

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 03-05**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Application of the industrial machinery exemption to various items in the taxpayer's manufacturing facility.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time.

Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling, and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[THE TAXPAYER] manufactures [CERTAIN CONSUMER PRODUCTS] at its facility in [COUNTY], Tennessee. The taxpayer requests a ruling on whether certain items in the facility qualify as industrial machinery under Tenn. Code Ann. § 67-6-206(a) and therefore are exempt from sales and use tax.

For purposes of this ruling, it is assumed that the taxpayer qualifies as a manufacturer under Tenn. Code Ann. §§ 67-6-102(a)(13) and 67-6-206(a). In other words, it is assumed that the taxpayer is generally entitled to the industrial machinery exemption because more than fifty percent (50%) of its revenue at the location is derived from the fabrication or processing of tangible personal property for sale and consumption off the premises. See *Tennessee Farmers' Coop. v. State ex rel. Jackson*, 736 S.W.2d 87 (Tenn. 1987). This ruling, therefore, focuses on whether specific items described by the taxpayer otherwise meet the definition of industrial machinery.

The taxpayer has divided the items at issue into three exhibits.

EXHIBIT A

Exhibit A includes the portion of the fabrication process that forms [RAW MATERIAL INTO COMPONENT MATERIALS]. The primary components are the proprietary [COMPANY] [EQUIPMENT MANUFACTURED BY AN UNRELATED COMPANY], together weighing 1.7 million pounds.

This portion of the fabrication process [FORMS THE RAW MATERIAL INTO COMPONENT MATERIALS]. The [COMPONENT MATERIALS ARE THEN] ready for transport to subsequent machines that convert it into its final form.

Items at Issue:

1. [THE SPECIALIZED] Machine
 - a. [PART A] distributes and injects raw materials into the process [CONVERTING THEM INTO COMPONENT MATERIALS].
 - b. [PART B] receives raw materials from the [PART A AND STARTS THE PROCESS OF FORMING THE COMPONENT MATERIALS].
 - c. [PART C] transports the [COMPONENT MATERIALS TO ANOTHER SECTION OF THE MACHINE].
 - d. [PART D FURTHER ASSISTS THE CONVERSION OF RAW MATERIALS INTO COMPONENT MATERIALS].
 - e. The [SPECIFICATIONS OF THE COMPONENT MATERIALS ARE CONTROLLED THROUGH THE OPERATION OF PART E OF THE PROPRIETARY MACHINERY].
 - f. The system monitors and controls proper raw material content in the [PRODUCT].
 - g. [PART G IS ALSO PART OF THE SPECIFICATION PROCESS FOR THE COMPONENT MATERIALS DEPENDING UPON THE PRODUCT BEING PRODUCED].

2. [AS PART OF THE PROCESS DEPICTED ON EXHIBIT A, RAW MATERIALS ARE COMBINED BY PART A-2 EQUIPMENT FOR USE IN THE FABRICATION PROCESS].
3. [THESE PART A-3 PIECES OF EQUIPMENT FURTHER REFINE THE FORM OF THE COMPONENT MATERIALS CREATED FROM RAW MATERIALS].
4. The [PART A-4 MACHINERY IS DIRECTLY INVOLVED IN RAW MATERIAL PREPARATION AND, AFTER COMBINING WITH ANY RECYCLED MATERIALS,] transports the raw material through [actual processing].
5. [THIS PART A-5 PROPRIETARY PROCESS MACHINERY IS DEDICATED TO COMPLETING CERTAIN STAGES OF THE TRANSFORMATION OF RAW MATERIALS].
6. The process control instruments are devices throughout the process that measure critical [CONDITIONS].
7. The process control computer system is a highly specialized computer custom built to control this particular process.
8. The process electrical power distribution and drive system takes power from the TVA grid and distributes the power to motors that run the process.
9. [PARTS A-9 ARE ESSENTIAL TO THE FORMATION OF THE COMPONENT MATERIALS ULTIMATELY PRODUCED FROM RAW MATERIALS].
10. The feed systems are specialized mixing and feed systems.
11. The process drive motors are dedicated motors driving the entire process.
12. The motor control centers are circuit breakers for all process drive motors.
13. [PART A-13 MOVES COMPONENT MATERIALS INTO THE FINISHING PROCESS].
14. [PART A-14 IS LIKEWISE A CENTRAL PART OF THE MANUFACTURING PROCESS AND IS PART OF THE PROCESS CONVERTING THE COMPONENT MATERIALS INTO FINISHED PRODUCT].
15. [PART A-15 IS AN ENVIRONMENTAL CONTROL REQUIRED FOR SEPARATING AND REMOVING CERTAIN ELEMENTS AND MATERIALS FROM THE WASTER CREATED DURING THE MANUFACTURING PROCESS].
16. [PART A-16 IS YET ANOTHER PART OF THE WASTE REMOVAL SYSTEM].

17. [PARTS A-17 ARE PART OF THE SYSTEM TRANSPORTING RAW MATERIAL TO THE OTHER MACHINES INVOLVED IN THE PROCESS WHICH TRANSFORMS RAW MATERIAL INTO COMPONENT MATERIALS].

18. The cleaner filters large contaminants from the raw material.

19. [THIS PROCESS DISTRIBUTION AND EXHAUST SYSTEM CONTROLS CERTAIN PARTS OF THE MANUFACTURING PROCESS CRITICAL TO THE FORMATION OF COMPONENT MATERIALS].

20. [PART A-20 IS A MIXING TANK WHICH ALLOWS FOR COMBINING RELEVANT CHEMICALS AND OTHER RAW MATERIALS IN THE PROPORTIONS NECESSARY TO CREATE THE DESIRED COMPONENT MATERIALS].

21. [PARTS A-21 ARE USED TO RECYCLE WATER EXCESS RAW MATERIALS DURING THE MANUFACTURING PROCESS].

22. [PART A-22 IS A FILTRATION SYSTEM WHICH IS NECESSARY TO THE PROPER OPERATION OF THE MACHINERY DESCRIBED IN PARAGRAPHS 20 AND 21 ABOVE].

23. The process equipment pads and anchors are specialized mounts for high-speed process equipment and maintain the precision needed in the alignment of the equipment.

EXHIBIT B

Exhibit B includes the portion of the fabrication process that prepares the raw materials for forming. It also includes the process alignment track. Also, there is a machine track specifically designed to control machine alignment.

This portion of the fabrication process starts with raw material, which is transported to the [COUNTY] site. [THE RAW MATERIALS ARE THEN MIXED WITH ADDITIONAL PRODUCTS AND CHEMICALS AND THE MANUFACTURING PROCESS IS BEGUN].

The machine track is specifically designed to maintain necessary process alignment [AS REQUIRED BY ENGINEERING STUDIES]. The track design is specifically tuned to accommodate this process. Other processes will not function on this track.

Items at issue:

1. The equipment [IS USED] for processing raw material [INTO THE FINISHED PRODUCT].
2. The process system is a central system for loading.

3. The process lubrication system is a central system for machine lubrication.
4. [PARTS B-4 ARE USED TO INSURE THAT THE COMPONENT MATERIALS HAVE THE CORRECT SPECIFICATIONS FOR THE PRODUCT THEN BEING PRODUCED].
5. [PARTS B-5 ARE AN INTEGRAL PART OF THE SYSTEM THAT DELIVERS RAW MATERIALS IN THE FORM NEEDED FOR THE TAXPAYER'S PROCESS].
6. [].
7. [PART B-7 IS A SPECIALLY CONSTRUCTED COLLECTION AREA TO HOLD AND MAINTAIN REFINED RAW MATERIAL BEFORE ITS ENTRY INTO THE PROCESS FORMING THE COMPONENT MATERIALS].
8. [PARTS B-8 HELP MOVE RAW MATERIALS INTO THE MANUFACTURING PROCESS].
9. [PARTS B-9 CONNECT PREVIOUSLY DESCRIBED PORTIONS OF THE MACHINERY].
10. [LIKEWISE, THE MACHINERY DESCRIBED IN PART B-10 IS ALSO CENTRAL TO TRANSPORTING RAW MATERIAL AND FEEDING IT INTO THE MANUFACTURING PROCESS].
11. Process instruments are process control devices throughout the process that measure [CONDITIONS].
12. Process drive motors are dedicated motors driving the process elements.
13. [THE TAXPAYER'S SPECIALLY LINED CONTAINERS HOLD VARIOUS STAGES OF THE RAW MATERIALS DURING THE FABRICATION PROCESS].
14. The system is a receiver and process overflow and helps recycle and minimize product waste.
15. The machine track with bedrock supports is a specifically designed and constructed base for the machine. It is an integral part of the machine due to its weight and need for stability in order to function properly in the fabrication.
16. The process equipment pads and anchors are specialized mounts for high-speed process equipment. They are critical to the fabrication process in maintaining the precision needed in the alignment of the equipment.
17. The first level process mat is specially engineered and constructed component parts of actual machinery needed for proper function to allow the fabrication process to operate continuously.

EXHIBIT C

Exhibit C includes the portion of the fabrication process that [COMPLETES THE FORMATION] and unloads the finished [PRODUCT] to the next processing area. The primary components are [SPECIALIZED EQUIPMENT]. There are also two process cranes with their necessary load bearing members.

[AS PART OF THIS PORTION OF THE FABRICATION PROCESS, ELEMENTS OF THE PROCESS NECESSARY TO COMPLETE TRANSFORMATION OF THE RAW MATERIALS INTO COMPONENT MATERIALS ARE MOVED INTO THE PROCESS THROUGH SPECIALIZED EQUIPMENT].

The cranes are necessary to install the [EQUIPMENT]. These must be changed frequently. The cranes also unload [FINISHED PRODUCT].

Items at issue:

1. The [SPECIALIZED EQUIPMENT CONSTRUCTED BY THE TAXPAYER IS AN ESSENTIAL PORTION OF THE FABRICATION PROCESS].
2. The process instruments are process control devices throughout the process that measure [CONDITIONS].
3. The crane is dedicated equipment to load and unload in the process.
4. The unloading crane is dedicated equipment to remove [FINISHED PRODUCT] from the process.
5. The alignment system is dedicated extra framing that sets and maintains alignment of the remainder of the taxpayer's proprietary system in the fabrication process.
6. The crane load bearing members are frames required in order for the cranes to function.

QUESTION

Which of the items enumerated in Exhibits A, B, and C are exempt from sales and use tax as industrial machinery under Tenn. Code Ann. § 67-6-206(a)?

RULING

Based on the information presented, all of the items enumerated in Exhibits A, B, and C qualify as industrial machinery, with the following exceptions:

1. Exhibit B, Item #13 – Only [A PORTION] of these [ITEMS] qualify as industrial machinery. The [OTHER PORTION] of each [ITEM] is actually the wall of the building and does not qualify for the exemption.

2. Exhibit C, Item #6 – The steel frames that support the crane are actually part of the outside walls, and possibly the roof, of the building. They do not qualify as industrial machinery. The cranes themselves and the track directly upon which they travel are industrial machinery.
3. Exhibit C, Item #5 – It is unclear whether the framing referred to in this item is part of the building itself. If it is part of the walls or roof of the building, it is not industrial machinery. Otherwise, it is.

ANALYSIS

Under Tenn. Code Ann. § 67-6-206(a), industrial machinery is exempt from sales and use tax. Industrial machinery is defined, in pertinent part, as:

(A) Machinery, apparatus and equipment with all associated parts, appurtenances and accessories, including hydraulic fluids, lubricating oils, and greases necessary for operation and maintenance, repair parts and any necessary repair or taxable installation labor therefore, which is necessary to, and primarily for, the fabrication or processing of tangible personal property for resale and consumption off the premises, or pollution control facilities primarily used for air pollution control or water pollution control, where the use of such machinery, equipment or facilities is by one who engages in such fabrication or processing as one's principal business....

(D) Such industrial machinery necessary to and primarily for the fabrication and processing of tangible personal property for resale or used primarily for the control of air or water pollution includes, but is not limited to:

(ii) Equipment used in transporting raw materials from storage to the manufacturing process, and transporting finished goods from the end of the manufacturing process to storage....

(F) Such industrial machinery necessary to and primarily for the fabrication or processing of tangible personal property for resale and consumption off the premises or used primarily for the control of air pollution or water pollution does not include machinery, apparatus and equipment used prior to or after equipment exempted by subdivision (a)(13)(D)(ii), and does not include equipment used for maintenance or the convenience or comfort of workers....

Tenn. Code Ann. § 67-6-102(a)(13).

This definition includes four basic requirements. First, the taxpayer must derive the majority of its revenues at the location from the fabrication or processing of tangible personal property for resale and consumption off of the premises (i.e. it must qualify as a manufacturer).¹ *Tennessee Farmers' Coop. v. State ex rel. Jackson*, 736 S.W.2d 87 (Tenn. 1987). Second, the item in question must be machinery, apparatus, or equipment. Third, the item must be necessary to the taxpayer's fabrication or processing of tangible personal property for sale and consumption off of the premises. Fourth, the item must be used primarily (more than 50% of the time) for such fabrication or processing.

In addition to these four basic requirements, the statute and case law establish various parameters in determining what qualifies as industrial machinery. These parameters include, but are not limited to, the following.

A building, even if it serves a special function, is not machinery, apparatus, or equipment. *Tibbals Flooring Co. v. Olsen*, 698 S.W.2d 60 (Tenn. 1985); *Tibbals Flooring Co. v. Huddleston*, 891 S.W.2d 196 (Tenn. 1994). Therefore, a building cannot qualify as industrial machinery. *Id.* However, an item does not lose its identity as industrial machinery merely by its affixation to real property during installation. *Hoyer-Schlesinger-Turner, Inc. v. Benson*, 479 S.W.2d 223, 224 (Tenn. 1972). Therefore, an item permanently attached to a building or other realty can be industrial machinery if the item otherwise constitutes machinery, apparatus, or equipment.

Industrial machinery includes equipment used in transporting raw materials from storage to the manufacturing process and equipment used in transporting finished goods from the end of the manufacturing process to storage. Tenn. Code Ann. § 67-6-102(a)(13)(D)(ii). However, it excludes machinery, apparatus and equipment used prior to or after the equipment described in the preceding sentence. Tenn. Code Ann. § 67-6-102(a)(13)(F); *Nuclear Fuel Services, Inc. v. Huddleston*, 920 S.W.2d 659 (Tenn. Ct. App. 1995). Items, including tanks, used primarily to store raw materials before fabrication or processing begins are not industrial machinery. *Woods v. General Oils, Inc.*, 558 S.W.2d 433, 436 (Tenn. 1977). Industrial machinery also excludes equipment used for maintenance or for the convenience or comfort of workers. Tenn. Code Ann. § 67-6-102(a)(13)(F).

Applying the statute and case law to the descriptions provided by the taxpayer, the [OTHER PORTION] of the [ITEMS] described in Exhibit B, Item #13, and the steel frames that support the cranes in Exhibit C, Item #6, do not qualify as industrial machinery because they are part of the actual building. They are not simply attached to the building upon installation. Instead, they are the walls and possibly part of the roof. As noted above, a building is not machinery, apparatus, or equipment. In contrast, the equipment pads (Exhibit A, Item #23; Exhibit B, Item #16) and the machine track (Exhibit B, Item #15) do not appear to be a part of the building.² They are industrial

¹ As previously noted, it is assumed for purposes of this ruling that the taxpayer meets this requirement.

² The taxpayer has stated that the equipment pads rest on top of the building floor.

machinery. As discussed in the “Ruling” section above, it is unclear whether the framing described in Exhibit C, Item #5, makes up part of the building. If so, then it would be taxable.

Based on the facts provided, all of the other items listed in Exhibits A, B, and C are exempt as industrial machinery. The taxpayer has stated that each of these items is necessary to and used primarily for its fabrication process. Moreover, the facts do not indicate that the items are otherwise excluded from the definition of industrial machinery.

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APPROVED: Loren L. Chumley
Commissioner of Revenue

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