**Final Written Determination**

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| **Docket Number:** | **WFD-P-2001-3** |

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| **Tax Type:** | **Kansas Compensating Tax; Kansas Retailers' Sales Tax** |
| **Brief Description:** | **Machinery and equipment including repair and replacement parts and accessories.** |
| **Keywords:** |  |
| **Approval Date:** | **05/25/2001** |

**Body:**

**Office of Administrative Appeals**

May 25, 2001

**Written Final Determination, Docket No. 00-488**

On August 28, 2000, the Taxpayer timely filed a written request for an informal conference with the Kansas Secretary of Revenue (Secretary). This was in response to a Notice of Final Denial of Retailers’ Sales and Consumers’ Compensating Use Tax dated August 1, 2000 from the Kansas Department of Revenue (Department). The Taxpayer had requested a refund for sales tax paid to various vendors and use tax accrued on a variety of machinery and equipment including repair and replacement parts and accessories.

Issue

The Taxpayer contends that its computers and peripheral equipment are utilized either in engineering a finished product or in controlling or measuring the process of manufacturing a product and are exempt as manufacturing machinery and equipment from sales and use tax pursuant to K.S.A. 79-3606(kk).

Discussion

K.S.A. 79-3606(kk), as it existed during the refund period in question (March 1994 through March 2000), provides that “on and after January 1, 1989, all sales of machinery and equipment used directly and primarily for the purposes of manufacturing, assembling, processing, finishing, storing, warehousing or distributing **articles of tangible personal property** in this state **intended for resale** by a manufacturing or processing plant or facility” shall be exempt from the sales tax. (emphasis added) The Taxpayer argues that the equipment it uses in the provision of telecommunications services, both billed and pre-paid services, should be exempt under the manufacturing machinery and equipment exemption contained in 79-3606(kk).  
  
While the Kansas retailers' sales tax act does not specifically define what a telecommunications company is, K.S.A. 79-3271(i) defines a 'Telecommunications company' as “any business entity or unitary group of entities whose primary business activity is the **transmission of communications** in the form of voice, data, signals or facsimile communications by wire or fiber optic cable.” (emphasis added) It is not contested that the Taxpayer is a telecommunications company.  
  
K.S.A. 79-3606(kk) requires a taxpayer to process tangible personal property for resale in order to qualify for the manufacturing machinery and equipment sales tax exemption. The Taxpayer argues that it sells tangible personal property and not a service.  
  
The Taxpayer's primary argument is that it sells telecommunications signals as tangible personal property that is processed, controlled or manufactured within the meaning of KSA 79-3606(kk). The Taxpayer further argues that prepaid telecommunications services as represented by a prepaid calling card (defined by K.S.A. 79-3602(f)(2) as tangible personal property) should also qualify the manufacturing machinery and equipment used to deliver this service as exempt pursuant to KSA 79-3606(kk).  
  
It is clear from the evidence, including the Taxpayer's own statements, that the Taxpayer is not selling tangible personal property. It is uncontroverted that the Taxpayer’s provision of telecommunications is subject to the Kansas retailers’ sales tax under KSA 79-3603(b). This statute imposes the tax on “(1) The gross receipts received from intrastate telephone or telegraph **services**, and (2) the gross receipts received from the sale of interstate telephone or telegraph **services**, . . .” (emphasis added)  
  
The Taxpayer may use tangible personal property in the form of electricity, electrical currents or some type of electrical impulse; however, it is not selling the electricity. To avail itself of the manufacturing machinery and equipment exemption, the Taxpayer would have to sell "tangible personal property,” not services. Since the Taxpayer sells services, it does not qualify for this exemption.  
  
In addition, the Taxpayer's argument that it's "taxable telephone services are tangible personal property when provided on a prepaid basis" fails for at least two reasons. First, even though the physical evidence of prepaid "telephone services" (i.e. the plastic or paper card) is defined by statute as tangible personal property, it is similar to the taxation of service or maintenance contracts defined in KSA 79-3603(r). The fiction that the services paid for by the purchase of prepaid calling cards or service contracts become tangible personal property is a result of the legislative intent that the "promise" to provide services in the future be taxable at the time the promise is made. It does not change the character of what the consumer purchased. A prepaid calling card does no more than evidence the purchase of a service that may or may not be delivered in the future. Second, while the actual manufacturing or processing of the plastic or paper card itself may qualify under the terms of KSA 79-3606(kk), the Taxpayer failed to meet its burden to qualify for this exemption.

Conclusion

Upon reconsideration of all of the facts and issues underlying the Department’s denial of the Taxpayer’s request for a refund of retailers’ sales and consumers’ use tax, and upon review of the additional information provided by the Taxpayer, it is the final determination of the Secretary’s Designee that the Department’s denial be sustained.  
  
  
Sincerely,  
  
  
  
David J. Heinemann  
Secretary’s Designee  
  
  
**Date Composed: 07/12/2001 Date Modified: 10/09/2001**