Ruling 96-08

Vermont Department of Taxes

Date: April 12, 1996

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Approved By: Edward W. Haase, Commissioner of Taxes

You requested a formal ruling on how leases are treated for Vermont sales and use tax. This ruling is based on the facts in your December 13, 1995 letter and the attached sample of your lease.

Issue: Is the lease between [Taxpayer] and its customer a rental of tangible personal property and taxable under 32 V.S.A. §§ 9701(6), 9771(1) or financing executed through a lease and exempt from sales tax under 32 V.S.A. § 9742(7)?

Facts: [Taxpayer] is a corporation with offices in [State] and does business in the state of Vermont. The [Taxpayer] conducts a variety of transactions but the issue at hand, and the substantial portion of their activity, is described as financing secured by equipment, vehicles and other tangible personal property. The [Taxpayer] records the transactions as notes receivable for financial accounting, and federal and state tax purposes.

The [Taxpayer] acts as a source of financing for the customer. The lease arrangement is used because it is more marketable than a straight note and provides more security for the creditor.

The customer selects the equipment. Often the customer has already purchased the equipment and paid any required sales tax prior to an application for a lease with the [Taxpayer]. If the customer has entered into a purchase agreement with a vendor, the purchase agreement invoice is assigned to the [Taxpayer] for payment. A commitment fee equal to the first period's payment is required prior to entering into the agreement to cover the lessor's cost of appraising the lessee's credit. This fee is applied toward the first payment or refunded if lessor declines to enter into an agreement. The lease payments are based on the cost of the equipment or an agreed upon amount which is usually less than the original cost of the equipment. If the [Taxpayer] and customer enter into a lease agreement, the customer pledges the equipment as security, transfers legal title to the [Taxpayer]. The [Taxpayer] transfers title back to the customer upon receipt of the payments specified in the lease agreement. Possession of the equipment remains with the customer at all times.

The lease agreement is for a specific period of time and payments. The lease agreement does not contain purchase or buy out options. When the customer meets the provisions of the lease agreement, the [Taxpayer] returns the title and relinquishes its security interest in the equipment without further payment by the customer.

Ruling: The lease agreement between the customer and the [Taxpayer] is a financing lease. The transfer of the security interest title to the [Taxpayer] and the lease payments are not subject to Vermont sales and use tax.

Vermont imposes the sales and use tax on the sale of tangible personal property. Sales, as defined in 32 V.S.A. § 9701(6), means "...any transfer of title or possession or both, exchange or barter, rental, lease or license to use or consume, condition or otherwise, in any manner or by any means whatsoever for a consideration, or any agreement therefor;...." The payments under a lease agreement would be subject to tax. A lease agreement has the following characteristics:

1. The lessor holds title and/or ownership of the tangible personal property.

2. The lessee may purchase the tangible personal property at the end of the lease agreement for other than a nominal amount and generally at fair market value.

3. The lease agreement can be renewed and the new payments may be a continuation of the existing payments, but not based on the value of the equipment.

The lease under consideration is a financing lease agreement. A financing lease agreement has the following characteristics:

1. The lessee transfers title or security interest to the tangible personal property to the lessor as collateral for a loan.

2. Upon lessee meeting the provisions of the lease and making all the specified lease payments, lessor returns title or security interest to lessee for either a nominal amount (e.g., $1.) or no additional payment.

3. The financing lease agreement payments are based on an agreed upon amount but not in excess of the purchase price of the tangible personal property plus any interest, processing or commitment fees.

4. The financing lease agreement is usually for a specified time period and not renewable under the same provisions. The [Taxpayer's] master lease, when amended by Exhibit Form [number] and Exhibit [number], is a financing lease agreement. The payments under this agreement are not subject to sales tax. If the tangible personal property is subject to Vermont's sales and use tax, the lessee is responsible for paying the sales tax to the vendor or remitting the use tax when the tangible personal property is originally purchased. The transfer of the tangible personal property from the lessee to the lessor as security for a loan is exempted under 32 V.S.A. § 9742(7).

This ruling is issued solely to your business and is limited to the facts presented as affected by current statutes and regulations. 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 the case of any change in the relevant statute or regulations.