



SC PRIVATE LETTER RULING #89-11

TO: ABC Authority

SUBJECT: Exemption
(Sales and Use Tax)

REFERENCE: S.C. Code Ann. Section 13-17-20 (Supp. 1988)
S.C. Code Ann. Section 13-17-90 (Supp. 1988)
S.C. Code Ann. Section 12-35-110 (Supp. 1988)
S.C. Code Ann. Section 12-35-170 (1976)
S.C. Code Ann. Section 12-35-550 (42) (Supp. 1988)

AUTHORITY: S.C. Code Ann. Section 12-3-170 (1976)
SC Revenue Procedure #87-3

SCOPE: A Private Letter Ruling is a temporary document issued to a taxpayer, upon request, and it applies only to the specific facts or circumstances related in the request. Private Letter Rulings have no precedential value and are not intended for general distribution.

Questions:

1. Are sales of tangible personal property ("direct items of cost") to the ABC Authority ("ABC"), for the so-called "RAMP" program, subject to the sales tax, pursuant to Code Section 12-35-510?
2. Are purchases of tangible personal property ("direct items of cost") by ABC, for the "RAMP" Program, subject to the use tax, pursuant to Code Section 12-35-810?

Facts:

The ABC Authority ("Authority") was created by the General Assembly per Act No. 50, effective April 29, 1983, as a public corporation.

The Authority's primary purpose is stated in Code Section 13-17-20, which reads, in part:

The authority is organized to enhance the research capabilities of the State's public and private universities, to establish a continuing forum to foster greater dialogue throughout the research community within the State, and to promote the development of high technology industries and research facilities in South Carolina.

To accomplish its objectives, the Authority operates through two divisions.

The Research Parks Division, using land donated by the State and acquired by the Authority, initiates and oversees development of parks to be used by private industry for research and development purposes. The 1983 Act required the Authority to establish three parks, initially; one each near Clemson University, the Medical University of South Carolina and the University of South Carolina. The Authority may establish and operate additional research parks as determined by the board of trustees. The Authority is responsible for all decisions and operations of these parks.

The Technology Management Division's purpose is to attract research companies to South Carolina to conduct research via subcontract agreements with the Authority. The first such project is the RAMP (Rapid Acquisition of Manufactured Parts) program, a \$90 million program, for the Navy. The RAMP program is for the purpose of developing and implementing technology for manufacture of replacement parts for Navy ships and aircraft; and is the focus of this document.

To accomplish the objectives of the RAMP program, ABC has created a consortium, consisting of several independent corporations. The consortium members utilize office/working space provided by ABC, at its facilities near Charleston, South Carolina.

Tangible personal property, which is purchased by ABC for the RAMP program, consists of computer hardware, software and manufacturing equipment. The consortium, under the umbrella of ABC, configures the aforementioned items into so-called "cells". Upon approval by the Navy, these "cells" are turned over, as a unit, to the Navy for use in manufacturing repair parts.

The RAMP contract, by reference, includes Federal Acquisition Regulation ("FAR") 52.245-5. The portion of FAR 52.245-5, germane to the questions at hand, reads:

- (2) Title to all property purchased by the Contractor [SCRA] for which the Contractor is entitled to be reimbursed as a direct item of cost under this contract shall pass to and vest in the Government upon the vendor's delivery of such property (emphasis added).

"Direct items of cost", as opposed to "indirect items of cost", are those items directly attributable to the RAMP program and subsequently turned over to the Navy (computer hardware, software and manufacturing equipment, or "cells"). This document does not address those items retained by ABC and/or not directly attributable to the RAMP program.

Discussion:

To answer the questions at hand, it is necessary to examine the sales and use tax statutes, case law, and the contract between ABC and the Navy.

1. SALES TAX

S.C. Code Section 12-35-510 imposes upon every person selling at retail a sales tax in an amount equal to five percent of "gross proceeds of sales".

The term "sale at retail" or "retail sale" is defined at Code Section 12-35-110, in part, as "all sales of tangible personal property except those defined in this article as wholesale sales" (emphasis added).

"Sale" is defined at Code Section 12-35-100, in part, as "[a]ny transfer exchange or barter, ..., of tangible personal property for a consideration" (emphasis added). Further, per Edisto Fleets, Inc. v. South Carolina Tax Commission, 256 SC 350, 182 SE2d 713 (1971), "[t]he terms 'sale' and 'purchase' are inextricably related and bound together and must be so construed". Code Section 12-35-70 defines "purchase", in part, as "acquired for a consideration, whether...effected by a transfer of title or of possession, or of both, ..." (emphasis added).

Code Section 12-35-550 contains certain exemptions from the sales tax. Paragraph (42) of that section exempts "[t]he gross proceeds of the sale of tangible personal property to the Federal Government...".

A California Second District Court of Appeals case, Lockheed Aircraft v. State Board of Equalization, 146 Cal. Rptr. 283 (1987), dealt with an analogous situation.

In Lockheed, Lockheed Aircraft Corporation and Aerojet-General Corporation acquired or manufactured special test equipment used for conducting functional tests of certain aircraft, torpedoes, related components and subsystems. The items being tested were manufactured by Lockheed and Aerojet for the federal government; and, the State of California sought to impose the sales or use tax on the purchase/use of the test equipment.

As with the contract between ABC and the Navy, the contracts in Lockheed provided title to the test equipment vested with the federal government, upon being acquired or produced by Lockheed and Aerojet.

The California sales tax statutes are very similar to South Carolina's. More specifically, the sales tax is imposed upon retailers selling tangible personal property at retail; "sale" is defined as "[a]ny transfer of title or possession...for a consideration"; "retail sale" does not include sales for resale (wholesale); and, sales to the federal government are exempt.

The Court, in Lockheed, concluded that the transactions between Lockheed and Aerojet and their suppliers were sales for resale, thereby excluded from being taxed. Furthermore, subsequent transfers of the test equipment to the federal government constituted exempt retail sales.

In Day & Zimmermann, Inc. v. Calvert 519 SW2d 106, cert den 423 US 832, 46 L ED 2d 50, 96 S CT 54, the Texas Supreme Court dealt with a similar situation. In that case, it was ruled:

...it is clear that the initial purchases by Day & Zimmermann were not taxable under the "Sale for Resale" exemption. Art. 20-04(0). Additionally, the second sale between Day & Zimmermann and the Federal Government is also exempt under both articles 20.04(C) and (H) since they are sales the State is "prohibited from taxing under the Constitution or laws of the United States or under the Constitution of this State"; and constitute "the receipts from the sale, ... of any taxable items to, ... [t]he United States, its unincorporated agencies and instrumentalities."

Also, in Industrial Vendors, Inc. v. Burts, 151 SE2d 867, a sales tax case involving a contract between the Charleston Naval Station and a vending machine company, the Supreme Court of South Carolina ruled:

This type contract appears to be in general use at military installations. The theory is that when the merchandise is placed in the machines, a sale to the governmental agency for resale is effected, and that the retail sales from the machines are made by the governmental agency. Hence, no South Carolina sales tax is incurred. The Tax Commission concedes that sales under this type contract are tax exempt.

2. USE TAX

The use tax is imposed at Code Section 12-35-810 upon "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...".

"Storage" is defined at Code Section 12-35-130, in part, as "any keeping or retention in this State, for any purpose except sale in the regular course of business..., of tangible personal property purchased at retail".

The term "use" is defined at Code Section 12-35-160 as:

...the exercise of any right or power over tangible personal property incident to the ownership of that property or by any transaction in which possession is given, except that it shall not include the sale of that property in the regular course of business.

Lockheed, also dealt with the imposition of the use tax. The State of California sought to impose the use tax based on the argument that the federal government took a mere legal title and Lockheed and

Aerojet retained the essential indicia of ownership, such as possession, use, and risk of loss".

However, the court rejected this argument as "sale" is defined as any transfer of title or possession. The Court reasoned "that a sale is contemplated even when something less than all indicia of ownership are transferred".

Also, the definition of "use" precluded imposition of the use tax. The California Statute defines the term, in part, as "the exercise of any right or power over tangible personal property incident to the ownership of that property...except...sale of that property in the regular course of business: (emphasis added).

It was ruled, since title vested in the federal government, Lockheed and Aerojet did not own the test equipment; and, also, the equipment was for sale "in the regular course of business".

Likewise, the Court ruled "storage", as contemplated in the statute, had not occurred. The key phrase being, as in the definition of "use", "except sale in the regular course of business".

Conclusions:

1. Sales of tangible personal property ("direct items of cost") to the ABC Authority ("ABC"), for the so-called "RAMP" program, are not subject to the sales tax, pursuant to Code Section 12-35-510.
2. Purchases of tangible personal property ("direct items of cost") by ABC, for the "RAMP" program, are not subject to the use tax, pursuant to Code Section 12-35-810.

SOUTH CAROLINA TAX COMMISSION

s/S. Hunter Howard Jr.

S. Hunter Howard, Jr., Chairman

s/A. Crawford Clarkson Jr.

A. Crawford Clarkson, Jr., Commissioner

s/T. R. McConnell

T. R. McConnell, Commissioner

Columbia, South Carolina
May 31, 1989