South Carolina's Multimillion Dollar Tax Problem: An Examination of the Manufacturer's Machine Exemption in the South Carolina Sales Tax System

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SOUTH CAROLINA'S MULTIMILLION DOLLAR TAX PROBLEM: AN EXAMINATION OF THE MANUFACTURER'S MACHINE EXEMPTION IN THE SOUTH CAROLINA SALES TAX SYSTEM

I. INTRODUCTION

Taxes have long been a means of support for the operation of governments of all types. In the United States, three systems of taxation currently dominate—income, property, and sales. South Carolina utilizes all three systems, and each has its own nuances and peculiarities. Each system—while maintaining default standards applicable to general classes of people—has, over time, and for various reasons, adopted a number of exclusions, exemptions, and deductions. This Comment focuses on an exemption under the South Carolina Sales and Use Tax System that has become a major issue for state government and for many state businesses. The exemption for "machines used in manufacturing . . . tangible personal property for sale," as explained by the state regulation governing machines, is the basis for numerous tax appeals that is estimated to involve eleven million dollars of taxes paid under protest. In a time of budgetary problems and revenue shortfalls, such a sum is significant. Two cases manifest the ongoing dispute over the correct interpretation of the law governing the exemption: an unpublished opinion of the South Carolina Court of Appeals, issued on January 8, 2003, and a South Carolina Administrative Law Judge Division decision, issued on July 8, 2003.

Any examination of an exemption in tax law must begin with a return to the

3. Id. §§ 12-36-5 to -2510.
4. Id. § 12-36-2120(17).
6. The Department of Revenue could not provide an estimate of how many tax appeals are pending, but the Department provided an eleven million dollar estimate to the State Budget and Control Board to help the General Assembly determine how much state revenue may be affected by these appeals. Telephone Interview with Malaney S. Pike, Attorney, South Carolina Department of Revenue (Nov. 14, 2003).

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foundations of the particular tax system. Part II of this Comment explores the sales tax system in South Carolina. It first scrutinizes the purpose behind the enactment of the sales tax in South Carolina, and then considers the purpose of an exemption, particularly, the machine exemption. These two purposes provide the bases for an analysis of the current statutory and case law. Part II concludes with a brief discussion of how companies take the exemption and how they appeal any items they feel should be exempted.

Part III of the Comment presents the current statutory and case law governing the machine exemption. A brief study of the machine exemption controversy provides an in-depth look at the language of the statute applicable to this controversy. Finally, Part III sets forth the case law adjudicating the tax disputes over the machine exemption.

Part IV of this Comment critiques the laws presented in Part III by dissecting the judicial interpretation of the statute to determine whether the courts correctly applied the law. This Comment seeks to predict the direction that the machine exemption is heading in South Carolina. Finally, this Comment gives corrective recommendations which provide an avenue for the state to realign the exemption with its original purpose, whether through case law or statute.

II. DISCUSSION OF THE SALES TAX SYSTEM

The sales tax arrived relatively recently compared with other sources of revenue. It was not adopted in South Carolina until 1951.9 Forms of a property tax have existed in America since the country’s founding, and the income tax has been a major component of state taxation since the early twentieth century.10 South Carolina currently employs all three of these forms of taxation, as well as many other less familiar forms, on a statewide level.11

A. Purpose of the South Carolina Sales Tax

The most effective examination of a state’s purpose in enacting a sales tax focuses on what the state is taxing. The relevant statute imposes a gross proceeds tax “upon every person engaged or continuing within this State in the business of selling tangible personal property at retail” as well as on a few other specific categories including electricity, communications, and coin-operated laundromats.12

10. See Jerome R. Hellerstein & Walter Hellerstein, State Taxation: Constitutional Limitations and Corporate Income and Franchise Taxes ¶ 1.01-1.02, at 1-1 to 1-3 (Warren, Gorham & Lamont 3d ed. 2000).
Simplified, the statute taxes the exchange of goods at the level of final sale or retail. This tax is admittedly "a vendor tax, which means that it is imposed on the seller rather than the purchaser." However, "this tax is generally passed forward to the buyer rather than being absorbed by the seller," so the ultimate consumer is traditionally considered the actual taxpayer.

Why is the state taxing these sales? "Taxes on sales or purchases are among the oldest kinds of taxes in all modern societies, because the exchange of cash for merchandise provides a visible opportunity for the tax collector to intervene and demand a share...." Furthermore, the public tolerates this tax, likely because the sales tax "is paid in small amounts, rather than all at once like property taxes or in larger installments or withholding like the income tax." Also, "many taxpayers... feel that they have more control or choice in paying sales tax." Because the tax only attaches when a purchase is made, the consumer decides when to pay the tax and how much tax to pay by deciding when and how much to purchase. Seemingly, the state taxes sales because the state needs more revenue and its citizens accept this tax with little hesitation. This produces a fairly broad purpose for this tax system, and any exemptions would probably not run counter to that purpose in such a way as to warrant concern. Stated differently, because the state is taxing only to raise extra money, it can provide for an exemption if the result of such an exemption is deemed better for the state than requiring taxation in that particular instance.

**B. Purpose of a Sales Tax Exemption**

In certain situations, a state may not wish to enforce the general sales tax. If so, it will then enact an exemption. Even if "a transaction is subject to sales... tax, a particular exemption in the statute may exempt it from sales... tax." South Carolina statute incorporates a multitude of such exemptions. The state recognizes five general categories of exemptions—government-related exemptions, business incentive exemptions, agricultural exemptions, educational exemptions,

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13. Ulbrich, supra note 9, at 57.
14. Id.
15. Id. at 57. Whenever a dispute arises in which a taxpayer contests taxes paid to the Department of Revenue, the taxpayer contesting the tax assessment will always be the seller of the good, not the consumer. Although the consumer may, for practical purposes, be thought of as the one paying the tax, the seller is, for legal purposes, the taxpayer. The seller must write the check to the state.
16. Ulbrich, supra note 9, at 56.
17. Id. at 57.
18. Id.
19. Id.
and general public good exemptions. This Comment focuses on the business incentive exemptions.

Ideally, a sales tax "reaches only sales to the ultimate consumer." If this "tax is charged on business inputs and again on the sales of final product, the tax burden on those items will be higher than the sales tax rate intends, and higher than goods from other states where the tax is only on final sales and purchases." Many of South Carolina's business incentive exemptions result from trying to avoid that extra tax burden. Businesses that come to South Carolina know that they will not have to pay taxes on certain expenses, or intermediate purchases, that will be necessary to the operation of their companies.

"The . . . exemption of intermediate purchases from the sales tax base constitutes one of the most significant areas of sales tax controversy" because of the substantial revenue the state gets from intermediate purchases, the large tax liabilities those purchases create for businesses, and the uncertainty and ambiguity of the exact scope of the exemptions. This Comment seeks to clarify one of South Carolina's business incentive exemptions—the machine exemption. South Carolina is not alone in offering this exemption. "Most states offer manufacturers a variety of tax incentives aimed at enticing businesses to locate or expand operations within their borders. Among those incentives are sales . . . tax exemptions . . . for machinery and equipment used in manufacturing."

As discussed above, "[t]he theoretical justification for exempting machinery . . . is . . . to avoid pyramiding of the tax." Another justification is to encourage the expansion of industry. Both justifications have the same goal—"enticing businesses to locate or expand operations within [the state's] borders." These two purposes provide the guidelines for all economically motivated exemptions. However, these purposes must be considered in conjunction with the purpose of the tax system. The state must balance the benefit of placating the business community with the benefit of the tax revenue that intermediate purchases provide. Perceived imbalances are often catalysts for controversies. These imbalances often arise from

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22. TAX INCENTIVES, supra note 20, at 131.
24. ULBRICH, supra note 9, at 59.
25. See TAX INCENTIVES, supra note 20, at 131-33.
29. 2 HELLERSTEIN & HELLERSTEIN, supra note 23, ¶ 14.05[1], at 14-65.
30. Id. at 14-66.
31. Tax Management, supra note 28, § 1330.01.
an unexpected or undesirable interpretation of an existing law. 32

C. Applying an Exemption

Exemptions are claimed on line 4 of the ST-3, South Carolina’s Sales and Use Tax Return Form. 33 If the claim for an exemption is denied, the taxpayer must pay taxes on the denied amount. The taxpayer then has two options. The taxpayer can accept the denial, pay the taxes, and do nothing more; or the taxpayer can file a written protest with the Department of Revenue. 34 If the Department of Revenue finds against the taxpayer, the taxpayer can request a contested case hearing before the administrative law judge division. 35 The decision by the administrative law judge division can be appealed to a circuit court, 36 and proceed through the court system. Depending on the final outcome, the Department of Revenue either keeps the protested money or refunds the money to the taxpayer.

III. PRESENTATION OF CURRENT LAW

A. The Machine Controversy

The machine exemption has been and remains a source of controversy. States have used both purposes mentioned above to justify this exemption. 37 The problem that has arisen is that states and taxpayers disagree on what constitutes a machine. “The definition . . . differs greatly among the states.” 38 To determine the proper definition in South Carolina, this Comment looks first to statutory law, 39 then to case law.

B. Statutory Law

The South Carolina General Assembly has exempted from sales tax the sale of “machines used in manufacturing . . . tangible personal property for sale.” 40 The

32. Theoretically, proposed statutes and regulations pass through the balancing test before adoption. If a newly passed law is unfavorable, it will instantly lead to litigation. On the other hand, litigation that involves a longstanding law does not typically contest the law itself, but the interpretation of the law.


35. Id. § 12-60-460.

36. Id. § 12-60-3380.

37. See 2 HELLERSTEIN & HELLERSTEIN, supra note 23, ¶ 12.04[5], at 12–63.

38. Tax Management, supra note 28, § 1330.03.

39. In this Comment, “statutory law” refers to both the South Carolina Code and to state regulations.

statute explains further:

"Machines" include the parts of machines, attachments, and replacements used, or manufactured for use, on or in the operation of the machines and which (a) are necessary to the operation of the machines and are customarily so used, or (b) 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. The statute attempts to address the disputed definition of machine. The statute construes "machines" to include "parts," "attachments," and "replacements" that "are necessary to the operation of such machines, and are customarily so used." Three characteristics must be present. Exempt items are 1) machines and all accessories that are both 2) necessary and 3) customary.

The South Carolina Department of Revenue, with the authority granted by the General Assembly, has promulgated a regulation to explain the exemptions found in the statute "in more detail." However, the subsection discussing machines adds nothing to the statutory interpretation except that it lists a multitude of examples of exemptions and non-exemptions. The regulation merely restates the three-part test already found in the statute.

Generally, when interpreting tax statutes, the statute granting the exemption is to be "strictly construed against the taxpayer." The taxpayer also bears the burden to prove "that he or she comes within the claimed exemption."

C. Case Law

When a statute contains undefined or unclear language, the judicial branch assumes its role as interpreter of the law. Prior and current case law may be helpful in defining a machine and in determining what the law currently exempts.

41. Id.
42. Id.
43. Id. § 12-4-320(1) (West 2000).
45. Id. 117-302.5.
46. 68 AM. JUR. 2D Sales and Use Taxes § 112 (2000).
47. Id. § 113.
I. Prior Case Law—Hercules Contractors & Engineers, Inc. v. S.C. Tax Commission

Hercules Contractors and Engineers, Inc. brought an action to recover taxes it had paid in protest.48 Hercules claimed exemptions on three waste treatment facilities and parts thereof, arguing that the buildings qualified as machines.49 The parties and trial judge identified the three facilities in question as "Klopman," "Hartwell," and "Burlington."50 The court of appeals agreed to hear the dispute.51 For purposes of this Comment, analysis of the Klopman facility is most relevant.

The Klopman "facility was constructed by Hercules for Klopman Mills . . . . The facility treat[ed] waste of the plant produced in connection with its manufacture of textile products for sale."52 The court, relying on the pollution abatement section of the statute,53 first recognized that "the fact that a pollution control machine acts upon the effluent from the plant, without acting directly upon the product being manufactured at the plant, [wa]s without significance."54 The focus of the case then turned to whether the facility itself could be classified as a machine. Rejecting the contentions of the Tax Commission, the court found that the building was a machine because it operated "as one single entity."55 The court adopted the viewpoint of several Pennsylvania rulings that looked at the use of the building rather than the form.56 Because the building acted as a single machine, its use was that of a machine rather than a building.

Once the court determined that the building was a machine, the components of the building could also be exempted as part of that building. "Its various parts and attachments" were judged to be "integral and necessary to the operation of the system as a whole."57 Applying this analysis, anything in the building, whether materials used to construct the building or mandatory ladders, could be exempt as a part of the machine if it was necessary and customary.58 The "integral and necessary" test was used only after the court determined what exactly qualified as a part of the machine (building). This test, then, should only apply to parts that are

49. Id.
50. Id. at 429, 313 S.E.2d at 302.
51. Id. at 426, 313 S.E.2d at 300.
52. Id. at 429, 313 S.E.2d at 302.
53. Both the statute and the regulation cited in the case have changed subsections since the Hercules case was decided in 1984, but the old statute and regulation are substantively equivalent to the current statute and regulation. The organization of the regulation has changed, but the new version does little to further aid statutory interpretation.
54. Hercules, 280 S.C. at 430, 313 S.E.2d at 303.
55. Id.
56. Id. at 431–32, 313 S.E.2d at 304.
57. Id. at 430, 313 S.E.2d at 303.
58. Where regulations require a machine to possess certain parts, that part necessarily becomes a part of the machine. The part becomes necessary for legal reasons rather than for practical reasons.
contained within some other item, where that other item has already been classified as a machine under the statute.

2. Current Controversy

a. Anonymous Corp. v. S.C. Department of Revenue

During the period between January 1, 1992 and December 31, 1994, a dispute totaling more than $500,000 arose between Anonymus Corporation (Taxpayer) and the South Carolina Department of Revenue (DOR) over the amount of sales tax owed by the Taxpayer.59 The disputed items consisted of various building "materials used to construct the Dorlastan facility,"60 a plant built to manufacture "an elastic spandex fiber known as Dorlastan."61 The Taxpayer postulated that the entire facility was a machine, thus exempting all the construction materials.62 The basis for this argument was the facility’s need for a specialized, climate-controlled environment that could protect the interior machines and products against outside elements and that could protect machines in the facility from chemicals and heat that might emanate from other machines.63 Alternatively, the company argued that "certain building materials purchased to construct the Dorlastan facility independently act as machines," thereby falling under the machine exemption.64

To determine whether the structure could be a machine, the court turned to Hercules Contractors & Engineers, Inc., v. S.C. Tax Commission65 in which a similar issue had been adjudicated.66 According to the court in Anonymous, "[t]he Hercules court opine[d] that something that is considered a structure or a fixture can also be considered a machine, notwithstanding that it is a fixture or a structure. However, it cannot be a machine if it is a building."67 The question then became how to tell the difference between a building that is a machine and a building that is just a building. In answering that inquiry, the judge in Anonymous relied heavily on the distinction in Hercules between a building that is generally beneficial and can "serve various users of the land" and a building that has "no use apart from the machine of which it is an integral part."68 If the structure can serve as a building, shelter, safehouse, or something similar, it is not exempt even if it seems to be part

60. Id. at 14.
61. Id. at 13.
62. Id. at 17.
63. Id. at 15–16.
64. Id. at 17.
67. Id. at 21.
68. Id.
of a machine. In other words, the building must have no meaningful value apart from its value as a machine.

The court distinguished the result in Hercules by deciding that "the Dorlastan facility buildings could have a use separate and apart from the machinery within."®9 Relying on testimony supporting the facility's greater value, the court ruled that "the Dorlastan building [was] nothing more than a building constructed to house the machinery needed to manufacture the Dorlastan fiber. It benefit[ed] the land generally and could serve other users."®0 Because the court found "that the Dorlastan structures and all of its supporting members d[id] not function in tandem with the machinery inside to create a single machine," it turned to the Taxpayer's alternative argument that individual items could be exempt as machines.®1

The court examined and rejected these items one by one.®2 The judge concluded that the building materials in dispute were "parts of buildings and [we]re not machines"®3 and that each of the other items in dispute were not an "integral part" of the manufacturing process.®4

b. S.C. Department of Revenue v. Springs Industries, Inc.

Having paid sales taxes on items that the company thought should have been tax exempt, Springs Industries, Inc. sought a refund from the South Carolina Department of Revenue.®5 "DOR rejected the request and [Springs] appealed."®6 The appeal generated a lawsuit that was resolved more than five years after the origination of the dispute.®7 Three disputes formed the subject matter of this suit; the relevant dispute was whether certain items are machines.®8 The other two issues have no bearing on this discussion. The appeal went first to the administrative law judge, who ruled in favor of Springs Industries in 1999.®9 To determine whether the items were machines, the judge looked at the statutory language, regulations, and case law.®0 The administrative law judge then broadly construed the definition, holding "that an item can be classified as a machine if it performs an 'essential or indispensable'

69. Id. at 22.
70. Id.
71. Id.
73. Id. at 34.
74. Id. at 28–29.
76. Id.
77. The Supreme Court of South Carolina denied certiorari on October 8, 2003.
79. Id.
80. Id. at 2–3.
function in the manufacturer’s operations.” A state circuit court affirmed the decision, and DOR appealed to the court of appeals. The court of appeals first analyzed both the statute and the regulation. The court then turned to Hercules, which in the court’s interpretation, defined the parts of a machine as those necessary to operate the entire facility, not just those necessary strictly for manufacturing. Using this broad interpretation, which is also known as the “integrated plant” theory, the court of appeals affirmed the ruling of the lower courts against DOR. Because certiorari was denied, the court of appeals ruling stands as the final authority in this case.

IV. CRITIQUE OF THE LAW

A. Court Interpretation

Because the Anonymous and Springs opinions were both based largely on the Hercules decision, this section begins with Hercules.

1. Hercules Contractors & Engineers, Inc. v. South Carolina Tax Commission

Initially, the Hercules court determined that the machine did not have to be part of the production process so long as it was a pollution controlling machine. The court’s holding was consistent with the statutory guidelines because the Klopman facility was constructed to process the pollution resulting from the business’s manufacturing. However, the statute does mandate the pollution that is being controlled be “caused or threatened by” a machine that is “used in manufacturing.”

Next, the court found the building could be a machine because it operated “as one single entity.” Nothing in the statute or regulation precludes such a decision, and the structure of the building did seem to be a part of the process. Therefore, the court in Hercules did not err in deciding that the facilities constituted machines

81. Id. at 3.
82. Id. at 1. Both sides appealed, but DOR appealed the issue relevant to this Comment.
83. Id. at 4–5.
86. See infra Part IV. C. 1.
88. Hercules, 280 S.C. at 430, 313 S.E.2d at 303.
89. Id. at 426, 313 S.E.2d at 302.
91. Hercules, 280 S.C. at 430, 313 S.E.2d at 303.
92. The building had pipes carrying pollution “from one part of the facility to another,” and “pumps and other mechanical devices” were part of the substance of the building. Id. at 429, 313 S.E.2d at 302–03.
that were exempt from sales tax. The holding did incorporate the "integral and necessary" test, but this test should be used only for the elements of an item that has already been classified as a machine. This too is legitimate under the statute, which includes parts of machines in the machine exemption.

2. Anonymous Corporation v. South Carolina Department of Revenue

The administrative law judge correctly applied Hercules to Anonymous in finding the Dorlastan facility to be non-exempt. The court in Hercules rested the exemption squarely upon its determination that the structures (vats, basins, tanks, and pumps) which formed the Klopman facility had "utterly no use apart from the machine of which they [were] an integral part." By contrast, the court in Anonymous judged that "the Dorlastan facility buildings could have a use separate and apart from the machinery within." The court could not have ruled any other way based on the precedent of Hercules.

The test used to determine whether individual items were exempt is the test established in Springs, although the items in Anonymous failed where the items in Springs succeeded.


The court of appeals, failing to duplicate its correct analysis in Hercules nearly twenty years prior, misinterpreted the definition of a machine in Springs. The opinion cited Hercules as precedent, but the Springs court erred, in finding that "in Hercules, the court exempted an entire pollution control facility as a machine used in manufacturing because it found the facility 'integral and necessary to the operation of [the plant] system as a whole.'" That is not the rationale in Hercules. The "integral and necessary" description applied to parts of the facility that made the facility operate "as one single entity." The facility in Hercules was a waste facility that qualified as a machine, not because it was necessary to the manufacturing operation, but because it satisfied the pollution requirement. Had it not met that aspect of the statute, it would not have been an exempt machine. Therefore, in Springs, the law that should have been applied from the Hercules opinion was that a machine can only be exempt from sales tax by being used in the

93. Id. at 430, 313 S.E.2d at 303.
98. Hercules, 280 S.C. at 430, 313 S.E.2d at 303.
99. Id.
manufacturing or by being part of the pollution control that is required by law.

Furthermore, the Springs court failed to consider the "well-settled rule that a statute granting a tax exemption is to be strictly construed against the exemption."\textsuperscript{100} By misinterpreting the definition of a machine, the court has not only failed to strictly construe the statute against the exemption, but has expanded the statute in favor of the exemption.

\textbf{B. Logical Progression}

The case law, with the exception of Anonymous, seems to give machines an increasingly broad definition despite no change in the statute. In fact, the Springs decision quite possibly renders the pollution provision in the statute void. The taxpayer must dispose of waste as part of the manufacturing process, so any pollution control would be necessary to the operation as a whole. All a taxpayer must prove now is that the business needs an item or that an item is somehow integrated into the business operations. If the court decides that the manufacturer in fact needs the item, the item is then exempt. If unchecked, this trend will continue until the statute is revised or nearly all sales to manufacturers are exempt.

\textbf{C. Recommendations}

\textit{1. Statutory Revision}

The first and most obvious recommendation is to revise the statute or regulation to more clearly define what qualifies as a "machine." The Department of Revenue will likely issue an advisory opinion acquiescing to the newest standard, the judiciary will continue to arbitrarily change the interpretation of the exemption, and things will remain unclear. A revision is imperative. This revision should adopt a consistent theory to be used any time a machine is a candidate for exemption. States typically use one of three theories—the "integrated plant" theory,\textsuperscript{101} the "physical change" test, or the "used directly" limitation.\textsuperscript{102} The integrated plant theory is the broadest of the interpretive theories.

Under the integrated plant theory, machinery and equipment are exempt if they perform an essential or indispensable function in the taxpayer’s manufacturing operations . . . . Presumably, most

\textsuperscript{100} Anonymous, No. 02-ALJ-17-0350-CC, at 17 (citing Chronicle Publishers, Inc. v. S.C. Tax Comm’n, 244 S.C. 192, 136 S.E.2d 261 (1964)).

\textsuperscript{101} South Carolina law does not currently employ this theory, but the outcome in Springs is leaning toward this theory if not wholly adopting it. If the state wants the "integrated plant" interpretation to be the official guideline, the General Assembly should make this determination, not the courts.

\textsuperscript{102} See 2 HELLERSTEIN & HELLERSTEIN, supra note 23, ¶ 14.05[2][a]-[e], at 14-67 to 14-88.
modern, or at least efficient manufacturing facilities employ few nonessential assets in their operations. Not surprisingly, a wide variety of machinery and equipment qualify for exemption in states that follow this approach.  

South Carolina is currently considered to have “embrace[d] . . . the integrated plant doctrine.” However, the statute does not mandate or even mention this theory. Furthermore, even if the court prefers this interpretation, the proper body to implement this theory in state law is the legislature. The “integrated plant” theory is too broad of an exemption, and it “narrows the sales tax base” too much. If the state adopts this approach, revenue will be lost, more items than those needed to avoid double taxation will be exempt, and a legislative over-correction may occur. Indeed, this over-correction may be more imminent than many believe. Several South Carolina state legislators, in both the House and the Senate, have shown signs of wanting to change or eliminate several sales tax exemptions in an effort to find more state revenue. Editorials in The State newspaper have applauded these actions. This effort to recapture lost revenue may lead to limiting the machine exemption severely enough that the new law would hurt South Carolina businesses more than a correct interpretation of the current statute.

At the opposite end of the spectrum, the “physical change” test constitutes the narrowest of the theories. In this test, “the exemption depends on whether the machinery physically transforms raw materials during the production process.” The two key determinations turn on when the manufacturing process begins and when it ends. “Many jurisdictions which follow this rule provide a statutory or regulatory framework for determining when manufacturing begins and ends.” South Carolina does not have such language and has no apparent intention of following this interpretation. It should not. This test exemptstoo little, leading to overtaxation. Requiring a physical change fosters double taxation because not every machine that helps manufacture a product effects a physical change upon the product.

The “used directly” limitation is somewhere between the other two theories. Anything that is “used directly in the manufacturing process” qualifies for an exemption. This theory is too vague and inconsistently applied to provide a

103. Tax Management, supra note 28, § 1330.04 (citation omitted).
104. 2 HELLERSTEIN & HELLERSTEIN, supra note 23, ¶ 14.05[2][d], at 14-80.
105. Id. ¶ 14.05[2][d][i], at 14-81.
107. Tax Management, supra note 28, § 1330.04 [B].
108. Id.
109. 2 HELLERSTEIN & HELLERSTEIN, supra note 23, ¶ 14.05[2][c], at 14-83.
useful standard.\textsuperscript{110}

\[ \text{A number [of] state courts have adopted an integrated plant theory, even though the statutes at issue contain a “used directly” limitation. Indeed, there has been a great deal of controversy over the meaning and application of the “used directly” limitation in the state courts, regardless of their position on the integrated plant theory.}\textsuperscript{111} \]

Each of these theories represents an area on the spectrum in the balance between relieving economic burdens and receiving tax revenues. However, each theory has drawbacks, whether too broad, too narrow, or too vague. None provide an acceptable alternative to the current situation; therefore, South Carolina should adopt none of these interpretive theories.

South Carolina should pioneer a new theory, with the legislature expressly adopting and defining it by statute. The current statutory language, “used in manufacturing,”\textsuperscript{112} should remain, but elaboration is necessary. The most effective theory would focus on the “intended purpose” of each machine. This “intended purpose” theory provides an exemption for any machine that the company purchases for the purpose of manufacturing the product.\textsuperscript{113} Machines that are purchased to make the product itself could be exempt, while machines purchased to benefit the product or the company in some other way (packaging, storage, air treatment) would not be exempt. Under this theory, any item that is performing its designed function to make the product what it is, even if not effecting a physical change, would be exempt. All other items, even if integrated into the plant as a whole, would not be exempt because they are not part of the taxation pyramid. This theory aims at eliminating the taxation pyramid, thereby achieving the exemption’s purpose. The state could keep the current “necessary and customary” requirements,\textsuperscript{114} and the burden of proof should remain on the taxpayer to prove both the intended purpose and the necessity of the machine.

Objections may arise in opposition to this theory. First, why throw another theory into the mix? Another theory is needed because the existing theories do not resolve the controversy,\textsuperscript{115} and because this theory is designed to replace the other theories, not stand side-by-side with them. Second, some may be concerned that disclosure of intended purposes will reveal trade secrets. However, this theory

\textsuperscript{110} Id. \S 14.05[2][e][ii], at 14-83 to 14-84.
\textsuperscript{111} Id. at 14-84 (citation omitted).
\textsuperscript{113} This theory is not currently found in any literature and is the sole product of the author. Any further use, expansion, or alteration of this idea and/or terminology is freely permitted. It is designed to clarify rather than muddle the current controversy surrounding the definition of a machine.
\textsuperscript{114} See supra Part III. B.
\textsuperscript{115} If one of the current theories did resolve the controversy in an acceptable way, that theory would likely be adopted and used consistently across the nation.
would not require any more disclosure than other theories. Third, how will this theory avoid becoming as ambiguous as any other? The intended purpose theory avoids ambiguity in two ways: Statutory specificity will effectively block many claims, and clear and consistent judicial interpretation of the statute will affirm the new standard for those claims that are adjudicated. Disputes as to the law's meaning foster controversies; however, mere factual disagreements are far more manageable and predictable. Finally, this change would have a positive impact on the business community in South Carolina. Businesses would be able to predict tax liability with more consistency, and the exempt items would not differ too much from what is presently expected to be exempt. The certainty gained by the taxpayer would be more valuable than the exemptions lost.

2. Judicial Caution

The second recommendation is addressed to the courts. When considering these cases, great care must be exercised in interpreting statutes and applying prior holdings. Although the role of the judiciary is not to give more care when more money is involved, these cases do emphasize judicial error more than other cases might. When a definition hinges on a balancing test, tipping the balance too far can force a legislative over-correction. The purpose of an exemption must be at the forefront when applying the exemption to specific items.

V. CONCLUSION

The definition of a machine for the purposes of the machine exemption, and thus the application of the exemption, has become unclear and controversial. The resulting dispute affects both the state of South Carolina and the manufacturers who operate in the state. Proper tax assessments have become difficult, as the government seeks to protect tax revenues while businesses fight to keep needed income. Both sides would benefit from a resolution to this controversy. The government would benefit from increased certainty as to the extent of tax revenue. Businesses would be able to better forecast their business costs.

The controversy exists because of vague statutory language. The statute as written fails to define a machine, and the examples provided in the regulation do not adequately guide taxpayers. The case law has further muddled the picture. Hercules set forth the law well, but now the law seems to be broadening and falling out of balance under Springs, which wrongly applied Hercules and created a new standard.

The only real solution to the current problem is for the path of South Carolina’s machine exemption law to be corrected and redefined. A new standard, utilizing the author’s “intended purpose” theory of exemption, would clarify the definition of a machine and restore balance to the dueling purposes of the machine exemption. Whether this new standard is adopted is not necessarily the primary argument. It is just the preferred avenue for implementing that argument. The most important
action that needs to be taken is a clarification of the definition. A clear standard will reduce litigation and save time, money, and effort.

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