Georgia Letter Ruling Number: LR SUT-2019-01
Topic: Service Providers
Date Issued: May 21, 2019

This letter is in response to your request for guidance on the application of Georgia sales and use tax in transactions involving the use of tangible personal property in connection with the delivery of services.

Facts Presented by Taxpayer

[Redacted], ("Taxpayer") is in the energy-saving business. It utilizes its proven [Redacted]("Platform") to generate net energy savings for its customers. Through its technology, Taxpayer's services improve a building efficiency (electricity, gas, steam, etc.) which drives immediate cost savings; improves customer and employee experiences; and reduces its customer's emissions and waste. Similar to energy (production) as a service, customers are attracted to Taxpayer's services because customers achieve net operating expense reductions, without upfront capital, while tracking the energy cost reductions via Taxpayer's platform.

Business Model – Taxpayer installs its platform in each of its prospective customer's facilities to evaluate the various options to reduce energy consumption. Taxpayer then installs equipment to reduce energy consumption and enters into service contracts with its customers for identified saved energy (i.e. electricity in KWh). As a component of the service agreement, Taxpayer owns and maintains the equipment for the life of the agreement and replaces any malfunctioning equipment at no cost to the customer.

Using its platform, Taxpayer measures the actual amount of energy saved due to the efficiency retrofit. Taxpayer then shares in the savings generated by charging a fixed rate per unit saved (kilowatt hours, etc.) that is predetermined, typically at a discount to its customer's utility rate. Taxpayer's technology can easily scale across technologies and facilities for each customer.

In other words, for each new customer, Taxpayer:

(1) Establishes a baseline level of energy consumption prior to the installation of its efficiency technology equipment and electric consumption meters;

(2) For each billing cycle after Taxpayer's equipment is installed, customers continue to pay their standard electric consumption bills; and

(3) Based on consumption reading equipment, customers, pay Taxpayer a fee computed by multiplying the applicable measured units saved by the agreed to fixed rate per unit of reduced energy usage. Thus, if no energy is saved, Taxpayer's fee is zero.

As an example, when Taxpayer acquires a new customer in San Francisco, the new customer and Taxpayer establish a pre-Taxpayer energy usage of $250,000 per month for the customer's electric, gas and/or steam usage. Taxpayer audits the customer's location and designs a customized retrofit to maximize savings and improve aesthetics for the location. Prior to full project installation, Taxpayer establishes priorities for the light levels and aesthetics. Due to Taxpayer's energy saving technology installed on-site, the customer's energy usage costs are reduced to $110,00 per month which the costumer pays in the normal course of its business operation. In addition, (assuming a fixed rate of 80% per unit saved rate for this example), customers pay Taxpayer a fee of $112,000 ($140,000 utility savings X 80%) for a total monthly energy expense of $222,000 and $28,000 in savings. Taxpayer is owed no further fees from this particular customer.

Tangible Personal Property for Taxpayer's Technology – As described above, Taxpayer's platform includes, but is not limited to LED tubes, lamps and bulbs, smart controls, HVAC equipment, water conservation tools and circuit-level electricity consumption meters in a customer's facilities. Taxpayer also provides replacements for malfunctioning equipment and consumption meters for its energy savings calculations.

It should be noted here that all upfront and replacement costs for material, labor, project management, components and installation are covered by Taxpayer. Taxpayer owns and controls the equipment 100% of the time, and it handles all installations.

Service – Taxpayer purchases and installs all of the efficiency technology with no customer participation. Customers have no right or ability to operate, access or alter any component. Customers and building owners grant Taxpayer and its subcontractors access to the building under the appropriate mechanism. After installation and not including maintenance repairs and replacements, the Service does not require direct human involvement to achieve expected energy savings. Performance monitoring is done by comprehensive micro-meters install throughout a facility that measures electricity consumption and performance on a fixture or circuit-level basis. Micrometer data is collected real-time and fed into Taxpayer's cloud-based analytics software. The performance monitoring system provides transparency and insight to customers of their consumption patterns and it is the backbone for the savings-based billing model.

End of Term Disposition – At the conclusion of a customer agreement, Taxpayer has options for what to do with the property and equipment on-site. For all agreements to date, Taxpayer either removes its property and equipment or abandons it on the customer's site. Taxpayer customers are not offered an option to purchase the equipment because they have no interest in purchasing the equipment they do not know how to operate. Taxpayer's decision is made on a case-by-case basis just prior to the end of each agreement.

Issue

Are the charges by Taxpayer for its Service Platform described above subject to Georgia sales and use tax?

Analysis

Georgia levies and imposes a tax (subject to certain exemptions) on the retail purchase, retail sale, rental, storage, use, or consumption of tangible personal property and on certain services.[1] "Retail sale" or a "sale at retail" means any sale, lease, or rental for any purpose other than for resale.[2] "Sale" means any transfer of title or possession, transfer of title and possession, exchange, barter, lease, or rental, conditional or otherwise, in any manner or by any means of any kind of tangible personal property for a consideration.[3] All sales, uses, consumption, distribution, and storage are taxable until specifically exempt from taxation by the Georgia Code. Services that are not specifically listed are exempt from Georgia sales and use tax.

When a transaction involves the sale of tangible personal property in connection with the delivery of a service, for application of Georgia sales and use tax purposes, the Department must make a determination as to whether the transaction is primarily the sale or lease of tangible personal property or a service. Georgia courts, generally, have adopted a "for the purpose of the customer" test to determine whether the transaction should be viewed as a sale of a service or as a purchase of tangible personal property.[4] More specifically, in determining whether a particular transfer of tangible personal property is either an incidental or an inconsequential element of a service transaction, the main consideration is the purpose of the customer. What is it that the customer primarily wishes to purchase, tangible personal property, or a service? If a customer is primarily interested in acquiring the tangible personal property, the sale is subject to Georgia sales and use tax. On the other hand, if a customer primarily wishes to purchase the skilled services of the service provider, because the customer cannot perform such services for himself due to the lack of equipment, time or skill, the sale or transfer of tangible personal property by the service provider is incidental to and but a means of providing the services that the customer wants. As such, this type of transaction is generally not subject to sales and use tax.

The Department, in making its decisions on these type of multi-component transactions, must examine a myriad of factors in order to apply the subjective test appropriately. Based on these factors the Department shall make its determination from a "for the purpose of the customer" perspective.

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[1] O.C.G.A. § 48-3-1 and 48-8-30
[2] O.C.G.A. § 48-8-2(31).
[3] O.C.G.A. § 48-8-3(33)(A).
[4] *See Inglett & Stubbs Int'l, Ltd. v. Lynnette T. Riley, 2015-2 Ga. Tax Tribunal (February 11, 2015) (citing Craig-Tourial Leather Co. Inc. v. Reynolds, 87 Ga. App. 360, 365 (1952)).*

In the case of Taxpayer, the following factors support a conclusion that "for the purpose of the customer", the transaction at issue is primarily a service, and therefore, the tangible personal property is but a means of providing the service.

As explicitly set forth in the Customer Agreement, Taxpayer owns and controls all of the equipment at all times. The customer has no right or capability to operate, access or alter any equipment, and moreover, the customer does not have the time or skill to perform Taxpayer's professional services. As such, at no time does the Customer ever have a need to understand any of Taxpayer's proprietary technology the equipment installation component, or the operational aspect of the equipment.

For billing purposes, Taxpayer only charges the customer based on a percentage of the savings that is created by Taxpayer's model. Moreover, the customer has no say in the equipment that is employed by Taxpayer, and the customer, by contract, does not receive an itemized price list of the equipment that is used as part of the overall transaction. The customer is only interested in the cost savings created by Taxpayer's service, which suggests that a customer views the equipment as merely an incidental element of the service aspect of the transaction.

The customer cannot duplicate the service provided by Taxpayer. To wit, but for proprietary software owned by Taxpayer that Taxpayer relies upon in creating the energy savings, the customer would not be able to create the savings generated by Taxpayer. As such. the equipment that is ultimately used by Taxpayer to create the energy savings is an incidental byproduct resulting from the efficiency creating service that is central to Taxpayer business model.

Notwithstanding the foregoing, we would be remiss without acknowledging that certain factors exist that are indicative of a taxable lease of tangible personal property. Specifically of note, this particular transaction is unique in that Taxpayer's control over the equipment is passive in nature. While Taxpayer maintains control and ownership pursuant to a contract, possession of the equipment lies with the customer throughout the term of the contract. Related thereto, Taxpayer delivers and installs the equipment, and gets paid a monthly fee based on the performance of such equipment.

Ultimately when balancing the factors, the Department deems the customer to be purchasing a service from Taxpayer, and in the process, Taxpayer uses and installs certain equipment as a necessary component relating to such efficiency savings services that it provides.

Ruling

Based on the facts presented, Taxpayer delivers and charges for a service, and such service also includes the transfer of tangible personal property for which no separate charge is made and that is ancillary to the service. Taxpayer is not required to collect Georgia sales and use tax on such charges.

We note that the ruling set forth above is based in part on Taxpayer's assertion that Taxpayer pays use tax in the appropriate state (whether Georgia or elsewhere) on all its purchases associated with the equipment used in connection with the service provided.

The opinions expressed in this ruling are based upon the information contained in your request and limited to the specific transactions, facts, circumstances and taxpayer in question. The facts herein are those presented by the taxpayer and the Department accepts them as true for this ruling. If the facts presented herein change, are not true, are different, or material facts have been omitted, the conclusions reached in this ruling may change. In addition, subsequent statutory or administrative rule changes or judicial interpretations of the statutes or rules upon which this advice is based may subject similar future transactions to a different tax treatment than that expressed in this ruling.