00-1158
TAX TYPE: SALES TAX
TAX YEAR: 7/95 – 6/98
DATE SIGNED: 10-11-2002
COMMISSIONERS: P. HENDRICKSON, B. JOHNSON, P. DEPAULIS
DISSENT: M. JOHNSON

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER	)	**ORDER**
	)	
Petitioner,	)	Appeal No. 00-1158
	)	
v.	)	
	)	Tax Type:
AUDITING DIVISION OF	)	Tax Periods: 07/01/95 – 06/30/98
THE UTAH STATE TAX	)	
COMMISSION,	)	
	)	
Respondent.	)	Judge: Davis

Presiding:

G. Blaine Davis, Administrative Law Judge
Pam Hendrickson, Commission Chair
R. Bruce Johnson, Commissioner
Palmer DePaulis, Commissioner
Marc B. Johnson, Commissioner

Appearances:

For Petitioner: REPRESENTATIVE-1 FOR PETITIONER, from the law firm of LAW FIRM
REPRESENTATIVE-2 FOR PETITIONER, from the law firm of LAW FIRM
REPRESENTATIVE-3 FOR PETITIONER
REPRESENTATIVE-4 FOR PETITIONER
REPRESENTATIVE-5 FOR PETITIONER

For Respondent: REPRESENTATIVE FOR RESPONDENT, Assistant Attorney General
RESPONDENT-1, from the Auditing Division
RESPONDENT-2, from the Auditing Division
RESPONDENT-3, Division Director, Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for an Initial Hearing pursuant to the provisions of Utah Code Ann. ∋59-1-502.5, on April 4, 2002.

Petitioner is a corporation which designs, manufactures and sells semiconductor memory products as tangible personal property. Its primary manufacturing facility is located in CITY-1, STATE-1, which was built inYEAR.

In 1995, Petitioner began construction of a manufacturing facility in CITY-2, which was approximately #####-square feet. The facility was designed as a series of separate buildings connected by a spine or corridor. Each building is dedicated to a certain function, and there are separate buildings for each phase of the manufacturing process, including fabrication, assembly, test, as well as separate buildings for non-manufacturing functions such as engineering and administration.

Because of changes which occurred in the computer and semiconductor markets, the CITY-2 facility has never become fully operational as a manufacturing facility. There are administrative and testing activities which occur at the facility. However, the physical conversion of raw materials into semiconductor products does not occur at the CITY-2 facility. Therefore, the clean rooms, clean room components, and electrical components do not come into contact with the raw materials that become the finished semiconductor products. Accordingly, the clean room and

electrical components in the CITY-2 facility do not directly control or operate any of the machinery that directly converts the raw materials into finished products.

At the hearing and in the brief filed by Petitioner, detailed explanations were given of the clean room manufacturing process. However, those activities did not occur at the CITY-2 facility. That facility was designed and constructed for such manufacturing activities, but only limited activities occurred at the CITY-2 plant during the audit period.

CITY-1 Manufacturing Facility and Process

The primary manufacturing of the products occurs at the plant of Petitioner in CITY-1, STATE-1. Even though the CITY-2 facility has never gone into full production, it was designed to perform in a manner similar to the CITY-1 plant. Therefore, an examination of the process of the CITY-1 plant is helpful in understanding the construction of the CITY-2 plant and the general semiconductor manufacturing process.

PETITIONER semiconductor memory products can only be manufactured in a clean room, which is to guarantee the quality and integrity of the products by minimizing contamination and vibrations that may damage the product. The clean room is a removable room within the exterior of the building. The floors, walls and ceilings of the clean room are specifically designed to create the elements required for the manufacture of semiconductors.

The manufacturing process starts in the clean room with an eight-inch silicon wafer, which may yield up to 500 individual parts. Patterns are etched or applied to the wafer, resulting in the electronic transistors that make the semiconductor function. Such patterns are applied to the

wafer in layers, and there may be as many as thirteen different layers in a part. The size of the parts, and correspondingly the size of the patterns, is continually shrinking. As the width shrinks, the tolerances for the elements required to manufacture such products become smaller.

The elements required to manufacture semiconductor products in the clean room include a particle-free air supply; controlled and consistent temperature and humidity; extremely pure gas, water and air; and clean and consistent electrical supply.

The clean room and electrical equipment establish and maintain these required elements. The electrical equipment is installed above and below the clean room to preserve the sterile environment and to reduce vibrations.

If any of the required elements are not maintained within the required tolerances or ranges, the products may be damaged or destroyed. As the products become smaller and more complex, the need for precision is greater and the tolerances must become less. At the current technology level, a dust particle wider than $1/100^{th}$ of the width of a human hair can contaminate and destroy PETITIONER product – and dust particles are only one of the potential contaminants.

The air in the clean room must be particle-free, properly conditioned and the air pressure must be balanced. To do this, the clean room equipment must create an "air wash", which is the constant exchange of the air in the clean room. Equipment performs the air wash by circulating or exchanging the entire volume of the air in the clean room once every eight to ten seconds. Clean rooms can contain up to 500,000 cubic feet, so the equipment must be sufficiently large to handle such volumes of air.

In addition to particle contamination, the manufacturing process is also susceptible to electrical contamination which may come as electrostatic discharge ("ESD") – commonly referred to as static electricity – or fluctuations in the electrical current. This potential contamination is managed by controlling the humidity, by using specialized clothing for workers, and by placing specialized coating on equipment and accessories. The semiconductor manufacturing process is so sensitive that the static electricity that is created by rubbing two pieces of cloth together can impact the quality and integrity of the products. Therefore, controlling ESD and maintaining a clean and consistent power supply is crucial to quality control.

PETITIONER also uses light waves in its manufacturing process to create semiconductor layers. In this process, extremely fine (WORDS REMOVED) waves of light are projected on the wafer creating the electronic pattern. Fluctuations in the electrical supply, improperly controlled temperature, or excessive humidity can cause deteriorations in the waves of light, which may destroy the quality and integrity of the products.

Accordingly, clean room and electrical equipment is required to minimize the potential particle, electrical and photolithographic contamination of PETITIONER products during the manufacturing process.

Audit Issues

Respondent performed a sales tax audit of Petitioner for July 1, 1995 through June 30, 1998. As a result of that audit, a statutory notice was issued on August 21, 2000, and Petitioner timely filed a Petition for Redetermination to challenge that audit. The parties have reached

agreement on some parts of the audit, but they have not been able to reach an agreement on the following items:

1. "Clean Room Equipment", which is machinery and equipment installed to heat, cool, humidify, filter, condition and balance the air required for the manufacturing process. "Clean Room Equipment" includes Make Up Air Units (MAU), Re-circulating Air Units (RFU), Chillers, Boilers, and flooring.

2. "Electrical Equipment", which is equipment used to provide clean and consistent electricity for the manufacturing process. "Electrical Equipment" includes electrical transformers, electrical switches, and batteries.

3. "Vax System".

4. There were also issues raised regarding fuses, storage tanks and generator sets. Petitioner has paid the taxes on some of these items, and it is the understanding of the Commission that the issues on the remaining portions of these items has been resolved between the parties.

Positions of the Parties

The position of Petitioner is that the clean room equipment and electrical equipment are manufacturing equipment which are exempt from sales and use tax pursuant to the provisions of Utah Code Ann. §59-12-104(14) and Rule R865-19S-85. The position of Petitioner with respect to the Vax System is that it is not subject to Utah sales or use tax because it was shipped to STATE-1.

The position of Respondent is stated in its brief is as follows:

> "The disputed items are not exempt under §59-12-104(14) because: (1) no manufacturing activities take place at Petitioner's facility in CITY-2, Utah;

(2) the disputed items are not used in a manufacturing process to manufacture an item sold as tangible personal property; and (3) the disputed items were converted by Petitioner into real property. Furthermore, Respondent submits that the Vax System at issue was actually shipped to a location in Utah and, thus, its purchase by Petitioner is taxable."

APPLICABLE LAW

The relevant portions of Utah Code Ann. §59-12-104(14) for the time periods at issue exempt from sales and use taxes:

(14)(a) the following purchases or leases by a manufacturer on or after July 1, 1995:
(i) machinery and equipment:
(A) used in the manufacturing process;
(B) having an economic life of three or more years; and
(C) used:
(I) to manufacure an item sold as tangible personal property; and
(II) in new or expanding operations in a manufacturing facility in the state; . . . .

For the times at issue, Utah Administrative Code, Rule R865-19S-85 provided in relevant part:

A. Definitions:
1. "De minimis" means that an item's use in nonqualifying activities is inconsequential in relation to the item's use for qualifying activities.
2. "Establishment" means an economic unit of operations, that is generally at a single physical location in Utah, where qualifying manufacturing processes are performed. If a business operates in more than one location (e.g., branch, or satellite offices), each physical location is considered separately from any other locations operated by the same business.
3. "Machinery and equipment" means:
a) electronic or mechanical devises incorporated into a manufacturing process from the initial stage where actual processing begins, through the completion of the finished end product, and including final processing, finishing, or packaging of articles sold as tangible personal property. This definition includes automated material handling and storage devices

when those devices are part of the integrated continuous production cycle; and

b) any peripheral device that is essential to a continuous manufacturing process. Qualifying peripheral devices include bits, jigs, molds, or devices that control the operation of machinery and equipment, but do not include gas, water, or electricity systems that constitute real property improvements as provided in B.

B. The sales and use tax exemptions for new or expanding operations and normal operating replacements apply only to purchases or leases of tangible personal property used in the actual manufacturing process. The exemptions do not apply to purchases of real property or items of tangible personal property that become part of the real property in which the manufacturing operation is conducted. If a separate gas, water, or electrical supply line is installed solely for the operation of the manufacturing equipment, the gas, water, or electrical supply line is an accessory to the manufacturing equipment rather than a part of the real property.

C. Machinery and equipment or normal operating replacements used for an activity that is not part of the manufacturing process are not exempt unless the use in the nonqualifying activity is de minimis. Examples of nonqualifying activities include:

1. research and development;

2. refrigerated or other storage of raw materials, component parts, or finished product; or

3. shipment of the finished product.

D. Where manufacturing activities and nonmanufacturing activities are performed or normal operating replacements purchased for use in the manufacturing operation are eligible for the sales and use tax exemption for new or expanding operations or for normal operating replacements if the manufacturing operation constitutes a separate and distinct manufacturing establishment.

1. Each activity is treated as a separate and distinct establishment if:

a) no single SIC code includes those activities combined; or

b) each activity comprises a separate legal entity.

2. Machinery and equipment or normal operating replacements used in both manufacturing activities and nonmanufacturing activities qualify for the exemption for new or expanding operations or for normal operating replacements only if the use in nonmanufacturing activities is de minimis.

E. Purchases of qualifying machinery and equipment or normal operating replacements are treated as purchases of tangible personal property under R865-19S-58, even if the item is affixed to real property upon installation.

Charges for labor to repair, renovate, or install tangible personal property shall be taxable or tax exempt as provided in R865-19S-78.

Effective July 4, 2001, Rule R865-19S-85 was amended to read in relevant part as follows:

A. Definitions:
1. "Establishment" means an economic unit of operations, that is generally at a single physical location in Utah, where qualifying manufacturing processes are performed. If a business operates in more than one location (e.g., branch or satellite offices), each physical location is considered separately from any other location operated by the same business.
2. "Machinery and equipment" means:
a) electronic or mechanical devices incorporated into a manufacturing process from the initial stage where actual processing begins, through the completion of the finished end product, and including final processing, finishing, or packaging or articles sold as tangible personal property. This definition includes automated material handling and storage devices when those devices are part of the integrated continuous production cycle; and
b) any accessory that is essential to a continuous manufacturing process. Accessories essential to a continuous manufacturing process include:
(i) bits, jigs, molds, or devices that control the operation of machinery and equipment; and
(ii) gas, water, electricity, or other similar supply lines installed for the operation of the manufacturing equipment, but only if the primary use of the supply line is for the operation of the manufacturing equipment.

. . . .

B. The sales and use tax exemptions for new or expanding operations and normal operating replacements apply only to purchases or leases of tangible personal property used in the actual manufacturing process.
1. The exemptions do not apply to purchases of real property or items of tangible personal property that become part of the real property in which the manufacturing operation is conducted.
2. Purchases of qualifying machinery and equipment or normal operating replacements are treated as purchases of tangible personal property under R865-19S-58, even if the item is affixed to real property upon installation.
C. Machinery and equipment or normal operating replacements used for a nonmanufacturing activity qualify for the exemption if the machinery and equipment

> or normal operating replacements are primarily used in manufacturing activities. Examples of nonmanufacturing activities include:
> 1. research and development;
> 2. refrigerated or other storage of raw materials, component parts, or finished product; or
> 3. shipment of the finished product.
>
> D. Where manufacturing activities and nonmanufacturing activities are performed at a single physical location, machinery and equipment or normal operating replacements purchased for use in the manufacturing operation are eligible for the sales and use tax exemption for new or expanding operations or for normal operating replacements if the manufacturing operation constitutes a separate and distinct manufacturing establishment if:
> 1. Each activity is treated as a separate and distinct establishment if:
> a) no single SIC code includes those activities combined; or
> b) each activity comprises a separate legal entity.
> 2. Machinery and equipment or normal operating replacements used in both manufacturing activities and nonmanufacturing activities qualify for the exemption for new or expanding operations or for normal operating replacements only if the machinery and equipment or normal operating replacements are primarily used in manufacturing activities.

Utah Code Ann. §59-12-104(52)(A) was enacted by the Utah Legislature to be effective July 1, 2001, and provides, in relevant part:

> "(A) sale or lease of semiconductor fabricating or processing materials regardless of whether the semiconductor fabricating or processing materials
> '(i) actually come into contact with a semiconductor; or
> (ii) ultimately become incorporated into real property'".

DISCUSSION

Vax System

The issue on the Vax System is the easiest of the issues to resolve. No evidence has been presented to establish that the purchase of the Vax System by Petitioner would be exempt from sales and use tax by way of the manufacturers exemption established in Utah Code Ann. §59-12-

104(14). Therefore, if the Vax System was delivered to Petitioner at its facilities in Utah, then the transaction is subject to sales and use tax within the State of Utah, even if the system may have been thereafter sent outside the State of Utah by Petitioner to one of its facilities in another state. On the other hand, if the system was delivered by the seller to Petitioner at any of its facilities outside of the State of Utah, it is not subject to sales and use tax within the State of Utah.

In this matter, Petitioner has presented invoices and other documentary evidence which persuades the Commission that the Vax System at issue in the audit was delivered to the facilities of Petitioner in the State of STATE-1 and was not delivered to Petitioner within the State of Utah.

Respondent relied upon emails by Petitioner's representatives indicating that the Vax System was delivered in Utah. On further investigation, those employees determined they had been in error. In an Affidavit presented to the Tax Commission, it was represented that the system was not delivered in Utah, and that Affidavit is supported by bills of lading.

Based upon the evidence, the Commission determines that the more persuasive evidence indicates the Vax System at issue in the audit report was delivered to Petitioner at its facilities within the State of STATE-1. Accordingly, the Commission determines that the Vax System, which is at issue in this proceeding, was not subject to sales and use tax within the State of Utah.

Manufacturing Equipment

The position of Respondent is that both the electrical equipment and the clean room equipment are not exempt from sales and use tax because:

> "(1) no manufacturing activities take place at Petitioner's facility in CITY-2; (2) the disputed items are not used in a manufacturing process to manufacture an item sold as tangible personal property; and (3) the disputed items were converted by Petitioner into real property." (Respondent's Memorandum for Initial Hearing).

The Respondent first argues that no manufacturing activities take place at the CITY-2 facility, because the primary activity which occurs at the facility is only testing the components. It is the position of Respondent that the testing is not a part of the manufacturing process, but is merely a checking of the product once the manufacturing process has been completed.

If the testing at the CITY-2 facility was limited to a random sample to be sure that the units produced were, in general, functioning properly, such an argument may be more persuasive. However, in this circumstance, Petitioner testified that every unit produced must go through a testing procedure to determine the individual capacity and classification of that particular processing chip. Until a chip has been tested and classified it cannot be sold. Accordingly, the Commission determines that the testing activities which occur at the CITY-2 facility are a part of the manufacturing process. Moreover, Respondent has allowed the exemption on other machinery and equipment at the same facility. Therefore, manufacturing activities do take place at the CITY-2 facility.

The second argument of Respondent is that the disputed items are not used in the manufacturing process "to manufacture an item sold as tangible personal property." The Commission will address this issue separately with respect to each type of property.

Electrical Equipment

With respect to the electrical transformers, electrical switches, and batteries, the Commission determines that whether this constitutes machinery and equipment "used to manufacture an item sold as tangible personal property" is governed by Utah Administrative Code, Rule R865-19S-85. Paragraph A.3. defines machinery and equipment which is exempt under the statute. Paragraph A.3.b) includes as part of the machinery and equipment, "any peripheral device that is essential to a continuous manufacturing process. Qualifying peripheral devices . . . do not include gas, water, or electricity systems that constitute real property improvements as provided in B." Subparagraph B. provides "if a separate gas, water, or electrical supply line is installed solely for the operation of the manufacturing equipment, the gas, water, or electrical supply line is an accessory to the manufacturing equipment rather than a part of the real property."

The Commission determines that under the Rule, these electrical transformers, electrical switches and batteries are part of the electrical supply line that is installed solely for the operation of the manufacturing equipment. It is therefore an accessory to the manufacturing equipment and not part of the real property. Accordingly, the Commission determines that those items are manufacturing equipment and are exempt from the sales and use tax pursuant to the statute.

Clean Room Equipment

This area includes make up air units (MAU), recirculating air units (RFU), chillers, boilers, and flooring.

Subparagraph B of Rule R865-19S-85 provides, in relevant part:

> "The sales and use tax exemptions for new or expanding operations and normal operating replacements apply only to purchases or leases of tangible personal property used in the actual manufacturing process." (Emphasis added).

Subparagraph C of Rule R865-19S-85 provides, in relevant part:

> "Machinery and equipment for normal operating replacements used for an activity that is not part of the manufacturing process are not exempt unless the use in the nonqualifying activity is de minimus." (Emphasis added).

At the hearing, the testimony was that the boilers were used 94% for the manufacturing process, and 6% for the administration building. It was also testified that the chillers were used 80% for the manufacturing process and 20% for the administration building. It is at least arguable that the non-manufacturing use of the boilers is de minimus, although the Commission makes no finding of that in this matter. However, the non-manufacturing use of the chillers is more than de minimus, which therefore disqualifies the chillers on that basis alone.

In addition, the Commission has carefully reviewed the actual use of the clean room equipment and finds that it is not used in the actual manufacturing process. Those items are used primarily to provide an environment in which the manufacturing process takes place. Those items are not part of the actual physical conversion of raw materials into semiconductor products, and are not part of the physical manufacturing process.

For periods after the audit period, the legislature enacted an exemption, which became effective July 1, 2001, and exempts from the sales tax:

> "(A) sale or lease of semiconductor fabricating or processing materials regardless of whether the semiconductor fabricating or processing materials
> '(i) actually come into contact with a semiconductor; or
> (ii) ultimately become incorporated into real property'".

(Utah Code Ann. §59-12-104(52)(A).)

Petitioner claims this amendment to the statute was merely to clarify an ambiguity and to enact into statute the current exemption. However, the Commission finds that it modified and increased the exemption[1] to something which had not been exempted prior to the enactment of that new statutory provision. Therefore, while that new statutory provision may exempt the clean room equipment which is at issue in this proceeding beginning on July 1, 2001, it was not exempt prior to the enactment of that provision in the statute. Even if Petitioner is correct that subparagraph (52) clarifies an ambiguity in subparagraph (14), the Commission has a duty to construe any such ambiguity narrowly when it is applied to tax exemptions. Therefore, a narrow construction of the statute prior to the enactment of subparagraph (52) would also conclude that these items were not "used in the actual manufacturing process"[2]. Accordingly, these items are subject to the sales and use tax imposed in the audit.

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1 There is no doubt, for example, that the three-year requirement for manufacturing equipment does not apply to semi-conductor, fabricating or processing materials.

2 We recognize that the distinction between equipment "that is essential to a continuous manufacturing process" and equipment that creates an environment "that is essential to a continuous manufacturing process" is a fine distinction. We believe the distinction is justified by the clear judicial

DECISION AND ORDER

Based upon the foregoing, the Commission determines that the Vax computer unit was not delivered in Utah and is not subject to sales and use tax in the State of Utah. The Commission further determines that the electrical equipment is part of the machinery and equipment as a peripheral device, and is therefore exempt from sales tax, but that the clean room equipment, including the make up air units, recirculating air units, chillers, boilers, and flooring are not used in the actual manufacturing process, and are therefore not exempt from sales and use tax in the State of Utah. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission
Appeals Division
210 North 1950 West
Salt Lake City, Utah 84134

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this _____ day of _____, 2002.

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mandate we have received to construe exemptions narrowly.

_____
G. Blaine Davis
Administrative Law Judge

BY ORDER OF THE UTAH STATE TAX COMMISSION.

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this _____ day of _____, 2002.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Palmer DePaulis
Commissioner

GBD/ssw/00-1158.int

DISSENT

Notwithstanding the principal that narrow statutory construction should be applied for tax exemption, I believe that any interpretation of a statute should be based on an objective standard, to the extent possible. In this case the problem is to narrow the gap between all of the equipment in a manufacturing facility and the machine that actually produces the product.

Sufficient business practices exist to distinguish the manufacturing process from other processes. Equipment such as chairs, lighting, tables, climate-control components, etc. is considered general plant equipment, while more specialized equipment is designed for specific non-manufacturing operations. These things have a function, purpose, and use that exist outside of the manufacturing process. They can be used for broad general processes such as plant operations, administration, support, and storage, or specific processes such as research and development or retailing, even if they occur in a manufacturing facility. Their relationship to the actual manufacturing process is incidental. These types of equipment exist regardless of the type of manufacturing, if any, which might take place. There are even other types of enclosures such as cubicles, offices, and separate rooms, whose purpose is to separate various functions from one another. Here again, the functions exist independent from the manufacturing process.

In this case, however, the MAU's, RFU's, and the flooring have a specific and unique manufacturing purpose. (I am persuaded that the boilers and chillers have more than a de minimus use, and are not necessarily clean room equipment.) They exist solely for, and are absolutely critical to, the manufacturing process and nothing else. And, there are no substitutes. This equipment has

no conceivable function outside of the manufacturing process. Without this specific equipment there would be no product; it is an integral component of the continuous manufacturing process. Consequently an interpretation of the statute that allows for this equipment to be exempt is not unduly "broad." In fact, while the transformers, switches and batteries have correctly been found to be exempt, they at least have possible functions outside of the manufacturing process. The MAU's, RFU's, and flooring, again, do not. It seems to me that distinguishing between the two, finding electrical equipment is used in the manufacturing process, while the clean room is not used in the manufacturing process because it creates an environment, is an abstraction; an artificial distinction rather than an objective standard. To the contrary, I believe that the clean room equipment can be construed to be an even narrower interpretation of "used in the manufacturing process" than do the electrical components.

In addition, I find that the addition of Subsection (52) has not re-characterized the general manufacturing process under Subsection (14). The new wording addresses processing and fabrication materials specifically. These appear to be, rather than the same thing as general machinery and equipment, equipment unique to semi-conductor processing and fabrication.

Finally, I would like to clarify my position on two parts of the statute. Subsection (14)(a)(i)(C)(I) of §59-12-104 states that the equipment must be used "to manufacture an item sold as personal property." (Emphasis added.) This clause must be considered in its entirety. The requirement that property be sold is what distinguishes this section from Subsection (14)(a)(i)(A), which addresses the manufacturing process. Subsection (14)(a)(i)(C)(I) does not restrict the

manufacturing process to "to manufacture an item," and is not relevant to the determination of what constitutes the manufacturing process.

In conclusion, the critical issue in this case is the determination of what constitutes the "manufacturing process," and whether the equipment under appeal is used in that process. I would find for the reasons expressed above, that the clean room equipment qualifies for the exemption.

Marc B. Johnson
Commissioner

00-1158
TAX TYPE: SALES TAX
TAX YEAR: 7/95 – 6/98
COMMISSIONERS: P. HENDRICKSON, B. JOHNSON, P. DEPAULIS, M. JOHNSON

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER,	)	**ADDENDUM TO ORDER**
	)	
Petitioner,	)	Appeal No. 00-1158
	)	
v.	)	
	)	Tax Type:
AUDITING DIVISION OF	)	Tax Periods: 07/01/95 – 06/30/98
THE UTAH STATE TAX	)	
COMMISSION,	)	
	)	
Respondent.	)	Judge: Davis

Presiding:
G. Blaine Davis, Administrative Law Judge
Pam Hendrickson, Commission Chair
R. Bruce Johnson, Commissioner
Palmer DePaulis, Commissioner
Marc B. Johnson, Commissioner

Appearances:
For Petitioner: REPRESENTATIVE-1 FOR PETITIONER
REPRESENTATIVE-2 FOR PETITIONER
REPRESENTATIVE-3 FOR PETITIONER
REPRESENTATIVE-4 FOR PETITIONER
For Respondent: REPRESENTATIVE FOR RESPONDENT, Assistant Attorney General
RESPONDENT-1, from the Auditing Division
RESPONDENT-2, from the Auditing Division
RESPONDENT-3, Division Director, Auditing Division

STATEMENT OF THE CASE

This matter originally came before the Utah State Tax Commission for an Initial Hearing pursuant to the provisions of Utah Code Ann. ∋59-1-502.5, on April 4, 2002. The

Commission thereafter issued its Initial Hearing Decision on October 11, 2002. On October 22, 2002, a letter was received from Petitioner requesting clarification of the decision of the Commission on "generator sets". After receiving a response from Respondent, and holding oral arguments thereon, on November 26, 2002 an Order was issued reopening the Initial Hearing to clarify the undetermined matters. That reopened hearing was held on January 7, 2003.

Based upon the representations and arguments of the parties presented on January 7, 2003, the Commission hereby determines as follows:

1. Because this matter was a reopening of the Initial Hearing, the only matters before the Commission were issues which had not been resolved in the Order issued by the Commission on October 11, 2002. Therefore, the Commission did not reconsider its decision for those matters which were decided in that Order.

2. Regarding the generators, Petitioner represented that all of the generators at issue were purchased, installed, and intended to be used in the manufacturing process to manufacture an item sold as tangible personal property in new or expanding operations in a manufacturing facility in this state. Petitioner further represented that there was one generator which was purchased to function for the administrative areas, and that sales tax was paid to the vendors on the purchase of that generator. Therefore, except for the generator purchased for the administrative areas of the facility, the Commission determines that the generators are similar in purpose and use to the other electrical equipment, including the transformers, electrical switches, and batteries as set forth in the Decision of the Commission dated October 11, 2002. Therefore, under Utah Administrative Code,

Rule R865-19S-85, as that rule was in effect as of the date of purchase, those generators were installed solely for the operation of the manufacturing equipment and are accessories "to the manufacturing equipment rather than part of the real property". Accordingly, the Commission determines that those generators are manufacturing equipment and are exempt from sales and use tax pursuant to the statute.

3. In the Commission's original Order in this matter dated October 11, 2002, the Commission applied the portion of Rule R865-19S-85.C which was in effect at the time of the transactions that were the subject of the audit. That rule adopted a "de minimus" standard to the non-qualifying (non-manufacturing) activity of the equipment. That rule was amended by the time the audit was actually performed, and the new rule adopted a "primary" standard for the non-qualifying equipment instead of having a "de minimus" standard. Petitioner argued that even though some of the equipment had a non-manufacturing use that was greater than "de minimus", it's manufacturing use was at least the "primary" use. Therefore, Petitioner argued that the new rule should have been applied which, under the interpretation of Petitioner, would have exempted the items set forth in the October 11, 2002 Order as "clean room equipment". However, the Commission determines that the appropriate rule to use is the rule that was in effect at the time of the acquisition of the items. The new rule, which adopts the "primary" standard, should be utilized for all purchases and uses occurring on or after July 4, 2001.

4. The Commission does not modify or change any other provision from the October 11, 2002 Order.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission
Appeals Division
210 North 1950 West
Salt Lake City, Utah 84134

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this _____ day of _____, 2003.

_____
G. Blaine Davis
Administrative Law Judge

BY ORDER OF THE UTAH STATE TAX COMMISSION.

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this _____ day of _____, 2003.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Palmer DePaulis
Commissioner

Marc B. Johnson
Commissioner

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