

08-1657  
SALES AND USE TAX  
TAX YEARS: 2005, 2006, 2007  
SIGNED: 12-06-2011  
COMMISSIONERS: R. JOHNSON, M. JOHNSON, M. CRAGUN  
CONCURRENCE: D. DIXON  
GUIDING DECISION

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BEFORE THE UTAH STATE TAX COMMISSION

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PETITIONER,  Petitioner,  v.  AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION,  Respondent.	<b>INITIAL HEARING ORDER</b>  Appeal No.    08-1657  Account No.   ##### Tax Type:     Sales and Use Tax Audit Period: February 1, 2005 to December 31, 2007  Judge:        Jensen
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**Presiding:**  
    Clinton Jensen, Administrative Law Judge

**Appearances:**  
    For Petitioner:    PETITIONER REP. 1, for the Taxpayer  
                          PETITIONER REP. 2, for the Taxpayer  
    For Respondent:   RESPONDENT REP. 1, Assistant Attorney General  
                          RESPONDENT REP. 2, from Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for an Initial Hearing on April 21, 2010. On June 26, 2008, the Auditing Division of the Utah State Tax Commission (“Division”) issued a Statutory Notice - Sales and Use Tax (“Statutory Notice”) to the Petitioner (the “Taxpayer”) for the audit period February 1, 2005 through December 31, 2007. In the Statutory Notice, the Division imposed \$\$\$\$ in additional sales and use tax plus interest in the amount of \$\$\$\$\$, for a total of \$\$\$\$\$. The Division did not impose penalties in connection with its audit.

The Statutory notice included six schedules indicating different classes of property or taxation issues. The parties resolved schedules 1, 2, 3, 5, and 6 prior to the initial hearing before the Commission. The parties’ dispute is thus limited to schedule 4, which dealt with costs related to the maintaining of printing equipment.

APPLICABLE LAW

For the period from February 1, 2005 to December 31, 2007, Utah law provided for a sales or use tax to be paid by the purchaser of “retail sales of tangible personal property made within the state.” Utah Code Ann. §59-12-103(1)(a) (2007). For the same period, Utah Code Ann. §59-12-103(1)(g) (2007) provided for sales or use tax to be paid by the purchaser of “amounts paid or charged for services for repairs or renovations of tangible personal property” unless exempted under Utah Code Ann. §59-12-104.

For the period from February 1, 2005 to December 31, 2007, Utah law provided for exemption from sales tax for property purchased for resale. *See* Utah Code Ann. §59-12-104.

Effective January 1, 2007, the Utah Legislature amended Utah tax laws to include the concept of a “bundled transaction.” For 2007 and 2008, bundled transactions were defined to include food items bundled with other items. Utah Code Ann. §59-12-102(12) (2007) defines a bundled transaction, in pertinent part, as follows:

- (a) “Bundled transaction” means the sale of two or more items of tangible personal property if:
  - (i) one or more of the items of tangible personal property is food and food ingredients;  
and
  - (ii) the items of tangible personal property are
    - (A) distinct and identifiable; and
    - (B) sold for one price that is not itemized.

Effective January 1, 2009, the Utah Legislature amended the definition of a bundled transaction to expand it beyond a food items bundled with other items. Utah Code Ann. §59-12-102(15) (2009) provided, in pertinent part, as follows:

- (a) "Bundled transaction" means the sale of two or more items of tangible personal property, products, or services if the tangible personal property, products, or services are:
  - (i) distinct and identifiable; and
  - (ii) sold for one nonitemized price.

Effective January 1, 2007, the Utah Legislature enacted different tax treatment for a “bundled transaction.” Like the 2007 version of the definition for “bundled transaction, the tax treatment applied to food products bundled with other items. Utah Code Ann. §59-12-103(2) (2007) allows for a lower tax rate on the food items in the bundled transaction than on the non-food items.

When the Utah Legislature expanded the definition of “bundled transaction” to include non-food transactions in 2009, it added language to Utah Code Ann. §59-12-103 (2009) to provide tax treatment for

bundled transactions not involving food. Describing the tax treatment for transactions not involving food, Utah Code Ann. §59-13-103(2)(d) (2009) provides, in pertinent part, as follows:

- (ii) Subject to Subsection (2)(d)(iii), for a bundled transaction other than a bundled transaction [involving food items]:
  - (A) if the sales price of the bundled transaction is attributable to tangible personal property, a product, or a service that is subject to taxation under this chapter and tangible personal property, a product, or service that is not subject to taxation under this chapter, the entire bundled transaction is subject to taxation under this chapter unless:
    - (I) the seller is able to identify by reasonable and verifiable standards the tangible personal property, product, or service that is not subject to taxation under this chapter from the books and records the seller keeps in the seller's regular course of business; or
    - (II) state or federal law provides otherwise;
  - (B) if the sales price of a bundled transaction is attributable to two or more items of tangible personal property, products, or services that are subject to taxation under this chapter at different rates, the entire bundled transaction is subject to taxation under this chapter at the higher tax rate unless:
    - (I) the seller is able to identify by reasonable and verifiable standards the tangible personal property, product, or service that is subject to taxation under this chapter at the lower tax rate from the books and records the seller keeps in the seller's regular course of business; or
    - (II) state or federal law provides otherwise.
- (iii) For purposes of Subsection (2)(d)(ii), books and records that a seller keeps in the seller's regular course of business includes books and records the seller keeps in the regular course of business for nontax purposes.

As of February 1, 2005, Utah Code Ann. §59-12-104 (2005) provided an exemption for sales tax on manufacturing equipment and normal operating replacements. The subsection giving the exemption provided, in pertinent part, as follows:

The following sales and uses are exempt from the taxes imposed by this chapter:

....

- (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) subject to the provisions of Subsection (14)(b), 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;

Effective July 1, 2006, the Utah legislature amended the manufacturing exemption at Utah Code Ann. §59-12-104 (2006) to provide an exemption, in pertinent part, for the following property:

(14) (a) except as provided in Subsection (14)(b), amounts paid or charged on or after July 1, 2006, for a purchase or lease by a manufacturing facility other than a cogeneration facility, for the following:

- (i) machinery and equipment that:
  - (A) is used:
    - (I) for a manufacturing facility except for a manufacturing facility that is a scrap recycler described in Subsection 59-12-102(43)(b):
      - (Aa) in the manufacturing process; and
      - (Bb) to manufacture an item sold as tangible personal property; or
    - (II) for a manufacturing facility that is a scrap recycler described in Subsection 59-12-102(43)(b), to process an item sold as tangible personal property; and
  - (B) has an economic life of three or more years; and
- (ii) normal operating repair or replacement parts that:
  - (A) have an economic life of three or more years; and
  - (B) are used:
    - (I) for a manufacturing facility in the state other than a manufacturing facility that is a scrap recycler described in Subsection 59-12-102(43)(b), in the manufacturing process; or
    - (II) for a manufacturing facility in the state that is a scrap recycler described in Subsection 59-12-102(43)(b), to process an item sold as tangible personal property;

#### DISCUSSION

The parties agree that the transactions in schedule 4 of the audit described in the Division's Statutory Notice are charges assessed to repair and maintain the Taxpayers digital printing equipment. For repairs to its printing equipment, the Taxpayer is the user of goods and services and would thus pay sales or use tax on the repairs unless the repairs are subject to an exemption. The parties agree that charges for tangible personal property such as toner that becomes part of the Taxpayer's products are exempt for sales tax if separately invoiced to the Taxpayer.

While some of the Taxpayer's repair charges are for individually itemized repairs, the majority of the charges are per printed impression or "per click." The parties agree that the invoices at issue are charges to maintain, service, and repair the Taxpayer's printing equipment without regard to whether they were invoiced per repair or per click. They also agree that at least some of the charges listed in schedule 4 have imbedded charges for toner for the Taxpayer's digital printing equipment. The toner charges are not separately identified on invoices that the Taxpayer received for the per repair or per click charges.

The Taxpayer advances three arguments in favor of its position that repair charges are not subject to sales tax. First, the Taxpayer requests direct exemption of the repair costs under the manufacturing exemptions in Utah Code Ann. §59-12-104. Second, the Taxpayer maintains that even if the repair costs are not directly exempt under Utah Code Ann. §59-12-104, they should be exempt because they become part of equipment that is exempt under Utah Code Ann. §59-12-104. Third, as an alternative argument, the Taxpayer argues that even if its costs to repair and maintain its equipment are not exempt, the costs for toner imbedded in its repair costs become part of the Taxpayer's finished product that is later held for resale and are thus exempt under Utah Code Ann. §59-12-104. The Division maintains that its audit concluding that sales tax is properly assessed on repair costs for digital printing equipment, including toner charges when those toner charges are not separately invoiced. The Commission considers each of the Taxpayer's arguments separately.

#### Manufacturing Exemption

Each of the manufacturing exemptions applicable to the periods at issue in this case allows exemptions for machinery and normal operating replacements that have, among other requirements, "an economic life of three or more years." The Taxpayer acknowledges that the invoices for its repairs do not differentiate between equipment with economic lives longer or shorter than three years. However, the Taxpayer relies on 2009 statutes for bundled transactions that allow a Taxpayer to remove items not subject to taxation from co-mingled transaction if "the seller is able to identify by reasonable and verifiable standards the tangible personal property, product, or service that is not subject to taxation under this chapter from the books and records the seller keeps in the seller's regular course of business" as described in Utah Code Ann. §59-13-103(2)(d)(ii)(A)(I) (2009).

The Taxpayer agrees that Utah Code Ann. §59-13-103(2)(d)(ii)(A)(I) (2009) was not in effect during the periods at issue in this case. The Taxpayer acknowledges the general rule that statutes do not have retroactive application. *See Harvey v. Cedar Hills City*, 2010 UT 12 ¶12 (courts apply version of statute in

effect at time of the events giving rise to suit). However, the Taxpayer argues that the 2009 discussion and tax treatment of bundled transactions merely codified already-existing Utah law. The problem with that argument is that the Taxpayer has not cited any statutes or case law that would indicate that Utah recognized the concept of a bundled transaction or gave bundled transaction tax treatment for food items before 2007 or for non-food items before 2009. Because there is no statutory basis or case law supporting the Taxpayer's position, the Commission applies the statutes in effect as of the date of the transactions at issue in this case. Under those statutes, the Taxpayer is not entitled to a manufacturing exemption for the items at issue in this case.

#### Short-life Repairs as Components of Longer-lived Equipment

The Taxpayer argued that because replacement parts are integrated into printing equipment with a life of more than three years, the three-year requirement applicable to replacement parts does not apply to parts that merely "repair" manufacturing equipment. The Taxpayer points to 2006 changes to Utah Code Ann. §59-12-104(14)(a)(ii) (2005) eliminating subsection (D), which had provided that "repairs and maintenance" did not qualify for the manufacturing exemption. The Taxpayer points to this statutory change as evidence that the legislature intended to add repairs as exempt under Section 104.

The problem with the Taxpayer's position with exemption is that the 2006 amendments to the manufacturing exemption specifically retained the requirement that "normal operating repair or replacement parts . . . have an economic life of three or more years." Utah Code Ann. §59-12-104(14)(a)(ii)(A) (2006). Thus, while the 2006 amendments may have enlarged the manufacturing exemption to remove a previous prohibition on repairs, it did not allow exemption for repairs independent of a three-year economic life or allow the repairs to adopt the economic life of the equipment to which they are attached. For these reasons, the Taxpayer has not demonstrated the applicability of a manufacturing exemption to the repairs at issue in this case, even those involved in transactions on or after July 1, 2006.

#### Purchases of Toner Comingled With Repair Transactions

The Taxpayer argues that even if repairs to printing equipment are not exempt, costs for toner imbedded in the repairs costs are exempt. The Taxpayer provided testimony that the toner at issue becomes part of the goods that the Taxpayer ultimately sells and were therefore purchased for resale and exempt under Utah Code Ann. §59-12-104. The Division did not dispute that toner became part of property ultimately sold

to others or that the toner would be exempt if separately itemized on documents evidencing their purchase. However, it argues that for purchases before 2009 changes to Utah law regarding bundled transactions, the Taxpayer's purchase of toner as a comingled element of repairs renders them taxable. The Taxpayer responded to this argument with the position that the 2009 changes to taxation of bundled transactions merely codified already-existing law. But as indicated earlier, the Taxpayer provided no evidence to support the position that Utah law allowed special tax treatment for bundled transactions involving non-food items before January 1, 2009. On that basis, there is not good cause to find error in the Division's treatment of toner purchases imbedded into repair invoices.

Clinton Jensen  
Administrative Law Judge

ORDER

On the basis of the foregoing, the Commission sustains the determinations of the Division as reflected in schedule 4 of its audit for the period from February 1, 2005 through December 31, 2007. 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 \_\_\_\_\_, 2011.

R. Bruce Johnson  
Commission Chair

Marc B. Johnson  
Commissioner

Michael J. Cragun  
Commissioner

**Commissioner Dixon Concur**

I concur with the majority, but write separately to further address the “reasonable and verifiable” standard raised by the Taxpayer, and whether “bundled transaction” language in 2008 legislation was meant to codify previous legislative intent.

I take administrative leave to note the Taxpayer is referring to HB 206 Tax Amendments (2008) sponsored by Rep. Harper. This bill can be viewed on the Utah State Legislature public website<sup>1</sup>. The language in the bill that became effective January 1, 2009 is underlined below:

*Section 8. Section 59-12-102 is amended to read: 59-12-102. Definitions.*

*(a) "Bundled transaction" means the sale of two or more items of tangible personal property, products, or services if the tangible personal property, products, or services are:*

- (i) distinct and identifiable; and*
- (ii) sold for one nonitemized price.*

*Section 10. Section 59-12-103 is amended to read: 59-12-103. Sales and use tax base -- Rates -- Effective dates -- Use of sales and use tax revenues.*

*(ii) Subject to Subsection (2)(d)(iii), for a bundled transaction other than a bundled transaction described in Subsection (2)(d)(i):*

- (A) if the sales price of the bundled transaction is attributable to tangible personal property, a product, or a service that is subject to taxation under this chapter and tangible personal property, a product, or service that is not subject to taxation under this chapter, the entire bundled transaction is subject to taxation under this chapter unless:*
- (B) (I) the seller is able to identify by reasonable and verifiable standards the tangible personal property, product, or service that is not subject to taxation under this chapter from the books and records the seller keeps in the seller's regular course of business; (more)....*

The Taxpayer advanced the argument that the 2008 language codified the previous intent of the Legislature and as such the Commission can look to see if the Taxpayer can “identify by reasonable and verifiable standards” an item of tangible personal property that may not be subject to sales tax.

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<sup>1</sup> HB 206 (2008)) <http://le.utah.gov/~2008/htmdoc/hbillhtm/HB0206.htm> Line 847 and Line 2374



I took administrative leave and listened to the audio files on HB 206 (2008) available on the Utah State Legislature public website. On House Day 38 (2008) Feb. 27, 2008, Rep. Harper presented HB 206 on the floor of the Utah House of Representatives. Rep. Harper references a “buff colored handout” that summarizes the 304 page bill; I did not view this handout as it was not available on the website <http://le.utah.gov/>. In presenting the bill Rep. Harper said:

**This bill . . . “allows businesses to track all their transactions and keep their records exactly as they are doing right now. So it is minimal or no impact on our businesses.”<sup>23</sup>**

It is possible that this legislative statement implies some type of legislative intent to codify existing practice, but it is also possible it was to allay concerns that the proposed legislation would place a new burden on businesses. While the 2008 legislation amended the bundled transaction language to include non-food items and added the reasonable and verifiable standard, it is not clear the purpose of the amendments was to codify prior legislative intent and make the 2008 law applicable to prior years. While there are conclusions that could be drawn when comparing specific words and phrases, none of the comparisons could be considered to be conclusive without documentation of legislative intent.

The Taxpayer also referenced two private letter rulings<sup>4</sup> (PLRs) issued by the Tax Commission -- PLR 02-020 (10/23/2002)<sup>5</sup> and PLR 09-009 (2/24/2009)<sup>6</sup>. Although PLR 02-020 was in effect during the audit periods the Taxpayer asks the Commission to consider the last paragraph in the PLR, which discusses per print charge repairs. The Taxpayer notes the PLR does not specifically say repair charges must be separately stated **on an invoice** (bold added). The last paragraph of PLR 02-020 reads:

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<sup>2</sup> <http://le.utah.gov/jsp/jdisplay/billaudio.jsp?sess=2008GS&bill=hb0206&Headers=true> Three minutes into recording as transcribed by Commissioner Dixon.

<sup>3</sup> As stated by Rep. Harper when presenting HB 206 the primary purpose of HB 206 was to bring Utah into compliance with the Streamline Sales Tax Agreement and to simplify tax reporting for businesses doing business inside and outside the State of Utah. Sen. Bramble in presenting in HB 206 (2008) on the Senate floor also said it was a bill to address the streamline sales tax and destination sourcing.

<sup>4</sup> A Private Letter Ruling is an informational statement of the Commission's interpretation of statute or administrative rules and their application to a particular set of facts or circumstances. A Private Letter Ruling typically addresses unusual or complex questions pertaining to a particular taxpayer. Routine tax questions are generally addressed by the correspondence group of the Taxpayer Services Division (from Tax Commission website).

<sup>5</sup> <http://tax.utah.gov/commission/ruling/02-020.html>

<sup>6</sup> <http://tax.utah.gov/commission/ruling/09-009.pdf>

“...If charges for toner or ink, which may be tax-exempt under the resale for component parts exemption, are imbedded in maintenance or repair charge, the entire charge is taxable. The charge for the nontaxable item must be **stated separately** (bold added); otherwise, it too is taxable.”

The Taxpayer then refers to PLR 09-009, specifically paragraph D on page eight. The paragraph speaks to the law on bundled transactions that went into effect January 1, 2009 and sites 59-12-103(2)(d), which contains the terms “reasonable and verifiable standards”. The paragraph includes the following:

“...If a transaction is bundled according to the current statutes and a seller has its underlying books and records in order, an otherwise nontaxable service may remain nontaxable even though it is both bundled with a taxable item and not separately stated.”

The Taxpayer proffers that in addressing the audit it met the requirements of PLR 09-009. The Taxpayer had service contracts with four companies in 2005, 2006 and 2007. For each machine serviced in each of those years, the Taxpayer identified the number of bottles of toner purchased under the service contract (for 2005 the Taxpayer estimated the number of bottles from the number of clicks on the digital printers). The Taxpayer determined that ( # ) bottles of toner were purchased at a cost of \$\$\$\$\$ during the audit period 2/1/05 through 12/31/07 and this amount should be deducted from the total taxable amount so that only \$\$\$\$\$ is carried to Part 1 Summary of Amount Subject to Tax.

As I understand the argument, the Taxpayer wants the Commission to find that because the 2008 law codified previous legislative intent, and PLR 09-009 is based on the 2008 law, and the Taxpayer can meet the requirements of paragraph D in PLR 09-009, then the toner should be exempt from sales tax. Because sales tax is an imposition tax that should be construed in favor of the taxpayer the legislative intent argument presented by the Taxpayer deserved further review. While I hold the material the Taxpayer provided shows the Taxpayer could identify by reasonable and verifiable standards from the books and records the seller keeps in the seller's regular course of business an amount of certain tangible personal property -- in this case toner -- that may not be subject to taxation, I cannot determine conclusively that the reasonable and verifiable standard can be applied to the appeal before the Commission.

D’Arcy Dixon Pignanelli  
Commissioner

Appeal No. 08-1657

**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.