



Private Letter Rulings

“Private letter rulings” are written statements issued to a taxpayer by the department, that interpret Wisconsin tax laws based on the taxpayer’s specific set of facts. Any taxpayer may rely upon the ruling to the extent the facts are the same as those in the ruling.

The ruling number is interpreted as follows: The “W” is for “Wisconsin”; the first four digits are the year and week the ruling becomes available for publication (80 days after it is issued to the taxpayer); the last three digits are the number in the series of rulings issued that year. The date is the date the ruling was issued.

Certain information that could identify the taxpayer has been deleted. Additional information is available in Wisconsin Publication 111, “How to Get a Private Letter Ruling From the Wisconsin Department of Revenue.”

The following private letter ruling is included:

Sales and Use Taxes

Service enterprises - testing services

Incidental - testing services

W0009001 (p. 26)

※ **W0009001** ※

Type Tax: Sales and Use Taxes

Issue: Service enterprises - testing services
Incidental - testing services

Statutes: Sections 77.51(5) and 77.52(2)(a), Wis. Stats. (1997-98)

Wis. Adm. Code: Section Tax 11.67 (November 1993 Register)

This letter responds to your request for a private letter ruling.

Facts

The taxpayer is a membership organization exempt from payment of federal income tax under section 501(c) (6) of the Internal Revenue Code of 1986, as amended (the “Code”). The taxpayer is a not-for-profit corporation formed under the laws of another state and is headquar-

tered in that state. It also has an office in Washington, D.C. The taxpayer has no office or other facility in Wisconsin. The taxpayer provides certain testing (“Testing”) services to specific enterprises (“Enterprises”) in Wisconsin.

The Testing program consists of the testing of Enterprises to determine whether the Enterprises meet certain standards required by federal law and by the taxpayer. Under a provision in 42 U.S.C., every Enterprise in the United States must be accredited periodically by a certain Agency of the United States (“AUS”) or another organization recognized by AUS as having standards that are equivalent to or more stringent than federal accreditation standards. The only entities that AUS has recognized for these purposes are the taxpayer, other not-for-profit organizations, and agencies of a few state governments.

In order to obtain accreditation, an Enterprise must, *inter alia*, participate in a Testing program. A Testing program evaluates the ability of participating Enterprises to accurately perform diagnostic services for clients. Specifically, the Testing program involves:

1. The transfer to a participating Enterprise of certain materials (“the Materials”) the composition of which is unknown to the Enterprise,
2. The analysis of the Materials by the Enterprise and transmission of the Enterprise’s findings to the taxpayer, and
3. The processing and evaluation of the Enterprise’s findings by the taxpayer.

By federal law, the furnishing of the Materials to the Enterprise must be by a government agency or a not-for-profit entity. Most of the Materials consist of a specific ingredient or other base that is “spiked” with the analytes for which each participating Enterprise must test. The taxpayer purchases the Materials from various manufacturers.

The manufacturer generally delivers the Materials by common carrier to a third party repackager retained by the taxpayer or ships the Materials by common carrier directly to each participating Enterprise. The manufacturer invoices the taxpayer for the Materials at the time

the manufacturer ships the Materials to the repackager or directly to the Enterprise. The repackager breaks down the manufacturer's bulk shipment into individual packages for shipment to the Enterprise, adds printed instructions supplied by the taxpayer, and then ships the materials by U.S. Mail or by common carrier to the participating Enterprise. The manufacturers are located both in and outside Wisconsin. The repackers are located outside Wisconsin.

The Enterprise has no independent use for the Materials apart from participating in the Testing program. Once a participating Enterprise has concluded its analysis of the Materials, the Enterprise generally disposes of those materials. The Enterprise sends a report of its analysis to the taxpayer at its headquarters in another state, where the taxpayer reviews the Enterprise's report. The taxpayer evaluates the Enterprise's analysis, and it provides its findings to the Enterprise and to the accreditation organization designated by the Enterprise. When the taxpayer provides the Enterprise with its results for each test, the taxpayer also provides the Enterprise with the mean result for that test, the standard deviation, the number of Enterprises that participated in the test, the standard deviation index, the lower and upper limits of acceptability, and a plot of the relative distance of the Enterprise's results from the established target as a percentage of the allowed deviation.

The taxpayer charges Enterprises a single subscription amount for participating in the Testing program. No separate charge is made for the Materials and for the Testing service. On average, the cost to the taxpayer of the Materials was historically about X% of the amount it invoiced customers for providing the Testing service. That percentage has been decreasing recently, and this year is expected to be approximately Y%. From time to time, the taxpayer also sells Materials to Enterprises (without providing Testing services) as replacements of items that were lost or broken prior to or during a test. The total sales of Materials apart from the testing program are equal to approximately Z% of the taxpayer's total receipts from the Testing program.

The specific Testing modules in which an Enterprise will enroll depends on the scope of the work done at the Enterprise. Thus, an Enterprise performing a wide range of analyses will participate in a larger number of modules than an Enterprise doing only basic testing. Each specific Testing module is priced separately.

Request

You ask the department to confirm that:

1. The "true object" of the taxpayer's Testing program is the administration of a Testing service rather than the provision of the Materials; therefore, the taxpayer's charges for participation in the Testing program are not subject to sales or use tax, and the taxpayer is deemed to be the consumer of the Materials.
2. The taxpayer is not subject to use tax on items shipped to Wisconsin Enterprises by common carrier from outside Wisconsin.
3. If the taxpayer is subject to use tax on items shipped to Wisconsin Enterprises by common carriers from outside Wisconsin, the taxpayer is entitled to a credit for tax properly paid to the state from which such materials were shipped.

Ruling

For purposes of the following ruling, it is assumed that although the taxpayer does not have a facility or office in Wisconsin, it is "engaged in business in Wisconsin" as the phrase is defined in sec. 77.51(13g), Wis. Stats. (1997-98), and sec. Tax 11.97, Wis. Adm. Code.

1. The taxpayer is providing a nontaxable service when it transfers Materials to a participating Enterprise and processes and evaluates the Enterprise's findings as a result of analysis of the Materials.

The Materials are considered to be transferred incidentally to participating Enterprises with the Testing services. Therefore, the taxpayer is considered to be the consumer of the materials used by the Enterprises.

Materials transferred to customers in Wisconsin without the furnishing of Testing services are subject to Wisconsin sales or use tax, unless the occasional sale exemption under sec. 77.54(7m), Wis. Stats. (1997-98), applies.

2. The taxpayer is not subject to Wisconsin use tax on its purchase of Materials that are shipped directly by out-of-state manufacturers (i.e., manufacturers with no business location in Wisconsin) to participating Enterprises in Wisconsin. However, the taxpayer is subject to Wisconsin sales or use tax on (a) Materials that are shipped by the repackager to participating Enterprises in Wisconsin and (b) Materials that are shipped by Wisconsin manufacturers (i.e., manufacturers with a business location in Wisconsin) to participating Enterprises in Wisconsin.

Materials furnished to customers without Testing services are not subject to Wisconsin sales or use tax because they are for resale.

3. The taxpayer may claim a credit against the Wisconsin use tax due on Materials for tax properly due and paid to another state on the same Materials (i.e., the sale of the Materials to the taxpayer would have had to occur in the other state or use of the materials must have first occurred in the other state).

Analysis:

1. Section Tax 11.67(1), Wis. Adm. Code (November 1993 Register), provides that when a transaction involves the transfer of tangible personal property along with the performance of a service, the true objective of the purchaser shall determine whether the transaction is a sale of tangible personal property or the performance of a service with the transfer of the property being merely incidental to the performance of the service. If the objective of the purchaser is to obtain the personal property, a taxable sale of that property is involved. However, if the objective of the purchaser is to obtain the service, a sale of the service is involved even though, as an incidence to the service, some tangible personal property may be transferred.

“Incidental” is defined in sec. 77.51(5), Wis. Stats. (1997-98), as depending upon or appertaining to something else as primary; something necessary, appertaining to, or depending upon another which is termed the principal; something incidental to the main purpose of the service. Tangible personal property transferred by a service provider is incidental to the service if the purchaser’s main purpose or objective is to obtain the service rather than the property, even though the property may be necessary or essential to providing the service.

The true objective of each participating Enterprise is to have the analysis of its testing results and accreditation by the taxpayer. Although the Materials are necessary for the Enterprise to perform the test, it is furnished incidentally with the taxpayer’s service.

Section 77.52(2)(a), Wis. Stats. (1997-98), provides that the sale of certain enumerated services are subject to tax. The Testing service furnished by the taxpayer is not one of those enumerated services subject to tax.

2. Section Tax 11.67(2)(a), Wis. Adm. Code (November 1993 Register), provides that a person who performs a nontaxable service is the consumer of the tangible personal property which it uses incidentally in rendering its services.
 - a. Out-of-State Manufacturer With No Business Location in Wisconsin (i.e., manufacturer has no nexus or manufacturer has nexus and properly holds or is required to hold a use tax registration certificate issued by the Department of Revenue)

Section 77.53(1), Wis. Stats. (1997-98), imposes a Wisconsin use tax on the storage, use, or other consumption of tangible personal property in Wisconsin.

In a decision dated July 27, 1982, the Wisconsin Court of Appeals, District IV, held in the case of *Wisconsin Department of Revenue vs. J.C. Penney, Inc.*, that a retailer’s catalogs published by a printer located outside Wisconsin that did not have nexus in Wisconsin, and shipped directly to the retailer’s customers in Wisconsin by mail or common carrier, were not subject to Wisconsin use tax. The Court concluded that J.C. Penney, Inc., had not “used” the catalogs in Wisconsin as defined in sec. 77.51(15), Wis. Stats. (1975-76). Because the catalogs moved by mail or common carrier from Minnesota to Wisconsin, they remained the property of the printer until they were delivered. Therefore, J.C. Penney, Inc., did not exercise any right or power over the tangible personal property in Wisconsin and was not subject to use tax on its purchase of the catalogs from the printer.

The department proposed sec. 77.51(15)(b), Wis. Stats., created by 1983 Wisconsin Act 27 (later renumbered sec. 77.51(22)(b) by 1983 Wisconsin Act 189), in an attempt to reverse the *J.C. Penney* decision and provide that for purposes of defining use, “‘enjoyment’ includes a purchaser’s right to direct the disposition of property, whether or not the purchaser has possession of the property. ‘Enjoyment’ also includes, but is not limited to, having shipped into this state by an out-of-state supplier printed material which is designed to promote the sale of property or services, or which is otherwise related to the business activities, of the purchaser of the printed material or printing service.”

However, in a decision dated May 21, 1985, the Circuit Court for Dane County in the case of *J.C. Penney, Inc., et al. vs. Wisconsin Department of Revenue*, held that the 1983 creation of sec. 77.51(15)(b), Wis. Stats., did not reverse previous court actions prohibiting the imposition of use tax on J.C. Penney, Inc., for catalogs it had printed by an out-of-state printer and sent to Wisconsin customers by mail or common carrier. The court held that because J.C. Penney did not exercise any right or power over the catalogs in Wisconsin, use tax could not be imposed. The department did not appeal this decision.

As a result of the *J. C. Penney* decisions, the taxpayer is not subject to Wisconsin use tax on Materials purchased from an out-of-state manufacturer with no nexus in Wisconsin who delivers the Materials by common carrier or the U.S. Mail to an Enterprise in Wisconsin. However, the *J. C. Penney* decision does not apply when the Materials are received by a repackager on behalf of the taxpayer. The taxpayer has ownership of the Materials when they are transported into Wisconsin to the Enterprise and has consumed them by transferring them incidentally with the nontaxable service provided.

Note: Under sec. 77.53(3), Wis. Stats. (1997-98), a retailer with no business location in Wisconsin that is engaged in business in Wisconsin (i.e., has nexus in Wisconsin) and makes sales of tangible personal property for delivery into Wisconsin is subject to Wisconsin use tax on such sales. “Retailer” is defined in sec. 77.51(13)(e), Wis. Stats. (1997-98), to include a person selling tangible personal property to a service provider who transfers the property in conjunction with the selling, performing or furnishing of any service, except certain taxable services, and the property is incidental to the service. Therefore, an out-of-state manufacturer with no business

location in Wisconsin that is engaged in business in Wisconsin (has nexus), is responsible for charging Wisconsin use tax on the Materials it sells to the taxpayer and delivers to participating Enterprises in Wisconsin.

- b. Manufacturer With Business Location in Wisconsin (i.e., manufacturer properly holds or is required to hold a Wisconsin seller’s permit)

Section 77.52(1), Wis. Stats. (1997-98), imposes a Wisconsin sales tax on tangible personal property sold at retail in Wisconsin.

If the manufacturer delivers the Materials to an Enterprise in Wisconsin, the sale of the materials to the taxpayer is subject to Wisconsin sales tax. If the manufacturer does not charge tax to the taxpayer, the taxpayer is liable for the sales tax under sec. 77.52(3) or 77.57, Wis. Stats. The *J.C. Penney* decision does not apply to the imposition of sales tax.

3. Section 77.53(16), Wis. Stats. (1997-98), provides that if the purchase, rental, or lease of tangible personal property or service subject to Wisconsin **state use tax** was subject to a sales tax by another state in which the purchase was made, the amount of sales tax paid the other state shall be applied as a credit against and deducted from the Wisconsin state use tax. “Sales tax” includes a use or excise tax imposed on the use of tangible personal property or taxable service by the state in which the sale occurred.

Section 77.71(2), Wis. Stats. (1997-98), provides, in part, that if a buyer has paid a similar local tax in another state on a purchase of the same property or services, the tax shall be credited against the Wisconsin **county and stadium use tax**.

There is no provision in the sales and use tax law that would provide a credit against Wisconsin **sales tax** for sales or use tax paid to another state.