



North Carolina Department of Revenue

Pat McCrory
GovernorJeffrey M. Epstein
Secretary

August 15, 2016

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

Re: Private Letter Ruling

[REDACTED]
FEIN: [REDACTED]

Dear Mr. [REDACTED]

The Department has completed its review of the letter from your firm dated May 17, 2016 with regard to [REDACTED] ("Taxpayer") in which your client requests a private letter ruling regarding the application of North Carolina State and local sales and use taxes to certain business transactions. This private letter ruling is a written determination issued under N.C. Gen. Stat. § 105-264.2 and applies the tax law to a specific set of existing facts furnished by you on behalf of Taxpayer. This written determination is applicable only to the taxpayer addressed herein and as such has no precedential value except to the taxpayer to whom the determination is issued.

Facts

Your letter states that Taxpayer "provides environmentally sustainable services to North Carolina businesses that result in a measurable reduction of solid waste sent to North Carolina's landfills. [Taxpayer's] two business lines consists [sic] of: (1) commercial waste removal services, and, (2) the manufacture and sale of purified and refined material products derived from waste materials."

"[Taxpayer's] trucks collect unusable raw waste materials from certain businesses for a fee. Once the waste is picked-up by [Taxpayer], title to the materials pass [sic] from the business to [Taxpayer]. The business owner forfeits the right to reclaim the waste material once [Taxpayer] has taken possession [of] it. In exchange for a guaranteed supply of high-quality waste content, the business is compensated in the form of discounted pick-up service fees charged by [Taxpayer]. So in essence, these businesses are both service customers and material suppliers. The discounted service fees provided to these businesses are generated in part by lower landfill dumping fees paid by [Taxpayer]. This is a direct result of the subsequent production of saleable products which [Taxpayer] is able to manufacture from the commercial waste materials received. These saleable products include purified and refined aluminum, newsprint, cardboard, glass, plastics and steel, all of which are sold to . . . manufacturing companies and manufacturing brokers."

You also state in your letter it is your belief that Taxpayer's "methodology used to produce raw material product for sale to customers appears to qualify as an industrial manufacturing operation for the North Carolina sales and use tax exemption and machinery & equipment

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privilege tax purposes.” Further, you state “electrical service used to power [Taxpayer’s] operations should . . . be exempt from sales and use tax.”

Included in your letter is extensive overview of the Taxpayer’s processes with emphasis on each process and various pieces of equipment. You provide a description of the machinery and processes as follows:

“[Taxpayer] incorporates a complex single-stream industrial manufacturing system which starts with the receiving of truckloads of the waste materials.

1. **Tipping Floor** — this dumping area is a large open concrete floor within the facility where raw waste material is dumped from the trucks after pick-up from the customer/supplier. The waste is weighed as required by NC Department of Environment & Natural Resources (NCDENR) [currently known as the North Carolina Department of Environmental Quality (“DEQ”)] regulations and then pushed onto drum feeders with front-end loaders.
2. **Loader and Skid Steer** — engine powered machine used to move material from the Tipping Floor staging area onto the Pitted Incline Conveyor.
3. **Pitted Incline Conveyor** -- this conveyor system is comprised of multiple linear tracks which bring the raw waste materials into the system and into the pre-extraction stations.
4. **Pre-extraction Stations** — flat conveyor belts moves *[sic]* the waste materials past personnel who manually remove rejected items such as large metal parts, electronic devices, and other objects that cannot be converted into saleable material product. The Pre-extraction Stations are also equipped with vacuum hoods located above the station used to remove plastic films.
5. **OCC (Old Corrugated Cardboard) Screens & Fine Screens** — OCC Screens are durable thick steel discs set in an elliptical offset pattern that provides *[sic]* lateral agitation to remove contaminants from the cardboard. All other non-cardboard fibers and containers fall between discs for separate additional subsequent processing via the Fine Screens. The extracted marketable cardboard is conveyed to bunker for baling and processing for shipment.
6. **Scalping Screens & Fine Screens (Future Expansion)** — the Scalping Screen contains cast chromium elliptical discs which break the glass in preparation for further cleaning. Broken glass fragments of 5 inches and under fall onto a Fine Screen located underneath. Glass pieces 2 inches and under are sent to the Glass Cleaning System (# 21).
7. **News Screens (Future Expansion)** — this machine is comprised of molded-rubber finger discs which extracts *[sic]* newspaper material from other mixed non-fiber materials, dirt and debris. The refined newspaper material extracted is then conveyed to the Optical Extractor.
8. **Optical Extraction Cleaning Fibers (Future Expansion)** — leaving the News Screen paper fibers are further processed on this machine which contains high-resolution color sensors where the contaminants (brown cardboard, metals, etc.) are removed.
9. **Fiber Line Quality Control** — the newspaper fiber stream is sent to a manual quality control location where trained personnel further remove impurities. When complete the newspaper is conveyed to a dedicated bunker for compression and baling.
10. **3D Finishing Screens (Future Expansion)** — glass fragments measuring from 2 to 5 inches received from the Scalping Screens are sent to a first extractor. The materials that fall in between the News Screen are led to a second extractor. In the 3D Finishing Screens, the extracted materials are channelled *[sic]* into three process streams: 2 inch or less particles fall between the discs and are sent to the Glass Cleaning System, other containers roll onto the side, and mixed paper adheres to the rubber discs and travels up the slope to the Ballistic Separator.
11. **Ballistic Extractor (Future Expansion)** — this machine is comprised of a series of angled moving cleats on a paddle which kick rolling rigid items down the paddle while flat flexible items are carried up the paddle, smaller items fall through a sieve mesh which removes additional non-usable waste.
12. **Optical Extraction for Cleaning Mixed Paper** — the mixed paper stream travels up the 3D Finishing Screen's slope to be cleaned by two Optical Extractor units. The Optical Extractors eject the plastic and the remaining metal is sent to the Flat and Light Separator to be cleaned

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- of all impurities and contaminants before heading to containers line. The mixed paper is finally sent to the fiber quality control.
13. **Ferrous Magnet** — this device is used on the containers stream to extract steel cans from the other materials. The steel cans are removed for further processing[.]
 14. **Optical Extraction for Plastics HDPE #2 (Future Expansion)** — extracts HDPE (#2) plastics from materials stream prior to sending extracted material to dedicated bunker for baling.
 15. **Plastic Perforator (Future Expansion)** — this machine is comprised of a PVC conveyor belt with cleats carrying the containers into a crush chamber. In the chamber knives on a rotating steel drum perforate and crush the container. Once crushed the plastic material moves through the Eddy Current device for the extraction of aluminium [*sic*] cans. This activity improves the quality of material bales.
 16. **Eddy Current Magnet Extractor** — this machine creates an electro-magnetic field which extracts aluminum, die-cast metal and copper from nonmetallic materials. These items are then sent to a dedicated bunker for baling.
 17. **Optical Extraction (2 Sides) (Future Expansion)** — this machine scans the material and separates the plastics by chemical composition. One side receives the PET #1 extracted plastics where it is [*sic*] cleaned of contaminants and sent with the mixed plastics. The second side, extracts aseptics, Tetrapak type containers, and mixed plastics.
 18. **Loader and Skid Steer** — engine powered machine used to move material from the OCC (Old Corrugated Cardboard) Screens to the Motion Floor Bunker.
 19. **Motion Floor Bunker** — facilities movement of finished goods material to the balers. The materials extracted during the process are sent to the moving floor bunker which begins compression of the materials while being transported to the balers.
 20. **Horizontal Two RAM Balers** — further processes the finished goods material by compression, pre-pressing and shearing the products[.]
 21. **Plastic Bag Vacuum Closed Door (Future Expansion)** — plastic bags are removed by the vacuum system that leads to a dedicated Close Door Baler.
 22. **Glass Cleaning System** — receives glass from the Fines Separator and the 3D Finishing Screen and removes all fragments from the glass to obtain a very high-quality purified fin[is]hed material product. The glass is then sent to a high-set Silo that loads up the trailer truck to carry the glass to the customer's facility[.]
 23. **Operations Room** — the control center of entire manufacturing operations contains computer systems and monitors to allow personnel to vary the speed of the processing operations and to continually measure quality control and productive output.
 24. **Bailer** — used to (1) prepare saleable products for shipment to the customer or (2) prepare rejected waste materials not sold to the customer for transportation to the landfill.
 25. **HVAC System** — provides positive clean ventilation air pressure and facilitates the removal of dust from the facility operating areas.
 26. **Rejected Waste Materials** — refuse items that are not able to be purified into a saleable raw material are compacted and sent to the land fill [*sic*].
 27. **Forklift** -- engine powered machine used to transport finished product from the bailer into warehouse storage and transport unusable materials from the bailer to trucks destined for the landfill.”

You further state in your letter that “it is our view that machinery & equipment used in all sections as described above, except those noted as items 1 and 23, would constitute an integral part of the industrial manufacturing process and would be exempt from North Carolina sales and use tax rate [*sic*], and would instead be subject to the 1% machinery & equipment privilege tax. Additionally, electrical service used to power these operations should also be exempt from sales and use tax.”

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Applicable Statutes and References

Under Article 5 (“Article”) of the North Carolina Revenue Act (“Act”)¹, N.C. Gen. Stat. § 105-164.1 *et. seq.*, Subchapter VIII: Local Government Sales and Use Tax, and Chapter 1096 of the 1967 Session Laws, State, local, and applicable transit sales and use taxes are imposed on a retailer engaged in business in the State on the retailer’s net taxable sales or gross receipts of tangible personal property, certain digital property, and certain services at the percentage rates listed in subdivision N.C. Gen. Stat. § 105-164.4(a). N.C. Gen. Stat. §§ 105-164.3(24), 105-164.3(32), 105-164.3(33), 105-164.3(35), 105-164.3(46), 105-164.3(49), 105-164.3(50), 105-164.4, 105-164.8, 105-467, 105-468, 105-483, 105-498, 105-507.2, 105-509.1, and 105-537. “The combined general rate applies to the gross receipts derived from sales of electricity and piped natural gas” pursuant to N.C. Gen. Stat. § 105-164.4(a)(9). The “combined general rate” is defined in N.C. Gen. Stat. § 105-164.3(4a), in part, as “[t]he State’s general rate of tax set in G.S. 105-164.4(a) plus the sum of the rates of the local sales and use taxes authorized . . . for every county in this State.”

N.C. Gen. Stat. § 105-164.6(a) provides that an excise tax at the applicable rate set in N.C. Gen. Stat. § 105-164.4 is imposed on the purchase price of “tangible personal property or digital property purchased, leased, or rented inside or outside [the] State for storage, use², or consumption in [the] State.” N.C. Gen. Stat. §§ 105-164.3(14), 105-164.3(32), 105-164.3(33), 105-164.3(44), 105-164.3(49), and 105-164.6

N.C. Gen. Stat. §105-164.13(5a) provides an exemption from the sales and use tax imposed by Article 5 of the Act for the sale at retail and the use, storage, or consumption in this State of products that are subject to the tax imposed under N.C. Gen. Stat. § 105-187.51. N.C. Gen. Stat. § 105-187.51 imposes a privilege tax on “[a] manufacturing industry or plant that purchases mill machinery or mill machinery parts or accessories for storage, use, or consumption in this State.” N.C. Gen. Stat. § 105-187.51(b) provides [t]he tax is one percent (1%) of the purchase price of the machinery, part or accessory purchased. The maximum tax is eighty dollars (\$80.00) per article. As used in this section, the term “accessories” does not include electricity.”

N.C. Gen. Stat. §105-164.13(57) provides an exemption from the sales and use tax imposed by Article 5 of the Act for the sale at retail and the use, storage, or consumption in this State of “[f]uel, piped natural gas, and electricity sold to a manufacturer for use in connection with the operation of a manufacturing facility. The exemption does not apply to electricity used at a facility at which the primary activity is not manufacturing.”

Questions on Behalf of Taxpayer

In your letter, you have asked the following questions on behalf of the Taxpayer:

1. Are the machinery and equipment used by Taxpayer, as above described, subject to the 1% privilege tax, with the maximum tax of eighty dollars (\$80.00) per article, imposed by N.C. Gen. Stat. § 105-187.51? If so, do the machinery and equipment qualify for the sales and use tax exemption provided in N.C. Gen. Stat. §105-164.13(5a)?
2. Does the electricity used by Taxpayer, in the processes above described, qualify for the sales and use tax exemption provided in N.C. Gen. Stat. §§ 105-164.13(5a) or 105-164.13(57)?

¹ References to the Act and North Carolina General Statutes are based on the laws in effect as of the date of issuance of this private letter ruling.

² “Use” is defined in part as the “exercise of any right, power, or dominion whatsoever over tangible personal property,” including withdrawal from storage, distribution, and installation. N.C. Gen. Stat. § 105-164.3(49).

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Responses

1. The machinery and equipment as described in your letter do not qualify as mill machinery under N.C. Gen. Stat. § 105-187.51 and are subject to the general State (4.75%), applicable local (2% or 2.25%), and applicable transit (0.5%) rates of sales and use tax.
2. The gross receipts derived from the sales of electricity to Taxpayer are subject to the combined general rate (7%) of sales and use tax.

Discussion

The 1% privilege tax rate set forth in N.C. Gen. Stat. § 105-187.51 is a lesser tax rate than the generally applicable rate of sales tax set forth in N.C. Gen. Stat. § 105-164.4 et seq. For this reason, N.C. Gen. Stat. § 105-187.51 constitutes a partial exemption from taxation and must therefore be strictly construed against the claim of partial exemption and in favor of the imposition of the higher rate of tax. *Hatteras Yacht Co. v. High*, 265 N.C. 653, 144 S.E.2d 821 (1965). Additionally, N.C. Gen. Stat. § 105-164.13(5a) provides an exemption from the sales and use tax for items subject to the 1% privilege tax. It is well established that a provision in a tax statute providing an exemption from a tax, otherwise imposed, is to be construed strictly against the taxpayer and in favor of the State. *Henderson v. Gill*, 229 N.C. 313, 317, 49 S.E.2d 754.

Under N.C. Gen. Stat. § 105-187.51 mill machinery or mill machinery parts and accessories must be for use by a manufacturing industry or plant in the production process to qualify for the exemption from sales and use tax under N.C. Gen. Stat. § 105-164.13(5a). The term “production” as a phase of industrial or manufacturing operations means all steps performed in processing and refining rooms, and in other quarters and departments of a plant, where conditioning, treating or other operations are done on ingredient materials as an actual routine on a processing or assembly line turning out a finished product of manufacture. 17 NCAC 7D .0102(a)(1). “To make an article manufactured, the application of the labor must result in a new and different article with a distinctive name, character, or use.”³

The material handling processes, machinery, and equipment as outlined in your letter are not transformative to ingredient materials resulting in “new and different” articles. Your letter states Taxpayer’s material handling processes receive waste materials and therefrom extract, separate, and clean cardboard, glass, newsprint, plastics, aluminum, die-cast metal, and copper. Taxpayer’s processes output cardboard, glass, newsprint, plastics, aluminum, die-cast metal, and copper. Since Taxpayer’s material handling processes do not result in new and different products of manufacture, Taxpayer is not a manufacturer, and the machinery and equipment used by Taxpayer are not used in the production phase of industrial or manufacturing operations. Therefore, the machinery and equipment described in your letter are not classified as mill machinery or mill machinery parts and accessories subject to the privilege tax imposed by N.C. Gen. Stat. § 105-187.51 and do not qualify for the exemption from sales and use tax provided under N.C. Gen. Stat. §105-164.13(5a). As previously stated, the purchase price of Taxpayer’s machinery and equipment are subject to the general State (4.75%), applicable local (2% or 2.25%), and applicable transit (0.5%) rates of sales and use tax.

N.C. Gen. Stat. § 105-187.51(b) specifically states “the term ‘accessories’ does not include electricity.” Therefore, electricity is not subject to the privilege tax imposed pursuant to N.C. Gen. Stat. § 105-187.51 or to the exemption from sales and use tax allowed pursuant to N.C. Gen. Stat. §105-164.13(5a). The exemption from sales and use tax for electricity provided pursuant to N.C. Gen. Stat. §105-164.13(57) only applies to a facility where the primary activity is manufacturing. Based on the facts presented, Taxpayer is not a manufacturer; therefore, purchases of electricity by Taxpayer do not qualify for the exemption from sales and use tax pursuant to N.C. Gen. Stat.

³ *Inhabitants of Leeds v. Maine Crushed Rock & Gravel Co.*, 127 Me. 51, 56, 141 A. 73, 75 (1928); also see *Duke Power Co. v. Clayton*, 274 N.C. 505, 164 S.E.2d 289 (1968)

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§ 105-164.13(57). Electricity used by Taxpayer is subject to the general combined rate (7%) of sales and use tax currently in effect.

While outside the scope of your original request for a private letter ruling, be advised that on July 14, 2016, the Governor signed Session Laws 2016-94. The Session Laws enact a new statutory subdivision, N.C. Gen. Stat. § 105-187.51B(a)(6), effective July 1, 2016, that provides:

“A person other than [a major recycling facility as defined in N.C. Gen. Stat. § 105-129.25 and subject to tax under N.C. Gen. Stat. § 105-187.51B(a)(1)] that gathers and obtains ferrous metals, nonferrous metals, and items that have served their original economic purpose and that converts them by processes, including sorting, cutting, classifying, cleaning, baling, wrapping, shredding, or shearing into a new or different product for sale consisting of prepared grades for the purchase of equipment, or an attachment or repair part for the equipment, that meets all of the following requirements:

- a. Is capitalized by the person for tax purposes under the Code.
- b. Is used by the person in a conversion process described in this subdivision
- c. Is not a motor vehicle or an attachment or repair part for a motor vehicle.”

For more detailed information concerning new statutory subdivision N.C. Gen. Stat. § 105-187.51B(a)(6), refer to **Important Notice: Certain Recyclers** dated August 11, 2016, available on the Department’s website, www.dornrc.com.

This ruling is based solely on the facts submitted to the Department of Revenue for consideration of the transactions described and the questions submitted. If the facts and circumstances given are not accurate, or if they change, then the taxpayer requesting this ruling may not rely on it. If a taxpayer relies on this letter ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material aspect from the facts and circumstances given in this letter ruling, the letter ruling will not afford the taxpayer any protection. It should be noted that this letter ruling is not to be cited as precedent and that a change in statute, a regulation, or case law could void this ruling.

If we may be of additional assistance, you may contact the Sales and Use Tax Division at the phone number listed on page one.

Issued on behalf of the Secretary of Revenue
By the Sales and Use Tax Division