

Ruling 2003-01

Vermont Department of Taxes

Dated: October 30, 2003

Written By: John Bagwell, Attorney for the Department

Approved By: Tom Pelham, Commissioner of Taxes

You have requested a formal ruling addressing questions that you have raised concerning the Vermont sales tax consequences of transactions described in your letter to the Vermont Department of Taxes ("Department") dated July 30, 2003. Your questions are, specifically:

Question 1. Is the acquisition of copiers by [company] for use in its commercial reprographic centers exempt from Vermont sales tax under the manufacturing exemption provided in 32 V.S.A. § 9741(14)?

Question 2. Do agreements between [company] and its customers concerning their use of convenience copiers constitute lease/rentals, or is [company] providing a service?

Question 3. Are the services provided by [company] at its commercial reprographic centers subject to Vermont sales tax?

Question 4. Are the services provided by [company] at its commercial reprographic centers subject to Vermont sales tax if the customers furnish the paper?

Question 5. If the Department's response to Questions 3 and 4 is derived from the category of "printing," support how it equates copying to printing.

Your ruling request does not refer to any Vermont sales tax exemptions other than the manufacturing exemption in Question 1. This ruling therefore presumes that [company]'s copy sales are at retail and no sales and use tax exemptions are available except to the extent provided in the Department's response to Question 1. This ruling also presumes that all transactions are subject to Vermont sales tax jurisdiction.

It is assumed that [company] referred to in the ruling request is the same entity as [company 2] which has a business tax account for sales and use tax currently in effect with the State of Vermont.

PRESENTED FACTS

Reprographic Centers: [company] maintains commercial reprographic centers where it makes copies of original documents submitted by its customers. It may also provide

related copying services such as binding, stapling and numbering, at either its commercial reprographic centers or at its customers' facilities. [company] provides the personnel, the supplies, and the equipment used to produce the copies.

The commercial reprographic centers are available to [company] customers during certain hours. Only [company] personnel operate the equipment and the various control functions. The customers are charged a base amount for which they are entitled to a certain number of copies, and are charged additional amounts per copy over the allotted number. [company] may or may not provide the paper, depending on the terms of the service, on a customer-by-customer basis.

Convenience Copiers. [company] places convenience copiers at customers' places of business. The customers are charged a base amount that allows them to make a certain number of copies. There is an additional per-copy charge for copies over the allotted number.

It is not unusual for customers to have the right to terminate their agreements with [company] by providing written notice 60 days prior to the termination and paying, if applicable, an early termination charge. The convenience copiers are usually combined with unrelated equipment and services under a single agreement, but work independently of each other. During the term of these agreements, customers may negotiate for different copiers that provide, for example, color and higher volume.

[company]'s customers have exclusive use of the copiers and have the right to operate the copiers by choosing different control functions. The copiers are available for customer use at any time during the agreed-upon period, usually three years.

[company] may or may not provide the paper, depending on the terms of service, on a customer-by-customer basis. It is responsible for the maintenance of the copiers and for providing the toner, developer and fuser used in the copiers. It does not charge its customers for the maintenance and supplies.

DISCUSSION

Discussion of Question 1. You ask, in effect, whether the receipts from the sale of copiers to [company] for use in its commercial reprographic centers are exempt from Vermont sales tax under the manufacturing exemption. The given facts indicate that they are.

These facts show that [company] personnel use the copying equipment to produce copies that reflect images taken from original documents. [company] then sells these copies to its customers, sometimes after the copies have been bound, stapled and numbered, for which it charges a base amount for a specified number of copies plus a per-copy charge over that amount. The copies are tangible personal property inasmuch as they can be seen, weighed, measured, felt, and touched. 32 V.S.A. § 9701(7) (defining "tangible personal property"). Under these circumstances, [company]'s

transactions with its customers constitute transactions that focus on the sale of tangible personal property rather than the services used to produce that property.

Receipts from the sale of equipment are exempt from Vermont sales tax if the equipment is used directly and exclusively (except for isolated or occasional uses) in the manufacture of tangible personal property for sale. 32 V.S.A. § 9741(14). "Manufacturing," for exemption purposes, includes "information processing." Vermont Sales/Use Tax Regulation ("Reg.") § 1.9741(14)-2(b) (eff. 3-30-98).

Information processing referred to in the Regulation is "an integrated series of operations in which information or images are produced and sold as tangible personal property," as long as the transaction focuses on the sale of tangible personal property rather than services. Reg. § 1.9741(14)-2(f). The facts described above show that the copying procedures at the commercial reprographic centers constitute "information processing" as defined in Reg. § 1.9741(14)-2(b), and therefore "manufacturing" for purposes of the manufacturing exemption.

In order to qualify for the manufacturing exemption, the copying equipment must be used directly and exclusively in manufacturing. 32 V.S.A. § 9741(14). This requirement will be met because the copying equipment is used directly in the copying process, and the facts indicate that it is so used 100% of the time.

[company] sometimes does not furnish the copy paper. In such cases, the paper evidently is furnished directly or indirectly by the customers. This causes the copying process to be classified as "fabrication" rather than "manufacturing." As noted in 32 V.S.A. § 9771(3), fabrication consists of "producing, fabricating, printing or imprinting of tangible personal property for a consideration for consumers who furnish either directly or indirectly the materials used in the producing, fabricating, printing or imprinting."

The distinction between manufacturing and fabrication does not, however, bar [company] from claiming the manufacturing exemption. Reg. § 1.9771(3)-1(a) observes that "[f]abrication is similar to manufacturing because in most instances a new part or shape is produced or manufactured, material is added or taken away, or appearance or makeup of the item [furnished by the customer] is altered."

The similarity between fabrication and manufacturing identified in the Regulation is evident in the copying process conducted at the commercial reprographic centers. Specifically, the appearance of blank copy paper furnished directly or indirectly by the customers is altered into paper that bears images copied from original documents. The Department accordingly considers the copying equipment to be exempt from Vermont sales tax under the manufacturing exemption even though the equipment is used from time to time in the fabrication process.

Discussion of Question 2. You ask whether the agreements between [company] and its customers concerning the use of convenience copiers constitute lease/rentals or whether [company] is providing a service. The given facts show that the agreements constitute leases for Vermont sales tax purposes rather than agreements for the provision of services.

Leases of tangible personal property are considered sales for Vermont sales tax purposes because 32 V.S.A. §9701(6) provides that a “lease” is considered a “sale” for sales tax purposes. [company]’s rental receipts from its copier leases are therefore subject to Vermont sales tax under 32 V.S.A. § 9771(1). This Section imposes sales tax on “receipts from . . . [t]he sale of tangible personal property sold at retail in this state.” As noted in Section 9701(6), the “sale” referred to in Section 9741 includes a “lease.”

Nothing indicates that the legislature meant for “lease” to be interpreted other than in accordance with its commonly understood meaning. A lease, as commonly understood, is a “contract granting use . . . of property during a specified period in exchange for rent.” *The American Heritage College Dictionary*, 3d ed., p.p. 772. “Rent” is defined as a “payment [fixed by contract] made for the use of . . . equipment . . . provided by another.” *Id.*, p. 1156.

The given facts show that [company]’s agreements with its customers fall within the commonly understood definition of a lease. They specify the terms of use, the duration of use, the consideration to be paid for the use, and notice of termination. They furthermore provide that the customers have exclusive equipment operating rights.

The fact that customers sometimes furnish their own paper does not alter the fact that the agreements are leases. Leases do not necessarily bar lessees from furnishing supplies for use in connection with the leased property.

Although the amount which [company]’s customers pay is ultimately measured by the number of copies, these payments, in the context of the agreements, constitute consideration for the use of the copiers rather than payment for the copies themselves.

[company] could have structured the agreements with its customers as agreements for the service of providing copies. The agreements were, however, structured as leases, and “a transaction is given its tax effect in accord with what actually occurred and not in accord with what might have occurred.” *Chittenden Trust Co. v. Commissioner of Taxes*, 143 Vt. 271, 275 (1983).

Discussion of Question 3. You ask whether the services provided by [company] at its commercial reprographic centers are subject to Vermont sales tax. The given facts show that they are.

Question 4, discussed below, indicates that Question 3 is limited to transactions in which [company] supplies the copy paper. When [company] supplies the copy paper, the copy sale transactions clearly focus on the sale of the copies rather than the provision of services.

Because the transactions focus on the sale of copies, the receipts from the copy sales are subject to Vermont sales tax under 32 V.S.A. § 9771(1) (which imposes sales tax on the transfer of tangible personal property at retail). And because the transactions focus on copy sales rather than services, all receipts for services rendered in the production of the copies are subject to Vermont sales tax under 32 V.S.A. § 9741(35). This Section

provides, in pertinent part, that “[w]hen the focus of the transaction is the transfer of tangible personal property, all receipts from the sale are taxable, including receipts from separately stated charges for services to produce the property.”

Discussion of Question 4. You ask whether the Department's response to Question 3 would be different if the customers provide the copy paper. The answer is "no". The receipts are still subject to Vermont sales tax under these circumstances, but under 32 V.S.A. § 9771(3) instead of 32 V.S.A. § 9771(1).

Section 9771(3) imposes sales tax on charges for producing, fabricating, printing, or imprinting tangible personal property for consumers who furnish the materials used in the process. The processes described in the statute are identified in Reg. § 1.9771(3)-1 as "fabrication."

Reg. § 1.9771(3)-1(a) observes that “fabrication is similar to manufacturing because in most instances a new part or shape is produced or manufactured, material is added or taken away, *or appearance or makeup of the item is altered.*” (emphasis added). The photocopy process at the commercial reprographic centers constitutes fabrication, as identified in this Regulation, because it alters the appearance of the copy paper furnished by the customers. Specifically, the blank paper is converted into paper bearing images copied from original documents.

Discussion of Question 5. You inquire as to how the Department would equate copying to printing if its responses to Questions 3 and 4 were derived from the category of "printing." The Department's responses to Questions 3 and 4 are not derived from the category of "printing." The Department notes, however, that other states have equated copying with printing. See, e.g., New York Commissioner of Taxation and Finance Advisory Opinion TSB-A-93(10)S Sales Tax, 11-25-93 (in connection with the fabrication process); Maine Revenue Services Instructional Bulletin No. 17, 1-1-00.

Statutes Enacted But Not Yet In Effect. Vermont has recently enacted statutes relating to streamlined sales tax provisions which will take effect on the first day of the second quarter following the date of Vermont's membership in the multistate streamlined sales and use tax agreement, but no earlier than January 1, 2005. These statutes, when they become effective, would appear not to alter the conclusions reached in this ruling. However, as noted below, this ruling is limited to the presented facts as affected by statutes and regulations in effect on the date of this ruling.

GENERAL PROVISIONS

This ruling will be made public after deletion of the parties' names and any information that may identify the parties. A copy of the ruling showing the proposed deletions is attached, and you may request, within 30 days, that the Commissioner delete any further information that might tend to identify interested parties. The final discretion as to deletions, however, remains with the Commissioner.

This ruling is issued solely to you and is limited to the facts presented as

affected by statutes and regulations in effect on the date of this ruling. Other taxpayers may refer to this ruling to determine the Department's general approach, but the Department will not be bound by this ruling in the case of any other taxpayer or in case of any change in the relevant statutes and regulations.

3 V.S.A. § 808 provides that this ruling will have the status of an agency decision or order in a contested case. You have the right to appeal this ruling within thirty (30) days.