IN THE SUPERIOR COURT
FOR THE
COMMONWEALTH OF THE **NORTHERN MARIANA** ISLANDS

ISLAND APPAREL, INC.,	)	**Civil Action No. 01-0110B**
Plaintiff,	)	
vs.	)	**ORDER ON MOTION FOR PARTIAL SUMMARY JUDGMENT**
SECRETARY OF FINANCE,	)	
Defendant.	)	

I. INTRODUCTION

¶1 Plaintiff Island Apparel, Inc. ("Island Apparel") silkscreens designs onto articles of ready-made clothing ("apparel") which it subsequently exports for sale outside the Commonwealth. For years, it has claimed **and** obtained a refund **of** excise taxes paid. In February of 2000, the Commonwealth took the position that Plaintiff was no longer entitled to any tax refunds. Through its Motion for Partial Summary Judgment, Plaintiff seeks a ruling from the court that, despite the Commonwealth's change in position, it is still entitled to a refund.

¶2 Robert Goldberg of Calvo and Clark, LLP, appeared for the Plaintiff, and Assistant Attorney General Sheila N. Trianni represented the Secretary of Finance. The court, having reviewed the record in this proceeding, including the memoranda, declarations, and exhibits, now issues its written decision GRANTING the motion.

FOR PUBLICATION

II. FACTUAL BACKGROUND

¶2 The facts giving rise to this controversy are straightforward and undisputed. Island Apparel imports certain apparel and other goods into the Commonwealth, silkscreens various designs onto the apparel, and then exports the silkscreened items outside of the Commonwealth. See Declaration of Clifford P. Shoemake, attached to Plaintiff's Motion for Partial Summary Judgment ("Shoemake Decl."); Declaration of Special Assistant to the Secretary of Finance, Robert Schrack ("Schrack Decl."), attached to the Commonwealth's Response to Plaintiff's Motion for Partial Summary Judgment at ¶¶ 4-6.

¶3 "For the privilege of first sale, use, manufacture, lease or rental of goods, commodities, resources, or merchandise in the Commonwealth," whether it be for business purposes or for personal use, the Commonwealth imposes an excise tax. See 4 CMC §1402. Although the statute does not define the term "use," pursuant to4 CMC §1408, a person importing goods, commodities, resources, or merchandise into the Commonwealth for, among other things, sale or use is entitled to a refund of taxes paid on those items, so long as the items were not used or sold within the Commonwealth.[1]

¶4 According to Plaintiff, the apparel onto which it silkscreens its designs and artwork and then subsequently exports for sale outside the Commonwealth is not "used" in the Commonwealth since the apparel is not worn in the Commonwealth and Plaintiff does not create a new or different product, but merely decorates or embellishes an existing one. The parties do not dispute that the change which Plaintiff makes to its clothing is purely aesthetic and superficial: Plaintiff starts with a T-shirt or other type of ready-made apparel and, after printing a design onto the item, ends up with the same article of clothing. Plaintiff concedes that the clothing has an altered appearance, but maintains that there is no change at all in the use: the T-shirts or sweatshirts are worn in the same manner and

[1] In material part, 4 CMC § 1408 provides:

> Upon application to the secretary [of Finance], any person who imports goods, commodities, resources, or merchandise into the customs territory of the Commonwealth for sale, use, lease or rental and exports them to a buyer outside of the customs territory of the Commonwealth shall be entitled to a refund of tax actually paid on those items, provided however, that such goods, commodities, resources, or merchandise exported were not used, sold, leased or rented within the Commonwealth prior to export.

provide the same protection from the elements. Since Plaintiffs printing process simply converts an undecorated garment into a decorated garment, Plaintiff claims the benefit of the exemption.

¶5 As evidence of the Commonwealth's agreement with its position, moreover, Plaintiff points to a letter dated February 13, 1997, in which the Department of Finance and Plaintiff agreed upon a procedure to credit the excise tax paid by Island Apparel on merchandise exported outside the Commonwealth, See Shoemake Decl. at ¶3; Letter from Department of Finance to Island Apparel dated February 13, 1997, attached to Shoemake Decl. as Ex. "A." According to Plaintiff, the Commonwealth performed under the February 13, 1997 Letter, along with an attached Memorandum of Understanding, to credit Island Apparel with monthly refunds of excise taxes for approximately two years. Shoemake Decl. at 74. When, on or about February 24, 2000, the Secretary of Finance inexplicably denied Plaintiffs request for a refund of excise taxes,[2] Plaintiff filed its complaint in this action seeking a complete refund of all excise taxes paid on apparel and other goods that Plaintiff imported into the Commonwealth and subsequently exported for sale.[3] Plaintiff essentially contends that the Government's two year history of refunding taxes constitutes proof positive that Plaintiff does nothing but add value to the items, and thus should continue to receive a refund of all excise taxes.

¶6 Defendant does not deny either the existence or contents of the February 13 Letter or that, for approximately two years, it refunded virtually all of the excise taxes paid. Response at 2; see also Letter from Customs Service Acting Director Jose C. Mafnas to Clifford Shoemake dated May 14, 1999, attached to Shoemake Decl. at Ex. "B" ("under present law there is no prohibition against issuance of a refund" and granting request for refund). Instead, it takes issue with Plaintiff's representations that the Letter constitutes some concrete agreement to provide refunds in perpetuity. Schrack Decl. at ¶¶7-9.[4] According to Defendant, the only matter appropriate for this court's review is its decision of February 25, 2000, putting Plaintiff on notice that it is not entitled to a refund or

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[2] See Shoemake Decl. at ¶ 8 and Ex. "D" thereto.

[3] The complaint alleges four claims in connection with the Commonwealth's refusal to refund excise taxes: (1) for judicial review; (2) for declaratory relief: (3) for injunctive relief; and (4) for damages.

[4] Although Defendant reads the letter only as the confirmation of a procedure for claiming a refund, at the same time, it agrees not to challenge Plaintiffs refunds prior to February 25. 2000.

credit under 4 CMC § 1408. See **Shoemake Decl.**, Ex. "C." In the Government's view, the apparel is "used" prior to export when Plaintiff silkscreens its designs on the clothing. ***Id.*** The Commonwealth further dismisses the decision of the prior Secretary of Finance to grant Plaintiff credit for excise taxes paid as without legal authority.

67 Although the Commonwealth does not dispute that Plaintiff starts and ends with the same product, it argues that by silkscreening its designs onto what was previously plain apparel, Island Apparel has transformed the clothing. In the Commonwealth's view, apparently any aesthetic change in appearance, regardless of how superficial, constitutes a taxable "use." According to the Commonwealth, there is no distinction between the addition of a coat of paint to a ready-made article, on the one hand, and the transformation of paper, by the addition of a design and verse, into a greeting card. In the Commonwealth's view, both of these processes involve a taxable "use" and the taxpayer would not be entitled to credit for excise taxes paid.

III. QUESTIONS PRESENTED

¶8 Whether Plaintiffs silkscreening of designs onto ready-made apparel qualifies as a taxable use of that apparel, so as to disqualify Plaintiff from receiving a refund of excise taxes paid.

¶9 In determining whether the silkscreening of designs onto ready-made apparel constitutes a taxable use of the apparel, what, if any, deference must the court give to the Secretary of Finance's interpretation of the statute.

IV. ANALYSIS

¶10 The controversy in this case hinges upon the statutory meaning of "use." To resolve this dispute, the court turns to time-honored principles of statutory construction. Both parties recognize that absent ambiguity, the language of a statute must be given its plain meaning, but where, as here, the construction or interpretation of a revenue statute is at issue, special canons of statutory construction apply. ***See Lenox,*** Inc. v. ***Tolson,*** 548 S.E.2d 513 (N.C. 2001). First, if a taxing statute can be construed one of two ways, any ambiguity must be resolved in favor of the taxpayer. See ***Pelligrino*** v. ***Comonwealth,*** Appeal No. 97-001 (N.M.I April 13, 1999), Slip Op. at 8-9. On the other hand, grants of exemption from taxation are most strongly construed against the taxpayer and in favor of taxing authorities. ***See City of Spokane ex rel. Wastewater Management Division v. Washington***

State Department of Revenue, 104 Wash. App. 253, 17 P.3d 1206, 1209 (2001); *Western Mass. Lifecare Corp. v. Bd. of Assessors of Springfield, 747* N.E.2d 97, 102-103 (Mass. 2001). Accordingly, Plaintiff has the burden of showing clearly and unmistakably that the exemption applies, and any ambiguity is "construed strictly, though fairly and in keeping with the ordinary meaning of [its] language, against the taxpayer." *City of Spokane, 17* P.3d at 1209. Finally, in determining whether Plaintiff has met its burden, the court is mindful that although tax exemptions are to be strictly construed, they should not be interpreted in a manner that frustrates the very purpose of exemption. *See Sumitomo Trust and Banking Co. v. Commissioner of Taxation and Finance, 720* N.Y.S.2d 251 *(N.Y. 2001); Transworld Systems,* Inc. *v. County of Sonoma*, 93 Cal.Rptr.2d 165, 168 (Cal.App. 2000).

¶11 To meet its burden, Plaintiff points to the surrounding statutory language, and particularly the words "sold, leased, or rented" in support of its interpretation that section 1408 was intended to impose taxation only upon income-generating activities within the Commonwealth. Plaintiff argues further that according to this *court's* ruling in *Office* of *the Attorney General v. Garments Seized at Mon On Ent., Inc.*,[5] the term "use" must be defined narrowly. Although Plaintiff provides no legislative history to substantiate its position, Plaintiff nevertheless argues that its interpretation is consistent with the intent of the legislature in enacting the refund provision, which, according to Plaintiff, was to spur investment and economic development by providing a tax incentive to those engaged in import-export ventures. Finally, Plaintiff points to the Department of Finance's two year history of granting the rebate and contrasts the prior administrative interpretation of the statute with its abrupt and inexplicable about-face to argue that the agency's initial and longstanding interpretation of the term "use" was correct.

¶12 For whatever reason, the Commonwealth offers no analysis to support its abrupt change in position, nor does it dispute that the rebate provision was enacted, at least in part, to exempt businesses engaged in importing and exporting. Instead, the focus of the Commonwealth's argument is its extremely broad definition of the word "use." Without any explanation for its change in

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[5] Civ. No. 98-1228 (N.M.I. Super.Ct. Aug. 24, 1999) (Order Granting in Part Potential Claimant's Motion for summary Judgment).

position, and even though there has been no amendment of the statutory language, the Secretary now takes the position that "use" means the exercise of any right or power over tangible personal property and that the apparel is "used" within the Commonwealth by its employment in the silkscreening process. See Letter from Secretary of Finance to Cliff Shoemake dated February 25, 2000, attached to Schrack Decl. as Ex. "2."

¶13 An administrative agency's construction or interpretation of a statute, which the agency is charged with enforcing, is entitled to serious consideration by a reviewing court, provided that the agency's construction is reasonable and does not contradict the statute's plain language. See, e.g., ***Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.***, 467 U.S. 837, 843-844, 104 S.Ct.2778, 2781-2, 81 L.Ed.2d 694 (1984); *Seldovia Native Ass'n, Inc. v. Lujan*, 904 F.2d 1335 (9th Cir. 1990).[6] This court, accordingly, has followed the rule that the construction given to a statute by the executive and administrative officers of the Commonwealth charged with its implementation is generally entitled to great weight and will be followed unless there are cogent reasons for holding otherwise. See, e.g., ***Commonwealth* v. *Dado***, Crim. No. 98-0261 (Written Decision Following Trial) at 10; ***Marquis* v. *City of Spokane***, 130 Wash.2d 97, 111, 922 P.2d 43 (1996) (a court "must give great weight to the statute's interpretation by the agency which is charged with its administration, absent a compelling indication that such interpretation conflicts with the legislative intent."). Notwithstanding the deference traditionally accorded to the construction of a statute by those charged with its execution, however, deference does not mean abdication. It is the judiciary which has the ultimate responsibility to construe the language of a statute and determine the law. ***See Marbury v. Madison***, 5 U.S. (1 Cranch) 137, 177, 2 L.Ed. 60, 73 (1803) ("It is emphatically the province and the duty of the judicial department to say what the law is"); *Impecoven* v. *Department of* ***Revenue***, 120 Wash.2d 357, 363, 841 P.2d 752 (1992) (despite granting deference to agency interpretations, courts retain the ultimate authority to determine the purpose and effect of a statute). See *also* 1 CMC

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[6] An agency decision involving the meaning or reach of a statute that reconciles conflicting policies "'represents a reasonable accommodation of conflicting policies that were committed to the agency's care by the statute, [and a reviewing court] should not disturb [the agency decision] unless it appears from the statute or its legislative history that the accommodation is not one that [the legislature] would have sanctioned."' Chevron *U.S.A., Inc., 467* U.S. at 845, 104 S.Ct. at 278 1-2 (quoting *United States v. Shimer, 367 U.S. 374, 382-83* (1961)).

§ 9112(f) (to the extent that the agency's decision rests upon interpretation of statutory language, such decisions involve questions of law which the court is charged with interpreting). The initial question to be addressed, therefore, is what weight, if any, the court must give to the Secretary's sudden interpretive change of heart regarding the application of the rebate statute.

¶14 The Alaska Supreme Court has held that when a "statutory interpretation . . . presents a question of law . . . no particular deference is owed to the agency's interpretation of the applicable statutes." ***Noey v. Department of Environ. Conservation.,*** 737 P.2d 796, 800 (Alaska 1987). Similarly, the Nevada Supreme Court has also declined to follow the traditional rule giving great weight to the statutory constructions of the state's agencies. While noting that deference may be proper when the agency's construction is "persuasive,"[7] the Nevada Supreme Court has held that a court "may properly undertake independent review of the administrative construction of a statute." ***Nevada Employment Sec. Dep't v. Capri Resorts, Inc.,*** 104 Nev. 527, 528,763 P.2d 50, 51 (1988) (per curiam) (citations omitted). Oregon merely gives agency interpretations "some weight"[8] or "some consideration." ***McPherson v. Employment Div., 285*** Or. 541,591 P.2d 1381 (1979). Even this-limited amount of deference, however, is only given to the extent the statutory term is technical and the agency's expertise involves a peculiar knowledge of a given field. An agency's mere administration over a "specialized program does not mean that its political head or changing personnel either need or acquire expertise." ***McPherson, 285*** Or. at 549, 591 P.2d at 1386.

¶15 In the court's view, when an agency is merely construing a statute, the question of whether judicial deference to the agency's interpretation is appropriate and, if so, the extent of such deference, depends upon a number of factors. See, e.g., ***Yamaha Corp. of America v. State Bd. of Equalization,*** 19 Cal.4th 1, 11-12, 78 Cal.Rptr. 2d. 1, 7 (1998). First, an agency's interpretation of a statute does not cover the same weight, and is not reviewed under the same standard, as a quasi-legislative delegation. Id. Had the Secretary of Finance issued formal regulations determining the circumstances

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[7] *See, e.g., State v. Morros,* 104 *Nev. 709.* 713, *766* P.2d *263, 266* (1988) *(per* **curiam);** *Nevada Power Co. v. Public Serv. Comm'n, 102 Nev.* 1, 4, 7 11 P.2d 867,869 (1986) **(per curiam).**

[8] *Zollinger v. Warner, 286 Or. 19.593* P.2d **1107 (1979).**

under which particular items are "used" **in,** let us say, the manufacturing process, and the regulations had been challenged in **the** refund process, then the proper scope of this court's review would be limited. ***E.g., Commonwealth*** v. ***Dado***, Crim. **No. 98-0261 (Written** Decision Following Trial) at 10 ("'The court may not . . . substitute its own construction of a statutory provision for a reasonable interpretation made by administrator of an agency, and will defer to the agency's construction of its governing statutes unless it is unreasonable") citing ***Chevron*** U.S.A., 467 U.S. 837, 843-844, 104 S.Ct.2778, 2781-2782, 81 **L.Ed.2d** 694 (1984)).

716 Regulations interpreting the statute, however, are not before the court. Instead of adopting a formal regulation, the Secretary and **her** staff have simply reconsidered the facts underlying the Plaintiff's particular transactions, reinterpreted the statute as they deemed applicable, arrived at certain conclusions as to Plaintiff's entitlement to a rebate, and denied the refund accordingly. The distinction is critical. Unlike formally promulgated regulations, an agency's interpretation of a statute does not implicate the **exercise** of a delegated lawmaking power. **Instead,** it represents the agency's view of the statute's legal meaning and effect: questions lying within the constitutional domain of the courts. Yet because an agency often interprets a statute within its administrative jurisdiction, it may possess special familiarity with satellite legal and regulatory issues. It is this "expertise," expressed as an interpretation (whether in a regulation or less formally, as in the case of the Secretary's letter rulings), that is the source of the presumptive value of the agency's **views. See, e.g.,** ***Syncor*** **Intern.** ***Corp. v. Shalala, 127*** F.3d 90, 94-95 **(D.C.Cir. *1997); Bond v. United States, 872*** F.2d **898, 901** (9" Cir. 1989); ***Yamaha Corp. of America, 78*** Cal.Rptr.2d at 11.

¶17 The Department of Finance's interpretation of the rebate statute in this case, however, is only the agency's legal opinion. Because it does not represent the exercise of a delegated legislative power to make law, it commands a commensurably lesser degree of judicial deference. ***Syncor*** Intern. Corp., ***127*** F.3d at ***94-95; Bond v. United States, 872*** F.2d at 901; ***Yamaha Corp. of America, 78*** Cal.Rptr.2d at 11. **Thus,** in determining what, if any, weight to give to an agency's interpretation of a statute it is charged with enforcing, the court looks first at factors that "assume the agency has expertise and technical knowledge, especially where the legal text to be interpreted is technical, obscure, complex, open-ended, or entwined with issues of fact, policy, and discretion. A court is

more likely to defer to an agency's interpretation of its own regulation than to its interpretation of a statute, since the agency is likely to be intimately familiar with regulations it authored and sensitive to the practical implications of one interpretation over another." *Yamaha* Corp. ,19 Cal. 4th at 12; see *also* ***Central Arizona Water Conservation District v. United States Environmental Protection Agency,*** 990 F.2d 1531, 1540 (9th Cir. 1993). The second group of factors weighing in the court's determination are those which suggest to the court that the agency's interpretation is likely to be correct: indications of careful consideration by senior agency officials ("an interpretation of a statute contained in a regulation adopted after public notice and comment is more deserving of deference than [one] contained in an advice letter prepared by a single staff member");[9] evidence that the agency has consistently maintained the interpretation in question, especially if it is long-standing, and indications that the agency's interpretation was contemporaneous with legislative enactment of the statute being interpreted. *Id.* at 12-14. See ***also J.R. Simplot Co., Inc. v. Idaho State Tax Com'n, 820*** P.2d 1206 (Idaho 1991).

¶18 Where, as here, an agency suddenly and inexplicably reverses a prior policy or statutory determination and fails to provide even a rudimentary explanation for its about-face, its most recent expression is entitled to virtually no deference at all. ***See Thomas Jefferson Univ. v. Shalala,*** 512 U.S. 504, 114 S.Ct. 2381, 129 L.Ed.2d ***405 (1994); INS v.*** *Cardoza-Fonseca,* ***480*** U.S. 421, 446 n. 30, 107 S.Ct. 1207, 1221 n. 30, 94 L.Ed.2d 434 (1987).[10] While an agency's initial interpretation of a statute is not instantly carved in stone, basic principles of administrative law require an agency to cogently explain why it has exercised its discretion in a given manner. ***E.g., Atchison, T & S.F.R. Co. v. Wichita Bd. of Trade,*** 412 U.S. 800, 806, 93 S.Ct. 2367, 2374, 37 L.Ed.2d 350 (1973); FTC ***v. Sperry & Hutchinson Co., 405*** U.S. 233,249, 92 S.Ct. 898, 907, 31 L.Ed.2d 170 (1972); ***NLRB v. Metropolitan Ins.*** Co., 380 U.S. 438, 443, 85 S.Ct. 1061, 1064, 13 L.Ed.2d 951 (1965). Sudden

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[9] ***Yamaha Corp., 19*** Cal.4th at 12.

[10] See *also* Davis *v. United States*, 50 Fed.Cl. *192. 204-205* (Fed. Cl. 200 1) (changes that are sudden and unexplained or that do not account for reliance on the agency's prior interpretation should give a court pause before it decides to defer to an agency's decision relying on that interpretation); *Henning* v. *Industrial* Welfare *Comm 'n,* 46 Cal.3d 1262, 252 Cal.Rptr. 278 (1988) (noncontemporaneous statutory interpretation contradicting agency's prior position cannot command significant judicial deference).

and unexplained change, on the other hand, or change that does not take into account the legitimate reliance upon a prior interpretation may qualify as arbitrary or capricious agency action or constitute an abuse of discretion. See ***Smiley v. Citibank (South Dakota),*** 517 U.S. 735, 742, 116 S.Ct. 1730, 135 L.Ed.2d 25 (1996). Thus, where, as here, an agency suddenly and inexplicably reverses its interpretation of a statute, the agency must show not only that its new policy is reasonable, but also that its departure from prior practice is equally reasonable. ***See Motor Vehicles Mfrs. Ass 'n of the United States*** v. ***State Farm Mut. Auto ins. Co.,*** 463 U.S. 29, 42, 103 S.Ct. 2856, 2866, 77 L.Ed.2d 443 (1983) (overturning an agency reversal because the agency had provided no explanation for its change in policy); ***Public Lands Council*** v. ***Babbit,*** 167 F.3d 1287, 1306 (10th Cir. 1999) (changes that are sudden and unexplained or that do not account for reliance on the agency's prior interpretation should give a court pause before it decides to defer to an agency's decision relying on that interpretation).[11]

¶19 In the instant case, the Department of Finance offers no explanation, let alone any "reasoned analysis" to support its sudden change in position. Although the language of the statute has remained the same, the Commonwealth makes no findings to justify its new interpretation of the statutory language and proffers no indication of the basis on which the Department of Finance has exercised *its* discretion.[12] Under these circumstances, the court will not "supply a reasoned basis for the agency's action that the agency itself has not given. " ***SEC v. Chenery Corp., 332*** U.S. 194, 196, 67 S.Ct. 1575, 1577, 91 L.Ed. 1995 (1947). Further, the court will not defer to the Department of Finance's construction of the rebate statute because it is inconsistent and at odds with what the parties apparently agree is the clear intent of the statute.

¶20 Contrary to the Commonwealth's current position, the court draws a distinction between

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[11] *Cf. Greater Boston Television Corporation v. FCC, 444* F.2d *841,852* (D.C.Cir.1970), cert. *denied, 403* U.S. 923, 91 S.Ct. 2233, 29 L.Ed.2d 701 (1971) ("An agency's view of what is in the public interest may change, eitherwith or without a change in circumstances. But an agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed. not casually ignored....") (citations omitted).

[12] "Expert discretion is the lifeblood of the administrative process. but 'unless we make the requirements for administrative action strict and demanding, expertise, the strength of modem government, can become a monster which rules with no practical limits on its discretion. " *Motor Vehicles Mfrs. Ass'n of the United States,* 463 U.S.at 42, 103 S.Ct. at 2866, quoting *New York v. United States,* 342 U.S. 882, 884 [72 S.Ct. 152, 153, 96 L.Ed. 662 (dissenting opinion) (footnote omitted).

simply affixing a logo to an article of clothing and transforming paper, by the addition of words and images, into a greeting card or newspaper. While Plaintiff and the printer of a greeting card may "use" similar printing techniques and technology, the end products are dramatically different. When a newspaper or a greeting card is printed, paper and ink are fundamentally transformed into a device for the communication and storage of information, opinions, and advertising. Plaintiffs printing process, on the other hand, simply converts an undecorated garment into a decorated garment, without any change in "use" at all. In light of what both parties apparently agree is the principal purposes prompting the statutory refund provision, that is, to kindle investment and economic development in the Commonwealth, the court finds no basis on which it can conclude that the Secretary's sudden and abrupt change in position is anything other than arbitrary and capricious. The court therefore declines to rule that any change in the appearance of an object exported into the Commonwealth for resale elsewhere, no matter how minor, constitutes a taxable "use."

CONCLUSION

¶21 A t-shirt, even after Plaintiff affixes its designs, remains a t-shirt. In the court's opinion, the critical issue is whether the whole is different than the sum of its parts. Since Plaintiffs combination of ink or paint and apparel does not transform the apparel into something that is "used" in the Commonwealth, the exemption applies. Accordingly, the court hereby enters partial summary judgment in favor of Plaintiff and against Defendant on Plaintiff's First, Second, and Third Claims for declaratory and injunctive relief.

Dated this 29 day of November, 2001.

TIMOTHY H. BELLAS, Associate Judge Pro Tempore