**Private Letter Ruling**

|  |  |
| --- | --- |
| **Ruling Number:** | **P-1999-76** |

|  |  |
| --- | --- |
| **Tax Type:** | **Kansas Retailers' Sales Tax** |
| **Brief Description:** | **Drum reconditioning; lubricating oils.** |
| **Keywords:** |  |
| **Approval Date:** | **03/11/1999** |

**Body:**

Office of Policy & Research  
  
  
March 11, 1999

XXXXXXXXXX  
XXXXXXXXXX  
XXXXXXXXXX  
XXXXXXXXXX  
XXXXXXXXXX  
XXXXXXXXXX  
  
Re: Kansas Sales Tax  
  
Dear XXXXX,  
  
Your correspondence of February 18, 1999, has been referred to my attention. Its contents are duly noted. Your letter states, in pertinent part, as follows:

We are writing to request a Private Letter Ruling on the payment of State Sales Tax on drum reconditioning. Our drums are reconditioned at XXXXXXXXXXXX located at XXXXXXXXXX in XXXXXX, Kansas XXXXXXX, telephone number XXXXXXXX. XXXXXXX is a wholesale/retail distributor of lubricating oils, which on average uses XXXXXXXXXX weekly.  
  
Please find the enclosed copies, which show the way we figure the cost of our oil, labels, seals, and freight into the products we sell. Our sales are primarily made to wholesale distributors, for which we have sales tax exemptions on file.  
  
We do not charge state sales tax on drums delivered to wholesale distributors, or to other state tax exempt businesses. Yet, we pay Kansas sales tax, even though we are not the final consumer and considering that the reconditioning of the drum is an ingredient or component part that becomes a part of the finished product -- in this case, the finished part being a drum of oil.  
  
We sell the drums for $20.00 per drum. This charge is a separate charge -- on that is not incorporated into the cost of the product. We will, at our discretion and inspection, buy back empty drums for $20.00. These drums are sold to the customer, because we do not know when or if we will ever receive those drums back.  
  
We would appreciate a ruling as soon as possible. Through our understanding, with respect to the enclosed copy of page 6 of the Kansas Exemption Certificates booklet, we should be exempt from state sales tax.

That portion of page 6 of the Kansas Exemption Certificates booklet to which you refer provides as follows:

**Uses That Are Exempt**  
  
Other items are exempt from sales tax because of how they are used. These are articles that are **ingredient or component parts** or are **consumed in the production** of property or services later sold to the final consumer. These two exemptions are applicable to many types of businesses.  
  
**Ingredient Or Component Parts**  
  
Ingredient or component parts are items that become a part of a larger whole or finished product which will be sold to the final consumer. To be considered an ingredient or component part, the item must be:

· necessary and essential to the finished product  
· be used in or on the finished product  
· become a physical part of the finished product, and  
· become an ingredient or compound part of property or service for retail sale.

For example, fabric, thread, buttons and zippers are component parts of an item of clothing (finished product) which will be sold at retail.  
  
Other items considered to be ingredient or component parts are not as obvious. Containers, labels and shipping cases, twine and wrapping paper may be ingredient parts. When these items are used to distribute property for sale, and are not reusable or returned to the producer or manufacturer, they qualify as ingredient parts.

The provisions on page 6 to which you refer are based on Kansas Statute Annotated (K.S.A.) 79-3602(l). The statute provides:

(l) “Ingredient or component part” means tangible personal property which is necessary or essential to, and which in actually used in and becomes an integral and material part of tangible personal property or services produced, manufactured or compounded for sale by the producer, manufacturer or compounder in its regular course of business. The following item of tangible personal property are hereby declared to be ingredients or component parts, but the listing of such property shall not be deemed to be exclusive nor shall such listing be construed to be a restriction upon, or an indication of, the type or types of property to be included within the definition of “ingredient or component part” as herein set forth:  
(1) Containers, labels and shipping cases used in the distribution of property produced, manufactured or compounded for sale which are not to be returned to the producer, manufacturer or compounder for reuse.  
(2) Containers, labels, shipping cases, paper bags, drinking straws, paper plates, paper cups, twine and wrapping paper used in the distribution and sale of property taxable under the provisions of this act by wholesalers and retailers and which is not to be returned to such wholesaler or retailer for reuse.  
(3) Seeds and seedlings for the production of plants and plant products produced for resale.  
(4) Paper and ink used in the publication of newspapers.  
(5) Fertilizer used in the production of plants and plant products produced for resale.  
(6) Feed for animals, fowl and aquatic plants and animals, the primary purpose of which is use in agriculture or aquaculture, as defined in K.S.A. 47-1901, and amendments thereto, the production of food for human consumption, the production of animal, dairy, poultry or aquatic plant and animals products, fiber, fur, or the production of offspring for use for any such purpose or purposes.  
(Emphasis added.)

The statute is interpreted by Kansas Administrative Regulation (K.A.R. 92-19-54). The regulation provides, in subsections (d), (e) and (f):

(d) Each container, wrapper or other shipping or handling material actually accompanying the product sold is not subject to sales tax.  
(e) Each retailer purchasing a container or other shipping or handling material for consumption which is not for resale as described in paragraph (d) is subject to sales tax. Each purchase by a retailer of a container or other shipping or handling material in which title remains with the retailer when the tangible personal property contained therein is sold by the retailer, or where the container or other shipping or handling materials are to be returned to the retailer by the consumer of the tangible personal property, is subject to sales tax.  
(f) Each purchase of a container, wrapper or other shipping or handling material by a retailer using the container, wrapper or other handling material to provide nontaxable services is deemed to be consumed by the service provider and is subject to tax.  
(Emphasis added)

The issue you present is nearly identical to that considered by the Board of Tax Appeals (BOTA) in *In The Matter Of The Appeal Of Hampel Oil Distributors, Inc.* In that case, a copy of which is enclosed for your review, the BOTA stated, in Paragraph 21, Page 7:

The Board finds that the facts in *Consumer Co-operative* are so similar to the facts in this matter as to be virtually undistinguishable (sic). The Board concludes that the drums do not meet the exemption of K.S.A. 1996 Supp. 79-3602(l)(2) as the drums are returnable containers. The Board concludes that the purchase of the drums by Hampel from the manufacturer of the drums is a taxable event under the retailer’s sales act. The Board affirms the decision on the designee on this issue. (Emphasis added.)

Based on the statute, the regulation, and their interpretation by the BOTA on nearly identical facts, we must conclude it is proper for you to pay sales tax when you purchase the drums. In addition, it is proper for you to pay sales tax on charges for reconditioning the drums. However, because the purchase of new drums or payment for the reconditioning of drums is a taxable event under the retailer’s sales tax act, you should not charge your customer’s sales tax on the “sale” of these drums.  
  
I trust this information is of assistance. If I can be of further service, please feel free to contact me.  
  
Sincerely,  
  
  
  
Jim Weisgerber  
Attorney  
Tax Specialist  
  
JW:jw  
  
Enclosure: *In The Matter Of The Appeal Of Hampel Oil Distributors, Inc.*  
  
  
**Date Composed: 03/29/1999 Date Modified: 10/11/2001**