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State of South Carolina  
**Department of Revenue**  
301 Gervais Street, P. O. Box 125, Columbia, South Carolina 29214

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SC Private Letter Ruling #97-5  
(TAX)

TO: XYZ, Inc.

SUBJECT: Security System  
(Sales and Use Tax)

DATE: September 18, 1997

REFERENCE: S. C. Code Ann. Section 12-36-910 (Supp. 1996)  
S. C. Code Ann. Section 12-36-1310 (Supp. 1996)  
S. C. Code Ann. Section 12-36-60 (Supp. 1996)  
S. C. Code Ann. Section 12-36-110 (Supp. 1996)  
S. C. Code Ann. Section 12-36-100 (Supp. 1996)

AUTHORITY: S. C. Code Ann. Section 12-4-320 (Supp. 1996)  
SC Revenue Procedure #94-1

SCOPE: A Private Letter Ruling is an official advisory opinion issued by the Department of Revenue to a specific person.

NOTE: A Private Letter Ruling may only be relied upon by the person to whom it is issued and only for the transaction or transactions to which it relates. A Private Letter Ruling has no precedential value.

Questions:

1. Are the monthly fees paid by a customer to XYZ, Inc. ("XYZ") for equipment and for electronically monitoring the customer's business for the purpose of burglary and fire protection subject to the sales and use taxes?
2. Are charges by XYZ to install the equipment subject to the sales and use taxes?
3. Are charges by XYZ to repair the equipment subject to the sales and use taxes?

Conclusions:

## **1. EQUIPMENT AND MONITORING**

**XYZ SELLS THE EQUIPMENT:** The sale by XYZ of the equipment is subject to the sales and use tax; however, the periodic charges by XYZ for the monitoring service are not for the access to, or use of, a communication system and are therefore not subject to the tax under Code Sections 12-36-910(B)(3) and 12-36-1310(B)(3).

**XYZ RETAINS TITLE TO THE EQUIPMENT:** The periodic charges by XYZ for the use of the equipment constitute sales of tangible personal property (transfers of possession, licenses to use, or rentals or other forms of agreement) that are subject to the sales and use tax. The separate periodic charges for the monitoring service are not for the access to, or use of, a communication system and are therefore not subject to the tax under Code Sections 12-36-910(B)(3) and 12-36-1310(B)(3).

## **2. INSTALLATION CHARGES**

Charges by XYZ to install the equipment are not subject to the sales and use taxes provided such charges are separately stated from the sales price of the property on the bills to customers and provided that XYZ's books and records of account show the reasonableness of such labor in relation to the sales price of the property.

## **3. REPAIR CHARGES**

Repair charges are addressed in Regulation 117-174.192. Based on this regulation, the following outlines the application of the tax to repairs made by XYZ.

### **XYZ SELLS THE EQUIPMENT**

With respect to security equipment sold to customers, the tax applies as follows:

1. If XYZ charges customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job, then these charges are subject to the tax. However, installation charges by XYZ with respect to these repair materials are not subject to the tax provided these charges are separately stated from the sales price of the property on billing to the customer and are reasonable.
2. If XYZ never charges customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job, then the tax is due at the time these materials are sold to or purchased by XYZ.

3. If XYZ charges some customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job and does not charge other customers, then XYZ may purchase all such material at wholesale and the tax is due at the time it charges the customer for the repair material or at the time it withdraws such material from inventory for the “no charge” repair. However, tax is not due on the withdrawal of the material for the “no charge” repair if XYZ is replacing a defective part under a written warranty contract provided the warranty contract was (at the time of the original purchase of the defective property) given without charge, the tax was paid on the sale of the defective part or on the sale of the property of which the defective part was a component, and the warrantee is not charged for any labor or materials (See Code Section 12-36-110.).
4. If XYZ uses repair materials that (a) do not pass to the customer or (b) that pass to the customer but lose their identity or are only incidental to the repair job, then the tax is due at the time these materials are sold to or purchased by XYZ.

### **XYZ RETAINS TITLE TO THE EQUIPMENT**

With respect to security equipment rented to customers the tax applies as follows:

1. If XYZ charges customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job, then these charges are subject to the tax. However, installation charges by XYZ with respect to these repair materials are not subject to the tax provided these charges are separately stated from the sales price of the property on billing to the customer and are reasonable.
2. If XYZ does not charge customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job, then XYZ may purchase such materials at wholesale. Such materials are considered to be resold by XYZ to the customer as part of the monthly rental for the equipment (Tax is due on the monthly rental charge for the equipment.).
3. If XYZ charges some customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job and does not charge other customers, then XYZ may purchase all such material at wholesale and the tax is due at the time it sells the repair material to the customer. Repair material for which XYZ does not charge customers and that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job are considered to be resold by XYZ to the customer as part of the monthly rental for the equipment (see item 3 above). Tax is due on the monthly rental charge for the equipment.

4. If XYZ uses repair materials that (a) do not pass to the customer or (b) that pass to the customer but lose their identity or are only incidental to the repair job, then the tax is due at the time these materials are sold to or purchased by XYZ.

Facts:

XYZ provides security services and monitoring services to commercial customers. The security system generally consists of a video transmitter, closed circuit television (“CCTV”) cameras, sensors, motion detectors, an alarm, control panel, keypad and electrical wiring.

The security system will be connected to a remote visual command center. XYZ provides remote video monitoring services from its Visual Command Center located outside the state.

The basic remote interactive video system involves CCTV cameras installed at remote locations. A video transmitter is integrated with the CCTV system which has the ability to dial-up the remote Visual Command Center. This dial-up function will be activated either by the Visual Command Center or by an alarm triggered at the site.

Remote interactive video not only provides the communication of video to outside locations but simultaneous two-way audio as well.

XYZ will provide commercial customers with both security system and monitoring services for a stated fee. The system will be either sold to customers or provided for specified period of time (service contracts).

Under the term of a service contract, title to the security system remains with XYZ. Service contracts are anticipated to be from three to five years, and the customer will have the option of renewing indefinitely. At the end of the service contract, the system will be returned to XYZ. Monitoring services will be for an expected contract term of three to five years. Service contract customers will only obtain the right to use the system for the period during which the monitoring services are being provided.

Service contract customers will be billed on a monthly, quarterly, or semiannual basis. Each billing will include separately stated charges for the use of the system and a monitoring service.

The question has arisen as to whether the monthly fees charged by XYZ are subject to the State sales and use taxes.

Discussion:

## **EQUIPMENT AND MONITORING**

This matter is similar to one addressed by the department in SC Technical Advice Memorandum #95-1. However, XYZ is distinguishable in that a specific charge is assessed the customer each payment period for use of the equipment under contracts in which XYZ retains title of the equipment. Based on these facts, the department will provide guidance for the following scenarios:

1. XYZ sells the equipment and provides the monitoring service, and
2. XYZ retains title to the equipment and the billing to the customer includes separately stated charges for the use of the system and a monitoring service.

### **XYZ SELLS THE EQUIPMENT**

There are two transactions involved in this example. The customer is first seeking monitoring services for security purposes. After the customer has decided to purchase the monitoring services, he must then determine if it is better to purchase the equipment or use XYZ's equipment.

With respect to the monitoring services, we must determine if the periodic charges for the monitoring services are subject to the sales and use tax.

The "sale or use of [communications] is subject to tax under [Chapter 36]" pursuant to Code Sections 12-36-910(B)(3) and 12-36-1310(B)(3), which impose the tax on the:

gross proceeds accruing or proceeding from the charges for the ways or means for the transmission of the voice or messages, including the charges for use of equipment furnished by the seller or supplier of the ways or means for the transmission of the voice or messages; . . .

In reviewing various communication issues in the past, the Department has concluded that charges for the ways or means of communication must be charges for access to, or use of, a communication system, whether this charge is based on a fee per specific time period or per transmission.

Since the periodic charges by XYZ are not for access to, or use of, a communication system, such charges are not subject to the tax under Code Sections 12-36-910(B)(3) and 12-36-1310(B)(3).

With respect to the second transaction, the purchase of the equipment, Code Section 12-36-910(A) is applicable and reads:

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. (Emphasis added.)

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 five percent of the sales price of the property, regardless of whether the retailer is or is not engaged in business in this State. (Emphasis added.)

Code Section 12-36-60 defines the term "tangible personal property" to mean:

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

Therefore, for the 5% sales or use taxes to apply, there must be a retail sale or retail purchase of tangible personal property.

Code Section 12-36-110 defines the terms "sale at retail" and "retail sale," in part, as follows:

Sale at retail and retail sale mean all sales of tangible personal property except those defined as wholesale sales. The quantity or sales price of goods sold is immaterial in determining if a sale is at retail.

Therefore, the sale by XYZ of the equipment is subject to the sales and use tax.

### **XYZ RETAINS TITLE TO THE EQUIPMENT**

In this example, XYZ charges the customer two fees on each bill - one for the monitoring service and one for use of the equipment.

The statutory provisions cited above also apply to this example. In other words, there are also two transactions involved. The customer is first seeking monitoring services for security purposes. After the customer has decided to purchase the monitoring services, he

must then determine if it is better to purchase the equipment or use XYZ's equipment.

As stated above, since the periodic charges by XYZ are not for the access to, or use of, a communication system, such charges are not subject to the tax under Code Sections 12-36-910(B)(3) and 12-36-1310(B)(3).

Now we must consider the periodic charge for use of the equipment. This is a sale under South Carolina law. Code Section 12-36-100 reads:

“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 to use or consume: and
- (4) a transfer of title or possession, or both.

Based on this definition and the previously cited statutory provisions, the charge for the use of the equipment constitutes a transfer of possession, a license to use, or a rental or other form of agreement that is subject to the sales and use tax. As stated earlier, the separate charge for the monitoring service is not subject to the sales and use tax.

## **INSTALLATION CHARGES**

Regulation 117-174.204 addresses the issue of installation charges. The regulation states:

Not subject to the sales or use tax are charges for installation incident to the sale of tangible personal property when such charges are separately stated from the sales price of the property on billing to customers and provided the seller's books and records of account show the reasonableness of such labor in relation to the sales price of the property.

Based on the above, an installation charge by XYZ is not subject to the tax with respect to equipment sold (see Code Section 12-36-100) provided the charge is separately stated from the sales price of the property on billing to the customer and it is reasonable.

## **REPAIR CHARGES**

Repair charges are addressed in Regulation 117-174.192 which reads:

Materials used in repairing, for tax purposes, fall into the following classes:

- (a) Materials which pass to the repairman's customers and which do not lose their identity when used by the repairman and which are a substantial part of their repair job (such as auto repair parts, radio tubes, and condensers) are sold at retail by the repairman. He must report sales tax on such sales, including tax on the service incidental thereto. He may, however, if making separate agreements to sell the repair parts and to perform labor and service required, remit tax only upon the price of the parts if his records and his invoices clearly show a separation of the amounts received from sales of parts and from the rendering of services.
- (b) Materials which pass to the repairman's customers but which lose their identity when used by the repairman or which are inconsequential in amount; such as paint, solder, and tack; are considered to have been used or consumed by the repairman and are taxable at the time of sale to him.
- (c) Materials which are used or consumed by the repairman and which do not pass on to his customers are supplies and taxable when sold to the repairman.
- (d) Materials which fall in class (b) or (c) are purchased at wholesale for use by a repairman who, in addition to using such materials as a repairman, sells the same kind of materials for use by others. These materials become subject to the sales tax upon their withdrawals for use by the repairman. Note, however, that a repairman is not considered a vendor unless he carries a stock of goods and sells outright therefrom a substantial amount. If the repairman makes only isolated sales or "accommodation" sales, he is not to be licensed as a seller under the sales tax law, in which case his supplier is liable for the tax.

In all instances materials are taxable when sold to repairmen for use in making repairs where such materials lose their identity as a result of such use. For instance, solder used in welding, paint used in automobile refinishing, thread used in mending clothes, cloth used in reupholstering. In all instances where the shape or composition of the repair material is materially changed, such altered or changed material is considered to have been used or consumed by the repairman, and, for that reason, subject to tax when sold to him. No tax on this material is to be collected by the repairman from his customer.

In instances where repair materials and repair parts are passed to the repairman's customers without charge, except necessary and customary minor adjustments, such parts or materials may be purchased at wholesale by the repairman licensed under the Sales Tax Law. The repairman is then liable for sales tax on such sales of materials and parts to his customers.

Based on this regulation, the following outlines the application of the tax to repairs made by XYZ.

### **XYZ SELLS THE EQUIPMENT**

With respect to security equipment sold to customers, the tax applies as follows:

1. If XYZ charges customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job, then these charges are subject to the tax. However, installation charges by XYZ with respect to these repair materials are not subject to the tax provided these charges are separately stated from the sales price of the property on billing to the customer and are reasonable.
2. If XYZ does not charge customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job, then the tax is due at the time these materials are sold to or purchased by XYZ.
3. If XYZ charges some customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job and does not charge other customers, then XYZ may purchase all such material at wholesale and remit the tax at the time it charges the customer for the repair material or at the time it withdraws such material from inventory for the "no charge" repair. However, tax is not due on the withdrawal of the material for the "no charge" repair if XYZ is replacing a defective part under a written warranty contract provided the warranty contract was (at the time of the original purchase of the defective property) given without charge, the tax was paid on the sale of the defective part or on the sale of the property of which the defective part was a component, and the warrantee is not charged for any labor or materials.
4. If XYZ uses repair materials that (a) do not pass to the customer or (b) that pass to the customer but lose their identity or are only incidental to the repair job, then the tax is due at the time these materials are sold to or purchased by XYZ.

## **XYZ RETAINS TITLE TO THE EQUIPMENT**

With respect to security equipment rented to customers the tax applies as follows:

1. If XYZ charges customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job, then these charges are subject to the tax. However, installation charges by XYZ with respect to these repair materials are not subject to the tax provided these charges are separately stated from the sales price of the property on billing to the customer and are reasonable.
2. If XYZ does not charge customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job, then XYZ may purchase such materials at wholesale. Such materials are considered to be resold by XYZ to the customer as part of the monthly rental for the equipment.
3. If XYZ charges some customers for repair materials that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job and does not charge other customers, then XYZ may purchase all such material at wholesale and remit the tax at the time it sells the repair material to the customer. Repair material for which XYZ does not charge customers and that pass to the customer, that do not lose their identity, and that are a substantial part of the repair job are considered to be resold by XYZ to the customer as part of the monthly rental for the equipment (see item 3 above).
4. If XYZ uses repair materials that (a) do not pass to the customer or (b) that pass to the customer but lose their identity or are only incidental to the repair job, then the tax is due at the time these materials are sold to or purchased by XYZ.