

THE STATE OF SOUTH CAROLINA
In The Supreme Court

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APPEAL FROM THE ADMINISTRATIVE LAW COURT S.C. SUPREME COURT

John D. McLeod, Administrative Law Judge

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

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

v.

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

APPENDIX FOR PETITION FOR A WRIT OF CERTIORARI

VOLUME II

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THE STATE OF SOUTH CAROLINA
In The Court Of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT

Honorable John D. McLeod, Administrative Law Judge

Case No. 16-ALJ-17-0113-CC
Appellate Case No. 2017-001519

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SC Court of Appeals

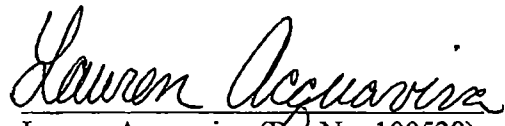
Books-A-Million, Inc., Appellant,

v.

South Carolina Department of Revenue, Respondent.

CERTIFICATE OF COUNSEL

The undersigned certifies that this Final Brief complies with Rule 211(b), SCACR.



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February 26, 2016

THE STATE OF SOUTH CAROLINA
In The Court Of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT

HONORABLE JOHN D MCLEOD, ADMINISTRATIVE LAW JUDGE

CASE NO. 16-ALJ-17-0113-CC
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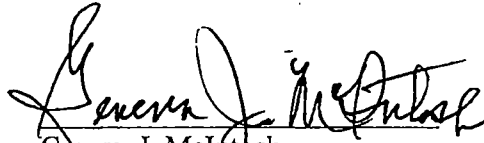
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PROOF OF SERVICE

I, Geneva J. McIntosh, do hereby certify that I have caused to be mailed postage pre-paid, by deposit in the United States Mail on the below date, a copy of the South Carolina Department of Revenue's Final Brief of Respondent in re: Books-A-Million, Inc. v. South Carolina Department of Revenue, Appellate Case No. 2017-001519 to Burnet R. Maybank, III, Esquire, and Jim Rourke, Esquire, Nexsen Pruet, P.O. Box 2426, Columbia, SC 29202-2426 this 26th day of February 2018.


Geneva J. McIntosh
Legal Assistant for Respondent

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

John D. McLeod, Administrative Law Judge

Case No. 16-ALJ-17-0113-CC
Appellate Case No. 2017-001519

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FINAL REPLY BRIEF OF APPELLANT

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I. STATEMENT OF ISSUES ON APPEAL

A. Did the Administrative Law Court Properly Find That Books-A-Million, Inc. Should Have Included the Proceeds From Its Sales of Club Memberships, Including Renewals, in Its Gross Proceeds of Sales?

II. ARGUMENTS

A. The ALC Erred in Holding that the Amounts Collected by Books-A-Million for the Membership Cards are Subject to Sales Tax.

1. General

The ALC Order held that “Membership Fees” collected by Books-A-Million for the sale of membership cards were subject to sales tax. The Order holds that the Membership Fee is subject to sales tax as gross proceeds of sale because the membership cards are sometimes sold in conjunction with the sale of tangible personal property (books, CDs and the like).

The Department’s brief repeatedly states that the sales tax statutes are “plain and unambiguous.” (e.g. Respondent’s brief at 5.) Indeed they are. The two relevant statutes are section 12-36-90 and section 12-36-130. Where does section 12-36-90 provide that sales tax is charged in a bundled transaction (i.e., the purchase of two or more items) on the sale of an otherwise exempt item (intangible)?

S.C. Code Section 12-36-90 provides in part:

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

- 1) The term includes:
 - a) The proceeds from the sale of property sold on consignment by the taxpayer;
 - b) The proceeds from the sale of tangible personal property without any deduction for:
 - i. The cost of goods sold;
 - ii. The cost of materials, labor, or service;
 - iii. Interest paid;
 - iv. Losses;
 - v. Transportation costs;
 - vi. Manufacturers or importers excise taxes imposed by the United States; or
 - vii. Any other expenses.

It does not. In fact, the quoted language twice recites gross proceeds means the value proceeding or accruing from the sale of “tangible personal property.” Code Section 12-35-140 defines the term “tangible personal property” and reads:

The term “tangible personal property” means personal property which may be seen, weighed, measured, felt or touched or which is in any other manner perceptible to the senses, except notes, bonds, mortgages or other evidences of debt and stocks and shall include rooms, lodgings or accommodations furnished to transients for a consideration.

For the purposes of this chapter the term “tangible personal property” shall be interchangeable with and apply with equal force and effect to services, accommodations *and intangibles*, including communications, *as are specifically provided for in this chapter.* (Emp. added).

Intangibles “specifically provided for” includes electricity and communications, but not membership cards. So, by necessity, Respondent’s entire case rests on the value “proceeding or accruing” language in the statute.

The second relevant statute is section 12-36-130. The Department states it is likewise plain and unambiguous. So does where section 12-36-130 include the sale of intangibles in the sales tax base?

Section 12-36-130, which defines “sales price” states:

“Sales price” means the total amount for which tangible personal property is sold, without any deduction for the cost of the property sold, the cost of the materials used, labor or service cost, interest paid, losses, or any other expenses.

(1) The term includes:

(a) Any services or transportation costs that are a part of the sale, whether paid in money or otherwise; and

(b) Any manufacturers or importers excise tax imposed by the United States.

(2) The term does not include:

- (a) A cash discount allowed and taken on the sale;
- (b) An amount charged for property, which is returned by the purchaser, and the full amount is refunded in cash or by credit;
- (c) The value allowed for secondhand property transferred to the vendor in partial payment;
- (d) The amount of any tax imposed by the United States with respect to retail sales, whether imposed upon the retailer or consumer, except for manufacturers or importers excise taxes.

Simply put, it does not. It does say sales price includes the total amount without any deduction for the cost of materials used, labor or service costs. The labor or service cost language is the basis for the Court's holding in *Meyers Arnold v. SC Tax Commission*, 285 SC 303, 328 SE2d 920 (1985). The Court held excluding layaway costs from the sales tax base violated the plain, no deduction for labor or service cost, language. Of course, a membership card is not a material, labor or service cost.

Neither statute explicitly addresses bundled transactions. As discussed below, the DOR has addressed this issue on many occasions.

2. Bundled Transactions

A bundled transaction is the sale of tangible personal property as well as a service or intangible. This case involves a bundled transaction as customers in many cases purchased tangible personal property (books) as well as an intangible, (a membership card) (In other cases, i.e. renewals, the customer purchases only an intangible, so the renewals were not bundled transactions.) Appellant did not keep records or capture this information but obviously some people only purchased memberships, for example as gifts during the Christmas.

Respondent's entire case is necessarily based upon the "value proceeding or accruing" the sale of tangible personal property as capturing the sale of intangibles in the sales tax base. But we

know this is not accurate. Customers who purchased a book and a gift card at Books-A-Million are not charged sales tax on the gift card, even though according to the DOR's analysis, the sale produces "value" proceeding or accruing the sale of the book. Customers who purchased a prepaid calling card along with a book similarly were not charged sales tax on it. Why not? They are intangibles, and in a bundled sale, each item purchased is separately examined. To belabor the point, there is no larger retailer than Walmart. Customers buy exempt (unprepared foods¹) and non-exempt goods at Walmart. Each item is separately analyzed for sales tax purposes in a bundled transaction. Customers don't pay sales taxes on groceries when they also purchase toasters or children's toys as groceries (like intangibles) are exempt. It doesn't matter that the groceries are "value proceeding or accruing" the purchase of the toaster and the children's toys. To further belabor the point, a customer who buys a bushel of apples as well as an apple peeler and an apple juicer only pays sales taxes on the peeler and the juicer, and not on the apples. And this is the law in South Carolina and virtually every other state with a sales tax.

Hellerstein & Hellerstein, *State Taxation* discusses bundled transactions at length, although it primarily deals with the sale of tangible personal property and the sale of a service (and not intangible). Hellerstein §12.08 [1][c] accordingly states:

[c] Services Coupled With a Transfer of Separate Property

In deciding whether a transaction involves the sale of tangible personal property or the sale of services, courts sometimes confuse services that are *separate and apart from the property* transferred or licensed with services *that are embodied in the property*. One may illustrate this point by comparing two different types of transactions – the licensing of motion picture films by producers to exhibitors, and transactions engaged in by landscape designers. Motion picture producers employ a large amount of expensive talent in producing films, including directors, actors, and others. Since the results of such work are embodied in the films that

¹ Unprepared foods are exempt from sales taxes, section 12-36-2128(75).

are delivered to exhibitors, however, most states tax motion picture rentals as licenses to use tangible personal property.

Landscape designers also use services in preparing the land and planting trees, shrubs, and flowers. Although they transfer shrubs, trees, and plants to their customers, the services are not embodied in those articles in the typical case in which landscape designers purchase trees and shrubs from a nursery. The trees and shrubs are thus separate and apart from the services, except for the service involved in planting them, in contrast to the motion picture negative and prints, which embody the services. Consequently, if a landscape designer separates the price of the trees and shrubs from the planting and other service charges, the sales tax will apply only to the price of those articles. No sales tax will be payable on the general landscaping work or the planting of trees and shrubs.

South Carolina follows the rules stated in Hellerstein. As argued at length on pgs. 21-23 of Appellant's Initial Brief, South Carolina does not include service charges in the sales tax base. When Vets sell pricey dog food, Ophthalmologists sell eye glasses, jewelry repairmen sell jewelry, barbershops and beauty shops sell shampoos, undertakers sell caskets or interior decorators sell mirrors or curtains, sales tax is imposed on the tangible personal property and not on the services, even if they charged in the same transaction. And this is so regardless if it is all contained in one bill, i.e. the value proceeding or accruing from the sale of the mirrors and curtains includes interior decorating services. And it doesn't matter if they are "inextricably linked," i.e. the customer wouldn't have purchased the mirror or curtains but for the interior decorator's services, or the services constitute value proceeding or accruing the sale of tangible personal property.

Hellerstein, *Id.*, also notes:

Some courts have recognized that the "true object" test (whatever its merit) should be applied only to cases in which the services are embodied in the tangible article transferred to the buyer. A bankruptcy case involving a California sales tax assessed against a correspondence school raised that question. The taxpayer offered a large number of courses in drafting, electrical service, radio and television repair, and other trades. As part of each course, the student received books, printed lessons, and, where applicable,

training kits and tools. The taxpayer charged tuition for each course, without separate charges for such items.

The taxpayer contended:

that the true object of its contracts was the educational service rather than the personal property transferred, and that a single contract calling for both the rendition of services and the transfer of property cannot be taxable in part and nontaxable in part. Debtor argued that if the transaction is severed, the true object test would be rendered meaningless; it would no longer be necessary to determine the overall object of the mixed contract, as each part would then be treated separately.

The court disagreed:

The Debtor's reliance on the true object test is misplaced. The test is appropriate where the services rendered are inseparable from the property transferred that is, where the services, so to speak, find their way into the property. All the examples used in Regulation 1501 to illustrate the true object test involve transactions in which the services become an integral part of the property; e.g. the artist's skill and labor are embodied in his painting; the record keeping, tax, and similar services of a firm which performs business advisory services are embodied in the forms, binders, and other property transferred during the course of the transactions...

Thus, the true object test should be used where the services and the property are inseparable and is inapplicable where these two elements are distinct.

The correspondence school rendered services that were separate and apart from, and not embodied in, the books, lessons, or other tangible personal property provided. These services included grading examinations, monitoring the students' progress, and consulting with instructors by mail or telephone. The court sustained the tax only on the "deemed retail prices" of the property furnished to the students.

South Carolina follows this as well. Sales tax is imposed on the dog food, eye glasses, jewelry, shampoo, caskets, and mirrors. But the sales tax base only includes the tangible personal property and not the services.

Lastly, Hellerstein, *Id.*, discusses the bundled transaction further as follows:

Citing this treatise, the California Court of Appeal similarly distinguished between “mixed transactions” and transactions in which the nontaxable service or intangible is “inseparably bundled” with the taxable sale of tangible personal property. The case involved optional service contracts sold along with computer products for a single lump-sum price. When placing orders, however, customers could select from a menu of options either to “upgrade” or “downgrade” a standard package. For example, a typical computer purchase package might include a standard service contract in the lump-sum price, but the purchaser could opt out of the service and reduce the lump-sum price by a specified amount. Similarly, the purchaser could agree to increase the purchase price by a specified amount in order to extend the service contract time period or to receive premium services. The effect of these selections on the lump-sum price was identified to the consumer during the order process but was not separately stated on the final receipt or invoice.

The determinative inquiry, according to the court, was whether the transactions were bundled or mixed. If bundled, the entire lump sum would be a taxable sale of tangible personal property, assuming that the “true object” of the transaction could be found to be the sale of a computer product, as argued by both Dell and the SBE. If, however, the transactions were mixed, then “the separate elements of the transaction are analyzed as separate transactions for tax purposes. The tangible property aspect of the transaction is taxed and the service aspect of the transaction is not taxed.

Thus, the court held:

[T]he proper approach under California law is to tax the computer (tangible personal property) and not the service contract (service or intangible). As other courts have recognized, “when there is a fixed and an ascertainable relationship between the value of the article and the value of the services rendered, and each is a consequential element capable of a separate

and distinct transaction, then the elements must be analyzed as separate transactions for tax purposes.

This discussion is only partially on point, but it uses the same “inextricable link” as the DOR brief and the ALC decision. Our case does not involve the sale of tangible personal property and a related service, but rather the sale of tangible personal property and a completely separate intangible. The only link is that they are sometimes purchased in the same transaction.

A classic bundled transaction is found in SC Private Letter Ruling #92-5 wherein customers purchased a package deal for one price of a dinner theater consisting of a four-course meal and a “wild 1800’s” show. At issue was whether admissions and sales taxes were imposed on the entire ticket price. The PLR noted “there is not one true object, but two – the sale of a meal and the sale of entertainment. They are sold together, and one is not incidental to the other.” The PLR held that “ABC will only be required to remit the sales tax on that portion of the charge representing the price of the meal and the admissions tax on that portion of the charge representing the price of admission, provided the price breakdown is reasonable...” The former Tax Commission distinguished *Meyers Arnold* as follows:

In addition, ABC is distinguishable from the above cited cases and decision of *Meyers Arnold v. South Carolina Tax Commission, supra*; *Regency Towers Association, Inc. v. South Carolina Tax Commission* [maid service at hotel], *supra*; and Commission Decisions #90-38 and #91-64 [engraving charges as part of the sale of trophies]. These cases and decisions fall into the class of transactions whereby “the article sold is the substance of the transaction and the service rendered is merely incidental to and an inseparable part of the transfer to the purchaser of the article sold...” As such, “the vendor is engaged in the business of selling at retail, and the tax which he pays ... [is measured by the total cost of article and services].”

Accordingly, the value of the “wild 1880’s” service (or intangible) was not included in the sales tax base, notwithstanding that it appeared on the same ticket receipt, i.e. it was value

proceeding or accruing the sale, and was inextricably linked, i.e. you couldn't have one without the other.

To repeat, the above is a bit confusing – they all involve the sale of a service rather than the sale of an intangible but the issue is the same: should the cost of an intangible be included in the sales tax base of the tangible? Hellerstein and the DOR agree, each should be analyzed separately. Intangibles are exempt from sales taxes and the DOR concedes a membership card is an intangible.

3. The Department Fails to Distinguish between the Sales at Issue in this Case and Sales of Other Memberships.

The thrust of the ALC Order is as follows:

Customers pay the Membership Fee to obtain discounts and free shipping on their purchases of tangible personal property. Thus, the Membership Fee is a direct result of the sale of tangible personal property. But for the [Appellant]'s sale of tangible personal property, the Appellant's would not be able to sell Millionaire's Club memberships and, therefore, would not collect Membership Fees.

But the "direct result" test is not followed by the DOR. Chapter 6, page 9 of the DOR's South Carolina Sales and Use Tax Manual (2017 Ed.) states that sales of certain memberships are not included in the sales tax base.

Examples of charges not includable in "gross proceeds" or "sales price" *and therefore not subject to the sales and use tax* are:

* * *

Membership fees charged by a membership-only warehouse offering a selection of brand-name merchandise to business owners and others where all membership types receive the same benefits;⁵⁷

(emphasis added). In the very recent SC Private Letter Ruling #16-1, the DOR similarly stated:

In certain circumstances, the Department has determined that membership fees related to the anticipated sales of tangible personal property are not includable in gross proceeds of sales and, therefore, are not subject to the sales and use tax. Examples include:

1. A retailer sells its product only to members and charges a membership fee that allows all members to purchase the tangible personal property at the same lower price.

Books-A-Million offers a selection of brand-name merchandise to business owners and others where all membership types receive the same benefits. It does not have a “membership-only warehouse” but under the ALC’s “inextricable link” analysis, this would make it less subject to sales taxes than a “membership-only warehouse.”

One other DOR Policy document makes this plain. At issue in SC PLR #90-8 was

At what point, if at all, are transactions related to XYZ’s “Travel Program” program subject to the sales and accommodations taxes – upon sale of the travel points or upon their redemption?

XYZ Resorts Travel Company, as part of its “Travel Program”, was selling memberships to the general public in a travel club. Participants entered into an agreement with XYZ to purchase travel points, redeemable at the company’s various resort facilities, and with companies that have contracted with XYZ. The travel points were valid for five years and could be used, in lieu of cash, for overnight accommodations, meals, greens fees and various services. The points could also be used for automobile rentals and airline tickets.

The DOR held that the travel points were not subject to sales taxes *until redeemed*:

Here, the “consideration” is not the cost of the points in that, no transfer of tangible personal property or accommodations has taken place at the time the points are purchased.

The transfer (exchange, etc.) of tangible personal property or accommodations takes place when the travel points are redeemed. The original purchase price of the travel points is the value of the “consideration.”

The transactions that are subject to the sales and accommodations taxes are those in which travel points are redeemed for tangible personal property or accommodations.

4. The ALC's and Department's Reliance on *Meyers Arnold* is Misplaced.

The ALC Order holds that notwithstanding the lack of statutory language subjecting membership cards to sales tax, the amounts collected for membership cards become subject to sales tax as gross proceeds of sale because the membership card was sold in conjunction with the sale of tangible personal property. The ALC Order and Respondent's Brief principally relies on *Meyers Arnold v. S.C. Tax Commission*, 285 S.C. 303, 328, S.E.2d 920 (1985), in support of its contention. Respondent's Brief at p. 9 states:

One of the issues in *Meyers Arnold* involved whether lay away fees paid in conjunction with lay away sales of tangible personal property were includable in gross proceeds of sales. *Meyers Arnold*, 285 S.C. at 307, 328 S.E.2d at 923. In determining whether the lay away fees were includable in gross proceeds of sales, the Court reasoned that but for the lay away sales *Meyers Arnold* would not receive any lay away fees; therefore, the lay away fees were included in the gross proceeds of sales and subject to tax. *Id.* In more general terms, *Meyers Arnold* holds that if a taxpayer could not collect a fee but for the sale of tangible personal property, then that fee is includable in the taxpayer's gross proceeds of sales.

In *Meyers Arnold*, 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. *Id.* at 307, 303 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 304, 307, 303 S.E.2d at 921, 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 parties in *Meyers Arnold* entered into a Stipulation of Facts (Appellant's Correspondence to Judge McLeod dated May 26, 2017 Enclosing Proposed Order and Portions of *Meyers Arnold* Record at pp. 24-25; R. p. 92-3. The Stipulation stated in relevant part:

6. The customer selects the merchandise he desires to purchase and elects to pay the full price in cash or by charge and take delivery, or not pay the full price and not take delivery by paying for the item on the lay away plan. If the lay away plan is elected, Meyers Arnold agrees to hold the merchandise for a period of time, while the customer makes monthly payments on the account.

7. The customer makes payments, and when the purchase price has been paid in full, the customer is entitled to possession of the merchandise.

The Tax Commission ruled against the Taxpayer on this issue, stating:

The final issue concerns the taxability of the gross proceeds from layaway sales. If a customer wishes to make a purchase and pay for the item over a period of time, Meyers-Arnold provides a layaway plan in which the property is kept by the store and the customer makes periodic payments until the full purchase price is paid. Upon final payment, the customer receives the property. The customer pays a One Dollar, nonrefundable fee which is included on the layaway form as a separate charge.

We find that the lay-away fee of One Dollar is subject to the sales tax. The tax is measured against the gross proceeds of sales and §12-35-30 states that gross proceeds of sales mean the value proceeding from the sale of tangible personal property *and that no reduction shall be given for the cost of labor or service or any other expense whatsoever*. Here the One Dollar fee is to cover the cost of the layaway plan and is part of the gross proceeds of sales and no reduction of the gross proceeds is allowed. The One Dollar is charged on all layaway sales and is nonrefundable.

We find further support for our position in §12-35-120 which defines sales price as including any services that are a part of the sale. Here the One Dollar charge is made on all sales under the layaway plan and the evidence shows that a sale would not be made unless the One Dollar fee were charged. Thus the statutory definition of sales price requires the inclusion of the One Dollar since such charge is a required part of the sale. R. pp. 89-90.

The Tax Commission argued in its brief before the Court of Appeals that the charge was a service fee for the sale of merchandise, and thus taxable. On pp. 4-5 of its brief (Appellant's Correspondence to Judge McLeod dated May 26, 2017 Enclosing Proposed Order and Portions of *Meyers Arnold* Record at pp. 57-58; R. p. 125-26) the Tax Commission argued:

*The statutory definition specifically states that the value proceeding from the sales shall not be reduced by “any deduction on account of ***labor or service cost***or any other expenses whatsoever***.” Such a definition is very broad and includes the service of a lay-away plan provided by Meyers Arnold. The fee for the lay-away service is charged to cover additional expenses incurred by Meyers Arnold for such items as storage and additional paperwork associated with a sale on lay-away. Thus, if the lay-away fee is part of “the value proceeding or accruing from the sale,” then such fee is part of gross proceeds and may not be reduced by the expenses which the lay-away fee represents. (Emp. added).*

The Court of Appeals ruled in favor of the Tax Commission, stating:

The question which must be resolved is whether the lay away fee charged is part of the gross proceeds of sales.

Section 12-35-30 defines gross proceeds of sales as “the value proceeding or accruing from the sale of tangible personal property ... *without any deduction for service cost.*” But for the lay away sales, Meyers Arnold would not receive the lay away fees. The fees are obviously charged for the service rendered in making lay away sales. For these reasons, this court holds the lay away fees are part of the gross proceeds of sales and subject to the sales tax. (285 S.C. at 307, 328 S.E.2d at 923)(Emp. added).

Meyers Arnold simply follows the rules contained in section 12-36-90, gross proceeds includes “The proceeds from the sale of tangible personal property without any deduction for: The cost of materials, labor, or service” and section 12-36-130, “Sales price means the total amount for which tangible personal property is sold, without any deduction for the cost of the property sold, the cost of the materials used, labor or service cost, interest paid, losses, or any other expenses.” The DOR so describes *Meyers Arnold* in Chapter 6, pgs. 1-2 of its Sales and Tax Manual, as follows:

In calculating gross proceeds or sales price, the retailer may not deduct the following (whether or not such costs are passed on to the customer or separately stated on the bill to the customer):

- The cost of goods sold;
- The cost of materials, labor, or service;

One of the guiding principles of what is includable in “gross proceeds” was established in *Meyers Arnold, Inc. v. South Carolina Tax Commission*, 285 S.C. 303, 328 S.E.2d 920 (1985). In that case,

the Court of Appeals of South Carolina held the element of service involved in a lay away sale was subject to tax as being part of the sale of tangible personal property. The test used by the court was as follows:

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

Accordingly, the total amount charged in conjunction with the sale or purchase of tangible personal property is subject to the tax. This test used by the court would also apply this principle to the use tax in determining what is includable in "sales price."

The DOR similarly describes it in SC PLR #92-5:

In addition, ABC is distinguishable from the above cited cases and decision of *Meyers Arnold v. South Carolina Tax Commission, supra*; *Regency Towers Association, Inc. v. South Carolina Tax Commission* [maid service at hotel], *supra*; and Commission Decisions #90-38 and #91-64 [engraving charges as part of the sale of trophies]. These cases and decisions fall into the class of transactions whereby "*the article sold is the substance of the transaction and the service rendered is merely incidental to and an inseparable part of the transfer to the purchaser of the article sold...*" As such, "the vendor is engaged in the business of selling at retail, and the tax which he pays ... [is measured by the total cost of article and services]." (Emp. added).

This rule is simply designed to prevent gaming or reduction of the sales tax base as follows:

Suppose Brooks Brothers sells a \$1200 suit with the bill as follows:

Suit - \$800

Tailoring - \$200

Cost of materials - \$200

The sales tax base is \$1200 – not \$800.

Your cell phone bill is chock full of add-ons. Your bill states:

Cell phone service - \$200

Regulatory recovery - \$100

Telecommunication taxes are imposed on the \$300 – not the \$200. Filling stations could bill as follows:

Gallon of gas - \$1.10

Environmental recovery - \$0.60

Gas taxes would be imposed on \$1.70 – not \$1.10. Alternatively, if the filling station customer paid for beer, snacks and gasoline, he would pay alcohol taxes on the beer, gas taxes on the gas, and sales taxes on the snack – notwithstanding that the gas and beer were value accruing or proceeding the purchase of the snack. Each would be analyzed separately at the cash register.

5. Inextricably Linked

As stated above, the ALC Order is premised on the notion that sales of Memberships are “inextricably linked” to sales of tangible personal property. Membership fees are not subject to sales taxes even if they “are inextricably linked to the sale of tangible personal property.” With the exception of certain statutory exceptions, unrelated services, like intangibles, are not subject to sales taxes even when they are performed in connection with the sale of tangible personal property. Even the DOR concedes that many services which are inextricably linked to the sale of tangible personal property are not included in the sales tax base.

B. The ALC Erred in Holding that Renewals of Memberships are Subject to Sales Taxes.

As stated above, renewals of memberships are generally automatic (unless either the customer or the store cancels the membership). Such renewals are not inextricably linked to the sale of merchandise nor are they value proceeding or accruing from the sale of tangible personal property. Accordingly, renewals would not be included in the sales tax base even if the original membership purchase was so included. Neither the ALC Order nor Respondent’s Brief argue that

renewals are subject to sales tax. 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.

C. The ALC Erred in Holding that the Statutes are Not Ambiguous.

In the context of a tax statute, it is a settled rule that ambiguities are resolved “against the government and in favor of the taxpayer.”

At the oral argument in this case, the Department could provide no rationale 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. The Department’s attorney plainly stated at the Oral Argument:

But again, we have to look at the factual differences between a membership only warehouse where you’re paying just to get into the door and the petitioner where your membership gets you discounted tangible personal property. And it gets back to whether there is an inextricable link. Is there really an inextricable link between paying

what's basically like an admission fee to get into the door from that tangible personal property? Maybe, maybe not. But the Department determined in its policies that there was not an inextricable link between those two and therefore that example wasn't subject to sales tax. *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.* But again, there's no analysis in our policy documents, so we don't really know where the Department drew that factual distinction. But it really comes down to in this case, is there an inextricable link between a membership that gives you discounted tangible personal property and the tangible personal property? R. p. 419, line 17 – p. 420, line 18.

The Department's brief simply states, "The Department's exclusion of membership fees of certain membership-only warehouses from gross proceeds of sales is irrelevant as these facts are not before the Court. Moreover, the fact that the application of different sets of facts to the statutory language may result in different outcomes does not render the statute ambiguous." The only different set of facts is that Sam's Club/Costco memberships are mandatory and Appellant's are optional. Where do the two sets of statutes include optional memberships and exclude mandatory? Obviously, a mandatory membership is more inextricably linked than an optional membership.

III. CONCLUSION

Walmart is the largest retailer in the United States. Walmart sells taxable goods, exempt goods (groceries) and services (optician services, services performed by pharmacy). A person who purchases groceries (exempt unprepared food), a crock pot to cook the groceries, and an eye exam at Walmart is charged sales taxes only on the crock pot, regardless of whether they are rung up in the same transaction at the cash register. It doesn't matter if the groceries were value proceeding or accruing the purchase of the crock pot or if the purchases were inextricably linked.

The Department is correct – sections 12-36-90 and 12-36-130 are plain and unambiguous. Both only tax intangibles "as are specifically provided for in this chapter" (section 12-35-140) and

neither tax intangible membership cards. And certainly neither exempt “warehouse-only” membership clubs but tax optional memberships. No basis exists to exempt membership only warehouses which are indeed inextricably linked to retail purchases and tax optional membership cards. *Meyers Arnold* simply stands for the proposition that you can’t 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 proposition that the purchase of an entirely separate intangible is included in the sales tax base.

As stated in Appellant’s initial brief, sales of memberships in the United States is huge. Many retailers, including museums and art galleries, offer discounts to those who purchase optional memberships. Are they all required to add membership fees when one purchases a discounted item at e.g. Riverbanks Zoo gift shop?



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February 26, 2018
Columbia, South Carolina

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THE STATE OF SOUTH CAROLINA
In the Court of Appeals

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APPEAL FROM THE ADMINISTRATIVE LAW COURT

SC Court of Appeals

John D. McLeod, Administrative Law Judge

Case No. 16-ALJ-17-0113-CC
Appellate Case No. 2017-001519

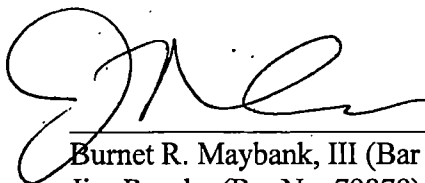
Books-A-Million, Inc.....Appellant,

v.

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

CERTIFICATE OF COUNSEL

The undersigned certifies that this **Final Reply Brief of Appellant** complies with Rule 211(b), SCACR.



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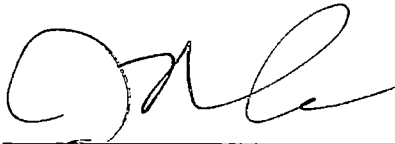
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South Carolina Department of Revenue.....Respondent.

PROOF OF SERVICE

I certify that I served the **Final Reply Brief of Appellant** on the Respondent by depositing copies of it in the United States Mail, postage prepaid, on February 26, 2018 addressed to their attorneys of record as follows:

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February 26, 2018

**THE STATE OF SOUTH CAROLINA
In The Court of Appeals**

Books-A-Million, Inc., Appellant,

v.

South Carolina Department of Revenue, Respondent.

Appellate Case No. 2017-001519

Appeal From The Administrative Law Court
John D. McLeod, Administrative Law Judge

Opinion No. Op. 5721
Heard March 9, 2020 – Filed April 29, 2020

AFFIRMED

Burnet Rhett Maybank, III, and James Peter Rourke, of
Nexsen Pruet, LLC, of Columbia, for Appellant.

Sean Gordon Ryan and Adam J. Neil, of Columbia, for
Respondent.

THOMAS, J.: In this case arising from a sales tax audit by the South Carolina Department of Revenue (SCDOR), Books-A-Million, Inc. (BAM) appeals from the order of the Administrative Law Court (ALC) that upheld SCDOR's assessment of taxes, penalties, and interest against BAM for BAM's failure to include sales of the Millionaire's Club Memberships (Club Memberships) in BAM's gross proceeds of sales. BAM argues the ALC erred in finding (1) the amounts collected by BAM

for Club Memberships are subject to sales tax; (2) renewals of Club Memberships are subject to sales tax; and (3) the statutes are not ambiguous. We affirm.

FACTS

BAM operates a discount book retail business headquartered in Birmingham, Alabama. BAM sells books, magazines, collectible supplies, cards, and other gifts in retail stores throughout the country and online. BAM operates thirteen retail locations in South Carolina. Customers pay a \$25 annual fee (Membership Fee) to belong to the Millionaire's Club (the Club). Customers can pay the Membership Fee separately or along with other store purchases. Club Memberships expire one year from the date of payment of the Membership Fee, unless the membership is automatically renewed. 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. 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. BAM does not charge sales tax on the cost of the Membership Fee.

On December 11, 2014, SCDOR informed BAM by letter that its sales and use tax returns for January 1, 2012, to August 31, 2015, were selected for audit. BAM provided SCDOR copies of its income statements for the audited periods. SCDOR's auditor compared BAM's gross proceeds of sales from the income statements to the gross proceeds of sales reported on BAM's sales and use tax returns.

During the audit, SCDOR discovered BAM was not charging sales tax on the cost of Membership Fees. Thus, on September 16, 2015, SCDOR issued a Proposed Notice of Assessment (PNOA) to BAM in the amount of \$242,076.97, due for sales tax on the cost of Membership Fees for the audited periods (including \$15,703.13 in interest and \$63.14 in penalties). The amounts listed in the PNOA resulted from adjustments caused by applying sales tax to the cost of Membership Fees. BAM timely objected to the PNOA by letter dated December 14, 2015, and SCDOR issued its determination on the matter on March 15, 2016.

BAM requested a contested case hearing before the ALC, challenging SCDOR's final determination. The sole issue before the ALC was whether the proceeds from BAM's South Carolina sales of Club Memberships were subject to sales taxes and

should have been included in BAM's gross proceeds of sales. Both parties filed motions for summary judgment, agreeing there were no material facts in dispute but disagreeing as to the application of the law to the undisputed facts. Prior to the hearing before the ALC, the parties filed stipulations of fact.

A hearing was held before the ALC on May 9, 2017. The ALC issued its order on June 1, 2017; however, on June 6, 2017, the ALC issued an order vacating its June 1 order and amending its order granting SCDOR's motion for summary judgment. BAM filed a motion for reconsideration, which was denied. This appeal follows.

STANDARD OF REVIEW

The Administrative Procedures Act provides our standard of review in an appeal from the ALC. *Schwiers v. S.C. Dep't of Health & Env'tl. Control*, 429 S.C. 43, 48, 837 S.E.2d 730, 733 (Ct. App. 2019). Section § 1-23-610(B) of the South Carolina Code provides this court must confine our analysis to the record, and we may reverse or modify the decision if the substantive rights of the petitioner have been prejudiced because the finding, conclusion, or decision is:

- (a) in violation of constitutional or statutory provisions;
- (b) in excess of the statutory authority of the agency;
- (c) made upon unlawful procedure;
- (d) affected by other error of law;
- (e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record; or
- (f) arbitrary or capricious or characterized by an abuse of discretion or clearly unwarranted exercise of discretion.

S.C. Code Ann. § 1-23-610(B) (Supp. 2019). "In determining whether the decision of the ALC was supported by substantial evidence, a reviewing court 'need only find, looking at the entire record on appeal, evidence from which reasonable minds could reach the same conclusion as the ALC.'" *Schwiers*, 429 S.C. at 49, 837 S.E.2d at 733 (quoting *Kiawah Dev. Partners, II v. S.C. Dep't of Health & Env'tl.*

Control, 411 S.C. 16, 28, 766 S.E.2d 707, 715 (2014)). "However, the [c]ourt may reverse the decision of ALC where it is in violation of a statutory provision or it is affected by an error of law." *Kiawah Dev. Partners, II*, 411 S.C. at 28, 766 S.E.2d at 715.

LAW/ANALYSIS

I. Club Membership Sales

BAM argues the ALC erred in finding the amounts collected by BAM for Club Memberships are subject to sales tax. We disagree.

Under South Carolina law, "[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." S.C. Code Ann. § 12-36-910(A) (2014).¹ For sales and use tax purposes, the term "person" "includes any individual, firm, partnership, limited liability company, association, corporation, receiver, trustee, any group or combination acting as a unit, the State, any state agency, any instrumentality, authority, political subdivision, or municipality." S.C. Code Ann. § 12-36-30 (2014). "Gross proceeds of sales, or any similar term, means the value proceeding or accruing from the sale . . . of tangible personal property." S.C. Code Ann. § 12-36-90 (2014). "Tangible personal property" is defined as "personal property which may be seen, weighed, measured, felt, touched, or which is in any other manner perceptible to the senses. It also includes services and intangibles . . . the sale or use of which is subject to tax under this chapter . . ." S.C. Code Ann. § 12-36-60 (2014). "It is presumed that all gross proceeds are subject to the tax until the contrary is established. The burden of proof that the sale of tangible personal property is not a sale at retail is on the seller." S.C. Code Ann. § 12-36-950 (2014).

When "an agency charged with administering a statute or regulation has interpreted the statute or regulation, courts, including the ALC, will defer to the agency's interpretation absent compelling reasons." *Kiawah Dev. Partners, II*, 411 S.C. at 34, 766 S.E.2d at 718. This court defers to an agency's interpretation of a statute

¹ Section 12-36-1110 imposed an additional one percent sales tax as of June 1, 2007. S.C. Code Ann. § 12-36-1110 (2014).

"unless it is 'arbitrary, capricious, or manifestly contrary to the statute.'" *Id.* at 34-35, 766 S.E.2d at 718 (quoting *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837, 844 (1984)).

At the hearing before the ALC, SCDOR argued a plain reading of the statute demonstrated that all persons engaged in the sale of tangible personal property at retail are liable for sales tax on their gross proceeds of sales. BAM argued sections 12-36-910(A) and 12-36-90 only imposed a sales tax on the gross proceeds of the sale of tangible personal property.

The ALC found BAM's argument failed to apply the plain meaning rule. Instead, the ALC found BAM's reading of the statute required the deletion of the words "persons engaged in the business of." Also, it found BAM's reading required deleting the phrase "proceeding or accruing" from the statute. The ALC stated, "A reading of a statute that requires eliminating words within the statute is not reasonable and does not comport with the plain meaning rule." The ALC further stated:

If [BAM] . . . were to stop selling tangible personal property, its [Club Membership] would not be able to survive as the [Club Membership] only exists as a means to provide discounts on BAM's sales 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.* Thus, I conclude [BAM] is in the business of selling tangible personal property at retail, and [BAM's] business is subject to South Carolina sales tax. (Emphasis added.).

The ALC continued:

When applying the plain meaning rule to the words in the statute, it is clear that *the statute is broad and encompasses the total value of a sale, not simply the amount paid for tangible personal property.* Moreover, a review of the case law demonstrates that gross proceeds of sales can include the value of services and intangibles

that are derived from the sale of tangible personal property. . . . Therefore, I agree with [SCDOR] and conclude that gross proceeds of sales includes all value that comes from or is direct result of the sale, lease, or rental of tangible personal property, including proceeds from fees related to incidental services, intangibles, or other benefits. (Emphasis added.).

The ALC considered two South Carolina cases in making its decision. In *Travelscape, LLC v. South Carolina Department of Revenue*, 391 S.C. 89, 97, 705 S.E.2d 28, 32 (2011), *Travelscape* contended it was not required to pay sales tax on the service and facilitation fees it retained from online hotel reservations because such fees were "derived from" the services it provided, not from the rental charge for the hotel room. Our supreme court found the fees charged by *Travelscape* for its services were subject to sales tax under the plain language of section 12-36-920(A) as gross proceeds because the service was merely incidental to the purchase of the accommodations and the cost of services is specifically included in the definition of gross proceeds of sales. *Id.* at 98, 705 S.E.2d at 33.

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 Arnold would not receive the lay away [sic] fees. The fees are obviously charged for the service rendered in making lay away [sic] sales." *Id.* Thus, this court held the layaway fees were part of the gross proceeds of sales and subject to the sales tax. *Id.*

The ALC also considered two Administrative Law Court cases in making its decision. In *Textile Restoration Services, Inc. v. South Carolina Department of Revenue*, 2015 WL 7443800, at *4 (S.C. Admin. Law Ct. Nov. 12, 2015), the court found SCDOR properly included charges for repairing, altering, storing, pick-up, and delivery of items incident to the dry cleaning service in the taxpayer's gross proceeds of sales. In *Tronco's Catering, Inc. v. South Carolina Department of Revenue*, 2010 WL 5781622, at *3 (S.C. Admin. Law Ct. Apr. 12, 2010), 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." "The statute further expressly states that the value of the sale must include costs for materials, labor, service, transportation, or for any

other expense." *Id.* "When the terms of a statute are clear and unambiguous, as they are here, there is no room for construction and the terms must be given their literal meaning." *Id.*

The ALC in this case concluded, "South Carolina case law demonstrates that gross proceeds of sales includes all value that comes from or is a direct result of the sale, lease, or rental of tangible personal property." Its order stated:

Customers pay the Membership Fee to obtain discounts and free shipping on their purchases of tangible personal property. Thus, the Membership Fee is a direct result of the sale of tangible personal property. But for [BAM's] sale of tangible personal property, [BAM] would not be able to sell [Club Memberships] and, therefore, would not collect Membership Fees. The Membership Fees are payment for services or benefits that are incident to the sale of tangible personal property. Moreover, the Membership Fees are inextricably linked to, and incapable of being separated from, the sale of tangible personal property.

Thus, the ALC held BAM's Club Membership Fees are includable in BAM's gross proceeds of sales and are subject to sales tax.

On appeal, BAM argues under the plain meaning of section 12-36-910, the Membership Fees collected by BAM are not subject to sales tax because Club Memberships are not tangible personal property under section 12-36-60, and therefore the Membership Fees cannot constitute gross proceeds of sales under section 12-36-90. BAM argues this case is distinguishable from *Meyers Arnold* and *Travelscape*:

The facts in *Meyers Arnold* and *Travelscape* . . . both involve the imposition of sales tax on fees charged by a retailer providing a service where the fees were inextricably intertwined with the sale of specific tangible personal property or accommodations. In *Meyers Arnold*, the customer could not purchase the lay away [sic] merchandise without paying the subject fee.

Likewise, in *Travelscape*, the customer could not purchase the accommodation without paying the fee. The charge for layaway/service fee in each case occurs only after the purchase of the underlying tangible personal property. In addition, neither customer would only pay the fee—presumably, neither taxpayer could charge only the fee, since that fee is so inextricably linked to the underlying purchase of tangible personal property or services.

BAM also cites to other states' cases interpreting their tax statutes in support of its argument. One of these cases is *Barnes & Noble Superstores, Inc. v. Huddleston*, 1996 WL 596955 (Tenn. Ct. App. Oct. 18, 1996). In that case, the Tennessee Commissioner of Revenue appealed from the trial court's grant of summary judgment in favor of Barnes & Noble. *Id.* at *1. The primary issue on appeal was whether Barnes & Noble's sale of \$10 annual membership cards, entitling the members to merchandise discounts, was subject to Tennessee sales tax. *Id.* The Commissioner's position was that the cards themselves were tangible personal property subject to sales tax, and payment of the \$10 fee constituted prepayment for merchandise because Barnes & Noble customers were in effect applying \$10 towards the later purchase of inventory. *Id.* At that time, Tennessee statute section 67-6-102(28) (1994) defined "tangible personal property" as personal property that "may be seen, weighed, measured, felt, or touched, or is in any other manner perceptible to the senses." *Id.* at *2. The court looked to the "language of the statute in order to ascertain and effectuate the intent of the General Assembly," and noted "[i]t is a general rule of construction that sales and use taxes will not be extended by implication beyond the clear import of the language used and will not be enlarged to embrace matters not specifically named." *Id.* The court then held the membership sales were not subject to taxation because the "true object of the subject transactions between [Barnes & Noble] and its customers is to bestow upon club members the intangible right to receive a discount on merchandise." *Id.* Further, "[t]he membership card is merely an indicia of that intangible right and incidentally aids in the exercise of that right." *Id.*

However, this court does not have to follow other states' interpretations of their tax laws in interpreting our own tax laws. *See State Farm Mut. Auto. Ins. Co. v. Goyeneche*, 429 S.C. 211, 224, 837 S.E.2d 910, 917 (Ct. App. 2019) ("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) ("The decisions of courts from other jurisdictions are, of course, only persuasive authority."); *cf. Widenhouse v. Colson*, 405 S.C. 55, 59 n.2, 747 S.E.2d 188, 191 n.2 (2013) (noting a state is not "required to defer to another state's judgment regarding 'the disposition or devolution of realty' in the forum state" (quoting *Williams v. State of North Carolina*, 317 U.S. 287, 294 n.5 (1942)), or required "to apply the law of another state in an action in its own courts" (citing *Magnolia Petroleum Co. v. Hunt*, 320 U.S. 430, 436-37 (1943))).

BAM also argues its Club Membership is similar to the purchase of gift cards and membership-only warehouses, which are not subject to sales tax in South Carolina. BAM points out SCDOR has determined the sale of prepaid telephone cards are not subject to sales tax at the time of sale if they are for use with a landline; however, they are subject to sales tax at the time of sale if they are for use with a mobile phone. S.C. Rev. Rul. 04-4. In a 2004 ruling, the SCDOR held:

The sale or recharge at retail of a *prepaid telephone calling card* . . . 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. *The taxable transaction takes place when the telephone calling card is used. . . .* The provider of the local telephone call is liable for the 5% sales tax on local calls made with the calling card.

...

The sale or recharge at retail of a *prepaid telephone calling card* for use in making local, long distance, or international telephone calls . . . that can only be used with a *wireless phone* or other wireless device, *is subject to South Carolina sales tax at the time of purchase.*

S.C. Rev. Rul. 04-4 (emphasis added). That ruling further states: "Other similar nontaxable transactions include the sale of gift certificates or traveler's checks. The taxable transaction occurs at the time the gift certificate or traveler's check is redeemed." BAM cites to SCDOR's South Carolina Sales and Use Tax Manual (2017 Ed.), chapter 6, page 9, which provides that "[m]embership fees charged by a membership-only warehouse offering a selection of brand-name merchandise to business owners and others where all membership types receive the same benefits" are not subject to the sales tax or use tax. The manual states in a footnote to the membership-only warehouse exemption that

A membership fee would be includable in gross proceeds and subject to the tax if the membership fee is the sales price for the tangible personal property. For example, if a direct mail movie rental company charged an annual or month[ly] fee to receive movies for short term use of movies and no other charges are paid by the customers to receive the movies, then the annual or monthly fee is the sales price of the tangible personal property and subject to the tax.

After reviewing the record, we find the decision of the ALC was supported by substantial evidence. 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. Thus, the ALC did not err in finding the amounts collected by BAM for Club Memberships are subject to sales tax.

II. Club Membership Renewals

BAM argues the ALC erred in finding renewals of Club Memberships are subject to sales tax. We disagree.

Because we find the ALC correctly determined sales of Club Memberships are subject to sales tax, we also find the ALC correctly determined renewals of Club Memberships are also subject to sales tax. *See Hagood v. Sommerville*, 362 S.C. 191, 199, 607 S.E.2d 707, 711 (2005) (declining to address an issue when the resolution of a prior issue is dispositive).

III. Ambiguous Statutes

BAM argues the ALC erred in finding the statutes are not ambiguous. We disagree.

"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). Courts "must give the words found in the statute their 'plain and ordinary meaning without resort to subtle or forced construction to limit or expand the statute's operation.'" *CFRE, LLC v. Greenville Cty. Assessor*, 395 S.C. 67, 74, 716 S.E.2d 877, 881 (2011) (quoting *Sloan*, 371 S.C. at 499, 640 S.E.2d at 459). "Thus if the words are unambiguous, we must apply their literal meaning." *Id.* at 74, 716 S.E.2d at 459; *Beach v. Livingston*, 248 S.C. 135, 139, 149 S.E.2d 328, 330 (1966) ("The language of a tax statute must be given its plain ordinary meaning in the absence of an ambiguity therein."). "The interpretation of a statute is a question of law reviewed de novo." *S.C. Dep't of Transp. v. Powell*, 424 S.C. 206, 210, 818 S.E.2d 433, 435 (2018).

At the hearing before the ALC, BAM argued sections 12-36-910(A) and 12-36-90 were ambiguous and should be construed in favor of the taxpayer. The ALC found BAM failed to point to any ambiguity in either section. Thus, the ALC concluded sections 12-36-910(A) and 12-36-90 were unambiguous, and the plain meaning rule applied. The ALC found the application of the plain meaning rule to the terms in the statutes at issue demonstrated the Membership Fees were includable in BAM's gross proceeds of sales and subject to sales tax.

On appeal, BAM again argues the statutes are ambiguous regarding whether optional membership fees are included in the sales tax base, and such ambiguity must be resolved in favor of the taxpayer.

S.C. Code Ann. § 12-36-910(A) (2014) states "[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." S.C. Code Ann. § 12-36-90 (2014) provides "[g]ross proceeds of sales, or any similar term, means the value proceeding or accruing from the sale, lease, or rental of tangible personal property."

Based on our review, we find the language of the statutes is not ambiguous, and the ALC's reading of the statutes was correct and consistent with the intent of the legislature. Thus, the ALC did not err in finding the statutes are not ambiguous.

CONCLUSION

Accordingly, the decision of the ALC is

AFFIRMED.

HUFF and MCDONALD, JJ., concur.

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT

John D. McLeod, Administrative Law Judge

Case No. 16-ALJ-17-0113-CC
Appellate Case No. 2017-001519

RECEIVED
MAY 14 2020
SC Court of Appeals

Books-A-Million, Inc. Appellant,

v.

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

APPELLANT BOOKS-A-MILLION, INC.'S PETITION FOR REHEARING

INTRODUCTION

Pursuant to Rule 221(a) of the South Carolina Appellate Court Rules, Books-A-Million, Inc. ("BAM") seeks rehearing of the Court's opinion in the above-captioned case filed on April 29, 2020. As explained below, the Court overlooked and misapprehended several things when it ruled that, as a matter of law, that BAM was liable for sales taxes on the sale of memberships as well as the renewal of memberships.

BRIEF FACTUAL SUMMARY

BAM operates a discount book retail business. BAM sells books, magazine, collectible supplies, cards, and other gifts in retail stores throughout the country and online. BAM operates thirteen retail locations in South Carolina. Customers pay a \$25 annual fee (“Membership Fee”) to belong to the Millionaire’s Club (the “Club”). Customers can pay the Membership Fee separately or along with other store purchases. Club Memberships expire one year from the date of payment of the Membership Fee, unless the membership is automatically renewed. 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. If customers do not opt out, BAM bills the annual Membership Fee to the credit or debit care provided when the customer initially enrolled in the Club. BAM does not charge sales tax on the cost of either the Membership Fee or the renewals.

Both the ALC and the Court of Appeals’ decision held that both the Membership Fees and the renewals are subject to sales taxes.

ARGUMENT

I. The Amounts Collected by BAM are not Subject to Sales Taxes Issue

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 South Carolina Sales Tax Act (§ 12-36-10 *et seq.*). (Intangible property is not subject to sales tax (an exclusion) as the Act only taxes tangible personal property.) The Sales Tax Act also contains numerous exemptions. Are all the exemptions overridden in a bundled transaction if one item is subject to sale taxes and the others are not?

Section 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. 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). 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 \$10 million, as the M&E is value proceeding or accruing from the purchase of non-exempt material handling equipment. (In our example, purchased from same vendor in the same transaction, all included in one invoice.) And in this example, M&E is an exempted item – the burden of proof falls on the taxpayer to establish the exemption, whereas in BAM's 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.

A ridiculous example? (“Lawyer Maybank, you ain’t gonna convince the Court with absurd examples!”) No – 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 approvingly by the Court of Appeals – held in *Tronco* that the rental of real property was included in the sales tax base! 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 expanded the sales tax limitation of tangible personal property to include real property, just as the Court of Appeals has expanded the limitation in this case to include intangibles.

II. Renewal of Memberships Issue

The Court of Appeals erred in holding that the sale of an intangible—the renewal of a membership fee twelve months after the sale of tangible personal property—is subject to sales tax. The General Assembly states that consideration “proceeding or accruing from the sale... of tangible personal property” is included in the sales tax base. § 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”.)

III. Walmart/Costco are not Subject to Sales Taxes – But BAM is - The Statutes are Ambiguous Issue

The General Assembly, by adoption of the Sales Tax Act, has not once mentioned the taxation of membership fees, other than to exclude intangibles. The Sales Tax Act is silent.

The Department in a policy document states that membership fees by a member-only warehouse is exempt from the sales tax base. *See* South Carolina Sales and Use Tax Manual (2017 ed.), chapter 6, at 9. Accordingly, WalMart (Sam's Club) and Costco are exempt from sales tax on their sale of membership fees – but BAM is not. And where does the Sales Tax Act give WalMart and Costco a huge (up to 9%, considering state and local sales taxes) competitive advantage over retailers offering voluntary membership programs?

The Court of Appeals' decision does not address the WalMart/Costco competitive advantage, other than to 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. 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 49 (emphasis in original). 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 than that.

The Court of Appeals' decision also notes:

In *Myers 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 Arnold would not receive the law away [sic] fees. The fees are obviously charged for the service rendered in making lay away [sic] sales.

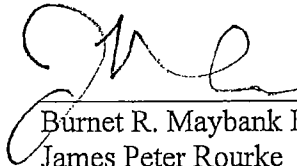
Id. at 50. “But for” the sale of tangible personal property, neither Sam's Club nor Costco could sell memberships.

The 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 Club/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 Comms., Inc. v. S.C. Dep't of Rev.*, 399 S.C. 313, 321, 731 S.E.2d 869, 873 (2012).

CONCLUSION

For all of the above reasons, Appellant requests that its Petition for Rehearing be granted and that the Court rehear and amend its decision.

Respectfully submitted this 13th day of May, 2020.



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THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT

John D. McLeod, Administrative Law Judge

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Respondent.


PROOF OF SERVICE

This is to certify that the foregoing Appellant's Petition for Rehearing was sent via US

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The South Carolina Court of Appeals

Books-A-Million, Inc., Appellant,

v.

South Carolina Department of Revenue, Respondent.

Appellate Case No. 2017-001519

ORDER

After careful consideration of the petition for rehearing, the Court is unable to discover that any material fact or principle of law has been either overlooked or disregarded, and hence, there is no basis for granting a rehearing. Accordingly, the petition for rehearing is denied.

Thomas C. Luff

J.

Paul W. Thomas

J.

Stephen P. McDonald

J.

Columbia, South Carolina

cc:
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FILED

July 14, 2020

Adam J. Neil, Esquire
The Honorable John D. McLeod