

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT
The Honorable Shirley C. Robinson
Administrative Law Judge

Case No. 11-ALJ-17-0430-CC

Field House Properties, Appellant,

v.

South Carolina Department of Revenue, Respondent.

FINAL BRIEF OF RESPONDENT

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TABLE OF CONTENTS

Page

| | |
|--|----|
| TABLE OF AUTHORITIES | ii |
| STATEMENT OF THE ISSUES ON APPEAL..... | 1 |
| STATEMENT OF THE CASE..... | 2 |
| ARGUMENT: | |
| DID THE ADMINISTRATIVE LAW COURT PROPERLY GRANT RESPONDENT’S MOTION FOR SUMMARY JUDGMENT IN HOLDING THAT THE PROPERTY TAX EXEMPTION FOR INVENTORIES UNDER S.C. CODE ANN. § 12-37-220(B)(30) (2000) DOES NOT APPLY TO PARKING SPACES SUBDIVIDED FOR INDIVIDUAL SALE..... | |
| I. THE LEGISLATURE ONLY INTENDED FOR § 12-27-220(B)(30) TO EXEMPT TANGIBLE PERSONAL PROPERTY BASED ON THE PLAIN MEANING OF THE TERM INVENTORY..... | 5 |
| II. THE LEGISLATIVE HISTORY OF THE STATUTES IN TITLE 12 SHOWS THE LEGISLATURE CONSIDERS TANGIBLE GOODS, NOT REAL PROPERTY; AS INVENTORY..... | 7 |
| III. FEDERAL TAX LAW LIMITS INVENTORY TO TANGIBLE PERSONAL PROPERTY | 10 |
| IV. THE DEPARTMENT’S LONGSTANDING ADMINISTRATIVE POLICY IS NOT TO TREAT REAL PROPERTY AS INVENTORY..... | 14 |
| CONCLUSION..... | 14 |
| CERTIFICATE OF COUNSEL..... | 16 |

TABLE OF AUTHORITIES

| CASES: | Page |
|---|------------|
| <u>Caughman v. Columbia Y.M.C.A.</u> , 212 S.C. 337, 47 S.E.2d 788 (1948)..... | 7 |
| <u>Charleston County Sch. District v. State Budget and Control Bd.</u> , 313 S.C. 1, 437 S.E.2d 6 (1993)..... | 6 |
| <u>Clark v. Aiken County Gov't</u> , 366 S.C. 102, 107, 630 S.E.2d 99, 101 (Ct. App. 2005)..... | 4 |
| <u>Hodges v. Rainey</u> , 341 S.C. 79, 85, 533 S.E.2d 578, 581 (2000)..... | 5 |
| <u>John D. Hollingsworth on Wheels, Inc. v. Greenville County Treasurer</u> , 276 S.C. 314, 278 S.E.2d 340 (1981)..... | 6 |
| <u>Homes by Ayres v. Comm'r of Internal Revenue</u> , 795 F.2d 832, (9 th Cir. 1986)..... | 11, 12, 14 |
| <u>Lee v. Thermal Engineering Corp.</u> , 352 S.C. 81, 91-92, 572 S.E.2d 298, 303 (Ct. App. 2002)..... | 6 |
| <u>Multi-Cinema Ltd. v. S.C. Tax Comm'n</u> , 292 S.C. 411, 357 S.E.2d 6 (1987)..... | 14 |
| <u>Olson v. S.C. Dep't of Health & Env'tl. Control</u> , 379 S.C. 57, 63, 663 S.E.2d 497, 500-01 (Ct. App. 2008)..... | 4 |
| <u>Palmetto Lumber Co. v. Southern Ry.</u> , 154 S.C. 129, 151 S.E. 279 (1929)..... | 7 |
| <u>Pee v. AVM, Inc.</u> , 344 S.C. 162, 168, 543 S.E.2d 232, 235 (Ct. App. 2001)..... | 6 |
| <u>S.C. Coastal Conservation League v. S.C. Dep't of Health and Env'tl. Control</u> , 390 S.C. 418, 425, 702 S.E.2d 246, 250 (2010)..... | 5 |
| <u>Smith v. S.C. Highway Comm'n</u> , 138 S.C. 374, 136 S.E. 487 (1927)..... | 9 |
| <u>Southlake Dev. Co. v. Sec'y of the Dep't of Revenue and Taxation</u> , 745 So.2d 203, 204 (Ct. App. 1999)..... | 8, 9 |

| | |
|--|--------|
| <u>State ex rel. McLeod v. Montgomery,</u> 244 S.C. 308, 136 S.E.2d 778 (1964)..... | 9 |
| <u>State v. Landis,</u> 362 S.C. 97, 606 S.E.2d 503 (Ct. App. 2004)..... | 6 |
| <u>State v. Pittman,</u> 373 S.C. 527, 561, 647 S.E.2d 144, 161 (2007)..... | 6 |
| <u>Turner v. S.C. Dep't of Health & Envtl. Control,</u> 377 S.C. 540, 544, 661 S.E.2d 118, 120 (Ct. App. 2008)..... | 4 |
| <u>Whitnerv. State,</u> 328 S.C. 1, 6, 492 S.E.2d 777, 779 (1997)..... | 6 |
| STATUTES: | |
| La. Rev. Stat. Ann. § 47.6006..... | 9 |
| S.C. Code Ann. § 1-23-610(B) (Supp. 2010)..... | 4 |
| S.C. Code Ann. § 12-37-210 (2000)..... | 5 |
| S.C. Code Ann. § 12-37-220(B)(30) (2000)..... | Passim |
| S.C. Code ann. § 12-37-1320 (1976)..... | 8 |
| S.C. Code Ann. § 12-37-1410 (1976)..... | 8 |
| S.C. Code Ann. § 12-37-1420 (1976)..... | 8 |
| S.C. Code Ann. § 12-43-220(b) (1976)..... | 7 |
| S.C. Code Ann. § 12-43-224 (2000)..... | 10 |
| S.C. Code Ann. § 12-43-225 (Supp. 2010)..... | 10 |
| 27 S.C. Code Ann. Reg. 117-1700.2 (Supp. 2010)..... | 14 |
| Act No. 145, 1979 S.C. Acts 252..... | 10 |
| Act No. 361, 1992 S.C. Acts 2075..... | 8 |
| Act No. 363, 1996 S.C. Acts 2226..... | 8 |

| | |
|---|------------|
| Act No. 472, 1980 S.C. Acts 1401..... | 8 |
| Act No. 540, 1986 S.C. Acts 4877..... | 8 |
| IRC § 471..... | 11, 12 |
| IRC § 1237..... | 13 |
| Treas. Reg. § 1.1237-1(a)(4) (1960)..... | 14 |
| OTHER AUTHORITIES: | |
| ALC Rule 68..... | 4 |
| <u>Black's Law Dictionary</u> (9 th ed. 2009)..... | 6, 7, 11 |
| <u>Glossary for Property Appraisal and Assessment 72</u> (International Association of Assessing Officers 1997)..... | 7 |
| IRS Publication 538, <u>Accounting Periods and Methods,</u> at 17 (March 2008)..... | 13 |
| IRS Rev. Proc. #2009-39..... | 12 |
| Rule 56(c), SCRCP..... | 4 |
| S.C. Rev. Rul. #91-7..... | 10, 11, 14 |
| U.C.C. § 9-102..... | 6 |

STATEMENT OF ISSUE ON APPEAL

Did the Administrative Law Court properly grant Respondent's Motion for Summary Judgment in holding that the property tax exemption for inventories under S.C. Code Ann. § 12-37-220(B)(30) (2000) does not apply to parking spaces subdivided for individual sale?

STATEMENT OF THE CASE

Petitioner (Field House) commenced this action in the Administrative Law Court (ALC) on August 16, 2011 by requesting a contested case hearing seeking relief from a Department Determination of Respondent (Department) upholding an assessment of property tax on real property. (R., p. 11, Request for Contested Case Hearing).

In December of 2006, Field House purchased an undeveloped parcel of real property near the University of South Carolina football stadium. (R., p. 1, Order, p. 1). Field House paved the parcel before subdividing out approximately ninety-nine parking spaces for vehicles. (R., p. 1; Order, p. 1). Field House then began selling the individual parking spaces. (R., p. 1, Order, p. 1). In October 2008, the Richland County Assessor issued Field House Notices of Classification, Appraisal, and Assessment of property taxes for fifty-five spaces not yet sold. (R., p. 1, Order, p. 1). The assessment valued each parking space at \$25,000 and assessed taxes totaling \$37,526 for the entire parcel. (R., p. 1, Order, p. 1).

Field House challenged the assessment by arguing that S.C. Code Ann. § 12-37-220(B)(30) (2000) exempted the parking spaces from property tax as "inventory." (R., p. 1, Order, p. 1). On November 10, 2008, the Assessor notified Field House of its decision not to adjust the assessment. (R., p. 2, Order, p. 2). By letter dated December 11, 2008, Field House notified the Department of its position regarding the parking spaces. (R., p. 2, Order, p. 2). On April 2, 2009, the Department's Property Tax Division notified Field House of its decision that the parking spaces were not exempt from property tax because the exemption for inventory under § 12-37-220(B)(30) only applies to personal property. (R., p. 2, Order, p. 2). On December 4, 2009, Field House paid to the Richland County

Assessor all of the 2008 property taxes assessed on the parking spaces. (R., p. 2, Order, p. 2).

Field House then filed with the Department a claim for refund dated March 9, 2010, again asserting that the parking spaces should be exempt as inventory. (R., p. 2, Order, p. 2). On March 26, 2010, the Department denied the claim for refund on the same grounds stated in its April 2, 2009 letter. (R., p. 2, Order, p. 2). Field House protested the denial by letter dated June 24, 2010. (R., p. 2, Order, p. 2). On July 18, 2011, the Department issued its final Determination that the parking spaces are not exempt as inventory under § 12-37-220(B)(30). (R., p. 11, Request for Contested Case Hearing, p. 1).

After Field House filed its request for a contested case hearing with the ALC, the parties submitted cross motions for summary judgment. (R., p. 20, Respondent's Motion for Summary Judgment; R., p. 31, Cross Motion for Summary Judgment and Memorandum in Opposition to Respondent's Motion for Summary Judgment). On February 10, 2012, without a hearing on the matter, the ALC granted the Department's Motion for Summary Judgment. (R., p. 1, Order, p. 1). On March 9, 2012, Field House filed and served its notice of appeal.

ARGUMENT

THE ADMINISTRATIVE LAW COURT PROPERLY GRANTED RESPONDENT'S MOTION FOR SUMMARY JUDGMENT IN HOLDING THAT THE PROPERTY TAX EXEMPTION FOR INVENTORIES UNDER S.C. CODE ANN. § 12-37-220(B)(30) (2000) DOES NOT APPLY TO PARKING SPACES SUBDIVIDED FOR INDIVIDUAL SALE.

In an appeal from the decision of an administrative agency, the Administrative Procedures Act provides the standard of review. Olson v. S.C. Dep't of Health & Env'tl. Control, 379 S.C. 57, 63, 663 S.E.2d 497, 500-01 (Ct. App. 2008); Turner v. S.C. Dep't of Health & Env'tl. Control, 377 S.C. 540, 544, 661 S.E.2d 118, 120 (Ct. App. 2008); Clark v. Aiken County Gov't, 366 S.C. 102, 107, 620 S.E.2d 99, 101 (Ct. App. 2005). S.C. Code Ann. § 1-23-610(B) (Supp. 2010) provides that this Court may reverse or modify an Administrative Law Judge's decision that prejudices the substantive rights of the appellant because the decision violates a statutory provision or is affected by other error of law.¹

The ALC's grant of summary judgment was proper if "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law." ALC Rule 68, and Rule 56(c), SCRCF. This case contains

¹Section 1-23-610(B) states:

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 characterized by abuse of discretion or clearly unwarranted exercise of discretion.

no genuine issue of material fact regarding the subdivided parking spaces. Further, the Department is entitled to judgment as a matter of law because, as the ALC properly held, subdivided real property is not exempt from property tax as inventory under § 12-37-220(B)(30) for the reasons set forth below. Accordingly, this Court should uphold the ALC's order granting the Department's Motion for Summary Judgment.

S.C. Code Ann. § 12-37-210 (2000) provides that all real and personal property in this State shall be subject to taxation. Section 12-37-220(B)(30) provides an exemption from property tax for "[a]ll inventories." As the ALC held, the taxpayer's subdivided parking spaces are not exempt from property tax under § 12-30-220(B)(30) as inventory for four reasons. First, the Legislature only intended for that section to exempt tangible personal property based on the plain meaning of the term inventory. Second, the legislative history of the statutes in Title 12 shows the Legislature considers tangible goods, not real property, as inventory. Third, federal tax law limits inventory to tangible personal property. Fourth, the Department's longstanding administrative policy is not to treat real property as inventory.

I. THE LEGISLATURE ONLY INTENDED FOR § 12-37-220(B)(30) TO EXEMPT TANGIBLE PERSONAL PROPERTY BASED ON THE PLAIN MEANING OF THE TERM INVENTORY.

Section 12-37-220(B)(30) provides an exemption from property tax for "[a]ll inventories." The plain language of the statute shows the Legislature intended for inventory to include only tangible personal property. The cardinal rule of statutory construction is to give effect to the intent of the Legislature. S.C. Coastal Conservation League v. S.C. Dep't of Health and Envtl. Control, 390 S.C. 418, 425, 702 S.E.2d 246, 250 (2010); Hodges v. Rainey, 341 S.C. 79, 85, 533 S.E.2d 578, 581 (2000) (citing

Charleston County Sch. District v. State Budget and Control Bd., 313 S.C. 1, 437 S.E.2d 6 (1993)). Legislative intent is first and foremost determined by the language of the statute. State v. Pittman, 373 S.C. 527, 561, 647 S.E.2d 144, 161 (2007) (citing Whitner v. State, 328 S.C. 1, 6, 492 S.E.2d 777, 779 (1997)). The language of a tax exemption statute must be given its plain, ordinary meaning and must be strictly construed against the claimed exemption. John D. Hollingsworth on Wheels, Inc. v. Greenville County Treasurer, 276 S.C. 314, 278 S.E.2d 340 (1981). “The legislature is presumed to have fully understood the meaning of the words used in a statute and, unless this meaning is vague or indefinite, intended to use them in their ordinary and common meaning or in their well-defined legal sense.” Pee v. AVM, Inc., 344 S.C. 162, 168, 543 S.E.2d 232, 235 (Ct. App. 2001). “Where a word is not defined in a statute, our appellate courts have looked to the usual dictionary meaning to supply its meaning.” Lee v. Thermal Engineering Corp., 352 S.C. 81, 91-92, 572 S.E.2d 298, 303 (Ct. App. 2002); see also State v. Landis, 362 S.C. 97, 606 S.E.2d 503 (Ct. App. 2004) (“When faced with an undefined statutory term, court must interpret the term in accord with its usual and customary meaning.”).

Black’s defines inventory as “raw materials or goods in stock.” Black’s Law Dictionary (9th ed. 2009). For purposes of bankruptcy law, it defines the term as “personal property leased or furnished, held for sale or lease, or to be furnished under a contract for service; raw materials, work in process, or materials used or consumed in a business, including farm products such as crops or livestock.” Id. The Uniform Commercial Code also limits the definition of inventory to movable goods. U.C.C. § 9-102. Further, inventory has been defined for property tax purposes as “the group of

personal property items whose value is exhibited by value in exchange, that is, ownership is solely for the purpose of sale rather than use.” Glossary for Property Appraisal and Assessment 72 (International Association of Assessing Officers 1997). In each case, inventory is specifically limited to personal property and does not include real property.

II. THE LEGISLATIVE HISTORY OF THE STATUTES IN TITLE 12 SHOWS THE LEGISLATURE CONSIDERS TANGIBLE GOODS, NOT REAL PROPERTY, AS INVENTORY.

Not only does the traditional plain meaning of inventory include only tangible goods, but nothing in the history of Title 12 shows the Legislature intended to broaden that definition to include real property. The exemption must receive a reasonable, practical, and fair interpretation consistent with the purpose, design, and policy of the lawmakers. Caughman v. Columbia Y.M.C.A., 212 S.C. 337, 47 S.E.2d 788 (1948). Thus, in determining the Legislature’s intent under § 12-37-220(B)(30), it is proper to trace the provision’s history and the history of related statutes. Palmetto Lumber Co. v. Southern Ry., 154 S.C. 129, 151 S.E. 279 (1929). The 1976 version of the Code set a general, uniform assessment rate of six percent for taxation of “[a]ll inventories of business establishments.” S.C. Code Ann. § 12-43-220(b) (1976). That provision is still in place today. Importantly, while § 12-37-220(B)(30) now overrides the six percent rate by exempting all inventories, the history of the subsection shows the Legislature only specifically considered tangible goods in allowing the inventory exemption.

In 1976, prior to the enactment of § 12-37-220(B)(30), the Code set forth rates for taxing “merchant’s inventories” and rules for fixing “the value of the inventories.”² S.C.

²A merchant is “[o]ne whose business is buying and selling goods for profit.” Black’s Law Dictionary (9th ed. 2009).

Code Ann. §§ 12-37-1410 and 12-37-1420 (1976). Similarly, Article 9 of the 1976 version of the Code required manufacturers to make a return of “all manufactured articles which have been offered for sale at retail or which have been available for sale at retail.” S.C. Code Ann. § 12-37-1320 (1976). The Legislature later made clear that § 12-37-1320 was describing a manufacturer’s retail inventory by changing the wording to exempt from tax “all inventories of manufacturers, except manufactured articles which have been offered for sale at retail or which have been available for sale at retail.” Act No. 472, 1980 S.C. Acts 1401 (codified at § 12-37-220(A)(6)). Ultimately, Act No. 540, 1986 S.C. Acts 4877, provided for abrogation of property tax on inventory: it exempted, “[e]ffective for the 1988 and subsequent taxable years, all inventories of business establishments.” Act No. 540, 1986 S.C. Acts 4877 (codified at § 12-37-220(B)(30)). Then, Act No. 361, 1992 S.C. Acts 2075, reworded subsection (B)(30) to exempt “[a]ll inventories.” Finally, Act No. 363, 1996 S.C. Acts 2226, repealed §§ 12-37-1410 and 12-37-1420 relating to merchants.

Thus, the Legislature only specifically considered tangible goods in allowing the inventory exemption. Put generally, not only does the traditional plain meaning of inventory include only tangible goods, but nothing in the history of Title 12 shows the Legislature intended to broaden the traditional meaning to include real property. In similar circumstances, the Louisiana Court of Appeal held that it could not expand the definition of inventory to include subdivided real property. In Southlake Dev. Co. v. Sec’y of the Dep’t of Revenue and Taxation, 745 So.2d 203, 204 (Ct. App. 1999), a taxpayer who subdivided undeveloped land to sell as residential lots claimed that the lots were inventory for purposes of property tax. The tax statute at issue in the case addressed

“inventory held by manufacturers, distributors, and retailers.” Id. at 206 (citing La. Rev. Stat. Ann. § 47:6006). The court noted that applicable administrative regulations limited inventory to personal property. Id. at 207-08. The court reasoned that including real property in inventory was unjustified because it would overreach both the traditional meaning of the term and the specific portrayals of the term in the statute:

Where there is any doubt about the intent or meaning of a law in derogation of long accepted rules, the statute is given the effect that makes the least rather than the most change in the existing body of the law. Moreover, the time honored maxim, *expressio unis et exclusio alterius* . . . teaches us that when the legislature specifically enumerates a series of things, the legislature’s omission of other items, which could have been easily included in the statute, is deemed intentional.

Id. at 206.

Further supporting the exclusion of real property from inventory is the Legislature’s longstanding taxation of real property held and subdivided for purposes of sale notwithstanding the inventory exemption. “Statutes pertaining to the same subject should be harmonized,” Smith v. S.C. Highway Comm’n, 138 S.C. 374, 136 S.E. 487 (1927), and “[a] statute must be interpreted so as to avoid absurd results,” State ex rel. McLeod v. Montgomery, 244 S.C. 308, 136 S.E.2d 778 (1964). Since 1979, the Legislature has specifically provided a tax rate for certain undeveloped parcels subdivided into lots for sale:

Notwithstanding the requirement that real property is required by law to be appraised at fair market value for ad valorem tax purposes, when undeveloped acreage is surveyed into subdivision lots and the conditional or final plat is recorded with the appropriate county official, the county assessor shall appraise each lot as an individual

property and then discount his gross actual market value estimate of the developer's lot holdings

Act No. 145, 1979 S.C. Acts 252 (codified at S.C. Code Ann. § 12-43-224 (2000)). Thus, rather than classifying subdivided lots held for sale as inventory, the Legislature has addressed them separately and provided a discounted tax therefor. In 2000, the Legislature narrowed the discount to parcels subdivided into "at least ten building lots." S.C. Code Ann. § 12-43-225 (Supp. 2010). Accordingly, although the parking spaces at issue do not fall under the current subdivided lots provision, the statutes show that the Legislature never intended for inventory to subsume subdivided lots for sale. To conclude otherwise would lead to disharmony and absurd results by rendering § 12-43-224 and § 12-43-225 meaningless.

III. FEDERAL TAX LAW LIMITS INVENTORY TO TANGIBLE PERSONAL PROPERTY.

Federal law also supports the conclusion that real property subdivided into parking spaces for sale is not exempt from property tax as inventory. While inventory is not specifically defined by the South Carolina Code, S.C. Rev. Rul. #91-7 advises looking to federal income tax law for guidance in defining inventory for property tax purposes:

. . . [T]here are several situations in which the income tax treatment of an item is dispositive of the property tax treatment. . . . For federal income tax purposes, inventory is defined as **merchandise** purchased for resale. . . .

Another federal income tax concept which is helpful in defining whether an item is considered inventory is treatment on sale.

S.C. Rev. Rul. #91-7 (emphasis added).

Federal income tax law limits inventory to merchandise because tax law has always treated the sale of goods as fundamentally different from the sale of land. In Homes by Ayres v. Comm'r of Internal Revenue, 795 F.2d 832 (9th Cir. 1986), the issue was whether inventory accounting could accurately reflect income from the construction and sale of tract housing developments. The Ninth Circuit ruled that a taxpayer could not use inventory accounting to report income from the sale of tract housing. Id. at 835. The court discussed the tax system's treatment of profit from the sale of land, and it made the same distinction that S.C. Rev. Rul. #91-7 made between gains from holding capital and gains from ordinary income:

“It has consistently been held that the costs of improvements to subdivided real estate held for sale are capital expenditures, allocable to the basis of the taxpayer in the various unsold lots.” Gain from the sale of property is defined as “the excess of the amount realized therefrom over the adjusted basis.” Section 1012 states that the basis of property is its cost, with some exceptions not relevant in this case. When subdivided lots are sold, “the cost or other basis of the entire property shall be equitably apportioned among the several parts, and the gain realized or loss sustained on the part of the entire property sold is the difference between the selling price and the cost or other bases allocated to such part.”

Id. (citations omitted). The court held that a taxpayer may only inventory property other than merchandise³ for income tax purposes if Internal Revenue Code (IRC) § 471⁴

³Merchandise is “a movable object involved in trade or traffic” and “an article of trading or the class of objects in which trade is carried on by physical transfer” and “generally excludes real estate.” Black’s Law Dictionary (9th ed. 2009).

⁴IRC § 471 provides the “General rule for inventories”:

(a) General rule

Whenever in the opinion of the Secretary the use of inventories is necessary in order clearly to determine the

expressly permits it or if the Tax Commissioner specifically allows it. Id. at 836. The court concluded that IRC § 471 does not expressly allow a taxpayer to use inventory accounting for property other than merchandise, and that “[t]he Commissioner has consistently maintained that real property cannot be inventoried for tax purposes.” Id. at 835-36 (citations omitted).⁵

The taxpayer specifically argues that federal law allows treating the spaces as inventory for two reasons. First, the IRS accepted the taxpayer’s 2007 federal income tax partnership return characterizing the parking spaces as inventory. This argument fails because merely processing the return as submitted does not constitute the consent of the IRS Commissioner that inventory accounting was proper. The Commissioner must consent through a regulation or similar formal, written document, such as a revenue ruling. See id. at 834. Indeed, federal guidelines regarding methods of accounting for

income of any taxpayer, inventories shall be taken by such taxpayer on such basis as the Secretary may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income.

(b) Estimates of inventory shrinkage permitted

A method of determining inventories shall not be treated as failing to clearly reflect income solely because it utilizes estimates of inventory shrinkage that are confirmed by a physical count only after the last day of the taxable year if--

(1) the taxpayer normally does a physical count of inventories at each location on a regular and consistent basis, and

(2) the taxpayer makes proper adjustments to such inventories and to its estimating methods to the extent such estimates are greater than or less than the actual shrinkage.

⁵The Commissioner has still not consented to inventory accounting for real property. See IRS Rev. Proc. #2009-39.

income expressly prohibit including in inventory “[r]eal estate held for sale by a real estate dealer in the ordinary course of business.” IRS Publication 538, Accounting Periods and Methods, at 17 (March 2008). Thus, a mere processed return without more does not constitute consent of the Commissioner or official IRS policy, *a fortiori* federal tax law, to which the Department could look for guidance.

Second, the taxpayer claims IRC § 1237 defines real property subdivided for resale as inventory. The taxpayer misreads the section; it simply discusses when subdivided property is held for sale in the ordinary course of business. The provision states:

Any lot or parcel which is part of a tract of real property in the hands of a taxpayer other than a C corporation shall not be deemed to be held primarily for sale to customers in the ordinary course of trade or business at the time of sale solely because of the taxpayer having subdivided such tract for purposes of sale or because of any activity incident to such subdivision or sale [if the following conditions are met.]

IRC §1237. In simplified terms, it provides that a taxpayer does not hold a parcel for sale in the ordinary course of business simply because it is subdivided as long as he has held it for five years and does not otherwise sell or develop real estate in the ordinary course of business. The purpose of the statute is to make mere subdivision of a parcel insufficient evidence to show the taxpayer is selling the property as a business rather than holding it as an investment, a distinction of considerable consequence for income tax rates. Further, the accompanying Treasury Regulation specifically states the section “has no application in determining whether or not real property is held by a taxpayer primarily for sale in his business if any requirement under the section is not met.” Treas. Reg. § 1.1237-1(a)(4)

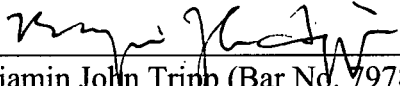
(1960). Whether a parcel is held for sale in the ordinary course of business is an altogether different question from its status as inventory. As was implicit in Homes by Ayres, even land sold to produce ordinary income is not treatable as inventory for federal income tax purposes.

IV. THE DEPARTMENT'S LONGSTANDING ADMINISTRATIVE POLICY IS NOT TO TREAT REAL PROPERTY AS INVENTORY.

Finally, real property subdivided into parking spaces for sale is not exempt from property tax as inventory because the Department's longstanding administrative policy is not to treat real property as inventory. The administrative position of an agency is entitled to great weight and should not be overruled absent compelling reasons. Multi-Cinema Ltd. v. S.C. Tax Comm'n, 292 S.C. 411, 357 S.E.2d 6 (1987). Here, the Department has never considered inventory to include real property. See S.C. Rev. Rul. #91-7 (answering "What is the definition of 'inventory' for property tax purposes?" with "Merchandise purchased for resale is 'inventory' for purposes of the business inventory tax exemption" (emphasis added)); 27 S.C. Code Ann. Regs. 117-1700.2 (Supp. 2010) (identifying inventory of merchants as personal property). Further, the taxpayer has not presented a compelling reason to alter this longstanding policy.

CONCLUSION

Because no genuine issue of material fact exists as to the taxpayer's subdivided parking spaces and because the ALC properly held that subdivided real property is not exempt from tax as inventory under §12-37-220(B)(30) for the reasons set forth above, the Department respectfully asks this Court to uphold the ALC's Order granting the Department's Motion for Summary Judgment.


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Columbia, South Carolina
October 3, 2012

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT
The Honorable Shirley C. Robinson
Administrative Law Judge

Case No. 11-ALJ-17-0430-CC

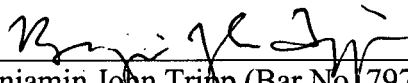
Field House Properties, Appellant,

v.

South Carolina Department of Revenue, Respondent.

CERTIFICATE OF COUNSEL

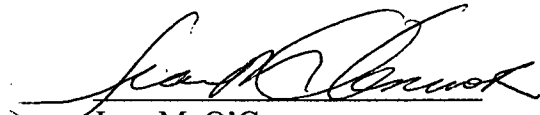
The undersigned certifies that this Final Brief complies with Rule 211(b),
SCACR.


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PROOF OF SERVICE

I, Jean M. O'Connor, do hereby certify that I have caused to be mailed, postage pre-paid, the Department of Revenue's Final Brief in re: Field House Properties v. South Carolina Department of Revenue, Docket No. 11-ALJ-17-0430-CC to John R. Alphin, Esquire, Strom Law Firm, LLC, 2110 Beltline Blvd., Suite A, Columbia, SC 29204 on this 4th day of October 2012.


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