

**New York State Department of Taxation and Finance
Office of Counsel
Advisory Opinion Unit**

TSB-A-10(53)S
Sales Tax
October 18, 2010

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S100908A

On September 8, 2010, the Department of Taxation and Finance received a Petition for Advisory Opinion from [REDACTED]. Petitioner asks whether the Customer described in the following hypothetical motor vehicle leasing situations is entitled to a capitalized cost reduction, and if so in what amount, for the value of the Customer's "trade-in" in computing the portion of a new vehicle lease that is subject to New York State sales tax for collection by the Dealer.

We conclude that the Dealer may allow a credit for the value of the Customer's trade-in vehicle against the capitalized cost of the vehicle to be leased, as described below. To the extent that reducing the capitalized cost reduces the total of the payments due under the lease, the amount subject to sales tax is reduced.

Facts

Petitioner presented the following facts and statements in the Petition for this advisory opinion.

Situation 1: A motor vehicle dealer in New York State (the "Dealer") acting as agent for a leasing company (the "Lease Company") that is an affiliate of the vehicle's manufacturer, leases a new motor vehicle to a Customer for a lease term in excess of 12 months. The new vehicle to be leased is titled in the name of and in the possession of the Dealer. As part of the transaction, the Customer trades in a used vehicle with a fair market value of \$12,000 subject to a lien, based on a bank loan with a remaining balance of \$10,000. Title to and possession of the "trade-in" is transferred from the Customer to the Dealer. The Dealer then pays off the loan and receives a release of the lien from the Bank. The Customer receives a reduction in the net cash/lease payments required to close the deal of \$2,000. The Lease Company takes title to the new lease vehicle and the future lease payments are made by the Customer to the Lease Company. The Dealer intends to resell the Customer's "trade-in" vehicle.

Situation 2: A motor vehicle dealer in New York State (the "Dealer") acting as agent for a leasing company (the "Lease Company") that is an affiliate of the vehicle's manufacturer, leases a new motor vehicle to a Customer for a lease term in excess of 12 months. The new vehicle to be leased is titled in the name of and in the possession of the Dealer. As part of the transaction, the Customer trades in a used vehicle with a fair market value of \$12,000. The used vehicle was leased from the same Leasing Company as the new vehicle. The used lease vehicle has a residual buyout option of \$10,000. The buyout option is transferred from the Customer to the Dealer. The Dealer then exercises the buyout option paying the Leasing Company the \$10,000, and possession of the used car is transferred from the Customer to the Dealer and title to the used vehicle is transferred from the Lease Company to the Dealer. The Customer receives a reduction in the net cash/lease payments required to close the deal of \$2,000. The Lease Company takes title to the new lease vehicle and the future lease payments are made by the Customer to the Lease Company. The Dealer intends to resell the Customer's "trade-in" vehicle.

Petitioner's representative subsequently provided the following additional information regarding both Situations 1 and 2: "Reduction in net cash required to close the deal" means the Dealer may reduce any one or more of the following amounts due when the lessee signs the lease to the extent of the value of the credit that the Dealer allows for the net value of the Customer's trade-in vehicle: down payment, sales tax due, vehicle registration fees, and the like. "Reduction in lease payments required to close the deal" means the Dealer would recalculate the monthly lease payments due over the term of the lease to reflect the value of the Customer's vehicle taken in trade that is applied against those lease payments. We understand "capitalized cost" to mean the total lease price of the vehicle, as determined by the lessor.

Analysis

The State's sales tax is imposed on the vendor's receipts from the retail sale of tangible personal property. "Sale" means a transfer of title or possession or both, or a rental or lease, in any manner or by any means whatsoever for a consideration, or any agreement therefor. "Receipt," as relevant here, means the sale price of the property, without any deduction for expenses of the vendor, including any charge by the vendor to the purchaser for delivery of the goods, but excluding any credit for tangible personal property accepted in part payment and intended for resale. This exclusion is often referred to as the "trade-in credit." The measure of the relevant State compensating use tax imposed by section 1110(a)(A) of the Tax Law is likewise the consideration given or contracted to be given for the property, less any credit for tangible personal property accepted in part payment and intended for resale (the trade-in credit). Notwithstanding any contrary provision of law, in the case of a lease of a motor vehicle with a gross vehicle weight of 10,000 pounds or less for a term of a year or more, all receipts due or consideration given or contracted to be given for the leased vehicle for the entire period of the lease (including any option to renew or similar provision, or combination of them) is subject to sales or use tax, as the case may be. Such tax due must be collected as of the date of first payment under the lease (or option to renew or similar provision), or as of the date of registration of such property with the Commissioner of Motor Vehicles, whichever is earlier. (Tax Law sections 1105(a), 1101(b)(3) and (5), 1110 and 1111(i).) All of these provisions apply with like force to county and city ("local") sales and use taxes (Tax Law section 1210(a)).

Trade-ins are treated differently in a lease situation than in an outright purchase situation. In the case of an outright purchase, the dealer will first determine the cost of the vehicle being purchased and add any taxable fees. The dealer will then reduce that total by the amount it is willing to allow as a trade-in allowance for the property the customer will trade in, and compute the sales tax due on the balance. However, when a customer trades in a vehicle as partial payment for the lease of a new vehicle, the dealer will determine the value of the vehicle being traded in, reduce the total lease price of the vehicle (capitalized cost) by the value of the property the lessee will trade in, and then re-compute the monthly lease payments based on the reduced capitalized cost. Alternatively, the dealer may choose to reduce the down payment or other charges due from the lessee in order to account for the value of the trade in. The sales tax is then computed by multiplying the total of the reduced amounts, plus any down payment, by the applicable tax rate.

For purposes of our general analysis in the following four paragraphs, we will assume the following facts: A consumer owns a motor vehicle and seeks to trade it in on a new vehicle that the consumer will lease for a term of more than one year. The vehicle to be traded in may or may not be subject to a lien for an outstanding loan balance. The fair market value of the vehicle to be traded in is \$15,000. The retail price of the new vehicle to be leased is \$40,000 if it were to be purchased outright. The capitalized cost of the leased vehicle, not adjusted for any trade-in, is \$43,000. For purposes of the following four paragraphs, we will also assume the lease has no down payment or option to renew or

similar provision. We will use these facts to demonstrate how these provisions of law apply generally to leased vehicles and the trade-in credit. We will then apply these provisions of law to Petitioner's two situations

Using these facts and assumptions, if a consumer purchases a new car outright for \$40,000, with no trade-in, sales tax would be due on the entire \$40,000. If the consumer trades in his or her car on the \$40,000 car, and the car dealer reduces the purchase price of the new car by the full \$15,000 value of the trade-in (that is, the dealer allows a credit against the receipts from the sale of the new car for the old car taken in trade to be resold), the taxable receipts are reduced by the amount of that credit to \$25,000, and the dealer should collect sales tax on that reduced amount. If the purchaser still has a loan outstanding of \$6,000 on the trade-in vehicle, and the purchaser will pay off that loan, either out-of-pocket or by borrowing extra money when he or she takes out a new loan to pay off the balance due on the new car, the amount of the trade-in credit would not be affected. On the other hand, if the dealer accepts the trade-in vehicle subject to the loan, the dealer would allow a credit of only \$9,000 against the new car purchase price, since the purchaser has "equity" of only that amount. Thus, the amount of the new car's purchase subject to tax would be \$31,000. Even if this last case is not a usual or likely occurrence, we point it out to clarify the result if there is outstanding debt that the dealer assumes.

We turn now to the computation of the taxable receipt in the case where a consumer trades in his or her vehicle at the time of leasing a new car under a lease of a year or more subject to section 1111(i) of the Tax Law, with no down payment or option to renew. The amount subject to tax with respect to such a lease is the amount of the monthly lease payment times the number of months of the lease term, plus any down payment paid at the lease inception. The calculation of the monthly payment, as well as any down payment, is a business decision to be made by the lessor, based on the value of the leased property, the length of the lease term, the residual value of the property at the end of the term, the value of any property taken in trade and intended for resale, the time value of money, the creditworthiness of the lessee, profit, and whatever other factors the lessor considers relevant. Once the lessor establishes the monthly payment amount, and any down payment amount, it is generally a simple matter to determine the amount subject to tax under section 1111(i). If a consumer wants to lease a vehicle that would sell for \$40,000 in an outright sale, and the lessor determines that the capitalized cost of that vehicle is \$43,000, the lessor will set the amount of the monthly lease payment based on its best business judgment. One lessor might be willing to lease the vehicle for \$400 per month for a term of 48 months based on its analysis of factors important to it. Another lessor might be willing to lease the same vehicle for \$425 for the same period based on its analysis of similar or different factors. The Tax Law looks at each of those leases and says sales tax is due on the product of the monthly payment times the number of months of the lease term. If the lessee in each of these cases is not trading in a car on the new leased vehicle, the lessor would not adjust the capitalized cost of the vehicle to determine the amount of the monthly lease payments on account of any credit against the total receipts subject to tax, since the lessor has not received any property of value in part payment of the vehicle to be leased.

However, if the consumer tells the lessor that he or she wants to trade in his or her car against the lease of the new vehicle, the lessor would consider the value of the trade-in and make a business decision as to how much the trade-in is worth and then another business decision as to how much to adjust the monthly payment due under the lease on account of the value of the vehicle being traded in. We understand from dealing with members of the automobile leasing industry that lessors refer to this calculation as affecting the capitalized cost of the new leased vehicle. That is, the vendor/lessor would determine how much credit to allow the lessee against the amount to be paid (the capitalized cost on which the monthly payment is based) for the purchase (i. e., the lease) of the new vehicle. Again, the Tax Law would look at the new, reduced total amount of the lease payments, times the number of months of

the lease term, as the proper amount subject to tax under section 1111(i). That reduction in the amount of the monthly payment on account of the trade-in, multiplied by the number of months of the lease term, constitutes the trade-in credit that reduces the receipts subject to tax, as defined in section 1101(b)(3). In the case where such a trade-in occurs as part of such a lease of a motor vehicle, the purchaser (lessee) is thus afforded the credit described in section 1101(b)(3) that a vendor may allow against the taxable receipt from the sale (lease) of the car.

Representatives of lessors have asserted in the past that the value of the trade-in car established by the lessor, or, alternatively, the portion of the value that exceeds the lessee's equity in the trade-in vehicle, should then be allowed as a further credit against the total of the lease payments subject to tax. In other words, multiply the amount of the monthly payment by the number of months to arrive at the total of the lease payments due under the lease, and then subtract the value of the trade-in, net of any debt on the vehicle that the lessor assumes, from that product. To do so would mean the vendor is allowing the trade-in credit twice - once when reducing the capitalized cost on which the monthly payments are calculated and again after determining the product of the monthly lease payment times the number of months in the lease term. That is not allowable. First, notwithstanding any other provision of law, section 1111(i) expressly sets forth the calculus of the receipts subject to tax for a long-term lease of a motor vehicle. Second, the lessor has already allowed a credit for the trade-in vehicle when it reduced the amount of the monthly payments, which are the receipts subject to tax, on account of the value of the trade-in. Thus, the lessor should calculate tax due with respect to a long-term lease of a vehicle on the sum of the lease payments, with no further reduction for any trade-in credit. The trade-in credit must be applied, if at all, as a reduction of the capitalized cost. If a customer has no equity in the trade-in property and, as a result, the lessor does not allow a trade-in credit against the capitalized cost of the vehicle to be leased, the lessor should not then allow a trade-in credit for that very property after the amount and number of the monthly lease payments have been established. The credit must be allowed, if at all, as a reduction in the capitalized cost or "base" from which the amount of the monthly payments is determined.

Based on the foregoing law and analysis, we now turn to Petitioner's situations 1 and 2. We assume for purposes of this analysis that the leased vehicles in situations 1 and 2 have a gross vehicle weight of 10,000 pounds or less. Since the leases in both situations are for a term in excess of one year, the provisions of section 1111(i) apply.

Situation 1 – The first thing to remember is that the sales tax trade-in credit works only to the extent that the vendor allows a reduction in the "sale price" of the property being sold. In a section 1111(i) motor vehicle lease situation, the sale price is the capitalized cost of the vehicle, not the total of the lease payments the lessee is required to pay. If the lease also requires the lessee to pay a down payment in addition to the lease payments, the down payment is also part of the sale price. Thus, the trade-in credit can be applied against the down payment to the extent not exhausted as a credit against the capitalized cost of the vehicle. In this case, the Dealer accepts the Customer's car in trade. The car is worth \$12,000. But it is subject to a lien of \$10,000, and the Dealer will pay off the loan. Thus the Dealer will allow only a \$2,000 credit to the seller. Petitioner indicates this credit will be applied against the "net cash/lease payments" required to close the deal. If the Dealer allows the \$2,000 credit entirely against the capitalized cost of the vehicle, and as a result reduces the monthly payments due from the Customer under the lease, the Dealer will thus collect less sales tax from the Customer than if the Dealer did not allow that credit. Since the Dealer applied the entire credit against the capitalized cost, the Dealer cannot apply it against anything else. On the other hand, if the Dealer applies the \$2,000 against other amounts the Customer owes to close the lease, then the monthly lease payments will not be reduced and the Customer will pay sales tax on those full lease payments. Thus, the Customer will not benefit from reduced monthly payments and reduced sales tax on those payments. If, in addition to the monthly lease

payments, the lease requires the Customer to pay a down payment of \$2,000 or more at the lease closing, and the Dealer instead applies the \$2,000 credit against the down payment, then the Dealer can allow the Customer the trade-in credit, and collect sales tax on the reduced down payment (plus the sales tax due on the total of the monthly lease payments). But if there is no down payment, and the Dealer does not allow the credit against the capitalized cost, then the Dealer must collect tax on the total of the monthly lease payments. The \$2,000 amount cannot be taken again as a credit against the total amount of lease payments after the monthly lease payment amount has already been reduced. To do so would result in the trade-in allowance being given effect twice, once when the dealer uses the allowance to reduce the capitalized cost of the vehicle and the monthly lease payments due based on the reduced capitalized cost, and again when the dealer credits the trade-in allowance against the total of the reduced monthly lease payments for purposes of determining the taxable amount due to the dealer for the leased vehicle. This is not allowable.

Situation 2 – In this situation, the facts are the same, except that the Customer “trades in” a leased vehicle with a fair market value of \$12,000, with a residual buyout option of \$10,000. The Customer transfers the option to the Dealer and the Dealer exercises it. Thus, the Dealer pays \$10,000 to purchase a vehicle worth \$12,000. As in Situation 1, the Dealer allows the Customer a \$2,000 credit against the net cash/lease payments required to close the deal. The analysis that applied to Situation 1 thus also applies to this situation.

For additional explanation concerning sales and use taxes on motor vehicle leases, see the Department’s PUB-839, *A Dealer’s Guide to Sales and Use Taxes on Long-Term Motor Vehicle Leases in New York State*. This publication assists automobile dealers in computing State and local sales and use taxes on long-term motor vehicle leases.

DATED: October 18, 2010

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Deputy Commissioner and Counsel

NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion.