Cite as Det. No. 06-0232, 26 WTD 125 (2007)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Refund of	)	D E T E R M I N A T I O N
	)	
	)	No. 06-0232
. . .	)	
	)	Registration No. . . .
	)	Docket No. . . .

RULE 178, RULE 211; RCW 82.12.020: USE TAX – LEASE – DOMINION AND CONTROL –RENTAL OF EQUIPMENT WITH OPERATOR. Sound and lighting company did not relinquish dominion and control over its equipment when it leased the equipment to its customers with an operator. As such, because the taxpayer did not pay retail sales tax on the equipment, taxpayer was liable for use tax on the equipment.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

C. Pree, A.L.J – Sound and lighting company petitions for refund of use tax it paid on its use of sound and lighting equipment, which it leased to customers both with and without an operator. We deny the petition because we conclude that the taxpayer did not relinquish dominion and control over the equipment to its customers when it leased the equipment with an operator.[1]

ISSUE:

Did a sound and lighting company relinquish dominion and control over its equipment, such that it is not liable for use tax on the equipment, when it leased the equipment to its customers with an operator?

FINDINGS OF FACT:

The taxpayer leases sound and lighting equipment to third parties. Approximately 93% of the time, it sets up the equipment and leaves it for its customers' own sound technicians to operate. However, approximately 7% of the time, the taxpayer operates the equipment, following directions provided by its customer. These directions are generally provided digitally via a disk

[1] Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

or other medium. The directions specify which program the taxpayer should follow. Alternatively, the customer may verbally explain what volume level, etc., it expects the taxpayer to use.

The taxpayer did not pay retail sales tax when it purchased the equipment. However, between 2001 and 2003 it paid use tax on the equipment. The taxpayer subsequently filed amended returns for the period of 2001 through 2003, claiming a credit of use tax it paid on the equipment in the total amount of $. . . .

The Taxpayer Accounts Administration Division (TAA) denied the credit because it concluded the taxpayer did not demonstrate it relinquished dominion and control over the equipment to its customers. TAA requested copies of the taxpayer's lease agreements with its customers, but the taxpayer did not provide them. At the hearing in this matter, the taxpayer explained its contracts are generally verbal.

The taxpayer appeals TAA's denial of its request for credit. The taxpayer argues it purchased the equipment for resale without intervening use and accordingly does not owe sales or use tax on its purchase and use of the equipment.

ANALYSIS:

Washington has both a retail sales tax and a use tax. Retail sales tax is an excise tax imposed on each retail sale in this state, to be paid by the buyer to the seller. RCW 82.08.020; RCW 82.08.050. The use tax complements the retail sales tax by imposing a tax, generally equal in amount to the retail sales tax, on the use of items of tangible personal property in this state, as a consumer, where the retail sales tax has not been paid. RCW 82.12.020; WAC 458-20-178 (Rule 178).

A sale to a person who presents a resale certificate and "[p]urchases for the purpose of resale as tangible personal property in the regular course of business without intervening use by such person" is expressly excepted from the definition of "retail sale." RCW 82.04.050(1)(a). The term "retail sale" includes the renting or leasing of tangible personal property to consumers. RCW 82.04.050(4). Thus, as we concluded in Det. No. 04-0145R, 24 WTD 400 (2005), "the retail sales tax does not apply upon sales of tangible personal property to persons who purchase the same solely for the purpose of renting or leasing such property **without** operators." (Emphasis added; *citing* WAC 458-20-211(6)(a) (Rule 211(6)(a)); *see also* Det. No. 00-024, 19 WTD 710 (2000).

In contrast, as Rule 211(4) explains, "Generally persons who rent equipment **with** an operator[2] are not purchasing the equipment for resale as tangible personal property and must pay retail sales or use tax at the time the equipment is acquired." (Emphasis and footnote added.) *See also* Rule 211(6) ("[T]he retail sales tax applies upon sales to persons who provide such property with

[2] Rule 211 explains that "rental of equipment with operator" means "the provision of equipment with an operator to a lessee to perform work under the specific direction of the lessee. In such cases the lessor is generally not responsible for performing work to contract specification and does not determine how the work will be performed."

operators for a charge, without relinquishing substantial dominion and control.") This is because persons who rent equipment with operators may be exercising sufficient dominion or control over the property to constitute "intervening use" of the property.[3]
Rule 211(3) explains the distinction between the rental of equipment with an operator and a "true" lease,[4] as follows:

> A true lease . . . of personal property does not arise unless the lessee . . . actually takes possession of the property and exercises dominion and control over it. Where the owner/lessor of the equipment . . . maintain[s] dominion and control over the personal property and actually operate[s] it, the owner/lessor has not generally relinquished sufficient control over the property to give rise to a true lease . . . of the property.

In discussing what constitutes dominion and control and the effect of the lessor retaining dominion and control over the property for purposes of its retail sales tax or use tax liability on its purchase or use of the property, Rule 211(4) explains:

> Persons renting operated equipment to others may purchase the equipment without payment of retail sales tax only when the equipment is rented as tangible personal property. This can be demonstrated only when:
>
> (a) The agreement between the parties is designated as an outright lease or rental, without reservations; and
> (b) The lessee acquires the right of possession, dominion, and control of the equipment, even to the exclusion of the lessor.
>
> This last requirement is a factual question and the burden of proof is upon the owner/operator of the equipment to establish that the degree of control has been relinquished necessary to constitute a lessor-lessee relationship. Weight will be given to such factors as who has physical, operating control of the equipment; who is responsible for its maintenance, fueling, repair, storage, insurance (risk of loss or damage), safety and security of operation, and whether the operator is a loaned employee. If control of these factors is left with the owner/operator, then as a matter of fact, there has not been a relinquishing of control of the equipment to the degree necessary to create a lessor-lessee

[3]Intervening use occurs when an item held for resale is used by the business as a consumer before the item is sold, or when an item held for lease is also used by the lessor for personal purposes. *See, e.g.,* Det. No. 04-0145R, 24 WTD 400 (2005). For purposes of the use tax, RCW 82.12.010(2) broadly defines "use" as having its "ordinary meaning, and shall mean the first act within this state by which the taxpayer takes or assumes dominion or control over the article of tangible personal property (as a consumer)." RCW 82.04.190, in turn, defines a "consumer" as "Any person who purchases, acquires, owns, holds, or uses any article of tangible personal property irrespective of the nature of his business . . . other than for the purpose (a) of resale as tangible personal property in the regular course of business."

[4] Rule 211 defines a "true" lease as "the act of leasing property to another for consideration with the property under the dominion and control of the lessee for the term of the lease with the intent that the property will revert back to the lessor at the conclusion of the lease."

> relationship for the rental of tangible personal property. This is true, even though the customer exercises some constructive control over such matters as when and where the equipment is used in connection with the construction work being performed, i.e., the contractor controls the job site.

Thus, the taxpayer's purchase and use of the equipment would not be subject to retail sales or use tax only if its agreement with its customers was designated a lease without reservations and its customers acquired the right of possession, dominion, and control of the equipment, to the exclusion of the taxpayer. We do not have information regarding many of the factors listed in Rule 211. However, we conclude that although the taxpayer followed the directions of its customers in adjusting the sound and lighting, the taxpayer retained physical, operating control of the equipment. Thus, because control of these factors was left with the taxpayer/operator, pursuant to Rule 211, "there has not been a relinquishing of control of the equipment to the degree necessary to create a lessor-lessee relationship for the rental of tangible personal property." As such, TAA was correct in denying the taxpayer's requested credit of use tax.

Although the taxpayer agrees it rents equipment with an operator approximately 7% of the time, it argues TAA "failed to apply the true object test." Rule 211(2) defines the "true object test" as "the analysis of a transaction involving equipment and an operator to determine if the lessee is simply purchasing the use of the equipment or purchasing the knowledge, skills, and expertise of the operator beyond those needed to operate the equipment." However, this test is not applicable to the determination of whether the lessor is liable for sales or use tax on its purchase and use of the equipment. Instead, this test is relevant in determining the lessor's B&O tax classification (and retail sales tax collection responsibilities, if any) with respect to the rental payments it receives from the lessee. *See* Rule 211(5)(d)(v). As explained above, Rule 211(4) addresses whether the lessor is liable for sales or use tax on its purchase and use of the equipment. We explained this distinction in a context similar to the taxpayer's, as well as an example in Rule 211, upon which the taxpayer relies.

Example (8)(g) in Rule 211 addresses a situation similar to the taxpayer's, as follows:

> ABC Sound Productions provides lighting, amplifying equipment, and speakers as part of the services it sells to entertainment promoters. ABC also provides several operators of the equipment. This is a rental of equipment with operator. In applying the true object test, the promoter is primarily purchasing the use of the lighting and sound equipment. The performer or promoter could be expected to specify the color, location, and degree of lighting and may also request changes and modifications to the level of sound amplification during the performance.

In Det. No. 00-073, 19 WTD 1032 (2000), we addressed a situation similar to example (8)(g) and concluded the taxpayer was not liable for service B&O tax on its receipts from customers, as the taxpayer argued, but was instead liable for retailing B&O and retail sales tax because it was renting equipment with an operator. We reasoned, "The key is the true object test," and "Promoters are primarily purchasing the use of sound and lighting equipment, not expertise of

the taxpayer beyond those skills needed to operate the equipment." *See* Rule 211(2)(e). As we explained in Det. No. 00-073:

> We also understand the taxpayer's confusion because many of the factors listed under subsection (4)(a) would appear to support the taxpayer's position that it keeps control of the equipment. The taxpayer retains physical, operating control of the equipment; and is responsible for its maintenance, fueling, repair, storage, and insurance. However, subsection (4) addresses whether taxpayers renting equipment with operators must pay retail sales tax on their purchase of the equipment by examining whether the equipment was acquired for resale . . . not the taxability of the taxpayer's charges to its customers. [Subsection (4)] is not meant to replace the true object test in determining whether the taxpayer is providing a service or renting equipment with an operator.

CONCLUSIONS OF LAW AND DISPOSITION:

The taxpayer's petition is denied.

Dated this 21st day of September, 2006.