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SC Court of Appeals

Exhibit A

(March 30, 2016 Order)

STATE OF SOUTH CAROLINA
ADMINISTRATIVE LAW COURT

RECEIVED

JUN 06 2016

SC Court of Appeals

Rent-A-Center East, Inc., and Rent
Way, Inc.,)
)
)
Petitioners,)
)
)
v.)
)
South Carolina Department of Revenue,)
)
)
Respondent.)

Docket No. 13-ALJ-17-0601-CC

ORDER

FILED

MAY 30 2016

SC ADMIN. LAW COURT

This matter is before the South Carolina Administrative Law Court ("ALC" or "Court") on requests for contested cases filed by Rent-A-Center East, Inc., and Rent Way, Inc., ("RAC" or "Petitioners") under S.C. Code Ann. § 12-60-460 (Supp. 2009).¹ Petitioners challenge the South Carolina Department of Revenue's ("Department" or "Respondent") Determinations that gross proceeds from Petitioners' sale or rental of tangible personal property should include proceeds from the sale of Liability Damage Waivers ("Waiver" or "Waivers") in the total amount of \$851,622.31 as of November 30, 2013.² A hearing was held before this Court on September 24 and 25, 2015.

The appealed assessment of taxes and interest includes the following details:

RENT-A-CENTER			
Audit Period	Tax	Interest	Total
4/1/07-10/31/10	\$521,694.93	\$96,652.51	\$618,347.44
RENT WAY			
4/1/07-12/31/09	\$192,158.64	\$41,116.23	\$233,274.87
TOTALS	\$713,853.57	\$137,768.74	\$851,622.31

¹ These cases were consolidated under case number 13-ALJ-17-0601-CC by consent order dated June 9, 2015.

² The Department originally included penalties, but these have been dropped and are not included in the assessments disputed. The amount claimed is from the Department's determinations on which interest continues to accrue.

EXHIBIT A

The sole issue in dispute is whether the sale of Waivers is properly subjected to sales tax under the provisions of South Carolina law.

FINDINGS OF FACT

Having taken evidence and observed the witnesses and exhibits presented at the hearing and having taken into consideration the burden of proof and the credibility of witnesses, the Court makes the following findings of fact by a preponderance of the evidence.

Petitioners are in the business of renting and selling tangible personal property in South Carolina and other states.

The rental/sale is initiated by execution of The Rental-Purchase Agreement ("Agreement") that defines the process by which ownership of the property can be transferred to the customer. The customer selects a contract term: weekly, semi-monthly, or monthly. The Agreement includes a total of scheduled payments with an initial payment, a number of regular payments, and a final payment. The Agreement also provides means by which the customer can make an early purchase any time after the first periodic payment by paying a specified percentage of the difference between the total scheduled payments and the total paid on the account.³

Regular periodic payments are due at the beginning of each term. The customer may choose to renew the Agreement by making an advance rental payment at the beginning of the next term (or change the term by making a payment in the amount required for a different term option). Each term payment is a renewal of the Agreement. The Agreement may be terminated at any time by the customer's surrendering or returning the property in good repair along with any past due rental payments or by carrying out the early purchase option. The customer is under no obligation to purchase the Waiver or, if purchased, to continue its effect past the term for which payment has been made.

Petitioners maintain and service the property during the payment period but are not responsible for unauthorized repairs or for damage caused by improper use. Under the terms of the Agreement, the customer is "responsible for the fair market value of the property if and as of the

³ For the purposes of this transfer, as stated in the Agreement, the payments scheduled on the account do not include any late charges or Waiver payments.

time it is lost, stolen, damaged, or destroyed.”

In addition to the disclosures about rental payments, the Agreement includes fees for the Waiver, taxes, and charges imposed for late payments. Under the terms of the Waiver, if loss is caused by means specified in the Waiver (lightning, fire, smoke, windstorm, theft, or flood) and occurs during the time in which both the Agreement and the Waiver provision remain in effect, Petitioners waive the customer’s liability. If the customer is not current with payments under the Agreement or has not purchased the Waiver for the period in which the damage or loss occurs, the Waiver is void or inapplicable.

The Optional Liability Waiver Provision, although a separate document, according to its terms, “is an additional part of the Rental Agreement,” specifies the amount charged for the Waiver, and provides that the fee is to be paid “with [the] weekly/semi-monthly/monthly rental payment while this Provision is in effect.” The Waiver fee is calculated as a percentage of the term rental.⁴ The Waiver may be enforced only so long as the Agreement’s “periodic payments including the liability waiver fee” have been paid through the date of loss. Waivers are only available on items acquired from Petitioners or an affiliated entity and are not available independently.

Petitioners contend that the Agreement and the Waiver are “two separate agreements, which for two separate charges provide two separate benefits to the customer.” The Court finds that the Agreement and Waiver are not separate agreements.

The documents are fundamentally interconnected. Both state the amount of the Waiver fee that the customer agrees to pay. The Waiver itself is self-described in its title as a “Provision” and explicitly states that it is “an additional part of the Rental Agreement.” A provision is “[a] clause in a statute, contract, or other legal agreement.” BLACK’S LAW DICTIONARY 1262 (8th ed. 2004). Moreover, without the underlying agreement to supply a durable good to the customer, the Waiver has no function or value that can be purchased separately. In his direct examination, Professor Pomp stated that the Agreement and the Waiver do not comprise a mixed or bundled transaction because the Waiver is optional. However, on cross-examination, Professor Pomp conceded that there would be no optional waiver unless there was some risk to waive. Further, in

⁴ Testimony indicates that the Waiver fee is 7.5% of the rental-purchase term payment.

responding to a hypothetical based on the purchase of a trophy divided into three optional stages — unassembled trophy, assembled trophy, and assembled trophy with engraving — Professor Pomp opined, “once you bought all three together, it wasn’t optional anymore.”

From the explicit terms of the documents and the testimony of the witnesses, the Court finds that there is one transaction, one document consisting of two forms: one in which liability damages to the subject durable good(s) are imposed on the customer and one in which the customer pays a fee to shift the risk of liability for specified damages to Petitioners.

CONCLUSIONS OF LAW

Based upon the above Findings of Fact, the Court concludes the following as matters of law. The ALC has jurisdiction to hear this contested case pursuant to S.C. Code Ann. §§ 1-23-600 (Supp. 2015) and 12-60-460.

Burden of Proof and Standard of Review

The standard of proof in this administrative proceeding is a preponderance of the evidence. *See Anonymous v. State Bd. of Med. Exam'rs*, 329 S.C. 371, 496 S.E.2d 17 (1998). In general, 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 & Envtl. Control*, 340 S.C. 118, 133, 530 S.E.2d 643, 651 (2000) (citing 2 Am. Jur. 2d Admin. Law § 360 (1994)). Here, Petitioners requested a contested case hearing and, therefore, have the burden of proof to show by a preponderance of the evidence that the Department’s tax assessments for the periods at issue were incorrect.

Applicable Tax Provisions

S.C. Code Ann. § 12-36-910(A) (2009) provides that “[a] sales tax, equal to five percent of the gross proceeds of sales, is imposed upon every person⁵ engaged or continuing within this State in the business of selling tangible personal property at retail.” The essential terms used in this provision are defined in related sections of Chapter 36 of Title 12.

Section 12-36-90 (2009) defines “gross proceeds of sales” as follows:

Gross proceeds of sales, or any similar term, means the value proceeding or accruing from the sale, lease, or rental of tangible personal property.... [and] includes . . .

⁵ Pursuant to S.C. Code Ann. § 12-36-30 (2009), “person” includes “any individual, firm, partnership . . . corporation . . .” As such, the Petitioner is a “person” in that it operates as a corporation.

(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;

* * *

(vii) any other expenses.

S.C. Code Ann. § 12-36-60 (2009) defines the term “tangible personal property” to mean:

. . . 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.⁶ [Emphasis added].

In applying these statutes, “[t]he cardinal rule of statutory interpretation is to determine the intent of the legislature.” *Jones v. State Farm Mut. Auto. Ins. Co.*, 364 S.C. 222, 230, 612 S.E.2d 719, 723 (2005). Furthermore, “[t]he legislature’s intent should be ascertained primarily from the plain language of the statute.” *State v. Landis*, 362 S.C. 97, 102, 606 S.E.2d 503, 505 (Ct. App. 2004). “What a legislature says in the text of a statute is considered the best evidence of the legislative intent or will.” *Bayle v. S.C. Dep’t of Transp.*, 344 S.C. 115, 122, 542 S.E.2d 736, 740 (Ct. App. 2001). “Revenue laws are generally construed in favor of the taxpayer and against the taxing authority.” *Clark v. S.C. Tax Comm’n*, 259 S.C. 161, 169, 191 S.E.2d 23, 26 (1972) (internal quotation marks omitted).

Analysis

In addressing sales tax statutes, South Carolina appellate courts have analyzed the statutory scope and application in three cases particularly relevant to circumstances in this case. The South Carolina Supreme Court in *Travelscape, LLC v. S.C. Dep’t of Revenue*, 391 S.C. 89, 705 S.E.2d 28 (2011), held that facilitation and service fees added to room rental rates were part of the actual

⁶ An intangible is “something that lacks a physical form; an abstraction, such as responsibility.” BLACK’S LAW DICTIONARY 823 (8th ed. 2004). As used in the UCC, a “payment intangible” is “a general intangible under which the account debtor’s principal obligation is a monetary obligation. S.C. Code Ann. § 36-9-102 (61) (2003). An account debtor is a person obligated to pay “for property that has been or is to be sold [or] leased.” S.C. Code Ann. § 36-9-102 (2) and (3) (2003). In this case, the customer is obligated to reimburse Petitioners “for the fair market value of the property if and as of the time it is lost, stolen, damaged or destroyed.”

price charged to the customer and were, therefore, includable in the gross proceeds of the sale and subject to the sales tax imposed by S.C. Code Ann. § 12-36-920(A).⁷ Although the fees in *Travelscape* were imposed on the customer and were not optional, services sold with the tangible personal property were part of the gross proceeds retained by the seller in addition to the costs for the rooms and labor involved in obtaining and reselling the right to use the rooms.

Likewise, the South Carolina Court of Appeals held that fees added to the cost of property sold on “layaway” were part of the transaction and taxable as part of the gross proceeds of the sale. *Meyers Arnold v. S.C. Tax Comm’n*, 285 S.C. 303, 328 S.E.2d. 920 (Ct. App. 1985). The purpose of the fee was to make the sale possible. Hence the sale and the fee were inextricably connected. The Court of Appeals found the layaway fee to be part of the gross proceeds. Like the service fees in *Travelscape*, the fees were not optional.

However, *Meyers Arnold* also addresses another question: whether gift wrapping is subject to sales tax. Although the Court ultimately found that because the service was free unless a more expensive paper was selected, the charge was for the paper, not the wrapping service, and was, therefore, exempt under S.C. Code Ann. § 12-35-550 (now S.C. Code. Ann. § 12-36-2120 (14)). Without this fact-specific exemption, the exercise of this option by the customer would have subjected the fees to sales tax. Thus, merely being optional does not prevent a part of the transaction from being subject to sales tax.

More recently, in *Boggero v. S.C. Dep’t of Revenue*, 414 S.C. 277, 777 S.E.2d 842 (Ct. App. 2015), the Court of Appeals considered whether “gross proceeds from the rental and servicing of portable toilets [were] subject to sales tax.” The Court identified the issue on appeal as whether the ALC “erred in finding that the true object of [the taxpayer’s] business was not a service and that [the] gross proceeds were therefore subject to the state sales and use tax.” The Court, after analyzing cases from other jurisdictions, decided that the “true object test” focuses on a factual inquiry into what a customer’s essential purpose is in a given transaction. The Court of Appeals also relied on *Palmetto Net, Inc. v. S.C. Tax Comm’n*, 318 S.C. 102, 105, 456 S.E.2d 385, 387 (1995) in which the South Carolina Supreme Court “deferred to the trial court’s factual findings

⁷ This section imposes a sales tax on accommodations and is complementary to S.C. Code Ann. § 12-36-910, the statute at issue here, which imposes a sales tax on tangible personal property.

when deciding whether a particular transaction was subject to a statutorily-based tax.” The general rule is that statutory interpretation is a question of law, but whether the facts of a case are correctly applied to a statute or whether activities meet a statutorily defined term is a question of fact. *See Boggero*, 414 S.C. at 280, 777 S.E.2d at 843 (citing *Hopper v. Terry Hunt Constr.*, 373 S.C. 475, 483, 646 S.E.2d 162, 167 (Ct. App. 2007) (*aff’d* by 383 S.C. 310, 680 S.E.2d 1 (2009)); *Burse v. S.C. Dep’t of Health & Envtl. Control*, 369 S.C. 176, 184-85, 631 S.E.2d 899, 904 (2006); *Dreher v. S.C. Dep’t of Health & Envtl. Control*, 412 S.C. 244, 251, 772 S.E.2d 505, 509 (2015)).

Petitioners contend that the Agreement and the Waiver are two separate and distinct transactions and that because the Waiver is optional it “is not inextricably linked to or embodied in the sale of tangible personal property.” This Court disagrees. In its Findings of Fact, this Court specifically found that the Agreement and Waiver are not separate agreements. Although purchasing the Waiver may be optional, once purchased it is merged into and becomes inextricable from the transaction and has no value apart from the underlying transaction. The amount of the fee is included in the Agreement, and the Waiver agreement, in turn, provides that it “is an additional part of the Rental Agreement.” *See generally S.C. Dep’t of Consumer Affairs v. Rent-A-Center, Inc.*, 345 S.C. 251, 547 S.E.2d 881 (Ct. App. 2001), *cert. dismissed*, 352 S.C. 419, 575 S.E.2d 547 (2002) (The Court of Appeals treats the Waiver as part of the Agreement.).

Petitioners also argue that a recent case before the ALC rejected Respondent’s characterization of *Meyers Arnold*. *See Alltel Commc’ns, Inc. v. S.C. Dep’t of Revenue*, 2015 WL 7681302 (S.C. Admin. Law Ct. Nov. 15, 2015). Although the decision of another Administrative Law Judge is not binding, it is instructive to consider how the facts of that case differ from those in this case. *See* ALC Rule 70 (f). *Alltel* involves two distinct, optional contract offers. One offered extended warranty coverage “against electrical/mechanical malfunction.” *Alltel* conceded that these charges were included in proceeds for which sales tax was due under a now-repealed section of the law.⁸ The second contract offered indemnification coverage providing repair or replacement for a lost, stolen, or damaged device. This coverage was provided for different costs under

⁸ S.C. Code Ann. 12-36-910 included a clause imposing sales tax on “gross proceeds accruing from the sale or renewal of a warranty, maintenance, or similar service contracts.” This tax was repealed by 2011 S.C. Act No. 32, § 2.b, effective September 1, 2011.

insurance policies covering Alltel. Alltel collected and remitted the premiums to its insurers, which reported and paid taxes as required to the South Carolina Department of Insurance. Unlike the cases cited, *Travelscape*, *Meyers Arnold*, and *Boggero*, and this case, Alltel did not retain the premiums. Thus, the payments did not become part of the gross proceeds; that is, they did not become part of “the value accruing from the sale, lease, or rental of tangible personal property.”

Here, the facts show that the Waiver fees are part of the “value proceeding or accruing from the sale, lease, or rental of tangible personal property” and (as Professor Pomp testified) become part of the income on which Petitioners pay tax. Customers who obtain durable goods from Petitioners could reasonably consider that the value of their doing so would be enhanced by avoiding the obligation to pay for lost or damaged items by shifting that risk to Petitioners. Thus, the true object of a transaction would be to obtain the use of an item while minimizing the financial risk for its damage, loss, or destruction.

Other jurisdictions have dealt with the taxability of these Waivers. Recently, the Utah Supreme Court, in *Rent-A-Center W., Inc. v. Utah State Tax Comm'n*, 2016 WL 67693 (Jan. 5, 2016), held that the Waiver was not subject to sales and use tax.⁹ The Utah Court reviewed its state tax code, specifically Utah Code Ann. § 59-12-103(1)(k), which reads: “(k) amounts paid or charged for leases or rentals of tangible personal property if within this state the tangible personal property is: (i) stored; (ii) used; or (iii) otherwise consumed.” The Utah Court interpreted “paid or charged for” in its tax statute as much narrower in reach than statutes in other states. The Utah Supreme Court found that the Utah statute “does not tax amounts ‘derived from’ the rental of tangible personal property, nor does it specifically include ‘services, for which tangible personal property’ is leased.” *Id.* at *4. Although the Utah Court rejected the argument that, because the Waiver was optional and separately itemized, it is not taxable, the Court concluded that “Rent-A-Center’s liability waiver fee is not ‘paid or charged for leases or rentals of tangible personal property.’” *Id.*

The Louisiana Court of Appeals, in *Rent-A-Center E., Inc. v. Lincoln Par. Sales & Use Tax Comm'n*, 60 So. 3d 95 (La. App. 2 Cir. 2011) (*writ denied*, 63 So. 3d 985 (2011)), found that

⁹ The Supreme Court of Utah issued its decision with the caveat that “[t]his opinion is subject to revision before final publication in the Pacific Reporter.”

Waivers were taxable. The Louisiana Court reviewed the pertinent statutes, specifically, La. Stat. Ann. § 47:302 (B)(1), which reads:

B. There is hereby levied a tax upon the lease or rental within this state of each item or article of tangible personal property, as defined herein; the levy of said tax to be as follows:

(1) At the rate of two per centum (2%) of the gross proceeds derived from the lease or rental of tangible personal property, as defined herein, where the lease or rental of such property is an established business, or part of an established business, or the same is incidental or germane to the said business.

The Louisiana Court found that Waiver sales constituted “gross proceeds derived from the lease or rental of tangible personal property.” *Lincoln Par.*, 60 So.3d at 99.

The South Carolina tax statutes in question are broader than Utah’s. Specifically, S.C. Code Ann. § 12-36-90 defines “gross proceeds of sales” as “the value proceeding or accruing from the sale, lease, or rental of tangible personal property.” The Utah statute only taxes amounts that were specifically “paid ‘for’ the lease or rental of tangible personal property.” However, in South Carolina, the statute taxes amounts “proceeding or accruing from the sale,” language far broader and more inclusive than the Utah statute in controversy. The South Carolina statute is more closely analogous to the Louisiana statute, in that the language, “derived from,” is similar to “proceeding or accruing from.” Therefore, other jurisdictions support the decision that Waivers are taxable under South Carolina’s tax statutes, as Waiver fees proceed or accrue from the sale or rental of tangible personal property.

In an analogous case, Louisiana discussed the taxability of collision damage waivers. In *Enterprise Leasing Co. of New Orleans v. Curtis*, 977 So. 2d 975, 980 (La. App. 1 Cir. 2007) (*writ denied*, 976 So. 2d 719 (2008)), the court observed,

... the real object of the transaction is the lease of tangible personal property, the motor vehicle. Clearly, the [collision damage waiver] can only be made available with the lease or rental of a motor vehicle. Enterprise cannot separate the [collision damage waiver] from the principal lease as the [collision damage waiver] does not exist without the automobile lease. Nor can the [collision damage waiver] be purchased from another lessor.

The Louisiana appellate court concluded that collision damage waiver payments were part of the gross proceeds derived from the lease or rental of automobiles since the parties contracted for the

collision damage waivers as part of the lease agreement and found that the payments were "merely incidental to the lease of the tangible property." *Id.*¹⁰

The analysis of the Louisiana appellate court is instructive. The Waivers here are nearly identical to Collision Damage Waivers. Both waivers shift risk, responsibility for damage or destruction, from the consumer to the company, and both are optional and obtained by fees additional to the rental price and should be included in the amount subjected to sales tax.

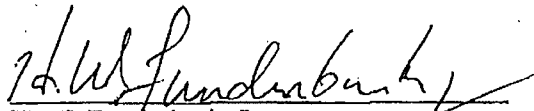
ORDER

For the reasons above, the Court finds that gross proceeds from Petitioners' sale or rental of tangible personal property should include fees from the sale of Liability Damage Waivers.

IT IS THEREFORE ORDERED THAT the Determinations of the Department are upheld.

IT IS FURTHER ORDERED THAT that the Department shall inform Respondents of the total amount due, from the tax liabilities of \$851,622.31 and accrued interest. Respondents shall remit payment to the Department within sixty (60) days of Department issuing the total amount due.

AND IT IS SO ORDERED.


H. W. Funderburk, Jr.
Administrative Law Judge

March 30, 2016
Columbia, South Carolina

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SC ADMIN. LAW COURT

¹⁰ In S.C. Rev. Rul. #93-1, dealing with automobile rentals, the Department determined that charges for a Collision Damage Waiver were "includable in 'gross proceeds of sales' and therefore subject to the sales tax." The Department specifically noted that the Collision Damage Waiver was optional and explained the waiver as follows:

The customer pays a fee for a release of financial responsibility to the company for any damages occurring to the car during use. For example, if the customer is involved in an accident, the customer will not be responsible to the company for repair costs if he or she purchased the collision damage waiver. The fee is separately stated from the rental price.

"The construction of a statute by an agency charged with its administration is entitled to the most respectful consideration and should not be overruled absent compelling reasons." *Sloan v. S.C. Bd. of Physical Therapy Exam'rs*, 370 S.C. 452, 469, 636 S.E.2d 598, 607 (2006).

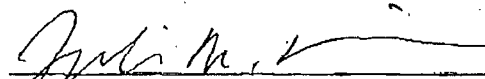
CERTIFICATE OF SERVICE

I, Julia M. Miller, hereby certify that I have this date served this upon all parties to this cause by depositing a copy hereof, in the United States mail, postage paid, in the Interagency Mail Service, or by electronic mail to the address provided by the party(ies) and/or their attorney(s).

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March 30, 2016
Columbia, S.C.


Julia M. Miller
Judicial Law Clerk

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