**TENNESSEE DEPARTMENT OF REVENUE**
**REVENUE RULING #97-29**

## WARNING

**Revenue rulings are not binding on the Department. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.**

### SUBJECT

Taxability of cylinders used by gas manufacturer.

### SCOPE

Revenue rulings are statements regarding the substantive application of law and statements of procedure that affect the rights and duties of taxpayers and other members of the public. Revenue rulings are advisory in nature and are not binding on the Department.

### FACTS

The taxpayer is a manufacturer located in Tennessee. It purchases cylinders and has the cylinders delivered to its Tennessee location. The taxpayer owns the cylinders. The cylinders are used to transport the taxpayer's finished product, gases, to the taxpayer's customers which may be located in Tennessee or outside of Tennessee.

The taxpayer offers two plans to customers with respect to the cylinders, "monthly rental" or "deposit." The customers who are on the monthly rental plan retain the cylinder for the first thirty days free of charge. After the initial thirty days, if the cylinder is not returned to the taxpayer, the customer is charged a monthly rental fee (approximately $.35 per day). The customers on the deposit plan pay a deposit (approximately $185.00, depending on the type of cylinder) and use the cylinder for the first sixty days free of charge. After sixty days, if the cylinder is not returned to the taxpayer, a rental fee (approximately $.24 per day) is accrued and deducted from the deposit paid by the customer. It would take approximately two years for the rental charges due to be offset by the deposit paid by the customer. If, after two years, the cylinder is not returned, the customer will be charged a monthly rental fee.

When the customer consumes the finished product, the cylinder is returned to the taxpayer's nearest location. The cylinder is then cleaned, serviced, and tested, if due for testing. The cylinder is then filled with finished product and sent out to another customer.

Most of the cylinders are returned to the taxpayer. The time frame a customer retains a cylinder depends on the finished product contained in the cylinder.

## QUESTIONS

1. Does the taxpayer have to pay sales and/or use tax on the purchase of the cylinder?

2. If the answer to question number 1 is yes, does the taxpayer have to charge sales and/or use tax on the rental of the cylinder in Tennessee?

3. Does the taxpayer have to charge sales and/or use tax on the deposit charged to the deposit plan customers in Tennessee?

4. If the answer to question number 3 is yes, should the sales and/or use tax collected by the taxpayer be refunded to the customer when the deposit, less a rental charge, is refunded to the customer?

5. (a) If the answer to question number 1 is no, does the taxpayer have to charge sales and/or use tax on the rental of the cylinder in Tennessee? (b) On the deposit?

## RULINGS

1. No.

2. Not applicable, due to the ruling for question number 1.

3. No tax is due on the collection of the deposit.

4. Not applicable, due to the ruling for question number 3.

5. (a) Yes. This would include situations involving deposits which are later applied to rental, when the cylinder is held for longer than the sixty-day period described in the facts.
(b) No tax is due on the collection of the deposit.

## ANALYSIS

The cylinder is clearly required in order to deliver the product, gases. The taxation of this type of container is governed by T.C.A. § 67-6-102(23)(E)(ii) and TENN. COMP. R. & REGS. 1320-5-1-.11(1).

T.C.A. § 67-6-102(23)(E) states, in pertinent part:

> "Sale at retail," "use," "storage," and "consumption" do not include the sale, use, storage or consumption of:
>
> * * *

> (ii) Materials, containers, labels, sacks, bags or bottles used for packaging tangible personal property when such property is either sold therein directly to the consumer or when such use is incidental to the sale of such property for resale ...

TENN. COMP. R. & REGS. 1320-5-1-.11 (hereinafter "Rule 11"), entitled "Containers, Wrapping and Packing Materials and Related Products" interprets this statute. The first paragraph of the regulation states:

> Items actually accompanying the product sold or shipped, without which the delivery of the product is impracticable on account of the character of the contents, and *for which there is no separate charge*, are not subject to Sales or Use Tax. These items include such things as containers, packing materials, labels or name plate affixed to products manufactured, and printed matter containing only directions for use. (Italics added.)

From the above, it can be seen that a container is tax exempt, if the container is necessary to accomplish delivery of the product, if the container accompanies the product as it is being sold (whether the sale is a sale to the consumer or a sale for resale), and if no separate charge is made for the container.

If a separate charge is made for the container, such a charge is taxable, in those cases where the sale of the product is taxable. The italicized portion of Rule 11 contemplates an exemption only for containers for which no separate charge is made. Further, the definition of "sales price" found in T.C.A. § 67-6-102(25)[1] would not permit the exclusion of the charge for the container.

With the above general analysis, each question presented in the ruling request will be addressed.

**1.**

If no charge is made to the customer for the cylinder, the purchase of the container is not subject to tax pursuant to the general analysis above. Whether or not the container is capable of being re-used does not have a bearing on this determination. See *Coca-Cola Bottling Co. of West Tenn. v. Celauro,* 1993 Tenn. LEXIS 319.

[1] "Sales price" means the total amount for which a taxable service or tangible personal property is sold, including any services that are a part of the sale of tangible personal property, valued in money, whether paid in money or otherwise, and includes any amount for which credit is given to the purchaser by the seller, without any deduction therefrom on account of the cost of the property sold, the cost of materials used, labor or service costs, losses, or any other expense whatsoever; provided, that cash discounts allowed and taken on sales shall not be included; provided, that "sales price" does not include any additional consideration given by the purchaser for the privilege of making deferred payments, regardless of whether such additional consideration shall be known as interest, time price differential on conditional sales contracts, carrying charges or any other name by which it shall be known; and provided further, that "sales price" does not include any federal retail excise tax imposed by §§ 4051-4053 of the Internal Revenue Code of 1954, as amended, or as such tax may be amended hereafter.

If a rental charge is made for the cylinder, the exemption explained in the foregoing does not apply to the cylinder rental charge. However, the taxpayer can acquire the cylinders without payment of tax as a purchase for resale, pursuant to TENN. COMP. R. & REGS. 1320-5-1-.32, which states in pertinent part:

> Tangible personal property sold to be used exclusively for renting or leasing may be sold upon a resale certificate.

Therefore, the taxpayer may purchase the cylinders free of tax, because the cylinders would either be exempt as containers or exempt as a purchase for resale.

**2.**

Since question number 1 was not answered in the affirmative, a ruling on this question is not required.

**3.**

Since the deposit does not represent a payment for the sale or rental of tangible personal property, or for a taxable service, but is merely security provided for the customer's safe return of the taxpayer's property, it is not subject to tax. Historically, the Department has not required the collection of sales tax on container deposits.

**4.**

Since question number 1 was not answered in the affirmative, a ruling on this question is not required.

**5.**

As explained previously, the exemption for containers does not apply in those situations where a charge for the container is made. Tax on rental of tangible personal property is imposed by T.C.A. § 67-6-204.[2] Therefore, if a cylinder is delivered to a consumer in Tennessee, or delivered for use in Tennessee, the Tennessee sales or use tax would apply to the rental charge for the cylinder.

[2] T.C.A. § 67-6-204(a) states: "It is declared to be the intention of this chapter to impose a tax on the gross proceeds of all leases and rentals of tangible personal property in this state where the lease or rental is a part of the regularly established business, or the same is incidental or germane thereto. The tax is levied as follows:
(1) At the rate of six percent (6%) of the gross proceeds derived from the lease or rental of tangible personal property, as defined herein, where 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 the business.
(2) At the rate of six percent (6%) of the monthly lease or rental price by lessee or renter, or contracted or agreed to be paid by lessee or renter, to the owner of the tangible personal property."

It should be noted that in those cases where a deposit is collected but later applied to the rental of the cylinder, as presented in the facts given in the ruling request, there is a tax consequence. In *Furniture Lease Co. v. Tidwell*, 495 S.W.2d 535 (Tenn. 1973), the Tennessee Supreme Court held that a deposit required by a lessor of tangible personal property was taxable as part of the gross proceeds of the lease, if the deposit were forfeited due to non-payment of the rental fee. The deduction of a rental fee from a deposit after the taxpayer's customer has held the cylinder for a longer period than allowed would similarly be subject to sales tax (at the time it is deducted from the deposit), if the cylinder had been delivered to the customer in Tennessee. In cases where a deduction is made from the deposit for cylinder rental, the tax can be collected by deduction from the deposit.

In regard to the second question [labeled "5(b)"], the question appears identical to that presented in question number 3 for which an analysis was previously provided.

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APPROVED: _____
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