

New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-85 (19)S
Sales Tax
June 12, 1985

STATE OF NEW YORK
STATE TAX COMMISSION

ADVISORY OPINION

PETITION NO. S840208A

On February 8, 1984 a Petition for Advisory Opinion was received from L.B. Smith, Inc., 2001 State Road, Camp Hill, Pennsylvania 17011.

The issue raised is whether a finance charge billed to a lessee who exercises a purchase option is subject to tax.

Petitioner is primarily engaged in the business of selling heavy construction equipment. Petitioner also leases such equipment for a monthly fee. Any costs incurred by Petitioner for the equipment being leased, such as interest, insurance, supplies etc., are included in determining the monthly lease charge and Petitioner charges sales tax on such charge.

In some instances the customer may actually want to purchase the equipment but cannot obtain financing. Under such circumstances, Petitioner may agree to lease the equipment to the customer for the same normal monthly lease charge and extend to the customer an option to purchase the equipment within a specified time period. The purchase price at the time of exercising the option is the same price the customer would have paid if he had purchased the equipment outright at the time the lease agreement was executed.

Upon exercising the purchase option, the customer is given credit toward the purchase price for all rental payments made to date. Additionally, however, the customer is required to pay a "finance charge" consisting of the total of the prime rate plus a fixed percentage computed on the declining unpaid balance from the date of commencement of the lease.

Petitioner maintains that this finance charge is the interest due from the customer in consideration of Petitioner's financing the equipment for the term of the lease prior to the exercise of the purchase option.

The issue as to the taxability of such charges has been addressed in the Sales and Use Tax Regulations at 20 NYCRR 541.9(b)(4). Such Regulations state:

"(4) Leases with option to buy. If a contractor leases equipment or motor vehicles with an option to buy, each lease payment is subject to tax. If the option is exercised, the amount subject to the tax is the total option purchase price for the equipment or motor vehicle.

* * *

TSB-A-85 (19)S
Sales Tax
June 12, 1985

Example 2: A lease agreement or contract provides for an option to purchase at a stated purchase price, less total lease payments made, plus one percent per month computed on the outstanding balance after each lease payment. The stated purchase price, less the lease payments, plus the one percent per month is the total option purchase price subject to the tax."

Since the original transaction entered into between Petitioner and its customer was a lease and the payments made by the customer were nothing more than rental payments, Petitioner did not extend any credit to the customer. The fact that the customer may exercise a purchase option at a future date does not alter the nature of the previous transaction for sales tax purposes.

Therefore, notwithstanding the fact that Petitioner characterizes its charge as a "finance charge", such charge is subject to tax as part of the total option price.

DATED: May 20, 1985

FRANK J. PUCCIA
Director
Technical Services Bureau

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth herein.