

Title: Lease of Equipment

Jan 12, 1994

Re: Technical Assistance Advisement 94M-001

Sales Tax / Documentary Stamp Tax;

Finance Agreement Denominated a Lease

Chapters 201 and 212, Florida Statutes

XXX (Herein the "**Parent**")

FEI# XXX

XXX (Herein the "**Leasing Company**")

Parent's Affiliate Banks and Non-banking Subsidiaries

Identified in Your April 28, 1993, Petition (Herein

collectively "**Affiliates**" or singularly "**Affiliate**")

Dear :

This response is in reply to your October 4, 1993, petition for the Department's issuance of a Technical Assistance Advisement ("TAA") pursuant to s. 213.22, F.S., concerning the captioned matter and parties. Your petition has been carefully examined and the Department finds it to be in compliance with the requisite criteria set forth in Chapter 12-11, F.A.C. Therefore, the Department is herewith granting your request for the issuance of a TAA and the ensuing discourse shall embody said ruling.

DISCUSSION OF FACTS

Your petition and supporting documents impart the following significant information regarding the issues under advisement herein:

FROM YOUR PETITION

"[Leasing Company] is an affiliate of [Parent]. [Parent] is the holding company of the [Affiliates] listed on the above chart.... [Leasing Company] is preparing documentation for equipment financing arrangements between

[Affiliate] and the customers of [Affiliate]. These financing arrangements will be utilized to allow the customers to finance through [Affiliate] the purchase of tangible personal property with the funds of [Affiliate]. Each of the financing arrangements will be evidenced by a 'Commercial Equipment Lease' (hereinafter referred to as the 'Finance Agreement'). A form Finance Agreement is attached to this request as Exhibit A.

"Although the Finance Agreement is denominated a 'lease,' the provisions of the Finance Agreement substantively create a financing and security arrangement rather than a 'true' lease. Under the Finance Agreement, [Affiliate] provides financing from time to time to allow the customers to purchase equipment. When the customer decides to purchase equipment, the customer executes a Schedule of Repayment (the 'Schedule') identifying the item to be purchased. The Schedule sets out the terms of repayment, the provisions of which are triggered by the execution of an Acceptance Certificate. The Acceptance Certificate is executed by the customer at the time it receives and accepts the equipment. The Acceptance Certificate and the Schedule are both attached to the Finance Agreement.

"The customer purchases the equipment from the party and at all times holds title to, and retains possession of, the equipment. At no time will [Leasing Company] or [Affiliate] hold title to the equipment or have the right to the possession of the equipment, except in the event that the customer defaults on its obligations with [Affiliate].

"The Schedule describes the property to be financed and the payment schedule under which the customer is to repay Affiliate for the financing of the equipment. The Schedule includes sections titled 'Interim Equipment Payments' and 'Equipment Payments' which state the term of the payments and the amount of each payment. The amount of Interim Equipment Payments includes interest only, and the amount of Equipment Payments includes both principal and interest. The actual amount financed by the customer is not

separately stated under the Equipment Payment section of the Schedule. The amount financed can be determined by looking at another section of the Schedule in which the customer authorizes [Affiliate] to pay the customer(or the customer and the seller jointly) a certain dollar amount for the equipment. In the event that the customer makes a prepayment under the Schedule, the finance Agreement provides that the final payment shall be adjusted to give credit for any unearned interest."

The following provisions are found in an attached document styled, "Commercial Equipment Lease" or as identified in your letter dated October 4, 1993, as a "Finance Agreement":

"MASTER LEASE. Lessee wishes to purchase certain equipment from time to time and has requested that Lessor provide the financing for such equipment pursuant to the terms of this Lease. The relationship between Lessor and Lessee is to be a continuing one over a period of time, with items of equipment being added to or deleted from the equipment financed by this Lease from time to time, by the addition or deletion of schedules to this Lease, and this Lease shall be a master lease agreement applying to all such equipment.

"In consideration of the foregoing and other valuable consideration, Lessor and Lessee agree as follows:

"LEASE. Lessor and Lessee agree that Lessor will finance pursuant to the provisions of this Lease the equipment that is described on one or more schedules of equipment executed pursuant to this Lease and signed by Lessor and Lessee from time to time, which schedules (the `Schedules') are incorporated herein by reference and are deemed to be included in any reference to this Lease....

"SECURITY INTEREST. Notwithstanding that this instrument is referred to as a `Lease,' Lessee will at

all times hold title to the Equipment during the term of payments for such Equipment. Lessee hereby grants to Lessor a security interest in the Equipment, whether now or hereafter covered by this Lease....

"Perfection of Security Interest. Lessee agrees to execute such financing statements, notices of lien, and powers of attorney, and to take whatever other actions are requested by Lessor to perfect and continue Lessor's security interest in the equipment, including the delivery to Lessor of all certificates of title or manufacturer's certificates of origin....

"Title. Lessee represents and warrants to Lessor that it holds good and marketable title to the Equipment, free and clear of all liens and encumbrances except for the lien of this Lease....

"LESSEE'S RIGHT TO POSSESSION. Until an Event of Default, Lessee may have possession and beneficial use of all the Equipment and may use it in any lawful manner not inconsistent with this Lease...."

The following provision is found in an attached document styled "Delivery and Acceptance Certificate":

"(f) Lessee acknowledges that Lessor is neither the manufacturer, distributor, seller, or owner of the Equipment, and that Lessor has no knowledge or familiarity with it...."

The following provisions are found in an attached document styled "Schedule of Equipment":

"Pursuant to the Lease, Lessee hereby requests and authorizes Lessor to pay \$_____ (the `Amount Financed') to the party or parties specified in the pay proceeds letter or letters provided in connection herewith. Lessee hereby grants to Lessor a security interest in the foregoing Equipment and the related property, as more fully described in the Lease."

REQUESTED ADVISEMENT

You endeavor to elicit the Department's advice regarding the following specific issues:

Sales tax: "Whether the Florida sales tax is inapplicable to above described transaction under which [Affiliate] is to provide financing in order for the customer to purchase tangible personal property."

Documentary stamp tax: "Whether the Florida documentary stamp tax is applicable to the total amount of payments made by the customer to [Affiliate] under the finance agreement (i.e., principal and interest) or whether it is applicable only to the portion of the total amount of payments which constitutes principal."

DISCUSSION OF LAW

SALES TAX

We consult the following passages of the Florida Statutes as pertinent to the resolution of your question regarding sales and use tax:

Section 212.02(16)(a), F.S.: "'Sale' means and includes: (a) Any transfer of title or possession, or both exchange, barter, license, lease, or rental, conditional or otherwise, in any manner or by any means whatsoever, of tangible personal property for a consideration...."

Section 212.05, F.S.: "It is hereby declared to be the legislative intent that every person is exercising a taxable privilege who engages in the business of selling tangible personal property at retail in this state, including the business of making mail order sales, or who rents or furnishes any of the things or services taxable under this chapter, or who stores for use or consumption in this state any item or article of tangible personal property as defined herein and who leases or rents such

property within the state.

"(1) For the exercise of such privilege, a tax is levied on each taxable transaction or incident, which tax is due and payable as follows:....

"(c) At the rate of 6 percent of the gross proceeds derived from the lease or rental of tangible personal property, as defined herein, except the lease or rental of a commercial motor vehicle as defined in s. 316.003(66)(a) to one lessee or rentee for a period of not less than 12 months when tax was paid on the acquisition of such vehicle by the lessor, when the lease or rental of such property is an established business or part of an established business or the same is incidental or germane to such business.

"(d) At the rate of 6 percent of the lease or rental price paid by a lessee or rentee, or contracted or agreed to be paid by a lessee or rentee, to the **owner** of the tangible personal property...."

(Emphasis Supplied)

Section 212.11(3), F.S.: "Except as otherwise expressly provided for herein, it is hereby declared to be the intention of this chapter to imposed a tax on the gross proceeds of all leases and rentals of tangible personal property in this state when the lease or rental is a part of the regularly established business, or the same is incidental or germane thereto."

Section 212.02(10)(g), F.S.: "(g) 'Lease,' 'let,' or 'rental' also means 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, except as expressly provided to the contrary herein."

The operative rule construing and elucidating the forgoing statutory definition of the term "Lease" is Rule 12A-1.071, F.A.C., which states the following:

"(1)(a) For the purpose of this rule, the term 'lease' includes any rental or license to use tangible personal property, unless a different meaning is clearly indicated by the context in which it is used. **The term refers to all**

transactions that are not bailments in which there is a transfer of possession of tangible personal property, without regard to limitations upon the use, for a consideration, without a transfer of title to the property.

It is not essential for a transfer of possession of tangible personal property to include the right to move the tangible personal property. It includes a transaction under which a person secures for a consideration the temporary use of tangible personal property which, although not on his premises, is operated by or under the direction or control of the person or his employees. All leases of tangible personal property other than conditional-sale type leases as described in paragraph (1)(d) of this Rule, are operating leases. Whether a transaction is a `sale' or a `rental, lease, or license to use' shall be determined in accordance with the provisions of the agreement.

"(b) Transfer of possession with respect to an operating lease means that one of the following attributes of tangible personal property ownership has been transferred:

"1. Custody or possession of the property, actual or constructive;

"2. The right to custody or possession of the property; or,

"3. The right to use and control or direct the use of the property. (Emphasis Supplied)

FINDING

It is clear from the foregoing statutory law, that the legislature intends the application of sales tax to the lease of tangible personal property. Moreover, it is clear that the statutory definition of the term `lease', set out above, with respect to the lease of tangible personal property contemplates an instrument which transfers possession and not title to the lessee for a consideration. Additionally, elucidation of the elements constituting a "lease" of tangible personal property for sales tax purposes are set forth in Rule 12A-1.071(1), F.A.C., above. Consistent with the statutory definition of such leases noted above, the rule envisions a lease for sales tax purposes as an instrument which for consideration grants the actual or constructive custody or possession of tangible personal property, the right to such custody or possession, or

the right to use and control or direct the use of tangible personal property. When considering the elucidation of the statutory definition of the term "lease" provided by the rule, keep in mind that agency determinations with regard to a statute's interpretation and applicability are entitled to great deference and have considerable persuasive force in the absence of clear error or conflict with legislative intent. Little Munyon Island, Inc. v. Department of Environmental Regulation, 492 So.2d 735, 737 (Fla. 1st DCA 1983); Santaniello v. Department of Professional Regulation, 432 So.2d 84, 85 (Fla. 1st DCA 1983); State Ex Rel. Szabo Food Serv., Inc. of N. C. v. Dickinson, 286 So.2d 529, 531 (Fla. 1973), reh. den. Jan. 9, 1974.

A careful examination of the terms and conditions of the Commercial Equipment Lease (the "Finance Agreement"), in particular those excerpts replicated above, reveals that such terms and conditions objectively manifest the substance of the Finance Agreement to be a financing contract and not a lease. The Finance Agreement does not transfer possession of the equipment to the Lessee (the "Purchaser"). To the contrary, the Purchaser receives possession and title to the equipment directly from the vendor and simply pays the purchase price to the vendor using funds advanced by Affiliate. Recall that item (e) of the terms of the Delivery and Acceptance Certificate which is incorporated into the Finance Agreement by reference contains an express acknowledgement that the Affiliate is neither the manufacturer, distributor, seller, nor owner of the Equipment. Thus, Affiliate cannot very well transfer possession or title to the equipment to the Purchaser when Affiliate has neither. In fact, under the terms of the Finance Agreement, the Affiliate will never have possession of or gain title to the equipment unless and until an act of default by the Purchaser occurs.

It is clear from the terms and conditions of the Finance Agreement that the substance and function of the Finance Agreement is to establish a contractual relationship of lender and borrower by and between Affiliate and Purchaser as opposed to that of lessor and lessee. The Finance Agreement in substance provides for the advancing of funds from Affiliate to

Purchaser for Purchaser's use in acquiring equipment from third party vendors. The Finance Agreement further provides for the creation, perfection, and maintenance of a security interest in favor of the Affiliate with respect to the equipment purchased by Purchaser in order to secure repayment by the Purchaser of the purchase funds advanced by Affiliate.

Inasmuch as the substance of the Finance Agreement reveals that it is a financing contract and not a lease under the sales tax law discussed herein, the payments made by Purchaser to Affiliate pursuant to and in accord with the Finance Agreement constitute the repayment of borrowed funds secured by the Purchaser's equipment as collateral and, hence, are not lease payments. The substance of a transaction and not the form in which it is cast determines its tax treatment. See Department of Revenue v. Anheuser-Busch, 527 So.2d 877 (Fla. 1st DCA 1988), reh. den. Aug. 1, 1988; Department of Revenue v. Seaboard Coastline R. Co., 480 So.2d 1349 (Fla. 1st DCA 1985), rev. den., 492 So.2d 1331 (Fla. 1986).

Therefore, in summation, the Department hereby affirms that the payments made by the Purchaser to the Affiliate pursuant to and in accord with the Finance Agreement are not subject to sales or use tax since: (i) neither title nor possession of the equipment ever resides with the Leasing Company or the Affiliates except in the event of a default by the Purchaser under the Finance Agreement; (ii) neither the Leasing Company nor the Affiliate can convey title or possession of the equipment to the Purchaser as neither is vested with title and neither has possession of the equipment; and (iii) the Finance Agreement does not operate nor does it have the capacity to transfer title or possession of the equipment from the Leasing Company or the Affiliate (neither of whom have title or possession of the equipment) to the Purchaser. In short, the Finance Agreement does not manifest the required element of transferring title or possession of the equipment for a consideration necessary to constitute a "sale" under the definition of the term "sale" provided in s. 212.02(16)(a), F.S., for sales tax purposes.

DOCUMENTARY STAMP TAX

Documentary stamp tax is due on the total amount financed unless the document clearly sets forth the principal amount distinguished from the interest portion. If the interest is unconditionally payable, the documentary stamp tax is payable on the total amount financed, both principal and interest.

This response constitutes a Technical Assistance Advisement under s. 213.22, F.S., which is binding on the Department only under the facts and circumstances described in the request for this advice as specified in s. 213.22, F.S. Our response is predicated on those facts and the specific situation summarized above. You are advised that subsequent statutory or administrative rule changes or judicial interpretations of the statutes or rules upon which this advice is based may subject similar future transactions to a different treatment than expressed in this response.

You are further advised that this response and your request are public records under Chapter 119, F.S., which are subject to disclosure to the public under the conditions of s. 213.22, F.S. Your name, address, and any other details which might lead to identification of the taxpayer must be deleted by the Department before disclosure. In an effort to protect confidential information, we request you notify the undersigned in writing within 15 days of any deletions you wish made to the request or this response.

Sincerely,

Daniel M. Wagner, Jr.
Tax Law Specialist
Technical Assistance

M.E. Clemens
Tax Audit Specialist
Technical Assistance

