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S.C. SUPREME COURT

THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM THE ADMINISTRATIVE LAW COURT

John D. McLeod, Administrative Law Judge

Opinion No. Op. 5721 (S.C. Ct. App. filed April 29, 2020)

Books-A-Million, Inc. ..... Petitioner,

v.

South Carolina Department of Revenue ..... Respondent.

PETITION FOR A WRIT OF CERTIORARI

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Pursuant to Rule 242 of the South Carolina Appellate Court Rules ("SCACR"), Petitioners Books-A-Million, Inc. ("Petitioner" or "BAM" or "Books-A-Million") petition the Court to issue a writ of certiorari to review the decision of the Court of Appeals styled *Books-A-Million, Inc. v. South Carolina Department of Revenue*, Op. No. 5721 (S.C. Ct. App. April 29, 2020) (Shearouse Adv. Sh. No. 17 at 45), finding in favor of the South Carolina Department of Revenue ("Department" or "Respondent" or "DOR"). Appendix ("App.") p. 525. For the reasons set forth below, the petition should be granted, and the decision of the Court of Appeals should be reversed.

CERTIFICATE OF COUNSEL

Counsel for Petitioner hereby certifies that a Petition for Rehearing was timely filed on May 14, 2020 (App. pp. 537-44), and finally ruled on by the Court of Appeals on July 14, 2020. App. p. 545.

QUESTIONS PRESENTED FOR REVIEW

I. Did the Court of Appeals err in holding that Books-A-Million, Inc. should have included the amounts collected from its sale of club membership fees, including renewals, in the gross proceeds of sales subject to sales tax?

STATEMENT OF THE CASE

This matter was before the South Carolina Administrative Law Court (the "ALC") pursuant to a Request for a Contested Case Hearing filed by Petitioner challenging the Department's final determination, in which the Department assessed Petitioner taxes, penalties, and interest following a sales tax audit for periods beginning January 1, 2012 and ending August 31, 2015. In its determination, the Department assessed Petitioner $226,310.70 in sales taxes, $15,703.13 in related interest, and $63.14 in related penalties. App. pp. 429-30.

The Department issued its final determination on March 15, 2016 (App. pp. 429-

34), and Petitioner timely appealed to the ALC. App. p. 5. The sole issue before the ALC was whether the proceeds from Petitioner's South Carolina sales and renewals of Millionaire's Club memberships should have been included in Petitioner's gross proceeds of sales and, therefore, subject to sales tax. The parties filed Stipulations of Facts with the Court on September 13, 2016. App. pp. 438-40. On March 6, 2017, both parties filed Motions for Summary Judgment. App. pp. 173, 208. The parties agreed there were no material facts in dispute but disagreed as to the application of the law to the undisputed facts. App. p. 546.

A Motions hearing was held before the ALC on May 9, 2017. On June 1, 2017, the ALC issued its Order ruling in favor of the Department. App. pp. 14-24. On June 6, 2017, the ALC issued an Order vacating the Previous Order and amending Order granting Respondent's Motion for Summary Judgment. App. pp. 3-13. The ALC Order upheld the Department's entire Assessment of taxes, penalties, and interest. *Id.*

Petitioner filed a Motion for Reconsideration (App. p. 151), which was denied (App. p. 25), and subsequently timely appealed. App. p. 353. The Court of Appeals affirmed in full the ALC Ruling in a decision styled as *Books-A-Million, Inc. v. South Carolina Department of Revenue*, Op. No. 5721 (S.C. Ct. App. April 29, 2020) (Shearouse Adv. Sh. No. 17 at 45). Petitioner then filed a Petition for Rehearing (App. p. 537), which the Court of Appeals denied on July 14, 2020. App. p. 545.

SUMMARY OF RELEVANT FACTS

As described in the Court of Appeals' recitation of facts, BAM operates a discount book retail business. App. p. 526. BAM sells books, magazine, collectible supplies, cards, and other gifts in retail stores throughout the country and online. *Id.* BAM operates thirteen retail locations in South Carolina. *Id.* Customers pay a $25 annual fee to belong

to the Millionaire's Club (the "Club"). *Id.* Customers can pay the membership fee separately or along with other store purchases. *Id.* Club memberships expire one year from the date of payment of the membership fee, unless the membership is automatically renewed. *Id.* Club memberships automatically renew each year for a one-year period unless customers affirmatively opt out of the automatic renewal or the Club membership is otherwise cancelled or terminated. *Id.* If customers do not opt out, BAM bills the annual membership fee to the credit or debit card provided when the customer initially enrolled in the Club. *Id.* BAM does not charge sales tax on the cost of either the membership fee or the renewals. *Id.*

Both the ALC and the Court of Appeals' decisions held that both the membership fees and the renewals are subject to sales taxes.

SUMMARY OF GROUNDS OF CERTIORARI

SCACR Rule 242 lists circumstances that weigh in favor of this Court issuing a writ of certiorari. Among those reasons listed in the Rule are where there are novel questions of law at issue. SCACR Rule 242(b)(1).

This case involves a pertinent novel issue of law regarding whether optional membership fees, an intangible, are subject to sales tax under S.C. Code Ann. § 12-36-90. All sides agree that sales of books and CDs by BAM are subject to sales tax. All sides agree that membership fees are an intangible. Intangibles (except for certain specified ones) are not subject to sales tax. So the issue before the Court is whether an optional membership fee is subject to sales taxes.

DOR Policy Documents state that mandatory membership fees are not subject to sales taxes. Mandatory membership fees are charged by competitors, principally Walmart

(Sam's Club) and Costco. See South Carolina Sales and Use Tax Manual (2020 Ed.) at ch. 6, p. 10.

The ALC and Court of Appeals held that in a bundled transaction (i.e., the purchase of two or more goods with different sales tax treatment), intangibles are included in the sales tax base according to the statutory wording in § 12-36-90, which provides that the sales tax base includes all consideration "proceeding or accruing from the sale ... of tangible personal property." So the issue before this Court is whether, in a bundled transaction, the words "proceeding or accruing from the sale ... of tangible personal property" override the numerous sales tax statutory exemptions and exclusions, so as to render otherwise exempt goods subject to sales taxes.

Bundled transactions are quite common. Developers routinely purchase real estate (exempt) together with personal property (subject to sales tax). Perhaps the most common example is a visit to Sam's Club. The customer purchases groceries (exempt), prescription drugs (exempt), a toaster (taxable) and canned goods (taxable). All are rung up on the same cash register receipt, i.e., the exempt goods (unprepared food and prescriptions) are value "proceeding or accruing from the same ... of [taxable] tangible personal property."

Under the Court of Appeals' decision, the real property is included in the developer's sales tax base and prescriptions and unprepared food are also subject to sales tax as they are all proceeding or accruing from the sale of tangible personal property.

While there are numerous Appellate Court decisions dealing with the sales tax base prior to the *Books-A-Million* decision, no Appellate Court case has ever held that the "proceedings or accruing" language in § 12-36-90 overrides statutory exclusions or exemptions. *Books-A-Million* is the first decision to do so. The Court of Appeals' decision

will allow the Department to expand the assessment of sales tax whenever it can draw a connection—however tenuous—between the sale of tangible personal property and an otherwise exempt transaction.

In addition, although strenuously argued at both the ALC and Court of Appeals level, neither Court addressed the obvious due process question of why Walmart (Sam's Club) and Costco's mandatory membership fees are not included in the sales tax base but BAM's optional fees are.

In view of the foregoing, and as discussed below, important reasons exist for this Court to issue a writ of certiorari and review the Court of Appeals' decision in this matter.

ARGUMENTS

I. THIS COURT SHOULD GRANT CERTIORARI BECAUSE THE COURT OF APPEALS ERRED IN APPLYING THE PLAIN MEANING RULE TO THE RELEVANT STATUTES.

The Court of Appeals erred in applying the plain meaning rule to § §12-36-910(A), 12-36-90 and 12-36-60, of the Retail Sales Tax Act, to hold that membership fees should be subject to sales tax. The plain meaning rule is only applicable when a statute is unambiguous, and to determine ambiguity, courts look to whether the statute's language can have more than one reasonable interpretation. *See Kennedy v. S.C. Ret. Sys.*, 345 S.C. 339, 348, 549 S.E.2d 243, 247 (2001). Consequently, "where the language relied upon is to bring a particular person within a tax law is ambiguous or is reasonably susceptible of an interpretation that will exclude such person, then the person will be excluded, any substantial doubt being resolved in his favor." *Cooper River Bridge, Inc. v. S.C. Tax Comm'n*, 182 S.C. 72, 76, 188 S.E. 508, 509-510 (1936); see also *Alltel Commc'ns, Inc. v. S.C. Dep't of Rev.*, 399 S.C. 313, 318, 731 S.E.2d 869, 872 (2012) ("[A]ny substantial doubt in the application of a tax statute must be resolved in favor of the taxpayer.").

Importantly, because we are not dealing with a sales tax exemption but instead the application of a taxing statute, it is a settled rule that ambiguities are resolved "against the government and in favor of the taxpayer." *Hadden v. S.C. Tax Comm'n*, 183 S.C. 38, 190 S.E. 249 (1937).

S.C. Code Ann. § 12-36-910(A) provides that the sales tax, equivalent to 5% of the gross proceeds of sale, "is imposed upon every person engaged or continuing within this State in the business of selling tangible personal property at retail." To determine whether the amounts collected by the membership fees fit within the category of "gross proceeds of sale," the phrase must be defined. S.C. Code Ann. § 12-36-90 provides the following definition: "Gross proceeds of sale, or any similar term, means the value proceeding or accruing from the sale, lease or rental of *tangible* personal property." (Emp. added). The term "tangible personal property" is subsequently defined in § 12-36-60 as follows:

> "Tangible personal property" means 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.

Based upon the language in these statutes and for the reasons outlined below, BAM asks this Court to grant certiorari because its Club membership fees do not fall within the relevant portions of the Retail Sales Tax Act. The DOR (and the ALC) conceded that membership fees are "intangibles." No sales tax statute imposes sales taxes on membership fees. The Retail Sales Tax Act is silent. The Act excludes intangibles in § 12-36-60. The DOR in its Policy Documents excludes mandatory membership fees. If mandatory membership fees are exempt, and optional membership fees are taxable – in the complete absence of any statute or regulation so providing – by definition the Act is ambiguous, and

Books-A-Million has provided a reasonably acceptable interpretation of the statutes; thus, ambiguity must be resolved in favor of Books-A-Million.

1. The Court of Appeals erred in ruling that the relevant statues are not ambiguous.

The Court of Appeals erred in its application of the plain meaning rule because the rule is only applicable when a statute, on its face, is unambiguous. *See Kennedy*, 345 S.C. at 348, 549 S.E.2d at 247. "The cardinal rule of statutory interpretation is to ascertain and effectuate the intent of the legislature." *Sloan v. Hardee*, 371 S.C. 495, 498, 640 S.E.2d 457, 459 (2007). Statutes should not be construed so as to lead to an absurd result. *Carolina Power & Light v. Town of Pageland,* 321 S.C. 538, 471 S.E.2d 137 (1996); *see also Fraternal Order of Police v. S.C. Dep't of Rev.*, 332 S.C. 496, 496, 506 S.E.2d 495, 496 (holding that if bingo taxes were considered a component of gross proceeds, it would demonstrate the *reduction ad absurdum* of the Department's position.)

In the case at hand, §§ 12-36-90, 12-36-60, and 12-36-910(A), are ambiguous. None of the statutes, and in fact, no part of the Retail Sales Tax Act mentions membership fees, other than to exclude intangibles. The Sales Tax Act is silent on the subject. By virtue, if the language of a statute can be broadly interpreted, the language is ambiguous unless the legislature's intent clearly indicates otherwise. However, the Court of Appeals erroneously construes the statutes' silence as readily clear that membership fees are subject to sales tax without providing any explanation for why the General Assembly would have written the statute intentionally broad and without any evidence that such intent existed. When examining legislative intent, it is clear that the Court of Appeals failed to recognize an alternative interpretation of the relevant statutes exists.

Under the Court of Appeals' broad interpretation of § 12-36-910(A), regulations

put in place by the General Assembly would directly contradict the Retail Sales Tax Act. For example, although no South Carolina regulations discuss the taxation of intangibles, the S.C. Code Regs. §117-308.1-308.16 list numerous services not subject to sales tax even where tangible personal property is sold in conjunction with the services. Such services include those provided by veterinarians, optometrists, and barber and beauty shops. All of these professions sell tangible personal property to customers such as dog food, glasses, and shampoo, and these items are subject to sales tax. But the services provided for in this bundled transaction are exempt. For example, if a man went to a barber shop to have his hair cut and purchased shampoo in the process, the barber would exempt the cost of the hair cut from the sales tax base but not the sale of shampoo. However, under the Court of Appeals' broad interpretation of the relevant statutes, such regulation would be irreconcilable with § 12-36-910(A)'s imposition of a sales tax on "every person engaged. . . in the business of selling tangible personal property at retail."

Additionally, if the legislature's intent was to include optional memberships in gross proceeds of sales, it begs the question if the statute is unambiguous why mandatory memberships sold by competitive retailers such as Costco and Sam's Club, are exempt from the sales tax base. If § 12-36-90 was clearly broad and "encompasses the total value of the sale," as the Court of Appeals reiterates, then mandatory memberships would certainly fit within this threshold as well. However, Court of Appeals' decision does not address the Walmart/Costco competitive advantage, other than cite an irrelevant example contained in a footnote of the Department's Sales and Use Tax Manual, where the "membership fee is the sales price for tangible personal property." *Books-A-Million, Inc.*, Op. No. 5721, at 54.

Yet, virtually every quote in the decision says BAM should stand in the same shoes as Walmart/Costco, whose membership fees are not included in their sales tax base. For example, the Court of Appeals finds:

> South Carolina case law provides that gross proceeds of sales includes all value that comes from or is a direct result of the sale of tangible personal property. The Membership Fee is a direct result of the sale of tangible personal property because BAM would not be able to sell Club Memberships but for BAM's sale of tangible personal property.

Id. WalMart (Sam's Club) and Costco could not sell membership fees but for their sale of tangible personal property:

> "'*Because the [Club Membership] cannot exist without [BAM] offering tangible personal property for sale, I conclude [BAM's Club Membership] and sales of tangible personal property are inseparable.*'"

Id. at 50. (emphasis added). Sam's Club and Costco are even more inseparable – a customer cannot get in the door without a membership card! Hard to be more inseparable that that.

The Court of Appeals' decision also notes:

> In *Meyers Arnold, Inc. v. South Carolina Tax Commission*, 285 S.C. 303, 307, 328 S.E.2d 920,923 (Ct. App. 1985), the issue was whether a layaway fee was part of the gross proceeds of sales. The court reasoned that "[b]ut for the lay away [sic] sales, Meyers Arnolds would not receive the law away [sic] fees. The fees are obviously charged for the service rendered in making lay away [sic] sales.

And the Court of Appeals' quote above explicitly includes the sale or lease of real property in the sales tax base "if they are incidental to and … enhance the value of the sale" of the tangible personal property. No appellate decision has ever contained such a holding.

Further, if the statute was as unambiguous as the Court of Appeals claims it to be, the Department would not have conceded that it had no rationale as to why membership

fees charged to customers of membership-only warehouses are not included in the sales tax base, whereas sales of memberships by Books-A-Million are included. Counsel for the Department stated at the Oral Argument before the ALC: "Maybe the Department's policy is too narrow. Because again, if you apply the plain meaning of the statutes here, I would argue that that example actually should be included in the sales tax base." App. p. 420, lines 7-11. However, despite counsel agreeing that the plain meaning rule would lead to two separate conclusions under the same statute (implying ambiguity), the Court of Appeals turns a blind eye and applies the rule regardless.

The Retail Sales Tax Act, and specifically § 12-36-90, do not mention membership fees. Neither the Department, the Administrative Law Court, nor the Court of Appeals provides a rationale why if membership fees (an intangible) are to be included in the sales tax base, optional membership fees are included but mandatory fees charged by membership-only warehouses (Sam's Cub/Costco) are not. Mandatory fees are obviously more inseparable than voluntary fees, and but for the purchase of a membership, a customer cannot get in a membership-only warehouse to purchase tangible personal property. By definition, the statute is therefore ambiguous, and the ambiguity must be resolved against the government. See *Alltel Commc'ns, Inc. v. S.C. Dep't of Rev.*, 399 S.C. 313, 321, 731 S.E.2d 869, 873 (2012).

2. The Court of Appeals erred in failing to recognize the reasonably susceptible interpretation of the relevant statutes provided by Books-A-Million, and, therefore, deference was incorrectly granted to Department.

The Court of Appeals erred in failing to acknowledge Books-A-Million's alternative, reasonable interpretation of § 12-36-910(A) that membership fees are not subject to sales tax as they are an exempt intangible. Such an interpretation is reasonable

and deserving of deference because not only has the Department admitted that the statutes are ambiguous, but the Department has ruled that the sale of other intangibles, including memberships, are not subject to sales tax. Although the Court of Appeals recognizes that an agency receives deference in interpreting and administrating a statute or regulation, the court should only defer to such interpretation if it is worthy of deference. *Kiawah Dev. Partners, II v. S.C. Dep't of Health & Envtl. Control*, 411 S.C. 16, 34, 766 S.E.2d 707, 718 (2014). The court should only defer to an agency's interpretation of a statute if it not "arbitrary, capricious, or manifestly contrary to the statute." *Id.* at 34-35, 766 S.E.2d at 718.

In a recent Order denying a Motion to Reconsider, the ALC noted that deference should only be given if the agency's interpretation if worthy of such **and** only if it can be characterized as a long-standing interpretation of a statute or regulation. *Synovus Bank v. S.C. Dep't of Rev.*, Docket No. 17-ALJ-17-0418-CC (C.J. Anderson, filed June 22, 2020). The ALC points out that the two elements are inseparable and examines the pitfalls of using one without the other. The ALC stated: "if there is no requirement that the interpretation be longstanding, an agency can simply espouse a view of the law in one case and a different view of the law in the next case and seek deference for both views no matter how short the timeframe," and "ignoring the requirements of a longstanding administrative interpretation would allow an agency to construe its statutes or regulations on a case-by-case basis and seek deference for that mutable interpretation." *Id.* As discussed below, it is evident that the Department has failed to establish a longstanding interpretation of the relevant statutes and regulations regarding the taxation of intangibles such as membership fees, and, thus, deference should have been given to Books-A-Million.

In SC Rev. Rul. 2004-4, the Department held that the sale of a prepaid telephone calling card was not subject to sales tax as an intangible notwithstanding that it was inextricably linked to the subsequent sale of a taxable service (telecommunications service). The Ruling states: "Prepaid Telephone Calling Card for Use with Land-Based Phones. The sale or recharge at a retail of a prepaid telephone calling card as described in the facts for use in making local, long distance, or international telephone calls, that can be used to make a call from a land-based phone, is not subject to sales tax since this transaction is not a sale of tangible personal property. The transaction is merely the exchange of money for an intangible evidence of debt – a future right to telephone service" (emphasis in original).

The Ruling also states: "Other similar nontaxable transactions include the sale of gift certificates or traveler's checks," even though gift certificates and Traveler's checks are inextricably linked to the subsequent purchase of tangible personal property.

Similarly, in SCDOR PLR #11-5, subscribers to a wireless telecommunications service could receive loyalty points under a "123" Loyalty plan. "Subscribers to these plans accrue points over time which can be exchanged for a discounted new phone, discounts on phone accessories" and other goods and services. At issue was whether "the value allowed for the loyalty points used for the discount were subject to the [sales] tax as part of the 'gross proceeds of sales' or 'sales price' of the tangible personal property." The Department held that it was not, stating:

> 2. When loyalty points are exchanged under a JKL Company "123 Plan" for discounts on the sale of tangible personal property, the value allowed for the loyalty points used for the discount is not a part of the "gross proceeds of sales" or "sales price" of the tangible personal property and is therefore not subject to the sales and use tax. In other

> words, the "gross proceeds of sales" or "sales price" of the tangible personal property subject to the sales and use tax does not include the discount allowed for the "123 Plan" loyalty points.
>
> For example, if a cell phone otherwise sells for $200, but a "123 Plan" subscriber can purchase the cell phone for $175 by exchanging a certain number of loyalty points, then the "gross proceeds of sales" or "sales price" upon which the tax is calculated is $175.

These rulings indicate that the Department's interpretation of whether intangibles are taxable are not longstanding but rather occur on a case-by-case basis. It is equally clear that in these instances, the Department has conceded an alternative, reasonable interpretation of the statute exists (i.e. that intangibles are not subject to sales tax). Given the Department's interpretation changes depending on the situation at hand, and given the Department has previously argued that intangibles are not subject to sales tax, it is evident that the Court of Appeals erred in granting deference to the Department and failed in considering Books-A-Million's reasonable interpretation that under § 12-36-910(A), membership fees (intangibles) are not subject to sales tax.

II. THIS COURT SHOULD GRANT CERTIORARI BECAUSE THE COURT OF APPEALS ERRED IN HOLDING § 12-36-910(A) IMPOSES A SALES TAX ON MEMBERSHIPS.

The Court of Appeals erred in holding that § 12-36-910 imposes a sales tax on membership fees because under § 12-36-60, tangible personal property excludes intangibles such as membership fees. Under § 12-36-60, only the sales of tangible personal property and services or intangibles explicitly stated (e.g., electricity) are subject to sales tax. For additional support, the All States Tax Guide provided by the RIA also confirms

that memberships would be excluded from tangible property. It closely tracks § 12-36-60 of the S.C. Code but with the addition of "membership":

> Nearly all sales and use taxes are levied on tangible personal property— sometimes also referred to as tangible personalty. This doesn't include real property such as buildings, ... Nor does it include intangible personal property consisting of mere rights of action and having no intrinsic value—such as contracts, deeds, **mortgages**, money, **stocks**, **bonds**, certificates of deposit, or ***membership***.

(emphasis added).

If a "membership"—described as a "mere right[] of action… having no intrinsic value"—appears as a nontaxable intangible in a manual providing state-by-state tax guidance, it is evident that § 12-36-60 excludes membership fees from its definition tangible personal property. Regardless, the ALC addressed a strikingly identical issue in *Alltel Comm'ncs, Inc. v. S.C. Dept. of Rev.*, 2015 WL 7681302 (S.C. Admin. Law Ct. Nov. 13, 2015).

In *Alltel Communications*, the ALC examined 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 phones were subject to sales tax when contracts were sold in conjunction with sales of wireless phones. Alltel argued that under the plain meaning rule of § 12-36-910, the indemnification coverage proceeds were not subject to sales tax because an insurance type product is not tangible personal property. Thus, it could not be a part of gross proceeds of sale under § 12-36-90. While ALC acknowledged the Department's arguments that § 12-36-910 did not reference insurance policies and insurance policies were tangible personal property, the court concluded that no imposition statute imposed a tax on indemnification coverage proceeds, and, therefore, they were not subject to sales tax.

Based upon the evidence that membership fees are also excluded from the relevant statutes and are not a form of tangible personal property, the Court of Appeals erred in ruling § 12-36-910(A) imposes a sales tax on Books-A-Million's membership fees.

III. THIS COURT SHOULD GRANT CERTIORARI BECAUSE THE COURT OF APPEALS ERRED IN HOLDING § 12-36-90 REQUIRED THE DELETION OF "PROCEEDING OR ACCRUING" UNDER BOOKS-A-MILLION'S INTERPRETATION OF THE STATUTE.

Further, the Court of Appeals' decision essentially holds that the words "proceeding or accruing from the sale…of tangible personal property" contained in S.C. Code Ann. § 12-36-90 override all the sales tax exemptions and exclusions contained in the Sales and Use Tax Act (§ 12-36-10 *et seq.*). Under such an interpretation, all the exemptions listed in the Act would be overridden in a bundled transaction if one item, a taxable item, was subject to sale taxes and the exemption was not.

Specifically, § 12-36-2120 contains some 80 exemptions. The Court of Appeals has essentially re-written the opening line of the section to read as follows:

> **§ 12-36-2120 Exemptions from Sales Tax**
>
> Unless it is value proceeding or accruing from the sale of non-exempt property, exempted from the taxes imposed by this chapter are the gross proceeds of sales, or sales price of….

To take a simple example, suppose a manufacturer builds a facility in South Carolina for a capital investment of $20 million. It purchases $8 million of machinery and equipment (M&E) and $2 million of material handling equipment from the same vendor in the same transaction on one invoice. Normally M&E would be exempt from sales taxes under § 12-36-2120(17) but material handling equipment is subject to sales tax as the manufacturer does not qualify for the material handling sales tax exemption under § 12-36-2120(51). Essentially, this would be a bundled transaction with one exempt item (M&E)

and one taxable item (material lending equipment). Is the sales tax base $2 million (material handling only) or $10 million (material handling and M&E)? Under the Court of Appeals' decision, the sales tax base is $10 million, as the M&E is value proceeding or accruing from the purchase of non-exempt material handling equipment. And in this example, M&E is an exempted item – the burden of proof falls on the taxpayer to establish the exemption, whereas in this case, intangibles are an exclusion and not included in the Sales Tax Act.

Example Two: Suppose a retailer goes out of business and sells its six stores in South Carolina to a former competitor. Sale one is a store with a real estate value of $1.2 million dollars together with furniture, fixtures and equipment (FF&E) of $60,000. Sales taxes are owed on the FF&E. Is the sales tax base $1,260,000 (real and tangible personal property) or $60,000 (tangible personal property only)? Real property is not subject to sales taxes as the Sales Tax Act only includes tangible personal property. Assuming the closing statement includes both the real and personal property, the Court of Appeals' decision states the sales tax base is $1,260,000 as the real property was purchased as value proceeding and accruing from the sale of tangible personal property.

While this may seem like an outrageous illustration, the Court of Appeals' decision includes this exact example! The decision cites *Tronco's Catering, Inc. v. S.C. Department of Revenue*, 2010 WL 5871622 (S.C. Admin. Law Ct. Apr. 12, 2010) with approval, noting the "court held 'the value of the sale of catered meals includes service, labor, *and room charges* [because] [s]uch charges are incidental to and merely enhance the value of the sale of catered meals'" and that "'[§ 12-36-920] further expressly states that the value of the sale must include costs for materials, labor, service, transportation, *or for any other*

expense." *Books-A-Million, Inc.. v. S.C. Dep't of Rev.*, Op. No. 5721 (S.C. Ct. App. filed April 29, 2020 (Shearouse Adv. Sh. No. 17 at 50-51) (emphasis added).

The ALC noted with approval by the Court of Appeals, held in *Tronco* that the rental of real property was included in the sales tax base then. If the *rental* of real property is included in the sales tax base so is the *sale* of real property if it is value proceeding and accruing from the sale of tangible personal property. The ALC Order expanded the sales tax limitation of tangible personal property to include real property, just as the Court of Appeals has improperly expanded the limitation in this case to include intangibles. And the Court of Appeals' quote above explicitly includes the sale or lease of real property in the sales tax base "if they are incidental to and ... enhance the value of the sale" of the tangible personal property. No Appellate decision has ever contained such a holding.

IV. THIS COURT SHOULD GRANT CERTIORARI BECAUSE THE COURT OF APPEALS ERRED IN FINDING THAT MEMBERSHIP FEES WERE "INEXTRICABLY LINKED" TO THE SALE OF TANGIBLE PERSONAL PROPERTY.

Though it did not address this conclusion directly, the Court of Appeals erred in finding the ALC's decision that membership fees were "inextricably linked" to the sale of tangible personal property was supported by substantial evidence. No South Carolina case has explicitly defined the phrase "inextricably linked." In the context of sales tax cases, courts generally rely on *Meyers Arnold v. South Carolina Tax Commission*, 285 S.C. 303, 328 S.E.2d 920 (Ct. App. 1985) and *Travelscape, LLC v. South Carolina Department of Revenue*, 391 S.C. 89, 705 S.E.2d 28 (2011) to describe what "inextricably linked" means. The fees at issue in those cases share two fundamental attributes—both are service-based fees and both cannot possibly be incurred as a stand-alone charge. In contrast, BAM's membership fees *are not* service-based and *can* be paid separately without the execution

of an underlying taxable transaction. Thus, BAM's membership fees are not "inextricably linked" to the underlying sale of tangible personal property and should not be included in the sales tax base.

In *Meyers Arnold v. S.C. Tax Commission*, the taxpayer was a merchandise retailer who allowed customers to purchase its merchandise either outright or under a layaway plan, for which the retailer charged a non-refundable layaway fee. 285 S.C. at 307, 328 S.E.2d at 923. The retailer "retain[ed] the goods purchased until the full price [of the retail merchandise was] paid." *Id.* The retailer paid sales tax on the layaway fees and sought a refund from the Tax Commission. *Id.* at 307, 303 S.E.2d at 923. The pertinent question before the Court of Appeals was whether the "fees charged by Meyers Arnold on sales made under its lay away plan are subject to sales tax." *Id.* The Court of Appeals ultimately held that "gross proceeds" of the sale were defined as "the value proceeding or accruing from the sale of tangible personal property . . . without any deduction for *service cost*." The Court further held that "[b]ut 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."

Similarly, in *Travelscape, LLC v. South Carolina Department of Revenue*, an online travel agency alleged that it was not required to pay sales tax on the service and facilitation fees it retained from online hotel reservations because such fees are "derived from" the services it provides, not from the rental charge for the hotel rooms. In evaluating the case, the South Carolina Supreme Court applied the plain meaning rule to § 12-36-920(A), which imposes a tax on the "gross proceeds derived from the rent charge for any room." The Court then looked to § 12-36-90(1)(b)(ii), which explicitly defined gross proceeds as "the

value obtained from the rental of accommodations *without deduction for the cost of services*" (emphasis added). Thus, given the explicit language of the statutes in relation to services, the Court applied the plain meaning rule and decided service and facilitation fees retained from online hotel reservations were subject to sales tax.

Both *Travelscape* and *Meyers Arnold* are distinguishable from the case at hand because they involve the imposition of sales tax on fees charged by a retailer providing services where the fees were inextricably linked to the sale of specific tangible personal property. In each case, there was no way the customer could pay the layaway fee or the room booking fee separately—the fee could only possibly be charged if the underlying transaction occurred.[1] However, neither case addresses whether intangibles, such as optional membership fees, are included in gross proceeds of sale, and neither of the cases address an optional fee. Specifically, *Meyers Arnold* simply stands for the proposition that a retailer cannot lower the sales tax base by separately itemizing cost of materials or services inextricably linked to the tangible personal property. It in no way stands for the

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[1] Indeed, even the DOR concedes that lay away fees are not subject to sales tax where there is not an accompanying sale of tangible personal property. In PLR #11-4, dealing with sales taxation of Layaway Sales, Layaway fees and Partial Payment Sales, the DOR states:

> The non-refundable layaway fee is only subject to the sales tax if there has been a layaway sale – a transfer of title or possession of the tangible personal property to the customer. If the layaway agreement is nullified because the customer failed to make a required payment and therefore no layaway sale occurs (no transfer of title or possession of tangible personal property occurs), then the non-refundable layaway fee and any layaway payments received are not subject to the sales tax.
>
> Note: If the layaway fee were refundable (i.e. the layaway fee is returned to the customer if the layaway sale does not occur), the application of the sales tax to the layaway fee would be the same as described in the above conclusion. In other words, if a layaway sale occurs (transfer of title or possession of tangible personal property occurs), then the layaway fee and the layaway payments received would be subject to the sales tax. If no layaway sale occurs (no transfer of title or possession of tangible personal property occurs), then the refundable layaway fee and any layaway payments received would not be subject to the sales tax.

proposition that the purchase of an entirely separate intangible is included in the sales tax base. This issue remains novel in South Carolina.

Further, unlike the case at hand, *Travelscape* and *Meyers Arnold* properly apply the plain meaning rule. Both cases involve statutes that explicitly include services within the gross proceeds of sale in each respective definition. However, the transaction in this case involves an intangible. Intangibles, by contrast, are not subject to sales taxes (except for certain specified intangibles).

The Court of Appeals also erred in relying on the ALC's interpretation of *Southeast Cinema v. S.C. Department of Revenue*, 2014 WL 2417715 (S.C. Admin. Law Ct. May 28, 2014) because although the case involved an intangible (a trademark), the intangible was inextricably linked. In *Southeast Cinema*, the ALC examined whether the proceeds from both the sale of an IMAX theatre and associated trademark were subject to sales tax. Ultimately, the court found that because the purchase agreement did not itemize the cost of the two items and because the theatre could not be used without the trademark license, the trademarks were "inextricably connected to" the theatre. No Appellate Court decision has ever so ruled.

However, the case at hand is readily distinguishable from *Southeast Cinema* because membership fees are optional and the purchase of a book does not depend on the membership fee. Indeed, it is hard to reconcile why mandatory membership fees charged by competing retailers would not be inextricably linked under this analysis. In *Southeast Cinema*, it is evident that the theatre and its trademark are fundamentally connected because the two cannot be broken up to respectively determine the value of each. The ALC noted that his decision may have been different if the trademarks had been separately

priced and the transaction structured differently. Books-A-Million's memberships do not share this difficulty. Memberships are optional, voluntary, and do not depend on the purchase of a book. A customer may purchase a membership and never purchase a book. On the contrary, a customer may purchase a book without ever purchasing a membership. Further, the value of the membership fee can be calculated independently at $25 per year. Accordingly, the Court of Appeals erred in finding an inextricable link between membership fees and the purchase of tangible personal property because, as explained above, such a conclusion is based on the misapplication of law.

Given that South Carolina has no precedent cases that address the novel issue of whether intangibles, such as membership fees, are included in gross proceeds of sale, Books-A-Million asked the Court of Appeals to examine the ruling of a nearly identical issue raised before the Tennessee Court of Appeals.

In *Barnes & Noble Superstores, Inc. v. Huddleston*, 1996 WL 596955 (Tenn. Ct. App. 1996), a bookstore sold "Reader's Choice" membership cards to customers. This membership program entitled customers for the annual fee of $10.00 to 10% discount on the bookstore's merchandise in stores across the country. *Id.* Customers could either present the membership card or give the membership number and expiration date of the card to utilize the membership. *Id.* Based on these facts, the Court held that "the true object of the subject transactions... is to bestow upon club members the intangible right to receive a discount on merchandise." *Id.* The court found the membership card was "merely an indicia of that intangible right and incidentally aids in the exercise of that right." Thus, the memberships could not be subject to sales tax. *Id.*

Likewise, Books-A-Million offers customers the opportunity to purchase a

membership that would entitle them to discounts. The main object of this membership is to gain an intangible right to receive exclusive discounts. Additionally, the Tennessee Commissioner of Revenue, similar to the Department in this case, attempted to characterize the membership fee in *Barnes & Noble* as a "prepayment for merchandise." The Tennessee court rejected this argument because, identical to this case, the "member has no obligation ever to purchase any merchandise." According to the court, "[t]he club member may ultimately elect not to avail himself of the privilege of buying anything." Based on the foregoing, the Tennessee Court of Appeals found Barnes & Nobles' membership fee to be intangible property, which was disconnected from the purchase of any underlying tangible personal property.

Despite the obvious similarities between *Barnes & Noble Superstores* and the case at hand, the Court of Appeals refused to entertain Tennessee's ruling without further explanation. Rather, the Court of Appeals reiterated its independence from other jurisdictions and disinclination to follow other states' interpretation of their tax laws. While this is indeed true, "when there is no South Carolina case directly on point, our courts may look to persuasive authority from other jurisdictions." *S.C. State Highway Dep't v. Wilson*, 254 S.C. 360, 366, 175 S.E.2d 391, 395 (1970).

V. THIS COURT SHOULD GRANT CERTIORARI BECAUSE THE COURT OF APPEALS' ERRED IN HOLDING THAT RENEWAL OF MEMBERSHIP FEES ARE SUBJECT TO SALES TAX.

The Court of Appeals erred in finding BAM's renewals of membership cards are subject to sales taxes because the renewals are automatic, rarely done in connection with the purchase of tangible personal property, and are automatically renewed 12 months after purchase. According to the Stipulations of Facts, "[m]emberships automatically renew each year for one-year periods unless the customers affirmatively opts out of the automatic

renewal.... So long as the customer does not opt out, the Petitioner bills the annual membership fee to the credit or debit card provided when the customer initially enrolled in the Club." App. pp. 4-5, 439. Such renewals are not inextricably linked to the sale of merchandise nor is their value proceeding or accruing from the sale of tangible personal property. Accordingly, renewals should not be included in the sales tax base even if the original membership purchase was so included.

The General Assembly states that consideration "proceeding or accruing from the sale... of tangible personal property" is included in the sales tax base. S.C. Code Ann. § 12-36-90. No Department policy documents, regulation or case (Administrative Law Court, Court of Appeals, or Supreme Court case) has ever held that twelve months later is "proceeding or accruing" under § 12-36-90. (Obviously it is not proceeding, so the question is whether it is "accruing".)

The Court of Appeals decision holds without explanation that twelve months is "accruing." Read literally, every purchase of exempt goods twelve months after the purchase of a taxable item is subject to the sales tax base. Books-A-Million holds that the purchase of a toaster, canned goods and an exempt prescription in the same transaction renders not only the initial purchase of the prescription in the same transaction renders not only the initial purchase of the prescription subject to sales tax but also the regular renewal of the prescription for the next year! No Appellate decision has ever previously so held. (Indeed diligent research reveals not a single Appellate decision construing the "accruing" language, so this is also a novel question of law).

CONCLUSION

For the above-stated reasons, BAM respectfully requests that this Court issue a writ of certiorari to review the Court of Appeals' Opinion in this matter.

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