THE STATE OF SOUTH CAROLINA
In The Supreme Court

RECEIVED
May 04 2023
S.C. SUPREME COURT

APPEAL FROM LEXINGTON COUNTY
Court of Common Pleas

William P. Keesley, Circuit Court Judge

CASE NO. 2021-CP-32-02753
Appellate Case No. 2023-000318

KCI USA, Inc., ... Respondent,

v.

South Carolina Department of Revenue, ... Appellant.

SOUTH CAROLINA DEPARTMENT OF REVENUE'S INITIAL BRIEF

Marcus D. Antley, III, Esquire (Bar No. 102176)
Associate Counsel
Jason P. Luther, Esquire (Bar No. 78021)
Chief Legal Officer
300A Outlet Pointe Boulevard
Columbia, SC 29210
Phone: 803-898-5623
Fax: 803-896-0171
Marcus.Antley@dor.sc.gov
courtorders@dor.sc.gov

Attorneys for the South Carolina Department of Revenue

Columbia, South Carolina
May 4, 2023

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Rules

STATEMENT OF ISSUES ON APPEAL

I. DID THE CIRCUIT COURT ERR BY FINDING RESPONDENT OVERCAME THE PRESUMPTION THAT THE DURABLE MEDICAL EQUIPMENT EXEMPTION IS CONSTITUTIONAL?

II. DID THE CIRCUIT COURT ERR BY SEVERING THE "PRINCIPAL PLACE OF BUSINESS" ELEMENT AND EXPANDING THE DURABLE MEDICAL EXEMPTION INSTEAD OF DECLARING THE ENTIRE DURABLE MEDICAL EQUIPMENT EXEMPTION VOID?

STATEMENT OF THE CASE

This matter came before the Circuit Court in accordance with the Revenue Procedures Act, S.C. Code Ann. § 12-60-80(B) (2014). The Department denied KCI USA, Inc.'s (Respondent) request for a refund of sales tax paid for durable medical equipment. *See* Department Determination (issued July 22, 2021) (**R. pp. ----**). Respondent filed a Complaint with the Circuit Court on August 20, 2021, in case number 2021-CP-32-02753 to request "[t]hat the Court declare unconstitutional that portion of S.C. Code Ann. § 12-36-2120(74)(c) (2014), as it requires that a provider must have its principal place of business in South Carolina in order to be eligible for the sales tax exemption on durable medical equipment and grant Respondent's refund claim." *See* Complaint (**R. pp. ----**). On September 21, 2021, the Department filed its Answer. *See* Answer (**R. pp. ----**).

The Department and Respondent stipulated to the operative facts and filed cross-motions for summary judgment, responses in opposition, and replies. *See* Department's Motion for Summary Judgment and Memo in Support (filed July 8, 2022) (**R. pp. ----**); Department's Response in Opposition (filed August 1, 2022) (**R. pp. ----**); Department's Reply (filed November 1, 2022) (**R. pp. ----**); Respondent's Motion for Summary Judgment (filed July 8, 2022) (**R. pp. ----**); Respondent's Response in Opposition (filed August 1, 2022) (**R. pp. ----**); Respondent's Reply to Department's Responses to Respondent's Motion for Summary Judgment (filed October 28, 2022) (**R. pp. -----**). The Circuit Court heard the cross-motions for summary judgment on November 2, 2022. The Circuit Court denied the Department's motion for summary judgment and granted Respondent's motion for summary judgment. *See* Order (filed February 2, 2023) (**R. pp. -----**). The Department appealed the Order on March 2, 2023.

STANDARD OF REVIEW

"When reviewing a grant of summary judgment, this Court applies the same standard applied by the circuit court pursuant to Rule 56(c), SCRCP." *Azar v. City of Columbia*, 414 S.C. 307, 310, 778 S.E.2d 315, 316 (2015). Summary judgment is proper when there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. *Young v. S.C. Dep't of Disabilities & Special Needs*, 374 S.C. 360, 649 S.E.2d 488 (2007); *Henderson v. Allied Signal, Inc.*, 373 S.C. 179, 644 S.E.2d 724 (2007); *Pittman v. Grand Strand Entm't, Inc.*, 363 S.C. 531, 611 S.E.2d 922 (2005); *Eagle Container Co., LLC v. County of Newberry*, 366 S.C. 611, 622 S.E.2d 733 (Ct. App. 2005); and *B & B Liquors, Inc. v. O'Neil*, 361 S.C. 267, 603 S.E.2d 629 (Ct. App. 2004). "This Court has a limited scope of review in cases involving a constitutional challenge to a statute because all statutes are presumed constitutional and, if possible, will be construed to render them valid." *Retail Servs. & Sys., Inc. v. S.C. Dep't of Revenue*, 419 S.C. 469, 472, 799 S.E.2d 665, 666 (2017).

FACTS

The relevant facts in this appeal are undisputed and were stipulated at the trial level. *See* Stipulation of Facts (**R. pp. ----**). Respondent is a Delaware corporation with its principal place of business in Texas. Respondent sells durable medical equipment and related supplies in South Carolina. Respondent remitted South Carolina sales tax to the Department on durable medical equipment and related supplies sales to customers in South Carolina. Respondent submitted refund claims, totaling $564,611.71 for sales tax paid on durable medical equipment and related supplies sold to customers in South Carolina during the period of October 1, 2014 through September 30, 2017. The Department denied the refund claims on May 5, 2020. Respondent filed a timely protest, and after exhausting its pre-hearing administrative remedies filed a request for a contested case hearing with the

Administrative Law Court on August 20, 2021. On the same date, Respondent also filed an action for Declaratory Judgment in the Lexington County Court of Common Pleas.

ARGUMENTS

Under South Carolina law, a sales tax of six percent of "the gross proceeds of sales, is imposed upon every person[1] engaged or continuing within this State in the business of selling tangible personal property at retail." S.C. Code Ann. §§ 12-36-910(A) and 12-36-1110 (2014). Respondent does not dispute that retail sales of durable medical equipment and related supplies are subject to sales tax in South Carolina. *See* Stipulation of Facts (**R. pp. ----**). The South Carolina Supreme Court has long upheld the constitutionality of the sales and use tax. *See Int'l Harvester Co. v. Wasson*, 281 S.C. 458, 316 S.E.2d 378 (1984). Respondent admits it is not challenging the sales tax. Hrg. Tr. 4:10-11 (**R. p. ----**).

S.C. Code Ann. § 12-36-2120(74) (2014) grants a sales tax exemption for durable medical equipment. Specifically, § 12-36-2120(74) provides:

> Exempted from the taxes imposed by this chapter are the gross proceeds of sales, or sales price of:
>
> ***
>
> (74) durable medical equipment and related supplies:
> (a) as defined under federal and state Medicaid and Medicare laws;
> (b) which is paid directly by funds of this State or the United States under the Medicaid or Medicare programs, where state or federal law or regulation authorizing the payment prohibits the payment of the sale or use tax; and
> (c) sold by a provider who holds a South Carolina retail sales license and **whose principal place of business is located in this State** (emphasis added).

---

[1]For sales and use tax purposes, the term person "includes any individual, firm, partnership, limited liability company, association, corporation, receiver, trustee, any group or combination acting as a unit, the State, any state agency, any instrumentality, authority, political subdivision, or municipality." S.C. Code Ann. § 12-36-30 (2014).

Undisputedly, Respondent's principal place of business is not located in South Carolina.[2] Therefore, Respondent does not qualify for the durable medical equipment exemption (DME Exemption) under the plain language of the statute. Without the DME Exemption, Respondent does not dispute that it is otherwise subject to sales tax in South Carolina for the durable medical equipment.

I. THE CIRCUIT COURT ERRED BY FINDING RESPONDENT OVERCAME THE PRESUMPTION THAT THE DURABLE MEDICAL EQUIPMENT EXEMPTION IS CONSTITUTIONAL.

A. Section 12-36-2120(74) is presumed constitutional.

As a fundamental matter, the South Carolina Supreme Court has made clear that statutes are presumed constitutional:

> This Court has a very limited scope of review in cases involving a constitutional challenge to a statute. All statutes are presumed constitutional and will, if possible, be construed so as to render them valid. A legislative act will not be declared unconstitutional unless its repugnance to the constitution is clear and beyond a reasonable doubt. A legislative enactment will be declared unconstitutional only when its invalidity appears so clearly as to leave no room for reasonable doubt that it violates a provision of the constitution.

Joytime Distributors & Amusement Co. v. State, 338 S.C. 634, 640, 528 S.E.2d 647, 650 (1999) (internal citations omitted). "The burden of establishing the unconstitutionality of a statute rests on the party asserting a constitutional violation." *Y. C. Ballenger Electrical Contractors, Inc. v. Reach-All Sales, Inc.*, 276 S.C. 394, 279 S.E.2d 127 (1981); *State v. Byrd*, 267 S.C. 87, 226 S.E.2d 244 (1976). In doing so, Respondent must "negate every conceivable basis" for upholding the law. *Thomson Newspapers v. City of Florence*, 287 S.C. 305, 338 S.E.2d 324 (emphasis added). "The taxpayer bears the burden of proving

[2]The Fourth Circuit recognizes two tests to determine a corporation's principal place of business: the nerve center (where the corporation's officers direct, control, and coordinate its activities) and corporate activities (where the bulk of corporate activities take place). *See Long v. Silver*, 248 F.3d 309, 314 (4th Cir. 2001); *Athena Auto., Inc. v. DiGregorio*, 166 F.3d 288, 290 (4th Cir. 1999); and *Peterson v. Cooley*, 142 F.3d 181, 184 (4th Cir. 1998).

the tax [exemption] is unconstitutional and it must overcome this Court's mandate to sustain a legislative enactment if there is "any reasonable hypothesis to support it." *D.W. Flowe & Sons, Inc. v. Christopher Constr. Co.*, 326 S.C. 17, 482 S.E.2d 558 (1997) as cited in, *Ed Robinson v. South Carolina Department of Revenue*, 588 S.E.2d 97 (October 13, 2003). The burden is upon the taxpayer to prove the unconstitutionality of a tax beyond a reasonable doubt, and it must negate every conceivable basis that might support it. *Sandy Springs Water Co. v. Dep't of Health & Env't Control*, 324 S.C. 177, 181, 478 S.E.2d 60, 62 (1996).[3]

B. Respondent cannot overcome the presumption of constitutionality and negate every conceivable basis to support the DME Exemption beyond a reasonable doubt.

One conceivable basis to support the DME Exemption is that its purpose and effect is to promote economic development. The United States Supreme Court has held "that a State may enact laws pursuant to its police powers that have the purpose and effect of encouraging domestic industry." *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 271 (1984). The Legislature has repeatedly used sales tax exemptions as a means to promote economic development. *See* S.C. Code Ann. § 12-36-2120(51) (2014) (sales tax exemption for material handling systems and material handling equipment used in the operation of a distribution facility or a manufacturing facility if the taxpayer invests "thirty-five millions dollars in real or personal property in this State... "); S.C. Code Ann. § 12-36-2120(64) (2014) (sales tax exemption for "sweetgrass baskets made by artists of South Carolina using locally grown sweetgrass"); S.C. Code Ann. § 12-36-2120(65) (2014) (sales tax exemption for computer equipment if "the taxpayer invests at least three hundred million dollars in real or personal property or both" in this State); S.C. Code Ann. § 12-36-2120(67) (2014) (sales tax exemption for "construction

[3]Respondent admits it has the burden to establish that the statute is discriminatory. Hrg. Tr. 11:22-12:2 (**R. pp. ----**).

materials used in the construction of a new or expanded single manufacturing or distribution facility, or one that serves both purposes, with a capital investment of at least one hundred million dollars in real and personal property at a single site in the State"); S.C. Code Ann. § 12-36-2120(72) (2014) (sales tax exemption for "building materials used to construct a new or renovated building or any machinery or equipment located in a research district"); and S.C. Code Ann. § 12-36-2691 (2014) (effectively five-year sales and use tax exemption for a person if it has a distribution facility and invests at least $125 million and maintains 1,500 full-time jobs in the State).

C. The DME Exemption is no different than numerous other economic development statutes, all of which are also presumptively constitutional.

Under Respondent's logic, all economic development exemptions would be unconstitutional. For example, an artist of Texas who uses locally grown sweetgrass is ineligible for the sales tax exemption offered to artists of South Carolina. *See* § 12-36-2120(64). As another example, the numerous sales tax exemptions for equipment and construction materials contingent on the taxpayer investing in real or personal property in the State would "force" taxpayers to give up the right to do business solely in interstate commerce. *See* §§ 12-36-2120(51), (65), (67), and (72). A third example is found in § 12-36-2691, which effectively provides a five-year sales and use tax exemption for a taxpayer if it has a distribution facility and invests at least $125 million and maintains 1,500 full-time jobs in the State. The Code is replete with tax exemptions that would be subject to the same constitutional challenge if the Court adopts Respondent's position. These tax exemptions go beyond those applicable to sales and use tax and would extend to other taxes like the motor fuel user fee credit, which only benefits South Carolina income tax filers. The consequences of finding the DME Exemption unconstitutional would be extensive.

D. There are other conceivable bases to support the DME Exemption.

Still, economic development is only one basis to support the DME Exemption. Another basis could be to shorten the supply chain to ensure South Carolina's most vulnerable populations have access to durable medical equipment. Perhaps, the Legislature had the foresight to pre-empt potential supply shortages like those experienced during the COVID-19 pandemic. Regardless, Respondent must prove beyond a reasonable doubt— the same burden of proof that the State must carry to convict a person of a capital crime— that no conceivable basis exists to support the statute. South Carolina currently has eighty-three (83) sales and use tax exemptions, not including effective exemptions like § 12-36-2691. Notably, Respondent cited no sales tax exemption declared to be in violation of the Commerce Clause.

II. THE CIRCUIT COURT ERRED BY SEVERING THE "PRINCIPAL PLACE OF BUSINESS" ELEMENT AND EXPANDING THE DURABLE MEDICAL EXEMPTION INSTEAD OF DECLARING THE ENTIRE DURABLE MEDICAL EQUIPMENT EXEMPTION VOID.

A. The "principal place of business" element is not severable.

If § 12-36-2120(74) is unconstitutional, the Court should declare the entire exemption void. "The test for severability is whether the constitutional portion of the statute remains complete in itself, wholly independent of that which is rejected, and is of such a character that it may fairly be presumed the legislature would have passed it independent of that which conflicts with the constitution." *Joytime Distributors & Amusement Co. v. State*, 338 S.C. 634, 648–49, 528 S.E.2d 647, 654 (1999) (internal citations omitted). Here, the nature of the exemption, along with general principles related to the interpretation and application of tax statutes in South Carolina, demonstrate that the principal place of business element of the DME Exemption is not severable.

B. The Legislature would not have passed the DME Exemption without the "principal place of business" element.

As a starting point to determining the Legislature's intent, South Carolina law presumes that the sale of tangible personal property is subject to a sales tax. South Carolina imposes sales tax on the "gross proceeds of sales" of "every person engaged or continuing within [South Carolina] in the business of selling tangible personal property at retail." S.C. Code Ann. § 12-36-910 (2014). Exemptions are the exception; not the rule. Taxpayers bear the burden of bringing themselves squarely within the parameters of the statute which grants the exemption. *See Owen Indus. Prods., Inc. v. Sharpe*, 274 S.C. 193, 262 S.E.2d 33 (1980); *S. Soya Corp. of Cameron v. Wasson*, 252 S.C. 484, 167 S.E.2d 311 (1969); and *S. Weaving Co. v. Query*, 206 S.C. 307, 34 S.E.2d 51 (1945). Exemption statutes are construed strictly against the taxpayer. *Home Medical Systems, Inc. v. S.C. Dep't of Rev.*, 382 S.C. 556, 564, 677 S.E.2d 582, 587 (2009) ("The language of a tax exemption statute must be given its plain, ordinary meaning and must be strictly construed against the claimed exemption."). Moreover, the "refund of taxes is solely a matter of governmental grace," and any party seeking such must bring itself squarely within the authorizing statute. *Asmer v. Livingston*, 225 S.C. 341, 82 S.E.2d 465 (1954).

Here, by including the principal place of business requirement, the Legislature signaled its intent to limit the exemption only to certain taxpayers, rather than granting the exemption to any taxpayer who sells durable medical equipment. Because sales tax exemptions are a matter of legislative grace as an exception to the general rule of taxability, it cannot be fairly presumed that the Legislature would have passed the DME Exemption independent of a principal place of business limitation. Clearly the Legislature did not intend for taxpayers like Respondent to get the exemption. Thus, the allegedly offending provision of § 12-36-2120(74)(c)— i.e. the principal place of business element— is not severable.

C. This Court has denied similar requests to expand sales tax exemptions.

In *Thayer v. South Carolina Tax Com'n*, our Supreme Court considered a sales and use tax exemption granted to "religious publications, including the Holy Bible."[4] 307 S.C. 6, 413 S.E.2d 810 (1992). The Court held that the exemption violated both the Free Press Clause and Establishment Clause of the United States Constitution. The Court found that the religious publication exemption was severable because "the remaining exemptions are complete in themselves and that the legislature would have passed the remaining exemptions independently." *Id.* at 13, 413 S.E.2d at 815. The exemption at issue in *Thayer* included a number of different categories of items, including newsprint papers, newspapers, and religious publications (including the Bible and the Department of Agriculture's The Market Bulletin). Each of these categories is unrelated and have very little in common, so it is reasonable to think that even if one category of items were severed from the exemption the Legislature would still have exempted the remaining categories.

Here, the DME Exemption is incomplete without the "principal base of business" element, and the Legislature would not have passed the exemption without this element. The DME Exemption applies to a single category of items, but only in limited circumstances if certain restrictive elements are met. One of those elements explicitly excludes taxpayers like Respondent from receiving the DME Exemption. It is unreasonable to assume the Legislature would have granted such a broad exemption if one of those limiting elements were severed. In fact, prior to July 1, 2007, no taxpayer received a South Carolina sales tax exemption for durable medical equipment. Even after its effective date, the Legislature slowly phased in the DME Exemption. Presumably, this would allow the Legislature to monitor the fiscal impact of the exemption. Contrary to the Legislature's methodical approach,

---

[4]S.C. Code Ann. § 12-35-550(7) (1976) is essentially the same exemption that was later recodified as S.C. Code Ann. § 12-36-2120(8) (2014).

severing the "principal place of business" element would immediately expand the exemption and make the State subject to refund claims from taxpayers seeking retroactive relief. Therefore, it cannot be fairly presumed that the Legislature would have passed the statute without the "principal place of business element." On the other hand, the DME Exemption can be severed from the remaining exemptions. The DME Exemption was passed independently from the exemptions provided in the other subsections. Therefore, the entire DME Exemption should fail if unconstitutional, but the remaining sales and use tax exemptions stand.

D. Respondent is not entitled to the DME Exemption.

Respondent and similarly situated taxpayers were not entitled to an exemption in the past; nor are they entitled to an exemption if the Court severs the durable medical equipment exemption. *See id.* at 14, 413 S.E.2d at 815. The Court "cannot create an exemption by reading something into the statute which the Legislature did not intend." *Id.* Also as in *Thayer*, the result should be prospective if the Court declares the DME Exemption void. Like the taxpayer in *Thayer*, Respondent claims its prior sales tax assessments (for durable medical equipment) must be forgiven and points to *McKesson Corp. v. Div. of Alcoholic Beverages & Tobacco, Dep't of Bus. Regul. of Fla.*, 496 U.S. 18, 18, 110 S.Ct. 2238, 2240, 110 L.Ed.2d 17 (1990). Even if Respondent were granted relief under *McKesson*, "[t]he State is free to choose which form of relief it will provide, so long as that relief satisfies the minimum federal requirements." *Id.* at 51–52. In other words, the Department decides whether to provide a refund to Respondent, assess taxpayers who received the exemption, or some combination of refunds and assessments.

However, "*McKesson* requires relief as a matter of federal law only when taxpayers involuntarily pay a tax that is unconstitutional under existing precedents." *Id.* at 13, 413 S.E.2d at

815. The Court in *Thayer* held that *McKesson* must be read in conjunction with its companion case *American Trucking*. Importantly, the United States Supreme Court in *American Trucking* held:

> In light of *McKesson* 's holding that a ruling that a tax is unconstitutionally discriminatory under the Commerce Clause places substantial obligations on the States to provide relief, the threshold determination whether a new decision should apply retroactively is a crucial one, requiring a hard look at whether retroactive application would be unjust.

Am. Trucking Associations, Inc. v. Smith, 496 U.S. 167, 181, 110 S.Ct. 2323, 2333, 110 L.Ed.2d 148 (1990). Here, Respondent offers no authority directly on point that the DME Exemption was unconstitutional when the Legislature passed it over fifteen years ago. As discussed above, the Legislature has passed multiple statutes before and after the DME Exemption that would fail to meet constitutional muster under Respondent's theory. Initially, Respondent did not even challenge the constitutionality of the DME Exemption and is only now seeking a refund after having paid the tax for at least three years without protest. Therefore, the proper remedy would be to sever the entire DME Exemption prospectively and deny Respondent's request for a retroactive exemption for which it has never qualified.

CONCLUSION

For the reasons stated above, this Court should reverse the Circuit Court's decision because the Respondent failed to overcome the presumption that the DME Exemption is constitutional and even if unconstitutional, the whole exemption must be declared void. Therefore, Respondent is not entitled to the DME Exemption.

{Signature on following page}

Respectfully Submitted,

Marcus D. Antley, III, Esquire (Bar No. 102176)
Associate Counsel
Jason P. Luther, Esquire (Bar No. 78021)
Chief Legal Officer
300A Outlet Pointe Boulevard
Columbia, SC 29210
Phone: 803-898-5623
Fax: 803-896-0171
Marcus.Antley@dor.sc.gov
courtorders@dor.sc.gov

Attorneys for Appellant
South Carolina Department of Revenue

Columbia, South Carolina
May 4, 2023