DEPARTMENT OF STATE REVENUE

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Letter of Findings Number: 04-20130070
Sales and Use Tax
For Tax Years 2009-2011

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ISSUES

I. Sales and Use Tax–Manufacturing Exemption.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-3-4; IC § 6-2.5-5-3; IC § 6-2.5-5-5.1; IC § 6-8.1-4-2; IC § 6-8.1-5-1; 45 IAC 2.2-5-8; 45 IAC 2.2-5-12; 45 IAC 15-3-2; Indiana Dep't of Revenue v. Miller Brewing Company, 975 N.E.2d 800 (Ind. 2012); Indiana Dep't of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520 (Ind. 1983); Indiana Dep't of Revenue v. Kimball Int'l Inc., 520 N.E.2d 454 (Ind. Ct. App. 1988); Mumma Bros. Drilling Co. v. Department of Revenue, 411 N.E.2d 676 (Ind. Ct. App. 1980); Indiana Dep't. of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96 (Ind. Ct. App. 1974); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Guardian Automotive Trim, Inc. v. Indiana Dep't of State Revenue, 811 N.E.2d 979 (Ind. Tax Ct. 2004); Graham Creek Farms v. Indiana Dep't of State Revenue, 819 N.E.2d 151 (Ind. Tax Ct. 2004); General Motors Corp. v. Indiana Dept. of State Revenue, 578 N.E.2d 399 (Ind. Tax Ct. 1991); Colonial Brick Corp. v. Dep't of State Revenue, 1998 Ind. Tax LEXIS 70 (Ind. Tax Ct. Jan. 14, 1998); Ind. R. App. P. 65(d); Letter of Findings 04-20060452 (August 13, 2007); Letter of Findings 04-20100634 (June 28, 2011).

Taxpayer protests the assessment of use tax on certain of its purchases.

II. Sales and Use Tax– Environmental Exemption.

Authority: IC § 6-2.5-3-2; IC § 6-2.5-5-30; IC § 6-8.1-5-1; Clean Air Act, 42 U.S.C. § 7401, et seq. (2007); 40 C.F.R. § 70.1, et seq. (2007); 40 CFR 63.1209.

Taxpayer protests the assessment of use tax on its purchase of a "cooling tower filter," "85 ppm propane nitrogen," and a spool assembly.

III. Sales and Use Tax–Imposition.

Authority: IC § 6-8.1-5-1; Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007).

Taxpayer argues that the Department incorrectly included a transaction from the 2008 tax year in the sample population.

IV. Sales and Use Tax–"Contractor Services."

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-3-4; IC § 6-8.1-5-1; 45 IAC 2.2-1-1; 45 IAC 2.2-3-7; 45 IAC 2.2-4-21; 45 IAC 2.2-4-22; Sales Tax Information Bulletin 60 (July 2006).

Taxpayer protests the imposition of use tax on its purchase of certain "contractor services."

STATEMENT OF FACTS

Taxpayer is a cement manufacturer in Indiana. Taxpayer has two manufacturing locations of which one uses a dry kiln process ("Dry Location") and the other uses a wet kiln process ("Wet Location"). These locations consist of quarries where stone is mined, delivered to the production areas, and through their kiln process is manufactured into cement. The Department conducted an audit review of Taxpayer's business records employing a statistical sampling methodology for Taxpayer's accounts payable expense purchases and a full review of Taxpayer's capital asset purchases for the 2009, 2010, and 2011 tax years. As a result of the audit, the Indiana Department of Revenue ("Department") determined that Taxpayer owed use tax for the 2009, 2010, and 2011 tax years. The Department found that Taxpayer had made a variety of purchases on which sales tax was not paid at the time of purchase nor was use tax remitted to the Department. Taxpayer protested the imposition of use tax related to certain of its capital asset and expense purchases. An administrative hearing was held, and this Letter of Findings results.

I. Sales and Use Tax–Manufacturing Exemption.

DISCUSSION

All tax assessments are prima facie evidence that the Department's claim for the tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A person who acquires property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b). Indiana also imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). In general, all purchases of tangible personal property are subject to sales and/or

use tax. An exemption from use tax is granted for transactions where sales tax was paid at the time of the purchase pursuant to IC § 6-2.5-3-4. In certain circumstances, additional enumerated exemptions from sales and/or use tax are available.

The Department found that Taxpayer purchased machinery and equipment without paying sales tax at the time of purchase, and assessed use tax on the purchases. Taxpayer asserts that as a manufacturer of cement, certain of the purchases were exempt under the "manufacturing exemption" in IC § 6-2.5-5-3(b).

Generally, all purchases of tangible personal property by persons engaged in the direct production, manufacture, fabrication, assembly, or finishing of tangible personal property are taxable. 45 IAC 2.2-5-8(a). A statute which provides a tax exemption, however, is strictly construed against the taxpayer. Indiana Dep't. of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96, 97 (Ind. Ct. App. 1974). "Exemption statutes are strictly construed because an exemption releases property from the obligation of bearing its fair share of the cost of government." General Motors Corp. v. Indiana Dept. of State Revenue, 578 N.E.2d 399, 404 (Ind. Tax Ct. 1991) aff'd 599 N.E.2d 588 (Ind. 1992) (Internal citations omitted). Thus, "[W]here such an exemption is claimed, the party claiming the same must show a case, by sufficient evidence, which is clearly within the exact letter of the law." RCA, 310 N.E.2d at 101. Accordingly, the taxpayer claiming exemption has the burden of showing the terms of the exemption statute are met. General Motors, 578 N.E.2d at 404.

IC § 6-2.5-5-3(b) provides:

> Transactions involving manufacturing machinery, tools, and equipment are exempt from the state gross retail tax if the person acquiring that property acquires it **for direct use in the direct production, manufacture**, fabrication, assembly, extraction, mining, processing, refining, or finishing **of other tangible personal property**. (**Emphasis added**).

Thus, the Legislature granted Indiana manufacturers a sales tax exemption for certain purchases, which are for "direct use in direct production, manufacture . . . of other tangible personal property." In enacting the exemption, the Legislature clearly did not intend to create a global exemption for any and all equipment which a manufacturer purchases for use within its manufacturing facility. "[F]airly read, the exemption was meant to apply to capital equipment that meets the 'double direct' test." Mumma Bros. Drilling Co. v. Department of Revenue, 411 N.E.2d 676, 678 (Ind. Ct. App. 1980). The capital equipment "in order to be exempt, must (1) be directly used by the purchaser and (2) be used in the direct production, manufacture, fabrication, assembly, extraction, mining, processing, refining, or finishing of tangible personal property." Indiana Dep't. of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520, 525 (Ind. 1983). "The test for directness requires the equipment to have an 'immediate link with the product being 'produced.'" Id. Accordingly, the sales tax exemption is applicable to that equipment which meets the "double direct" test and is "essential and integral" to the manufacture of taxpayer's tangible personal property. General Motors, 578 N.E.2d at 401. The application of Indiana's double-direct manufacturing exemptions often varies based on a determination of when a taxpayer's manufacturing process is considered to have begun and ended.

An exemption applies to manufacturing machinery, tools, and equipment directly used by the purchaser in direct production. 45 IAC 2.2-5-8(a). Machinery, tools, and equipment acquired for "direct use in the direct production" is defined in 45 IAC 2.2-5-8(c) as "manufacturing machinery, tools, and equipment to be directly used by the purchaser in the production process" that have "an immediate effect on the article being produced." Property has "an immediate effect" when it becomes "an essential and integral part of the integrated process which produces tangible personal property." 45 IAC 2.2-5-8(c). 45 IAC 2.2-5-8(d) excludes pre-production and post production activities by providing that "'direct use in the production process' begins at the point of first operation or activity constituting part of the integrated production process and ends at the point that the production has altered the item to its complete form." Therefore, proper application of the exemption requires determining at what point "production" begins and at what point "production" ends.

Further, 45 IAC 2.2-5-8(g) states:

> Machinery, tools, and equipment which are used during the production process and which have an immediate effect upon the article being produced are exempt from tax. Component parts of a unit of machinery or equipment, which unit has an immediate effect on the article being produced, are exempt if such components are an integral part of such manufacturing unit. The fact that particular property may be considered essential to the conduct of the business of manufacturing because its use is required either by law or by practical necessity does not itself mean that the property "has an immediate effect upon the article being produced." Instead, in addition to being essential for one of the above reasons, the property must also be an integral part of an integrated process which produces tangible personal property.

Additionally, 45 IAC 2.2-5-8(j) provides:

> Machinery, tools, and equipment used in managerial sales, research, and development, or other non-operational activities, are not directly used in manufacturing and, therefore, are subject to tax. This category includes, but is not limited to, tangible personal property used in any of the following activities: management and administration; selling and marketing; exhibition of manufactured or processed products; safety or fire prevention equipment which does not have an immediate effect on the product; space heating; ventilation and cooling for general temperature control; illumination; heating equipment for general

temperature control; and shipping and loading.

Accordingly, tangible personal property purchased for use in the production of a manufactured good is subject to sales and use tax unless the property used has an immediate effect on and is essential to the production of the marketable good. Thus, it is only the property that has an immediate effect on and is essential to the direct production of a marketable good that is exempt.

A. "Waste Fuel System."

Taxpayer asserts that the purchases of a "magnum DS switch," a "waste fuel tank 5," "vertical tanks," a "blending tank," a "RAM pump unit," a "solenoid relay," "EGS 1/2 & 3/4 female unions," a "SS sleeve shaft," "RAM service parts kit for waste fuel facility," an "I/O module box," an "AOD pump" for fuel storage, and an "impeller" are directly used in and are an integral part of cement manufacturing as part of its "alternative fuel" system that processes waste fuel ("waste fuel system"). Taxpayer uses "waste fuel" to power the kiln, which is used in manufacturing the cement. Before the "waste fuel" is fed into the kiln, Taxpayer processes the "waste fuel" through a "waste fuel system" that breaks down and removes pieces of sediment to make the "waste fuel" burn more efficiently. Taxpayer asserts that since the kiln needs a continuous supply of fuel, then any and all parts of Taxpayer's "waste fuel system" are used in direct production.

The Department notes that it has previously addressed this issue of Taxpayer's "waste fuel system" and issued Letter of Findings 04-20060452 (August 13, 2007), 20071031 Ind. Reg. 045070695NRA in which the Department denied the Taxpayer's protest finding that Taxpayer's "waste fuel system" did not qualify as manufacturing equipment.

During the course of the protest, Taxpayer submitted a diagram indicating how the "waste fuel system" works. Additionally, Taxpayer points to excerpts of texts of a number of examples in the regulations and attempts to analogize its situation to the examples. Taxpayer further supports its assertion by citing to three different court cases. The first is Colonial Brick Corp. v. Dep't of State Revenue, 84T10-9609-SC-117, 1998 Ind. Tax LEXIS 70 (Ind. Tax Ct. Jan. 14, 1998), which is an unpublished Tax Court case. The second is Indiana Dep't of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520 (Ind. 1983). The third is Guardian Automotive Trim, Inc. v. Indiana Dep't of State Revenue, 811 N.E.2d 979 (Ind. Tax Ct. 2004).

First, Taxpayer points to excerpts of text of a number of examples in the regulations. However, the examples are not analogous to Taxpayer's situation and more importantly are not treated as part of the law. 45 IAC 15-3-2(g). As the Indiana Supreme Court noted in Miller Brewing Co. "examples are 'included in' rules 'for illustrative purposes only,' meaning that they are not themselves rules. 45 Ind. Admin. Code 15–3–2(g) (2008). Such illustrations 'specifically designated as examples' of how rules apply 'are not to be considered as an official part of such rules.'" Indiana Dep't of Revenue v. Miller Brewing Co., 975 N.E.2d 800, 804 (Ind. 2012). "[An example when] 'specifically designated' as an example and not a rule . . . does not have the force of law." Id.

Second, Taxpayer cites to an unpublished court case decision to support its assertion. Taxpayer's reliance on an unpublished tax court case is unjustified because unpublished tax court decisions do not have precedential value. See Ind. R. App. P. 65(d).

Third, the court in Cave Stone held that transportation equipment used in the taxpayer's aggregate stone production process was exempt from sales tax because the equipment was essential to achieving the transformation of crude stone into aggregate stone. Cave Stone, 457 N.E.2d at 525. In arriving at that decision, the Cave Stone court found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Id.

Finally, the court in Guardian Automotive held that the acetone and the mask processing equipment that used acetone to periodically clean paint masks that were used in its automotive components production process qualified for the manufacturing exemptions. Guardian Automotive, 811 N.E.2d at 985. Guardian used acetone to periodically clean its paint masks. Id. at 980. The petitioner rotated a set of masks some of which were actively involved in the production process and some of which were alternatively taken out of the production process and were being cleaned and readied for use. Id. at 981. The court noted, "If the masks were not cleaned periodically, the resist build-up caused the mask lines to become irregular which, in turn, caused a variety of defects on the plastic part: paint splatters, bar shadows, and poor paint application. These defects rendered Guardian's products unmarketable to its customers." Id. As the court further noted, "To sustain continuous production of its parts, Guardian processed the masks in synchronization with the manufacturing process." Id. The court agreed with the petitioner that the mask processing equipment qualified for the equipment exemption because the equipment was "essential and integral to the overall production of Guardian's automotive trim products . . . ." Id. at 985.

Again, in applying any tax exemption, including the exemption found within 45 IAC 2.2-5-8(c), the general rule is that "tax exemptions are strictly construed in favor of taxation and against the exemption." Indiana Dep't of Revenue v. Kimball Int'l Inc., 520 N.E.2d 454, 456 (Ind. App. Ct. 1988).

Taxpayer proposes that Cave Stone and Guardian Automotive stand for the proposition that once manufacturing begins any and all equipment used will be exempt. Taxpayer states that you have to look at Taxpayer's process as a whole and anything used in that process is exempt. Thus, Taxpayer implies that Cave Stone and Guardian Automotive allow for a blanket exemption to any and all equipment used in its entire manufacturing process. Taxpayer is mistaken.

As provided above, in Cave Stone, the court found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. Additionally, in Guardian Automotive, the court noted, "If the masks were not cleaned periodically, the resist build-up caused the mask lines to become irregular which, in turn, caused a variety of defects . . . which . . . rendered Guardian's products unmarketable to its customers." Guardian Automotive, 811 N.E.2d at 981. In other words, the court focused on the fact that the acetone and the mask processing equipment had an immediate effect on Guardian's manufactured automotive components.

However, in Taxpayer's case, the "waste fuel system" does not have an immediate effect on the manufactured cement. While the "waste fuel system" may make the use of "waste fuel" more efficient, Taxpayer could manufacture cement without using a "waste fuel system." Particularly, since Taxpayer could choose either to use "waste fuel" without processing it or to purchase fuel that is ready for production. Thus, the "waste fuel system" is a separate system distinct and removed from the actual manufacturing of the cement. The "waste fuel system" simply functions to process the "waste fuel" before the fuel enters into the manufacturing process. Accordingly, the processing of "waste fuel" is a preproduction activity and does not fall under the exemption.

Therefore, Taxpayer's protest to the imposition of use tax on the purchases used in its "waste fuel system" is respectfully denied.

B. "Black 5 Gal Pails."

The Department found that use tax was due on Taxpayer's purchase of "black 5 gal pails." Taxpayer maintains that the "black 5 gal pails" are used to accumulate and store "in house waste" that is used for kiln fuel and therefore, qualify for the manufacturing equipment exemption.

While equipment that is used to actually extract the waste from the production process can qualify for the manufacturing exemption, any equipment that is used to collect, transport, store, or otherwise process the waste after its extraction is subject to tax. See Graham Creek Farms v. Indiana Dep't of State Revenue, 819 N.E.2d 151 (Ind. Tax Ct. 2004) (exempting equipment that actually remove waste from the production process, but not extending the exemption to equipment that is used to transport the waste that has been removed from production.) Since the "black 5 gal pails" are used to collect, store, and transport the waste of the manufacturing process that has been extracted from the production process, the "black 5 gal pails" used to move the waste are used in a post-production activity and are taxable. It does not matter that this waste will later re-enter a new cycle of the production process. Once the waste is removed from the production process, any transporting of the waste is a post production activity. While the waste may at some point re-enter Taxpayer's production process, the waste's transport does not become a production activity until it actually re-enters the production process. Therefore, the "black 5 gal pails" that are used in transporting the "in house waste" do not qualify for the manufacturing exemption.

Accordingly, Taxpayer's protest to the imposition of use tax on the "black 5 gal pails" is respectfully denied.

C. "Fly Ash System: Compressor."

Taxpayer asserts that the compressor was purchased and installed on the fly ash tank storage tank, which is part of Taxpayer's "fly ash system" and is exempt from sales and use tax. Taxpayer maintains that the "fly ash system" transports the fly ash from the fly ash tank into the raw mill. The "fly ash system" is used to feed fly ash into the raw mill where it is mixed with other ingredients to form slurry, which is fed into the kiln. Taxpayer states the compressor shoots a burst of air into the fly ash before it enters the rotary valve for the raw mill main feed belt.

The Department notes that it has previously addressed this issue of Taxpayer's "fly ash system" and issued Letter of Findings 04-20060452 (August 13, 2007), 20071031 Ind. Reg. 045070695NRA in which the Department denied the Taxpayer's protest finding that Taxpayer's "fly ash system" that Taxpayer used to transport the fly ash is used in a preproduction activity and did not qualify as manufacturing equipment.

The "fly ash system" is used to feed fly ash into the raw mill where it is mixed with other ingredients to form slurry, which is fed into the kiln. The conveyor system moves the fly ash from storage into the raw mill. Taxpayer maintains that since the fly ash tank is attached to its computer system that controls its manufacturing process, the fly ash tank and its component parts are part of the manufacturing process. Taxpayer reasons that since the fly ash tank and its component parts are part of the manufacturing process, then they are used in direct production of cement and are exempt. As discussed previously, Taxpayer mistakenly implies that Cave Stone allows for a blanket exemption to any and all equipment used in the entire process of cement making.

As provided above, the court in Cave Stone found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. While the "fly ash system" that is connected to Taxpayer's computer system may be a necessary part of Taxpayer's manufacturing system, the compressor and other components of the "fly ash system" are not machinery that has an immediate effect on the manufactured cement. During the time the fly ash is in the storage tank and on the conveyor system, the fly ash is not being mixed, altered, combined, or changed in form. The storage tank and conveyor system simply function to transport a raw material before it enters into the manufacturing process. Accordingly, even when connected to a computer system, the storage and transporting of the fly ash by a conveyor system is a preproduction activity and does not fall under the exemption.

Therefore, Taxpayer's protest to the imposition of use tax on its purchase of a compressor for the "fly ash

system" is respectfully denied.

D. Slurry Tank.

The Department found that use tax was due on Taxpayer's January 30, 2009, purchase–which the auditor described as the materials portion of a time and materials contract that included "bearings; gen. tach; misc parts" (p. 27 of the audit report). At the time of the audit, the Department was unable to verify the nature of the transaction. Therefore, as Taxpayer had not paid sales tax at the time of the transaction, the Department assessed use tax on the purchase. As stated previously, Indiana imposes "an excise tax, known as the use tax," on tangible personal property that is acquired in retail transactions and is stored, used, or consumed in Indiana. IC § 6-2.5-3-2(a).

Taxpayer asserts that the materials were purchased to repair the slurry tank and therefore are exempt from sales and use tax. Taxpayer states that the slurry is mixed in the raw mill, transported to and held in the slurry tank, and then transported to and fired in the kiln to produce clinker. Taxpayer maintains that slurry is work-in-process and is temporarily held in the slurry tank between the raw mill and the kiln. Taxpayer reasons that since the slurry tank is used in the manufacturing process, parts purchased for the slurry tank are exempt.

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the slurry tank would be tax exempt to the extent that the slurry tank is exempt. The issue becomes whether the slurry tank is exempt "manufacturing equipment."

45 IAC 2.2-5-8(e) states:

> Tangible personal property used in or for the purpose of storing raw materials or finished goods is subject to tax except for temporary storage equipment necessary for moving materials being manufactured from one (1) machine to another or from one (1) production step to another.
>
> (1) Temporary storage. Tangible personal property used in or for the purpose of storing work-in-process or semi-finished goods is not subject to tax if the work-in-process or semi-finished goods are ultimately completely produced for resale and in fact resold.
>
> (2) Storage containers for finished goods after completion of the production process are subject to tax.
>
> (3) Storage facilities or containers for materials or items currently undergoing production during the production process are deemed temporary storage facilities and containers and are not subject to tax.

Since the slurry tank is used to temporarily hold work-in-process, pursuant to 45 IAC 2.2-5-8(e)(1) the slurry tank is equipment that is directly used during the production process qualifying for the "manufacturing equipment" exemption. Therefore, pursuant to 45 IAC 2.2-5-8(h)(2) repair parts purchased for the slurry tank would also be tax exempt.

Accordingly, Taxpayer's protest to the imposition of use tax on its January 30, 2009, purchase of "bearings; gen. tach; misc parts" for the slurry tank is sustained.

E. "Maintenance Agreement."

The Department found that use tax was due on Taxpayer's June 19, 2009, purchase which the auditor described as the purchase of a "maintenance agreement (No details provided)" (p. 25 of the audit report). At the time of the audit, the Department was unable to verify the nature of the transaction. Therefore, as Taxpayer had not paid sales tax at the time of the transaction, the Department assessed use tax on the purchase. As stated previously, Indiana imposes "an excise tax, known as the use tax," on tangible personal property that is acquired in retail transactions and is stored, used, or consumed in Indiana. IC § 6-2.5-3-2(a).

Taxpayer asserts that the "maintenance agreement" was purchased for computer software for its "CBX x-ray machine." Taxpayer maintains that since the "maintenance agreement" was purchased for software that runs exempt equipment, the "maintenance agreement" is also exempt from tax. The CBX x-ray machine is in the quality control laboratory and is located immediately next to the kiln burn floor. Taxpayer states that the "CBX x-ray machine" analyzes production samples and therefore is exempt under 45 IAC 2.2-5-8(i). Taxpayer takes "[s]amples every minute to determine whether changes in production are necessary; such changes occur every five minutes."

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a "maintenance agreement" purchased for the software for the "CBX x-ray machine" would be tax exempt to the extent that the "CBX x-ray machine" is exempt. The issue becomes whether the 'CBX x-ray machine" is exempt "manufacturing equipment."

45 IAC 2.2-5-8(i) states:

> Testing and inspection. Machinery, tools, and equipment used to test and inspect the product as part of the production process are exempt.
>
> –EXAMPLE–
>
> Selected parts are removed from production according to a schedule dictated by statistical sampling methods. Quality control equipment is used to test the parts in a room in the plant separate from the production line. Because of the functional interrelationship between the testing equipment and the machinery on the production line and because of the product flow, the testing equipment is an integral part of the

integrated production process and is exempt.

Consequently, not all testing and inspecting equipment would qualify for exemption. The testing and inspecting equipment must have a functional interrelationship with the machinery on the product line and the product flowing in production to qualify for the manufacturing equipment exemption. Thus, testing and inspecting that take place prior to or after production is complete would not qualify.

Since the "CBX x-ray machine" is used to test the product during production according to a schedule for purposes of quality control of the production system, the "CBX x-ray machine" is equipment directly used during the production process qualifying for the "manufacturing equipment" exemption. Therefore, pursuant to 45 IAC 2.2-5-8(h)(2) a "maintenance agreement" purchased for the software for the "CBX x-ray machine" would also be tax exempt.

Accordingly, Taxpayer's protest to the imposition of tax on its June 19, 2009, "maintenance agreement" purchase (p. 19 of the audit report) for software for the "CBX X-Ray Machine" is sustained.

F. Plant Water Tower.

Taxpayer asserts that the materials in its November 18, 2010, purchase were used to repair the "RIP Plant Water Tower" that "contains the water for the slurry." Taxpayer states that "in the raw mill, water creates slurry, becoming part of the work-in-process." Taxpayer argues that since the water tower is physically integrated into the manufacturing system through pipes connecting the tower to the raw mill, the water tower is used in direct production. Taxpayer cites to 45 IAC 2.2-5-8 and maintains that "[t]he water tower has an immediate effect on the work-in-process because it is an essential and integral part of the system furnishing the water to the manufacturing system."

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the well would be tax exempt to the extent that the plant water tower is exempt. The issue becomes whether the plant water tower is exempt "manufacturing equipment."

As provided above, the court in Cave Stone found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. While the water tower may be a necessary part of Taxpayer's manufacturing system, the "water tower" and piping are not machinery that has an immediate effect on the manufactured cement. During the time water is in the water tower and pipes, the water is not being mixed, altered, combined, or changed. The water tower and pipes simply functions to store and transport a raw material before it enters into the manufacturing process. Accordingly, the storage and transporting of the water by the water tower and pipes is a preproduction activity and does not fall under the exemption.

Alternatively, Taxpayer maintains that if this purchase is taxable, it should be treated as a capital item and not an expense item in the statistical sample. Taxpayer asserts that "[t]he purpose of a statistical sample is to provide a picture of a company's reoccurring expenses during the audit period . . . [and] this major repair to the water tower occurs at most only once every 5.5 years." Taxpayer argues that "[t]reating the purchase, therefore, as a regular occurrence and projecting it as though it occurred regularly during the audit period unfairly skews [Taxpayer's] liability."

Taxpayer suggests that including this particular repair distorts the projection because this repair occurs irregularly. However, the Department has the authority to use methods considered necessary to determine a taxpayer's proper tax liability as provided by IC § 6-8.1-4-2. The Department used a statistical sample selected from Taxpayer's records and a projection method to perform the audit of Taxpayer's expense purchases. The expenses chosen in the statistical sample were divided into six stratums of related purchases based upon the dollar amount of the purchases. As noted above, having protested the audit results, it is the taxpayer's burden of demonstrating that the sampling method is wrong, not that an alternative method would produce a different result. It is not relevant that Taxpayer makes this particular repair "once every 5.5 years." The only relevant fact is that there was a repair transaction during the projection period. Repairs to equipment are a normal occurrence for a manufacturing plant. As such, it does not seem that a cement manufacture having a repair on a piece of equipment would be abnormal, unrelated or incidentally related to the manufacturing operations.

The Department agrees that a recalculation of taxpayer's sales and use tax liabilities could very well result in a different result than the one reached by the audit. However, an administrative hearing is not the appropriate forum by which to explore variances. Taxpayer asks the Legal Division to intrude into an area of expertise of which the Legal Division has little experience and for which Taxpayer has no legal challenge. Taxpayer has failed to demonstrate clear error on the part of the audit.

Accordingly, Taxpayer's protest to the imposition of use tax on its purchase of a water tower is respectfully denied.

G. "Heat Tape."

Taxpayer asserts that its October 22, 2010, purchase of "heat tape" is exempt because the tape was used on the water pipes to prevent them from freezing. Taxpayer maintains that the "heat tape" is wrapped around the water pipes of exempt equipment and is therefore exempt.

"Heat tape" is not equipment or machinery, does not become part of the product, but is a material consumed

by Taxpayer. Therefore, the related statute and manufacturing exemption at issue would be the "consumption exemption" found at IC § 6-2.5-5-5.1.

IC § 6-2.5-5-5.1(b) provides and exemption for "tangible personal property" that is "acquired . . . for direct consumption as a material to be consumed in the direct production of other tangible personal property . . . ." The exemption for direct consumption in production is further explained at 45 IAC 2.2-5-12. The Department refers to 45 IAC 2.2-5-12(b) and (f), which state:

> (b) The exemption provided by this regulation [45 IAC 2.2] applies only to tangible personal property to be directly consumed in direct production by manufacturing, processing, refining, or mining. It does not apply to machinery, tools, and equipment used in direct production or to materials incorporated into the tangible personal property produced.
>
> . . .
>
> (f) Other taxable transactions. Purchases of materials consumed in manufacturing, processing, refining, or mining activities beyond the scope of those described in subsection B above [subsection (e) of this section] are taxable. Such activities include postproduction activities; storage step) [sic.]; **maintenance**, testing and inspection (except where in direct production); (except where essential and integral to the process system); management and administration; sales; research and development; exhibition of products; safety or fire prevention; space heating; ventilation and cooling equipment for general temperature control; illumination; shipping and loading.

(**Emphasis added**.)

Therefore, items purchased for consumption in a taxpayer's post production activities are subject to tax. Pursuant to 45 IAC 2.2-5-12(f), maintenance is a post production activity. Since "Heat tape" is used in the maintenance of the pipes, it is used in a post production activity and is subject to tax. Given that maintenance is subject to tax regardless of the status of the equipment, the Department declines to address the status of the equipment upon which the tape is used at this time.

Accordingly, Taxpayer's protest to the imposition of use tax on its purchase of "heat tape" is respectfully denied.

H. Wells.

Taxpayer asserts that the "materials for well repair" purchase on October 22, 2010, (p. 27 of audit report) was used to repair the wells that are part of the system furnishing water during manufacturing process and therefore are exempt. Taxpayer maintains that since the wells are exempt manufacturing equipment, the repair parts purchased for wells are also exempt.

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the well would be tax exempt to the extent that the well is exempt. The issue becomes whether the wells are exempt "manufacturing equipment."

As provided above, in Cave Stone, the court found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. Additionally, in Guardian Automotive, the court noted, "If the masks were not cleaned periodically, the resist build-up caused the mask lines to become irregular which, in turn, caused a variety of defects . . . which . . . rendered Guardian's products unmarketable to its customers." Guardian Automotive, 811 N.E.2d 979, 981 (Ind. Tax Ct. 2004). In other words, the court focused on the fact that the acetone and the mask processing equipment had an immediate effect on Guardian's manufactured automotive components.

In Taxpayer's case, the wells do not have an immediate effect on the manufactured cement. While the wells may be a necessary part of Taxpayer's manufacturing system, the wells are not machinery that has an immediate effect on the manufactured cement. Taxpayer could manufacture cement without using the wells. Taxpayer's acquisition of "well water" is a separate process that is distinct and removed from the actual manufacturing of the cement. The wells simply function to draw and/or transport the "well water" before the "well water" enters into the cement manufacturing process. Accordingly, the wells are used in a preproduction activity, as to the concrete manufacturing process, and do not fall under the manufacturing exemption. See Letter of Findings 04-20100634 (June 28, 2011), 20110928 Ind. Reg. 045110493NRA (Finding that "while water is used within the direct processing of Taxpayer's product, the water wells are used to draw and collect water and therefore constitute a pre-production activity. Consequently, the water wells are not exempt from taxation.")

Therefore, Taxpayer's protest to the imposition of use tax on "repair parts" for the wells is respectfully denied.

I. Water Treatment Chemicals.

Taxpayer asserts that its August 4, 2010, purchase of water treatment chemicals "are added to the process water, which becomes part of the slurry (work-in-process) that enters the kilns." Taxpayer states that the chemicals are added to "process water" that is used in the raw mills to create slurry. Taxpayer maintains that the chemicals are either consumed in the kiln qualifying for the manufacturing "consumption exemption" or become incorporated into the slurry qualifying for the manufacturing "incorporation exemption."

As provided above, in Cave Stone, the court found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave

Stone, 457 N.E.2d at 525. Additionally, in Guardian Automotive, the court noted, "If the masks were not cleaned periodically, the resist build-up caused the mask lines to become irregular which, in turn, caused a variety of defects . . . which . . . rendered Guardian's products unmarketable to its customers." Guardian Automotive, 811 N.E.2d at 981. In other words, the court focused on the fact that the acetone and the mask processing equipment had an immediate effect on Guardian's manufactured automotive components.

However, in Taxpayer's case, the chemicals do not have an immediate effect on the manufactured cement. While the chemicals are added to the "process water" may make the use of "process water" more efficient, Taxpayer could manufacture cement without using the chemicals. Particularly, since Taxpayer could choose either to use "process water" without the chemicals or to purchase water that is ready for production. Thus, adding chemicals to the "process water" is a separate process both distinct and removed from the actual manufacturing of the cement. The chemicals simply functions to treat the "process water" before it enters into the manufacturing process. Accordingly, the treatment of the "process water" is a preproduction activity and does not fall under the exemption.

Therefore, Taxpayer's protest to the imposition of use tax on water treatment chemicals is respectfully denied.

J. Idler Roll.

The Department found that use tax was due on Taxpayer's March 16, 2010, purchase–which the auditor described as "hi-vol roller bearings" (p. 20 of the audit report). At the time of the audit, the Department was unable to verify the nature of the transaction. Therefore, as Taxpayer had not paid sales tax at the time of the transaction, the Department assessed use tax on the purchase. As stated previously, Indiana imposes "an excise tax, known as the use tax," on tangible personal property that is acquired in retail transactions and is stored, used, or consumed in Indiana. IC § 6-2.5-3-2(a).

Taxpayer asserts that the bearings were purchased to repair the idler roll and therefore are exempt from sales and use tax. Taxpayer states that the idler roll is located at the quarry. It moves the crushed stone exiting the crusher to the temporary storage bins, which are used to hold and transport the crushed stone to the raw mill. Taxpayer maintains that since crushed stone is work-in-process and the idler roll transports the crushed stone to the bins that temporarily hold and transport the stone, the idler roll is manufacturing equipment. Taxpayer reasons that since the idler roll is used in the manufacturing process, parts purchased for the idler roll are exempt.

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the idler roll would be tax exempt to the extent that the idler roll is exempt. The issue becomes whether the idler roll is exempt "manufacturing equipment."

45 IAC 2.2-5-8(f) sets out the rule for determining when equipment is used in an exempt manner and when it is used in a non-exempt manner. 45 IAC 2.2-5-8(f) states:

(1) Tangible personal property used for moving raw materials to the plant prior to their entrance into the production process is taxable.

(2) Tangible personal property used for moving finished goods from the plant after manufacture is subject to tax.

(3) Transportation equipment used to transport work-in-process or semi-finished materials to or from storage is not subject to tax if the transportation is within the production process.

(4) Transportation equipment used to transport work-in-process, semi-finished, or finished goods between plants is taxable, if the plants are not part of the same integrated production process.

Since the idler roll is used to transport work-in-process, pursuant to 45 IAC 2.2-5-8(f)(3) the idler roll is equipment that is directly used during the production process qualifying for the "manufacturing equipment" exemption. Therefore, pursuant to 45 IAC 2.2-5-8(h)(2) repair parts purchased for the idler roll would also be tax exempt.

Accordingly, Taxpayer's protest to the imposition of use tax on its March 16, 2010, purchase of "hi-vol roller bearings" (p. 20 of the audit report) for the idler roll is sustained.

K. Flowmeter.

The Department found that use tax was due on Taxpayer's October 27, 2009, purchase of a flowmeter (p. 19 of audit report). Taxpayer asserts that the flowmeter was purchased to measure amount of bulk cement that is put in each individual bag in the automated packaging line and therefore is exempt from sales and use tax. Taxpayer states that its cement is packaged in individual bags, placed on pallets, and sold by the pallet. Taxpayer maintains that since the flowmeter measures the amount of cement that goes into each bag, it is exempt from tax under 45 IAC 2.2-5-8(d).

45 IAC 2.2-5-8(d) excludes pre-production and post production activities by providing that "'direct use in the production process' begins at the point of first operation or activity constituting part of the integrated production process and ends at the point that the production has altered the item to its complete form." Therefore, proper application of the exemption requires determining at what point "production" begins and at what point "production" ends.

Since the flowmeter is used in transporting and measuring Taxpayer's product to create the packaged

product–i.e., the individual bags of cement, the flowmeter is used during production of the product. Therefore, the flowmeter qualifies for the manufacturing equipment exemption.

Accordingly, Taxpayer's protest to the imposition of use tax on its October 27, 2009, purchase of a flowmeter (p. 19 of the audit report) is sustained.

L. Reducer.

Taxpayer asserts that its July 7, 2009, purchase of a reducer–which the auditor described as "reducer (south scale)" (p. 16 of audit report)–was purchased as a repair part for the scale that measures work-in-process in Taxpayer's manufacturing process and therefore is exempt from sales and use tax. Taxpayer maintains that the reducer is used in the scale that measures and controls the amount of clinker that is removed from temporary storage for the finish mills. Taxpayer reasons that since the scale is used in the manufacturing process, a part purchased for the scale is also exempt.

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the reducer would be tax exempt to the extent that the reducer is exempt. The issue becomes whether the reducer is exempt "manufacturing equipment."

"Direct production" is the performance of an integrated series of operations which transform the matter into the marketable article. 45 IAC 2.2-5-8(k). For the scale to be "directly used" in Taxpayer's "direct production" process they must have an immediate effect on the article being produced. 45 IAC 2.2-5-8(c). For the scale to have an "immediate effect" on the article being produced, the scale must be an essential and integral part of an integrated process that produces the article.

As an illustration of this, Example 1 under 45 IAC 2.2-5-8(d) states:

> The production of pharmaceutical items is accomplished by a process which begins with weighing and measuring out appropriate ingredients, continues with combining and otherwise treating the ingredients, and ends with packaging the items. Equipment used to transport raw materials to the manufacturing plant is employed prior to the first operation or activity constituting part of the integrated production process and is taxable. Weighing and measuring equipment and all equipment used as an essential and integral part of the subsequent manufacturing steps, through packaging, qualify for exemption. Equipment which loads packaged products from the packaging step of production into storage, or from storage into delivery vehicles, is subject to tax.

In this case, Taxpayer established that the scale functions as a device to measure work-in-process as part of Taxpayer's production process. In the example cited above, "weighing and measuring equipment" was considered to be part of the first step in production. Taxpayer has described an integrated, automated production process that depends on precise measurement of various combinations of materials. Since the scale is used to measure work-in-process, the scale is equipment that is directly used during the production process qualifying for the "manufacturing equipment" exemption. Therefore, pursuant to 45 IAC 2.2-5-8(h)(2), repair parts purchased for the scale would also be tax exempt.

Accordingly, Taxpayer's protest to the imposition of use tax on its July 7, 2009, purchase of a reducer (p. 16 of audit report) for the scale is sustained.

M. "P & H Crane Rail."

Taxpayer asserts that its August 25, 2009, purchase of a replacement rail (p. 8 of the audit report) was used to replace the rail in the rail system to which the "P & H crane" is attached and runs along. Taxpayer states that the "P & H crane" is used to transport clinker from its temporary storage in the clinker cooler to the finish mill. Taxpayer, therefore, maintains that the rail system attached to the "P & H crane" is used to transport work-in-process in Taxpayer's manufacturing process and is exempt from sales and use tax. Taxpayer reasons that since the rail system is used in the manufacturing process, a replacement part purchased for the rail system is also exempt.

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the "P & H crane rail system" would be tax exempt to the extent that the "P & H crane rail system" is exempt. The issue becomes whether the "P & H crane rail system" is exempt "manufacturing equipment."

45 IAC 2.2-5-8(f) sets out the rule for determining when equipment is used in an exempt manner and when it is used in a non-exempt manner. 45 IAC 2.2-5-8(f) states:

> (1) Tangible personal property used for moving raw materials to the plant prior to their entrance into the production process is taxable.
>
> (2) Tangible personal property used for moving finished goods from the plant after manufacture is subject to tax.
>
> (3) Transportation equipment used to transport work-in-process or semi-finished materials to or from storage is not subject to tax if the transportation is within the production process.
>
> (4) Transportation equipment used to transport work-in-process, semi-finished, or finished goods between plants is taxable, if the plants are not part of the same integrated production process.

Since the "P & H crane rail system" is used to transport work-in-process, pursuant to 45 IAC 2.2-5-8(f)(3) the

"P & H crane rail system" is equipment that is directly used during the production process qualifying for the "manufacturing equipment" exemption. Therefore, pursuant to 45 IAC 2.2-5-8(h)(2) repair parts purchased for the "P & H crane rail system" would also be tax exempt.

Accordingly, Taxpayer's protest to the imposition of use tax on its August 25, 2009, purchase of a replacement rail (p. 8 of the audit report) for the "P & H crane rail system" is sustained.

N. "12 Strand Fiber Optics."

Taxpayer asserts that its December 29, 2011, purchase of "12 strand fiber optics"–which the auditor described as "12 strand fiber optics from office to east silo" (p. 24 of the audit report)–was used as part of the automated "finished product load-out" system which dispenses the finished cement from the finished product silo into customer trucks. Taxpayer maintains that since the "12 strand fiber optics" links the computer to the dispensing mechanism of the "finished product load-out" system that dispenses the final product in the amount that is sold to the customers. Taxpayer states that the "finish product load-out" system functions similarly to "key for the silo." Taxpayer reasons that the dispensing of the product into the customer's trucks is similar to packaging and therefore is exempt.

As provided above, in Cave Stone, the court found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. Additionally, in Guardian Automotive, the court noted, "If the masks were not cleaned periodically, the resist build-up caused the mask lines to become irregular which, in turn, caused a variety of defects . . . which . . . rendered Guardian's products unmarketable to its customers." Guardian Automotive, 811 N.E.2d at 981. In other words, the court focused on the fact that the acetone and the mask processing equipment had an immediate effect on Guardian's manufactured automotive components.

45 IAC 2.2-5-8(d) excludes pre-production and post production activities by providing that "'direct use in the production process' begins at the point of first operation or activity constituting part of the integrated production process and ends at the point that the production has altered the item to its complete form." Therefore, proper application of the exemption requires determining at what point "production" begins and at what point "production" ends.

However, based upon the information provided, a computer system that functions as a "key for the silo" does not have an immediate effect on the product being produced. Taxpayer's finished product silo holds Taxpayer's finished product in its completed form. Therefore, the computer system performs a post-production activity.

Accordingly, Taxpayer's protest to the imposition of tax on its purchase of "12 strand fiber optics" is respectfully denied.

O. Crusher.

Taxpayer asserts that its August 24, 2011, purchase of fuses–which the auditor described as "CHSWG SCLS-6R 5.08 MAX KVCLS 6R" (p. 23 of audit report)–were purchased to repair the secondary crusher that crushes stone at the quarry in Taxpayer's manufacturing process and therefore is exempt from sales and use tax.

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the crusher is tax exempt to the extent that the crusher is exempt. Since the crusher is manufacturing equipment that is exempt as part of Taxpayer's manufacturing process, the repair part purchased for the crusher is also exempt.

Accordingly, Taxpayer's protest to the imposition of use tax on its August 24, 2011, purchase of fuses (p. 23 of the audit report) for the crusher is sustained.

P. "Petron Gear Shield NC Lubricant."

Taxpayer asserts that its December 7, 2011, purchase of "petron gear shield nc lubricant" (p.21 of the audit report) was used to lubricate the kiln drive for kiln #1 and is exempt from sales and use tax under 45 IAC 2.2-5-12(e). Taxpayer maintains that this special lubricant is used to lubricate the kiln drive which controls the gears that are mixing the materials in the kiln.

Lubricant is a material consumed by Taxpayer. Therefore, the related statute and manufacturing exemption at issue would be the "consumption exemption" found at IC § 6-2.5-5-5.1. IC § 6-2.5-5-5.1(b) provides an exemption for "tangible personal property" that is "acquired . . . for direct consumption as a material to be consumed in the direct production of other tangible personal property . . . ." The exemption for direct consumption in production is further explained at 45 IAC 2.2-5-12. The Department refers to 45 IAC 2.2-5-12(e), which states in relevant part:

> (e) "Have an immediate effect upon the article being produced or mined." Purchases of materials to be consumed during the production or mining process are exempt from tax, if the consumption of such materials has an immediate effect upon the article being produced and mined, or upon machinery, tools, or equipment which are both used in the direct production or mining process and are exempt from tax under these regulations [45 IAC 2.2].

Since the lubricant directly affects the kiln that is a piece exempt manufacturing equipment that is used by Taxpayer in the direct production, the lubricant qualifies for the consumption exemption.

Accordingly, Taxpayer's protest to the imposition of use tax on its December 7, 2011, purchase of "petron

gear shield nc lubricant" (p. 21 of the audit report) for the kiln drive is sustained.

Q. Inline Heater.

The Department determined that Taxpayer's October 24, 2011, purchase of an inline heater (p.27 of the audit report) was subject to tax because it was "pre-heating a raw material" prior to its entry into the production process. Taxpayer maintains that the inline heater is exempt manufacturing equipment.

Taxpayer asserts that the inline heater is used to allow oil to properly flow in the pipes leading to the kiln. Taxpayer maintains that the oil has to be heated so that it can be pumped through the pipes at the frequency required for production.

As provided above, in Cave Stone, the court found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. Additionally, in Guardian Automotive, the court noted, "If the masks were not cleaned periodically, the resist build-up caused the mask lines to become irregular which, in turn, caused a variety of defects . . . which . . . rendered Guardian's products unmarketable to its customers." Guardian Automotive, 811 N.E.2d at 981. In other words, the court focused on the fact that the acetone and the mask processing equipment had an immediate effect on Guardian's manufactured automotive components.

However, in Taxpayer's case, the inline heater does not have an immediate effect on the manufactured cement. While the inline heater may be necessary to Taxpayer's production process, the inline heater is readying an item consumed in production. Thus, the inline heater has a separate function both distinct and removed from the actual manufacturing of the cement. The inline heater simply functions to process the oil before it enters into the manufacturing process. Accordingly, the pre-heating of the oil is a preproduction activity and does not fall under the exemption.

Therefore, Taxpayer's protest to the imposition of use tax on the purchase of an inline heater is respectfully denied.

R. "V-Ball Controller Housing."

Taxpayer asserts that its July 30, 2009, purchase of ball valves (p. 27 of audit report) were purchased as repair parts for the "v-ball controller housing" that is used in Taxpayer's manufacturing process and therefore is exempt from sales and use tax. Taxpayer maintains that the valve on the v-ball controller housing controls the amount of work-in-process raw feed that enters the kiln from the raw mill and therefore is used to transport work-in-process between manufacturing steps.

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the "v-ball controller housing" would be tax exempt to the extent that the "v-ball controller housing" is exempt. The issue becomes whether the "v-ball controller housing" is exempt "manufacturing equipment."

45 IAC 2.2-5-8(f) sets out the rule for determining when equipment is used in an exempt manner and when it is used in a non-exempt manner. 45 IAC 2.2-5-8(f) states:

(1) Tangible personal property used for moving raw materials to the plant prior to their entrance into the production process is taxable.

(2) Tangible personal property used for moving finished goods from the plant after manufacture is subject to tax.

(3) Transportation equipment used to transport work-in-process or semi-finished materials to or from storage is not subject to tax if the transportation is within the production process.

(4) Transportation equipment used to transport work-in-process, semi-finished, or finished goods between plants is taxable, if the plants are not part of the same integrated production process.

Since the "v-ball controller housing" is used in transporting work-in-process, pursuant to 45 IAC 2.2-5-8(f)(3) the "v-ball controller housing" is equipment that is directly used during the production process qualifying for the "manufacturing equipment" exemption. Therefore, pursuant to 45 IAC 2.2-5-8(h)(2) repair parts purchased for the "v-ball controller housing would also be tax exempt.

Accordingly, Taxpayer's protest to the imposition of use tax on July 30, 2009, purchase of ball valves (p. 27 of audit report) for the "v-ball controller housing" is sustained.

S. Quality Control Laboratory: Electrical System.

Taxpayer asserts that its August 24, 2011, purchase of a transformer–which the auditor described as "H-D 23-28-275-6 7.5 KVA 120/240" (p. 27 of audit report)–was purchased to repair the electrical system furnishing electricity to the quality control laboratory that is located in the mill building. Taxpayer maintains that the electricity powers the laboratory that is used to conduct quality control testing during production. Taxpayer reasons that since the electrical system is used to power the laboratory that is used in the manufacturing process, a part purchased to repair the electrical system is also exempt.

Pursuant to 45 IAC 2.2-5-8(h)(2) "[r]eplacement parts, used to replace worn, broken, inoperative, or missing parts or accessories on exempt machinery and equipment, are exempt from tax." Accordingly, a part purchased for the electrical system would be tax exempt to the extent that the electrical system is exempt. The issue becomes whether the electrical system is exempt "manufacturing equipment."

The Department refers to 45 IAC 2.2-5-8 (l)(1):

Equipment used to modify energy purchased from public utilities purchased for the production process is exempt if the equipment is used to modify the utilities for use by exempt equipment.

Taxpayer's quality control laboratory is located immediately next to the kiln burn floor. Taxpayer states that it analyses production samples in the quality control laboratory and its quality control laboratory equipment is exempt under 45 IAC 2.2-5-8(i). Taxpayer takes "[s]amples every minute to determine whether changes in production are necessary; such changes occur every five minutes."

45 IAC 2.2-5-8(i) states:

Testing and inspection. Machinery, tools, and equipment used to test and inspect the product as part of the production process are exempt.

–EXAMPLE–

Selected parts are removed from production according to a schedule dictated by statistical sampling methods. Quality control equipment is used to test the parts in a room in the plant separate from the production line. Because of the functional interrelationship between the testing equipment and the machinery on the production line and because of the product flow, the testing equipment is an integral part of the integrated production process and is exempt.

Consequently, not all testing and inspecting equipment would qualify for exemption. The testing and inspecting equipment must have a functional interrelationship with the machinery on the product line and the product flowing in production to qualify for the manufacturing equipment exemption. Thus, testing and inspecting that take place prior to or after production is complete would not qualify.

Since the quality control laboratory has equipment that is used to test the product during production according to a schedule for purposes of quality control of the production system, the laboratory equipment is directly used during the production process qualifying for the "manufacturing equipment" exemption. Therefore, pursuant to 45 IAC 2.2-5-8(h)(2) a transformer purchased to repair the electrical system for the quality control laboratory would also be tax exempt.

Accordingly, Taxpayer's protest to the imposition of use tax on its August 24, 2011, purchase of a transformer–which the auditor described as "H-D 23-28-275-6 7.5 KVA 120/240" (p. 27 of audit report) is sustained.

T. Gypsum Hopper Grate.

Taxpayer asserts that the gypsum hoper grate it purchased on January 22, 2010, (p.27 of the audit report) is used to remove the oversized pieces of gypsum from entering the gypsum storage silo and is exempt from sales and use tax under 45 IAC 2.2-5-12(e). Taxpayer maintains that since the gypsum hopper grate prevents the oversized pieces of gypsum from entering the silo–which meters the gypsum into the finish mill–the grate is part of the manufacturing production process and is exempt.

As provided above, the court found that the "focus of the analysis should be whether the equipment is an 'integral part of manufacturing and operates directly on the product during production.'" Cave Stone, 457 N.E.2d at 525. The gypsum hopper grate is used to sort the gypsum before it goes into the storage silo. Therefore, the gypsum hoper grade readies a raw material, gypsum, for the manufacturing process. Thus, the gypsum hopper, at best, is a separate system both distinct and removed from the actual manufacturing of cement. The gypsum hopper grate simply functions to sort the gypsum before it enters into the manufacturing process. Accordingly, the sorting of the gypsum is a preproduction activity that does not fall under the exemption.

Accordingly, Taxpayer's protest to the imposition of use tax on its purchase of a gypsum hopper grate is respectfully denied.

FINDING

Taxpayer's protest is sustained in part and denied in part. Taxpayer's protest to the imposition of use tax on its January 30, 2009, purchase of "bearings; gen. tach; misc parts" for the slurry tank is sustained, as discussed in subpart D. Taxpayer's protest to the imposition of tax on its June 19, 2009, "maintenance agreement" purchase (p.19 of the audit report) for software for the "CBX X-Ray Machine" is sustained, as discussed in subpart E. Taxpayer's protest to the imposition of use tax on its March 16, 2010, purchase of "hi-vol roller bearings" (p. 20 of the audit report) for the idler roll is sustained, as discussed in subpart J. Accordingly, Taxpayer's protest to the imposition of use tax on its October 27, 2009, purchase of a flowmeter (p. 19 of the audit report) is sustained, as discussed in subpart K. Taxpayer's protest to the imposition of use tax on its August 24, 2011, purchase of fuses (p. 23 of the audit report) for the crusher is sustained, as discussed in subpart O. Taxpayer's protest to the imposition of use tax on its December 7, 2011, purchase of "petron gear shield nc lubricant" (p. 21 of the audit report) for the kiln drive is sustained, as discussed in subpart P. Taxpayer's protest to the imposition of use tax on July 30, 2009, purchase of ball valves (p. 27 of audit report) for the "v-ball controller housing" is sustained, as discussed in subpart R. Taxpayer's protest to the imposition of use tax on its August 24, 2011, purchase of a transformer–which the auditor described as "H-D 23-28-275-6 7.5 KVA 120/240" (p. 27 of audit report) is sustained, as discussed in subpart S. However, Taxpayer's protest to the imposition of tax on all of the other purchases is respectfully denied, as discussed in the other subparts not specifically listed above.

II. Sales and Use Tax–Environmental Exemption.

DISCUSSION

All tax assessments are presumed to be accurate; the taxpayer bears the burden of proving that an assessment is incorrect. IC § 6-8.1-5-1(b).

The Department determined that use tax was due on the purchases of a "cooling tower filter," "85 ppm propane nitrogen," and a spool assembly that Taxpayer had made without paying sales tax. As stated previously, Indiana imposes "an excise tax, known as the use tax," on tangible personal property that is acquired in retail transactions and is stored, used, or consumed in Indiana. IC § 6-2.5-3-2(a). Taxpayer maintains that the purchases were made to comply with environmental standards and are exempt under IC § 6-2.5-5-30.

IC § 6-2.5-5-30, in relevant part, provides:

> Sales of tangible personal property are exempt from the state gross retail tax if:
>
> (1) the property constitutes, is incorporated into, or is consumed in the operation of, a device, facility, or structure predominately used and acquired for the purpose of complying with any state, local, or federal environmental quality statutes, regulations or standards; and
>
> (2) the person acquiring the property is engaged in the business of manufacturing, processing, refining, mining, or agriculture.

(Emphasis added).

A. "Cooling Tower Filter."

Taxpayer maintains that the "cooling tower filter" was purchased for the "cooling tower" which is part of Taxpayer's "dust collection system." Taxpayer asserts that the Indiana Department of Environmental Management ("IDEM") required Taxpayer to install the "dust collecting system" before Taxpayer could receive a "Title V Environmental Permit" from the Environmental Protection Agency under Title V of the Clean Air Act. See Clean Air Act, 42 U.S.C. § 7401, et seq. (2007) & 40 C.F.R. § 70.1, et seq. (2007). Taxpayer states:

> [T]he water cooling tower . . . is part of a system that pumps water to the dust recycling system. It supplies water to the nozzles in the conditioning tower. We believe that this function means that the cooling tower and its components are incorporated into the function of a facility required by the EPA.

During the hearing process, Taxpayer was asked to present the statutes and/or written requirements from IDEM that Taxpayer purchase "cooling tower filter." However, the consent decree Taxpayer presented does not mention the "cooling tower filter." The Department through its own research found where IDEM required the purchase of "cooling tower filters." Therefore, the cooling tower filter was purchased to comply with an environmental quality standard and is exempt from sales and use tax under the "environmental exemption" as defined in IC § 6-2.5-5-30.

Accordingly, Taxpayer's protest to the imposition of tax on its January 12, 2010, purchase of a cooling tower filter (p. 27 of the audit report) is sustained.

B. "85 PPM Propane Nitrogen."

The Department determined that Taxpayer's $246.82 purchase of "85 ppm propane nitrogen" was subject to use tax because it was used to process raw materials prior to their entry into production. Taxpayer maintains that the "85 ppm propane nitrogen" is required by an Environmental Protection Agency regulation and is exempt as a purchase required for pollution control. Taxpayer states that this nitrogen is a certified calibration gas used daily on the kilns to monitor gas emission concentrations. Taxpayer further asserts that the Environmental Protection Agency requires this type of monitoring pursuant to 40 CFR 63.1209.

Taxpayer has provided sufficient documentation to support Taxpayer's assertion that the "85 ppm propane nitrogen" was purchased to comply with the gas emission monitoring pursuant to 40 CFR 63.1209 and is exempt from sales and use tax under the "environmental exemption" as defined in IC § 6-2.5-5-30.

Accordingly, Taxpayer's protest to the imposition of tax on its April 29, 2011, $246.82 purchase of "85 ppm propane nitrogen" (p. 15 of the audit report) is sustained.

C. "Baghouse: Spool Assembly."

Taxpayer asserts that the "spool assembly" is part of the drop out chamber screw installed to repair the "baghouse." Taxpayer maintains that the Indiana Department of Environmental Management ("IDEM") required Taxpayer to install the "baghouse" to comply with "Title V Environmental Permit" requirements of the Environmental Protection Agency under Title V of the Clean Air Act. See Clean Air Act, 42 U.S.C. § 7401, et seq. (2007) & 40 C.F.R. § 70.1, et seq. (2007). Taxpayer reasons that since the "baghouse" is required by an Environmental Protection Agency regulation and therefore a part purchased to repair the "baghouse" is exempt as a purchase required for pollution control.

During the protest, Taxpayer presented a consent decree from IDEM requiring Taxpayer to purchase the "baghouse." Taxpayer has provided sufficient documentation to support Taxpayer's assertion that the "spool assembly" purchased for the "baghouse" was required to comply with an environmental quality standard and is exempt from sales and use tax under the "environmental exemption" as defined in IC § 6-2.5-5-30.

Accordingly, Taxpayer's protest to the imposition of tax on its September 23, 2010, purchase of a spool assembly (p. 23 of the audit report) for the baghouse is sustained.

FINDING

Taxpayer's protest is sustained. Taxpayer's protest to the imposition of tax on its January 12, 2010, purchase of a cooling tower filter (p. 27 of the audit report) is sustained, as discussed in subpart A. Taxpayer's protest to the

imposition of tax on its April 29, 2011, $246.82 purchase of "85 ppm propane nitrogen" (p. 15 of the audit report) is sustained, as discussed in subpart B. Taxpayer's protest to the imposition of tax on its September 23, 2010, purchase of a spool assembly (p. 23 of the audit report) for the baghouse is sustained, as discussed in subpart C.

III. Sales/Use Tax–Imposition.

DISCUSSION

All tax assessments are prima facie evidence that the Department's claim for the tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

The Department found that use tax was due on Taxpayer's January 14, 2009, $12,866.25 purchase–which the auditor described as "plc controller/energy saving device" (p. 8 of audit report). Taxpayer maintains that this purchase was actually made during 2008 and therefore cannot be included in the audit. The Department's audit used the information from Taxpayer's accounting system to determine the sample population. Taxpayer claims that when it originally entered this invoice in its accounting system, Taxpayer mistakenly entered the invoice date as January 14, 2009. Since the date of the transaction was entered as January 14, 2009, in Taxpayer's accounting system, the Department included this purchase as part of the sample population for the audit of the 2009 to 2011 tax years.

During the protest, Taxpayer presented the invoice for this transaction. The invoice was dated January 14, 2008. Therefore, since the date of the transaction is actually January 14, 2008, this transaction cannot be included in the Department's audit of 2009 to 2011 tax years. Thus, the audit division is requested to remove the item from the sample population and to adjust the calculations accordingly.

FINDING

Taxpayer's protest to the Department's inclusion of its purchase of a "plc controller/energy saving device" (p. 8 of audit report) is sustained.

IV. Sales and Use Tax–"Contractor Services."

DISCUSSION

The Department found that Taxpayer purchased tangible personal property without paying sales tax at the time of purchase, and assessed use tax on the purchases. Pursuant to IC § 6-8.1-5-1(c), all tax assessments are presumed accurate, and the taxpayer bears the burden of proving that an assessment is incorrect.

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A person who acquires tangible personal property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b). Indiana also imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). In general, all purchases of tangible personal property are subject to sales and/or use tax. An exemption from use tax is granted for transactions where sales tax was paid at the time of the purchase pursuant to IC § 6-2.5-3-4. In certain circumstances, additional enumerated exemptions from sales and/or use tax are available.

Taxpayer maintains that the Department incorrectly assessed use tax on its purchases from two "service contractors:" "Contractor A" and "Contractor F."

A. "Contractor A."

The Department found that use tax was due on Taxpayer's March 31, 2009, purchases from "Contractor A" where the auditor described the purchases as "misc parts for smoke/heat detection systems" (p. 8 of the audit report). At the time of the audit, the Department was unable to verify the nature of the transactions. Therefore, as Taxpayer had not paid sales tax at the time of the transactions, the Department assessed use tax on the purchases. As stated previously, Indiana imposes "an excise tax, known as the use tax," on tangible personal property that is acquired in retail transactions and is stored, used, or consumed in Indiana. IC § 6-2.5-3-2(a).

Taxpayer asserts that the Department's assessment of use tax on the two purchases from "Contractor A" is incorrect because these are service transactions that are exempt from use tax. Taxpayer maintains that the invoiced amount represents a charge "for labor only." During the hearing process, Taxpayer provided purchase orders and invoices for the two transactions in question.

However, based upon the documentation provided, the transactions in question were not "labor only" service transactions as the Taxpayer suggests. The purchase orders and invoices provided demonstrate that the transactions represent the payment of one "lump sum" amount for each transaction that covers the provision of 1 unit–i.e., the smoke/heat detection system–and the requisite number of hours to complete the installation of that unit. Therefore, the transactions in question represent "lump sum" payments for "improvements to reality."

The Department refers to 45 IAC 2.2-4-21, which states:

(a) In general, all sales of tangible personal property are taxable, and all sales of real property are not taxable. The conversion of tangible personal property into realty does not relieve a liability for any owing and unpaid state gross retail tax or use tax with respect to such tangible personal property.

(b) All construction material purchased by a contractor is taxable either at the time of purchase, or if purchased exempt (or otherwise acquired exempt) upon disposition unless the ultimate recipient could have

purchased it exempt (See 6- 2.5-5 [45 IAC 2.2-5]).

Additionally, 45 IAC 2.2-3-7, in relevant part, explains:

(a) Contractors. For purposes of this regulation [45 IAC 2.2] "contractor" means any person engaged in converting construction material into realty. The term "contractor" refers to general or prime contractors, subcontractors, and specialty contractors, including but not limited to persons engaged in building, cement work, carpentry, plumbing, heating, electrical work, roofing, wrecking, excavating, plastering, tile and road construction.

(b) Construction material. For purposes of this regulation [45 IAC 2.2], "construction material" means any tangible personal property to be used for incorporation in or improvement of a facility or structure constituting or becoming part of the land on which such facility or structure is situated.

Also, 45 IAC 2.2-4-22(d)-(e), states:

(d) Disposition subject to the state gross retail tax. A contractor-retail merchant has the responsibility to collect the state gross retail tax and to remit such tax to the Department of Revenue whenever he disposes of any construction material in the following manner:

(1) Time and material contract. He converts the construction material into realty on land he does not own and states separately the cost for the construction materials and the cost for the labor and other charges (only the gross proceeds from the sale of the construction material are subject to tax); or

(2) Construction material sold over-the-counter. Over the counter sales of construction materials will be treated as exempt from the state gross retail tax only if the contractor receives a valid exemption certificate issued by the person for whom the construction is being performed or by the customer who purchases over-the-counter, or a direct pay permit issued by the customer who purchases over-the-counter.

(e) Disposition subject to the use tax. With respect to construction material a contractor acquired tax-free, the contractor is liable for the use tax and must remit such tax (measured on the purchase price) to the Department of Revenue when he disposes of such property in the following manner:

(1) He converts the construction material into realty on land he owns and then sells the improved real estate;

(2) He utilizes the construction material for his own benefit; or

(3) Lump sum contract. He converts the construction material into realty on land he does not own pursuant to a contract that includes all elements of cost in the total contract price.

A disposition under C. [subsection (e)(3) of this section] will be exempt from the use tax if the contractor received a valid exemption certificate from the ultimate purchases (purchaser) or recipient of the construction material (as converted), provided such person could have initially purchased such property exempt from the state gross retail tax.

(Emphasis added).

Generally, in a lump sum contract between a customer and its contractor, the contractor bears responsibility for paying the tax on the construction materials. In a time and materials contract between a customer and its contractor, the contractor acts as a retail merchant and sales or use tax is due from the contractor's customers on the cost of the materials.

Sales Tax Information Bulletin 60 (July 2006), 20060823 Ind. Reg. 045060287NRA, defines a "lump sum contract" as "a contract in which all of the charges are quoted as a single price." On the other hand, a "time and materials contract" is defined as "a contract in which all charges for labor, construction materials and other items are separately stated." Id. "'Construction materials' means any tangible personal property to be used for incorporation in or improvement of a facility or structure constituting or becoming part of realty. Id. "Examples of installations that constitute improvements to realty are: doors, garage doors, garage door openers, windows, cabinets, garbage disposals, water heaters, water softeners, alarms, furnaces, central air conditioning units, gutters, and carpeting." Id.

In Taxpayer's situation, the installation of "heat detection systems" into realty by a "construction contractor" would qualify as "improvements to realty." Since, based upon the documentation presented, these "improvements to realty" were billed on a "lump sum" basis, the "construction contractor" was liable for the payment of tax upon the materials used.

Accordingly, upon reviewing the documentation, Taxpayer's protest to the imposition of tax on the two transactions with "Contractor A" on March 31, 2009, for "heat detection systems" (p. 8 of the audit report) is sustained.

B. "Contractor F."

The Department found that use tax was due on Taxpayer's purchases from "Contractor F" where the auditor described the purchase as the materials portion of a time and materials contract for the "installation of smoke/heat detectors" (p. 8 of the audit report) and the "materials portion of a fire suppression system" (p.10 of the audit report). Taxpayer asserts that the Department's assessment of use tax on the "Contractor F" purchases is incorrect because these are for materials and services billed under a "lump sum" contract for which Taxpayer is not properly subject to use tax. During the hearing process, Taxpayer provided a "quote" and two payment invoices for the two transactions in question.

In Taxpayer's situation, the installation of "smoke/heat detectors" and a "fire suppression system" into realty by a "construction contractor" would qualify as "improvements to realty." However, based upon the documentation provided, the transactions in question were not billed under "lump sum" contracts as the Taxpayer suggests. The quote, while incomplete, provided for the payment of sales tax on the materials and the invoices that followed showed payments for the materials and labor supplied to the taxpayer listed separately. Therefore, based upon the documentation presented, the transactions in question were billed under a "time and materials" contract for "improvements to reality." Since, based upon the documentation presented, these "improvements to realty" were billed on a "time and materials" basis, the contractor acts as a retail merchant and sales or use tax is due from the contractor's customers on the cost of the materials under 45 IAC 2.2-4-22(d)(1). Thus, Taxpayer's purchase of the materials provided under the contract is subject to sales and use tax.

Accordingly, Taxpayer's protest to the imposition of use tax on the materials provided to install "smoke/heat detectors" and a "fire suppression system" by "Contractor F" is respectfully denied.

FINDING

Taxpayer's protest is denied in part and sustained in part. Taxpayer's protest to the imposition of tax on the two transactions with "Contractor A" on March 31, 2009, for "heat detection systems" (p. 8 of the audit report) is sustained, as discussed in subpart A. However, Taxpayer's protest to the imposition of use tax on the materials provided to install "smoke/heat detectors" and a "fire suppression system" by "Contractor F" is respectfully denied, as discussed in subpart B.

SUMMARY

Taxpayer's protest is denied in part and sustained in part.

• Manufacturing Exemption Issue: Taxpayer's protest to the imposition of use tax on its January 30, 2009, purchase of "bearings; gen. tach; misc parts" for the slurry tank is sustained, as discussed in Issue I(D). Taxpayer's protest to the imposition of tax on its June 19, 2009, "maintenance agreement" purchase (p.19 of the audit report) for software for the "CBX X-Ray Machine" is sustained, as discussed in Issue I(E). Taxpayer's protest to the imposition of use tax on its March 16, 2010, purchase of "hi-vol roller bearings" (p. 20 of the audit report) for the idler roll is sustained, as discussed in Issue I(J). Accordingly, Taxpayer's protest to the imposition of use tax on its October 27, 2009, purchase of a flowmeter (p. 19 of the audit report) is sustained, as discussed in Issue I(K). Taxpayer's protest to the imposition of use tax on its August 24, 2011, purchase of fuses (p. 23 of the audit report) for the crusher is sustained, as discussed Issue I(O). Taxpayer's protest to the imposition of use tax on its December 7, 2011, purchase of "petron gear shield nc lubricant" (p. 21 of the audit report) for the kiln drive is sustained, as discussed in Issue I(P). Taxpayer's protest to the imposition of use tax on July 30, 2009, purchase of ball valves (p. 27 of audit report) for the "v-ball controller housing" is sustained, as discussed in Issue I(R). Taxpayer's protest to the imposition of use tax on its August 24, 2011, purchase of a transformer–which the auditor described as "H-D 23-28-275-6 7.5 KVA 120/240" (p. 27 of audit report) is sustained, as discussed in Issue I(S). However, Taxpayer's protest to the imposition of tax on all of the other purchases is denied.

• Environment Exemption Issue: Taxpayer's protest is sustained. Taxpayer's protest to the imposition of tax on its January 12, 2010, purchase of a cooling tower filter (p. 27 of the audit report) is sustained, as discussed in subpart A. Taxpayer's protest to the imposition of tax on its April 29, 2011, $246.82 purchase of "85 ppm propane nitrogen" (p. 15 of the audit report) is sustained, as discussed in subpart B. Taxpayer's protest to the imposition of tax on its September 23, 2010, purchase of a spool assembly (p. 23 of the audit report) for the baghouse is sustained, as discussed in subpart C.

• Imposition Issue: Taxpayer's protest to the Department's inclusion of its purchase of a "plc controller/energy saving device" (p. 8 of audit report) is sustained, as discussed in Issue III.

• Contractor Services Issue: Taxpayer's protest to the imposition of tax on the two transactions with "Contractor A" on March 31, 2009, for "heat detection systems" (p. 8 of the audit report) is sustained, as discussed in Issue IV(A).

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