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SC Court of Appeals

THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM THE ADMINISTRATIVE LAW COURT

H.W. Funderburk, Jr., Administrative Law Judge

Opinion No. Op. 5972 (S.C. Ct. App. filed March 1, 2023)

McEntire Produce, Inc. ..... Petitioner,

v.

South Carolina Department of Revenue ..... Respondent.

PETITION FOR A WRIT OF CERTIORARI

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Pursuant to Rule 242 of the South Carolina Appellate Court Rules ("SCACR"), Petitioner McEntire Produce, Inc. ("Petitioner" or "McEntire") petitions this Court to issue a writ of certiorari to review the decision of the Court of Appeals styled *McEntire Produce, Inc. v. South Carolina Department of Revenue*, Op. No. 5972 (S.C. Ct. App. March 1, 2023) (Howard Adv. Sh. No. 8 at p. 23) ("Opinion"), which reversed the holding of the Administrative Law Court ("ALC") and found in favor of the South Carolina Department of Revenue ("Department"). Appendix ("App.") pp. 1-43 ("ALC Order"). For the reasons set forth below, the petition should be granted, and the decision of the Court of Appeals should be reversed.

CERTIFICATE OF COUNSEL

Counsel for Petitioner hereby certifies that a Petition for Rehearing was timely filed on March 16, 2023, App. pp. 1328-55, and finally ruled on by the Court of Appeals on May 18, 2023. App. p. 1356.

QUESTIONS PRESENTED FOR REVIEW

I. Did the Court of Appeals err in refusing to extend the Machine Exemption to the purchases at issue, which were essential and indispensable to McEntire's activities as a fresh food processor?

II. Did the Court of Appeals err in disregarding the extensive findings of fact of the ALC?

III. Did the Court of Appeals err in creating an "as needed" standard for the Machine Exemption, which is unfounded in case law, statute, or regulation?

STATEMENT OF THE CASE

This matter came before the ALC in accordance with the Administrative Procedures Act, S.C. Code Ann. §§ 1-23-310 et seq. (2005 & Supp. 2015), for a contested case hearing. McEntire filed a request for a contested case hearing with the ALC on March 7, 2017, to challenge a Department Determination issued by the Department on February 7, 2017. App. pp. 1177, 736-745. In the Department Determination, the Department concluded that the McEntire's purchases of certain supplies and protective clothing were subject to use tax for tax periods October 1, 2012

through September 30, 2015 and were not exempt from use tax under § 12-36-2120(17) (Supp. 2018). App. pp. 736-45.

On November 14 and 15, 2018, the ALC held a two-day contested case hearing. Thereafter, the ALC issued its Final Order on September 6, 2019, and determined that the majority of the items at issue, including those items identified as protective clothing, for which the McEntire sought exemptions were exempt from use tax under § 12-36-2120(17), hereinafter referred to as the "Machine Exemption." App. p. 42. The ALC further found that the items designated as protective clothing were also exempt from use tax under a separate provision in § 12-36-2120(17)(b) commonly referred to as the "Pollution Control Machine Exemption." *Id.*

On September 19, 2019, the Department filed a Motion for Reconsideration, and/or to Alter or Amend. App. pp. 46-72. The ALC issued an order on October 16, 2019, denying the Department's Motion for Reconsideration. App. pp. 44-45. The Department appealed the Order and the Order Denying McEntire's Motion to Reconsider, Alter or Amend to the Court of Appeals by filing a Notice of Appeal on November 20, 2019.

On appeal, the Court of Appeals reversed both determinations without oral argument pursuant to SCACR Rule 215, finding all of the purchases at issue were subject to use tax. App. pp. 1311-1327. In response to the ALC's reversal, McEntire filed a Petition for Rehearing, which was denied by the Court of Appeals on May 18, 2023. App. pp. 1328-1355, 1356.

SUMMARY OF ARGUMENTS

McEntire respectfully petitions this Court for a writ of certiorari to review the decision of the Court of Appeals. Most importantly, the unique nature of McEntire's facility compels this court to review the Court of Appeals' Opinion in this case. No South Carolina appellate court has addressed the application of the Machine Exemption in a sophisticated, ready-to-eat produce processing facility which maintains stringent climate- and microbe-controlled environments

mandated by both federal and state law to protect public health. The very nature of McEntire's facility creates a novel question of law at issue. SCACR Rule 242(b)(1).

Second, the Court of Appeals' Opinion repeatedly substitutes its own factual judgment for the ALC's factual determination. The ALC, as the finder of fact in this case, made important findings of fact and conclusions in its 43-page Order which were supported by substantial evidence which the Court of Appeals ignored, with little to no meaningful examination or explanation. The Court of Appeals' deference to the Department's position in this case is troubling in light of the substantial testimony and documentation provided by McEntire's employees and expert witnesses.

Finally, in finding certain items at issue failed to qualify for the Machine Exemption, the Court of Appeals created a virtually impossible bar to exemption. It found that in order for a purchase of machinery to qualify under the Machine Exemption, the machinery must be used continuously, year-round and without break. This position fails to recognize both the seasonal nature of operations of many manufacturers and processors and any number of machines that are not employed continuously during a manufacturer's process, but instead only when needed as part of that process.

In view of the foregoing, and as discussed below, important reasons exist for this Court to issue a writ of certiorari and review the Court of Appeals' Opinion in this matter.

ARGUMENTS

I. THIS COURT SHOULD GRANT CERTIORARI BECAUSE THE APPLICATION OF THE MACHINE EXEMPTION TO A FRESH FOOD PROCESSOR IS A NOVEL QUESTION OF LAW.

a. No South Carolina Court Has Addressed the Application of the Machine Exemption to a Fresh Food Processor.

SCACR Rule 242 lists circumstances that weigh in favor of this Court issuing a writ of certiorari. Among those reasons listed in the Rule are where there are novel questions of law at

issue. SCACR Rule 242(b)(1). This case involves the novel question of how the Machine Exemption—which we know applies to machines used in manufacturing, processing, agricultural packaging, recycling, compounding, mining, or quarrying tangible personal property—should apply to a fresh food *processer* like McEntire.

Appellate courts in South Carolina have only addressed the application of the Machine Exemption to pure manufacturers. First, in *Southeastern Kusan, Inc. v. South Carolina Tax Commission*, 276 S.C. 487, 280 S.E.2d 57 (1981), the taxpayer "manufacture[d] plastic parts and s[old] them predominantly to other manufacturers where the parts become integrated into a final product, e.g., plastic components in furniture, in textile machinery, and in stereo equipment." *Id.* at 489, 280 S.E.2d at 87.

Next, in *Hercules Contractors & Engineers, Inc. v. South Carolina Department of Revenue*, 280 S.C. 426, 313 S.E.2d 300 (Ct. App. 1984), the facility at issue "treat[ed] waste of the plant produced in connection with its manufacture of textile products for sale" and was "situated in an uncovered area on plant property and consists of various vats, basins, tanks, pumps and other mechanical devices, as well as troughs and pipes which carry the waste from one part of the facility to another." *Id.* at 429, 313 S.E.2d at 302-03.

In this case, McEntire has argued and the ALC has agreed that it is involved in the "specialized and highly-regulated arena of fresh food processing." App. p. 5. The ALC found McEntire was "regulated by the Food and Drug Administration (FDA), the South Carolina Department of Agriculture (SCDA), and the South Carolina Department of Health and Environmental Control (DHEC)." App. p. 6. These state and federal agencies "heavily regulate the fresh produce industry and dictate that certain requirements be met so that a product can safely enter the consumer marketplace." App. p. 25. Given the sensitivity and specialized nature of its

output (i.e., the food we eat everyday), McEntire's processing requirements are more expansive than those of a traditional manufacturer.

The ALC consistently acknowledged this point. For example, the ALC found that "... given McEntire's highly regulated business as a fresh produce processor, the machinery and equipment used both before and after the actual production line processing of the fresh produce are integral and necessary not only to the overall manufacturing process, but also to the health and safety functions *imbedded within the manufacturing of fresh produce.*" App. p. 22 (emphasis added). Additionally, in finding the purchases at issue qualified for the Machine Exemption, the ALC specifically identified the unique concerns of a fresh food processor:

> Additionally, the Court finds that other items fall within the Machine Exemption because they are *integral and necessary to the manufacturing process by virtue of maintaining the integrity and safety of the finished food product by preventing its contamination....* State and federal agencies heavily regulate the fresh produce industry and dictate that certain requirements be met so that a product can safely enter the consumer marketplace. As such, *while many of the supplies at issue may not be used directly in the production line, they are integral and necessary to the processing of fresh produce under the Integrated Plant Concept and are integrated and harmonized as continuous and vital elements of production within the McEntire plant.*
>
> *Ever present in [McEntire]'s manufacturing process is the aspect of safety in producing a noncontaminated product, which is the subject of federal guidelines....*
>
> *It is evident that temperature and other environmental controls permeate the entire production process, from the time produce is harvested and delivered form the farms until the finished product leaves the McEntire plant.* In fact, testimony from Carter McEntire revealed that with the help of food safety engineers and experts, *the plant and much of the equipment inside of it was specially designed and built to correlate with the complete and other environmental controls that are required to reduce the possibility of food contamination.*

App. p. 26 (emphasis added). The ALC's findings reflect the more comprehensive processing requirements of a fresh food producer like McEntire. The ALC thus concluded "McEntire's

manufacturing operations consist of more than the simple production line manufacturing occurring in the cutting room as determined by the Department." *Id.*

b. The ALC's Application of the Machine Exemption to a Fresh Food Processor is Consistent with South Carolina's Adoption of the Integrated Plant Concept.

The Court of Appeals appears to have agreed with the Department's exceptionally limited view of the Integrated Plant Concept, which provides that "activities that occur prior to and after the sorting, cutting, washing, and packaging of produce (i.e., air quality control, storage, material handling) are not absolutely necessary and are not considered a part of the processing of fresh produce and the associated machines or items do not qualify for the machine exemption to the use tax." App. p. 1318. In the Department's and Court of Appeals' view, the timing of the use of the item at issue is paramount. This position directly contradicts S.C. Rev. Rul. #04-7, which states:

> Previously, the Department adhered to the "Production Line Theory" in determining what machinery was used in manufacturing. Under this theory, items were found to be exempt only if "used directly" in manufacturing process. Based upon the recent court decisions, the "Production Line Theory" will no longer be used. Instead, the court mandated machinery is exempt if such machinery is "integral and necessary" to the manufacturing process. This change is generally less restrictive than the Department's prior interpretation. As such, some machines that the Department would previously have held subject to the tax are exempt.

The Court of Appeals' Opinion concludes the ALC erred in relying on *Niagara Mohawk Power Corp. v. Wannamaker*, 144 N.Y.S.2d 458 (N.Y. App. Div. 1955). App. p. 1316. To the contrary, while noting"[t]Niagara court held that directness of the activity is not the test and that its "test is whether all parts of the plant contribute, continuously and vitally, to production and whether they are all integrated and harmonized," App. p. 22, the ALC's conclusions are based on whether the machinery at issue in this case were "integral" and "necessary" to McEntire's processing of fresh produce. *See id.* The ALC **did not** expand draw conclusions based on *Niagara* that, for example, material handling equipment should be subject to the Machine Exemption.

The Integrated Plant Concept reflects a more nuanced and accurate representation of the manufacturing process, especially for fresh food processors, which are required to maintain stringent quality control over its perishable product from entry into to exit from its facility. As noted by the ALC and Court of Appeals, the Integrated Plant Concept would grant an exemption under the Machine Exemption for all machines "essential" or "indispensable"[1] to the processors' process.

Moreover, the Integrated Plan Concept appropriately acknowledges that the machines at issue in this case are being used continuously throughout the processing of fresh produce—and each contributes as an essential and indispensable component to that process.

II. THIS COURT SHOULD GRANT CERTIORARI BECAUSE THE COURT OF APPEALS ERRED IN APPLYING THE STANDARD OF REVIEW.

After two full days of testimony, including four witness for the McEntire and more than three hundred pages of exhibits, the ALC determined that most, but not all, of the purchases at issue were used directly in the processing of fresh food and thus exempt from tax. On appeal, the Court should have acknowledged the Department's significant burden to demonstrate that the ALC's findings were not supported by the substantial evidence. However, the Court of Appeals simply ignored these findings and simply adopted the Department's litigation position with respect to each item at issue. Those positions were directly contradicted by the substantial evidence in the record and manufacturing principles in general.

[1] The Court of Appeals agrees "essential" and "indispensable" are synonymous with "integral" and "necessary." *See* App. p. 1318. ("The machine exemption regulation does not define the terms 'integral' and 'necessary.' Those are commonly defined as 'essential to completeness' and 'an indispensable item.' *Merriam-Webster Collegiate Dictionary* 607 & 776 (10th ed. 1993). The regulation also does not define 'essential' or 'indispensable,' but the common dictionary definitions for both terms provide that something is essential or indispensable if it is 'of the utmost importance' or 'absolutely necessary.' *Merriam-Webster Collegiate Dictionary* 396 & 593 (10th ed. 1993).").

a. Sales and Use Tax Exemptions in this Case

The crux of this case is whether certain purchases identified by the Department qualified for either the Machine Exemption or the Pollution Control Machine Exemption. With respect to the Machine Exemption, S.C. Code Ann. § 12-36-2120(17) exempts sales of "machines used in manufacturing, processing, agricultural packaging, recycling, compounding, mining, or quarrying tangible personal property for sale." S.C. Regs. 117-302.5(b)(1) (2012) states a "machine qualifies for the exemption under Code Section 12-36-2120(17) if the machine is *integral and necessary* to the manufacturing process and the product being manufactured is being manufactured 'for sale.'" As noted by the Court of Appeals, that regulation has established a three-part, *fact-intensive* test to determine whether a machine or part of a machine is "integral and necessary" to the manufacturing process:

> (a) The machine is used at a manufacturing facility. . . .
> (b) The machine is used in, and serves as an essential and indispensable component part of the manufacturing process, and is used on an ongoing and continuous basis during the manufacturing process.
> (c) The machine must be substantially "used in manufacturing . . . tangible personal property for sale."

App. p. 1315.

With respect to the Pollution Control Machine Exemption, § 12-36-2120(17)(b) provides that "machines" also include "parts of machines, attachments, and replacements used, or manufactured for use, on or in the operation of the machines and which . . . (b) are necessary to comply with the order of an agency of the United States or of this [s]tate for the prevention or abatement of pollution of air, water, or noise that is caused or threatened by any machine." Therefore, in order to qualify for the pollution control portion of the Machine Exemption, there must be: (1) at least one machine used in the manufacturing process that causes or threatens to cause pollution of air, water, or noise: (2) a State or federal agency that requires that the pollution

be prevented or abated; and (3) the item at issue is used to prevent or abate that pollution. *See also* App. p. 30.

b. The Standard of Review

When the Court of Appeals reviews an ALC Order, S.C. Code Ann. § 1-23-610(B) (Supp. 2017) provides the applicable standard of review:

> (B) The review of the administrative law judge's order must be confined to the record. The court may not substitute its judgment for the judgment of the administrative law judge as to the weight of the evidence on questions of fact. The court of appeals may affirm the decision or remand the case for further proceedings; or, it may reverse or modify the decision if the substantive rights of the petitioner have been prejudiced because the finding, conclusion, or decision is:
>
> * * * *
>
> (e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record[.]

This Court recently described the standard of review in another tax case: *Rent-A-Center West, Inc. v. South Carolina Department of Revenue*, 418 S.C. 320, 326, 792 S.E.2d 260, 263-64 (2016):

> In reaching a decision in a contested violation matter, the ALC serves as the sole finder of fact in the de novo contested case proceeding...*When the evidence conflicts on an issue, the court's substantial evidence standard of review defers to the findings of the fact-finder*....
>
> *The decision of the [ALC] should not be overturned unless it is unsupported by substantial evidence* or controlled by some error of law....Substantial evidence is evidence which, considering the record as a whole, would allow reasonable minds to reach the conclusion that the administrative agency reached.... Substantial evidence ... is more than a mere scintilla of evidence.

Id. (emphasis added and internal quotation marks and citations omitted).

In *Risher v. Department of Health and Environmental Control*, 393 S.C. 198, 712 S.E.2d 428 (2011), this Court added "the possibility of drawing two inconsistent conclusions from the evidence does not prevent an administrative agency's finding from being supported by substantial evidence." *Id.* (citing *Palmetto Alliance, Inc. v. Pub. Serv. Comm'n* 282 S.C. 430, 432, 319 S.E.

2d 695, 696 (1984)). In *Charleston County Assessor v. University Ventures, LLC*, 421 S.C. 1984, 805 S.E. 2d 216, 202 (2017), the Court of Appeals stated:

> In reaching a decision in a contested violation matter, the ALC serves as the sole finder of fact in the *de novo* contested case proceeding." "The Rules of Procedure for the Administrative Law Judge Division require that the AL[C[make independent findings of fact in contested case hearings, and the Administrative procedures Act clearly contemplates that the AL[C] will make [its] own findings of fact in a contested case hearing." When the evidence conflicts on "an issue, the [c]ourt's substantial evidence standard of review defers to the findings of the fact-finder."

Id. (citations omitted).

To be clear, while the Court of Appeals, like ALCs, hear cases *de novo*, the law does not appoint the Court of Appeals as a finder of fact. The Court of Appeals is not present for the ALC's evidentiary hearing and is therefore limited to reviewing only the record. *Id.* Because the Court of Appeals does not have access to the evidence of the case, the ALC is better situated to make findings as to the facts of the case compared to the Court of Appeals. South Carolina law takes the position that when there is a conflict of evidence, the Court of Appeals' "substantial evidence" standard defers to the findings of the fact finder, the ALC. *Be Mi, Inc. v. S.C. Dep't of Revenue*, 408 S.C. 290, 297, 758 S.E.2d 737, 741 (Ct. App. 2014); *Risher*, at 210, 712 S.E.2d at 435.

The Court of Appeals is only permitted to modify or reverse the findings of fact of an ALC if there is no "substantial evidence" that supports the finding or if the finding is controlled by erroneous law. *Engaging and Guarding Laurens County's Environment ("EAGLE") v. S.C. Dept. of Health and Environmental Control*, 407 S.C. 334, 341, 755 S.E.2d 444, 448 (2014); *see also Be Mi, Inc.*, at 297, 758 S.E.2d at 740; *Risher*, at 210, 712 S.E.2d at 434. Under this standard of review, the Court of Appeals must look at the entirety of the record and determine if there is evidence "from which reasonable minds could reach the same conclusion that the ALC

reached." *EAGLE*, at 342, 755 S.E.2d at 448; *Be Mi, Inc.*, at 297, 758 S.E.2d at 742; *Risher*, at 210, 712 S.E.2d at 434.

c. Substantial Evidence and Findings in this Case

For each item ruled on by the ALC in this matter, McEntire submitted substantial evidence regarding its use and placement in McEntire's facility and how those items contributed to the processing of fresh food. Understanding the fact-intensive nature of the inquiry regarding whether purchases at issue were machines integral and necessary to manufacturing and processing, McEntire presented witness testimony of its employees, expert testimony regarding the use of protective clothing for food safety purposes, diagrams documenting the flow of produce from entry into to exit from McEntire's facility, site diagrams, and food safety plans. Importantly, the Department presented no contrary factual testimony.

However, after review of this substantial record and without the opportunity for oral argument, the Court of Appeals ignored or disregarded these findings and inserted its own factual determinations. The following summarizes the Court of Appeals' findings, juxtaposed with those of the ALC.

1. Forklifts, Pallet Jacks, Hand Trucks and Lubricants

The Court of Appeals concluded that because forklifts, pallet jacks, and hand trucks (and lubricants used therein) "feed the bin dumping conveyance system and not the first processing machine, they are not tax-exempt conveyance machines." App. p. 1320. However, the ALC specifically found to the contrary.

With respect to the forklifts, the ALC found that they were "used in the climate-controlled areas of the plant to move 800-2,000 lb. pallets of produce into and out of the rack system and onto the conveyer belt that feeds in to the cutting room. In fact, 75-80% of the forklift usage can be attributed to dumping the product directly onto the conveying system." App. p. 6. After exhaustive

review of McEntire's operations, including schematics, site plans (App. pp. 500-02), flow charts (App. pp. 491-99), and two days' worth of testimony, the ALC found the forklifts, alternatively, (1) transported material from one process stage to another and (2) fed the first processing machine by dumping raw produce into the cutting room. *See* App. pp. 23-24.

With respect to the pallet jacks and hand trucks, the ALC found that:

> Testimony also revealed that the majority of the use of **Hand Trucks, Pallet Jacks, and Oil Lubricant Used Therein (9)** could be attributed to moving sliced tomatoes and sack onions from the low-care areas to the cutting room/high-care area *to feed the in-line for the cutting machine. As machines that feed the first processing machine and as material handling machinery used to transport in-process material from one process stage to another within the integrated plant*, the Court finds that these items also fall within the parameters of the Machine Exemption.

Id. (emphasis added). The ALC's conclusion is based on detailed testimony of Mr. Carter McEntire, who described the use of this equipment within the high-care area and also noted these items "bring the goods directly into the production line." App. p. 78:12-13. The Department did not contradict or refute that testimony.

2. Floor Drain Covers

Inconceivably, the Court of Appeals' Opinion finds that even though "drain covers ***are*** a 'mechanical device or combination of mechanical powers, parts, attachments and devices to perform some function' as provided in Regulation 117-302.5(B)(1)" (emphasis added), they are **not** tax exempt. App. p. 1321. The ALC Order and findings support the position that purchases drain covers should be exempt from tax. The ALC found:

> Stainless steel floor drain covers are used in the high-care area and serve as both a filter and a drain in [McEntire]'s recycling of fresh water. These higher quality drains must be used because waste material was previously entering the closed water system and causing adulteration of the water. [McEntire] uses about 300,000 gallons of water per day and recycles about half of that. When water is sprayed onto the produce in the cutting process, runoff goes onto the floor and mixes with debris. Through the drain system,

> the water is separated from the debris and some flows back to the plant where it is recycled while the rest goes to the city sewer system.

App. p. 14. The ALC thus concluded the floor drain covers qualified as machines used in processing fresh food produce in McEntire's facility, the Department did not refute this testimony, and then the Court of Appeals found that even though the drain cover qualified as a machine, its purchase was not exempt from tax.

3. Water Storage Tanks

As to the water storage tanks, this Court of Appeals concluded that "McEntire did not present evidence the tanks were used during processing." To the contrary, McEntire presented substantial evidence as noted in the ALC's decision. App. p. 27. Specifically, Mr. McEntire testified at length that the tanks supplied water that was mixed with a sanitizer to wash the produce in the high-care area, which the Department did not dispute was part of McEntire's processing of fresh produce. App. pp. 21-22. The ALC Order explicitly found as a fact that "[o]ne tank is used to mix sanitation chemicals with chilled water. This mixture is pumped into the high-care area to wash the produce *during the cutting process*" and again that "[o]ne tank mixes sanitation chemicals with chilled water that is sprayed on produce and on the cutting machine in the cutting room/high-care area *during the production line part of the manufacturing process*." App. pp. 14, 27 (emphasis added). The ALC Order noted that "the other tank is used to capture, sanitize, and recirculate some of the runoff water so that it can be reused later in the manufacturing process." App. p. 14. Thus, the Court of Appeals' Opinion ignores clear findings of fact regarding the use of water storage tanks in McEntire's processing of fresh food.

4. Bar Code Scanners, Black Ink Aerosol Cans, and Mobile Computer Stands

The Court of Appeals' Opinion finds that the bar code scanners, black ink aerosol cans, and mobile computer stands were merely "[a]dministrative machines" used for "recordkeeping." App. p. 1320. By contrast, the ALC Order identified specific manufacturing purposes for each item at issue. For example, it found the bar code scanners were "used to track all produce through the manufacturing process," and that "[i]n the event that contamination is found on any piece of produce, the FDA requires that the product be easily traced back to the farm where it was harvested and forward through the manufacturing process and on to the customer in order to identify the source of the contamination and to prevent its spread." App. p. 11. Further, the black ink aerosol cans are used "to spray a 'use-through code' and a 'lot code' onto the finished packaging" in order to "assist in the FDA trace-back process." *Id.* Finally, the mobile computer stands supported the "critical care checkpoints" which were required by law. *Id.* In sum, the ALC found these items were "used in the tracking process and also integral and necessary" to McEntire's manufacturing process, because "federal law requires [McEntire] to track produce not only back to the harvest point, but also during the manufacturing process and forward to the consumer." App. p. 26.

Moreover, the Court of Appeals failed to differentiate its conception of "administrative machines" used for recordkeeping from S.C. Regs. 117-302.1(e), which provides that "plates attached by the manufacturer to his product for identification purposes" are covered by the Machine Exemption. Just like the plates eligible for the Machine Exemption by regulation, the purchases at issue in this case are used to facilitate the easy identification of product.

5. Warehouse Racks, Pallet Flow Brakes, Stacking Containers

The Court of Appeals determined purchases warehouse racks, pallet flow brakes, and stacking containers were not exempt under the Machine Exemption because they constituted

simple storage machines. However, the ALC specifically found these items performed more than a mere storage function. With respect to the stacking containers, the ALC found they were used in the "work in progress" section of the facility to separate processed produce until combined. App. p. 12. Thus, stacking containers hold partially processed produce until ready to be combined with other partially processed produce. The ALC Order provides: "For example, the combination of cabbage and carrots makes coleslaw. Once the carrots are cut to specified form, they are held in the stacking containers until the cabbage is processed. The combining of these component pieces into a bag to be sealed, labeled, and palletized completes the manufacturing process with respect to the mixed product." *Id.*

With respect to the racks and pallet flow brakes found on the racks, the ALC specifically found they were part of the processing process because they were "designed to assist in cooling and maintaining the required temperature of the produce during processing to avoid spoliation and prevent contamination." *Id.* The racking system allowed "cold air to flow through the rack system and over the individual items of produce so that the temperature does not exceed 40 degrees." *Id.* Thus, contrary to the Court of Appeals' assertions, these items at issue perform far more sophisticated functions than mere storage—they are integral to the processing of produce.

6. Blower Fans

The Court of Appeals also determined the purchase of blower fans failed to qualify for the Machine Exemption because McEntire "did not provide evidence as to where the blower fans are used, except to say they are used in multiple areas." App. p. 1321. To the contrary, at the hearing, Mr. McEntire pointed to the specific areas of the facility where these blower fans were located (Q. All right. And where would you use the blower fan? A. In every room that you see that is in blue or gray – or green, depending on your color. Here on this schematic." App. p. 232:16-20.) Based

on this combination of testimony and visual evidence, the ALC found the blower fans qualified for the Machine Exemption. It found as a matter of fact and law the blower fans served both temperature-control and filtration purposes. It noted:

> blower fans are used to circulate refrigerated air throughout the facility in both the high-care and low-care areas. Without the blower fans, [McEntire] could not maintain the required temperature in the facility. Additionally, blower fans are used to prevent unfiltered air from entering the high-care area where air is filtered to an exact standard to maintain an elevated level of sanitation.

App. p. 13.

7. Cleaning Machines and Floor Treatment Chemicals

With respect to cleaning machines and floor treatment chemicals, the Court of Appeals found those purchases were not exempt because "there was no testimony the chemicals were used on any exempt machines." App. p. 1322. To the contrary, the ALC Order made a number of findings of fact that the cleaning machines were used on machines located in the high care area. First, the ALC found: "Every night, a specific sanitation shift utilizes cleaning machines, called 'foamers' to sanitize the machines and surfaces used in the high-care area. [McEntire]'s witness testified that those machines are required by the FDA and that 80% of their use occurs in the high-care area." App. p. 14. Next, the ALC found: "Cleaning Machines (19) and Floor Treatment Chemicals (17) are both used in the cutting room/high-care area to sanitize the machines and surfaces directly involved in the production line. [McEntire] testified that 80% of the cleaning machines or 'foamers' are required by the FDA to sanitize surfaces in the cutting room nightly." App. p. 27.

The ALC's findings are based on McEntire's witnesses. Specifically, Mr. Carter testified:

> So during our sanitation step, which is primarily in the grayed-out area of the schematic, that's the high-care area. We have an entire shift of

> sanitation where our sanitation technicians use this machine to take cleaning chemicals and *both foam and sanitize the processing equipment.*

App. p. 229:16-22 (emphasis added). When asked about the extent of the use, Mr. McEntire testified:

> Q: Okay. Are these cleaning machines ever used out -- and where are the cleaning machines actually used? If you get Jim to ---
>
> A: In the gray area of the schematic, which is the high-care area.
>
> Q: Okay. So they're only used in the high-care area?
>
> A: Primarily. We can use them in the raw area.

App. p. 230:10-17. Thus, McEntire presented substantial evidence regarding the applicability of the Machine Exemption to these purchases, to which the Court of Appeals should have deferred.

8. General Maintenance Tools

The Court of Appeals found general maintenance tools were not eligible for the Machine Exemption because it failed the "ongoing and continuous basis" test found in SC Regs. 117-302.5(B)(1)(b). According to the Court of Appeals, "the evidence demonstrates [McEntire] uses its maintenance tools on an 'as needed' basis." App. p. 1322.

By contrast, after listening to the testimony of McEntire's witnesses, the ALC found that McEntire "uses maintenance tools to maintain, repair, install, and uninstall equipment" and that "[i]n the cold, damp environment of the facility, machinery wears out so quickly that [McEntire] has thirty (30) fulltime employees *working continuously* to repair and maintain equipment." App. p. 13. The ALC concluded:

> [McEntire] employs thirty (30) fulltime employees who only work to maintain, repair, install, and uninstall equipment within the facility. Because the processing of fresh produce is regulated by climate control and other environmental controls, the cold and damp conditions inside of the plant cause machinery to constantly require maintenance and repairs. Thus, general ***Maintenance Tools*** *that are*

> *used to maintain, repair, install, and uninstall exempt machines inside of the plant are used on an ongoing, continuous basis* and therefore fall within the Machine Exemption.

App. p. 23 (emphasis added). To state the obvious, maintenance tools – and indeed any machine – are always going to be used only on a "as needed" basis. The ALC's findings of fact and conclusions of law are based on the testimony of McEntire's witnesses, who testified that "30 of the 600 people who do nothing but keep machines and equipment like refrigeration equipment running" and that the tools are used when machines "break[], require[] care, or require[] installation...." App. p. 235:7-9, 19-21. Given the extreme conditions of the high care room, "machinery is not, especially machinery that has electrical components, does not like water present. So we have a fair amount of break-downs due to water intrusion." App. p. 236:1-5. Substantial evidence thus supports the ALC's findings that the general maintenance tools were used on an "ongoing and continuous" basis, and thus qualified for the Machine Exemption

9. Protective Clothing

Finally, the Court of Appeals found the protective clothing at issue in this case (i.e., coveralls, eyewear, gloves, aprons, and hairnets) did not qualify under the Machine Exemption or the Pollution Control Machine Exemption based on S.C. Regs. 117-302.5(B)(10), which provides that "[p]rotective clothing worn by an employee working in the area in which the manufacturing process occurs does not qualify as a machine." However, the Court of Appeals again failed to address the ALC's findings of fact with respect to this item. The ALC differentiated clothing protecting the employee from the protective clothing in this case, which "protect[s] the consumer and public from harm." App. p. 40. The ALC cited the expert witness testimony of Dr. David Gombas, who concluded the protective clothing served dual purposes: "(1) to substitute for the employee's street clothing so that the employee is not bringing the pollution into the facility or contacting the produce with that pollution; [and] (2) within the facility, as contamination may

occur from the produce itself, the water, or the equipment and other exposed surfaces through cross-contamination, to minimize the opportunity to spread the contamination on to a broader range of food." App. p. 39. *See* also App, pp. 372:21-373:1.

Importantly, the regulation cited by the Court of Appeals does not define "protective clothing." Federal law pertaining to raw food processors, 21 CFR §117.10(b), does not refer to the required items as protective clothing, but instead refers to "outer garments, gloves, hairnets, headbands, caps, beard covers, or other effective hair restraints." Similarly, DHEC Regs. 61-3-301.11(B) do not refer to the items at issue as "protective clothing," but instead require food employees to use gloves, hair restraints, and clothing that covers body hair.

The ALC's position differentiating clothing protecting the employee with clothing protecting the product is consistent with the position of at least two state taxing authorities. Massachusetts has issued guidance noting that "the term 'protective use' does not refer to clothing designed primarily to protect the product being manufactured, e.g., 'clean room' clothing or hats and gloves work by workers in the food service industry..." Massachusetts Directive 99-3: Sales and Use Tax Treatment of Protective Clothing, *available at* https://www.mass.gov/directive/directive-99-3-sales-and-use-tax-treatment-of-protective-clothing. Similarly, the Connecticut bulletin notes that "safety apparel does not include clothing and equipment intended to protect the product being worked upon, such as clean room clothing or gloves and hairnets work by food service industry workers." Connecticut PS 2004(4): Sales and Use Tax Exemption for Safety Apparel, *available at* https://portal.ct.gov/DRS/Publications/Policy-Statements/2004/PS-20044 Sales-and-Use-Tax-Exemption-for-Safety-Apparel. Both states acknowledge that clothing and gear protecting the product being manufactured or processed is distinguishable from more

common apparel protecting the wearer, and thus could be characterized as a "machine," which is consistent with the ALC's findings.

In sum, because the coveralls, eyewear, gloves, aprons, and hairnets at issue in this case can qualify as machines for purposes of both the Machine Exemption and the Pollution Control Machine Exemption, and because there is no dispute they met the other requirements of these Exemptions, the purchases of those items should be exempt from tax.

d. The Department is Not Entitled to Deference in this Case

The Court of Appeals' Opinion is based at least in part on its deference to the Department's interpretation of its own statutes and regulations. *See* App. p. 1323. However, as reiterated most recently in *Jack's Custom Cycles, Inc. v. South Carolina Department of Revenue,* 439 S.C. 35, 48, 885 S.E.2d 433, 440 (Ct. App. 2023), the Court of Appeals it should reject the Department's interpretation where the plain language of the statute is contrary to the agency's interpretation. *Brown v. Bi-Lo, Inc.*, 354 S.C. 436, 440, 581 S.E.2d 836, 838 (2003). "Words in a statute must be given their plain and ordinary meaning without resorting to subtle or forced construction to limit or expand the statute's application." *Be Mi, Inc.*, 408 S.C. at 298, 758 S.E.2d at 741 (quoting *Epstein v. Coastal Timber Co.*, 393 S.C. 276, 285, 711 S.E.2d 912, 917 (2011)). Further, although the "construction of a statute by the agency charged with its administration will be accorded the most respectful consideration and will not be overruled absent compelling reasons," an administrative construction "affords no basis for the perpetuation of a patently erroneous application of the statute." *State v. Sweat*, 386 S.C. 339, 351, 688 S.E.2d 569, 575-76 (2010) (quoting *Dunton v. S.C. Bd. of Exam'rs in Optometry*, 291 S.C. 221, 223, 353 S.E.2d 132, 133 (1987) and *Monroe v. Livingston*, 251 S.C. 214, 217, 161 S.E.2d 243, 244 (1968)). Courts will

reject an agency's interpretation if it conflicts with the statute's plain language. *CFRE, LLC v. Greenville Cnty. Assessor*, 395 S.C. 67, 77, 716 S.E.2d 877, 882 (2011).

In this case, given the fact the Court of Appeals appears to have disregarded bot the ALC's findings of fact and the substantial evidence presented in this case, the Court of Appeals has erred in simply deferring to the Department's interpretation of the statutes and regulations at issue in this case. See App. p. 1323.

III. THIS COURT SHOULD GRANT CERTIORARI BECAUSE THE COURT OF APPEALS HAS CREATED A SEASONAL OR "AS NEEDED" EXCEPTION TO THE MACHINE EXEMPTION WHICH IS UNFOUNDED IN STATUTE, CASE LAW, OR REGULATION.

Specifically, this Court held that general maintenance tools and generator rentals were not exempt from sales and use tax as they were either used on an "as needed basis" or only used seasonally based on the needs of the business.

To be clear, virtually every manufacturer works on a seasonal basis to some extent and regularly adds and removes certain machines from their manufacturing process to meet demand for their products or to produce new or different products during the year. These machines are no less integral or necessary to the manufacturing process and, when needed, are continuously used during such process. The Court of Appeals' decision fails to recognize this and seemingly imposes a new requirement that a machine be used year-around to be a part of the "manufacturing process." The plain language of the applicable statute, the facts of this case, and manufacturing processes in general do not support any such ostensible requirement.

Moreover, with respect to general maintenance tools, the Court of Appeals has created an impossible standard—if a machine is used on an "as needed" basis, it cannot qualify of the Machine Exemption. To state the obvious, maintenance tools – and indeed any machine – will *always be used* only on a "as needed" basis. In our case, even the machine that slices the raw

produce—a machine that all parties agree is exempt from tax under the Machine Exemption—is only used when needed. For example, during a shift change, slicers presumably are turned off because there is no need to cut the produce at that time. As another example, if McEntire has no immediate orders for processed produce, the slicers are not necessary at that moment and presumably would be shut down, pending future orders.

In sum, the imposition of these standards of use are unfounded in statute, regulation or case law, and will render the Machine Exemption virtually inapplicable.

CONCLUSION

For the above-stated reasons, McEntire respectfully requests that this Court issue a writ of certiorari to review the Court of Appeals' Opinion in this matter.

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June 19, 2023
Columbia, South Carolina

THE STATE OF SOUTH CAROLINA
in The Supreme Court

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APPEAL FROM THE ADMINISTRATIVE LAW COURT

Harold W. Funderburk, Jr., Administrative Law Judge
Docket No. 17-ALJ-17-0060-CC
Appellate Case No. 2019-001933

Opinion No. 5972 (S.C. Ct. App. Filed March 1, 2023)

McEntire Produce, Inc.....Petitioner,

v.

South Carolina Department of Revenue..... Respondent.

PROOF OF SERVICE

I certify I have served Petitioner's Petition for a Writ of Certiorari on counsel of record for the South Carolina Department of Revenue and to the Clerk of the Court of Appeals via electronic mail on June 21, 2023, addressed to:

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Shareholder

June 19, 2023

The Honorable Patricia A. Howard
Clerk South Carolina Supreme Court
1231 Gervais Street
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RE: McEntire Produce, Inc. vs. South Carolina Department of Revenue
Docket No. 17-ALJ-17-0060-CC
Appellate Case No. 2019-001933
Opinion No. 5972

Dear Ms. Howard:

Enclosed for filing is the Petition for a Writ of Certiorari and Proof of Service of same on counsel for South Carolina Department of Revenue and the Clerk of the Court of Appeals in the above-referenced matter. Our firm's check for $250.00 in payment of the filing fee is also enclosed.

Thank you for your assistance in this matter.

Very truly yours,

Jim Rourke

Enclosure

cc: The Honorable Jenny Abbott Kitchings
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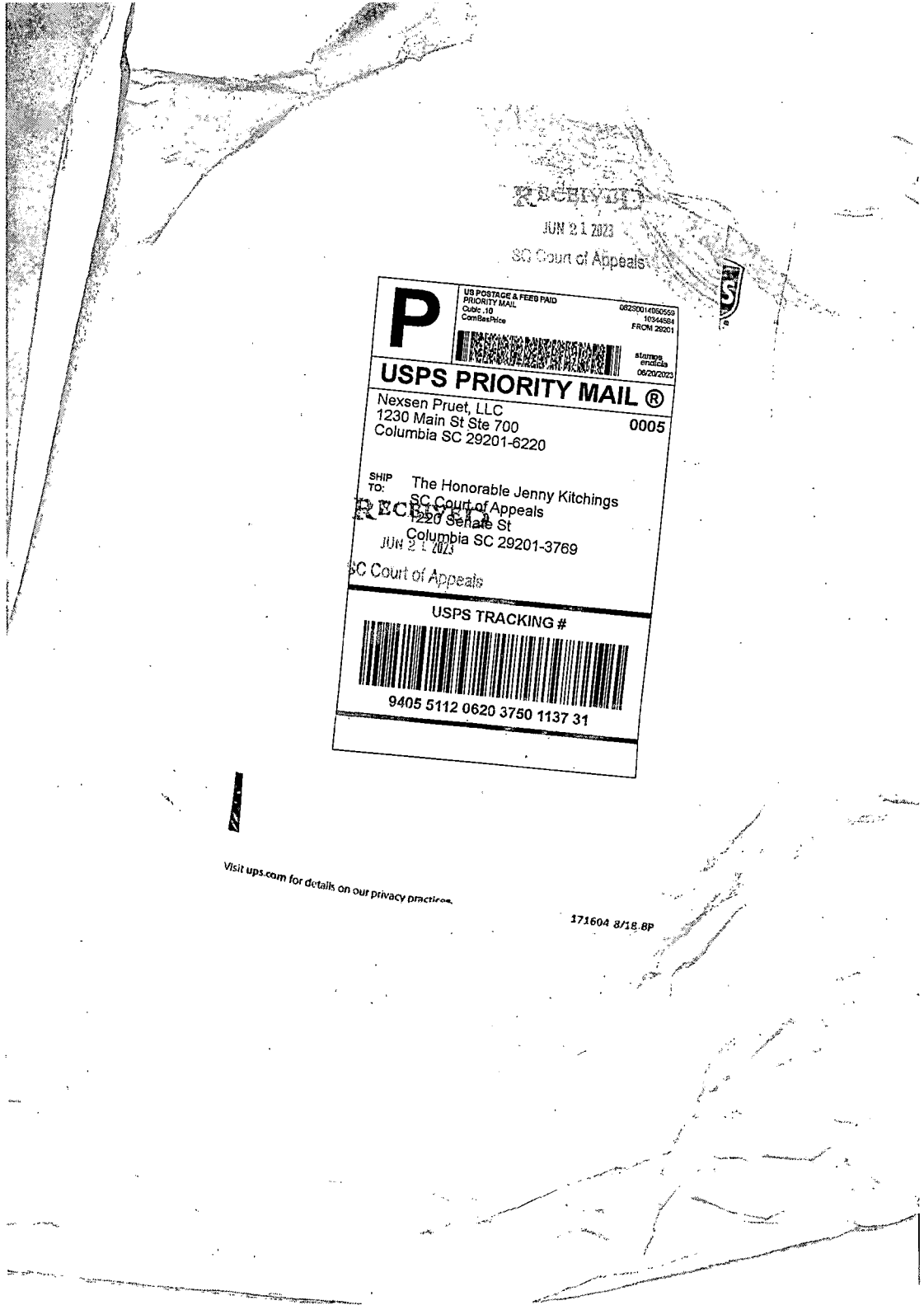

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