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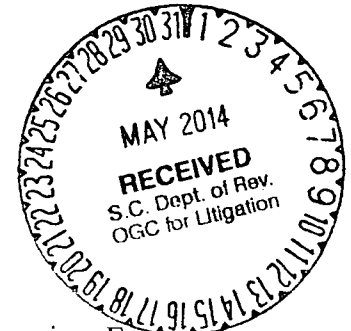
**STATE OF SOUTH CAROLINA
ADMINISTRATIVE LAW COURT**

SC ADMIN. LAW COURT

Southeast Cinema Entertainment, Inc.,)
)
Petitioner,)
)
v.)
)
South Carolina Department of Revenue,)
)
Respondent.)

Docket No.: 12-ALJ-17-0390-CC

ORDER



APPEARANCES: Petitioner: Jeffrey T. Allen, Esquire, and Erik P. Doerring, Esquire
Respondent: Adam N. Marinelli, Esquire

STATEMENT OF THE CASE

This matter is before the South Carolina Administrative Law Court (“the ALC” or “the Court”) pursuant to a Request for a Contested Case Hearing filed by Southeast Cinema Entertainment, Inc. (“Petitioner”) challenging the South Carolina Department of Revenue’s (“Respondent’s” or “the Department’s”) denial of a refund request for sales tax paid on the purchase of cinema equipment from IMAX Corporation (“IMAX”). Petitioner owns and operates a movie theatre business located in Charleston, South Carolina. On or about September 30, 2008, Petitioner entered into an agreement (“the Agreement”) to purchase an IMAX theatre system (“the system”) from IMAX for \$1.15 million. IMAX, which has a nexus with the State of South Carolina,¹ charged Petitioner sales tax on the purchase price of the system and on related “additional payments.”

Petitioner obtained an assignment of rights from IMAX, and submitted a request to the Department for a refund of part of the sales taxes it paid on the purchase of the system. Specifically, Petitioner submitted an ST-14 form requesting a refund totaling \$71,000.57, alleging most of the purchase price of the system reflected the value of un-taxable, intangible property. The Department denied the request by letter dated September 2, 2011, and Petitioner

¹ The “Commerce Clause nexus, for sales and use tax purposes, requires some physical presence within the taxing jurisdiction.” Travelscape, LLC v. S.C. Dep't of Revenue, 391 S.C. 89, 104, 705 S.E.2d 28, 36 (2011).

timely contested the Department's denial on November 3, 2011. On August 2, 2012, the Department upheld its denial, finding the full purchase price of the system was subject to South Carolina sales tax. Petitioner then appealed to this Court. Petitioner and the Department subsequently filed Cross Motions for Summary Judgment, and this Court held a hearing on those Motions on December 13, 2013.

FACTS

The Agreement is entitled "Agreement for the Purchase and Sale and Maintenance of IMAX® Digital MPX Projection System and Trademark License." Pursuant to the Agreement, IMAX had a duty to: (1) sell to Petitioner a large format digital projection system and provide certain related services; (2) provide maintenance services for a large format digital projection system;² and (3) license to Petitioner certain IMAX trademarks. The Agreement describes IMAX as being "in the business of developing, selling and leasing large format projection systems and providing certain related services." The Agreement states the sale was solely for the purchase of the system. It further states the purchase price for the system was \$1,150,000.00,³ which included the first year's maintenance fee of \$40,000.⁴ The purchase price was split into installment payments, but the parties did not indicate whether, for example, \$500,000 was for the purchase of the projector and \$610,000 was for the purchase of the sound system.⁵

The Agreement also required Petitioner to make "additional payments" to IMAX in arrears on a monthly basis. These "additional payments" were equal to \$40,000 (annually) or a percentage of theater admission proceeds, whichever was greater.

Petitioner, after conducting its own market research, determined that the material components of the system, if purchased from a vendor other than IMAX, would have a retail value of approximately \$170,694.33. Based on this valuation of the material components, Petitioner requested the Department refund the portion of the sales tax it paid on the purchase

² The "system," as defined by the Agreement, includes the projection system, the sound system, the screen, and a 3D glasses cleaning machine.

³ Specifically, the Agreement states: "Subject to the terms and conditions contained herein, IMAX hereby sells to Client and Client hereby purchases from IMAXC the System," and "[Petitioner] shall pay US\$1,150,000 as purchase price for the system (the "Purchase Price"), which shall be payable as IMAX directs."

⁴ The parties did not contest the inclusion of the maintenance fee as part of the purchase price.

⁵ The purchase price was paid in installments; however, the installments were not structured in a way to reflect the purchase of different components of the IMAX system or the related services or benefits.

price of the system that was in excess of \$170,694.33. Petitioner claimed the remainder of the purchase price after subtracting the value of the material parts related to intangible and un-taxable benefits associated with the purchase of the IMAX trademark license.

ISSUES

- I. **Whether Petitioner is entitled to a refund of a portion of the sales taxes it paid on the initial purchase of the system.**
- II. **Whether Petitioner is entitled to a refund of sales taxes it paid on “additional payments” related to the purchase of the system.**

CONCLUSIONS OF LAW

Based upon the submitted briefs, oral arguments presented, and a thorough examination of the applicable statutes and jurisprudence, I conclude the following as a matter of law:

This Court has jurisdiction to hear this contested case pursuant to section 1-23-600 of the South Carolina Code (Supp. 2013). Generally, the party asserting the affirmative issue in an adjudicatory administrative proceeding has the burden of proof. See Leventis v. S.C. Dep't of Health & Env'tl. Control, 340 S.C. 118, 133, 530 S.E.2d 643, 651 (Ct. App. 2000) (citing 2 Am.Jur.2d *Administrative Law* § 360 (1994)). Here, Petitioner requested a contested case hearing and, therefore, has the burden of proof to show by a preponderance of the evidence that the Department's tax assessment was incorrect. See id.; Anonymous (M-156-90) v. State Bd. of Med. Examiners, 329 S.C. 371, 375, 496 S.E.2d 17, 19 (1998) (holding the standard of proof in “administrative hearings is generally a preponderance of the evidence”).

This Court's Rules of Procedure provide “[t]he South Carolina Rules of Civil Procedure . . . may, in the discretion of the presiding administrative law judge, be applied to resolve questions not addressed by these rules.” ALC Rule 68. Rule 56(c) of the South Carolina Rules of Civil Procedure provides summary judgment is properly granted when the “pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that any party is entitled to a judgment as a matter of law.” See Bovain v. Canal Ins., 383 S.C. 100, 105, 678 S.E.2d 422, 424 (2009). In determining whether summary judgment is proper, this Court must construe all ambiguities, conclusions, and inferences arising from the evidence against the moving party. See Byers v. Westinghouse Elec. Corp., 310 S.C. 5, 7, 425 S.E.2d 23, 24 (1992). Although the evidence and inferences drawn therefrom generally must be construed against the moving party, “the nonmoving party may not rest upon the mere allegations or denials of the pleadings, but a

response by affidavit or otherwise . . . must set forth specific facts creating a genuine issue for trial.” Rule 56(e), SCRCF.

“If a statute's language is plain, unambiguous, and conveys a clear meaning ‘the rules of statutory interpretation are not needed and the court has no right to impose another meaning.’” Buist v. Huggins, 367 S.C. 268, 276, 625 S.E.2d 636, 640 (2006) (quoting Hodges v. Rainey, 341 S.C. 79, 85, 533 S.E.2d 578, 581 (2000)). “The words of the statute must be given their plain and ordinary meaning without resorting to subtle or forced construction to limit or expand the statute's operation.” Id. “The cardinal rule of statutory construction is to ascertain and effectuate the intent of the legislature.” Id.

DISCUSSION

I. The taxpayer is not entitled to a refund for sales taxes paid on its initial purchase price for an IMAX theater system.

Section 12-36-910(A) of the South Carolina Code imposes “[a] sales tax, equal to five percent of the *gross proceeds of sales*, [] upon every person engaged or continuing within this State in the business of selling *tangible personal property at retail*.” (emphasis added). “Retailers” are every person “selling or auctioning tangible personal property whether owned by the person or others.” S.C. Code Ann. § 12-36-70(1)(a). Tangible personal property is defined as:

personal property which may be seen, weighed, measured, felt, touched, or which is in any other manner perceptible to the senses. It also includes services and intangibles, including communications, laundry and related services, furnishing of accommodations and sales of electricity, the sale or use of which is subject to tax under this chapter and does not include stocks, notes, bonds, mortgages, or other evidences of debt.

S.C. Code Ann. § 12-36-60. Next, “gross proceeds of sales” means “the value proceeding or accruing from the sale, lease, or rental of tangible personal property.” S.C. Code Ann. § 12-36-90. Furthermore, gross proceeds of sales includes:

(b) the proceeds from the sale of tangible personal property without any deduction for:

- (i) the cost of goods sold;
- (ii) the cost of materials, labor, or service;
- (iii) interest paid;
- (iv) losses;

- (v) transportation costs;
- (vi) manufacturers or importers excise taxes imposed by the United States;
- or
- (vii) any other expenses;

S.C. Code Ann. § 12-36-90(1). Similarly, “sales price” is defined as “the total amount for which tangible personal property is sold, without any deduction for the cost of the property sold, the cost of the materials used, labor or service cost, interest paid, losses, or any other expenses. S.C. Code Ann. § 12-36-130.

These definitions demonstrate the Legislature’s intent to disallow deductions for the retailer’s cost of labor and services and “any other expenses” from the gross proceeds of sales in computing sales tax liability. §§ 12-36-90(1)(b), -130. Additionally, “tangible personal property” includes, to an extent, “intangibles.” Some of the “intangibles” that are taxable are listed in the statute. See § 12-36-60. Notably, all of the listed “intangibles” subject to sales tax appear to be the subject of the retail sale and not incident to the retail sale. See id.

It is generally accepted that the sale of a trademark license is the sale of an intangible. See Media General Communications, Inc. v. South Carolina Department of Revenue, 388 S.C. 138, 141, 694 S.E.2d 525, 526 (2010). In Medial General, the South Carolina Supreme Court addressed an issue related to the Department’s accounting practices and allocation of income taxes. While the case did not deal with sales taxes, part of Media General’s income included payments for the use of its licenses and trademarks. Id. The Supreme Court categorized these as “intangible assets.” Id. Specifically, the court stated “[t]hese intangibles include[e] licenses and other authorizations issued by the Federal Communications Commission (“FCC”) for the operation of various television broadcasting affiliates, as well as trademarks.” Similarly, in Geoffrey, Inc. v. South Carolina Tax Commission, 313 S.C. 15, 19, 437 S.E.2d 13, 16 (1993), another income tax case, the supreme court referred to the licensing of trademarks as an “intangibles.”

In this case, Petitioner contends the purchase price of the system was approximately \$170,694.33 and the remainder of the sales price was payment for the purchase of IMAX’s trademark license, which was intangible property and not subject to sales tax. Accordingly, Petitioner argues the Department only had authority to tax it for the value of the system and not the full purchase price. Conversely, the Department contends section 12-36-130’s admonition

that “any other expenses” cannot be deducted from the price of tangible personal property for the purposes of calculating the sales tax encompasses ancillary purchases like the trademark license. As a result, the Department argues the total amount charged in conjunction with the sale or purchase of tangible personal property is subject to sales tax. This Court agrees with the Department.

In supporting its case, the Department cites to Meyers Arnold, Inc. v. South Carolina Tax Commission, 285 S.C. 303, 305, 328 S.E.2d 920, 922 (Ct. App. 1985). In Myers Arnold, the South Carolina Court of Appeals addressed whether lay away fees associated with a lay away purchase were subject to sales tax. Id. The court of appeals determined:

But for the lay away sales, Meyers Arnold would not receive the lay away fees. The fees are obviously charged for the service rendered in making lay away sales. For these reasons, this court holds the lay away fees are part of the gross proceeds of sales and subject to the sales tax.

Id. at 303, 328 S.E.2d at 923. Thus, the court of appeals found that under the definition of “gross proceeds of sale,” the lay away fee constituted the price for a service incident to the purchase of the layaway item, which was not deductible for the purpose of administering the sales tax. Moreover, in Myers Arnold, the court of appeals also addressed whether the sales tax applied to wrapping paper services, and ultimately held “section 12–35–550(14) of the [South Carolina] Code and Regulation 117–174.154 clearly exempt the proceeds of the sale of gift wrapping paper from the sales tax when the paper is used *incident* to the delivery of tangible personal property”. (emphasis added). It further found, in contrast, Regulation 117–174.238 provides the gross proceeds from charges for gift wrapping not incident to the purchase of tangible personal property are subject to the sales and/or use tax.” Id. at 306, 328 S.E.2d at 922. Therefore, Myers Arnold suggests that service fees or benefits that are incident to the sale of tangible personal property are part of the gross proceeds of sale and subject to sales tax.

Here, I find Petitioner cannot parse the purchase price of the system into its alleged component parts to reduce its tax burden. Although the purchase of a trademark license is generally considered an intangible and un-taxable, Petitioner has not presented this Court with an itemized accounting sheet showing the purchase price of \$1.15 million is the sum of the cost of the system and the cost of the trademark. See Media General Communications, 388 S.C. at 141, 694 S.E.2d at 526; Geoffrey, 313 S.C. at 19, 437 S.E.2d at 16. Nor does the contract itself make a distinction between the cost of the system and the cost of the trademark when setting out the

purchase price. The only parsing of the purchase price is the Agreement's provision allowing for installment payments, which do not reflect any kind of itemization. The plain language of the Agreement states the \$1.15 million purchase price is for the system, which is tangible personal property. See Progressive Max Ins. Co. v. Floating Caps, Inc., 405 S.C. 35, 46, 747 S.E.2d 178, 184 (2013) ("If [the contract's] language is plain, unambiguous, and capable of only one reasonable interpretation, no construction is required and the contract's language determines the instrument's force and effect."). Accordingly, the entire purchase price is subject to sales tax.

Furthermore, the benefit of the trademark is granted only by virtue of purchasing the system. The limited "Trademark License" is conditionally granted to the Petitioner "solely in connection with the naming, marketing, promotion and operation of the Theatre utilizing the system." In addition, the Agreement requires Petitioner to obtain prior approval from the IMAX corporation for use of the IMAX name, IMAX formatted content, software, advertising materials, etc., which can only be used in conjunction with the system. Thus, although a valuable intangible asset, the limited trademark license Petitioner received when it purchased the system is inextricably connected to the purchase of the system.

In sum, because the plain language of the Agreement provided the purchase price was solely for the system, and the alleged intangibles were inextricably linked to the purchase of the system, I find the initial purchase price represents the gross proceeds of sale and is subject to sales tax. See § 12-36-90(1)(b) (disallowing deductions for the retailer's cost of labor and services and "any other expenses" from the gross proceeds of sales in computing sales tax liability); Meyers Arnold, 285 S.C. at 305-06, 328 S.E.2d at 922-23 (suggesting service fees or benefits incident to the purchase of tangible personal property are part of the gross proceeds of sale and subject to sales tax). Moreover, because this is a legal issue, and Petitioner has failed to demonstrate a genuine issue as to any material fact to prevent Respondent from being entitled to judgment as a matter of law regarding the application of sales tax to the full purchase price, I grant Respondent's motion for summary judgment and deny Petitioner's motion for summary judgment as to this issue. See Rule 56(c), SCRCP.

II. The additional monthly installment payments for the system are not subject to sales tax.

Petitioner argued at the hearing that the additional payments equal to the greater of \$40,000.00 or a percent of net admissions proceeds⁶ should not be subject to sales tax. Petitioner contended the additional payments should be characterized as “box office fees,” which are exempt from sales tax pursuant to section 12-36-2120(35) of the South Carolina Code. The Court agrees.

Subsection 35 of section 12-36-2120 specifically exempts from sales taxes “motion picture film sold or rented to or by theaters.” § 12-36-2120(35). Here, the percentage of net admissions proceeds IMAX charges Petitioner is essentially a fee for showing films provided by IMAX, which is a box office fee. A box office fee is no more than a charge for renting film, which is exempt from sales tax under section 12-36-2120(35).

The Department argues the additional payments, because they were established in the Agreement as part of the purchase of the system, are part of the gross proceeds of sale. In support of this assertion, the Department cites the part of the Agreement governing “Film Programming,” which states:

Client shall exhibit all IMAX Approved Content commencing from the earliest date any such content is released for exhibition at the Theatre provided that such content is offered to Client on commercially reasonable terms generally found in the industry.

This section of the Agreement refers to “terms generally found in the industry,” which may or may not relate to the rental price of films. “Terms” can also relate to the number of required showings, the length of a film’s run, etc. Accordingly, this Court finds the Department’s argument unpersuasive. Further, because the Agreement makes it clear the box office fees are separate charges from the purchase price of the system, I find the Department’s argument that

⁶ The Agreement defines the percentage payment referred to here as “three percent (3%) of Net Theatre Admissions for Hollywood Films exhibited at the Theatre plus five percent (5%) of Net Theatre Admissions for all other content exhibited in the Theatre.” “Net Theatre Admissions” means “amounts received by [Petitioner] for admission to the Theatre after deducting amusement or entertainment taxes, admissions or gross receipts taxes, value added taxes, sales taxes or other similar impositions levied on the admissions price by and actually paid by [Petitioner]”

Regulation 117-313.1 prevents Petitioner from arguing the additional payments are not part of the gross proceeds of sale is also unpersuasive.⁷

Accordingly, this Court finds the additional payments are box office fees, which are exempt from sales tax under section 12-36-2120(35). Because this is a legal issue, and Respondent has failed to demonstrate a genuine issue as to any material fact to prevent Petitioner from being entitled to judgment as a matter of law regarding the application of sales tax to the additional payments, I grant Petitioner's motion for summary judgment and deny Respondent's motion for summary judgment as to this issue. See Rule 56(c), SCRPC.

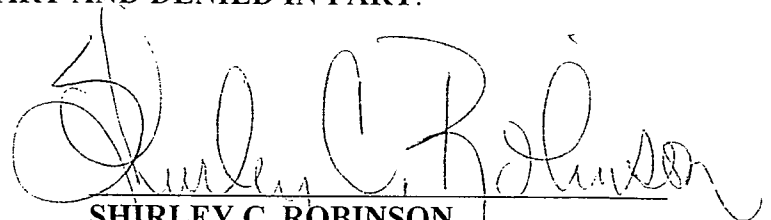
CONCLUSION

South Carolina law imposes a sales tax on the gross proceeds of the sale of tangible personal property. Here, Petitioner paid \$1.15 million to purchase the system, which was tangible personal property. Therefore, the Department properly denied Petitioner's claim for a refund of sales taxes based on its allegation that the value of the system (and therefore gross proceeds of sale) was actually much less than \$1.15 million. However, the Department incorrectly charged sales tax on the "additional payments" Petitioner made pursuant to the Agreement. These "additional payments" were box offices fees, which are exempt from sales tax under section 12-36-2120(35).

THEREFORE, IT IS HEREBY ORDRED that the Petitioner's Motion for Summary Judgment **IS GRANTED IN PART AND DENIED IN PART**, and the Department's Motion for Summary Judgment **IS GRANTED IN PART AND DENIED IN PART**.

AND IT IS SO ORDERED.

Columbia, South Carolina
May 28, 2014


SHIRLEY C. ROBINSON
Administrative Law Judge
Department of Social Services

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This 28 day of May 2014
By: Teekha Henderson
Judge

⁷ Regulation 117-313.1 admonishes that "no method of billing will serve to exempt from the measure of the tax the cost of material used, labor or service cost . . . or any other expenses." S.C. Regs. Ann. 117-313.1.