

RECEIVED

Jul 08 2024

S.C. SUPREME COURT

THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM THE ADMINISTRATIVE LAW COURT

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

CASE NO. 17-ALJ-17-0060-CC
Appellate Case No. 2023-000973

McEntire Produce, Inc. Petitioner,

v.

South Carolina Department of Revenue, Respondent.

BRIEF OF RESPONDENT

Dare P. Bailey (Bar No. 76152)
300A Outlet Pointe Boulevard
Columbia, SC 29210
Phone: 803-898-5110
Fax: 803-896-0171
Dare.Bailey@dor.sc.gov
courtorders@dor.sc.gov

Attorney for the South Carolina Department of Revenue

Columbia, South Carolina
July 8, 2024

TABLE OF CONTENTS

TABLE OF AUTHORITIES	iii-iv
COUNTER-STATEMENT OF ISSUES ON APPEAL.....	1
STATEMENT OF THE CASE.....	1
STANDARD OF REVIEW	1
FACTS	2
ARGUMENTS.....	7
I. Because McEntire has not sufficiently challenged the Court of Appeals’ decision as it relates to the taxability of most of the disputed items, their taxability is law of the case	7
II. Because the disputed items were not “machines used in manufacturing” as defined by the Machine Exemption and Regulation, the Court of Appeals properly declined to extend the Machine Exemption beyond its plain meaning and the plain meaning of the Regulation.....	9
A. Interpreting statutes and regulations are questions of law, rather than questions of fact, and the Court of Appeals did not err in reversing the ALC	13
B. McEntire cannot and has not identified any fact the Court of Appeals has ignored or disregarded because the Court of Appeals did not disturb any of the ALC’s facts	14
C. The Regulation explicitly excludes the disputed items from “machines used in manufacturing” for purposes of the Machine Exemption.....	15
1. Floor Drain Covers	16
2. Conveyance Items: Forklift Batteries, Forklift Parts, Forklift Repair Parts, Forklift Rental, Pallet Jacks, and Oil Lubrication for hand trucks and pallet jacks.....	18

3. Chemical Items: Floor Cleaning Chemicals.....	19
4. Maintenance Items: General Maintenance Tools and Cleaning Machines.....	19
5. Storage Items: Blower Fans, Warehouse Racks, Stacking Containers, Pallet Flow Brakes, and Water Storage Tanks.....	21
6. Administrative Items: Bar Code Scanners, Black Ink Aerosol Cans, and Mobile Computers Stands.....	22
7. Protective Clothing Items: Coveralls, Eyewear, Gloves, Aprons, and Hairnets	23
a. McEntire classified the tangible personal property identified as Coveralls, Gloves, Aprons, Eyewear, and Hairnets as “protective clothing”	23
b. The Clean Room Exemption is not the same as the Machine Exemption	25
III. Because McEntire uses its General Maintenance Tools and Generators only as needed or seasonally, the Court of Appeals did not err in finding these items taxable because they were not “used in manufacturing” as required by South Carolina law.....	26
CONCLUSION	28

TABLE OF AUTHORITIES

Cases	Page(s)
<i>Biales v. Young</i> , 315 S.C. 166, 432 S.E. 2d 482 (1993).....	7, 9
<i>Carolina Chloride, Inc. v. Richland Cnty.</i> , 394 S.C. 154, 714 S.E.2d 869 (2011).....	25-26
<i>Glasscock, Inc. v. U.S. Fidelity & Guar. Co.</i> , 348 S.C. 76, 557 S.E. 2d 689 (Ct. App. 2001).....	7-8
<i>Kiawah Resort Assocs.</i> , 318 S.C. 505-506.....	23-24
<i>Niagara Mohawk Power Corporation v. Wanamaker</i> , 286 A.D. 446, 144 N.Y.S.2d 458 (1955).....	16
<i>Richland Cnty v. Palmetto Cablevision</i> , 261 S.C. 222, 199 S.E.2d 168) (1973).....	25-26
<i>S.C. Dep't of Revenue v. Blue Moon of Newberry, Inc.</i> , 397 S.C. 256, 725 S.E.2d 480 (2012).....	2, 14
<i>Sloan Const. Co. v. Southco Grassing, Inc.</i> , 395 S.C. 164, 717 S.E.2d 603 (2011).....	7-9
<i>State v. Whitner</i> , 399 S.C. 547, 732 S.E.2d 861 (2012).....	14
<i>TNS Mills, Inc. v. S.C. Dep't of Revenue</i> , 331 S.C. 611, 503 S.E.2d 471 (1988).....	2
<i>Transp. Ins. Co. & Flagstar Corp. v. S.C. Second Injury Fund</i> , 389 S.C. 422, 699 S.E. 2d 687 (2010).....	14
 Statutes	
S.C. Code Ann. § 1-23-610(B).....	Passim
S.C. Code Ann. § 1-23-610(B)(d) (Supp. 2020).....	13, 15
S.C. Code Ann. § 12-36-910 (2014).....	5, 9
S.C. Code Ann. § 12-36-1310(A) (2014).....	5, 9
S.C. Code Ann. § 12-36-2120(17).....	Passim
S.C. Code Ann. § 12-36-2120(51).....	10
S.C. Code Ann. § 12-36-2120(54).....	12, 25-26
 Regulations	
S.C. Code Ann. Regs. § 117-302.5 (2012).....	13, 23
S.C. Code Ann. Regs. § 117-302.5(B).....	5, 9
S.C. Code Ann. Regs. § 117-302.5(B)(1).....	Passim
S.C. Code Regs. § 117-302.5(B)(4)(a).....	7
S.C. Code Regs. § 117-302.5(B)(6).....	20
S.C. Code Ann. Regs. § 117-302.5(B)(7).....	Passim
S.C. Code Regs. § 117-302.5(B)(8).....	17
S.C. Code Ann. Regs. § 117-302.5(B)(9).....	6
S.C. Code Ann. Regs. § 117-302.5(B)(10).....	23

S.C. Code Ann. Regs. 117-302.5(C).....	13
S.C. Code Ann. Regs. 117-302.5(C)(24).....	21

COUNTER-STATEMENT OF ISSUES ON APPEAL

- I. Did the Court of Appeals correctly apply the definition of “machines used in manufacturing” to the facts found by the ALC to conclude certain items are not exempt under the plain language of the Machine Exemption and Regulation?
- II. Did the Court of Appeals err by finding that “machines” used only seasonally or as-needed do not qualify for a sales and use tax exemption because they are not used in an ongoing and continuous basis as required by the Machine Exemption and Regulation?

STATEMENT OF THE CASE

On March 7, 2017, McEntire Produce, Inc. (McEntire) appealed the South Carolina Department of Revenue’s (Department) February 7, 2017 Department Determination to the South Carolina Administrative Law Court (ALC). The Determination assessed McEntire additional tax on certain items of tangible personal property between October 1, 2012, and September 30, 2015 (Audit Period), because the items were not exempt pursuant to section 12-36-2120(17) of the South Carolina Code of Laws (2014) (Machine Exemption). After a hearing on November 14 and 15, 2018, the ALC issued its Final Order on September 6, 2019, finding most of the disputed items were “machines used in manufacturing” and therefore, tax-exempt pursuant to the Machine Exemption. (R.p. 42). On October 16, 2019, the ALC denied the Department’s Motion for Reconsideration. (R.p. 44-45). Thereafter, the Department appealed to the South Carolina Court of Appeals. (R.p. 1311). The Court of Appeals reversed the ALC’s decision on March 1, 2023, because it was affected by an error of law. (R.p. 1311-1327). McEntire’s Petition for Rehearing was denied on May 18, 2023. (R.p. 1356). This Court granted Certiorari on March 27, 2024.

STANDARD OF REVIEW

Section 1-23-610(B) of the South Carolina Code of Laws articulates the standard of review for state agency decisions. S.C. Code Ann. § 1-23-610(B). Section 1-23-610(B) provides:

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:

- (a) in violation of constitutional or statutory provisions;
- (b) in excess of the statutory authority of the agency;
- (c) made upon unlawful procedure;
- (d) affected by other error of law;
- (e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record; or
- (f) arbitrary or capricious or characterize by abuse of discretion or clearly unwarranted exercise of discretion.

Interpreting sales tax exemptions and their accompanying regulations is a question of law. *S.C. Dep't of Revenue v. Blue Moon of Newberry, Inc.*, 397 S.C. 256, 725 S.E.2d 480 (2012) (holding that the determination of whether certain facts satisfy the language of a Department regulation is a question of law). Additionally, taxpayers bear the burden of proving they are entitled to an exemption. *See TNS Mills, Inc. v. S.C. Dep't of Revenue*, 331 S.C. 611, 618, 503 S.E.2d 471, 475 (1988) ("The burden is on claimants to prove their right to an exemption by bringing themselves clearly within the conditions imposed by the statute.").

Interpretation and application of tax statutes and accompanying regulations, including the tax exemption and regulation at issue here, is a question of law subject to de novo review by the Court of Appeals without any deference to the ALC's legal conclusions. As set forth in section 1-23-610(B) above, if the ALC's decision is affected by an error of law, the Court of Appeals may reverse.

FACTS

McEntire operates a fresh produce processing facility in Columbia, South Carolina, and processes lettuce, onions, cabbage, tomatoes, and other vegetables for sale. (R.p. 2, Stip. 1; R.p. 6).

McEntire's produce processing includes washing, sorting, cutting, mixing, and packaging the fresh produce at the facility. (R.p. 2, Stip. 1). The majority of McEntire's facility is divided into two climate-controlled areas: the "high-care" and "low-care" areas. (R.p. 6, 500-02). The high-care area, or the cutting room, is where produce is cut into smaller pieces and packaged. (R.p. 6). The low-care areas are generally storage areas. (R.p. 6). Before processing, produce is received, ripened, and sorted (including defect removal) in the low-care area. (R.p. 6). Then the raw materials are transported into the high-care area to be cut, chopped, washed, weighed, and bagged. (R.p. 6). After the produce is processed, it is transferred back into the low-care area and boxed, labeled, and stored until it is shipped from the facility. (R.p. 6).

As a fresh produce manufacturer, McEntire purchases certain tangible personal property tax-free using an exemption certificate. (R.p. 737). The Department audited McEntire's sales and use tax returns for tax periods October 1, 2012, through September 30, 2015, and determined McEntire owed sales and use tax on a number of items of tangible personal property. (R.p. 735). McEntire claimed the items of tangible personal property were tax-exempt pursuant to the Machine Exemption as "machines used in manufacturing." McEntire identified¹ the tangible personal property it claims² is exempt as "machines used in manufacturing" as being the following disputed items:

Floor Drain Covers	Floor Cleaning Chemicals	Coveralls
Forklift Batteries	Blower Fans	Eyewear
Forklift Parts	Warehouse Racks	Gloves
Forklift Repair Parts	Stacking Containers	Aprons
Forklift rental	Pallet Flow Brakes	Hairnets

¹ McEntire stipulated these were the types of tangible personal property purchased during the Audit Period in dispute. (R.p. at 4-5).

² The following items of tangible personal property were no longer in dispute when this matter reached the South Carolina Court of Appeals: warning signs and stickers, towels, refrigerator in quality assurance lab, lamps, plastic shelves for maintenance parts room, utility cart for maintenance tools, brooms, squeegees, white boards in production offices, and drug test kits. (R.p. 1-43).

Pallet Jacks	Storage Water Tanks
Oil Lubricant <i>for hand trucks and pallets</i>	Bar Code Scanners
Cleaning Machines	Black Ink Aerosol Cans
General Maintenance Tools	Mobile Computer Stand
Cut Wheel and Disc Maintenance Tools	Generator rental

McEntire uses Warehouse Racks for storing produce in raw coolers in the low-care area before it's transported to the cutting room in the high-care area, as well as storing the processed produce in the finished goods storage coolers (also in a low-care area) before it is shipped from the facility. (R.p. 194, 211, 500-501). The Warehouse Racks have Pallet Flow Brakes, which slow down the pallets as they move within the low-care area coolers. (R.p. 213). McEntire uses Forklifts (along Forklift Batteries, Parts, and Repair Parts), Pallet Jacks, and hand trucks to transport produce from place to place within the facility. (R.p. 209, 218, 254, 1217). As a food manufacturer, McEntire is required to purchase food grade Oil Lubricant to use on the Pallet Jacks and hand trucks. (R.p. 12). For the most part, McEntire uses these items of tangible personal property in the palletizing, shipping, finished storage, raw storage, tomato repack, and receiving dock areas of the facility. (R.p. 219, 1217). However, McEntire does not use any Forklifts in the high-care area. (R.p. 209, 255, 1217).

McEntire also purchased items to use when not washing, sorting, cutting, mixing, or packaging of fresh produce. These include maintenance items (Cleaning Machines, General Maintenance Tools, and Cut Wheel and Disc Maintenance Tools), recordkeeping items (Bar Code Scanners, Black Ink Aerosol Cans, and Mobile Computer Stands), other storage items (Water Storage Tanks, Stacking Containers and Blower Fans), protective clothing items (Gloves, Aprons, Coveralls, Hairnets, and Eyewear), Floor Drain Covers, and Floor Treatment Chemicals.

McEntire uses General Maintenance Tools to maintain, repair, install, and uninstall equipment throughout its facility. (R.p. 13, 23, 235, 1226). McEntire uses these tools on an "as-needed" basis (e.g. to fix a machine that breaks down from water intrusion) in all parts of the facility. (R.p. 235,

1226). McEntire also rents ethylene Generators when they are needed to speed up the ripening process of tomatoes. (R.p. 14, 24, 216-17, 257, 1227-28).

RELEVANT STATUTES AND REGULATION

The South Carolina Sales and Use Tax Act (Act) imposes a sales tax on “every person engaged or continuing within this State in the business of selling tangible personal property at retail.” S.C. Code Ann. § 12-36-910 (2014). The use tax is imposed on “the storage, use, or other consumption in this State of tangible personal property purchased at retail for storage, use, or other consumption in this State . . .” S.C. Code Ann. § 12-36-1310(A) (2014). The Act provides a sales and use tax exemption (Machine Exemption) for “machines used in manufacturing, processing . . . recycling, compounding, mining, or quarrying tangible personal property for sale.” S.C. Code Ann. § 12-36-2120(17) (Supp. 2020). In addition, the Act provides a sales and use tax exemption for machines that are “necessary to comply with the order of an agency of the United States or of this State for the prevention or abatement of pollution of air, water, or noise that is caused or threatened by any machine used as provided in this section.” S.C. Code Ann. § 12-36-2120(17)(b) (Supp. 2020) (Pollution Control Machine Exemption).

Regulation 117-302.5 (Regulation), which was promulgated by the Department and approved by the General Assembly, further explains the sales and use tax exemptions for manufacturers and processors, including the machine exemptions found in section 12-36-2120(17). *See* S.C. Code Ann. Regs. 117-302.5 (2012). The Regulation provides a general definition for “machine” for purposes of the Machine Exemption: “[a] machine . . . includes every mechanical device or combination of mechanical powers, parts, attachments and devices to perform some function and produce a certain effect or result . . .” *Id.*

In order to qualify for the Machine Exemption, the machine must be “integral and necessary to the manufacturing³ process” S.C. Code Reg. § 117-302.5(B)(1). A machine is “integral and necessary” to the manufacturing process if the machine “is used on an ongoing and continuous basis during the manufacturing process.” S.C. Code Reg. § 117-302.5(B)(1)(b). However, “[a] machine is not part of the manufacturing process merely because it is integral and necessary to the manufacturer.” *Id.* “For example, machines used for warehouse, distribution, or administrative purposes are integral and necessary to the manufacturer, but not part of the manufacturing process.” *Id.* The Regulation provides that, in order to be deemed “integral and necessary,” the machine “must be substantially ‘used in manufacturing . . . tangible personal property for sale,’” meaning more than one-third of the machine’s use must be for manufacturing tangible personal property for sale. S.C. Code Reg. § 117-302.5(B)(1)(c) (emphasis added).

The Regulation also provides specific guidance regarding instances when the Machine Exemption would or would not apply. For example, the Regulation provides examples of non-exempt items in 10 different categories including conveyances, chemicals, maintenance, storage, buildings, administrative (furniture, equipment, and supplies), and protective clothing, with another 32 examples of exempt manufacturing machines and machine parts. *See* S.C. Code Reg. § 117-302.5(B)(1)–(32). Relevant to this appeal, items that do not qualify for the exemptions under section 12-36-2120(17) include recordkeeping items, protective clothing, chemicals used to clean floors within the manufacturing facility, and maintenance machines. *See* S.C. Code Reg. § 117-302.5(B)(5), (6), (9) and (10). Moreover, machines used for storage, including racks used to store raw materials, storage tanks

³ For purposes of the Regulation, “manufacturing” also includes “processing.” Regulation 117-302.5(B)(1).

used to store water, and racks used to store a finished product while it cures, do not qualify for the exemptions under section 12-36-2120(17). *See* S.C. Code Reg. § 117-302.5(B)(7).

Finally, the Regulation provides that the following conveyances fall within the Machine Exemption: (1) conveyance machines⁴ which feed the first processing machine; (2) conveyance machines which transport in-process materials from one process stage to another; and (3) conveyance machines discharging the finished product from the last processing machine. *See* S.C. Code Reg. § 117-302.5(B)(4)(a). However, “[w]arehouse machinery used only for warehouse purposes, loading and unloading, storing, transporting raw materials and finished products, etc., is subject to tax” *Id.*

ARGUMENTS

I. Because McEntire has not sufficiently challenged the Court of Appeals’ decision as it relates to the taxability of most of the disputed items, their taxability is law of the case.

Only matters sufficiently raised and argued are properly before this Court. Short, conclusory statements without supporting authority or argument are considered abandoned on appeal. *See Glasscock, Inc. v. U.S. Fidelity & Guar. Co.*, 348 S.C. 76, 81, 557 S.E. 2d 689, 691-692 (Ct. App. 2001) (“South Carolina law clearly states that short, conclusory statements made without supporting authority are deemed abandoned on appeal and therefore not presented for review.”). Furthermore, failure to sufficiently identify or challenge the lower court’s ruling on appeal deems the lower court’s ruling law of the case. *Sloan Const. Co. v. Southco Grassing, Inc.*, 395 S.C. 164, 169-170, 717 S.E.2d 603, 606 (2011); *Biales v. Young*, 315 S.C. 166, 432 S.E. 2d 482 (1993). Here, McEntire has not sufficiently challenged the Court of Appeals’ decision finding many of the disputed items McEntire purchased

⁴ Any item must still meet the basic test of being a “machine” in order to qualify for the exemptions under section 12-36-2120(17).

during the Audit Period were not “machines used in manufacturing.” Accordingly, the taxability of these items are law of the case, and respectfully, not presented for review.

Despite McEntire’s conclusory and generic statement that “virtually all” of the Court of Appeals’ legal conclusions were “based on faulty or incomplete characterizations of witness testimony and evidence presented at the ALC,” McEntire does not advance specific arguments with supporting authority for those particular items McEntire does contend are exempt.⁵ (Pet. Br. at 12). In fact, McEntire’s Brief consists primarily of block quotations from the ALC and Court of Appeals decisions and, in some instances, summaries of testimony. (Pet. Br. at 9-31). McEntire does not point out any inconsistencies between the Court of Appeals’ legal conclusions and the ALC’s findings of fact. (Pet. Br. at 9-31). McEntire does not articulate when or how the Court of Appeals substituted its judgment for the ALC’s as to the weight of the evidence. *Id.* McEntire does not point to a single fact the Court of Appeals overlooked or disregarded. *Id.* Nor does McEntire identify a single fact the Court of Appeals disregarded, changed, or substituted for the ALC’s findings. *Id.* Thus, McEntire has abandoned most, if not all, of its arguments on appeal.⁶ See *Glasscock, Inc. v. U.S. Fidelity & Guar. Co.*, 348 S.C. 76, 81, 557 S.E. 2d 689, 691-692 (Ct. App. 2001).

In addition to failing to sufficiently argue any of the issues on appeal, McEntire also does not mention or challenge the taxability of all 25 items of tangible personal property the Court of Appeals found taxable. Of the 25 items considered by the Court of Appeals, McEntire’s Brief does not identify or advance any argument challenging the taxability of 9 disputed items: Stacking Containers, Forklift

⁵ McEntire identifies 15 items in its subsection headers: Forklift (Rentals), Pallet Jacks, Bar Code Scanners, Warehouse Racks, Blower Fans, Water Storage Tanks, Cleaning Machines, General Maintenance Tools, Generator Rental, Floor Drain Covers, Coveralls, Eyewear, Gloves, Aprons, and Hairnets. (Pet. Br. at 11-31). While not identified in the subsection headers, McEntire also mentions the Floor Cleaning Chemicals in the Cleaning Machines subsection. (Pet. Br. at 24).

⁶ McEntire has not abandoned its arguments for Warehouse Racks and Protective Clothing Items.

Batteries, Forklift Parts, Forklift Repair Parts, Pallet Flow Brakes, Black Ink Aerosol Cans, Oil Lubricant, Cut Wheel and Disc Maintenance Tools, and Mobile Computer Stands. Therefore, the taxability of these items is law of the case. *Sloan Const. Co. v. Southco Grassing, Inc.*, 395 S.C. 164, 169-170, 717 S.E.2d 603, 606 (2011); *Biales v. Young*, 315 S.C. 166, 432 S.E. 2d 482 (1993).

Accordingly, McEntire has not sufficiently challenged the Court of Appeals' decision as it relates to at least 23 of the 25 disputed items. McEntire has not identified or advanced arguments for 9 of the items. McEntire has not advanced arguments for 14 of the items it identified in headings. In fact, McEntire only identifies and advances arguments for two disputed items – Warehouse Racks and Protective Clothing Items.

II. Because the disputed items were not “machines used in manufacturing” as defined by the Machine Exemption and Regulation, the Court of Appeals properly declined to extend the Machine Exemption beyond its plain meaning and the plain meaning of the Regulation.

South Carolina law imposes a sales and use tax on the gross proceeds from retail sales of tangible personal property. S.C. Code Ann. §§ 12-36-910, 12-36-1310(A) (2014). Along with imposing a sales and use tax on purchases of tangible personal property, South Carolina Law also provides for exemptions from that tax. Specifically, section 12-36-2120(17) of the South Carolina Code of Laws sets forth an exemption from sales and use tax for purchases of tangible personal property constituting “machines used in manufacturing, processing, agricultural packaging, recycling, compounding, mining, or quarrying tangible personal property for sale.” (Supp. 2020). This exemption is commonly referred to as the Machine Exemption.

According to the Machine Exemption, tangible personal property is exempt from sales and use tax if it is *both* a “machine” *and* “used in manufacturing.” *Id.* The meanings of “machine” and “used in manufacturing” and the phrase “machine used in manufacturing,” as they are used in the Machine Exemption are further explained in section 117-302.5 of the South Carolina Code of Regulations (2012) (Regulation). The Regulation explains that for purposes of the Machine

Exemption, a “machine used in manufacturing” means a “mechanical device or combination of mechanical powers, parts, attachments and devices to perform some function and produce a certain effect or result.” S.C. Code Reg. § 117-302.5(B)(1).

To be “used in manufacturing,” the machine must be “integral and necessary” to the manufacturing tangible personal property for sale. S.C. Code Reg. § 117-302.5(B)(1). The Regulation establishes a 3-part test to determine whether the machine is being “used to manufacture” as intended by the Machine Exemption. The machine must (1) be used at a manufacturing facility; (2) as an essential and indispensable component part of the manufacturing process *and* is used on an ongoing and continuous basis during the manufacturing process; and (3) be used at least one-third of the time to manufacture tangible personal property for sale. *Id.*

In addition to creating a 3-part test to determine whether a particular item of tangible personal property is exempt pursuant to the Machine Exemption, the Regulation also contains guidance related to *specific types of tangible personal property* purchased by manufacturers. These explanations and examples follow the Regulation’s general guidance in subsection (B). The Regulation’s item-specific provisions relevant to this tax controversy are excerpted below.

(4) Conveyances:

(a) The general rule with reference to material handling machinery and/or mechanical conveyers is that such machinery is subject to tax up to the point where the materials go into the process. The machine feeding the first processing machine(s) is exempt. The last machine to come within the exemption is that machine which discharges the finished product from the last machine used in the process. Material handling machinery used for transporting (in process) material from one process stage to another comes within the exemption. Warehouse machinery used only for warehouse purposes, loading and unloading, storing, transporting raw materials and finished products, etc., is subject to the tax, unless exempt under provisions of Code Section 12-36-2120(51). If material handling machinery is customarily used for a dual purpose that is partly for an exempt purpose and partly for a taxable purpose, and is not otherwise exempt under the provisions of Code Section 12-36-2120(51), the machinery may be purchased free of the tax under the machine exemption (Code Section 12-36-2120(17)) provided the exempt use represents a substantial portion of its use.

For example, the following conveyances are exempt . . .

(ii) Warehouse machines (e.g., forklifts) that are used substantially to feed raw material into or onto the first processing machine in the manufacturing processing area in addition to being used in loading, unloading, storing, and transporting raw materials from the warehouse to the manufacturing area, or transporting finished products from the manufacturing area to the warehouse.

(b) Conveyances are subject to the tax up to the point where the materials go into the process. The last machine to come within the exemption is that machine which discharges the finished product from the last machine used in the process. Under this rule, the following conveyors are subject to the tax:

(i) Conveyors used solely by the taxpayer in the warehousing of raw materials and finished goods. . . .

(v) **Warehouse machines** that are used for warehouse purposes, such as loading, unloading, storing, transporting raw materials from the warehouse to the manufacturing area, or transporting finished products from the manufacturing area to the warehouse.

(5) Chemicals:

(b) Situations in which the chemicals would not qualify as a part under the machine exemption and would therefore be subject to the sales and use tax, include:

(i) Chemicals used to clean non-exempt machines, such as storage tanks.

(ii) Chemicals used to clean floors, walls, and other parts of the manufacturing facility. . . .

(6) Maintenance:

Maintenance machines used at a manufacturing facility are not exempt from the tax as a machine used in manufacturing tangible personal property for sale.

Machines that are used to maintain non-exempt machines (machines that are not integral and necessary to the manufacturing process), or are not used on an ongoing, continuous basis to maintain exempt manufacturing machines (machines that are integral and necessary to the manufacturing process) are maintenance machines and are not exempt from the tax as machines used in manufacturing tangible personal property for sale.

The following machines are maintenance machines and therefore subject to the sale and use tax:

(a) Pressure washing machines and ultrasonic cleaning machines used to clean non-exempt machines or parts, such as storage tanks.

(b) Machines used to clean floors and other parts of realty (e.g., machines used in removing sawdust from the floor of a sawmill).

(c) Machines, such as maintenance machines, which are not integral and necessary to the manufacturing process.

(d) Machines, such as pressure washing machines and ultrasonic cleaning machines, used to clean exempt manufacturing machines or parts when the cleaning of the exempt manufacturing machine or part is not integral and necessary to the manufacturing process, such as those that are not essential in ensuring the functioning of the exempt machine or part during the manufacturing process or those that are not essential in ensuring the quality of the product is maintained. In addition, if the cleaning is not an ongoing, continuous activity, then the machines are not integral and necessary to the manufacturing process.

(7) Storage:

Machines used at a manufacturing facility for storage are not exempt from the tax as a machine used in manufacturing tangible personal property for sale. For example, the following machines are for storage and therefore taxable:

(a) Racks used to store raw materials or finished goods.

(b) Storage tanks used to store raw materials, gasses, or water.

(c) Racks and tanks used to store a finished product while it cures.

Note: See example of exempt warehouse machines in Section (B)(4)(a)(ii). . . .

(9) Administrative Machines, Furniture, Equipment and Supplies:

Administrative machines, furniture, equipment, and supplies, such as office computers used for word processing, recordkeeping, employee payroll, customer billing, purchasing, accounting, and similar purposes, office furniture, office supplies, such as pens, pencils, paper, and similar items, educational material, or items used for the personal comfort, convenience, or use of the employees, are not machines used in the process of manufacturing tangible personal property for sale and are not exempt from the tax.

(10) Protective Clothing:

Protective clothing worn by an employee working in the area in which the manufacturing process occurs does not qualify as a machine and is not exempt from the tax as a machine used in manufacturing tangible personal property for sale under Section 12-36-2120(17). However, "clothing and other attire required for working in a Class 100 or better as defined in Federal Standard 209E clean room environment" is exempt under the provisions of Section 12-36-2120(54).

S.C. Code Reg. § 117-302.5(B) (emphasis added).

Finally, in subsection (C) the Regulation gives specific examples of tangible personal property that qualify as a “machine” for purposes of the Machine Exemption with the caveat that the “machine” must also satisfy the “used in manufacturing” 3-part test. The specific types of tangible personal property described in the Regulation’s examples relevant to this tax controversy are:

(4) Pressure washing machines and ultrasonic cleaning machines, used to clean exempt manufacturing machines or parts, when the cleaning of the exempt manufacturing machine or part is to ensure the functioning of the exempt machine or part during the manufacturing process or to ensure the quality of the product is maintained. . . .

(8) Tanks which are a part of the chain of processing operations. . . .

(24) Machines used to condition air (including humidification systems) for quality control during the manufacturing process of tangible personal property made from natural fibers and synthetic materials. This exemption applies to the pipes and duct used to distribute the processed air to the production areas within the plant.

(25) Recording instruments attached to manufacturing machines. . . .

S.C. Code Regs. § 117-302.5(C).

A. Interpreting statutes and regulations are questions of law, rather than questions of fact, and the Court of Appeals did not err in reversing the ALC.

McEntire argues the Court of Appeals violated section 1-23-610(B) of the South Carolina Code of Laws by substituting its judgment as to the weight of the evidence for the judgment of the ALC. (Pet. Br. at 7-31). Essentially, McEntire maintains the Court of Appeals disagreed with the ALC’s factual findings, found the ALC’s factual findings were not supported by substantial evidence, and found the items taxable based on the Court of Appeals’ *alleged* factual findings. (Pet. Br. at 7-31). This argument is flawed because the questions presented to the Court of Appeals were questions of law—not questions of fact—and the Court of Appeals correctly reviewed and reversed the ALC’s decision based on the ALC’s error of law.

Under the Administrative Procedures Act, the Court of Appeals may reverse the ALC if it’s finding, conclusion, or decision affected by error of law. *See* S.C. Code Ann. § 1-23-610(B)(d) (Supp.

2020). The interpretation of a statute or construction of a regulation is a question of law for the Court of Appeals to decide. *See S.C. Dep't of Revenue v. Blue Moon of Newberry, Inc.*, 397 S.C. 256, 725 S.E.2d 480, 483 (2012) (holding that the determination of whether certain facts satisfy the language of a Department regulation is a question of law). “Questions of statutory interpretation are questions of law, which are subject to *de novo* review and which [the appellate court] is free to decide without any deference to the court below.” *See State v. Whitner*, 399 S.C. 547, 552, 732 S.E.2d 861, 863 (2012); *see also Transp. Ins. Co. & Flagstar Corp. v. S.C. Second Injury Fund*, 389 S.C. 422, 427, 699 S.E. 2d 687, 689 (2010) (“Statutory interpretation is a question of law.”). Interpreting sales tax exemptions and accompanying regulations is no different—it is a question of law subject to *de novo* review by the Court of Appeals without any deference to the ALC’s conclusions. If the Court of Appeals finds the ALC’s decision was controlled by an error of law, it may reverse the ALC pursuant to section 1-23-610(B) of the South Carolina Code of Laws.

B. McEntire cannot and has not identified any fact the Court of Appeals has ignored or disregarded because the Court of Appeals did not disturb any of the ALC’s facts.

In this case, the Court of Appeals reversed the ALC’s legal conclusions by applying item-specific provisions of the Regulation to the facts *as found by the ALC*. The Court of Appeals reversed the ALC’s decision solely because it was affected by an error of law without disturbing a single factual finding. In fact, the section of the Court of Appeals’ recitation of the facts can be tied directly to the parties’ stipulation of facts or the ALC’s factual determinations.

The Court of Appeals examined the facts as found by the ALC about each type of tangible personal property McEntire purchased during the Audit Period, including where within McEntire’s facility the item was used and for what purpose. (R.p. 1316, 124). In light of the plain language of the Machine Exemption and the Regulation, the Court of Appeals reversed the ALC’s legal conclusions. *Id.* The Court of Appeals identified the disputed issue and item type, cited the specific provision of the Regulation applicable to each grouping of items, and applied the legal definitions of

“machines” and “used in manufacturing” and “machines used in manufacturing” as intended by the Machine Exemption to the facts as the ALC found them. The Court of Appeals reversed the ALC’s legal conclusions regarding the disputed items’ taxability, not because the ALC’s decision was not supported by the ALC’s findings of fact, but because the ALC had *erred as a matter of law* by misapplying the Machine Exemption—by ignoring the Regulation—to the facts that the ALC found about the items of tangible personal property McEntire purchased during the audit period.

Notably, McEntire does not identify a single fact the ALC found in this case that the Court of Appeals ignored or disregarded. Instead, McEntire makes vague and conclusory statements alleging the Court of Appeals rejected or ignored the ALC’s facts *without identifying a single fact found inconsistent with the ALC*. The Court of Appeals did not resolve any factual disputes between the parties. The ALC erred as a matter of law when it failed to apply the Regulation *in its entirety* to the items in dispute. McEntire admitted as much in its Petition for Rehearing, in which it said the Court of Appeals “overlooked and misapprehended several things when it overturned the ALC decision and ruled that *as a matter of law*, (1) McEntire’s various machines were not exempt under the manufacturer’s sales tax exemption; and (2) certain gear worn by employees required by federal law were not exempted.” (R.p. 1329). Thus, the Court of Appeals was right to reverse the ALC’s order pursuant to the appropriate standard of review in section 1-23-610(B)(b) of the South Carolina Code of Laws because it was affected by an error of law.

C. The Regulation explicitly excludes the disputed items from “machines used in manufacturing” for purposes of the Machine Exemption.

In this case, the ALC found the items at issue were “machines used in manufacturing” because they met the Machine Exemption’s *general requirements* under subsection (B)(1) of the Regulation. But the ALC’s analysis was incomplete because it never took the next step of applying the *item-specific provisions* of the Regulation. Without disturbing any of the ALC’s factual findings, the Court of Appeals corrected this legal error by finding all 25 items taxable based on the application of the plain language

of the Regulation and Machine Exemption. The Regulation explicitly excludes the disputed items, as demonstrated in the Court of Appeals' decision reversing the ALC's erroneous conclusions of law.⁷

To further illustrate this point, below is an analysis of the relevant section of the Regulation as applied to each disputed item of tangible personal property.

1. Floor Drain Covers

The ALC described McEntire's Floor Drain Covers as "stainless steel" and found McEntire used the items "as both a filter and a drain in [McEntire's] *recycling of fresh water*." (R.p. 14 (emphasis added); *see also* R.p. 239:6 – 240:15). The ALC found the Floor Drain Covers were "machines used in manufacturing" as they were used in the high-care area to separate debris from water and allow the run-off water to escape through the floor to be filtered and reused. (R.p. 28).

However, to qualify for the Machine Exemption, the tangible personal property must be *both* a machine *and* be used in manufacturing. While an item may be used in manufacturing, it must still meet the definition of "machine" to be exempt from tax. In reversing the ALC, the Court of Appeals applied the definition of "machine" in the Regulation to the facts as found by the ALC. In particular, the Court of Appeals specifically noted the Floor Drain Covers were not a "mechanical device or combination of mechanical powers, parts, attachments and devices to perform some function," and therefore, not a "machine" for purposes of the Machine Exemption. (R.p. 1321).

⁷ McEntire argues the Court of Appeals reversed the ALC because of its reliance on *Niagara Mohawk Power Corporation v. Wanamaker*, 286 A.D. 446, 144 N.Y.S.2d 458 (1955), in defining the limits of McEntire's manufacturing process. (Pet. Br. at 9–10). However, although the Court of Appeals mentioned the ALC's consideration of *Niagara* and the Integrated Plant Theory, it did so *without substantive comment*. The Court of Appeals merely noted the ALC's discussion of *Niagara* and outlined the Department's arguments regarding *Niagara*, the Court of Appeals did not offer an ultimate finding regarding whether the ALC was correct to rely on *Niagara* or whether the Court of Appeals correctly defined the scope of McEntire's manufacturing process. (R.p. 1316-1317). Thus, the questions of whether the ALC erred in defining McEntire's manufacturing process, applying the Integrated Plant Theory, or reliance on *Niagara* were not answered by the Court of Appeals.

The substantial evidence on the whole record also supports the Court of Appeals' conclusion. The Floor Drain Covers are described as perforated stainless steel plates that allows the run-off water and chemicals used in the high-care area to exit through the floor drain system. (R.p. 239:6 – 240:15). Each is not a “mechanical device or combination of mechanical powers, parts, attachments and devices to perform some function,” and therefore, not a “machine used in manufacturing.”

The ALC's error in failing to apply the definition of “machine” as set forth in the Regulation to the facts found about the Floor Drain Covers was compounded by the ALC's failure to apply the item-specific provision of the Regulation applicable to parts and fixtures of buildings that house manufacturing processes. Even if the Floor Drain Covers are properly considered part of the plant's high-care area floor drain system, they are nevertheless excluded from the definition of “machines used in manufacturing” by subsection (B)(8) of the Regulation, which provides: “A building which houses a manufacturing process, and the various parts of such a building, are not exempt from the tax as a machine, or a part or attachment to a machine, used in manufacturing tangible personal property for sale.” The tangible personal property identified as Floor Drain Covers in this case are items affixed to the floor of McEntire's building. (R.p. 239:6 – 240:15). They serve as a barrier between areas in the plant – just as any other door, wall, floor, ceiling, walkway, or gate. Therefore, the Floor Drain Covers are part of McEntire's building and not exempt from sales and use tax pursuant to the Machine Exemption based on the Buildings Items exclusion in the Regulation. S.C. Code Reg. § 117-302.5(B)(8).⁸

⁸ McEntire appears to suggest that subsection (C)(2) of the Regulation related to “[t]raveling water screens used to filter water from a river, lake, or other water source at a water treatment plant processing water for sale” may also provide a basis to exempt the floor drain covers. (Pet. Br. at 28). This argument should be disregarded. Nothing in the record suggests the floor drain covers were filtering water from a river, lake, or other water source, that McEntire's facility was a water treatment plant, or that McEntire processed water for sale.

2. Conveyance Items:⁹ Forklift Batteries, Forklift Parts, Forklift Repair Parts, Forklift Rental, Pallet Jacks, and Oil Lubricant for hand trucks and pallet jacks

The ALC found the Forklift Batteries, Forklift Parts, Forklift Repair Parts, Forklift Rental, Pallet Jacks, and Oil Lubricant for hand trucks and pallet jacks (collectively “Conveyance Items”) were machines McEntire used to move produce from one location in the facility to another at varying stages of the manufacturing process. (R.p. 12-13). The ALC determined these Conveyance Items were exempt because (a) they met the definition of “machines” in the Regulation based on the (b) frequency ratio of McEntire’s forklift use attributable to dumping produce into the conveyance belt. (R.p. 23-24). The ALC again applied the general “machines used in manufacturing” guidance articulated in subsection (B)(1) of the Regulation without discussing the application of the item-specific provisions related to Conveyance Items

The Court of Appeals reversed the ALC’s decision because the Regulation provides that material handling machinery and conveyances are not “machines used in manufacturing.” (R.p. 1320). Hence, it was affected by an error of law. The Court of Appeals relied on subsections (B)(4)(a) and (B)(4)(a)(ii), finding the disputed items were conveyance items used for loading, unloading, and moving produce around the facility and thus were not “machines used in manufacturing” as used in the Machine Exemption. (R.p. 1320).¹⁰

⁹ McEntire’s brief lists Forklifts and Pallet Jacks in the section header. (Pet. Br. at 12). Other than quoting the Court of Appeals and the ALC, and summarizing witness testimony, the entire 3-page section contains 6 sentences – all related to McEntire’s Forklifts and how they are used. (Pet. Br. at 12-15). McEntire does not identify or discuss the other items related to its Forklifts – Forklift Batteries, Forklift Parts, or Forklift Repair Parts. Similarly, McEntire did not identify or discuss the Pallet Jacks or Oil Lubricant.

¹⁰ To the extent McEntire suggests the Court of Appeals created an additional requirement for warehouse machinery to be exempt, the argument is without merit. (Pet. Br. at 12). The portion of the Conveyance Items provision the Court of Appeals quoted explains when warehouse machinery that is also used for manufacturing qualifies for the Machine Exemption.

3. Chemical Items: Floor Cleaning Chemicals

The ALC found that because the Floor Cleaning Chemicals were used to sanitize the floor in the high-care area, they were exempt “machines used in manufacturing” and therefore exempt. (R.p. 14). Importantly, the ALC did not consider subsection (B)(5)(b)(ii) of the Regulation. The Court of Appeals found the ALC erred as a matter of law by failing to apply subsection (B)(5)(b)(ii) of the Regulation, which specifically excludes “chemicals used to clean floors” from the definition of “machines used in manufacturing” for purposes of the Machine Exemption. In correcting the ALC’s error of law by applying an overlooked portion of the Regulation, the Court of Appeals did not disturb any of the ALC’s factual findings. In fact, it makes no difference whether the chemicals were used in McEntire’s high-care area when the Regulation plainly states that chemicals used to clean floors—regardless of where the floors are located—*are not exempt machines*.

4. Maintenance Items: General Maintenance Tools and Cleaning Machines

The ALC found the General Maintenance Tools are used within McEntire’s facility and that the cold and wet environment in the processing plant caused all the machinery to “constantly require maintenance and repairs.” (R.p. 23). The ALC further found the General Maintenance Tools are used on exempt machines on an “ongoing and continuous basis” by McEntire’s employees and were therefore exempt. (R.p. 23). The ALC also found the Cleaning Machines used to clean the surfaces and machines in the high-care area of McEntire’s facility were exempt “machines used in manufacturing” because the FDA requires McEntire to sanitize the food processing area nightly. (R.p. 14, 27). With respect to both items, the ALC did not address subsection (B)(6)(d) of the Regulation, which specifically addresses maintenance tools and cleaning machines.

The Court of Appeals reversed the ALC’s determination with respect to the General Maintenance Tools based on subsection (B)(5)(a)(i), finding the ALC’s factual determination that McEntire used the General Maintenance tools on an “as needed” basis inherently means the General

Maintenance Tools were not “used on an ongoing and continuous basis” for purposes of the Machine’s Exemption’s definition of “used in manufacturing.” (R.p. 1322). With respect to the Cleaning Machines, the Court of Appeals noted there was no testimony in the record that they were used on any exempt machines. (R.p. 1322). Therefore, the Court of Appeals found the ALC erred as a matter of law in failing to consider whether the Cleaning Machines were used to clean exempt machines and if so, if the cleaning of the exempt machines ensures their function during the manufacturing process. (R.p. 1322).

As the Court of Appeals noted, the Regulation explains a manufacturer’s maintenance machines do not qualify for the Machine Exemption when the items are not used on an ongoing and continuous basis *to maintain exempt machines*. S.C. Code Reg. § 117-302.5(B)(6). The ALC premised its decision to exempt the maintenance tools and cleaning machines primarily on the fact that those items were used generally in the high-care area of the manufacturing facility. (R.p. 13-14). However, McEntire has not identified evidence indicating which exempt machines are being maintained by the disputed General Maintenance Tools and Cleaning Machines. Because McEntire failed its burden of proof to present this evidence to the ALC, the ALC could not and did not make any factual findings identifying any exempt machines being maintained by McEntire’s General Maintenance Tools or Cleaning Machines. Indeed, McEntire’s argument with respect to the Maintenance Tools is simply that “Maintenance tools – and indeed any machine – are always going to be used only on an ‘as needed’ basis.” (Pet. Br. at 25). McEntire seemingly rests its argument that using something when it is needed – as opposed to using it constantly – means it is “used in manufacturing” as used in the Machine Exemption. This is not consistent with the Machine Exemption and the Regulation.

As explained above, defining a statutory term is a question of law – not a question of fact. Therefore, the Court of Appeals did not err in concluding the maintenance items were not exempt based on the Machine Exemption and Regulation. The ALC made no factual findings that McEntire’s

Cleaning Machines and General Maintenance Tools were used to maintain exempt machines because McEntire did not present any evidence as to which exempt machines require the General Maintenance Tools or the Cleaning Machines.

5. Storage Items: Blower Fans, Warehouse Racks, Stacking Containers, Pallet Flow Brakes, and Water Storage Tanks

McEntire argues the Court of Appeals found McEntire's Warehouse Racks, Stacking Containers, and Blower Fans were not used in the manufacturing process. (Pet. Br. at 17). This is inaccurate. The Court of Appeals corrected the ALC's erroneous legal conclusions regarding whether the Storage Items were tax-exempt pursuant to the Machine Exemption. Importantly, McEntire appears to concede that storage items, like these, are not exempt pursuant to subsection (B)(7). (Pet. Br. at 19). The Regulation plainly states machines used for storage are "not exempt from the tax as a machine used in manufacturing." S.C. Code Ann. Regs. 117-302.5(B)(7) (including storage racks, storage tanks used to store water, and racks and tanks used to store a finished product).

Because subsection (B)(7) is clear that "machines used for storage are taxable," (Pet. Br. at 19), McEntire instead argues these items fall within the "more specific" category of exempt machines and machine parts found in subsection (C)(24) of the Regulation. *See* S.C. Code Ann. Regs. 117-302.5(C)(24) (explaining the exemption applies to machines "used to condition air (including humidification systems) for quality control during the manufacturing process"). The Department agrees that subsection (C)(24) is much more specific than (B)(7) and it specifically applies to an entirely different type of tangible personal property. Subsection (B)(7) relates to tangible personal property used to hold and store materials or the finished product. By contrast, subsection (C)(24) relates to machines designed to condition air.

The ALC found the Blower Fans were machines used to circulate already-conditioned air throughout the facility and the Warehouse Racks, Stacking Containers, and Pallet Flow Brakes are used to position and store the produce within the facility between stages of the process. (R.p. 12-13).

The ALC found these items “all work to maintain the proper temperature within the plant and also to hold and transport the produce before and after it is cut.” (R.p. 26). Because McEntire is required to keep the produce at a certain temperature during the manufacturing process, the ALC found these machines are integral and necessary to McEntire’s manufacturing process. (R.p. 26). Although the ALC relied upon and quoted federal regulations requiring food to be *stored and transported* at specific temperatures, the ALC did not discuss whether these items fell within any of the specific examples of tangible personal property frequently purchased by manufacturers addressed in the Regulation.

Similarly, the ALC found the Water Storage Tanks were essential to McEntire’s manufacturing process, noting the tanks are used to store and mix water with chemicals and to collect run-off cleaning mix. (R.p. 27). As with many of the other items, the ALC’s analysis only discussed the general provision of the Regulation related to whether an item is a “machine used in manufacturing,” without considering the more specific provisions of the Regulation applicable to water storage tanks.

The Court of Appeals properly corrected this error of law. Under the ALC’s facts, the Blower Fans, Warehouse Racks, Stacking Containers, Pallet Flow Brakes, and Water Storage Tanks are not “machines used in manufacturing” pursuant to subsection (B)(7) of the Regulation. The Storage Items provision of the Regulation excludes machines used to store and hold raw materials or finished goods, including storage tanks used to store water. S.C. Code Reg. §117-302.5(B)(7).

6. Administrative Items: Bar Code Scanners, Black Ink Aerosol Cans, Mobile Computer Stands

The ALC found the Bar Code Scanners, Black Ink Aerosol Cans, and Mobile Computer Stands were exempt “machines used in manufacturing” because they are used by McEntire in its efforts to comply with federal laws requiring produce to be tracked throughout the manufacturing process and facility. Thus, because these items are used in the tracking process, the ALC reasoned they must be “integral and necessary to McEntire’s manufacturing.” (R.p. 26). This legal conclusion is affected by an error of law. The ALC failed to consider the item-specific provision of the Regulation titled

Administrative Machines, Furniture, Equipment and Supplies, which explicitly exclude McEntire’s recordkeeping items from “machines used in manufacturing.”

The Court of Appeals corrected the ALC’s decision because subsection (B)(9) of the Regulation explicitly says recordkeeping machines are not exempt under the Machine Exemption. (R.p. 1320). Moreover, the Regulation makes clear that a machine—including those used for administrative purposes—is not a part of the manufacturing process “merely because it is integral and necessary to the manufacturer.” S.C. Code Reg. §117-302.5(B). Instead, the machine must be integral and necessary to the manufacturing process. *Id.*

7. Protective Clothing Items: Coveralls, Eyewear, Gloves, Aprons, Hairnets

The ALC found McEntire’s protective clothing items were exempt pursuant to section 12-36-2120(17) as both “machines used in manufacturing” and “pollution control machines used in manufacturing.” (R.p. 26-27, 29-40). However, the ALC’s decision does not mention the Protective Clothing Items-specific provision of the Regulation. *See* S.C. Code Ann. Reg. 117-302.5(B)(10). Thus, the Court of Appeals reversed the ALC’s decision, relying on the portion of the Regulation excluding protective clothing from the definition of “machine” as used in the Machine Exemption. (R.p. 1326). The Court of Appeals did so without disturbing any facts the ALC determined about McEntire’s recordkeeping items.

a. McEntire classified the tangible personal property identified as Coveralls, Gloves, Aprons, Eyewear, and Hairnets as “protective clothing.”

To the extent McEntire may argue the tangible personal property collectively referred to as “protective clothing” throughout this tax controversy is not accurately classified as “protective clothing” for purposes of the Regulation, this issue was not raised to or ruled upon by the ALC; therefore, it is not preserved for review. *See Kiawah Resort Assocs.*, 318 S.C. at 505-506. At all times – up until the Court of Appeals applied the Regulation’s Protective Clothing Items-specific provision – both parties, the ALC, and the Court of Appeals referred to McEntire’s collection of tangible personal

property identified as Coveralls, Eyewear, Gloves, Aprons, and Hairnets as “protective clothing.” McEntire has never suggested these items should be considered anything other than “protective clothing.” In fact, during opening statements, McEntire made clear this tax controversy covered two issues: “certain machinery and equipment, but *primarily protective clothing*. . . .” (R.p. 150:19 – 152:25).

We - - the major issue in dispute today, however, is protective clothing. And McEntire buys a large amount of *protective clothing* each year. And so the issue is whether that *protective clothing* is subject to tax. . . .

And we contend the two exemptions that cover the *protective clothing*. One is the Class 100 Cleanroom Exemption, and McEntire will testify federal law. State law requires there be a Class 100 Cleanroom at the facility when there is, and a protective clothing is required by federal law to use in a Class 100 Cleanroom.

The second exception we contend that applies to *protective clothing* is the Pollution Control Exemption. . . . So that’s *the major issue today is whether protective clothing is exempt from sales tax*. We contain it is exempt under the Class 100 Cleanroom and the Pollution Control Exception. . . .

Id.

In addition to identifying the Coveralls, Eyewear, Gloves, Aprons, and Hairnets as protective clothing items, McEntire never asked the ALC or the Court of Appeals to define “protective clothing” as used in the Regulation. Similarly, McEntire never asked either court whether the at-issue items of tangible personal property satisfied the legal definition of “protective clothing,” as used in the Regulation. Therefore, these issues are not preserved for review. *See Kiawah Resort Assocs. v. S.C. Tax Comm’n*, 318 S.C. 502, 505-506, 458 S.E.2d 542, 544 (1995) (stating issues not raised to and ruled on by the ALC are not preserved for appellate review).

The Regulation specifically excludes tangible personal property considered “protective clothing” from the definition of “machine” for purposes of the Machine Exemption. This means that even if the items of tangible personal property McEntire has identified as “protective clothing” do prevent or abate pollution *they are excluded* from the definition of “machine” for purposes of the *Machine*

Exemption. The Pollution Control Machine Exemption is only available for tangible personal property that qualifies as a “machine” – regardless of how the manufacturer may use the property.

b. The Clean Room Exemption is not the same as the Machine Exemption.

To the extent McEntire’s Brief can be construed as alleging the Court of Appeals erred in failing to consider whether the protective clothing at issue is exempt from sales and use tax pursuant to the Clean Room Exemption, this argument is not preserved nor properly before this Court. *See Carolina Chloride, Inc. v. Richland Cnty.*, 394 S.C. 154, 171-172, 714 S.E.2d 869, 878 (2011) (“If the trial judge is deemed to have alternatively ruled Carolina Chloride failed to exhaust its administrative remedies, this ruling, right or wrong, would require affirmance as Carolina Chloride did not timely dispute this alternative ground.”) (citing *Richland Cnty v. Palmetto Cablevision*, 261 S.C. 222, 199 S.E.2d 168) (1973) (stating an unchallenged ruling, right or wrong, becomes law of the case).

The Clean Room Exemption, found at section 12-36-2120(54) of the South Carolina Code of Laws, exempts purchases of “clothing and other attire required for working in a Class 100 or better as defined in Federal Standard 209E clean room environment” from sales and use tax. The Clean Room Exemption is cross-referenced in subsection (B)(10) of the Regulation, addressing protective clothing). The provision in the Regulation identifies the *Clean Room* Exemption as an additional exemption to consider when determining whether the retail sale of tangible personal property identified as protective clothing is subject to sales and use tax. The first sentence of the subsection provides: “Protective clothing worn by an employee working in the area in which the manufacturing process occurs does not qualify as a machine and is not exempt from the tax as a machine used in manufacturing tangible personal property for sale under Section 12-36-2120(17).” This explicitly excludes McEntire’s protective clothing items from the legal definition of “machines” as used in the Machine Exemption. The next (and final) sentence of the subsection then provides: “However, ‘clothing and other attire required for working in a Class 100 or better as defined in Federal Standard

209E clean room environment' is exempt under the provisions of Section 12-36-2120(54).” Clearly, this does not create an exception to the exclusion of items of protective clothing from the definition of “machine” as used in the Machine Exemption. Instead, the Regulation simply *points out a different exemption is available* to exempt protective clothing when the protective clothing is required by law.

The ALC thoroughly considered whether the protective clothing items at issue were exempt from sales and use tax under the Clean Room Exemption. (R.p. 40-41). Ultimately, the ALC found McEntire failed to present sufficient evidence to substantiate these protective clothing items were exempt under the Clean Room Exemption. (R.p. 41). McEntire accepted, and did not appeal, this ruling. That finding is law of the case. Therefore, to the extent McEntire now may be suggesting that the Court of Appeals erred because it failed to consider whether the protective clothing at issue is exempt from sales and use tax pursuant to the Clean Room Exemption, that argument is not preserved and not properly before this Court. *See Carolina Chloride, Inc. v. Richland Cnty.*, 394 S.C. 154, 171-172, 714 S.E.2d 869, 878 (2011).

III. Because McEntire uses its General Maintenance Tools and Generators only as needed or seasonally, the Court of Appeals did not err in finding these items taxable because they were not “used in manufacturing” as required by South Carolina law.

McEntire argues the Court of Appeals created a new or additional eligibility factor for the Machine Exemption by finding a machine “seasonally” or “as-needed” is not “used in manufacturing” pursuant to the Machine Exemption. This misconstrues the Court of Appeals’ decision.

As discussed above, the Machine Exemption exempts the tangible personal property that is *both* a “machine” *and* “used in manufacturing.” S.C. Code Ann. § 12-36-2120(17). The Regulation articulates a general 3-part test to determine whether property constituting a “machine” is “used in manufacturing.” S.C. Code Ann. Reg. 117-302.5(B)(1). To be “used in manufacturing,” the property must serve “as an essential and indispensable component part of the manufacturing process, *and is* used on an ongoing and continuous basis during the manufacturing process.” *Id.* (emphasis added).

That is to say, if the item is not an “essential and indispensable component part” of the machine, it is not “used in manufacturing” as contemplated by the Regulation *even if* it is used on an “ongoing and continuous basis” because it fails the second factor of the Regulation’s 3-factor test defining “used in manufacturing.”

The Regulation states the “machine” qualifies for the Machine Exemption if it is “integral and necessary to the manufacturing process.” S.C. Code Regs. Ann. 117-302.5(B)(1). The Court of Appeals in this case defined the terms “integral” and “necessary” as they relate to the Machine Exemption and Regulation:

The machine exemption regulation does not define the terms “integral” and “necessary.” Those are commonly defined as “essential to completeness” and “an indispensable item.” 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.”

(R.p. 1318) (internal citations omitted).

Practical application of the defined terms within the Machine Exemption and Regulation requires the property to be “used in manufacturing” to be an exempt machine. S.C. Code Ann. § 12-36-2120(17). To be “used in manufacturing,” the machine must be “integral and necessary” to the manufacturing process. S.C. Code Regs. Ann. 117-302.5(B)(1). The Regulation does not specifically define those terms; however, it sets forth the 3-part test, which includes determining whether the at-issue property is used on an ongoing and continuous basis. *Id.* During the discussion of the Machine Exemption and Regulation’s application, the Court of Appeals further clarified – and McEntire has not challenged – the meaning of “integral” and “necessary” as used in the Regulation. (R.p. 1318).

In reversing the ALC’s legal conclusion that McEntire’s purchases of tangible personal property (a) that McEntire used frequently (but not always) and (b) that is used at an employee’s discretion to hasten production, the Court of Appeals found the ALC erred as a matter of law in applying the Regulation’s plain meaning to the facts as found by the ALC. *Id.* This is neither

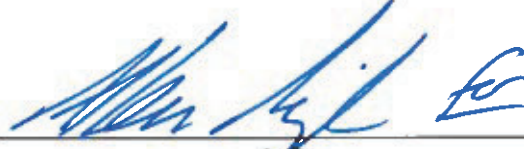
expanding nor limiting the Machine Exemption’s general application. Indeed, the Court of Appeals merely applied the correct and unchallenged meanings of the defined elements of the Machine Exemption and Regulation. Accordingly, the Court of Appeals corrected the ALC’s error of law that resulted in the ALC incorrectly finding that property used when it is needed (as needed) or when it is desirable to speed up production (seasonally) is used on an “ongoing and continuous basis” as used in the Regulation. Thus, the ALC’s decision was affected by an error of law that resulted in the ALC impermissibly expanding the Machine Exemption beyond its plain meaning to find property that is *not integral and necessary* to the manufacturing process because it is *not always required* for the manufacturing machine function is used on an “ongoing and continuous basis” pursuant to the Regulation. The Court of Appeals corrected the ALC’s error of law, it did not create a new exception to the Machine Exemption.

CONCLUSION

Based on the foregoing, the Court of Appeals’ decision in this case should be affirmed. McEntire has abandoned the taxability of 23 of the 25 items on appeal. The Court of Appeals properly reversed the ALC’s decision that was affected by an error of law. The ALC’s error of law resulted in the ALC impermissibly broadening the Machine Exemption to apply to tangible personal property that is not “machines use in manufacturing” as explained in the Machine Exemption and the Regulation. The Court of Appeals corrected this error of law without changing, disturbing, or ignoring any of the ALC’s facts. Additionally, the Court of Appeals did not create a new requirement for the exemption by referring to the opposite of “ongoing and continuous” as “as needed” or “seasonal.” Accordingly, the Department respectfully asks this Court to affirm the Court of Appeals.

<Signature on following page>

SOUTH CAROLINA DEPARTMENT OF REVENUE

A handwritten signature in blue ink, appearing to read 'Dare Perry Bailey', is written over a horizontal line.

Dare Perry Bailey [S.C. Bar No. 76152]

Jason P. Luther [S.C. Bar No. 78021]

300A Outlet Pointe Blvd.

Columbia, SC 29210

(803) 898-5110

Dare.Bailey@dor.sc.gov; CourtOrders@dor.sc.gov

Columbia, South Carolina
July 8, 2024