

REQUEST LETTER

04-011

NAME
ADDRESS
PHONE
FAX

Dear Commissioner:

Enclosed find an excised portion of a letter from NAME, TITLE, 1ST COMPANY) for your review.

In his letter, NAME claims a sales tax exemption on equipment installed by a private contractor (2ND COMPANY”) on their CITY, Utah power plant.

I request the commission research the basis of this exemption and determine if 1ST COMPANY is exempt from sales tax on equipment purchased and installed in their facility.

This equipment would include such things as gas turbines, condensers, cooling towers, steam generators etc. The plant is projected to cost \$\$\$\$\$\$.

I would appreciate the benefit of your research in a private letter.

Thank you.

Sincerely,
NAME

*** EXCERPTS FROM NAME LETTER ***

3. Please state whether 1ST COMPANY has a sales tax exemption on equipment installed by 2ND COMPANY in the CITY Plant.

Yes, 1ST COMPANY is a Utah energy services interlocal entity organization under the Utah Interlocal Act. Utah Code Ann. §§ 11-13-101 *et seq.* As an energy services interlocal entity, 1ST COMPANY is exempt from payment of sales tax on its purchases of tangible personal property. See *id* § 59-12-104. The Interlocal Act defines “project” as an “electric generation and transmission facility owned by a Utah interlocal entity or an electric interlocal entity.” *Id.* § 11-13-103(10). Facilities owned by an energy services interlocal entity, are not addressed by the Utah Code. As defined by the Utah Code, facilities owned by an energy services interlocal entity do not constitute a project Under

Section 11-13-103 and, as a result, sales of tangible personal property to an energy services interlocal entity are generally not subject to sales and use tax.

Moreover, the Utah State Tax Commission has issued 1ST COMPANY a sales tax exemption certificate, which 1ST COMPANY has been relying on for the last several weeks.

RESPONSE LETTER

May 5, 2004

NAME
ADDRESS

RE: Private Letter Ruling Request – Sales and Use Tax Exemption for 1ST COMPANY

Dear NAME,

You have requested the Commission research sales and use tax issues relating to the 1ST COMPANY. We understand that 1ST COMPANY is an “energy services interlocal entity” that is organized under the Utah Interlocal Cooperation Act (“Interlocal Act”) and that it is building a power plant in Utah. Specifically, you ask whether 1ST COMPANY is exempt from Utah sales and use tax on its purchases of equipment, such as gas turbines, condensers, cooling towers, steam generators, etc., that will be installed by a private contractor in the plant. Before addressing the specific sales tax exemptions that may apply to 1ST COMPANY, we must first address determine certain issues that relate to recent changes in the Interlocal Act.

I. Political Subdivision. In 2002, the Legislature amended the Interlocal Act (§§ 11-13-101 *et seq.*) in S.B. 29 to allow for the creation of three different types of “interlocal entities” instead of the one type authorized prior to amendment. Utah Code Ann. §11-13-203(1) provides that an “interlocal entity” created under this section is a political subdivision of the state, with subsection 203(2) providing for the creation of a “Utah interlocal entity,” subsection 203(3) for an “electric interlocal entity,” and subsection 203(4) for an “energy services interlocal entity.” NAME has stated in the excerpts of his letter that you provided that 1ST COMPANY is an energy services interlocal entity. Assuming this assertion to be correct, Section 11-13-203(1) provides that 1ST COMPANY would therefore be a political subdivision of the State of Utah. We note that should this assumption be incorrect, our determination for regarding exemptions would be different.

II. Sales Tax Exemption for Political Subdivisions: S.B. 29 also amended Section 59-12-104(2), which provides that the following sales are exempt, with certain exceptions, from taxation (new language is underlined):

(2) sales to the state, its institutions, and its political subdivisions; however, this exemption does not apply to sales of:

- (a) construction materials except:
 - (i) construction materials purchased by or on behalf of institutions of the public education system as defined in Utah Constitution [Article X, Section 2](#), provided the construction materials are clearly identified and segregated and installed or converted to real property which is owned by institutions of the public education system; and
 - (ii) construction materials purchased by the state, its institutions, or its political subdivisions which are installed or converted to real property by employees of the state, its institutions, or its political subdivisions; or
- (b) tangible personal property in connection with the construction, operation, maintenance, repair, or replacement of a project, as defined in [Section 11-13-103](#), or facilities providing additional project capacity, as defined in [Section 11-13-103](#);

Prior to the 2002 amendments provided in S.B. 29, entities created under the Interlocal Act, as political subdivisions, received the same sales and use exemption as the State of Utah and its other political institutions (except for certain educational institutions). Under that exemption, all sales of tangible personal property to an entity created under the Interlocal Act were exempt except for “construction materials” that were not converted into real property by the entities’ own employees.

However, S.B. 29 then added an additional exception to the political subdivision sales tax exemption found in Section 59-12-104(2). The new exception applies to purchases of tangible personal property in connection with a “project” or “facilities providing additional project capacity,” as defined in the amended Interlocal Act. Accordingly, we must first determine whether 1ST COMPANY’ power plant is considered either a “project” or “facilities providing additional project capacity” before we can determine the extent of 1ST COMPANY sales and use tax exemption under the amended law.

Definition of “project” and “facilities providing additional project capacity.” The specific sales tax exemption applicable to 1ST COMPANY depends on whether 1ST COMPANY is considered a “project entity” and its facilities considered a “project” under the amended Interlocal Act.

Prior to S.B. 29, “project entity” was defined to mean “a legal or administrative entity created under this chapter which owns a project . . .” (Section 11-13-3(7).) “Project” was defined to mean “an electric generating and transmission project owned by a legal or administrative entity created under this chapter . . .” (Section 11-13-3(6).) S.B. 29 amended “project entity” to mean “a Utah interlocal entity or an electric interlocal entity that owns a project.” (Section 11-13-103(11).) “Project” was amended to mean “an electric generation and transmission facility owned by a Utah interlocal entity or an electric interlocal entity” and includes “a project entity’s ownership interest in . . . facilities that provide additional project capacity. . . .” (Section 11-13-103(10).)

Presently, the definitions of “project entity” and “project” specifically refer to and include facilities owned by only two of the three types of entities created under S.B. 29: 1) a Utah interlocal entity; 2) and an electric interlocal entity. These definitions, however, are silent with respect to ownership of a facility by the third type, an energy services interlocal entity. This is the type of

entity NAME represents to be 1ST COMPANY designation. Because the Legislature specifically designated the other two types of interlocal entities as “project entities” but did not include an energy services interlocal entity in the definition, we believe that the Legislature intended an energy services interlocal entity **not** to be a “project entity” and, accordingly, its facilities **not** to be a “project” or “facilities that provide additional project capacity.”

IV. Sales and Use Tax Exemption Applicable to 1ST COMPANY. The Legislature has provided certain exceptions to the exemption for sales of tangible personal property to a political subdivision of the State of Utah. The new exception from the sales tax exemption provided in Section 59-12-104(2)(b) only applies to certain transactions relating to “projects” and “facilities providing additional project capacity.” Because S.B. 29 does not lead us to consider 1ST COMPANY’ facilities to be a “project” or “facilities providing additional project capacity,” we do not find the new exception to the sales tax exemption to apply to purchases made by 1ST COMPANY.

Consequently, 1ST COMPANY is still subject to the same general exceptions as the State of Utah and most of its other political subdivisions. Therefore, 1ST COMPANY is exempt on its purchases of tangible personal property except for, in accordance with Section 59-12-104(2)(a)(ii), “construction materials” that are not converted to real property by COMPANY’ own employees. (As COMPANY is building a new power plant and has hired a private contractor to build it, COMPANY is not exempt on its purchases of “construction materials” that become part of the realty for sales and use tax purposes.)

However, you have asked specifically whether certain equipment, such as gas turbines, condensers, cooling towers, and steam generators, are exempt. Any exemption for these items depends on whether they are considered “construction materials” and whether they are converted to real property by other than COMPANY own employees. The definition of “construction materials,” as found in Section 59-12-102, was unchanged by S.B. 29 and means “any tangible personal property that will be converted into real property.” (We note that this definition has not been affected by the enactment of the Streamlined Sales Tax provisions that become effective July 1, 2004). Under current practice, the Commission considers “construction materials” to include materials and items that go into the construction of a building or structure, as well as equipment that serves the function of that building or structure. COMPANY may not purchase construction materials tax-free, however, if they are converted into real property by a private contractor. That is, tangible personal property incorporated into the buildings and structures at COMPANY power plant, as well as the equipment that becomes part of the realty and serves the function of the buildings and structures (such as HVAC systems), are taxable if they are constructed or installed by a private contractor and rather than COMPANY own employees.

The Commission, however, does not consider items, including equipment, that serve the business or production process located in the building or structure to be “construction materials.” Furthermore, the Commission considers equipment, which is installed in a power plant as part of the power generating process, to remain personal property after its installation. Accordingly, equipment, including gas turbines, condensers, cooling towers, and steam generators, installed to serve COMPANY power generating process, remain tangible personal property for sales and use tax

purposes after their installation. Therefore, COMPANY may purchase these items of equipment used in the power generating process tax-free, even if they are installed by a private contractor.

Before concluding, we should clarify a statement made in the excerpt from NAME letter. NAME indicated that “the Utah State Tax Commission has issued 1ST COMPANY a sales tax exemption certificate, which 1ST COMPANY has been relying on” An “exemption certificate” is a certificate issued by a purchaser to a seller, not something issued by the Tax Commission to a purchaser to facilitate claims of tax exemption. What the Tax Commission issues is a “license” or “sales tax account number.” Neither that license nor the account number should be viewed as granting some kind of broad or automatic sales tax exemption. The actual exemptions are still generally based on the status of the purchaser, the use or disposition of the property or service by the purchaser, and/or the actual type of property or service being purchased. It is not uncommon for a company having been issued a sale tax account number to wrongly believe that it has an exemption for everything it purchases.

Hopefully, the information in this letter will clarify which purchases 1ST COMPANY may make tax-free and which ones it cannot. Should you have any other questions, please contact us.

For the Commission,

Marc B. Johnson
Commissioner

MBJ/KC
04-011