

**TENNESSEE DEPARTMENT OF REVENUE
REVENUE RULING # 12-02**

WARNING

Revenue rulings are not binding on the Department. This ruling is based on the particular facts and circumstances presented, and is an interpretation of the law at a specific point in time. The law may have changed since this ruling was issued, possibly rendering it obsolete. The presentation of this ruling in a redacted form is provided solely for informational purposes, and is not intended as a statement of Departmental policy. Taxpayers should consult with a tax professional before relying on any aspect of this ruling.

SUBJECT

The applicability of the Tennessee sales and use tax industrial machinery exemption in a [REDACTED] manufacturing facility.

SCOPE

Revenue Rulings are statements regarding the substantive application of law and statements of procedure that affect the rights and duties of taxpayers and other members of the public. Revenue Rulings are advisory in nature and are not binding on the Department.

FACTS

Since [YEAR], the Taxpayer has operated an industrial facility in [REDACTED], Tennessee (the “Facility”). The Facility, used for manufacturing, [REDACTED]. [REDACTED]. The Facility is a shell that encompasses the industrial machinery, equipment, appurtenances, and other items referenced below, [REDACTED].

In general, the operations and activities at the manufacturing plant consist of the procurement of [TYPE OF] materials ([REDACTED], etc.) and the transformation of these materials by the industrial machinery and appurtenances into [PRODUCTS]. Industrial machinery in this phase of production is located in the “[PHASE A] Manufacturing” area of the manufacturing facility. Once the [PRODUCTS] are produced, the machinery and appurtenances transform the [PRODUCTS] into [OTHER PRODUCTS], which are subsequently packaged for delivery. Industrial machinery in this phase of the production is located in the “[PHASE B] Area” of the manufacturing facility. [REDACTED].

[REDACTED], the Taxpayer requests guidance on the sales and use tax implications of the items referenced in the three categories detailed below. These items are purchased and installed by the Taxpayer’s contractors.

A description of each particular item or service is set forth in Appendix A.

RULINGS

- A) Are the items that will be purchased [REDACTED] (and listed in the table below) exempt from the Tennessee sales and use tax?

Ruling: All of the items listed below will be exempt from Tennessee sales and use tax except the floor coating, the exterior wall siding, safety showers, piping labels, fire stop, and lighting fixtures.

- B) Will the Taxpayer’s contractors’ purchases of these same items be exempt from the Tennessee sales and use tax?

Ruling: A contractor may not use the Taxpayer’s industrial machinery authorization to make exempt purchases. However, a contractor may apply for its own industrial machinery exemption authorization number for the Taxpayer’s project, and may make exempt purchases with that authorization number.

ANALYSIS

A) *Taxability of Purchases*

The following chart lists items or services purchased for the expansion of the Taxpayer’s facility, states whether the service or item is exempt, and gives a numerical explanation as to the item’s or service’s taxability. A description of each explanation is given below the chart.

Item / Service	Exempt When Purchased by Taxpayer?	Explanation
[REDACTED]	Yes	1
Process Tanks	Yes	1
Freight Elevator	Yes	1, 4
Electrical Distribution Equipment	Yes	1, 3
Special Coatings	Yes	1, 2
Floor Coating	No	8
Exterior Wall Siding	No	8
Chillers	Yes	1, 2
[REDACTED]	Yes	1
MUA Units	Yes	1, 2
[REDACTED]	Yes	1
Safety Showers	No	8
Air Receiver	Yes	1, 2

Item / Service	Exempt When Purchased by Taxpayer?	Explanation
Filters	Yes	1, 2
Heat Exchangers	Yes	1, 2
[REDACTED]	Yes	1, 2
[REDACTED]	Yes	1
Pumps	Yes	1
Variable Speed Drive Machinery	Yes	1, 2
Standpipe	Yes	1
Vacuum Strainers	Yes	1
Dust Collection Machinery	Yes	1, 2
[REDACTED]	Yes	1
Medium Voltage Motors	Yes	1, 2
Primary Unit Substation	Yes	1, 3
Secondary Unit Power Substation	Yes	1, 3
Low Voltage Motors	Yes	1, 2
Instruments and Controls – [PHASE A] Area	Yes	1, 2
Bollards/Wheel Stops	Yes	1, 2
Inserts	Yes	1, 2
Large & Small Diameter Piping	Yes	1
Instrumental Panels	Yes	1, 2
Bolts and Gaskets	Yes	1, 2
Piping Labels	No	8
Expansion Joints and Equipment Hoses	Yes	1, 2
Mechanical Base Plates	Yes	1, 2
Wires and Cables	Yes	1, 2, 3
Fire Stop	No	8
Heat Tracing	No	8
Lighting Fixtures	No	8
Devices and Plates	Yes	1, 2
Communication Monitoring Equipment	Yes	1, 2

Item / Service	Exempt When Purchased by Taxpayer?	Explanation
Demolition Services	Yes	7
Excavation and Backfill Services	Yes	7
Heavy Haul Services	Yes	7
Nelson Stud Installation	Yes	5, 6
Optical Alignment Services	Yes	7
NDE Testing	Yes	7
Engineering Services	Yes	7

1) Industrial Machinery

Under the Retailers' Sales Tax Act, TENN. CODE ANN. § 67-6-101 *et seq.*, the retail sale of tangible personal property is generally subject to the Tennessee sales and use tax.¹ However, TENN. CODE ANN. § 67-6-206(a) (2011) exempts “industrial machinery” from the sales and use tax, providing that “[a]fter June 30, 1983, no tax is due with respect to industrial machinery.”²

TENN. CODE ANN. § 67-6-102(46)(A)(i) (2011) defines “industrial machinery” in pertinent part as “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 therefor, that is necessary to, and primarily for, the fabrication or processing of tangible personal property for resale and consumption off the premises ... where the use of such machinery, equipment or facilities is by one who engages in such fabrication or processing as one’s principal business.”

¹ TENN. CODE ANN. § 67-6-102(78) (2011) defines a “retail sale” as any “sale, lease, or rental for any purpose other than for resale, sublease, or subrent.” The term “sale” is defined under the Tennessee sales and use tax laws in pertinent part as “any transfer of title or possession, or both, exchange, barter, lease or rental, conditional or otherwise, in any manner or by any means whatsoever of tangible personal property for a consideration.” TENN. CODE ANN. § 67-6-102(80)(A). Additionally, TENN. CODE ANN. § 67-6-102(91)(A) defines “tangible personal property” in pertinent part as “personal property that can be seen, weighed, measured, felt, or touched.”

² The burden is on the taxpayer to establish entitlement to an exemption from taxation. The Tennessee Supreme Court has stated that “[a]lthough the rule is well-established that taxing legislation should be liberally construed in favor of the taxpayer and strictly construed against the taxing authority, it is an equally important principle of Tennessee tax law that ‘exemptions from taxation are construed against the taxpayer who must shoulder the heavy and exacting burden of proving the exemption.’” *Am. Airlines, Inc. v. Johnson*, 56 S.W.3d 502, 506 (Tenn. Ct. App. 2000) (quoting *Rogers Group, Inc. v. Huddleston*, 900 S.W.2d 34, 36 (Tenn. Ct. App. 1995)). The Tennessee Supreme Court has also stated that the burden is on the taxpayer to establish the exemption, and any well-founded doubt is sufficient to defeat a claimed exemption from taxation. *Am. Airlines*, 56 S.W.3d at 506 (citing *Tibbals Flooring Co. v. Huddleston*, 891 S.W.2d 196, 198 (Tenn. 1994); *United Cannery, Inc. v. King*, 696 S.W.2d 525, 527 (Tenn. 1985)).

Therefore, in order for a purchase of tangible personal property to be exempt from the Tennessee sales and use tax as industrial machinery, four requirements must be met. First, the use must be by a manufacturer. Second, the tangible personal property must be machinery, apparatus or equipment. Third, the tangible personal property must be necessary to the fabrication or processing of the products sold by the manufacturer. Fourth, the tangible personal property must be primarily for the fabrication of the products sold by the manufacturer.

First, under the facts presented, the Taxpayer qualifies as a manufacturer. A manufacturer is defined under TENN. CODE ANN. § 67-6-102(46)(A)(i) as “one who engages in [the] fabrication or processing [of tangible personal property for resale and consumption off the premises] as one’s principal business.” Manufacturing is a taxpayer’s principal business if more than fifty percent of its revenues at a given location are derived from fabricating or processing tangible personal property for resale. *Tenn. Farmers’ Coop. v. State ex rel. Jackson*, 736 S.W.2d 87, 91-92 (Tenn. 1987). The Taxpayer has indicated that its only business is operating a manufacturing facility, and [REDACTED]. The Taxpayer is therefore a manufacturer that may be entitled to the exemption provided in TENN. CODE ANN. § 67-6-206(a).

Second, each item listed above with only a (1) in the explanation column qualifies as machinery, apparatus, or equipment. While several items, such as [REDACTED], clearly qualify as machinery or equipment, other items, such as the [REDACTED] and process tanks, must fall under the broader term “apparatus.” Neither the Tennessee Code nor the Tennessee courts have defined the term “apparatus” for purposes of Tennessee sales and use taxation. The Tennessee Supreme Court has stated that when a statute does not define a term, it is proper to look to common usage to determine the term’s meaning. *See, e.g., Tenn. Farmers Assur. Co. v. Chumley*, 197 S.W.3d 767, 782-83 (Tenn. Ct. App. 2006); *Beare Co. v. Tenn. Dept. of Revenue*, 858 S.W.2d 906, 908 (Tenn. 1993). WEBSTER’S NINTH NEW COLLEGIATE DICTIONARY 96 (1991) defines the term “apparatus” as “a set of materials or equipment designed for a particular use” or “an instrument or appliance designed for a specific operation.”

Additionally, the Tennessee Supreme Court has interpreted the phrase “machinery, apparatus, and equipment” to include “the devices conveying the materials and components from one part of the manufacturing or fabricating process to another.” *Eastman Chemical Co. v. Johnson*, 151 S.W.3d 503, 509-510 (Tenn. 2004). This expanded definition would also include the large and small diameter piping, the pumps, and the standpipe as industrial machinery.

Third and fourth, each item listed above with only a (1) in the explanation column is necessary to and primarily for the production process. The terms “necessary” and “primarily” are also undefined by the Tennessee Code and the Tennessee courts for Tennessee sale and use tax purposes. The common definition of the term “necessary” is “that which cannot be dispensed with; essential; indispensable; ... inherent in the situation; unavoidable from the premises ... rendering some essential and intimate service.” WEBSTER’S NEW TWENTIETH CENTURY DICTIONARY (2nd ed. 1964). Thus, in order for machinery, equipment, or apparatus to be “necessary” to the manufacturing process, it must be essential to the manufacturing process as engaged in by a taxpayer.

The term “primarily” has been defined by the Tennessee Supreme Court for purposes of the industrial machinery exemption as “first of all; principally; or fundamentally” and as “first in

rank or importance, chief, principal, basic or fundamental.” *Woods v. General Oils, Inc*, 558 S.W.2d 433, 436 (Tenn. 1977). (citing WEBSTER’S THIRD NEW INTERNATIONAL DICTIONARY (1961); *Breen v. Indus. Acc. Bd.*, 436 P.2d 701 (Mont. 1968); *Twentieth Century Mfg. Co. v. United States*, 444 F.2d 1109 (Ct. Cl. 1971)). The machinery, equipment, or apparatus satisfies this test if more than fifty percent of its use is in the manufacturing operation.

2) Associated parts, appurtenances and accessories

“Industrial machinery” as defined in pertinent part by TENN. CODE ANN. § 67-6-102(46)(A)(i) includes “[m]achinery, apparatus and equipment *with all associated parts, appurtenances and accessories.*” (Emphasis added.) Therefore, items that are not necessarily machinery themselves, but become a part of or are added to qualifying machinery, are also exempt under the industrial machinery exemption.

Each of the items listed under this category are attached to or are a part of a larger, more integral piece of machinery, apparatus, or equipment that itself qualifies for the exemption.

3) Machines used to generate, produce, and distribute electricity

The term “industrial machinery” also includes “[m]achines used for generating, producing, and distributing utility services, electricity, steam, and treated or untreated water.” TENN. CODE ANN. § 67-6-102(46)(D)(i). The electrical distribution equipment and the two substations distribute electricity to the machinery and thus are exempt industrial machinery.

4) Transport of raw materials and finished product to and from the process

Equipment used to transport raw materials from storage to the manufacturing process and to transport the finished product to storage after completion of the manufacturing process is treated as industrial machinery pursuant to TENN. CODE ANN. § 67-6-102(46)(D)(ii).

Because the freight elevator is used solely for this purpose, it is exempt industrial machinery.

5) Repair and installation of industrial machinery

Generally, the repair or installation of tangible personal property is subject to the Tennessee sales and use tax. TENN. CODE ANN. § 67-6-205(c)(4)&(6) (2011). However, “industrial machinery” specifically includes “any necessary repair or taxable installation labor” of the machinery.

Thus, the Nelson stud installation services performed on the industrial machinery are exempt from the sales and use tax.

6) Installation to real property

The installation of tangible personal property that becomes part of real property is not subject to the Tennessee sales and use tax. TENN. COMP. R. & REG. 1320-5-1-.27(2) (1974).

Thus, any charges made for the Nelson stud installation that becomes part of real property will not be taxable. However, the contractor that performs Nelson stud installation that becomes part

of real property will owe sales and use tax on the property purchased or used in making the installation. TENN. COMP. R. & REG. 1320-5-1-.07(1) (2000).

7) Non-taxable service

Services are subject to the Tennessee sales and use tax only if they are enumerated under the Retailers' Sales Tax Act or are included as part of a taxable sale of tangible personal property or a service. The demolition, excavation and backfill, heavy haul, optical alignment, NDE testing, and engineering services each are purchased as services and not as part of a sale of tangible personal property or enumerated service. Further, none of these services are themselves enumerated by the statute. Thus, these services are not subject to the Tennessee sales and use tax.

8) Taxable purchases of tangible personal property

As stated under explanation (1), unless a specific exemption applies, the retail sale of tangible personal property is generally subject to the Tennessee sales and use tax. The floor coating, exterior wall siding, safety showers, piping labels, fire stop, and light fixtures, if purchased as tangible personal property, are not exempt from the Retailers' Sales Tax Act and thus are subject to the Tennessee sales and use tax.

Although each of these items will be used in the Taxpayer's manufacturing facility, they do not qualify as industrial machinery. In order to qualify as industrial machinery, an item must be machinery, apparatus, or equipment and must be necessary to and primarily for the manufacturing process. None of these items are necessary to or primarily for the process. While some of these items may relate to or assist in the manufacturing process, none are essential in the actual fabrication of the Taxpayer's product. Further, each of these items has a primary purpose beyond manufacturing.

B) Contractors' Purchases

The Taxpayer has also asked whether its contractors may purchase the qualified industrial machinery discussed above on a tax-exempt basis. While the contractors may not use the Taxpayer's industrial machinery authorization to make exempt purchases, they may apply for their own respective exemption authorization numbers, which will apply only to the Taxpayer's project.

TENN. CODE ANN. § 67-6-209(b) (2011) requires a contractor to pay Tennessee sales or use tax on purchases of tangible personal property used in the performance of a contract. This is because the contractor is the user and consumer of such tangible personal property. However, TENN. CODE ANN. § 67-6-206(a) (2011) provides that no tax is due on industrial machinery. The definition of "industrial machinery" includes all qualifying items that are used by a manufacturer. TENN. CODE ANN. § 67-6-102(46)(A)(i) (2011). Therefore, if an item qualifies for the industrial machinery exemption, the purchase of the item is exempt, regardless of who actually makes the purchase and installs the item. Further emphasizing this fact, TENN. CODE ANN. § 67-6-209(c) states that the contractor's use tax described above shall not apply if the contractor and the purchases made by the contractor would otherwise be exempt.

Thus, a contractor installing the qualified industrial machinery discussed above for the Taxpayer may apply to the Tennessee Department of Revenue for its own industrial machinery authorization number. Such an industrial machinery authorization number will enable the contractor to purchase the industrial machinery for the Taxpayer's facility exempt from the Tennessee sales and use tax.

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APPROVED: Richard H. Roberts
Commissioner of Revenue

DATE: 04/30/2012

APPENDIX A

ITEM	DESCRIPTION/FUNCTION
[REDACTED]	[REDACTED]
Process Tanks	Tanks used exclusively in the [PHASE A] area for channeling [MATERIALS] prior to distribution to different industrial machinery. They agitate and maintain a constant pressure on the [MATERIALS].
Freight Elevator	Transports raw materials from storage to manufacturing and finished goods to storage areas.
Electrical Distribution Equipment	Controls, monitors, and channels electric power to machinery located in the [PHASE A] and [PHASE B] areas.
Special Coating[REDACTED]	Utilized to maintain and repair industrial machinery in the [PHASE A] and [PHASE B] areas by preventing corrosion from accumulating on the machinery; enables optimal functions of the machinery. The coatings are applied to and cover the industrial machinery.
Floor Coating	Utilized on the floor in the [PHASE A] and [PHASE B] areas to prevent the accumulation of dust and other debris that can damage and interfere with the optimum utilization of industrial machinery.
Exterior Wall Siding	Serves as an external, structural support for machinery located in the interior of the [PHASE A] area.
Chillers	Located in the [PHASE A] area and connected to the [REDACTED – INDUSTRIAL MACHINERY]; maintain the proper temperature of the machinery by regulating and controlling the air and water temperature of the machinery.
[REDACTED]	[REDACTED].
MUA Units	Ensure the required temperature and humidity in the [PHASE A] area by regulating and filtering the air pumped into a [REDACTED – INDUSTRIAL MACHINERY]. They are a part of the HVAC system and are affixed to the [REDACTED – INDUSTRIAL MACHINERY].
[REDACTED]	[REDACTED].
Safety Showers	Located in the [PHASE A] and [PHASE B] areas to comply with federal, state and local laws.
Air Receiver	Utilized in the [PHASE A] and [PHASE B] areas to accumulate air necessary to insure the safe shut down of air actuated equipment in the event of power loss. They are attached to the [REDACTED – INDUSTRIAL MACHINERY].
Filters	Insure the purity of chemicals by eliminating and reducing the risk of accumulation of debris and impurities. They are a part of the chemical skids, which are industrial machinery used for chemical dosing.
Heat Exchangers	Facilitate the transfer of heat energy required for the channeling of raw materials in the [PHASE A] area. They are connected to and a part of the [REDACTED – INDUSTRIAL MACHINERY].
[REDACTED]	[REDACTED].

ITEM	DESCRIPTION/FUNCTION
[REDACTED]	[REDACTED].
Pumps	Used in the [PHASE A] and [PHASE B] areas to transport industrial fluids from one piece of machinery to another.
Variable Speed Drive Machinery	Electrical machinery that regulates the speed of motors that power machinery located in the [PHASE A] and [PHASE B] areas.
Standpipe	Pipe that functions as a buffer to control process flows between various pieces of machinery located in the [PHASE A] area.
Vacuum Strainers	Reduce and help eliminate contaminants that form in [REDACTED]; used in the [PHASE A] area.
Dust Collection Machinery	Attached to the industrial machines in the [PHASE A] area; reduces the accumulation of dust and debris that can damage and interfere with the optimum utilization of the machinery.
[REDACTED]	[REDACTED].
Medium Voltage Motors	Used exclusively to drive large process equipment located in the [PHASE A] area.
Primary Unit Power Substation	Located on the rear of the main industrial machines; used exclusively to distribute power to the individual motors driving the process equipment.
Secondary Unit Power Substation	Located on the rear of the main industrial machines; used exclusively to distribute power to the individual motors driving the process equipment.
Low Voltage Motors	Power and drive small process equipment located in the [PHASE A] area.
Instruments and Controls - [PHASE A] Area	Used to control equipment such as pumps and fans in the [PHASE A] area; located on the ground and machine floor levels.
Bollards/Wheel Stops	Prevent mobile equipment from damaging fixed equipment used in the manufacturing process. They are attached to the mobile industrial machinery such as the [REDACTED – INDUSTRIAL MACHINERY] via an anchoring mechanism to the floor.
Inserts	Adjustable steel components that allow the adjustment of mechanical equipment; required to accommodate manufacturing equipment installation. They are welded to the industrial machinery.
Large & Small Diameter Piping	Transports in-process fluids from one system to another; runs through the [REDACTED]; the bulk of the piping is located around the machine.
Instrument Panels	Located in the [PHASE A] and [PHASE B] areas; attached to and control equipment.
Bolts and Gaskets	Integral part of the piping system located throughout the facility.
Piping Labels	Glued to various parts of the piping to identify the types of fluids transported.
Expansion Joints and Equipment Hoses	Mechanical components that insure the flexibility of process piping systems; used within the [REDACTED – INDUSTRIAL MACHINERY]. They connect the large and small diameter piping to the industrial machinery.
Mechanical Base Plates	Located under the manufacturing equipment frame to insure proper alignment; directly used to support the [REDACTED – INDUSTRIAL

ITEM	DESCRIPTION/FUNCTION
	MACHINERY]. Bolted onto the [REDACTED – INDUSTRIAL MACHINERY] and act as a foundation to the machinery.
Wires and Cables	Located in the [PHASE A] and [PHASE B] areas; integral part of the functioning of the [REDACTED – INDUSTRIAL MACHINERY] and ensure power distribution and control signal communication. Attached to and provide connectivity to the industrial machinery.
Fire Stop	Sealing materials that prevents fire from spreading in openings made to allow cable passage; seals penetrations used for cabling; used on cables that are necessary to the functioning of the equipment.
Heat tracers	Tracers are heating cables that run along all piping outside of the building to prevent process fluids from freezing.
Lighting Fixtures	General lighting that allows clear eyesight of the manufacturing equipment; also generally necessary for the building.
Devices and Plates	Instruments that are used to directly support the [REDACTED – INDUSTRIAL MACHINERY]. Bolted onto the [REDACTED – INDUSTRIAL MACHINERY] and act as a foundation to the machinery.
Communication Monitoring Equipment	Transfers manufacturing data from one manufacturing system to another; integral part of the [REDACTED – INDUSTRIAL MACHINERY]. Provides an interactive platform to control, gauge, and monitor the industrial machinery.
Demolition Services	Service provided by contractor to improve real property.
Excavation and Backfill Services	Service provided by contractor to improve real property.
Heavy Haul Services	Transport of oversized, overweight, or similarly difficult loads in the improvement of real property.
Nelson Stud Installation	Labor charge relating to industrial machinery welding or real property contractor services.
Optical Alignment Services	Locating, reporting and issuing reports on precession and misalignment concerns relating to industrial machinery.
NDE Testing	Labor subcontract for the nondestructive testing of real property construction.
Engineering Services	Required in the construction of the manufacturing plant.