

**STATE OF NORTH CAROLINA
COUNTY OF WAKE**

**BEFORE THE NORTH CAROLINA
DEPARTMENT OF REVENUE
OAH NO: 09 REV1582**

[Taxpayer],)
)
 Petitioner,)
)
 v.)
)
N. C. DEPARTMENT OF REVENUE,)
)
 Respondent.)

FINAL AGENCY DECISION

THIS MATTER came before the North Carolina Department of Revenue (“Department”) from the Decision of the Honorable Donald W. Overby, Administrative Law Judge, filed in the Office of Administrative Hearings on June 8, 2010. The official administrative record was transmitted by the Office of Administrative Hearings to the Department on June 22, 2010. By letter dated June 22, 2010, each party was notified of the opportunity to file exceptions to the Administrative Law Judge’s Decision as well as file a supporting brief and proposed final order. Written documentation was submitted by both parties. [Taxpayer] (“Petitioner”) was represented by [Petitioner’s attorney], and the North Carolina Department of Revenue (“Department” or “Respondent”) was represented by David D. Lennon, Esq., Assistant Attorney General. After a full review of the entire record of this matter, including the official record as defined in N.C. Gen. Stat. § 150B-37(a), and upon consideration of audio recordings of the testimonial evidence presented, the briefs, exceptions, proposed order, and other documents filed or submitted by the parties, the Department makes the following Final Agency Decision:

FINDINGS OF FACT

The Department hereby adopts all Findings of Fact set forth in the Decision of the Administrative Law Judge, as follows:

1. Petitioner is a North Carolina corporation, formed [on a date certain], that is in the business of conducting ultrasonic imaging of pregnant women and providing still graphic imagery, and moving DVD video ultrasonic imagery for fees determined by the “package” purchased by the consumers.
2. Petitioner contends that the controlling statute does not apply to what it does in that it produces diagnostic ultrasound imagery.

3. Petitioner was licensed on [a second date certain] to use the name “[Trade Name]” by [owner of the trade name], a[n out-of-state] Corporation owned then and now by [Owner of Corporation].
4. Petitioner was originally incorporated by [two incorporators] (collectively, “former owners”) and was owned by them until it was purchased by [Current Owner] on December 31, 2004.
5. [Current Owner], the current President and owner of Petitioner, has operated the business of Petitioner since she acquired it.
6. The North Carolina Department of Revenue conducted an audit (“Audit”) of Petitioner for the period September 1, 2004 through May 31, 2006 (“Audit Period”).
7. Based upon the Audit, the Department determined that Petitioner was selling the graphic and video images of *in utero* babies at retail, and issued a proposed assessment to Petitioner for unpaid North Carolina sales tax, interest, and penalties for the Audit Period in the total amount of \$15,703.95. By the time of the Notice of Final Determination, the amount due had increased with interest through December 31, 2008, to \$17,657.66.
8. Petitioner timely requested a departmental review of the proposed assessment, and upon the Department’s issuance of its Notice of Final Determination upholding the assessment, Petitioner timely filed its Petition with the Office of Administrative Hearings.
9. During the audit period until time of hearing, no one from the Department had actually visited the Petitioner’s site to observe how the business was conducted; however, that is not controlling in that the auditor dealt directly with Petitioner’s representative as is customary practice.
10. [Current Owner] bought the previous owners’ shares in [Petitioner] in part because she wanted the use of the name “[Trade Name]” because of the name recognition and the relationship with area doctors.
11. The Stock Purchase Agreement by which [Current Owner] acquired [Petitioner] specifically acknowledges the license with [Trade Name] and provides for its continuation under [Current Owner]’s ownership.
12. The License Agreement provides that it continues in effect and applies to the successors and assigns of the initial Licensee. The License Agreement requires the Licensee to adhere to the “nondiagnostic” nature of the business.
13. According to Michael Stephenson, an Administrative Officer in the Sales and Use Tax Division of the Department, the Petitioner did not initially deny that it was selling photographs and videos when the Department first assessed the taxes in this case.

14. [Current Owner] is a certified sonographer who has worked at [a certain] Medical Center and various other medical facilities performing ultrasounds that are the same as or similar to those performed at Petitioner's business. Only certified sonographers use the ultrasound equipment at Petitioner's business.
15. [Current Owner] contends that since she has owned [Petitioner], it has only performed medical diagnostic ultrasound examinations, and she contends that Petitioner requires a doctor's order to perform an ultrasound examination.
16. [Trade Name]'s website provides that all potential clients must be under the care of a doctor or midwife. It further states that the provider must be aware that they are getting an "elective ultrasound and conformation (sic) is made."
17. Petitioner as well requires its consumers to be under a doctor's care. The "doctors' orders" furnished in support of Petitioner's position that it is performing diagnostic ultrasounds do not direct the performance of any ultrasound examination, but merely give permission to Petitioner to conduct an ultrasonic examination.
18. Petitioner does not give the consumers any medical advice and cannot give a diagnosis based on the ultrasounds performed.
19. [Petitioner's employee] has worked for [Petitioner] since early 2008, becoming employed after the audit in question. She is a certified sonographer. [Petitioner's employee] confirms that during the time that she has been with Petitioner, the client intake procedure involves customers selecting and paying for "packages" that include an examination for a specified period of time, and recorded still or video ultrasonic images of the fetus.
20. [Petitioner's employee]'s [sic] experience with Petitioner is that the length of the procedure is determined solely by the "package" purchased by the consumer, and that the number and type of still and video ultrasonic images of the fetus increased directly with the price of the "package" selected.
21. The length of time spent with the consumer and the number and duration of the images provided by Petitioner to the consumer are totally dependent on which "package" is purchased and is not driven by medical diagnoses.
22. The ultrasound machine Petitioner uses for its ultrasonic imagery is of a type used for medical ultrasonic examinations.
23. The ultrasound machine used by Petitioner was acquired from the former owners, and, to the best of [Current Owner]'s knowledge, the former owners did not perform any medical diagnostic ultrasound examinations in the conduct of Petitioner's business.

24. The website for [Trade Name] during the Audit Period advertised that its licensees provide “packages” for specified prices, consistent with the pricing structure described by [Petitioner’s employee]’s [sic] testimony.
25. The website for [Trade Name] advertised during the Audit Period that its licensee’s services were “nondiagnostic.”
26. During the latter part of the Audit Period, after [Current Owner] had acquired ownership of Petitioner, she provided information for a website for the shopping center in which Petitioner is located, in which she furnished a direct link to the [Trade Name] website, which specified that the services of its licensees were “nondiagnostic.”
27. [Current Owner] contends that she could not control the contents of the [Trade Name] website, and that she had been involved in a dispute with the licensor of [Trade Name], in which she had requested the website be changed to specify that Petitioner could conduct diagnostic ultrasonic procedures.
28. The License Agreement provides that the Licensee (Petitioner herein) “shall be responsible” to tailor its own brochures, advertisements and marketing ideas to suit its business. Although Petitioner has apparently been in negotiations with the Licensor over changing some of the promotional literature, she has not changed those matters within her own control. These include a brochure provided by Petitioner’s representative to Respondent, captioned “[Trade Name]” and specifically states that the procedures are non-diagnostic. She likewise did not change the advertisements within the shopping center where the business is located.
29. Even to the date of hearing, well past the audit period, Petitioner’s contention that she is trying to distance herself from the non-diagnostic aspect of the franchise is not supported by the evidence. The benefits Petitioner derived from continuing with the franchise and using the name have thus far out-weighed the negatives, and she has continued to reap the benefits of that relationship with its name recognition.
30. Copies of emails from [Current Owner]’s exchanges with the licensor of [Trade Name] are from 2008, well after the Audit Period in this case, and in any event, show that the licensor made the changes requested by [Current Owner] at that time, thus establishing that Petitioner did have the ability to affect the contents of the [Trade Name] website.
31. [The property manager], property manager of the shopping center in which Petitioner is situated, confirmed that Petitioner never removed the link to the [Trade Name] website which was contained in Petitioner’s section of the shopping center website, and that Petitioner never provided any language for the shopping center website to qualify or disclaim any part of the [Trade Name] website to which it was linked.
32. [Current Owner] and her accountant, [Petitioner’s accountant], CPA, both admitted that the recorded ultrasonic images given Petitioner’s customers are tangible property.

33. [Petitioner's accountant] was qualified and received as an expert on North Carolina tax law. On cross-examination, he admitted that if Petitioner was selling the recorded ultrasonic still and video images, those sales would be subject to sales tax.
34. Eddie Dalton was the Department's audit supervisor in this case. The figures on the sales of "packages" contained in the audit report were provided to the Department by Petitioner.
35. The assessment in this case was based upon applying the sales tax rate to the figures on the sales of "packages" contained in the audit report.
36. Petitioner did not present any evidence challenging the calculation of the tax figures in the Department's assessment, other than to contest that the transactions on which the assessment was based was [*sic*] subject to sales tax.

CONCLUSIONS OF LAW

The Department hereby adopts all Conclusions of Law set forth in the Decision of the Administrative Law Judge, as follows:

1. N.C. Gen. Stat. § 105-164.4(a) (2005) provides "A privilege tax is imposed on a retailer [based upon] the retailer's net taxable sales or gross receipts, as appropriate."
2. The term "retailer" is defined by N.C. Gen. Stat. § 105-164.3 (35) (2005), in pertinent part, as, "[E]very person engaged in the business of making sales of personal property at retail, either within or without this State."
3. "Sales or selling" is defined by N.C. Gen. Stat. § 105-164.3 (36) (2005) as, "[t]he transfer of title or possession of tangible personal property . . . in any manner, or by any means whatsoever, for a consideration paid or to be paid."
4. "Sales Price" is defined by N.C. Gen. Stat. § 105-164.3 (37) (2005) to include, "the cost of all materials used, labor or service costs . . . and any other expense of the retailer."
5. Any sales of tangible personal property are statutorily presumed to be subject to sales tax, "until established to the contrary by proper records." N.C. Gen. Stat. § 105-164.26 (2005).
6. The burden of proof rests entirely upon a taxpayer to prove that it falls within an exemption or exception from the tax. *Henderson v. Gill*, 229 N.C. 313, 317, 49 S.E.2d 754,757 (1948).
7. The decision of the Administrative Law Judge is to be based upon the preponderance of the evidence. N.C. Gen. Stat. § 150B-34.

8. Petitioner failed to present evidence sufficient to establish that it was conducting medical diagnostic ultrasonic examinations.
9. The documentation presented by Petitioner was consistent with a business producing ultrasonic images for sale at retail, rather than a medical facility conducting diagnostic ultrasonic examinations.
10. Petitioner's efforts to disassociate itself from the business model and website of [Trade Name] are not convincing, in that Petitioner has continued to sell "packages" consistent with the business model of [Trade Name], has not disassociated itself from [Trade Name] in its advertising and shopping center website, and the earliest contemporaneous records showing any assertion by Petitioner that it is performing medical diagnostic ultrasonic examinations are from 2008, which is well after the Audit Period at question in this case.
11. The evidence supports the Department's conclusion that Petitioner was, during the Audit Period, engaged in the business of selling tangible personal property, to wit: recorded still and video ultrasonic images of *in utero* babies, at retail, that the sales figures for "packages" upon which the assessment was based accurately reflect the gross retail sales, and that the tax, penalties, and interest assessed by the Department in this case are true, accurate, and correct.
12. Petitioner has failed to show, by a preponderance of the evidence, that it is entitled to any exemption or exclusion from the tax assessment at issue.
13. Petitioner has failed to show, by a preponderance of the evidence, that the Respondent was arbitrary, capricious, or erroneous in upholding its assessment of sales tax, penalties, and interest against Petitioner for the Audit Period.

DECISION

The Department determines that the Findings of Fact and Conclusions of Law of the Administrative Law Judge, as adopted by the Department, support the Administrative Law Judge's Decision in favor of the Respondent. The Department hereby adopts the Decision of the Administrative Law Judge in the above captioned case, upholding the tax assessment issued to Petitioner by Respondent. The Final Determination dated December 29, 2008 issued to Petitioner by Respondent is affirmed as to the tax in the amount of \$11,943.01, penalties in the amount of \$2,985.48, and interest calculated through today in the amount of \$3,688.99, for a total amount of tax, penalties, and interest due as of August 10, 2010 of \$18,617.48, plus interest accruing at the rate of \$1.64 per day after August 10, 2010, until the tax is paid in full.

APPEAL

Pursuant to N.C. Gen. Stat. § 150B-45, a party wishing to appeal the final decision of the Department in a contested tax case arising under N.C. Gen. Stat. § 105-241.15 may commence such an appeal by filing a Petition for Judicial Review in the Superior Court of Wake County and in accordance with the procedures for a mandatory business case set forth in N.C. Gen. Stat. §

7A-45.4(b) through (f) within 30 days after being served with a written copy of this Final Agency Decision. Before filing a petition for judicial review, a taxpayer must pay the amount of tax, penalties, and interest that this Final Agency Decision states is due. N.C. Gen. Stat. § 105-241.16.

Under N.C. Gen. Stat. § 150B-47, the Department is required to file the official record in the contested case under review, any exceptions, proposed findings of fact, or written arguments submitted to the Department, as well as the Department's Final Agency Decision, with the reviewing court within 30 days of receipt of the Petition for Judicial Review. Consequently, a copy of the petition must be sent to the following address: North Carolina Department of Revenue, ATTN: Janice W. Davidson, 1429 Rock Quarry Road, Suite 105, Raleigh, North Carolina 27610, at the time the appeal is initiated to insure timely filing of the record.

This the 10th day of August, 2010.

NORTH CAROLINA DEPARTMENT OF REVENUE

/s/ Janice W. Davidson

Janice W. Davidson, Esq.
Agency Legal Specialist, II.
North Carolina Department of Revenue