OKLAHOMA TAX COMMISSION

TAX POLICY AND RESEARCH DIVISION
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November 30, 2000

Re: Our file Number LR-00-185; Whether a transaction is correctly classified as a lease of tangible personal property, and the correct taxation of certain transactions if it is.

Dear

This is in response to your inquiry which consisted of a very detailed fact situation and three questions. I have set out your fact situation below, followed by your questions and our answers:

FACTS

COMPANY is a corporation engaged in the business of purchasing tangible personal property ("TPP") and providing it to various non-profit institutions ("INSTITUTION"), one or more of which is located in Oklahoma, in return for consideration as discussed below. INSTIUTION (sic) is exempt from paying sales and use taxes pursuant to Oklahoma statutes.

COMPANY enters into an agreement with INSTITUTION for an initial term of 10 years. COMPANY contracts with third parties to have the TPP installed on INSTITUTION's property. COMPANY provides initial training regarding the TPP to INSTITUTION. In return for the TPP, INSTITUTION is required to remit a specified amount of money to COMPANY at specified intervals. In addition, INSTITUTION grants COMPANY the exclusive right to sell services relating to the TPP. The revenues from the sale of these services are to be split between INSTITUTION and COMPANY based on a revenue sharing arrangement. Pursuant to the contract, INSTITUTION receives all of the receipts from the sales of service until a certain financial milestone is met. Once the first milestone is met, the receipts in excess of the first milestone are compared to a second financial milestone. If the receipts are in excess of that second milestone, INSTITUTION and COMPANY share the receipts according to a fixed percentage. If the receipts do not exceed the second milestone, COMPANY retains all receipts in excess of the first

milestone. The, second financial milestone is intended to ensure COMPANY is covered for all costs -- including depreciation, interest and finance charges relating to the TPP. INSTITUTION has possession and ultimate control of TPP. INSTITUTION's employees direct-operate the TPP. However, as a part of the agreement COMPANY is to provide the institution with an individual who is available by pager or by phone 12 hours a day/7 days a week and in person while the TPP is being operated. This individual would be present or available by telephone to provide any technical assistance needed during the operation of the TPP. In addition this individual would be present while the TPP was in operation to ensure the service arrangements that have been made with third parties are carried out by INSTITUTION. INSTITUTION has the right to reject providing any services sold by COMPANY, unless it would be unreasonable to reject the sales.

COMPANY provides all services and maintenance functions as required of the manufacturer of the TPP as set forth in the Full Service Maintenance Agreement and standard warranty. Damages that are outside the scope of these agreements are the responsibility of INSTITUTION. Both parties provide to carry insurance on the TPP. INSTITUTION is responsible for providing all utilities that are necessary to operate the TPP.

It is estimated that INSTITUTION's use of the TPP to fulfill COMPANY's service arrangements is less than 25% of the total time the TPP is in use. COMPANY provides the material for INSTITUTION to fulfill COMPANY's services arrangements.

Upon expiration of the contract INSTITUTION has three options. INSTITUTION can return the TPP to COMPANY, purchase the TPP outright from COMPANY (purchase price is stipulated in the contract) or renew the agreement. In addition, INSTITUTION has the right, at anytime during the contract, to purchase TPP for a stipulated price. It is COMPANY's full expectation that upon completion of the contract INSTITUTION will exercise the option to purchase the TPP.

ISSUES

A. Is the transaction correctly classified as a lease?

Response: Yes.

B. Is the original purchase of the TPP exempt from sales/use tax?

Response: It would be exempt only if COMPANY is buying it for resale, including buying it for lease or rental, and if COMPANY holds an Oklahoma Sales tax permit.

C. Are the payments received from INSTITUTION subject to sales/use tax?

Response: Your fact situation stated that INSTITUTION was exempt from sales tax. We do not have enough information concerning the status of INSTITUION to make an affirmative statement concerning that exemption. However, if it is in fact exempt, the

payments from INSTITUTION to COMPANY are not subject to sales tax. On the other hand, for the revenues that arise from the sale of the services for COMPANY, since the tangible personal property held for resale is being used for COMPANY's own use, sales tax is due on the "sales value" of such use of the tangible personal property. "Sales Value" is defined in Oklahoma Tax Commission Rule 710:65-1-2.

This response applies only to the circumstances set out in your request of September 1, 2000. Pursuant to Commission Rule 710:1-3-73(e), this Letter Ruling may be generally relied upon **only** by the entity to whom it is issued, assuming that all pertinent facts have been accurately and completely stated, and that there has been no change in applicable law.

If I can be of further assistance, please feel free to contact me.

Sincerely,
OKLAHOMA TAX COMMISSION

Michael G. Pillow
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