
State of South Carolina
Department of Revenue
300A Outlet Pointe Blvd., Columbia, South Carolina 29210
P.O. Box 125, Columbia, South Carolina 29214

SC PRIVATE LETTER RULING #13-2

SUBJECT: Hospital Communications System
Rental of Tangible Personal Property or a Service
(Sales and Use Tax)

REFERENCES: S.C. Code Ann. Section 12-36-910 (2000, Supp. 2011)
S.C. Code Ann. Section 12-36-1110 (Supp. 2011)
S.C. Code Ann. Section 12-36-60 (2000)
S.C. Code Ann. Section 12-36-110 (2000)
S.C. Code Ann. Section 12-36-70 (2000)
S.C. Reg. 117-308.8 (Supp. 2011)

AUTHORITY: S. C. Code Ann. Section 12-4-320 (2000)
S. C. Code Ann. Section 1-23-10(4) (2005)
SC Revenue Procedure #09-3

SCOPE: A Private Letter Ruling is an advisory opinion issued to a specific taxpayer by the Department to apply principles of law to a specific set of facts or a particular tax situation. It is the Department's opinion limited to the specific facts set forth, and is binding on agency personnel only with respect to the person to whom it was issued and only until superseded or modified by a change in statute, regulation, court decision, or another Departmental advisory opinion, providing the representations made in the request reflect an accurate statement of the material facts and the transaction was carried out as proposed.

Question:

Are the charges by ABC Communications, Inc. ("ABC") to a hospital, nursing home, or similar institution (hereinafter "hospitals") for its XYZ System and services, as described in the facts, subject to the sales and use tax?

Conclusion:

The charges by ABC to hospitals for its XYZ System and services, as described in the facts, are subject to the sales and use tax because the "true object" of the transaction is the retail lease of tangible personal property.

The hospital is the user and consumer of the monitoring equipment provided by ABC as part of its Primary Package for the use of monitoring patients. Similarly, the hospital is also the user and consumer of the equipment provided by ABC as part of its Shared Revenue Package for patient use as part of the professional medical care provided by the hospital. As such, the tax is based on the total “gross proceeds of sales” of the Product and Services Agreement, as described in the facts, unless otherwise exempt by South Carolina Law.

However, the charges by ABC to hospitals for installation of monitoring equipment are excluded from the tax base where: (1) ABC separately states charges for installation on the billing to the hospital and (2) maintains proper books and records of account that show the installation charges are reasonable in relation to charges to lease such equipment.

Facts:

ABC, pursuant to its Products and Services Agreement, contracts with hospitals to provide the XYZ System and services. The XYZ System and services consists of two packages- the Primary Package and the Shared Revenue Package.

The Primary Package consists of the following:

Product 1 monitors and records bedside activity in the patient’s room.

Product 2 allows Authorized Users to view monitored rooms from the Nurse’s Station.

Product 3 enables the admitting physicians and non-physician staff members to view their patients from any personal computer.

Product 4 allows the Hospital to activate a safety module that will notify the nursing station when a patient exits a defined area in the patient room.

Product 5 monitors and records activity in any area of the Hospital that the Hospital would desire security cameras to be placed.

The Shared Revenue Package consists of the following:

Product 6 enables patients to allow family members and friends to monitor and videoconference with them in their private rooms.

Product 7 allows the patient access to the Internet using the wireless keyboard and the television in the room or personal laptop computers. While ABC provides the equipment to access the internet, hospitals provide actual access to the internet.

Product 8 allows the patient, family and/or friends access to a wide selection of movies for their viewing pleasure while they are in their Hospital room.

Product 9 allows mothers to view their newborn child from their Hospital bed while the baby is in the Nursery or Neo-Natal Intensive Care Unit.

In order to use the XYZ System, ABC installs equipment, which consists of room communication platforms, monitoring stations, head-end control servers, cameras, and software. While ABC provides the equipment necessary for monitoring, it does not offer the service of actually monitoring patient rooms, waiting rooms, or common areas.

ABC is responsible for installation, product upgrades, service, repair, and training. The hospital is responsible for providing appropriate connection to the internet. ABC retains title to the equipment installed at the hospital and the customer retains exclusive ownership of the data and video contained in the equipment.

As part of ABC's Products and Services Agreement, hospitals pay a certain contracted fee for its Primary Package. Regarding the Shared Revenue Package, ABC's Products and Services Agreement provides that hospitals share the revenue obtained from providing patients with these products with ABC.

Discussion:

Code Section 12-36-910(A) imposes a sales tax and reads:

A sales tax, equal to [six]¹ 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.

Code Section 12-36-1310(A) imposes a use tax and reads:

A use tax is imposed on the storage, use, or other consumption in this State of tangible personal property purchased at retail for storage, use, or other consumption in this State, at the rate of [six]² percent of the sales price of the property, regardless of whether the retailer is or is not engaged in business in this State.

Code Section 12-36-60 defines "tangible personal property" as:

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

¹ Code Section 12-36-1110 increased the sales and use tax rate by 1% beginning June 1, 2007.

² See footnote #1.

Thus for sales or use tax to apply, there must be a retail sale or purchase of tangible personal property. Code Section 12-36-100 provides definitions for the terms “sale” and “purchase.” This section states:

“Sale” and “purchase” mean any transfer, exchange, or barter, conditional or otherwise, of tangible personal property for a consideration including:

- (1) a transaction in which possession of tangible personal property is transferred but the seller retains title as security for payment, including installment and credit sales;
- (2) a rental, lease, or other form of agreement;
- (3) a license, lease, or other form of agreement;
- (4) a transfer of title or possession, or both.

Based on the above, a sale for sales and use tax purposes includes any rental, lease, license to use or other form of agreement.

At times a further inquiry is required to determine if the transaction is a sale or rental of tangible personal property versus the furnishing of a service. The so-called "true object" test is generally used to delineate sales of services from sales of tangible personal property.

The "true object" test is best described in 9 *Vanderbilt Law Review* 231 (1956) as:

The true test then is one of basic purpose of the buyer. When the product of the service is not of value to anyone other than the purchaser, either because of the confidential character of the product, or because it is prepared to fit the purchaser's special need - a contract or will prepared by a lawyer, or the accident investigation report prepared for an insurance company - this fact is evidence tending to show that the service is the real purpose of the contract. When the purpose of a contract is to produce an article which is the true object of the agreement, the final transfer of the product should be a sale, regardless of the fact that special skills and knowledge go into its production. Under this analysis, printing work, done on special order and of significant value only to the particular customer, is still a sale. The purchaser is interested in the product of the services of the printer, not in the services per se. Similarly, it would seem that contracts for custom-produced articles, be they intrinsically valuable or not, should be classified as sales when the product of the contract is transferred.

The *Vanderbilt Law Review* article, citing *Snite v Department of Revenue*, 398 Ill. 41, 74 N.E.2d. 877 (1947), also establishes the following general rule:

If the article sold has no value to the purchaser except as a result of services rendered by the vendor, and the transfer of the article to the purchaser is an actual and necessary part of the services rendered, then the vendor is engaged in the business of rendering service, and not in the business of selling at retail. If 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, then 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]. If the service rendered in connection with an article does not enhance its value and there is a fixed or ascertainable relation between the value of the article and the value of the service rendered in connection therewith, then the vendor is engaged in the business of selling at retail, and also engaged in the business of furnishing service, and is subject to tax as to the one business and tax exempt as to the other.

While the above quotes do not establish rigid rules, they do provide general guidance in determining the purpose of a transaction as in this case.

Regarding certain medical facilities, South Carolina Regulation 117-308.8 states, in pertinent part:

Hospitals, infirmaries, sanitariums, nursing homes and like institutions are engaged primarily in the business of rendering services. They are not liable for the sales tax with respect to their gross proceeds or receipts from meals, bandages, dressings, drugs, x-ray photographs and other tangible personal property where such property is used in the rendering of the primary medical service to patients. This is true irrespective of whether or not such tangible items are billed separately to their patients. Hospitals, infirmaries, sanitariums, nursing homes and like institutions are deemed to be the users or consumers of such tangible personal property and the instate sellers of these items are required to report and remit the tax due on the sale of such property to the hospitals, infirmaries, sanitariums, nursing homes, and like institutions or in case of out-of-state purchases, use tax shall be reported and remitted by the purchaser.

Where drugs, prosthetic devices and other supplies are furnished to their patients as a part of the medical service rendered, such hospitals, infirmaries, sanitariums, nursing homes and like institutions are deemed to be users or consumers of such drugs, prosthetic devices and other supplies.

Based on the above, the transaction between ABC and hospitals is a retail lease of tangible personal property.

The next question then is what is the basis on which the tax is imposed? As stated previously, the basis of sales tax is “gross proceeds of sales,” and the basis of use tax is the “sales price.” Section 12-36-90 defines “gross proceeds of sales” as “the value proceeding or accruing from the sale, lease, or rental of tangible personal property. . . .” It includes the proceeds from the sale without any deduction for: (1) the cost of goods sold; (2) the cost of materials, labor, or service; (3) interest paid; (4) losses; (5) transportation costs; (6) manufacturers or importers excise taxes

imposed by the United States; or (7) any other expenses. Section 12-36-130 defines “sales price” as “the total amount for which tangible personal property is sold, without any deduction for the cost of the property sold, the cost of the materials used, labor or service cost, interest paid, losses, or any other expenses. . . .”

In Meyers Arnold, Inc. v. South Carolina Tax Commission, 285 S.C. 303, 328 S.E.2d 920, 923 (1985), the South Carolina Court of Appeals 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....(Emphasis added).

Thus, the tax is based on the total “gross proceeds of sales” of the Product and Services Agreement, as described in the facts. Here, as described in the facts, because the “true object” of the transaction is the retail lease of tangible personal property (the XYZ System and services) the charges are subject to the sales and use tax.

The hospital is the user and consumer of the monitoring equipment provided by ABC as part of its Primary Package for the use of monitoring patients. Similarly the hospital is the user and consumer of the equipment provided by ABC as part of its Shared Revenue Package for patient use as part of the professional medical care provided by the hospital. Thus, the tax is based on the total “gross proceeds of sales” of the Product and Services Agreement, as described in the facts, unless otherwise exempt by South Carolina Law.

However, South Carolina Regulation 117-313.3 excludes from the tax base, charges to install tangible personal property provided: (1) “such charges are separately stated from the sales price of the property on billing to customers; and (2) the seller’s books and records of account show the reasonableness of such labor in relation to the sales price of the property.”

SOUTH CAROLINA DEPARTMENT OF REVENUE

s/William M. Blume, Jr.
William M. Blume, Jr., Director

April 16 _____, 2013
Columbia, South Carolina