

06-0890
SALES AND USE
TAX YEARS: 2000, 2001, 2002, 2003, 2004, 2005
SIGNED: 03-28-2008
COMMISSIONERS: R. JOHNSON, D. DIXON
DISSENT: P. HENDRICKSON, M. JOHNSON
GUIDING DECISION

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER,

Petitioner,

v.

AUDITING DIVISION OF THE
UTAH STATE TAX COMMISSION,

Respondent.

INITIAL HEARING ORDER

Appeal No. 06-0890

Account No. #####

Tax Type: Sales and Use Tax

Audit Periods: 02/01/00 – 12/31/02;
09/01/02 – 06/30/05

Judge: Chapman

Presiding:

Kerry Chapman, Administrative Law Judge

Appearances:

For Petitioner: PETITIONER REP. 1, ACCOUNTING FIRM
PETITIONER REP. 2, ACCOUNTING FIRM
PETITIONER REP. 3, from PETITIONER

For Respondent: RESPONDENT REP. 1, Assistant Attorney General
RESPONDENT REP. 2, from Auditing Division
RESPONDENT REP. 3, from Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for an Initial Hearing on January 2, 2008.

PETITIONER (“PETITIONER”) owns and operates two FACILITIES in Utah, one near CITY 1 and the other near CITY 2. Both of these facilities manufacture PRODUCTS for its customers, which may include (WORDS REMOVED).

Auditing Division began a review of PETITIONER's sales and use tax liabilities after the Petitioner submitted a refund request for taxes paid on certain transactions to Taxpayer Services Division for the period from February 1, 2000 through December 31, 2002 and Taxpayer Services Division issued a refund of tax in the amount of \$\$\$\$\$, plus interest accrued to the date of the refund.

Subsequently, Auditing Division (the "Division") audited the refund. On May 26, 2006, the Division disallowed the refund by issuing a Statutory Notice for the period February 1, 2000 through December 31, 2002 ("First Statutory Notice"), in which it assessed \$\$\$\$\$ in additional sales and use tax, plus interest in the amount of \$\$\$\$\$ (which included the interest refunded to the Petitioner plus additional interest that had accrued since the refund). No penalties were imposed. This assessment will be referred to in this decision as the "First Audit Assessment."

In addition, the Division conducted a separate audit of the Petitioner on all other transactions for the period September 1, 2002 through June 30, 2005. On June 9, 2006, the Division issued a second Statutory Notice for this period ("Second Statutory Notice"), in which it assessed \$\$\$\$\$ in additional sales and use tax, plus interest in the amount of \$\$\$\$\$, for a total of \$\$\$\$\$. No penalties were imposed. This assessment will be referred to in this decision as the "Second Audit Assessment."

The Division issued its assessments after determining that certain of the Petitioner's purchases on which it did not pay Utah sales and use tax were subject to taxation. Prior to the Initial Hearing, the parties had agreed on the taxability of some of the transactions.

At the Initial Hearing, the Petitioner originally contested five types of transactions found on the Division's assessments. After hearing the Petitioner's proffered evidence and testimony, the Division agreed that two of the five types of transactions were not taxable and agreed to remove those transactions from its audit assessments.

Specifically, the Division agreed to remove first the “prep” charges associated with the Petitioner’s purchases of MATERIAL that were then incorporated into the PRODUCT A it produced for sale. These “prep” charges were separately listed charges found on 16 invoices the Petitioner submitted to the Division from three different vendors (COMPANY A, COMPANY B, and COMPANY C). The Division agreed that these charges were associated with the purchase of the MATERIAL, which were eligible for the sales purchased for resale exemption. Second, the Division agreed to remove the June 14, 2005 purchase of a fork lift for \$\$\$\$\$, as shown on Invoice No. #####. The Division agreed that this particular fork lift qualified for the manufacturing machinery and equipment exemption.

However, the parties continue to disagree on three types of transactions that the Division taxed in its two assessments, as follows:

1. The Petitioner’s purchases of EQUIPMENT, which it uses in its manufacturing process to produce PRODUCT A for sale to its clients. The Petitioner contends that these items qualify for exemption under the manufacturing machinery and equipment exemption, while the Division claims that the items do not qualify because the Petitioner has not shown whether or not they have an economic life of three or more years;

2. The Petitioner’s purchases from COMPANY D of MATERIALS that the Petitioner used to make EQUIPMENT. The Petitioner used the EQUIPMENT in its manufacturing process not only in its two Utah facilities, but also in its other facilities located in the United States. The Petitioner contends that the MATERIALS are exempt either under the sale for resale exemption or the manufacturing exemption. The Division contends that the MATERIALS are taxable because the Petitioner has not shown that it sells the EQUIPMENT, thereby excluding the purchases from the resale exemption, and because the Petitioner has not shown that the EQUIPMENT have an economic life of three or more years, thereby disqualifying the purchases from the manufacturing exemption; and

3. The Petitioner's purchases of certain parts that are incorporated into the machinery and equipment it uses in its manufacturing process. The Petitioner contends that the parts are "replacement" parts that qualify for the manufacturing exemption, while the Division contends that the parts are "repair" parts that do not qualify for exemption.

APPLICABLE LAW

Manufacturing Machinery and Equipment Exemption. Utah law provides for a number of sales and use exemptions in Utah Code Ann. §59-12-104. Section 59-12-104(14)¹ provides for the exemption of certain tangible personal property used in a manufacturing facility, as follows in pertinent part:

- (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 manufacture an item sold as tangible personal property; and
 - (II) in new or expanding operations in a manufacturing facility in the state; and
 - (ii) . . . normal operating replacements that:
 - (A) have an economic life of three or more years;
 - (B) are used in the manufacturing process in a manufacturing facility in the state;
 - (C) are used to replace or adapt an existing machine to extend the normal estimated useful life of the machine; and
 - (D) do not include repairs and maintenance[.]

Utah Admin. Rule R865-19S-85 ("Rule 85")² provides guidance concerning the

¹ All citations to the Utah Code in this decision are to the 2005 version of the Code unless otherwise indicated. Although the applicable statutory provisions remain substantially the same throughout the audit periods, some of the subsections were renumbered over the periods. The Commission further notes that in 2006, subsequent to the audit periods at issue, the manufacturing exemption was substantially revised regarding replacement parts. However, the 2006 revisions regarding replacement parts have no effect on the issues in this decision.

² The version of Rule 85 cited is the one that was in effect from July 4, 2001 through June 30, 2005. The version of the rule in effect during 2000 and the first half of 2001, however, is similar enough to the later

manufacturing machinery and equipment exemption, as follows in pertinent part:

A. Definitions:

....

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 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 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.

...

5. "Normal operating replacements" includes:

- a) new machinery and equipment or parts, whether purchased or leased, that have the same or similar purpose as machinery or equipment retired from service due to wear, damage, destruction, or any other cause within 12 months before or after the purchase date, even if they improve efficiency or increase capacity.
- b) if existing machinery and equipment or parts are kept for backup or infrequent use, any new, similar machinery and equipment or parts purchased and used for the same or similar function.

....

E. The manufacturer shall retain records to support the claim that the machinery and equipment or normal operating replacements are qualified for exemption from sales and use tax under the provisions of this rule and Section 59-12-104.

....

Sale for Resale Exemption. Section 59-12-104(26) provides an exemption from sales and use tax for sales of "property purchased for resale in this state, in the regular course of business, either in its original form or as an ingreEQUIPMENTnt or component part of a manufactured or compounded product[.]"

version as to have no effect on the Commission's decision.

DISCUSSION

I. Has the Petitioner Shown that the EQUIPMENT Used in its Manufacturing Process Have an Economic Life of Three or More Years?

Section 59-12-104(14)(a) provides an exemption for purchase of machinery and equipment if a number of qualifications are met. Both parties agree that the EQUIPMENT at issue meet most of the requirements necessary to qualify for the exemption because they are used in the manufacturing process by a manufacturing facility in Utah to produce tangible personal property for sale. The only requirement to qualify for the exemption at issue is whether the EQUIPMENT have an economic life of three or more years, as set forth in Subsections 59-12-104(14)(a)(i)(B), (a)(ii)(A). The Division argues that the Petitioner has not shown that the equipment has an economic life of three or more years, while the Petitioner contends that it has.

Petitioner's Information and Arguments. The Petitioner proffers that EQUIPMENT are equipment used to WORDS REMOVED. The EQUIPMENT, which may be either EQUIPMENT or EQUIPMENT, generally cost less than \$\$\$\$ each. The EQUIPMENT are made up of (WORDS REMOVED). The EQUIPMENT are made up of (WORDS REMOVED). (SENTENCE REMOVED).

The Petitioner proffers that while the life of a EQUIPMENT depends on the amount of times the EQUIPMENT is used, it is common, with ordinary repairs and occasional knife replacements, for EQUIPMENT to last several years depending on the size and frequency of customers' box orders. The Petitioner also states that a EQUIPMENT is retained until that same customer orders more PRODUCT A or until other customers order PRODUCT A with the same specifications. In an Affidavit of PLANT MANAGER ("PLANT MANAGER Affidavit"), who is the plant manager of the Petitioner's facility in CITY 1, Utah, PLANT MANAGER states in paragraph 16 that "the useful lives of the overwhelming majority of these EQUIPMENTs cannot be measured in months or years. Rather, they are measured by discreet (sic)

product runs dictated as customers need the specific units ordered from time to time.” In paragraphs 18, Mr. PLANT MANAGER further states that “[t]he overwhelming majority of the EQUIPMENTs at the Plant have a useful life well in excess of three years, taking into account that their use is intermittent. Most of the Plant’s EQUIPMENTs are in storage for a longer period than they are on the machine.”

The Petitioner also proffers that EQUIPMENT are equipment used to (WORDS REMOVED) during the manufacturing process. The EQUIPMENT are made of (WORDS REMOVED) material. In the manufacturing process, the EQUIPMENT are temporarily attached to (WORDS REMOVED). Once the process is complete, the (X) are washed and stored until the next order. Each (X) is specific to each printed image, so that if the image or wording changes, a new (X) must be made.

The Petitioner proffers that the life of a ITEM is dependent on the number of times it is used, i.e., the number of (WORDS REMOVED). In paragraph 22 of the PLANT MANAGER Affidavit, PLANT MANAGER states that the “individual product runs [in which the EQUIPMENT are used] are typically intermittent and not lengthy in duration.” He further states in paragraphs 23 and 24 that “[t]he ultimate life of the ITEM, as with EQUIPMENTs, is dictated by the number of times of use, rather than any daily, weekly, monthly or yearly interval” and that in “the majority of the cases, the useful life of the print EQUIPMENT is in excess of three years.”

The Petitioner admits that it expenses the EQUIPMENT and specialty EQUIPMENT instead of capitalizing them for income tax purposes because of their relatively low cost. The Petitioner explains that these items rarely, if ever, cost more than \$\$\$\$ and, as a result, do not meet the \$\$\$\$ threshold the company uses to capitalize attachments to equipment. The Petitioner also admits that it has not included the EQUIPMENT on its personal property tax returns. However, it argues that these circumstances should not disqualify the EQUIPMENT from having an economic life of three or more years. The Petitioner argues that it is common for corporations to establish a reasonably low cost threshold amount for purposes of expensing

an item instead of capitalizing it. The Petitioner also contends that this practice is common for corporations required to follow the General Accepted Accounting Principles (“GAAP”) and is accepted by the Internal Revenue Service (“IRS”).

The Petitioner argues that the proper standard to determining “economic life” should be whether: 1) the normal replacement interval for such items, given the nature of the taxpayer’s business, is three or more years; or 2) there is reasonable expectation that, at the time of purchase, the items will still be useful three or more years after the purchase.

The Petitioner admits if that the EQUIPMENT were used eight hours a day for several weeks, they would probably need to be replaced. However, the Petitioner does not believe that this fact establishes a life of less than three years for the equipment at issue. Because the Petitioner would rarely, if ever, use a EQUIPMENT or ITEMS for such a continuous interval and because it routinely keeps EQUIPMENT for future use in excess of three years, it believes that it has shown that the EQUIPMENT remain economically useful for and, accordingly, have an economic life of three or more years. As an example, the Petitioner contends that a EQUIPMENT or ITEMS with a useful, or manufacturing, life of only eight hours should qualify for the exemption if the item was used for four hours at the time of purchase, then stored for three years for future use of the remaining four hours. Under these circumstances, the Petitioner contends that the “economic” life of the item is more than three years.

The Petitioner states that its arguments are supported by a decision issued by a State of Washington administrative law judge (“ALJ”) in Washington Tax Determination No. 99-306, 19 WTD 502 (November 23, 1999). In that decision, the ALJ considered whether rubber EQUIPMENT used by a Washington manufacturer of plastic bags had a “useful life of one year or more,” as required under Washington law. The taxpayer used the EQUIPMENT intermittently and stated that it routinely kept the EQUIPMENT for use for more than one year. The taxpayer did not capitalize the EQUIPMENT for income

tax purposes and estimated that approximately 75% of the EQUIPMENT that it stored after the first use are reused at a later time. The Washington Department of Revenue argued that the EQUIPMENT would not have a useful life of one year if used on a regular and recurring basis, instead of intermittently.

The ALJ applied a Washington rule that provided that equipment has a useful life of one or more years if the “equipment [was] expected at the time of purchase to last at least one year, as established by industry or business practice . . . (This is commonly based on the actual experience of the person claiming the exemption.)” When applying this rule, the ALJ determined that EQUIPMENT used only once did not qualify for the exemption. The ALJ also determined that the EQUIPMENT at issue appeared to have a useful life of one or more years because the normal replacement interval for the EQUIPMENT, given the nature of the taxpayer’s business, is one year or more and because the taxpayer expects the EQUIPMENT to last at least one year at the time of purchase, given the taxpayer’s actual experience. Nevertheless, the ALJ also determined that not all EQUIPMENT still in inventory after one year of purchase would qualify as having a life of one or more years, such as EQUIPMENT with time sensitive information (e.g., dates) that would be useless prior to one year after the date of purchase.

Division’s Arguments. The Division argues that the Petitioner has not demonstrated that its EQUIPMENT have an economic life of three or more years. First, the Division argues that the Petitioner has not shown that the EQUIPMENT will be used for more than one job. The Division explains that at the time the EQUIPMENT are purchased, the Petitioner does not know whether it will use the items more than once because it does not know whether it will receive future orders for the exact same PRODUCT A for a period of three or more years.

Second, the Division states that the fact the Petitioner expensed, instead of capitalizing, its purchases of the EQUIPMENT for income tax purposes suggests that the items have an economic life of less than three years. Furthermore, the Division argues that when EQUIPMENT are physically present and used

in the manufacturing process, they should be included on the personal property tax return filed with the appropriate county government, regardless of whether they are capitalized or expensed for income tax purposes. The Division proffers that the Petitioner did not list the EQUIPMENT on its property tax returns, also suggesting that the items do not have an economic life of three or more years.

The Division further asks the Commission to consider that the Utah Supreme Court has determined that exemption statutes should be narrowly construed in favor of taxation. *See Parson Asphalt Prod. Inc. v. Utah State Tax Comm'n*, 617 P.2d 397 (Utah 1980). Given the information proffered at the Initial Hearing, the Division asks the Commission to find that the Petitioner has not shown that the EQUIPMENT at issue have an economic life of three or more years.

Commission's Analysis and Conclusion. For income tax purposes, the Petitioner has decided to expense, instead of capitalizing, the EQUIPMENT at issue. Furthermore, the Petitioner has not reported the EQUIPMENT on its property tax returns. Although the Commission believes these circumstances are factors to consider when determining whether a property has an economic life of three or more years for purposes of the manufacturing exemption, the Commission does not consider these facts dispositive. First, neither Section 59-12-104(14) nor Rule 85, which concern the manufacturing exemption, specifically requires equipment to be capitalized or be reported on property tax returns to qualify for the exemption.³ Second, the Commission recognizes that a taxpayer's decision to expense equipment instead of capitalizing it may be dependent on the cost of the equipment instead of its economic life.

Furthermore, the Commission notes that the Legislature has provided that machinery and equipment may qualify for the manufacturing exemption if its *economic life*, not actual manufacturing life, is

³ In *xxxxx v. Auditing Division, USTC Appeal No. 94-1556*, the Commission determined that certain equipment had an economic life of three or more years, even though the taxpayer expensed the equipment instead of capitalizing it. Unlike the circumstances in this appeal, the Division agreed in that case that the equipment would have had an economic life of three or more years had the taxpayer not expensed it.

three or more years. For this reason, the Commission is persuaded that a taxpayer's business practices are important when determining whether a taxpayer will receive an economic benefit from an item for three or more years. In this case, one of the Petitioner's plant managers, PLANT MANAGER, stated in his affidavit that "the overwhelming majority" of the EQUIPMENT and the "majority" of the EQUIPMENT have a useful life in excess of three years, given the Petitioner's intermittent use and storage of the items. For these reasons, it appears that a majority of the EQUIPMENT at issue have an economic life of three or more years and that the purchases of these items may qualify for the manufacturing exemption.

Concerning the EQUIPMENT, the Commission finds PLANT MANAGER's statement that an "overwhelming majority" of the EQUIPMENTs have a useful life in excess of three years to be sufficient to carry the Petitioner's burden of proof. The Commission believes that the test must be applied at the outset of the purchases and, accordingly, be based on the Petitioner's reasonable expectation at the time of purchase. Because the Petitioner has proffered that its expectation at the time of purchase is that an "overwhelming majority" of EQUIPMENT will have a useful life in excess of three years, only a de minimis number of EQUIPMENTs will have a life of less than three years. The Commission concludes that the Petitioner has reasonably established that all EQUIPMENT purchases should receive the manufacturing exemption.

In contrast, the Commission finds PLANT MANAGER's statement that only a "majority" of the EQUIPMENT have a useful life in excess of three years to be insufficient to carry the Petitioner's burden of proof. At the time of the Petitioner's purchase of EQUIPMENT, its expectation is not that an overwhelming majority of the EQUIPMENT will have a useful life of three years or more. As a result, the Commission concludes that at the time of purchase, the Petitioner expects a significant number of EQUIPMENT not to have a useful life of three years or more. Without more explicit information about the actual transactions or the percentage of EQUIPMENT that qualify for exemption, the Commission finds that

the Petitioner has not proffered sufficient evidence for the Commission to grant the manufacturing exemption to any of its purchases of EQUIPMENT.

II. Are the MATERIALS Used to Make EQUIPMENT Exempt from Taxation?

The Petitioner purchases many of the EQUIPMENT it uses in the manufacturing process. However, it also produces some EQUIPMENT itself that are used not only in its two Utah facilities, but also in its facilities in other states. The Petitioner purchases MATERIALS to make the EQUIPMENT. The Division does not contest that the chemicals are a component part of the EQUIPMENT. The Petitioner believes that its purchases of the MATERIALS are exempt from taxation either under: 1) the manufacturing exemption, because the chemicals are used to manufacture an item (i.e., the ITEMS) that qualifies for the exemption; or 2) the sale for resale exemption of Section 59-12-104(26), because the chemicals become a component part of EQUIPMENT that it uses in its plants.

Manufacturing Exemption. For EQUIPMENT that have an economic life of three years or more and qualify for exemption, the Petitioner argued that any MATERIALS purchased to produce such EQUIPMENT would also qualify for exemption. As discussed above, the Commission has determined that the Petitioner's EQUIPMENT do not qualify for the manufacturing exemption. As a result, the Commission need not address whether the chemicals would qualify for the manufacturing exemption. Accordingly, any MATERIALS used to produce these EQUIPMENT would also not qualify for exemption.

Sale for Resale Exemption. The Petitioner also argued that the sale for resale exemption applies. Section 59-12-104(26) specifies that this exemption applies only to items that are incorporated into a *product that is sold*. From the testimony proffered, it appears that the Petitioner uses a number of the EQUIPMENT produced with the MATERIALS at its Utah plants. Because these EQUIPMENT are not "resold," the component parts used to produce these EQUIPMENT do not qualify for the sale for resale

exemption. Furthermore, the Petitioner has proffered no evidence to show that it sells any of the EQUIPMENT it produces with the MATERIALS. In fact, the Petitioner proffered that it does not know if any of the EQUIPMENT are sold. Accordingly, the Commission finds that the MATERIALS at issue do not qualify for the sale for resale exemption.

Conclusion. Based on the evidence and testimony provided at the Initial Hearing, the Commission finds that the Petitioner has not demonstrated that the MATERIALS it purchased are exempt from taxation. Accordingly, the Commission sustains the Division's assessment of tax on the Petitioner's purchases of MATERIALS.

III. Has the Petitioner Shown that the Division Improperly Assessed Tax on Exempt Purchases of "Normal Operating Replacements"?

The Petitioner states that the Division has imposed tax on its purchases of "normal operating replacements," which it claims are exempt under the manufacturing exemption. Section 59-12-104(14)(a)(ii) provides the requirements that must be met for machinery or equipment to qualify as exempt "normal operating replacements." Subsections 59-12-104(14)(a)(ii)(C),(D) provide that items qualify as "normal operating replacements" only if they "are used to replace or adapt an existing machine to extend the normal estimated useful life of the machine" and are not "repairs and maintenance."

The Petitioner gives an example of the equipment it believes the Division has improperly assessed. The Petitioner states that a drive shaft purchased to replace a broken or worn drive shaft in a press would qualify as an exempt normal operating replacement because it is a needed replacement. The Petitioner argues that such parts qualify for exemption because they are used to replace or adapt an existing machine in order to extend the normal operating life of the machine. The Petitioner claims that the drive shaft is deemed to extend the life of the machine, because without the new part, the machine would not continue to operate. The difficulty in this matter is determining whether the contested items were purchased to adapt an existing

machine or to extend the normal estimated life of the machine or whether they were purchased merely as to repair or maintain a machine.

To decide whether a new part is an exempt normal operating replacement or a taxable repair, the Commission looks first to the plain language of the statute and gives the terms contained in the statute their ordinary meaning. As a result, the Commission must determine whether the Petitioner has shown that the purchases at issue concerned items to “replace” an existing machine or to “adapt an existing machine to extend the normal estimated useful life.” If the Petitioner were actually replacing an old machine with a new one and the other statutory requirements were satisfied, the Petitioner’s purchases would clearly qualify for exemption. The Commission notes, however, that replacing a part or parts of a piece of machinery or equipment is not the same as replacing an existing machine. As a result, the replacement of parts is not necessarily exempt.

In determining whether the purchase of a part is exempt, the Commission must consider whether the part was purchased to “**adapt** an existing machine to extend the useful life” (emphasis added), in addition to the other statutory requirements. The Commission notes that instead of phrasing the exemption to encompass all purchases of replacement parts that extend a machine’s useful life, the Legislature set forth the limitation that the item purchased must “adapt” the existing machine to extend the useful life. When interpreting a statute the Commission must assume that each term included in the statute was used advisedly. *See MacFarlane v. Utah State Tax Comm’n*, 2006 UT 25 (Utah 2006). Furthermore, where the Legislature has not specifically defined a word, the Commission considers its ordinary or dictionary definition. *See Hercules, Inc. v. Utah State Tax Comm’n*, 21 P.3d 231 (Utah Ct. App. 2000).

Webster’s II New Riverside University Dictionary (1988), p. 77, defines “adapt” to mean “to adjust to a specified use or situation.” It is clear that in drafting the statute in this manner, the Legislature did not provide the exemption merely for items used to replace a broken part with the same part. Instead, the

exemption applies to items used to replace a part, which may or may not be broken, with something that would result in an adjustment to the machine that would extend its useful life.

Using these criteria, the Commission must consider each item and its purpose to determine whether it is an exempt normal operating replacement or a taxable repair part. Without additional information, it appears that the drive shaft the Petitioner used as an example would be a taxable repair part because it does not replace the press or adapt the press to extend its useful life. Furthermore, at the Initial Hearing, the presiding officer asked the Petitioner to go through the transactions at issue and describe the items that were purchased, why they were purchased, and how they affected the machines into which they were incorporated. The Petitioner stated that it did not have this information available at the Initial Hearing. For these reasons, the Commission finds that the Petitioner has not demonstrated that the purchases at issue were for items that qualified as exempt normal operating replacements. Accordingly, the Commission sustains the Division's determination that the items at issue were for repairs and its assessment of tax on these transactions.

ORDER⁴

Based upon the foregoing, the Commission approves the Division's decision to remove from its audit assessments: 1) the Petitioner's June 14, 2005 purchase of a fork lift, as identified on Invoice No. #####; and 2) the "prep" charges associated with the Petitioner's purchases of MATERIAL from COMPANY A, COMPANY B, and COMPANY C, as identified on the 16 invoices proffered at the Initial Hearing. For the remaining transactions that remain in dispute, the Commission finds that the Petitioner has proven that its purchases of EQUIPMENT qualify for the manufacturing exemption and are exempt from taxation.

4 Two of the Commissioners determined that the Petitioner's purchases of EQUIPMENT are exempt from taxation, while the other two Commissioners determined that the purchases should be taxable. In accordance with Utah Code Ann. §59-1-205(2)(c), when a Commission vote result is a tie vote, "the position of the taxpayer is considered to have prevailed."

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However, the Commission sustains the Division's assessments of additional tax on the remainder of the disputed transactions. 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 _____, 2008.

Kerry Chapman
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 _____, 2008.

R. Bruce Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

DISSENT

Appeal No. 06-0890

Although we agree with most of our colleagues' majority decision, we dissent in regards to one issue. We would find that the Petitioner's evidence is insufficient to grant the manufacturing equipment exemption to the Petitioners' purchases of EQUIPMENT.

Although we agree that PLANT MANAGER's statement indicates that an "overwhelming majority" of the EQUIPMENT would qualify for the exemption, his statement also implies that a minority of the EQUIPMENT would not qualify for the exemption. Rule 85(E) provides that a "manufacturer shall retain records to support the claim that the machinery and equipment or normal operating replacements are qualified for exemption from sales and use tax." The Petitioner has not provided sufficient records or other evidence for the Commission to determine the number of EQUIPMENT transactions that are exempt or to estimate what percentage of those transactions qualify for exemption. Without such evidence, we would sustain the Division's assessment on all of the Petitioner's purchases of EQUIPMENT.

Pam Hendrickson
Commissioner

Marc B. Johnson
Commissioner

Notice: If a Formal Hearing is not requested as discussed above, failure to pay the balance resulting from this order within thirty (30) days from the date of this order may result in a late payment penalty.

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