

**M e m o r a n d u m**

570.0405

**To** : Mr. Walt Shaffer**Date** : September 29, 1978**From** : Legal**Subject** :

This is in response to your memorandum of July 14, 1978 concerning the above-referenced taxpayer. Your inquiry concerns the correct application of tax to certain computers withdrawn from taxpayer's inventory for short periods of time and utilized for testing in the manufacturing process.

Taxpayer has put certain of its Work-In-Process (WIP) computer units into production line testing. The reasons given for the WIP loaners are: (1) that they are used to test production line items such as plug-in-boards, trunk lines, etc.; and (2) that they are being tested for long term reliability confidence. WIP computer units are used for 90 days, refurbished, and returned to the WIP inventory for final assembly and packaging for market. The amount of refurbishing necessary to restore marketability of a unit is usually negligible and usually involves correcting cosmetic wear and tear.

The units are complete computers except for the final stage of construction. The final stage of construction consists of the addition to the units of "skins" or covers, otherwise the units are fully operational.

The computers contain approximately 48 plug-in-boards, easily accessible from the back panels. Batches of plug-in-boards are sent to the testing area where 20 to 21 computers will be used to test them. Those not passing satisfactory function tests are returned to another area for eyeball searching for visual defects. The sound plug-in-boards are inserted into new computers. Four plug-in-boards are tested at a time by removing their opposite number from the test computer and inserting them in their place.

We are of the opinion that when computers such as the ones described in your letter are taken off the production line and utilized for testing other components, such as plug-in-boards, a taxable intervening use has taken place. The fact that \_\_\_\_\_ sometimes tests, improves, and refines the computers as a result of their being in the testing area does not change our analysis that a taxable use of the machinery is made prior to its being covered and sold.

We are enclosing for your reference a copy of a letter written September 21, 1977 concerning the correct application of tax to computers utilized in a similar manner. If after

reviewing this letter you have further questions concerning this matter, I will be happy to discuss this matter with you further.

MCA:ba

Attachment

cc: Mr. D. F. Brady w/attachment