

The Project will consider this draft paper at its April 12 meeting.

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STREAMLINED SALES TAX PROJECT

ISSUE PAPER ON LEASE OR RENTAL

ISSUE

To define the terms "lease" and "rental" so that lessors operating in multiple states have common terms that will ease their sales tax compliance burden. The subgroup on lease or rental was assigned the task of developing definitions for those terms. The subgroup met in Denver (twice), Milwaukee, Raleigh, Minneapolis, Louisville, Dallas, and New Orleans. Interested persons from the private sector participated in these meetings along with the government representatives.

BACKGROUND

Most states subject the lease of tangible personal property to their sales tax. In most states, leasing property is an alternative to buying property and is treated like the sale of the property. South Dakota taxes leasing as a service. Illinois, Maine and New Jersey do not tax leases, but require the lessor to pay tax on the items they intend to lease or rent. Arkansas, California, Colorado, Michigan, Mississippi, Missouri, Nevada, North Dakota, and Rhode Island give the lessor the choice of paying tax on the purchase price, or paying tax on the lease payments.

The need to have uniformity in the definition of lease and with other lease issues is driven by the complexity resulting from the disparate treatment existing today. States differ in the following areas:

1. The definition of a lease.
2. The time allowed for sale/leaseback decisions. Exclusion on purchase or on leaseback payments also differs.
3. Whether or not a credit is given for taxes paid to other jurisdictions.
4. The use of varying sourcing rules.
5. Accelerated tax payments versus taxing the stream of payments.
6. The treatment of taxes on motor vehicles and motor vehicle leases.

DEFINITION OF LEASE

A review of state laws found fourteen states with a specific lease definition, either in statute or regulation. (Alabama, Florida, Georgia, Kentucky, Louisiana, Minnesota,

Mississippi, New Jersey, New Mexico, North Carolina, Tennessee, Texas, Virginia, Washington)

Twenty-eight states and the District of Columbia specifically include leases in their definition of sale or sale at retail. (Arizona, Arkansas, California, DC, Florida, Georgia, Kansas, Kentucky, Maine, Maryland, Massachusetts, Minnesota, Mississippi, Nebraska, Nevada, New Jersey, New York, North Dakota, Oklahoma, Pennsylvania, Rhode Island, South Carolina, Tennessee, Texas, Utah, Vermont, Virginia, Washington, and West Virginia)

Examples of State Definitions of Lease or Lease/Rental

Alabama - "A transaction whereunder the person who owns or controls the possession of tangible personal property permits another person to have the possession or use thereof for a consideration and for the duration of a definite or indefinite period of time without transfer of the title to such property."

Florida - "The leasing or rental of tangible personal property and the possession or use thereof by the lessee or rentee for a consideration, without transfer of the title of such property."

Georgia - "The leasing or renting of tangible personal property and the possession or use of the property by the lessee or renter for a consideration without transfer of the title to the property."

Kentucky - "The term "lease or rental" means the grant to another of the right to use and possess tangible personal property for a period of time and for a consideration. The term "lease or rental" includes financing transactions by a financial institution or leasing affiliate of a financial institution although title is transferred principally for the purpose of securing the lessor's financial interest. The term does not include the lease or rental of real property or a transaction which provides a service. The providing of a service is any transaction which includes both services and tangible personal property for a consideration where the performance of the service is the essence of the transaction."

Louisiana - "The leasing or renting of tangible personal property and the possession or use thereof by the lessee or renter, for a consideration, without transfer of the title of such property."

Minnesota - "Leasing includes all transfers of possession of TIPP or the use thereof by the lessee for a consideration when the title remains with the lessor at the end of the lease."

Mississippi - "Any agreement entered into for consideration that transfers possession or control of tangible personal property to a person for use with this state."

New Jersey - "The possession or control of tangible personal property by an agreement, not transferring sole title, as may be evidenced by a contract, contracts, or by implication

from other circumstances including course of dealing or usage of trade or course of performance, for a period of more than 28 days.

New Mexico - "Leasing means an arrangement whereby, for a consideration, property is employed for or by any person other than the owner of the property except that the granting of a license to use property is the sale of a license and not a lease."

North Carolina - "A transfer, for consideration, of the use but not the ownership of property to another for a period of time."

Tennessee - "The leasing or renting of tangible personal property and the possession or use thereof by the lessee or renter for a consideration, without transfer of the title of such property."

Texas - "A transaction, by whatever name called, in which possession but not title to tangible personal property is transferred for a consideration."

Virginia - "The leasing or renting of tangible personal property and the possession or use thereof by the lessee or renter for a consideration, without transfer of the title to such property."

Washington - "The act of granting to another the right of possession to and use of tangible personal property for a consideration."

Explanation of lease or rental definition

In reviewing the state's definitions of sale, sale at retail, lease or rental, there were three common factors. First, the lessee must have possession or use of the product. Second, the lessee must give consideration to the lessor. Third, the transaction can not transfer title to the property.

The subcommittee proposed the following as the definition of lease or rental.

"Lease or rental means any transfer of possession or control of tangible personal property for a fixed or indeterminate term for consideration. A lease or rental may include future options to purchase or extend.

1) Lease or rental does not include:

- a) A transfer of possession or control of property under a security agreement or deferred payment plan that requires the transfer of title upon completion of the required payments;
- b) A transfer of possession or control of property under an agreement that requires the transfer of title upon completion of required payments and payment of an option price does not exceed the greater of \$100 or 1 % of the total required payments; or
- c) The provision of tangible personal property along with an operator for a fixed or indeterminate period of time. A condition of this exclusion is that the operator is necessary for the equipment to perform as

designed. For the purposes of this subsection, an operator must do more than maintain, inspect, or set-up the tangible personal property.

2) Lease or rental does include:

Agreements covering motor vehicles and trailers where the amount of consideration may be increased or decreased by reference to the amount realized upon sale or disposition of the property as defined in 26 USC 7701(h)(1).

3) Characterization of Transaction for Other Purposes:

The definition provided in this section shall be used for the purposes of this chapter regardless if a transaction is characterized as a lease or rental under generally accepted accounting principles, the Internal Revenue Code, the [state commercial code], or other provisions of federal, state or local law.

Transition Rule:

This definition will be applied only prospectively from the date of adoption and will have no retroactive impact on existing leases or rentals. The definition of lease in this section shall neither impact any existing sale-leaseback exemption or exclusion that a state may have, nor preclude a state from adopting a sale-leaseback exemption or exclusion after the effective date of this agreement."

There are two things that must occur for a transaction to be a lease: (1) the lease must transfer possession or control of the item; and (2) there must be consideration given by the lessee to the lessor. These two items are common to all state lease definitions.

The exclusions in Subsection 1 address areas where states differ on the treatment of leases. The purpose of the exclusions is to establish one set of rules in those situations.

A lease does not transfer ownership, and the first two items under Subsection 1 seek to satisfy that a lease does not transfer ownership. The first two items in Subsection (1) identify sales that involve payments that extend over a period of time. These look like leases because of multiple payments. In both instances, the contract requires that the buyer receive the title to the product. The first exclusion differs from the second in that in the second, the final payment (the option price) may not be the same as the previous payments. If the option payment exceeds the listed thresholds, then the transaction was a lease.

The third item in Subsection (1) defines the difference between a lease and a service. Under this exclusion, if an operator accompanies property, the transaction is not a lease of the property but a service. This exclusion contains conditions. In certain instances, such as scaffolding, the owner of property requires that a representative of the owner set-up the property. In other instances, such as portable toilets, a representative of the owner will provide service to the property. There have been disagreements over whether setting-up the property or providing service to the property constitutes providing

an "operator." The first condition of this exclusion is that the operator is necessary for the equipment to perform as designed. The equipment does not operate itself and it is the equipment owner, or representative, that operates the equipment. The second condition is that an operator must do more than maintain, inspect, or set-up the equipment.

The language found in Subsection (2) relates to a motor vehicle lease containing a terminal rental adjustment clause (TRAC). These are leases but with a unique feature. When the lease is terminated and the vehicle is sold, the final lease payment reflects an adjustment for the difference between the selling price of the motor vehicle and its book value. The definition uses a federal law for further clarification.

The purpose of Subsection (3) is to clearly state that this definition is the only definition that may be used for sales and use tax purposes. Neither states nor industry would be allowed to use alternative lease definitions for sales tax purposes. The intent of this language is that a court would also not be allowed to use an alternative lease definition for sales tax purposes.

The subcommittee discussed the need to state that if this definition is different from what a state has, that adopting this definition should not alter how tax applies to existing leases. The language at the end of the definition is intended to have the scope of this definition apply prospectively from its adoption by a state. This language is not part of the definition, but should become part of a state statute so that it is clear the adoption of the definition does not change the tax on existing leases.

LEASE SURVEY RESULTS

The subcommittee surveyed SSTP states concerning the impact of the proposed definition. Twenty-six states responded to the survey. (Arkansas, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Minnesota, Missouri, New Jersey, North Carolina, North Dakota, Oklahoma, Rhode Island, South Dakota, Tennessee, Texas, Utah, Vermont, Washington, Wisconsin, and Wyoming)

The survey asked three questions:

- 1) Is the preceding definition what your state uses to define lease or rental? If not, how does it differ from your definition?
- 2) What statutory changes would you have to make to your law to accommodate this definition?
- 3) What, if any, impact would this have on your sales or use tax collections?

Fourteen states said this definition is identical to or consistent with their current definition. (Idaho, Indiana, Louisiana, Minnesota, Missouri, North Carolina, North Dakota, Rhode Island, South Dakota, Tennessee, Texas, Vermont, Washington, and Wyoming)

Nearly every state would have to make some change to their law. The two most often cited changes involved the exclusions in 1(b) and 1(c).

Thirteen states stated that sales tax collections would be constant or that any changes would be nominal. (Idaho, Indiana, Louisiana, Missouri, North Carolina, North Dakota, Oklahoma, Rhode Island, South Dakota, Texas, Vermont, Washington, and Wyoming) Iowa and Maryland stated that adopting the proposed definition would change tax collections by \$1 million per year. The remaining states identified areas where this definition would increase or reduce tax collection, but were unable to put a dollar amount on the change.

Each state's response to the survey questions is in the appendix at the end of this paper.

OTHER ISSUES

Sale-leaseback

There was considerable discussion about including a sale-leaseback provision. States differ in the amount of time permitted between the purchase and the leaseback. Failure to make the second transaction within the prescribed time results in the taxation of both transactions. Some states view both transactions as completely separate, and both are taxable. Although industry is unified in support of ending double taxation there was a divergence of opinion relating to the appropriate method to resolve the issue.

The subcommittee discussed the following language as a possible exclusion from a lease.

"Sales, assignments or transfers of property that remains in the control and possession of the same person before and after the sale, assignment or transfer of tangible personal property, provided the person paid sales or use tax when they acquired such property in a taxable transaction."

The industry submitted the following definition.

"A "sale-leaseback" is a transaction through which an owner/user (Seller-Lessee) of property sells the property to another party (Purchaser-Lessor) who leases it back within (a certain period) from when the property was originally placed in service by the owner/user (Seller-Lessee). A sale-leaseback shall be considered a financing arrangement and shall not be considered a separate sale, use or lease of property. For purposes of this definition, the certain period will not be less than 180 days."

This issue has been assigned to a subcommittee for further research and discussion.

The definition of "rental"

The American Rental Association firmly believes in the need for a separate definition of "rental." This subcommittee had several discussions on this issue (some with and without the Rental Association) and have concluded that one definition is sufficient for most states. Some states, such as Texas, state in statute "that the terms "rental" and "lease" are to be used interchangeably." The statutes from Alabama, California, Connecticut, District of Columbia, Florida, Georgia, Illinois, Indiana, Louisiana, Mississippi, North Carolina, Pennsylvania, Tennessee, Texas, Virginia, Washington, and Wisconsin are written so that the terms "lease" and "rental" are synonymous. Rhode Island is the only state with a specific statutory definition of "rental." There are some states, such as South Dakota, that use time as a determining factor for which tax might apply to certain property. In South Dakota the sales tax applies to motor vehicles leased or rented for twenty-eight days or less, and the motor vehicle excise tax applies to those leased or rented for more than twenty-eight days.

Motor vehicles

No conversation about lease or rental lasts long without discussion of the various ways states tax motor vehicles. The SSTP specifically removed motor vehicles from certain portions of the project, including sourcing and multiple rates (see Uniform Sales and Use Tax Administration Act, as amended January 24, 2001, Sections 310(i) and 308 (a)(6), respectively).

It is important to note that most states tax motor vehicles in the sales/use tax statutes. Only eleven states have special taxes for the purchase or lease of motor vehicles. These special taxes are not impacted by the Streamlined Sales Tax Project. However, motor vehicles are impacted by the Project in those states that tax motor vehicles under their sales tax.

While excluding motor vehicles would significantly ease the Project's work, it also provides this industry with very little of the Project's benefit. A subcommittee has been established to identify the issues and propose solutions related to motor vehicles. These issues include, but are not limited to, multiple rates, sourcing, calculating tax, credits/reciprocity, definitions, and administration. We suggest that this workgroup continue its assignment after the leasing workgroup has concluded.

Licenses

Software is often licensed. States that wish to tax licensed software include "license" in their definition of sale, specifically impose a tax on software, or interpret their definition of sale to include the transfer of licensed software. The tangible personal property committee suggested that the Lease and Rental subcommittee evaluate this concept. The lease subcommittee postponed this discussion until the definition of "sale." The tangible personal property committee suggested that the lease subcommittee look at the UCITA definition of license since licensing is typically the way software is provided to customers. The UCITA definition of license is:

"License" means a contract that authorizes access to, or use, distribution, performance, modification, or reproduction of, information or informational rights, but expressly limits the access or uses authorized or expressly grants fewer than all rights in the information, whether or not the transferee has title to a licensed copy. The term includes an access contract, a lease of a computer program, and a consignment of a copy. The term does not include a reservation or creation of a security interest to the extent the interest is governed by [Article 9 of the Uniform Commercial Code].

APPENDIX A- LEASE DEFINITION SURVEY RESULTS.

1. How does this definition differ from your definition?

Arkansas - Arkansas does not specifically define lease/rental. Rather it is included in the definition of "sale" ("sale" includes the exchange, barter, lease or rental of tpp). In the case of leases or rentals of tpp, the tax shall be paid on the rental or lease payments made to the lessor of such tpp during the term of the lease or rental; however, except for short term rentals (less than 30 days) and rentals of motor vehicles, the tax shall not apply to gross receipts derived from leases or rentals of tpp upon which either the Arkansas sales or use tax was paid at the time of purchase.

Georgia - The nominal purchase option, as written, would not be consistent with Georgia's taxation of such a transaction. We would treat such transactions as taxable unless it could be shown that the substance is a secured loan with a nominal buyout. A lease with an operator, with control or right to direct the operator, is a taxable transaction.

Idaho - The main difference is that neither the Idaho statute nor rules provide a specific definition of the nominal option payment for a conditional sale.

Illinois - Lessors of tangible personal property under true leases (those with no buy-out option at the end of the lease or one that requires payment of the fair market value) in Illinois are deemed end users of the property to be leased. As end users of tangible personal property located in Illinois, lessors owe Use Tax on their cost price of such property. In the case of a true lease, the lessors of the property being used in Illinois would be the parties with Use Tax obligations. The lessors would either pay their suppliers, if their suppliers were registered to collect Use Tax, or would self-assess and remit the tax to the Department. If the lessors already paid certain taxes in another state with respect to that tangible personal property, they would be exempt from Use Tax to the extent of the amount of such tax properly due and paid in such other state.

Indiana - While Indiana has no specific codified definition of lease or rental, the proposed definition is generally consistent with administrative decisions. A transaction in which property is transferred for consideration together with an operator for the property, has been consistently evaluated by Indiana in terms of the "control" exercised by the transferee. If the person receiving the property exercises sufficient control over the operation of the property, the transaction is a lease and subject to Sales Tax, however, if the owner of the property retains control of the property and the operator, the transaction is a nontaxable service.

Iowa - A purchase for lease is not a purchase for sale or resale. If a lessor purchases an item of tangible personal property to lease the item that purchase is subject to sales or use tax unless the lease is longer than five months, the person is regularly engaged in the business of leasing and sales or use tax is paid on the lease or rental receipts. Our courts view the purchase as one transaction and the lease of the item purchased as a separate transaction. We have several different exemptions in our statute relating to the leasing of various items but not every thing purchased for lease is exempt from sales or use tax.

Kansas - One part of the Kansas sales tax act taxes leases and rentals as a sale. Another part taxes leases and rentals as a service. Kansas treats each lease period as a separate sale. This means that when property is leased from an out-of-state lessor, Kansas claims tax on the lease payments when the property from out-of-state is located in Kansas. Similarly, when property is rented here and removed for use outside Kansas, we claim tax is due on those lease payments where the property is in Kansas. This normally only includes the first lease payment when the property is picked up here. Kansas also distinguishes between a lease and financing arrangement based on how the transaction is treated for federal income tax purposes. Generally, if a lessee can take the depreciation on the property, the transaction is treated as a financing transaction with sales tax due on the full amount up front. This is inconsistent with the proposal's Section 3), "Characterization of the Transaction for other purposes." Kansas allows a sale for resale exemption when items are purchased to be leased or rented. For Kansas, this practice has been problematic since it allows businesses like contractors to form separate entities that lease their equipment back. Kansas loses tax when a contractor who has done this uses it outside Kansas and on exempt Kansas projects.

Louisiana - LA utilizes basically the same definition, with three differing items:

- a- LA provides for "use" instead of "control." In our view, "use" is a more precise "action verb" whereas "control" is more nebulous, because "control" could be argued to mean "control" in a legal and not physical sense. Also, the use of "control" brings its own set of problems for LA; we have situations where natural gas compressors are argued to be under the "control" of the owner (i.e. a nontaxable service) even though the lessee has physical "possession."
- b- LA specifies that the lease/rental is "without transfer of title." When an outright sale occurs, one also gets "possession" or "control." The way the SSTP definition currently reads, it states "*any* transfer of possession or control." So, this would include sales, too! It seems more precise to say that in a lease/rental situation that title remains with the owner.
- c- LA law continues its core definition with a discussion that "leases" of autos are for 180 days or more; "rentals" of autos are for less than 180 days. Additionally, (1)(a) and (b) of the SSTP definition are currently LA's administrative policy, so it will be useful to "upgrade" that policy by putting it into the statute. The same applies to (1)(c), except that there is significant dispute (primarily with the compression equipment) about when there is an operator provided. Bringing this language into the statute would provide clarity in these and other situations.

Maine - Maine does not define Lease or Rental and generally does not tax leases or rentals. Maine does tax certain leases such as leases of automobiles, the rental of hotel rooms and videotapes.

Maryland - It differs in several respects most importantly, it specifies that all transactions for equipment and operators are not leases or rentals. Existing MD regulations specify that a lease or rental occurs if billing is on a time basis and control transfers to the customer.

Minnesota - The definition of lease is substantially the same as the proposed definition. Minnesota law draws a distinction between a "lease" and a "conditional sales contract." A lease is defined as a transfer of possession or the use of tangible personal

property by the lessee for a consideration, if title remains with the lessor at the end of the lease. A lease is a series of sales with sales tax due on each lease payment. A conditional sales contract means a contract, whether or not the contract is designated as a lease, that provides that the purchaser or lessee is to obtain title to the property at the end of the term of the contract or has the option to purchase the property at the end of the term of the contract for a nominal amount. Nominal amount is defined in law to mean an amount so small, slight, or negligible that it is not economically significant and bears no relation to the real value of the items being purchased. For purposes of administering this provision, Minnesota issued a revenue notice that further defines "nominal amount" as one percent or less of the value of the tangible personal property at the time that the contract is signed. Minnesota does not reference the provision in 2) of the proposed definition. However, leases of motor vehicles and trailers fall under the same guidelines as leases of other tangible personal property in Minnesota. An agreement where the amount of the lease payment may be increased or decreased based on the amount realized on the sale or disposition of the property would not make a lease into a sale for Minnesota sales tax purposes.

Missouri - Lease or rental means any transfer of the right to possession or use of tangible personal property for a term in exchange for consideration. However, if a taxpayer uses tangible personal property to provide a service to the taxpayer's customer and the use of the property is a necessary or mandatory part of the service transaction, then any temporary transfer of the property as part of the service transaction is not a lease or rental of the property.

New Jersey - "Rental" is not specifically defined but an agreement as described above, entered into with an initial term of 28 days or less is treated as a rental. It is possible to have consecutive rental periods, resulting in a transaction of multiple months in length, which is still treated as a rental for sales tax purposes.

North Carolina - The definition of lease or rental means a transfer, for consideration, of the use but not the ownership of property to another for a period of time.

Administratively, we have set out provisions in an agreement that would classify a transaction as a conditional sale or a financing arrangement and not a lease, however, there are no statutory thresholds. The sublease is currently applied under our general sale for resale statutes. We follow the lease with an operator principle, however, this is again set out by rule and not by statute. Motor vehicles are subject to highway use tax based on a vehicle being titled in the State. A lessor has the option of paying the highway use tax up front or paying on the rental stream. I am not familiar with the US Code provision and am not able to advise at this time if it will be an issue. It does not appear that this would affect the application of tax. There is no provision in sales or use tax law or highway use tax law for this reference. Our statutes have no language regarding the characterization of the agreement; however, administratively, the terms of the agreement are determinative of the application of tax and not how the agreement is termed.

North Dakota - the proposed definition in 1(a) and 1(c) is similar to our statutory and administrative definitions. North Dakota currently provides an option of tax up-front or on payments for the transaction described in 1(b).

Oklahoma - Oklahoma does not follow the exclusion of 1(b).

Rhode Island - For the most part. Rhode Island currently offers the lessor an option to pay tax "up front" based on the cost of the property to the lessor.

South Dakota - The state does not have a written definition of a lease or rental. With exception of 1(b) this definition is consistent with our application of tax on leases. 1(b) has not been used in all situations to define a lease versus a purchase. Using this definition sales tax would be collected on transactions under 1(b) as a sale of tangible personal property rather than a lease, which should result in the same tax collection. Motor vehicles are subject to a different tax and would not be subject to this definition.

Tennessee - There is no distinction for agreements with a nominal option to purchase upon completion of the required payments as described in 1(b). These are currently taxed as periodic payments are made and are taxed again when the final purchase of the item is made. Tennessee law is more restrictive on its treatment of tangible personal property provided with an operator. There is currently no provision in Tennessee law covering Paragraphs (2) and (3) of the proposed definition.

Texas - The preceding definition is consistent with Texas' definition of a lease or rental, except Texas defines lease to include agreements that provide for the transfer of title after payments for a fixed term. Additionally, motor vehicles leases are taxed under a separate statute, and are not included in our regular sales and use tax statute.

Utah - There is no specific definition of lease or rental in statutes, regulations or rulings. The definition of "sale" in Utah Code Ann. 59-12102(25)(e) includes any transaction under which right to possession, operation, or use of any article of tangible personal property is granted under a lease or contract. Administrative Rule 8865-19S-32 Leases and Rentals Pursuant to Utah Code Ann. 59-12-103, states that a lessee may, at its option, treat a conditional sale lease as either a sale or lease for sales or use tax purposes. A conditional sale lease is a lease in which: 1. the consideration the lessee is to pay the lessor for the right to possession and use of the property is an obligation for the term of the lease not subject to termination by the lessee, and 2. the total consideration to be paid by the lessee is fixed at the time the lease is executed and cannot be modified by use, condition, or market value, and either: a. the lessee is bound to become the owner of the property; or b. the lessee has an option to become the owner of the property for no additional consideration or nominal additional consideration upon compliance with the lease agreement. Nominal consideration in this sense means ten percent or less of the original lease amount. The rule also provides for determination of the base if treated as a sale. Administrative Rule 8865-19S-32 states leases and rentals can include an operator, but that charges for such leases or rentals are exempt from sales and use tax.

Vermont - These are not defined terms in VT statute or regulation. By policy, we treat as installment sales lease-options where the option price is nominal. The proposed definition uses this approach but is more precise. This would not apply to highway vehicles that are subject to a separate tax.

Washington - There isn't a statutory definition of lease or rental and the proposed definition is mostly consistent with the current practice.

Wisconsin - Whether equipment provided with an operator is a lease depends on whether the lessee directs, supervises, or in some other manner is responsible for the satisfactory completion of the job. If the lessee exercises such control, the transaction is a lease of tangible personal property that is subject to Wisconsin sales or use tax. The

charge for the operator may be excluded from the amount subject to tax if the use of the operator is optional and separately stated. A common example is the use of cranes and other heavy equipment at construction sites. Usually the lessee is on site supervising or directing the operator or the crane or equipment. Therefore, the transaction is a lease (rather than a service) and taxable. In determining whether a transfer of an asset is a conditional sale versus a lease (impacts when the tax is reported - up front or on each payment), administratively Wisconsin looks to how the transaction is handled for federal income tax purposes. Such treatment is a little broader than the \$100 or 1-% test in the proposed definition 1(c). Licenses are included in the Wisconsin definition of lease. It is not clear whether licenses are specifically included in the proposed definition of lease or rental. Prospective changes affecting leases do not apply to existing leases except where the lease extended, renewed or modified on or after the effective date of the change.

Wyoming - The preceding definition is compatible with what our state uses. Wyoming does not differentiate between capital and operating leases. Indeterminate term leases are treated the same as term certain leases in Wyoming. The sales tax is collected during the lease stream.

2. What statutory changes would you have to make to your law to accommodate this definition?

Georgia - adopt the new language.

Idaho - The provision from subsection (1)(c) would have to be added to the Idaho statute.

Illinois - There currently is no statutory definition of a lease or rental. Legislation would need to be introduced to add that definition.

Indiana - With the exception of the change discussed above concerning equipment provided with an operator, Indiana would make no statutory changes.

Kansas - Would need to revise the definition and imposition sections, which are quoted above. It would be helpful to have the proposal be supported by a model regulation that more fully explains how the proposal should be applied. I am unclear how the proposed definition would treat rentals that are delivered in Kansas and used in another state. (Typical concerns are for such things as ice makers, refrigerators and other commercial fixtures.) I am unclear on whether the proposal is intended to exempt the purchase of items that will be held for rental. I am also unclear of how sale-leaseback transactions are taxed. Under Kansas law, these transactions are generally treated as financing arrangements with tax being collected only once on the transaction.

Louisiana - After the core definition, LA provides for 7 state level exclusions from the definition of "lease or rental." Those exclusions would have to be made into exemptions.

Maine - Maine would have to adopt the definition of Lease or Rental and impose the tax on lease streams.

Maryland - we would recommend that the general assembly specifically adopt this definition by legislation.

Minnesota - Would only need to change the definition of "nominal amount" to comply with the proposed definition.

Missouri - We do not foresee additional changes to statute, except adoption of the proposal. Adoption of this definition would potentially lead to minimal changes in interpretation of existing statutes under current case law.

New Jersey - Since the SSTP definition treats leases & rentals the same for sales tax purposes, New Jersey would have to amend its definition of "lease" to include "rentals" and delete the "more than 28 days" requirement. New Jersey also taxes leases and rentals differently. New Jersey law treats "the purchase of tangible personal property for lease" as a retail sale. Thus, the tax is legally imposed on & due from the lessor as the retail purchaser of the property (although the lessor delays payment of the tax until the property is actually leased, at which time it is due in full). The lessor can recoup this amount as an expense of the lease but should not invoice it as "sales tax" because the lessee is not responsible for the tax in a lease transaction. The definition of "retail sale" would have to be amended to delete the provision defining the purchase of property for lease as a retail sale. A rental is treated differently in that each rental payment is subject to the collection of sales tax by the rental company. The incidence of the tax is on the customer. It is possible to have consecutive rental periods which would exceed 28 days but still be taxed as a rental rather than a lease. In order to adopt the SSTP definition, significant statutory changes will be required, since the current law distinguishes between the two types of transactions and imposes the tax on a different party (lessor in a lease/renter in a rental) at a different time (up-front in a lease/with each rental period in a rental).

North Carolina - The primary definition would have to be modified somewhat and the provisions for what a lease is not, the motor vehicle provisions and the characterization provisions would have to be added.

North Dakota - We would have to provide a definition for "lease or rental".

Oklahoma - To comply with 1.b., we would adopt new regulation.

Rhode Island - Currently the lessor has an option to pay tax on cost. Although this isn't addressed in this section, it may have to be changed if leases are required to follow all other sales rules.

South Dakota - No changes necessary.

Tennessee - Replace the current definition of "lease or rent" with the SSTP definition and modify T.C.A. Section 67-6-204(b) to be consistent with the SSTP provision on providing tangible personal property with an operator. This section of Tennessee law currently provides: (b) If the owner of the property maintains continuous supervision over the personal property being leased or rented, and furnishes an operator or crew to operate such property, the owner is rendering a service, and the same is not subject to sales or use tax. On the other hand, if the owner does not furnish the crew or operator, but merely rents the property, and the lessee operates it personally for a stated consideration or price, either by the day or week or month, in such case, the sales or use tax would apply as the lessee has the possession, use and control of the property. If the owner of the property furnishes flight training, the owner is rendering a service, and the property used therein shall not be subject to sales or use tax. Repeal or revise Rule 32(6) which provides in part: "Where it is contemplated that a person shall have the right to use tangible personal property only on the premises of the

owner, and such premises are occupied by the owner in the conduct of his business, the transaction shall be regarded as a license to use tangible personal property, and not as a rental thereof, and the owner shall pay any applicable Sales or Use Tax on the purchase price thereof. The transaction shall not be regarded as a license to use if the premises are occupied by the lessee or the property is removed from the premises of the lessor."

Texas - No statutory change would be required, but rule amendment would be necessary.

Utah - Rule 8865-19S-32 would need to be modified to be consistent with the SSTP definition.

Vermont - None. We could adopt the definition by rule.

Washington - Washington tax statutes don't define lease or rental and the proposed definition is mostly consistent with our current practice. Not much would have to be done statutorily. One exception is in the area of transfers for resale. We would not need a change for sales tax purposes, but because we tax these as sales for business and occupation tax (a gross receipts tax on the privilege of engaging in business) purposes, we would have to make some accommodation in the law to continue to tax these wholesale transactions.

Wisconsin - The imposition of sales or use tax on the "sale, lease, or rental" of tangible personal property or taxable services would be revised to impose tax on the "sale, lease, rental, or license" of tangible personal property or taxable services.

Wyoming - Enact a law that incorporates the preceding definition.

3. What, if any, impact would this have on your sales or use tax collections?

States that said this would little or no impact on tax collections.

Idaho, Missouri, North Dakota, Rhode Island, South Dakota, Vermont, Texas, Washington, Wyoming

Indiana - Impossible to accurately predict but suspect minimal to none.

Louisiana - For the most part, collections should remain more or less constant, as the two definitions are not that different. The addition of "along with an operator" could lead to increased collections by clarifying the department's position and making it mandatory in the statute.

North Carolina - The impact should be minimal. Some transactions currently considered to be leases might be conditional sales contracts with the thresholds; however, I do not imagine that the total amount collected will vary to a significant degree.

Oklahoma - The impact would be a minimal positive impact. Currently transactions under 1(b) are considered rentals and only the monthly receipts are taxable. If the transaction is considered a sale, then the full gross receipts over the term of the contract would be due upon transfer of possession.

States that said this would have an impact on tax collections or are unsure.

Georgia - The impact would be difficult to project.

Illinois - The provisions regarding nominal options to purchase being limited to the lessor of \$100 or 1 % of the contract price would impact some leases whereby the Department has characterized other payment amounts in excess of \$100 or 1 % of the contract price as still being a nominal payment amount. This will require the Department to treat these types of leases as conditional sales agreements with differing tax treatment in this State. This may actually reduce tax collections because Illinois taxes leases up-front on the purchase price of the leased property as described above. We are not exactly sure what effect subpart (2) of the definition would have on Illinois sales and use tax collections.

Iowa - I would guess it is going to be more than a million per year.

Kansas - The current Kansas treatment of leases and rentals has created loop-holes that need to be plugged. Any statutory change for leases and rental should help plug them and increase revenues. However, I am uncertain if the purchase of property to be rented is exempt under the proposal, or how lease made in interstate commerce are to be treated. These things would also impact on revenues.

Maine - If the Maine legislature chooses to adopt the SSTP definition and impose tax on existing lease streams, the financial impact is not expected to be significant. However, if the legislature does not choose to tax existing leases, the financial impact will be significant.

Maryland - The blanket exemption for equipment and operator transactions would reduce receipts by some amount (possibly offset by a reduction in some sales for resale claims). Without doing a study, I would estimate the fiscal effect at less than \$1,000,000.

Minnesota - Adopting the proposed nominal definition would treat more transactions that are now considered sales under Minnesota law as leases. This would create a shift in sales tax revenues collected and remitted on these contracts from up-front payment to a per lease payment.

New Jersey - Currently, the state receives the tax up-front, in full, with no right to a refund if the property is damaged, destroyed, moved out of state, etc. Presumably, the State could adopt the SSTP definition of "lease or rental" and amend its statute to include the requirement that the tax be paid at the time the transaction is entered into (up-front), rather than with each payment.

Tennessee - The change in treatment of leases with nominal option to purchase (i.e. treating this as an up-front sale rather than lease) would accelerate revenues. The change in treatment of what we have considered leases under 1(b) appears to decrease revenues because we would not be treating the transaction as a lease and then as a sale.

Utah - The impact would be difficult to project at this time.

Wisconsin - A revenue loss will result from transfers of equipment with operators which are currently treated as leases. Note that this is an area of great confusion for taxpayers and auditors. Although we would expect a revenue loss, the confusion we currently face would be gone.