

## REQUEST LETTER

06-001

NAME  
ADDRESS

Dear Sir,

In accordance with the provisions of Utah Admin Rule R861-1A-34, we request the Utah State Tax Commission confirm our understanding of the Utah sales and use tax exemption resulting from the business activities outlined below.

### FACTS:

COMPANY was formed as a joint venture of the NEWSPAPER 1 and the NEWSPAPER. COMPANY purchases paper, ink, and other materials and prints, sells, and distributes the NEWSPAPER 1 and NEWSPAPER 2. In addition to printing these papers, COMPANY currently is contracted to print the NEWSPAPER 3 and other commercial printing jobs for distribution to residents and businesses located in CITY.

COMPANY currently operates a printing facility located in the CITY. COMPANY has made the decision to expand this facility to increase printing capacity. This new facility will be located approximately 1.5 miles away from the old facility. A new building is being built with all new infrastructure being put into service at the new site. The new facility will have new presses, material handling equipment, as well as new piping and ink containers. COMPANY will purchase 3 new printing presses for the new facility.

There are a number of business reasons as to why COMPANY has decided to replace the existing presses at the new facility rather than move the old presses to the new facility. The first is that the old presses can continue to run while the new presses are put into service. It is expected that the new presses and the old presses will run parallel for approximately 3 months while the staff gets trained on the new presses and so all of the tests can be run. The new presses will produce approximately 66% more copies of the papers than the old presses were able to print. This will allow COMPANY to see more contract printing jobs similar to the contract that is in place with NEWSPAPER 3. Additionally, the old presses were outdated technology. When a part broke on one of the old presses, COMPANY had to have a new part made by a machine shop in order to replace the part. If an electrical item were to break, COMPANY would have to spend considerable time and money in having an electrician rewire existing circuit boards. The new presses also reduce the amount of inputs that go into the papers that are printed. This reduction allows for COMPANY to operate at a higher profitability than it did previously.

Finally, the new presses will allow for COMPANY to produce three times as many color pages as the old presses. This allows for COMPANY to offer a broader range of advertising to its customers.

In addition to the new presses, the new facility will have extensive racking and material handling equipment that was not present at the other facility. This new racking and material handling equipment will allow for COMPANY to offer new services to its customers, whereby they will be able to target specific neighborhoods for targeting advertising. These new services will be a new revenue stream for COMPANY.

### ISSUES:

1. Are the purchase of the new presses by COMPANY exempt from Utah sales and use tax under the manufacturing exemption offered by the state of Utah?
2. Is the purchase of piping and other devices essential to the presses and other equipment exempt from Utah sales and use tax under the manufacturing exemption?

### CONCLUSIONS:

1. COMPANY'S purchase of new presses should be exempt from Utah sales and use tax under the

manufacturing exemption.

2. COMPANY'S purchase of piping and other devices essential to the manufacturing equipment should be exempt from Utah sales and use tax under the manufacturing exemption.

DISCUSSION:

### Issue 1

Utah Code Ann §59-12-104(14) states the following sales and uses are exempt from the taxes imposed by this chapter:

- 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;
  - 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;
- b. the rates for the exemption under Subsection (14)(a)(ii) are as follows:
  - i. beginning July 1, 1996, through June 30, 1997, 30% of the sale or lease described in Subsection (14)(a)(ii) is exempt;
  - ii. beginning July 1, 1997, through June 30, 1998, 60% of the sale or lease described in Subsection (14)(a)(ii) is exempt; and
  - iii. **beginning July 1, 1998, 100% of the sale or lease described in Subsection (14)(a)(ii) is exempt.** [Emphasis added.]

Utah Admin. R. R865-19S-85(A)(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. [Emphasis added].

Utah Admin. R. R965-19S-85(A)(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 efficiently 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. [Emphasis added.]

The new presses purchased by COMPANY for the new plant meets the definition of “normal operating replacements” as defined in Utah Code Ann. §59-12-104(14)(a)(ii) because of the new presses have an economic life of three or more years, the new presses are used in the manufacturing process in a Utah manufacturing facility, the new presses are replacing existing equipment, and the purchases of the new presses do not include repairs and maintenance. The new presses purchased by COMPANY will take about 3 months to install and will replace the old presses within 12 months from the purchase date of the new presses as required by Utah Admin. R. R865-19S-85(A)(5).

Since the new presses purchased by COMPANY are used from the initial stage of the manufacturing process through the completion of the final product that is sold as tangible personal property, the new presses, including the new material handling and racking equipment, qualify as “machinery and equipment” as defined in Utah Admin. R. R865-19S-85(A)(2).

The Supreme Court of Utah upheld the Utah State Tax Commission’s (“Commission”) determination that Holnam, Inc’s (Holnam”) manufacturing equipment purchases were for a new or expanding operation and not for normal operating replacements because the machinery and equipment was not purchased in the ordinary course of business and Holnam’s primary purpose was not to modernize or update the old plant but to increase production or capacity. *Morgan County v Holnam, Inc. and Utah State Tax Comm’n*, 2001 UT 57 29 P3d 629, 07/02/2001 (Utah). The result of Holnam’s new plant was the doubling of its capacity from 350,000 tons of cement per year to 700,000 tons per year. The commission distinguished machinery and equipment purchased for “a new or expanding operation” from “normal operation replacements” to determine that Holnam’s purchases were for a new or expanding operation. The Commission determined and the Supreme Court of Utah upheld that the purchase of qualified manufacturing machinery and equipment qualify as “normal operating replacements” pursuant to Utah Code Ann. §59-12-104 when the purchases are made in the ordinary course of business and the primary purpose of a constructing a new manufacturing plant is to modernize or update the plant. *Id.*

Holnam was audited by the Commission and assessed sales tax deficiencies for failure to pay sales tax on the purchase of manufacturing equipment for its new cement manufacturing plant. When Holnam petitioned the Commission for re-determination, the Commission determined that the machinery and equipment Holnam purchased for the new manufacturing plant qualified for the manufacturing equipment exemption from sales tax as equipment used in “new or expanding operations” rather than as “normal operating replacements” that qualified for only a partial exemption pursuant to Utah Code Ann. §59-12-104. After July 1, 1998, the exemption for normal operating replacements became 100% pursuant to Utah Code Ann. §59-12-104(b). Subsequently, Morgan county, as intervenor, sought review by the Supreme Court of Utah of the Commission’s determination regarding Holman. The Supreme Court of Utah upheld the Commission’s determination. *Id.*

COMPANY’S primary purpose in constructing the new plant is to modernize and update the old plant by replacing the old presses with new presses. The old presses are out of date, thus making it difficult to obtain repair parts for these old presses. The new presses will be of familiar nature as the old presses, even though the new presses are expected to improve efficiency and increase production. Thus, the new presses purchased by COMPANY for use in its Utah printing facility should qualify as normal operating replacements and thus be exempt from Utah sales and use tax pursuant to Utah Code Ann. §59-12-104(14)(a).

## Issue 2

The definition of “Machinery and equipment” for purposes of qualifying for the Utah sales and use tax exemption for “normal operating replacements” includes “any accessory that is essential to a continuous manufacturing process.” Utah Admin R. R865-19S-85(A)(2)(b)(ii). These accessories include devices whose only function is to

control the operation of machinery and equipment used in the manufacturing process and supply lines whose primary use is for the operation of the manufacturing equipment. *Id.*

Supply lines that serve the general needs of the property where the manufacturing facility is housed will generally be viewed as real property. Utah information Publication No. 42, 04/01/2002. However, manufacturing equipment and machinery and essential accessories appurtenant to the manufacturing equipment remain tangible personal property even when attached to real property pursuant to Utah Admin. R. R865-19S-58(D).

The Utah Tax Commission stated that electrical components that are installed on a separate line that are used only to operate the manufacturing equipment will be deemed "machinery and equipment" for the purposes of the manufacturing exemption pursuant to Utah Code Ann. §59-12-104(a)(ii) Utah Advisory Opinion No. 99-13, 06/09/1999.

COMPANY will be installing new piping supply lines and other devices solely for the operation of the manufacturing equipment. These new piping supply lines and devices meet the requirements in Utah Code Ann §59-12-104(14)(a)(ii) for "normal operating replacements" because the piping and devices have an economic life of three or more years, the piping and devices are used in the manufacturing process in a Utah manufacturing facility, the piping and devices are used to replace or adapt an existing machine to extend the useful life of the machine, and the purchases do not include repairs and maintenance.

Thus, the new piping supply lines and devices installed by COMPANY for the sole purpose of the operation of the manufacturing equipment should qualify as "machinery and equipment" pursuant to Utah Admin. R. 865-19S-85(A)(2)(b)(ii) and should qualify for the manufacturing exemption from Utah sales and use tax as a normal operating replacements per Utah Code Ann. §59-12-104(a)(ii).

Please consider the above facts and our related conclusions, and provide a written response detailing your confirmation or any exceptions to these conclusions. If you require additional information or would like to discuss this request further, please call me at PHONE. Thank you in advance for your consideration.

Sincerely yours

NAME  
ADDRESS

## **RESPONSE LETTER**

January 17, 2007

NAME  
ADDRESS

Re: Private Letter Ruling 06-001  
Utah Sales Tax Applicability to Printing Presses and Related Equipment

Dear NAME,

This is in response to your letter in which you requested an Advisory Opinion regarding the COMPANY purchase of printing presses. You have asked whether the presses themselves are subject to Utah sales or use tax. You have asked the same question regarding ink piping, ink containers, and automated racking devices used to support the presses.

As explained in your letter, COMPANY plans an expansion to increase and modernize its printing facilities. It is building a new facility to accomplish this. This modernization has been ongoing throughout the summer of 2006. You provided four main reasons indicating why COMPANY made the decision to build the new facility rather than update its existing facility. First, by building a new facility while the old one is still operational, NAME will be in a position to fully install and test the new presses and train its staff regarding the use of the new equipment in a way that minimizes any effect on NAME current production. Your letter intimated and you confirmed by phone that NAME will likely sell or scrap the old equipment after determining that the new equipment is fully functional. Second, the new equipment is faster and better than the old presses. Third, the new equipment solves obsolescence problems because replacement parts are more readily available for the new presses. Fourth, the new presses have an increased capacity for color printing and will thus increase the types of printed material that NAME can produce.

New infrastructure will accompany the new printing presses. This includes new piping, ink containers, racks, and sorting equipment. You provided additional information by telephone regarding the high degree of automation of the racks and sorting equipment. This includes the automatic counting, collating, and sorting of advertising inserts by zip code. This enables NAME to send a store's advertising materials only to the areas near a single store or multiple locations of a given chain of stores. With regard to the integration of the racking equipment into the manufacturing process, you indicated by telephone that the racks are attached to the press equipment and that the NAME does not sell unsorted printed materials. Rather, the printed materials go directly from printing to sorting without being touched by NAME personnel. While it would be possible for someone to go to the press and pull a printed item from the press before sorting, NAME does not have a market for unsorted printing and thus does not consider its manufacturing process complete until it is sorted.

Producing newspapers and related materials are manufacturing processes under SIC classification 2711 and related codes. On the basis of the information you have provided, the presses themselves will be exempt from sales and use tax under exemptions for equipment for new, expanded, or continuing manufacturing operations. This is true under both versions of the statute applicable to this work. The current exemption statute for manufacturing equipment, Utah Code Section 59-12-104(14), became effective July 1, 2006 and provides an exemption for:

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 other than 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.

For purchases pre-dating July 1, 2006, the older version of this statute would be applicable. That version of the exemption statute provides that the following are exempt:

- c. 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;
  - ii. subject to the provisions of Subsection (14)(b), normal operating replacements that:

- e. have an economic life of three or more years;
  - f. are used in the manufacturing process in a manufacturing facility in the state;
  - g. are used to replace or adapt an existing machine to extend the normal estimated useful life of the machine; and
  - h. do not include repairs and maintenance;
- d. the rates for the exemption under Subsection (14)(a)(ii) are as follows:
- i. beginning July 1, 1996, through June 30, 1997, 30% of the sale or lease described in Subsection (14)(a)(ii) is exempt;
  - ii. beginning July 1, 1997, through June 30, 1998, 60% of the sale or lease described in Subsection (14)(a)(ii) is exempt; and
  - iii. beginning July 1, 1998, 100% of the sale or lease described in Subsection (14)(a)(ii) is exempt.

Under both versions of this statute, new printing presses for manufacturing printed materials are exempt. Under the current version of the statute, the new presses would qualify as “machinery and equipment” used in a manufacturing facility “to manufacture an item sold as tangible personal property” and would “have an economic life of three or more years” and would therefore come under this exemption. Although the earlier statute made a distinction between equipment for “new and expanding operations” and “normal operating replacements,” the printing presses would be exempt regardless of their characterization as new equipment or operating replacements.

You have also asked about sales or use tax that may be applicable to racking equipment, as well as piping and ink containers used to support the printing presses that NAME will be installing. These will likewise be exempt from sales and use tax. For purposes of the exemption of machinery and equipment as described in Utah Code Section 59-12-104(14), the Commission agrees with your analysis that Utah Admin. Rule R865-19S-85(A)(2) defines machinery and equipment in a way that includes ink piping, containers, and automated equipment for racking and sorting. Under this rule, “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.

Under this rule, the ink containers and piping are part of “gas, water, electricity, or other similar supply lines installed for the operation of the manufacturing equipment” because their use, as you described, is dedicated to the printing equipment. The automated racking system comes under the definition of “automated material handling and storage devices” that are “part of the integrated continuous production cycle” of printing and sorting manufactured advertising materials. NAME sells sorted rather than unsorted materials and thus the equipment to do that sorting is included in the “final processing, finishing, or packaging” of items that are “sold as tangible personal property.”

Our analysis is based on the assumption that the facts as you have represented them are correct. Should the conditions or circumstances be other than as you have represented, our conclusions may differ. If you have any other questions, please contact us.

For the Commission,

Marc B. Johnson  
Commissioner

PLR 06-001