



MAINE REVENUE SERVICES SALES, FUEL & SPECIAL TAX DIVISION INSTRUCTIONAL BULLETIN NO. 22

MANUFACTURERS

This Bulletin is intended solely as advice to assist persons in determining, exercising or complying with their legal rights, duties or privileges. It contains general and specific information of interest as well as interpretations and determinations by Maine Revenue Services regarding issues commonly faced by your business. Portions of the Sales and Use Tax Law referred to in this bulletin can be found at the end of the bulletin in Attachment #1. Also attached are applicable Sales and Use Tax Rules. Particular attention should be given to Maine Revenue Services Rule 303 (“Sales to Industrial Users”).

The purpose of this bulletin is to provide guidance to all manufacturers, both large and small, regarding the scope of the relevant sales and use tax exemptions found in Title 36 M.R.S.A., §1760. As you read the bulletin, you should bear in mind that the burden of proving that a purchase qualifies for exemption rests with the purchaser.

This bulletin is not intended to be all-encompassing. As a result, it may not be specific enough to address every situation encountered by any particular manufacturer. More detailed information should be requested in writing from the Sales/Excise Tax Division.

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I. PRODUCTION DEFINED

The term “manufacturer” means an entity that is engaged in the production of tangible personal property for later sale or lease. The question of exactly what is and what is not “production” has great importance when considering the sales and use tax exemptions available to manufacturers. The term is defined in §1752(9-B) of the statute as follows:

9-B. Production. “Production” means an operation or integrated series of operations engaged in as a business or segment of a business that transforms or converts personal property by physical, chemical or other means into a different form, composition or character from that in which it originally existed.

“Production” includes manufacturing, processing, assembling and fabricating operations that meet the definitional requisites, including biological processes that are part of an integrated process of manufacturing organisms or microorganic materials through the application of biotechnology.

“Production” does not include biological processes except as otherwise provide by this subsection, wood harvesting operations, the severance of sand, gravel, oil, gas or other natural resources produced or severed from the soil or water, or activities such as cooking or preparing drinks, meals, food or food products by a retailer for retail sale. The foregoing are examples of activities that are not included within the term “production.”

In summary, in order for “production” to exist, a business must be engaged, in whole or in part, in the transformation of raw materials into a new and different product. Some common examples are:

- A paper mill converting wood chips into paper.
- A wood crafter converting lumber into finished furniture.
- A seamstress converting cloth material into a dress.

A. WHEN PRODUCTION BEGINS

The point at which production begins depends on whether or not the raw materials used in the production process are stored. If the materials are stored, production begins with the movement of the materials from storage to the first production machine. If the materials are not stored, production begins with the movement of the materials from point of delivery to the first production machine.

For example, a manufacturer of furniture receives rough sawn lumber and stores this lumber in a warehouse. The first production machine for this manufacturer will likely be a planer. Production begins when the rough lumber is removed from storage and brought to the planer. If this movement to the planer is accomplished mechanically, the machine in question is considered to be used in production.

In another example, a manufacturer of plastic widgets stores its plastic pellets in storage tanks. The first production machine is machinery that melts down the pellets into a liquid form. Production begins when the plastic pellets move toward the melting machine. If this is accomplished through a piping system, for instance, production begins when the pellets leave the storage tank and the piping system is considered part of production.

B. WHEN PRODUCTION ENDS

Production ends with the completion of the finished product before the product is stored for later delivery. This may include packaging operations – but only those that are part of a series of operations with the production line and the packaging is performed before the product is stored. Packaging operations that occur after the product has been placed in storage or that occur within the storage facility are not part of production.

For example, if a manufacturer of videotapes has within its production line a machine that inserts the tapes into a cardboard sleeve and shrink-wraps each individual tape, this packaging operation is part of production. In contrast, if the tapes are instead sent to a storage room and later shrink-wrapped into packages of 10 and inserted into cardboard boxes for shipping to customers, this later packaging operation is not part of production.

C. EXCLUSIONS FROM “PRODUCTION”

Machinery and equipment used in certain activities or operations is excluded from the definition of “production” for purposes of the Sales and Use Tax Law and as a result is taxable unless covered by a different exemption. Items used primarily in the following functions are not considered to be used in production and therefore generally **do not** qualify for exemption:

1. Acquisition of raw materials. Machinery or equipment used in the acquisition of raw materials, including wood-harvesting operations and severing sand, gravel, or other natural resources from soil or water.

Examples of taxable items: Cameras used by newspaper photographers to record images on film for later selection and use in newspaper production; chain saws used to harvest wood for subsequent milling; excavation equipment used to extract clay from which bricks are later formed.

2. Storage and handling (pre- and post-production). Machinery or equipment used in the storage or handling of exempt material prior to the movement of the materials between point of receipt or storage area and the first production operation, or after the completion of any in-line packaging operation.

Examples of taxable items: A crane used primarily to unload logs from trucks into storage piles, prior to movement of the logs to a debarker or pulp grinder; an ice machine used primarily to keep fresh food cold during delivery, rather than to chill or freeze food as a step in the processing; a forklift used primarily to move palletized product from the palletizer to a warehouse pending shipment.

3. Product transportation/distribution. Machinery or equipment used in the transportation of product on public ways between different production sites, or in the distribution of product to customers.

Examples of taxable items: A truck used to carry packaged product to customers.

4. Biological processes. Machinery or equipment used in connection with biological processes. A biological process is a natural process that occurs with little or no intervention from humans or machinery.

Examples of taxable items: Equipment used in the hatching of eggs or in the growing of crops. (But see Part II, Section I for information on an exception to this rule in the case of biotechnology.)

5. Activities by a retailer in connection with the preparation of food to be sold by the retailer. Machinery or equipment used by a retailer in the preparation of food to be sold by the retailer.

Examples of taxable items: Refrigerators, ovens and blenders used by a restaurant in the preparation of meals.

6. Administrative functions. Machinery or equipment used in administrative, personnel, security, inventory control, administrative record keeping, ordering, billing, or similar support functions.

Examples of taxable items: Computers used primarily for billing, payroll and business correspondence; telephone systems; security cameras.

7. Quality control. Machinery or equipment used for quality control purposes (other than as described in Part II, section A(4)(g)).

8. Maintenance/cleaning. Machinery or equipment used to clean, repair, or maintain real or personal property in the manufacturing facility (other than attachments to exempt machinery and equipment described in Part II, section A(4)(e) below).

Examples of taxable items: A floor polishing machine; welding equipment used to repair production piping; equipment used to sharpen the blades of saws used at a lumber mill; brooms and other cleaning supplies.

9. Safety/fire protection. Machinery or equipment used for fire protection or the protection and safety of workers or other persons (unless the equipment is attached to or incorporated into exempt machinery and equipment).

Examples of taxable items: A plexiglass screen (not attached to exempt equipment) used to protect passing workers and visitors from flying debris; fire extinguishers and fire sprinkler systems; an emergency shower and eyewash station; security systems; standard safety clothing and other standard safety items worn by employees.

10. Non-specialized environmental controls (lighting, HVAC, etc.). General plant lighting, heating, ventilation, air conditioning, or similar environmental control designed for the

comfort or convenience of employees. (See Part II, section A(4)(i) below regarding specialized environmental control items essential to a particular production process).

Examples of taxable items: *A general building HVAC system used to cool and ventilate a room where wood workers assemble furniture; an office humidifier; thermostats used to control a boiler used primarily to heat a building.*

11. Certain electrical equipment. Electrical equipment located prior to the last transformer at the manufacturing facility that steps electricity up or down to the voltage at which the electricity is primarily used by other exempt machinery and equipment, when the electricity has been purchased from or supplied by another person, except as provided in Part II, section (A)(4)(j) below.

Examples of taxable items: *In a meat packing plant that receives 34.5KV electricity from the grid and steps the electricity down with its own transformer to 12KV, then transmits the electricity with its own wires to a second transformer that reduces the voltage to 480 volts for use at that voltage by its production machinery, the first transformer would be taxable (the second transformer would be exempt).*

II. EXEMPTIONS

The Maine Sales and Use Tax Law provides the following categories of exemptions to manufacturers:

- A. Machinery and Equipment Used in Production
- B. Ingredients (Raw Materials)
- C. Items that are Consumed or Destroyed
- D. Fuel and electricity
- E. Water Pollution Control Facilities
- F. Air Pollution Control Facilities
- G. Machinery and Equipment Used in Research

A. MACHINERY AND EQUIPMENT USED IN PRODUCTION

The exemption for production machinery and equipment found in §1760(31) sets forth a number of requirements. The item being purchased must fall within the statutory definition of “machinery and equipment.” The machinery or equipment in question must be (i) purchased for use by the purchaser; (ii) purchased for use **primarily** in production; (iii) purchased for use **directly** in production; and (iv) purchased for use in producing *tangible personal property* that is *intended to be sold or leased* ultimately for final use or consumption.

1. Machinery and equipment. The term “machinery and equipment,” as defined in §1752(7-B), includes both new and used machinery and equipment as well as parts and attachments for such machinery and equipment. (All parts are included, including repair and replacement parts).

The statutory definition excludes foundations for machinery and equipment that are permanent supports, such as most foundations composed of concrete. (Foundations that can be dismantled and moved, such as many steel supports, are considered part of the machinery and equipment that they support.) Also excluded from “machinery and equipment” are so-called “special purpose buildings” used to house or support machinery and equipment.

Examples of taxable items:

- Permanently affixed concrete pillars on which a piece of production machinery sets do not qualify as exempt machinery and equipment.
- A kiln that houses machinery and equipment used in the drying of finished lumber is a special purpose building and does not qualify as exempt machinery and equipment (in contrast to the piping, controls and other equipment within the walls of the kiln, which does qualify as exempt machinery and equipment).

Examples of exempt items:

- Angle iron used to construct a support frame is exempt, provided the machinery or equipment it supports qualifies as production machinery or equipment.
- A movable concrete base is exempt, provided the machinery or equipment it supports qualifies as production machinery or equipment.

2. Use by the purchaser. The purchaser of the machinery and equipment must also be the *user of machinery and equipment in the production process* in order to qualify for the exemption. Lessors of machinery and equipment under a true lease are not entitled to an exemption even though the lessee is using the machinery and equipment in production. The taxable “use” by the purchaser/lessor in this situation is the derivation of income through the leasing of the equipment. (But see the exception for “sale/leaseback” transactions, explained at Part III, Section A of this bulletin.)

In another example, if a subsidiary of the manufacturer purchases equipment and allows the parent manufacturer to use it in the manufacturer’s own production, the subsidiary does not enjoy the exemption since, as the purchaser, the subsidiary is not the user of the equipment in production.

3. Use primarily in production. “Primarily” is defined in §1752(9-A) to mean more than 50% of the time. Thus, if an item of machinery or equipment has multiple uses, it must be used in an exempt activity more than 50% of its time in operation in order to qualify as exempt production machinery. For instance, a forklift may be used not only to move work in process between production machines, but also to load delivery vehicles, or to move raw material from one storage location to another storage location. In this example, only the time used in moving the “work in process” would qualify as “use in production.” The amount of time in this function would need to exceed 50% of its total use in order for the forklift to be exempt as “primarily” used in production.

4. Use directly in production. “Directly” is defined in §1752(2-A) as including operations that are “integral and essential to production,” as contrasted with activities that are “simply incidental, convenient or remote to production.” For instance, a wood planer in a

furniture manufacturer's facility is clearly essential to the production of the finished furniture, while items in a machine shop used to maintain and repair production machinery are only "incidental" to production and are therefore not exempt. The term "directly" does not include support operations. Machinery and equipment used in the following operations is therefore taxable:

- Administrative operations;
- Storage and warehouse operations;
- Maintenance operations (including not only those operations occurring in an area devoted solely to maintenance, but also maintenance activities occurring in the production area itself);
- Receiving and shipping operations;
- Heating and lighting, including in production areas (except as provided in (i) below);
- Safety and fire protection (including those activities required by state or federal agencies); and
- Transportation on public ways between production sites.

The following is a non-exclusive list of activities considered to be "directly" in production:

(a) Acting on raw materials. The processing of raw material at the production site, or the holding of raw material as it is being processed.

Examples: A wood planer acting on rough lumber to plane and reduce thickness; machinery that mixes raw materials before the raw material is added to the production line; a printing press that acts upon paper and ink in producing a printed product for sale; a rock crusher that crushes rock which is then further processed in a kiln as a part of the manufacture of cement for sale; a freezer used to flash-freeze vegetables in the production of frozen vegetables for sale.

(b) Processing or holding exempt materials. The processing of other exempt materials, or holding of such materials as they are being processed, so that they or the materials resulting from the processing can be used or reused in a production process or in connection with the operation of exempt machinery or equipment. As used in this Bulletin, "exempt materials" means work in process and materials the purchase of which by the taxpayer would be exempt in whole or in part under 36 MRSA §1760(9-D) (fuel and electricity used at a manufacturing facility), 36 MRSA §1760(9-G) (fuel oil or coal, the by-products from the burning of which become an ingredient or component part of tangible personal property for later sale), or 36 MRSA §1760(74) (property that becomes an ingredient or component part of, or that is consumed or destroyed or loses its identity in production of, tangible personal property) and may include without limitation raw materials, electricity, fuel, water, ice, steam, air, oil, gas, chemicals, gases, catalysts, grinding or blasting materials, reagents, lubricants, solvents, acids, printing plates, color separations, tagging materials and other substances and materials used in connection with the operation of exempt machinery and equipment.

Examples: *A lime kiln that prepares chemicals for use in a kraft pulping process at a paper manufacturing facility; equipment that deionizes or demineralizes water for use by other exempt machinery and equipment; a chipper for wood used to fuel a boiler used to supply steam or electricity to saws and planers at a lumber mill.*

(c) Handling or moving exempt materials. The handling, moving or transmitting of exempt materials from one production machine to another; or between a storage area (or point of receipt if there is no storage) and the first production operation; or between a production operation and a temporary holding area prior to further production operations. (However, transportation of raw materials or work in process on public ways between different production sites is not considered an activity “directly” in production.)

Examples: *A forklift used to move lumber from planer to sanding machine; a conveyor system that moves work in process from one production machine to another, or from a storage pile at the point of receipt to the first production machine; piping used to move oil from a storage tank to a boiler used to generate electricity to power the other exempt machinery and equipment at a potato processing plant; conveyors used to move lime from storage at the point of receipt to a lime kiln used to prepare chemicals for use in a kraft pulping process at a paper manufacturing facility.*

(d) Protection or temporary holding of exempt materials or work in process. Machinery and equipment that preserves, protects, or temporarily holds exempt materials (including work in process) between different production operations or that is used to temporarily hold exempt materials. “Temporary holding” as used in this Bulletin includes (1) equipment or functions designed to avoid delays in production resulting from reasonably anticipated fluctuations in rate of supply or use of the stored items, and (2) equipment such as a tank, chest or tower used to hold exempt material previously processed and awaiting delivery to other production equipment for further processing or use. An item of equipment is presumed to be for “temporary holding” if it holds work in process or exempt material only for periods of less than 24 hours.

Examples: *Steel racks used in temporary holding of finished lumber that is to be sized and cut; a holding tank used in temporary holding of raw material between two production machines; racks or “skids” used by a printer in the temporary holding of pages of printed material pending printing of additional pages, inserts or covers needed to produce the final product; bins used in sorting and temporary holding of yarns produced by a fabric manufacturer for subsequent use in weaving fabric; a tank used to hold a 12-hour supply of an exempt process chemical for use in the event of an interruption of supply.*

(e) Removal of waste products from production machinery. Removal of waste or by-products from the immediate vicinity of exempt machinery and equipment, for the purpose of permitting that machinery and equipment to operate continuously.

Examples: *A conveyor used to remove chips and sawdust from the planer; an ash grate for a boiler used to produce steam and electricity to power manufacturing equipment at the same facility; a blanket wash application system for a printing press; a dryer hood and exhaust fan used to remove excessive moisture from a production machine.*

(f) Control of exempt production machinery. Manually or automatically controlling, or monitoring for the purpose of manually or automatically adjusting or controlling, the operation of exempt production machinery.

Examples: Process control computers, such as a computer that controls the cuts of a band saw; a temperature gauge for a boiler that produces steam or electricity used by other exempt equipment; a valve used to control the flow of gas used in welding; a camera used to monitor the shape of the plume of flame in a kiln used in a production operation to ensure that the kiln is functioning properly.

(g) Testing or monitoring. Testing or monitoring exempt materials (including work in process) if the equipment used for this purpose is physically attached to exempt machinery and equipment, or is used to test every item or batch of product or exempt material.

Examples: A moisture meter that verifies the moisture content of 100% of the lumber used in making furniture; a chart recorder used to monitor the pH of water to be used in process or work in process held within a tank; a color density meter used to determine whether each batch of product meets color specifications for top grade product; a full volume detector used to ensure that the product container is properly filled and sealed.

(h) In-line packaging operations (pre-storage). Packaging operations that are part of a series of operations within the production line and that are performed before the final product is stored. (As noted in section I-C above, packaging operations that occur after the product has been placed in storage or that occur within a separate storage facility are not part of production.)

Examples: Machinery and equipment used to insert a videotape into a cardboard sleeve and shrink-wrap it; equipment used to sort and count product for packaging; equipment used to box, bottle, can, or label product.

(i) Machinery and equipment that controls the production environment. Controlling the production environment by means of *specialized* plant lighting, ventilation, air purification or prevention of contamination, humidity or temperature regulation, or similar environmental control essential to a particular production process.

Examples: Air handling equipment used for a “clean room” in a computer chip manufacturing facility; equipment used to reduce contamination or to control temperature and humidity in a clean room; equipment used to monitor air quality in a clean room; air conditioning equipment connected or otherwise directed to computers used to control a manufacturing process; thermometers and humidity meters used to monitor the environment for process control computers or exempt electrical equipment.

(j) Certain electrical equipment. The last transformer at the manufacturing facility that steps electricity up or down to the voltage at which the electricity is primarily used by other exempt machinery and equipment, and wiring, switches and other electrical equipment between that transformer and other exempt machinery and equipment; and machinery and equipment used to avoid electrical damage to such transformer or other exempt machinery and equipment or to

ensure uninterrupted power supply to exempt machinery and equipment, including by means of providing back-up or emergency power or surge protection.

Examples: *In a meat packing plant that receives 34.5KV electricity from the grid and steps the electricity down with its own transformer to 12KV, then transmits the electricity with its own wires to a second transformer that reduces the voltage to 480 volts for use at that voltage by its production machinery, the second transformer would be exempt.*

5. Tangible personal property intended for sale or lease. To be eligible for exemption, machinery or equipment must be used in the production of tangible personal property that is intended to be sold or leased ultimately for final use or consumption. “Tangible personal property” is defined in §1752(17) as something that can be seen, touched or perceived by the senses. The definition specifically includes electricity.

The product being produced must also be sold or leased *as tangible personal property*. Machinery and equipment used to produce property that will be sold as *real property*, or that will be used by the producer rather than sold, does **not** qualify for exemption. (For more on this topic, see Instructional Bulletin No. 28, “Installing Tangible Personal Property in Real Property.”)

Examples:

- A cabinetmaker who produces and installs kitchen cabinets and passes title to the cabinets after installation, is selling real property, not tangible personal property. The cabinetmaker’s purchase of machinery and equipment thus does *not* qualify for exemption.
- A cabinetmaker who produces and installs kitchen cabinets and passes title to the cabinets **before** installation is engaged in selling tangible personal property. The cabinetmaker’s purchase of machinery and equipment would therefore qualify for exemption.
- A retailer that manufactures free-standing shelving units for its own use is not selling the shelves. The retailer’s purchase of machinery and equipment to build the shelves does not qualify for exemption.

B. INGREDIENTS OR COMPONENT PARTS

Section 1760(74) provides an exemption for tangible personal property, other than fuel or electricity, that becomes an ingredient or component part of the item being produced. This category includes all raw materials that get physically converted into, or physically attached to the finished product, including tags and labels.

C. ITEMS THAT ARE CONSUMED OR DESTROYED

Section 1760(74) of the law provides a separate tax exemption for tangible personal property, other than fuel or electricity, that is consumed or destroyed or loses its identity in the production process. These are items that have a normal life expectancy of less than one (1) year

in the use to which they are applied. An item that is obsolete only over a longer period of time is not considered “consumed or destroyed.” Maine Revenue Services Rule 303 provides additional guidance on this topic.

Examples of items that are consumed or destroyed in the production process:

- Items that are essential to the operation of production machinery and equipment, such as lubricants;
- Items that come in contact with raw material but does not become part of the finished product, such as solvents.
- Items that come in contact with raw material and are no longer of use afterwards, such as sandpaper.

Examples of items that are **not** consumed or destroyed in the production process:

- Items that are consumed or destroyed before production begins, such as lubricants for a chain saw used to harvest trees to be manufactured into lumber;
- Items that are consumed or destroyed after production ends, such as lubricants for a forklift used primarily to move finished product from storage to trucks for shipment to customers.
- Items that are not used “directly” in production.

D. FUEL AND ELECTRICITY

Section 1760(9-D) of the Sales and Use Tax Law provides a partial exemption for fuel and electricity used at a “manufacturing facility.” 95% of the cost of the fuel and electricity is exempt, while the remaining 5% is subject to the general sales tax rate.

A manufacturing facility, as defined in §1752(6-A), is a site where production machinery is located. This includes not only the machinery and equipment used directly in production, but all machinery, equipment, structures and facilities located at the site and used in support of production or associated with the production. As a result, if a site includes production machinery, all fuel and electricity used at that site is eligible for the partial exemption. Separate electric meters, fuel tanks or heating systems need not be maintained for the purpose of separating production areas from non-production areas.

A manufacturing facility does not include a site at which a retailer is primarily engaged in making retail sales of items that it does not produce itself. Thus, for example, a hardware store is not a “manufacturing facility,” and is not entitled to the 95% energy exemption, merely because it has a key cutting machine on the premises.

This partial sales tax exemption applies to all types of fuel, including #2 heating fuel, diesel fuel, oxygen, acetylene, and wood chips.

E. WATER POLLUTION CONTROL FACILITIES

Section 1760(29) of the law provides an exemption for water pollution control facilities. In order to qualify for this exemption, a facility must be certified by the Commissioner of the Department of Environmental Protection (DEP) as a facility that is engaged in disposing, isolating or treating of water-borne industrial or other waste. Once a facility has been certified

by DEP, an exemption is allowed for any materials used in the construction, repair or maintenance of the facility, as well as for any machinery and equipment used primarily for reducing, controlling or eliminating water pollution. This includes, but is not limited to, thickeners, incinerators, pipelines or conduits, pumping stations, force mains and all other constructions, devices, appurtenances and facilities used for collecting or conducting water borne industrial or other waste. It does not include supplies other than maintenance materials and pollution control chemicals. It also does not include septic tanks and the pipelines and leach fields connected to septic tanks.

F. AIR POLLUTION CONTROL FACILITIES

Section 1760(30) of the law provides an exemption for air pollution control facilities. In order to qualify for this exemption, a facility must be certified by the Commissioner of Environmental Protection (DEP) as a facility that is engaged in reducing, controlling, eliminating or disposing of industrial or other air pollutants. Once a facility has been certified by DEP, an exemption is allowed for any materials used in the construction, repair or maintenance of the facility as well as for any machinery and equipment used primarily for reducing, controlling or eliminating air pollutants. This does not include machinery or equipment installed for the benefit of people, such as air conditioners, dust collectors, fans and similar items; nor does it include facilities designed or installed for the reduction or control of automobile exhaust emissions.

G. MACHINERY AND EQUIPMENT USED IN RESEARCH AND DEVELOPMENT

Section 1760(32) of the law provides an exemption for machinery and equipment used in research and development. As with the exemption for production machinery, several requirements must be satisfied:

- The item being purchased must be machinery and equipment;
- It must be used by the purchaser in research and development;
- It must be used *directly* in research and development; and
- The machinery or equipment must be used *exclusively* in research and development.

“Research and development” for the purposes of this exemption is limited to the experimental and laboratory sense of that term. It does not include the ordinary testing or inspecting of materials or products for quality control, efficiency surveys, management studies, consumer surveys, advertising, or promotions. It also does not include research done in connection with literary, historical or similar projects.

H. CONTRACTS WITH U.S. GOVERNMENT

The exemptions mentioned above also apply to those entities engaged in the production of tangible personal property pursuant to a contract with the United States Government or any agency thereof.

I. BIOTECHNOLOGY

Although the term “production” as defined in §1752(9-B) excludes biological processes generally, it does include “biological processes that are part of an integrated process of manufacturing organisms or microorganic materials through the application of biotechnology.” As a result, the exemptions mentioned above also apply to entities engaged in biotechnological applications.

These applications include recombinant DNA techniques, biochemistry, molecular and cellular biology, immunology, genetics and genetic engineering, biological cell fusion techniques and new bioprocesses using living organisms or parts of organisms to produce or modify products, improve plants or animals, develop microorganisms for specific uses, identify targets for small-molecule pharmaceutical development, transform biological systems and useful processes and products or to develop microorganisms for specific uses.

With respect to research and development in biotechnological applications, the exemption in §1760(32) is not limited to machinery and equipment. It also includes instruments and supplies, such as microscopes and diagnostic testing materials. (See the statute itself for more detail.)

J. FUEL OIL AND COAL

Section 1760(9-G) provides an exemption for the use of fuel oil or coal in those situations where the by-products that result from the burning of the fuel or coal becomes an ingredient of tangible personal property being produced for sale.

III. OTHER IMPORTANT CONSIDERATIONS

A. LEASING

Generally speaking, the exemption for production machinery and equipment does not apply to machinery and equipment being leased. The exemption provided to a manufacturer does not extend to the lessor of equipment even though the equipment will be used in production. Furthermore, the lessor is generally liable for use tax on the cost of the equipment being leased.

The following are exceptions to this general application:

1. Sale/leaseback transactions. If machinery and equipment that qualifies for exemption is purchased by a manufacturer and subsequently sold to and leased back from a lessor, the sales/use tax exemption still applies. It is immaterial whether the original purchase and subsequent sale/leaseback transaction occur simultaneously or at some time in the future. It is also immaterial whether or not actual use of the machinery and equipment is made by the manufacturer before the sale/leaseback transaction occurs.

2. Lease “in lieu of purchase.” A lease that is determined by the State Tax Assessor to be a lease “in lieu of purchase” is a “sale” as defined in §1752(13). As a sale, machinery and equipment being purchased pursuant to a lease in lieu of purchase meets the requirement of

“purchase by the user” and would be exempt provided it meets the other requirements of exemption. For more on this topic, see Maine Revenue Services Rule 316 (“Rental of Tangible Personal Property”).

3. Interim Rentals. Machinery and equipment being rented under the “interim rental” provision of the statute (§1758) is treated as a sale, with the lessor being the retailer, the rental payment being the sale price and lessee being the purchaser/consumer. An interim rental, therefore, meets the requirement of “purchase by the user” and is exempt provided it meets the other applicable requirements of the law.

B. TRANSPORTATION

As noted above, machinery and equipment must be used “directly” in production in order to qualify for exemption. Thus transporting work in process between production machines is a qualifying activity. However, transportation of raw material to the production site, transportation of work in process on public ways between production sites and transportation of finished products to customers are all non-qualifying activities.

Certain vehicles used in interstate or foreign commerce may be exempt pursuant to §1760(41), depending upon the circumstances. For more information on this subject, see Maine Revenue Services Rule 318 and Instructional Bulletin No. 34.

C. BY-PRODUCTS AND RECOVERED RAW MATERIALS

The manufacturing process generally results in a certain amount of waste. In many situations this waste must be disposed of, but in certain manufacturing environments it can be recycled, sold as a by-product or used as an ingredient of another product.

Removing waste from a production machine is an activity that is considered “directly” in production. Machinery and equipment that handles or processes the product after that point may or may not qualify for exemption.

Examples of **exempt** activities involving by-products and recovered raw materials:

- Re-cycling the by-product or recovered raw material back into production. This activity is “directly” in production and machinery and equipment used primarily for this purpose is exempt.
- Using the by-product or recovered raw material as an ingredient in the production of another product. This activity is also considered “directly” in production and machinery and equipment used primarily for this purpose is exempt.

Example of a **taxable** activity involving by-products:

- Selling the by-product “as is.” In this case, removing the waste from the production machine is “directly” used in production, but machinery and equipment used after this point is **not** used directly in production since nothing more is done to the by-product to change its form, character, or composition.

D. TANGIBLE PERSONAL PROPERTY VS. REAL PROPERTY

The purchase by a construction contractor of materials for the construction of real property (buildings, fixtures attached to buildings, etc.) or for incorporation into real property does not qualify for the machinery and equipment exemption.

Examples of such items are:

- Wires, conduits, outlets and other electrical items installed to facilitate the use of the building *as a building* rather than for purposes of a particular production process;
- Heating and air conditioning units (including ductwork) installed to facilitate the use of the building *as a building*, rather than for purposes of a particular production process such as that described in Part II, section A(4)(i);
- Special purpose buildings;
- Permanent foundations composed of concrete.

If machinery and equipment is purchased as tangible personal property *before* being incorporated into realty and, as tangible personal property, meets all of the other requirements of exemption, the machinery and equipment would qualify for exemption. Since this type of arrangement between the contractor and the purchaser is the exception, rather than the norm, manufacturers are cautioned that proper contractual terms are necessary for correct application of the exemption. For more information on this topic, see Instructional Bulletin No. 28 (“Installing Tangible Personal Property in Real Property”).

E. EXEMPT PURCHASE DOCUMENTATION

A manufacturer claiming that the purchase of tangible personal property qualifies for exemption must provide its vendor with a “Blanket Certificate of Exemption.” (See copy attached.) The manufacturer should indicate on this certificate the grounds for exemption by checking off the appropriate category. The vendor should retain this certificate in its file to document the exempt sale. If multiple purchases are made from one vendor, the certificate may act as a “blanket” certificate, covering all subsequent purchases of like items. Remember that it is the **responsibility of the purchaser** to understand all requirements of the law before claiming any exemption. If your business is audited, Maine Revenue Services need not prove that a purchase does not qualify for exemption; you must prove that it does.

F. DIRECT PAY PERMIT

Pursuant to Rule 308, certain manufacturers and utilities that commonly acquire a substantial amount of tangible personal property under circumstances making it impractical to determine at the time of purchase whether the use will be taxable or exempt, may qualify for a “direct payment permit” issued by Maine Revenue Services. This permit allows the manufacturer to purchase most items of tangible personal property without paying tax -- but the purchaser then becomes accountable directly to the State for payment of appropriate use tax. The direct pay permit must be provided to the vendor at the time of purchase to document the exempt sale and, as with the blanket certificate of exemption, need only be provided once to cover subsequent purchases of like items. See Rule 308 for more information and qualifications.

IV. ADDITIONAL INFORMATION

The information in this bulletin addresses some of the more common questions regarding the Sales and Use Tax Law faced by your business. It is not intended to be all-inclusive. Requests for information on specific situations should be in writing, should contain full information as to the transaction in question and should be directed to the:

**MAINE REVENUE SERVICES
SALES, FUEL & SPECIAL TAX DIVISION
P.O. BOX 1065
AUGUSTA, ME 04332-1065
TEL: (207) 624-9693
TTY: (207) 287-4477**

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DEFINITIONS

2-A. Directly. "Directly," when used in relation to production of tangible personal property, refers to those activities or operations which constitute an integral and essential part of production, as contrasted with and distinguished from those activities or operations which are simply incidental, convenient or remote to production.

6-A. Manufacturing facility. "Manufacturing facility" means a site at which is located machinery and equipment used directly and primarily in either the production of tangible personal property intended to be sold or leased ultimately for final use or consumption or the production of tangible personal property pursuant to a contract with the United States Government or any agency thereof. It includes the machinery and equipment and all machinery, equipment, structures and facilities located at the site and used in support of production or associated with the production.

7-B. Machinery and equipment. "Machinery and equipment" means machinery, equipment and parts and attachments for machinery and equipment, but excludes foundations for machinery and equipment and special purpose buildings used to house or support machinery and equipment.

9-A. Primarily. "Primarily," when used in relation to production, means more than 50% of the time.

9-B. Production. "Production" means an operation or integrated series of operations engaged in as a business or segment of a business that transforms or converts personal property by physical, chemical or other means into a different form, composition or character from that in which it originally existed.

"Production" includes manufacturing, processing, assembling and fabricating operations that meet the definitional requisites, including biological processes that are part of an integrated process of manufacturing organisms or microorganic materials through the application of biotechnology.

"Production" does not include biological processes except as otherwise provided by this subsection, wood harvesting operations, the severance of sand, gravel, oil, gas or other natural resources produced or severed from the soil or water, or activities such as cooking or preparing drinks, meals, food or food products by a retailer for retail sale. The foregoing are examples of activities that are not included within the term "production."

17. Tangible personal property. "Tangible personal property" means personal property that may be seen, weighed, measured, felt, touched or in any other manner perceived by the senses, but does not include rights and credits, insurance policies, bills of exchange, stocks and bonds and similar evidences of indebtedness or ownership. "Tangible personal property" includes electricity. "Tangible personal property" includes any computer software that is not a custom computer software program.

EXEMPTIONS

9-D. Fuel and electricity used at a manufacturing facility. Ninety-five percent of the sale price of all fuel and electricity purchased for use at a manufacturing facility. For purposes of this subsection, "sale price" includes, in the case of electricity, any charge for transmission and distribution.

9-G. Fuel oil or coal. Fuel oil or coal, the by-products from the burning of which become an ingredient or component part of tangible personal property for later sale.

12-A. Packaging materials. Sales of containers, boxes, crates, bags, cores, twines, tapes, bindings, wrappings, labels and other packing, packaging and shipping materials to:

A. Persons engaged in the business of packing, packaging, shipping and transporting tangible personal property; or

B. Persons for use in packing, packaging or shipping tangible personal property sold by them or on which they have performed the service of cleaning, pressing, dyeing, washing, repairing or reconditioning in their regular course of business that are transferred to the possession of the purchaser of that tangible personal property;

29. Water pollution control facilities. Sales of any water pollution control facility, certified as such by the Commissioner of Environmental Protection, and any part or accessories thereof, or any materials for the construction, repair or maintenance of a facility.

As used in this subsection, unless the context otherwise indicates, the following terms have the following meanings.

A. "Disposal system" means any system used primarily for disposing of or isolating industrial or other waste and includes thickeners, incinerators, pipelines or conduits, pumping stations, force mains and all other constructions, devices, appurtenances and facilities used for collecting or conducting water borne industrial or other waste to a point of disposal, treatment or isolation, except that which is necessary to the manufacture of products.

B. "Facility" means any disposal system or any treatment works, appliance, equipment, machinery, installation or structures installed, acquired or placed in operation primarily for the purpose of reducing, controlling or eliminating water pollution caused by industrial or other waste, except septic tanks and the pipelines and leach fields connected or appurtenant thereto.

C. "Industrial waste" means any liquid, gaseous or solid waste substance capable of polluting the waters of the State and resulting from any process, or the development of any process, of industry or manufacture.

D. "Treatment works" means any plant, pumping station, reservoir or other works used primarily for the purpose of treating, stabilizing, isolating or holding industrial or other waste.

30. Air pollution control facilities. Sale of any air pollution control facility, certified as such by the Commissioner of Environmental Protection, and any part or accessories thereof, or any materials for the construction, repair or maintenance thereof.

As used in this subsection, unless the context otherwise indicates, the following terms have the following meanings.

A. "Facility" means any appliance, equipment, machinery, installation or structures installed, acquired or placed in operation primarily for the purpose of reducing, controlling, eliminating or disposing of industrial or other air pollutants.

Facilities such as air conditioners, dust collectors, fans and similar facilities designed, constructed or installed solely for the benefit of the person for whom installed or the personnel of such person, and facilities designed or installed for the reduction or control of automobile exhaust emissions shall not be deemed air pollution control facilities for purposes of this subsection.

31. Machinery and equipment. Sales of machinery and equipment:

A. For use by the purchaser directly and primarily in either the production of tangible personal property intended to be sold or leased ultimately for final use or consumption, or in the production of tangible personal property pursuant to a contract with the United States Government or any agency thereof. This exemption applies even if the purchaser sells the machinery or equipment and leases it back in a sale and leaseback transaction. This exemption also applies whether the purchaser agrees before or after the purchase of the machinery or equipment to enter into the sale and leaseback transaction and whether the purchaser's use of the machinery or equipment in production commences before or after the sale and leaseback transaction occurs; and

B. To a bank, leasing company or other person as part of a sale and leaseback transaction, by a person that uses the machinery or equipment as described in paragraph A, whether the original purchaser's use of the machinery or equipment in production commences before or after the sale and leaseback transaction occurs.

32. Machinery and equipment for research. Sales of machinery and equipment for use by the purchaser directly and exclusively in research and development in the experimental and laboratory sense and sales of machinery, equipment, instruments and supplies for use by the purchaser directly and primarily in biotechnology applications, including the application of technologies such as recombinant DNA techniques, biochemistry, molecular and cellular biology, immunology, genetics and genetic engineering, biological cell fusion techniques and new bioprocesses using living organisms or parts of organisms to produce or modify products, improve plants or animals, develop microorganisms for specific uses, identify targets for small-molecule pharmaceutical development, transform biological systems and useful processes and products or to develop microorganisms for specific uses. Equipment and supplies used for biotechnology include but are not limited to microscopes, diagnostic testing materials, glasswares, chemical reagents, computer software and technical books and manuals. "Research

and development" includes testing and evaluation for the purposes of approval and compliance with regulatory standards for biotechnological products or materials. "Research and development" does not include the ordinary testing or inspecting of materials or products for quality control, efficiency surveys, management studies, consumer surveys, advertising, promotions or research in connection with literary, historical or similar projects.

41. Certain instrumentalities of interstate or foreign commerce. The sale of a vehicle, railroad rolling stock, aircraft or watercraft which is placed in use by the purchaser as an instrumentality of interstate or foreign commerce within 30 days after that sale and which is used by the purchaser not less than 80% of the time for the next 2 years as an instrumentality of interstate or foreign commerce. The State Tax Assessor may for good cause extend for not more than 60 days the time for placing the instrumentality in use in interstate or foreign commerce. For purposes of this subsection, property is "placed in use as an instrumentality of interstate or foreign commerce" by its carrying of, or providing the motive power for the carrying of, a bona fide payload in interstate or foreign commerce, or by being dispatched to a specific location at which it will be loaded upon arrival with, or will be used as motive power for the carrying of, a payload in interstate or foreign commerce. For purposes of this subsection, "bona fide payload" means a cargo of persons or property transported by a contract or common carrier for compensation which exceeds the direct cost of carrying that cargo or pursuant to a legal obligation to provide service as a public utility or a cargo of property transported in the reasonable conduct of the purchaser's own nontransportation business in interstate commerce.

74. Property used in production. Sales of tangible personal property, other than fuel or electricity, that becomes an ingredient or component part of, or that is consumed or destroyed or loses its identity directly and primarily in either the production of tangible personal property for later sale or lease, other than lease for use in this State, or the production of tangible personal property pursuant to a contract with the United States Government or any agency of the United States Government. Tangible personal property is "consumed or destroyed" or "loses its identity" in that production if it has a normal physical life expectancy of less than one year as a usable item in the use to which it is applied.



MAINE REVENUE SERVICES SALES/EXCISE TAX DIVISION

INDUSTRIAL USERS BLANKET CERTIFICATE OF EXEMPTION

For purchases of Tangible Personal Property for Use in Production
Under Section 1760, subsections 9-D, 29, 30, 31, 32 and 74 of the Maine Sales and Use Tax Law.

I hereby certify that I hold a valid Sales Tax Registration No. _____ issued pursuant to the Sales and Use Tax Law, that I am engaged in the production of _____ and that tangible personal property to be purchased from _____ is exempt for the reason(s) indicated below:

- []a. To become an ingredient or component part of tangible personal property either in the production of tangible personal property for later sale or lease, other than lease for use in this State, or in the production of tangible personal property pursuant to a contract with the Federal Government or any agency thereof. §1760 (74)
- []b. To be consumed or destroyed or to lose its identity directly and primarily either in the production of tangible personal property for later sale or lease, other than lease for use in this State, or in the production of tangible personal property pursuant to a contract with the Federal Government or any agency thereof. §1760 (74)
- []c. Constitutes machinery and equipment, or repair or replacement parts, to be used by me directly and primarily in either the production of tangible personal property for sale or lease, the production of tangible personal property pursuant to a contract with the Federal Government or any agency thereof or in the generation of radio and television broadcast signals by broadcast stations regulated under 47 Code of Federal Regulations, Part 73. §1760 (31)
- []d. Constitutes machinery and equipment, or repair or replacement parts, to be used by me directly and exclusively in research and development in the experimental and laboratory sense or machinery, equipment, instruments and supplies to be used by me directly and primarily in biotechnology applications. §1760 (32)
- []e. Is fuel or electricity for use at a manufacturing facility (95% of the sale price is exempt)
Meter/Account Number(s) _____. §1760 (9-D)
- []f. To be used as part of or for the construction, repair or maintenance of a water or air pollution control facility, certified as such by the Commissioner of Environmental Protection. §1760 (29-30)

I further certify that I assume full liability for payment to the State of Maine of any use taxes, together with penalties and interest, that may later be determined to be due on any purchases covered by this certificate because of a taxable use of the property.

NAME OF COMPANY

DATE

SIGNATURE

TITLE

NOTICE TO RETAILERS: Retailers making exempt sales covered by this certificate must appropriately mark or stamp all invoices to indicate they are exempt sales. For items a through d and f above, the words "Maine Sales Tax Exempt" will satisfy this requirement. For item e above, the words "Fuel/electricity used at a manufacturing facility" will satisfy this requirement.

The certificate may also be used for occasional exempt purchases rather than blanket use by filling out as far as applicable, striking out the word "Blanket" and listing on the reverse side the date of order and the quantity and description of the tangible personal property ordered; or by incorporating the purchase order by reference to this certificate, as by listing date and order number.

ST-P-70

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