affect its liability, as provided by G.S. 105-164.7. The auditors have made every effort to properly determine the Taxpayer’s taxable retail sales and to allow credit for taxes paid by customers, including highway use taxes such customers paid in error. Therefore, the assessment was appropriately issued within G.S. 105-241.1 and is sustained, as amended, in its entirety.

This decision does not address the Taxpayer's arguments concerning the Commerce Clause of the United States Constitution, since the Secretary is without authority to decide constitutional issues.

Wherefore the assessment is sustained, as amended, and is declared to be final and immediately due and collectible.

Made and entered this 26th day of October, 2005.

Eugene J. Cella
Assistant Secretary of Revenue For
Administrative Tax Hearings