



301 Gervais Street, P.O. Box 125, Columbia, South Carolina 29214

SC PRIVATE LETTER RULING #90-12

TO: XYZ Associates

TAX MANAGER: John P. McCormack

SUBJECT: U.S. Army Watercraft Program
(Sales and Use)

REFERENCE: S.C. Code Ann. Section 12-36-910(A) (As Amended June, 1990)
S.C. Code Ann. Section 12-36-1310(A) (As Amended June, 1990)
S.C. Code Ann. Section 12-36-1330(A) (As Amended June, 1990)
S.C. Code Ann. Section 12-36-2130(1) (As Amended June, 1990)
S.C. Code Ann. Section 12-36-110 (As Amended June, 1990)
S.C. Code Ann. Section 12-36-120(1) (As Amended June, 1990)
S.C. Code Ann. Section 12-36-100 (As Amended June, 1990)
S.C. Code Ann. Section 12-36-2120(2) (As Amended June, 1990)

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 to, or purchases by, XYZ Associates of "end-item hardware" subject to the sales and use tax?
2. Are transfers by XYZ Associates to the federal government of "end-item hardware" exempt from the tax pursuant to Code Section 12-36-2120(2)?
3. Are sales to XYZ Associates of "end-item hardware", which they then sell to other retailers, subject to the sales tax?

Facts:

XYZ Associates ("XYZ") has a "cost-plus-fixed-fee" contract with the U.S. Army to operate, maintain and support a facility known as the ABC Storage Activity ("Activity"). The purpose of

the Activity is to repair U.S. Army amphibians, watercraft, causeway systems and parts and components thereof. The program is known as the U.S. Army Watercraft Program.

The question at hand concerns one aspect of XYZ's contract with the Army. Specifically, we have been asked to address the taxing of transactions concerning "end-item hardware". "End-item hardware" are the supplies necessary to maintain small Army watercraft such as rafts or landing crafts, and may include such items as flares, fire extinguishers, life jackets, and various other supplies. These items are purchased by XYZ and assembled into kits. An example of a kit may be all the supplies of a raft (i.e.: oars, rations, first aid supplies, and life jackets).

XYZ submits that some "kits" are installed by them; some are shipped to other retailers under contract with the federal government, for subsequent installation; and, others are installed by the Army. XYZ is presently paying the sales or use tax on purchases of all items in question.

In addition, an examination of XYZ's contract with the federal government reveals the following pertinent information:

c. Section I, page 16, incorporates, by reference, Federal Acquisition Regulation ("FAR") 52.245-5, "Government Property (Cost-reimbursement, Time-and-Material, or Labor-Hour Contracts)". Section (c)(3) of the FAR reads, in part, "[t]itle to all property purchased by the contractor for which the Contractor is entitled to be reimbursed as a direct item of cost under this contract and...is to vest in the Government, shall pass to and vest in the Government upon the vendor's delivery of such property".

Discussion:

Code Section 12-36-910(A) imposes the sales tax, 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.

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

An 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 consumption in this State, at the rate of five percent of the sales price of the property,

Further, Code Section 12-36-1330(A) reads, in part:

Every person storing, using or otherwise consuming in this State tangible personal property purchased at retail is liable for the use tax....

Code Section 12-36-2130(1) exempts from the use tax:

property the gross proceeds of sales of which are required to be included in the measure of the tax imposed by the provisions of Article 9 of this chapter [sales tax] and on which the [sales] tax has been paid by its seller or retailer.

In summary, the sales tax is imposed upon retail sales made in the State and the use tax is imposed on property used, stored, or consumed upon which the sales tax has not been paid.

Furthermore, the term "sale at retail" is defined at Code Section 12-36-110, in part, as, "...all sales of tangible personal property except those defined in this article as wholesale sales". A wholesale sale is defined in Code Section 12-36-120(1) as a sale of "tangible personal property to licensed retail merchants, jobbers, dealers or other wholesalers for resale, and do not include sales to users or consumers;..."

Code Section 12-36-100 defines the terms "sale" and "purchase", and 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.

In summary a sale occurs with the transfer of 1) title, 2) possession, or 3) title and possession of tangible personal property for a consideration.

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 to the facts in question in determining when a sale occurs.

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 XYZ and the U.S. Army, 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.

Furthermore, Code Section 12-36-2120(2) exempts from the sales and use tax the gross proceeds of the sales, or sales price of :tangible personal property sold to the federal government; ...

As stated in the "Facts", XYZ's contract with the federal government reveals that "[t]itle to all property purchased by [XYZ] for which [XYZ] is entitled to be reimbursed as a direct item of cost under this contract and...is to vest in the Government, shall pass to and vest in the Government upon the vendor's delivery of such property".

Conclusions:

1. Sales to, or purchases by, XYZ Associates of "end-item hardware" are not subject to the sales and use tax, as such constitute wholesale sales of tangible personal property pursuant to Code Section 12-36-120. Such "end-item hardware" are being resold to the U.S. Army.
2. Transfers by XYZ Associates to the federal government of "end-item hardware" qualify as retail sales or retail sales and installation, and are exempt from the tax pursuant to Code Section 12-36-2120(2).
3. Sales to XYZ Associates of "end-item" hardware, which they then sell to other retailers for resale, qualify as wholesale sales and are not subject to the sales tax. Sales by XYZ Associates of "end-item" hardware to other retailers under contract with the federal government, which they use to repair U.S. Army watercraft or sell to the federal government under contracts similar to XYZ's, are also not subject to sales and use tax, as such sales qualify as wholesale sales or exempt retail sales.

Note: This ruling applies only to the sale or purchase of "end-item hardware" subject to the provisions of Federal Acquisition Regulation ("FAR") 52.245-5.

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
August 14, 1990