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THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT COUNTY

H. W. Funderburk, Jr., Administrative Law Judge

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

Appellate Case No. 2016-001210

Rent-A-Center East, Inc. and Rent Way, Inc., Appellants,

v.

South Carolina Department of Revenue, Respondent.

APPELLANTS' PETITION FOR REHEARING

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Pursuant to Rule 221 of the South Carolina Appellate Court Rules, Rent-A-Center East, Inc. ("RAC East") and Rent Way, Inc. (Rent Way") (collectively "Rent-A-Center") hereby petition for rehearing of this Court's Opinion in the above-captioned appeal. See Rent-A-Center East, Inc. and Rent Way, Inc. v. South Carolina Department of Revenue, Op. No. 5615 (S.C. Ct. App. filed January 16, 2019) (Shearouse Adv. Sh. No. 3 at 27) ("Op.") The Court should grant rehearing and issue a revised opinion in favor of Rent-A-Center reversing the decision of the Administrative Law Court ("ALC"), which ruled in favor of the South Carolina Department of Revenue (the "Department"), based on the grounds set forth below.

INTRODUCTION

This Court held that proceeds from the sale of optional waivers (which negate the risk of certain covered events, including lightening, fire, smoke, windstorm, theft and flood occurring to property rented by the customer from Rent-A-Center)[1] ("Waivers") sold by Rent-A-Center are subject to sales tax in South Carolina. In doing so, Rent-A-Center would respectfully submit that the Court overlooked, misunderstood or misapplied South Carolina law and/or the evidence in the record.

First, the Court overlooked, misunderstood or misapplied South Carolina law regarding the two statutory construction issues raised by Rent-A-Center by failing to: (a) construe the relevant statutes pursuant to their plain meaning; and (b) construe any ambiguities in the relevant statutes in favor of the taxpayer and against imposition of the tax. Op. at pp. 30-33.

In addition, the Court's holding appears to have overlooked, misunderstood or misapplied the law in interpreting the sales tax imposition statute (S.C. Code Ann. §12-36-910) to tax **persons** and not **transactions**. Op. at pp. 31-32. This was not the basis of the ALC's

[1] See Tr., R. pp. 157:12- 159:11 and 163:6-10; Waiver, R. pp. 344-345.

decision, which ignored the imposition statute and instead found the Waivers subject to sales tax under the "measure of tax" or gross proceeds statute (S.C. Code Ann. §12-36-90). See Order, R. pp. 4-8. This Court's Opinion that persons and not transactions are subject to sales tax, if not altered, would mean that *all* transactions of retailers are subject to sales tax. For example, a hair salon that sells haircare products, and thus is a service provider as well as a retailer, would suddenly be faced with its hair cutting services being subject to sales tax. This is not consistent with the plain language of the statute, the related regulations, the relevant case law, the Department's own policy manual and the trial testimony of its manager of policy. Rather, as the law and the Department's past policies and practices in interpreting the law make clear, only specific transactions are subject to sales tax in South Carolina- sales of tangible personal property and certain enumerated services not relevant here. S.C. Code Ann. §12-36-910(A) and (B); S.C. Code Ann. Regs. §117-308.

Because the Court of Appeals, unlike the ALC, found that the imposition statute imposes a sales tax on Waivers, it determined that the ALC did not err in reaching the "measure of tax" statute. Op. at p. 6. Rent-A-Center agrees that if an imposition statute imposes a tax, then the "measure of tax" statute comes into play. However, the ALC did not find an imposition statute that applied to the Waivers, and Rent-A-Center respectfully submits that as previously stated, the Court of Appeals erred in finding to the contrary. Therefore, the "measure of tax" statute should not have been reached. Moreover, even if one could skip to the "measure of tax" statute, it only reaches proceeds that proceed or accrue from the sale of tangible personal property, and the proceeds from the sale of a Waiver proceed or accrue from the sale of an intangible.

Finally, the Court overlooked, misunderstood or misapplied South Carolina law and/or the evidence in the record in its application of the true object test to conclude that the sale of a Waiver is subject to sales tax. No substantial evidence supported the ALC's finding that the sale of a Waiver is inextricably linked to the Rental Agreement such that the true object test should be applied. Instead the evidence showed that the two transactions, while related, were not inextricably linked and could easily be separated and thus, the intangible Waivers should not be subject to sales tax.

In sum, rehearing is necessary in this matter because the Opinion does not comport with South Carolina law and because the ALC's conclusions are not supported by substantial evidence. Accordingly, the Court should issue a revised Opinion reversing the ALC's order.

LAW/ANALYSIS

I. THE COURT OF APPEALS OVERLOOKED, MISAPPLIED OR MISUNDERSTOOD SOUTH CAROLINA LAW AS TO TWO STATUTORY CONSTRUCTION ERRORS BY THE ALC.

The Court of Appeals overlooked, misapplied or misunderstood South Carolina law and/or the ALC's order in finding that (a) the plain meaning rule was either applied by the ALC or is irrelevant because the ALC reached the correct result; and (b) no ambiguity exists in the sales tax imposition statute and thus it need not be construed in favor of the taxpayer and against imposition of the tax.

First, as argued in Rent-A-Center's Final Brief in more detail, { TC "A. The ALC Erred in Failing to Apply the Plain Meaning Rule." \f C \l "2" }the ALC erred in failing to apply the plain meaning rule. In construing statutes, the court should start with the text of the statute itself, must give words their plain and ordinary meaning and cannot re-write statutes where the language is clear. See Hodges v. Rainey, 341 S.C 79, 85, 533 S.E.2d 578, 581 (2000){ TA

\l "Hodges v. Rainey, 341 S.C 79, 533 S.E.2d 578 (2000)" \s "Hodges" \c 1 }; State v. Leopard, 349 S.C. 467, 471, 563 S.E.2d 342, 344 (Ct. App. 2002){ TA \l "State v. Leopard, 349 S.C. 467, 563 S.E.2d 342 (Ct. App. 2002)" \s "Leopard" \c 1 }; Rosmer v. Pfizer, 263 F.3d 263 (4th Cir. 2001){ TA \l "Rosmer v. Pfizer, 263 F.3d 263 (4th Cir. 2001)" \s "Rosmer" \c 1 }; Alltel{ TA \l "Alltel v. S.C. Dept. of Rev., 2015 WL 7681302 (S.C. Admin. Law Ct. Nov. 13, 2015)" \s "Alltel" \c 1 } v. S.C. Dept. of Rev., 2015 WL 7681302, slip op. at pp. 17-20 (S.C. Admin. Law Ct. Nov. 13, 2015){ TA \s "Alltel" } (applying the plain meaning rule to the imposition statute to determine whether a taxpayer's indemnification coverage proceeds were subject to sales tax). While the Court of Appeals recognized that the plain meaning rule should be applied (Op. at p. 30), it appears to have concluded either that the ALC implicitly applied it or that it does not matter whether it applied it because the ALC reached the correct result. Op. at pp. 31-32. Moreover, the Court appears to have misunderstood or misapplied the plain meaning rule as its finding that the imposition statute imposes a tax on all persons and not on transactions is not supported by the plain meaning of the statute, particularly when read in conjunction with related statutes and regulations. See infra §II.

As discussed in more detail below, while the ALC failed to identify an imposition statute that imposes a tax on Waivers and relied instead on the "measure of tax" statute { TA \l "S.C. Code Ann. § 12-36-60" \s "12-36-60" \c 2 }as the basis for imposing sales tax on the Waivers,[2] the Court of Appeals found that the imposition statute "levies a sales tax on persons" and not on particular transactions. Op. at pp. 31-32. The ALC and Court of Appeals' failure to properly apply the plain meaning rule caused both courts to improperly construe the taxing

[2] See Order, R. pp. 4-8; Order Denying Mot. for Reconsideration, R. p. 13.

statutes at issue and to err in finding the Waivers subject to sales tax. See infra Section II for full discussion of the proper application of the plain meaning rule to the statutes at issue.

In addition, the Court of Appeals misunderstood or misapplied South Carolina law in determining that no ambiguity exists in the tax statutes at issue such that the ALC did not need to construe them in favor of the taxpayers and against imposition of the tax. { TC "B. The ALC Erred in Failing to Construe the Tax Statutes at Issue in Favor of the Taxpayers and Against SCDOR and Imposition of the Tax." \f C \l "2" }The law is clear that where there is a question of imposition of tax (or coverage) and not one of exemption, the taxing statutes should be construed in favor of the taxpayer and against the imposition of the tax (as opposed to an exemption statute, which is construed against the taxpayer claiming the exemption and in favor of the government); United States v. Merriam, 263 U.S. 179, 188 (1923){ TA \l "United States v. Merriam, 263 U.S. 179 (1923)" \s "Merriam" \c 1 } (citations omitted) (stating that if the words in a tax statute are in doubt then "the doubt must be resolved against the Government and in favor of the taxpayer"); Clark v. S.C. Tax Comm'n, 259 S.C. 161, 191 S.E.2d 23 (1972){ TA \l "Clark v. S.C. Tax Comm'n, 259 S.C. 161, 191 S.E.2d 23 (1972)" \s "Clark" \c 1 } (holding that "[r]evenue laws are generally construed in favor of the taxpayer and against the taxing authority"); see also Rent-A-Center's Final Brief at pp.11-12 (discussing the policy reasons underlying this rule, including due process of law, which require that taxpayers be given clear notice and warning of the circumstances that will lead to their payment of taxes and that tax laws, which are drafted by the State, be construed against the State).

The Court of Appeals found that the taxing statutes at issue are not ambiguous, and, thus, the ALC should not have applied this rule of statutory construction. See Op. at pp. 32-

33. While Rent-A-Center contends that the taxing statutes at issue are unambiguous in the sense that they do not subject the Waivers to sales tax, the Department's arguments, which the ALC and the Court of Appeals appear to have adopted, create an ambiguity in the statute and thereby invoke this rule of statutory construction. The heading of the imposition statute states that the sale tax is "on tangible personal property" and certain enumerated items (see S.C. Code Ann. § 12-36-910{ TA \s "12-36-910" }), and the statutory definition of tangible personal property confirms that only items enumerated under the sales tax chapter are subject to sales tax as "tangible personal property." See S.C. Code Ann. §12-36-60{ TA \s "12-36-60" }. See also S.C. Code Regs. §117-308 (providing that the sales tax applies to particular transactions) and infra §II (for additional law and discussion on same).[3]

In a case very similar to this one, the ALC found the imposition statute for sales tax ambiguous and ruled that it must be construed in favor of the taxpayer and against imposition of the tax. Alltel{ TA \s "Alltel" } Communications, Inc. v. S.C. Dept. of Rev., 2015 WL 7681302 (S.C. Admin. Law Ct. Nov. 13, 2015)(concluding that sales tax imposition statute did not impose a tax on indemnification coverage proceeds sold in conjunction with wireless phones, and, thus, such proceeds were not subject to sales tax). The interpretation of the imposition statute by the Department and the Court of Appeals that leads to the faulty conclusion that the sales tax applies to everything that a retailer of tangible personal property

[3] Case law also confirms that services are generally not taxable. See Boggero{ TA \s "Boggero" } v. S.C. Dept. of Rev., 414 S.C. 277, 777 S.E.2d 842 at n. 1 (Ct. App. 2015) (noting that "[g]enerally, the gross proceeds from services are not subject to sales and use tax")(citations omitted). The Court of Appeals' statement in this case correctly focuses on the transaction (a sale of services) and not the seller.

sells renders the imposition statute, at best, ambiguous and, therefore, it must be construed in favor of Rent-A-Center and against imposition of the sales tax.

Based on the above, the Court should grant the Petition for Rehearing and reverse the ALC's decision because the ALC erred in failing to apply the plain meaning rule and in failing to construe the imposition statute in favor of the taxpayer and against imposition of the tax.

II. THE COURT OF APPEALS OVERLOOKED, MISUNDERSTOOD OR MISAPPLIED SOUTH CAROLINA LAW IN HOLDING THAT THE IMPOSITION STATUTE IMPOSES A SALES TAX ON PERSONS AND NOT TRANSACTIONS.

The Court of Appeals overlooked, misapplied or misunderstood South Carolina law in holding that the imposition statute imposes a sales tax on **persons** and not **transactions**. As previously stated, the ALC failed to identify an imposition statute that imposes a tax on intangible Waivers and referred instead to the "measure of tax" statute { TA \l "S.C. Code Ann. § 12-36-60" \s "12-36-60" \c 2 }as the basis for imposing sales tax on the Waivers.[4] Rent-A-Center's briefing before this Court contains extensive argument on why this is improper. See Rent-A-Center Final Brief at pp. 14-20 and and 26-28 and Final Reply Brief at pp. 6 and 10-13.[5] However, the Court of Appeals found that the sales tax imposition statute

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[4] See Order, R. pp. 4-8; Order Denying Mot. for Reconsideration, R. p. 13.

[5] As the Final Brief also discussed, the ALC's decision that the Waivers are subject to sales tax appears to be primarily based on the following three cases (in addition to the measure of tax statute at S.C. Code Ann. §12-36-90{ TA \s "§12-36-90" }): Travelscape, LLC v. S.C. Dept. of Rev., 391 S.C. 89, 705 S.E.2d 28 (2011){ TA \l "Travelscape, LLC v. S.C. Dept. of Rev., 391 S.C. 89, 705 S.E.2d 28 (2011)" \s "Travelscape" \c 1 }; Meyers{ TA \s "Meyers" } Arnold v. S.C. Tax Comm'n, 285 S.C. 303, 328 S.E.2d 920 (Ct. App. 1985); and Boggero{ TA \s "Boggero" }{ TA \s "Boggero" } v. S.C. Dept. of Rev., 414 S.C. 277, 777 S.E.2d 842 (Ct. App. 2015). Order, R. pp. 5-7. Rent-A-Center argued that none of these cases supports the ALC's conclusion that the Waivers are subject to sales tax. See Rent-A-Center Final Brief at pp. 17-25. Because this Court agrees that these cases are "not directly analogous to the instant appeal because they involve attempts to deduct service fees" (Op. at p. 36) and because

does, in fact, apply to Waivers. More specifically, the Court found that the sales tax statute "levies a sales tax on persons" and does not apply "to transactions and certain enumerated services." Op. at p. 6. This interpretation is contrary to South Carolina law, sales tax law generally, the Department's interpretation of the law in its policies and the testimony of the manager of policy at the Department at the trial of this case.

First, the conclusion that the sales tax imposition statute applies to persons and not transactions is contrary to the plain meaning of the statute as well as South Carolina law and sales tax law generally. The relevant part of the imposition statute reads as follows:

> **SECTION 12-36-910**{ TA \s "12-36-910" }**.** Five percent tax on tangible personal property; laundry services, electricity, communication services, and manufacturer-consumed goods.
>
> (A) A sales tax, equal to five percent of the gross proceeds of sales, is imposed upon every person engaged or continuing within this State in the business of selling tangible personal property at retail.

The imposition statute then describes those enumerated services that are subject to sales tax, including operating a laundry (S.C. Code Ann. §12-36-910(b)(1){ TA \l "S.C. Code Ann. § 12-36-910(b)(1)" \s "12-36-910(b)(1)" \c 2 }), providing accommodations (S.C. Code Ann. §12-36-920{ TA \l "S.C. Code Ann. § 12-36-920" \s "12-36-920" \c 2 }), providing communications services (S.C. Code Ann. §§12-36-910(b)(3){ TA \l "S.C. Code Ann. § 12-36-910(b)(3)" \s "§12-36-910(b)(3)" \c 2 }& (5){ TA \l "S.C. Code Ann. § 12-36-910(b)(5)" \s "12-36-910(b)(5)" \c 2 } and 12-36-1310{ TA \l "S.C. Code Ann. § 12-36-1310" \s "12-36-

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its affirmance of the ALC did not rely on these cases and is based on separate grounds, Rent-A-Center will not repeat those arguments herein but incorporates them herein by reference. Certainly absent an imposition statute imposing a tax and/or substantial evidence that the Rental Agreement and Waiver are inextricably linked and that the true object of the transaction was the purchase of tangible personal property, the ALC could not properly find the Waivers taxable on the basis of these three cases.

1310" \c 2 }), and selling electricity (S.C. Code Ann. §12-36-910(b)(2){ TA \l "S.C. Code Ann. § 12-36-910(b)(2)" \s "12-36-910(b)(2)" \c 2 }).

The tax code defines "tangible personal property" (which is subject to sales tax) 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* . . . .

S.C. Code Ann. §12-36-60{ TA \s "12-36-60" } (emphasis added). Thus, only the sales of tangible personal property and those services or intangibles that are *specifically identified* in the sales tax chapter are subject to sales tax. S.C. Code Ann. §§12-36-910{ TA \s "12-36-910" } and 12-36-60{ TA \s "12-36-60" }.[6] As the ALC has explained, a retailer is subject to sales tax under the imposition statute "because it is engaging in a retail sales transaction and because that sales transaction is for tangible personal property." Textile Restoration Services, Inc. v. S.C. Dept. of Rev., 2015 WL7443800, slip. op. at 3 (S.C. Admin. Law Ct. November 12, 2015).

S.C. Code Regs. §117-308 also confirms that the sales tax applies to transactions and not persons. This regulation provides that "[t]he receipts from services, when the services are the true object of the transaction, are not subject to the sales and use tax, unless the sales and use tax is specifically imposed by statute on such services (i.e. accommodation services,

[6] The only exception to this rule is that where a bundled transaction is at issue, certain services that are inextricably linked to the sale of tangible personal property can be subject to sales tax if the "true object" of the sale is the purchase of tangible personal property and not the purchase of a service. See Boggero{ TA \s "Boggero" } v. S.C. Dept. of Rev.{ TA \s "Boggero" }, 414 S.C. 277, 777 S.E.2d 842 (Ct. App. 2015); S.C. Regs. §117-308. No such transaction is at issue here. See infra §IV.

communication services)." See also S.C. Code Regs. §117-308 (listing sixteen different professional, personal or other services that are not subject to sales and use tax, including doctors, lawyers, architects, beauty and barber shops and painters among others). The regulation also notes that "several businesses, in addition to selling nontaxable services, also sell tangible personal property and should be licensed to report the tax." Id.{ TA \l "Boggero v. S.C. Dept. of Rev., 414 S.C. 277, 777 S.E.2d 842

(Ct. App. 2015)" \s "Boggero" \c 1 } Such retailers would only owe sales tax on the transactions involving the sale of tangible personal property and not on the "nontaxable services" or other nontaxable items such as intangibles. See id.[7] These regulations clearly recognize that a retailer can sell both taxable and nontaxable items.

In addition, it is widely accepted that sales tax is a transactional tax. See e.g. J. Hellerstein & W. Hellerstein, State Taxation, 3d ed. at §12.01 (2000) (citing R. Haig & C. Shoup, The Sales Tax in the American States 3 (1934))(discussing definition of sales tax as "any tax which includes within its scope all business sales of tangible personal property at either the retailing, wholesaling, or manufacturing stage with the exceptions noted in the taxing law;" describing the retail sales tax as "a single-stage levy on consumer expenditures;" and

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[7] There are also numerous regulations providing that certain charges for labor (i.e. a service) are not taxable even though sold in conjunction with the sale of tangible personal property. See S.C. Code Ann. Regs. §117-313.3 (installation charges); S.C. Code Ann. Regs. §117-306 (repair charges); S.C. Code Ann. Regs. §117-313.4 (alteration charges); S.C. Code Ann. Regs. §117-318.2 (interest charges on seller financing). Such regulations would not be valid if the imposition statute actually imposed sales tax on all retailers of tangible personal property for all transactions. See also S.C. Rev. Ruling #14-7 (providing that optional charges for hurricane rental insurance sold in conjunction with sleeping accommodations are not subject to sales tax but mandatory charges are). If the Department believes that its interpretation of the imposition statute in this case (i.e. that it applies to persons and not transactions) is correct, it has had many years to challenge these regulations but has not done so.

noting that state sales taxes are "collected from the purchaser by the seller and are collected on a *transaction-by-transaction basis.*") (emphasis added); Tronco's Catering, Inc. v. S.C. Dept. of Rev., 09-ALJ-17-0089-CC at p. 8 (Admin. Law Ct. April 12, 2010) (stating that "[s]ales tax under § 12-36-90 is a transactional tax. A transactional tax is a tax that must be determined on a transaction-by-transaction basis. In order to derive the correct and appropriate tax base, each transaction must be analyzed separately and the type of transaction specifically identified.").

Moreover, despite the Department's arguments in its briefs to the contrary, the long-standing policy of the Department is that the sales tax is a transactional tax. Its Sales and Use Tax Manual from 2015 states that "[i]n addition to *applying to the sale or use of tangible personal property* (*e.g.,* furniture, clothing, computers, etc.), the sales and use taxes also apply to:

(1) certain communication services,
(2) laundry and dry cleaning services,
(3) electricity,
(4) the fair market value of tangible personal property manufactured within South Carolina or brought into South Carolina by its manufacturer for storage, use, or consumption in South Carolina by the manufacturer,
(5) transient construction property, and
(6) the furnishing of accommodations."

See S.C. Department of Revenue Sales and Use Tax Manual (2015).[8] The current edition of the manual also confirms that the sales tax "is a 'transaction tax' imposed with respect to the transaction of a 'retail sale' of tangible personal property." S.C. Department of Revenue Sales

[8] The Department's Sales and Use Tax Manual is published by its Policy Section in the Office of General Counsel, and the 2015 edition was available on the Department's website at www.dor.sc.gov at the time this appeal began and is cited in Rent-A-Center's Final Reply Brief. Although the 2018 version appears to be the only edition currently available on the website, it contains similar language at Chap. 7, p. 1.

and Use Tax Manual at Chapter 2, p. 1 (2018). Furthermore, the manager of policy at the Department correctly testified at trial that ". . . under the code, the way the Department looks at it is, sales tax is a transactional tax." (Tr., R. at p. 271:23-25).

A strikingly similar case was addressed by the ALC in Alltel{ TA \s "Alltel" } Communications, Inc. v. S.C. Dept. of Rev., 2015 WL 7681302 (S.C. Admin. Law Ct. Nov. 13, 2015).[9] The issue in Alltel{ TA \s "Alltel" } was whether sales proceeds from optional contracts sold by Alltel for indemnification coverage in the form of repair or replacement for lost, stolen or damaged wireless communication devices were subject to sales tax when the contracts were sold in conjunction with the sales of wireless communication devices. Alltel argued that under the plain meaning of the imposition statute (S.C. Code Ann. §12-36-910){ TA \s "12-36-910" }, the indemnification coverage proceeds were not subject to tax because an insurance type product is not tangible personal property under §12-36-60{ TA \s "12-36-60" } and therefore cannot be part of its gross proceeds of sales under §12-36-90{ TA \l "S.C. Code Ann. § 12-36-90" \s "§12-36-90" \c 2 }. Id. at 17. The ALC noted the Department's concessions that no imposition statute referenced insurance policies (which term it used to refer to the indemnification coverage at issue) and that the policies are not tangible personal property. Id. Applying the plain meaning rule, the ALC then concluded that no imposition statute imposed a tax on indemnification coverage proceeds, and, thus, not subject to sales tax. Id. at 18.

[9] The Department initially appealed the Alltel{ TA \s "Alltel" } decision; however, the parties subsequently settled the case and dismissed the appeal, and, thus, this opinion is a final decision of the ALC.

The plain meaning of the relevant statutes as well as the related regulations, general sales tax law, relevant case law, the Department's policies and practices as set forth in its sales and use tax manual and its manager of policy's testimony at trial all show that the imposition statute applies to transactions and not persons. Furthermore, no South Carolina statute identifies the sale of anything similar to a Waiver (whether a service or an intangible)[10] as taxable. See S.C. Code Ann. §12-36-910{ TA \s "12-36-910" }; Tr., R. p. 292:17-24. In fact, the Department admits that the Waivers are not taxable on their own, which underscores that the imposition statute does not cover them. See Tr., R. pp. 294:19- 295:2. Therefore, the proceeds from the sale of Waivers are not subject to sales tax.

Based on the above, this Court should grant Rent-A-Center's Petition for Rehearing and reverse the ALC's decision, which failed to find an imposition statute imposing a sales tax on intangible Waivers, and, thus, should have found that the Waivers are not subject to sales tax.

III. THE COURT OF APPEALS OVERLOOKED, MISUNDERSTOOD OR MISPPLIED SOUTH CAROLINA LAW IN AFFIRMING THE ALC'S RELIANCE ON THE "MEASURE OF TAX" STATUTE (S.C. CODE ANN. §12-36-90) TO REACH THE INCORRECT CONCLUSION THAT WAIVERS ARE SUBJECT TO SALES TAX.

The Court of Appeals overlooked, misunderstood or misapplied the law in affirming the ALC's reliance on the "measure of tax" statute to reach the incorrect conclusion that the Waivers are subject to sales tax. See Op. at pp. 35-36. This Court found that the ALC could rely on the "measure of tax" statute because substantial evidence supported the ALC's findings that "the Waivers were merely incidental to the Rental Agreements," or, stated differently, "the Waivers and Rental Agreements were inextricably linked." Op. at p. 35. It did not

[10] The parties agreed that the sale of a Waiver is not the sale of tangible personal property. Tr., R. pp. 290:17- 291:6.

address Rent-A-Center's argument that a "measure of tax" statute cannot be reached unless an imposition statute is first identified, possibly because the Court of Appeals found (incorrectly) that S.C. Code Ann. §12-36-910 imposes a sales tax on persons not transactions and/or because it found (incorrectly) that the transaction was bundled and subject to sales tax under the true object test.

Rent-A-Center agrees that the "measure of tax" statute can be reached if either an imposition statute imposes a tax or if the transaction is a bundled transaction and the true object of the sale is the purchase of tangible personal property. However, because as is discussed in sections II (no imposition statute) and IV (no bundled transaction) herein, neither of these situations applies here, Rent-A-Center submits that the ALC improperly reached the "measure of tax" statute.{ TA \s "§12-36-90" } See Rent-A-Center's Final Brief at pp. 26-28 (discussing the tax policy reasons why if no imposition statute imposes a tax, then one cannot reach the "measure of tax" statute and citing the following decisions in support of same: Alltel{ TA \s "Alltel" }, 2015 WL 7681302, slip op. at pp. 18-20 (rejecting the Department's arguments that sales proceeds from optional indemnification contracts sold in conjunction with wireless communications devices were subject to sales tax as "value proceeding or accruing from the sale of tangible personal property" under the gross proceeds of sales statute where no imposition statute imposed such a tax); Brock Serv., LLC v. Ala. Dept. of Rev., No. S. 14-1236, slip op. at pp. 3-10 (Ala. Tax Tribunal Sept. 28, 2015){ TA \l "Brock Serv., LLC v. Ala. Dept. of Rev., No. S. 14-1236 (Ala. Tax Tribunal Sept. 28, 2015)" \s "Brock" \c 1 } (finding that labor services provided in conjunction with renting of scaffolding were not subject to sales tax under the imposition statute (which mirrors the South Carolina imposition statute) and rejecting argument that the gross proceeds of sales statute (which mirrors the South

Carolina gross proceeds of sales statute a/k/a "measure of tax statute") justified imposing a tax noting that "the broad definition of 'gross proceeds' at §40-12-220(4) prevents a lessor from deducting its overhead, labor, and other operating expenses from its otherwise taxable gross proceeds. Like the gross proceeds in Thyssenkrupp, the labor receipts in issue in this case were never gross proceeds subject to the rental tax to begin with."); Rent-A-Center West, Inc. v. Utah State Tax Comm'n, 367 P.3d 989, 991-994 and n. 1 (Utah 2016){ TA \l "Rent-A-Center West, Inc. v. Utah State Tax Comm'n, No. 20140129 (Utah January 5, 2016)" \s "Rent-A-Center West" \c 1 } (addressing the Waivers that are also at issue here and determining that they were not subject to sales tax because they were not "an amount paid or charged for leases or rentals of tangible personal property" as the Utah imposition statute required; that whether the fees could be encompassed within the definition of "purchase price" or "sales price" in the definitions statute was irrelevant because they were not encompassed by the imposition statute; and that a long-standing Tax Commission regulation was invalid because it "impermissibly broaden[ed] the language of the statute"); Letter Ruling No. CL 2290, 2000 Mo. Tax Ltr. Rul. LEXIS 37 (Mo. Dep't Rev. May 18, 2000){ TA \l "Letter Ruling No. CL 2290, 2000 Mo. Tax Ltr. Rul. LEXIS 37 (Miss. Dep't Rev. May 18, 2000)" \s "Letter Ruling No. CL 2290" \c 3 } (ruling that the sale of optional damage waiver protection for a separately stated price was not taxable as it was not the sale of tangible personal property nor was it specifically listed as a taxable service under the relevant statutes); Ky Dept. of Rev. v. Rent-A-Center East, Inc. and Rent-Way, Inc., Op. no. 16-CI-1075 (Ky. Cir. Ct. Sept. 11, 2017), appeal filed, October 10, 2017 (holding that sales of optional intangible Rent-A-Center waivers were not subject to tax under the imposition statute, which must be narrowly construed). But see Rent-A-Center East v. Lincoln Par. Sales & Use Tax Comm'n, 60 So.3d 95 (La. App. 2

Cir. 2011), writ denied, 63 So.3d 985 (2011){ TA \l "Rent-A-Center East v. Lincoln Par. Sales & Use Tax Comm'n, 60 So.3d 95 (La. App. 2 Cir. 2011), writ denied, 63 So.3d 985 (2011)" \s "Rent-A-Center East" \c 1 } (finding the Rent-A-Center waivers taxable).

Furthermore, even if the ALC properly reached the "measure of tax" statute, the ALC erred in finding the Waiver proceeds to be a part of Appellants' "gross proceeds of sale." See Order, R. pp. 8 and 10. South Carolina law defines "gross proceeds of sales" as "the value proceeding or accruing from sales and leases or rental of tangible personal property." S.C. Code Ann. §12-36-90{ TA \s "§12-36-90" }.

The ALC's Order found the Waiver fees to be part of "the value proceeding or accruing from the sale, lease, or rental of tangible personal property." Order, R. p. 8. This is not supported by any evidence and is contrary to the law. Proceeds from the rental of property under a **Rental Agreement** are clearly "a value proceeding or accruing from" the sale or rental of tangible personal property (such as, for example, the rental of a television). On the other hand, Waiver proceeds are "a value proceeding or accruing from" the sale of intangible **Waivers**, which provide the customers, via separate, optional agreements and for a separate itemized charge, with the option to avoid certain risks of loss of the property rented. Tr., R. pp. 171:4-10 and 178:2-12. See also Alltel{ TA \s "Alltel" }, 2015 WL 7681302, slip op. at p. 17-19 (finding that proceeds from the sale of indemnification coverage did not proceed or accrue from sale of tangible personal property as such coverage was not tangible personal property); and Rent-A-Center Final Brief at pp. 29-30 (for full discussion of Alltel).[11]

[11] The ALC's Order also appears to have relied on the ALC's mistaken belief that the value of the rented property in the customer's hands is enhanced by the Waiver. Order, R. p. 8. This is an incorrect interpretation of the evidence and the "measure of tax" statute. The ALC has erroneously shifted the focus from the value that proceeds or accrues to the seller (which is the

Based on the foregoing, Rent-A-Center respectfully requests that the Court grant the Petition for Rehearing and reverse the ALC because it failed to invoke an imposition statute prior to relying on the "measure of tax" statute and because it erred in finding the Waiver proceeds to be "gross proceeds."

IV. THE COURT OF APPEALS OVERLOOKED, MISAPPLIED OR MISUNDERSTOOD THE LAW REGARDING THE TRUE OBJECT TEST AND INCORRECTLY CONCLUDED THAT SUBSTANTIAL EVIDENCE SUPPORTED THE ALC'S CONCLUSION THAT THE WAIVER AND THE RENTAL AGREEMENT WERE INEXTRICABLY LINKED.

The Court of Appeals overlooked, misapplied or misunderstood the law regarding the true object test and incorrectly concluded that substantial evidence supported the ALC's conclusion that the Waiver and the Rental Agreement were inextricably linked.

The ALC found that the Rental Agreement and Waiver were inextricably linked and thus applied the true object test and concluded that a customer's true object in entering these transactions was the rental of items and therefore that the Waivers were subject to sales tax. Order, R. p. 7. The Court of Appeals acknowledged that evidence could "support a finding that the Waivers were separate and distinct from the Rental Agreements," and thus not inextricably linked or fundamentally interconnected (as this Court phrased it), including evidence that the Waivers were optional and could be canceled at any time without canceling the Rental Agreement, that the fee for the Waiver was listed on the customer's receipt and that

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focus of the imposition statute) to the value received by the customer. As the Department's manager of tax policy agreed, the relevant value under the statute is the value received by the seller, i.e. the "gross proceeds" it receives from the customer. Tr., R. pp. 301:21-25 and 302:17-22. Additionally, the value of the rented property does not change because a customer purchased a Waiver. If a customer rents a television that is valued at $500 and then purchases a Waiver, the television's value remains $500. Tr., R. pp. 232:11- 234:20. No substantial evidence supports the conclusion that the value of the rented property is increased due to the Waiver.

payment of the Waiver fee did not count toward the purchase of rental property. Id. However, this Court concluded that substantial evidence also supported the ALC's finding that the Waivers were not separate and distinct from the Rental Agreement, and, thus, it stated that it would not substitute its judgment for that of the ALC. Op. at p. 34. Rent-A-Center would respectfully submit that the Court of Appeals' conclusion on this issue is premised on a misunderstanding or misapplication of the law regarding the true object test.

Courts use the "true object" test to determine the true object of a bundled transaction, i.e. whether it is a sale of taxable tangible personal property or a sale of a non-taxable service or intangible). See Tr., R. pp. 234:24- 235:9 (testimony of Appellants' tax policy expert, Professor Richard Pomp, explaining that where you have one combined or integrated transaction with two elements such that a bundled transaction exists, the true object test seeks to determine "which elements are going to dominate and control how we characterize the [integrated] transaction"). See also Boggero{ TA \s "Boggero" } v. S.C. Dept. of Rev., 414 S.C. 277, 777 S.E.2d 842 (Ct. App. 2015); Southeast Cinema Entertainment v. S.C. Dept. of Rev., 2014 WL 2417715 (S.C. Admin. Law Ct. 2014) (reversed and remanded on an unrelated issue by 2015 WL 9393942 (Dec. 23, 2015)); Keith Purdy, d/b/a A Southern Bartender v. S.C. Dept. of Rev., Docket No. 17-ALJ-17-0002-CC (April 26, 2018), appeal filed July 5, 2018.

Thus, the first question is whether a bundled transaction exists such that the true object test needs to be applied. S.C. Rev. Ruling #06-08 (2006) defines a bundled transaction as "a transaction consisting of distinct and identifiable properties or services, which are sold for one nonitemized price but which are treated differently for [sales and use] tax purposes." The revenue ruling goes on to state that "the portion of the price attributable to any nontaxable

property or service is subject to tax unless the provider can reasonably identify that portion from its books and records kept in the regular course of business for purposes other than sales taxes."

South Carolina courts have applied the true object test on several occasions. In Boggero{ TA \s "Boggero" }, for example, the Court of Appeals applied it to a taxpayer who both rented and serviced portable toilets. 414 S.C. 277, 777 S.E.2d 842. The evidence at trial showed that servicing toilets was not optional but was included with the rental of the toilets; that invoices were not clearly itemized as to the amounts charged for the rental of the portable toilets (tangible personal property) versus the amounts charged for the service of waste removal, including many invoices that simply charged a single flat fee; and that the taxpayer charged more for toilets that had more amenities. Id., 414 S.C. at 286-87, 777 S.E.2d at 846-47. The Court held that there was substantial evidence that the true object of the transaction was the renting of the toilets and implicitly found that the rental and service transactions were bundled and could not be easily separated. Id., 414 S.C. at 286-87, 777 S.E.2d at 846-48.

In Southeast Cinema, the ALC examined a sale involving an IMAX theater and its trademark licenses. 2014 WL 2417715, slip op. at pp. 2 and 5-6. It found that the entire gross proceeds were subject to sales tax because the purchase agreement, which covered both the theater and the trademark, did not itemize the cost of the two items (in fact, the agreement stated that the purchase price was for the IMAX theater, not the trademark) and the IMAX theater could not be used without the trademark license such that the trademark was "inextricably connected to" the purchase of the IMAX system. Id. at p. 5-6.

Most recently, in 2018, the ALC applied the true object test in the context of a bartending service that sold bartending services as well as alcohol. A Southern Bartender,

Docket No. 17-ALJ-17-0002-CC, slip. op. at pp. 8-9. The court held that where the taxpayer provided both bartending and alcohol, but the bartending services were a separate line item on the invoice, the bartending services were "separable from the provision of alcohol and/or other tangible goods, and thus, do not represent the retail sale of tangible personal property." Id. at p. 9. On the other hand, it ruled that where the taxpayer provided bartending services and beverages based on a non-itemized, per person fee, the provision of bartending services was merely incidental to (and presumably not separable from) the sale of the tangible personal property (i.e., the alcohol). Id. at p. 8.[12]

At trial, Professor Richard Pomp (Rent-A-Center's tax policy expert) also discussed an engraved trophy example to illustrate how one would analyze whether a bundled transaction exists. (Tr., R. pp. 249:9- 250:24 and 255:23- 256:25). He explained that once the trophy is assembled and engraved, it has been altered or improved such that assembly and engraving are no longer optional if one is going to purchase that trophy. The engraving has been physically

[12] While an earler ALC decision reached what at first glance might appear to be an inconsistent result, that case is distinguishable. See Tronco's Catering, Inc. v. S.C. Dept. of Rev., 09-ALJ-17-0089-CC at pp. 4-9 (S.C. Admin. Law Ct. April 12, 2010)(finding separately-stated catering labor and service charges were subject to sales tax and noting that true object of customer was to buy food; however, the primary basis for the ruling (and what distinguishes Tronco's from this case) is that the charges for the catering services are not deductible under S.C. Code Ann. §12-36-90 as either the "cost of materials, labor or service" or as "any other expenses." Additionally, the ALC found that the catering services enhanced the value of the meal. The Waivers here are clearly not a cost or expense of providing rental items and, as discussed above (see supra n. 11), the Waivers do not enhance the value of a rental item). See also Ky Dept. of Rev. v. Rent-A-Center East, Inc. and Rent-Way, Inc., Op. no. 16-CI-1075 (Ky. Cir. Ct. Sept. 11, 2017) at pp. 5-6, appeal filed, October 10, 2017 (holding that the same optional intangible Waivers sold by Rent-A-Center that are at issue here were not inextricably linked to the Rental Agreements and noting that the Waivers did not interfere with the customer's right to possess the rental item, the Waiver payments did not contribute to payment of the rental item and the Waiver simply entitled the customer to a single consideration that Rent-A-Center would not pursue certain claims for loss or damage and thus finding the Waivers were not subject to sales tax as no imposition statute imposed a tax on intangibles).

incorporated into the trophy and thus is inextricably linked to the trophy such that the sale of the trophy and the assembly/engraving services constitute a bundled transaction.

The ALC in this case found that the Rental Agreement and the Waiver are inextricably linked (and thus a bundled transaction) based on two purported facts: (1) that a single agreement exists, and (2) that once the Waiver is purchased, "it is merged into and becomes inextricable from the transaction and has no value apart from the underlying transaction." Order, R. p. 7. The ALC's apparent finding that the Waiver "merges into and becomes inextricable from [the Rental Agreement]" does not appear to be based on any additional facts beyond that it found a single agreement (which is not determinative) and its erroneous belief that the Waiver "has no value apart from the underlying transaction." Order, R. p. 7. This latter finding regarding value is not supported by any evidence in the record and instead is contradicted by all evidence pertaining to the Waivers' continuing separate existence and value, and thus, is clearly erroneous for all of the reasons set forth in Rent-A-Center's Final Brief. See Rent-A-Center's Final Brief at pp. 24-25.[13] The Court of Appeals does not mention this

[13] To the extent the ALC was implying that the Waiver has no value apart from the underlying transaction because a customer does not purchase one without also renting an item, this is not a valid basis for finding the transactions to be bundled. As Professor Pomp responded when asked this question at trial:

> It doesn't make it a bundled transaction. It can still be a separate transaction. It has a factual predicate but that doesn't mean it's not a separate transaction. I mean, if I buy a car from you . . . for $10.00, you could get car washes for the next year. Those car washes aren't going to become taxable if they won't otherwise be taxable because of the factual predicate I had to buy the car. I'll sell you my casebook, and you know that's tangible personal property, even though most of the value of the book is an intellectual property, but we do it as tangible. And then I say, anyone who buys the book today for a discounted price can get an hour's worth of consultation with me. Normally legal services aren't taxable. They don't become taxable because you couldn't

purported fact in its opinion and does not appear to have considered it as part of the substantial evidence supporting the ALC.

The evidence cited by the Court of Appeals as constituting substantial evidence that the Waiver is "fundamentally interconnected" to the Rental Agreement included the following: that the fee for the Waiver and the fee for the Rental Agreement are paid at the same time; that the Waiver can only be enforced if all payments are made under the Rental Agreement; that the Waiver fee is calculated as a fixed percentage of the term payment under the Rental Agreement; that the customer must enter into a Rental Agreement to buy a Waiver; that Rent-A-Center does not offer Waivers to third parties; and that the Waiver states (per Rent-A-Center due to requirements imposed by consumer protection laws in various states) that the Waiver is an additional part of the Rental Agreement. Op. at p. 8.

Rent-A-Center submits that while these facts may show that the Waiver and Rental Agreement are related in certain ways, they do not rise to the level of substantial evidence that the transactions are so fundamentally interconnected or inextricably linked that they cannot be easily separated. First, S.C. Rev. Ruling #06-08 defines a bundled transaction as "a transaction consisting of distinct and identifiable properties or services, which are sold for one nonitemized price." That is not the case here as the charge for the Waiver is separately itemized. Tr., R. pp. 168:17- 169:8; Waiver, R. pp. 344-345; Sample Receipt, R. pp. 346-347. Moreover, even if the Court believes that this is not determinative, the other factors referenced by South Carolina courts (in addition to a non-itemized price, which is present in

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> get those services without purchasing the book. So you can have a factual predicate, but that doesn't make the second transaction somehow part of the bundled transaction.

Tr., R. pp. 252:24- 253:20.

Boggero, Southeast Cinema and A Southern Bartender) that have expressly or implicitly found a bundled transaction or an inextricable link are not present here. In this case, the intangible Waiver is optional and not mandatory (unlike the services in Boggero and the intangible in Southeast Cinema) and the taxable rental items can be used without the non-taxable Waiver (unlike the theater in Southeast Cinema which could not be used without the intangible trademark). Nor does the intangible Waiver here alter or improve the rented item as the engraving did for the trophy in Professor Pomp's example at trial (the trophy also was not optional and the price was not itemized).

In sum, in Boggero, Southeast Cinema, A Southern Bartender and the trophy example, strong evidence of a fundamental interconnection or inextricable link exists such that it is difficult to break apart the two transactions and determine the appropriate value of each. None of the factors supporting an inextricable link in those cases is present here. The cost of the Waivers is itemized, the Waivers are optional, the rental item can be used without the Waiver and the Waiver does not become incorporated into the rental item. Accordingly, this Court should grant the Petition for Rehearing and reverse the ALC's decision that the Rental Agreement and the Waiver are fundamentally interconnected or inextricably linked as that conclusion is not supported by substantial evidence and is contrary to South Carolina law.

CONCLUSION

Based on the above, the Court should grant the Petition for Rehearing and issue a revised Opinion reversing the order of the ALC.

Respectfully submitted,

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Charleston, South Carolina
February 19, 2019

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT COUNTY

H. W. Funderburk, Jr., Administrative Law Judge

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

Appellate Case No. 2016-001210

Rent-A-Center East, Inc. and Rent Way, Inc., Appellants,

v.

South Carolina Department of Revenue, Respondent.

PROOF OF SERVICE

I, the undersigned Administrative Assistant of the law offices of Nelson Mullins Riley & Scarborough LLP, attorneys for Rent-A-Center East, Inc. and Rent Way, Inc., hereby certify that I have served all counsel in this action with a copy of the pleading(s) hereinbelow specified via U.S. Mail to the following address(es):

Pleadings:

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February 19, 2019

Via Hand Delivery
The Honorable V. Claire Allen
Deputy Clerk South Carolina Court of Appeals
1220 Senate Street
Columbia, SC 29201

RE: Rent-A-Center East, Inc. and Rent Way, Inc., Appellants,
v. South Carolina Department of Revenue, Respondent.
SC Appellate No.: 2016-001210
Our File No. 017856/09003

Dear Ms. Allen:

Enclosed for filing are the originals and seven (7) copies of the following:

1. Appellants Rent-A-Center East, Inc. and Rent Way, Inc.'s Petition for Rehearing; and
2. Proof of Service for Petition for Rehearing.

We have also enclosed the required $50.00 filing fee. Please return the clocked in copies of each to our firm's courier.

By copy of this letter the Petition for Rehearing and the Proof of Service are being served upon the Respondent. Thank you for your assistance with this matter, and please do not hesitate to contact us with any questions or concerns.

With kind regards,

Bryson M. Geer

BMG:gh
Enclosures
cc: Sean G. Ryan, Esq.
Lauren Acquaviva, Esq.