

New York State Department of Taxation and Finance
Taxpayer Services Division
Technical Services Bureau

TSB-A-97(40)S
Sales Tax

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S951023A

On October 23, 1995, the Department of Taxation and Finance received a Petition for Advisory Opinion from Western New York Beverage Industry Collection & Sorting, 2240 Harlem Road, Cheektowaga, New York 14225-4902. Petitioner, Western New York Beverage Industry Collection & Sorting, thereafter submitted additional information pertaining to the Petition.

The issues raised by Petitioner are as follows:

1. Whether receipts received by Petitioner from the service of picking up and recycling full containers are subject to sales tax as the maintenance of real property, property or land pursuant to Section 1105(c) (5) of the Tax Law.
2. Whether the can machines that make up part of Petitioner's material handling and testing system constitute production equipment and are thus eligible for the exemption from sales tax provided by Section 1115(a) (12) of the Tax Law.
3. Whether Petitioner's electrical transformer is also eligible for the exemption from sales tax as provided by Section 1115(a) (12), and if not, whether the transformer, as installed, is a capital improvement to real property, property or land within the meaning and intent of Section 1101(b) (9) (i) of the Tax Law.

Petitioner submitted the following facts as the basis for this Advisory Opinion.

Petitioner's business consists of recycling metal cans, plastic bottles and glass bottles (collectively referred to as "containers"). All recycled containers are sold by Petitioner to various independent third parties. Petitioner states that, in sum and substance, the "used" containers constitute Petitioner's raw materials.

Recycling of Full Containers. In addition to recycling empty containers, Petitioner from time-to-time accepts for recycling containers that have not been opened. These containers hold "stale" products, typically beer that has exceeded its "expiration date." Petitioner picks up the full containers and recycles them in the same manner that it recycles empty containers. The crusher/compactors that perform this recycling function have large drains beneath them to catch the fluids that escape when the full containers rupture during compression. Petitioner sells these recycled containers in the same manner that it sells all other recycled materials.

Petitioner charges its customers for picking up and recycling the full containers. The charge which Petitioner imposes on its customers for picking up and recycling the full containers is less than that which the customers would be charged by a disposal facility for outright disposal of the full containers.

Can Machines. The containers that Petitioner ultimately recycles are placed in plastic bags by retail vendors and then retrieved by Petitioner's trucks. The trucks deliver the bags of containers to Petitioner's facility in Buffalo, New York, where the containers are unloaded and placed directly in storage pending recycling. The containers remain in the storage area until there is sufficient capacity on the appropriate recycling line to recycle them. No actions are taken on the containers before they are placed in storage; for example, they are not tested, weighed, or inspected before being placed in storage.

Each type of container (metal, plastic and glass) is handled by a discrete group of equipment. Of relevance is the equipment that recycles the metal cans. When the metal cans are retrieved from storage, the first piece of equipment that they come in contact with in Petitioner's continuous and integrated material handling system is a "can machine." The plastic bags full of cans are emptied into a collection bin located at one end of the can machine. As they fall out of the bin, the cans are separated (single-file) onto individual runways. The cans are then moved by an internal conveyor on the machine past a laser scanner which is connected to a computer. The laser scanner reads the UPC bar code on the can. From this information, Petitioner identifies the specific type of metal can, including the can's metallic content. This information is also used by Petitioner to account for the can's deposit, allowing Petitioner to bill the appropriate party for reimbursement of the deposit on that can.

Aluminum cans must be recycled separately from bimetallic cans (i.e., cans with metals other than, or in addition to, aluminum). After being identified for metallic content, the cans are sent by a connected and continuous web of conveyor belts to the appropriate crusher/compactor for recycling. The crusher/compactor compresses the cans into blocks of metal. The blocks of metal are then removed, placed on skids, weighed, and placed in storage pending delivery to customers.

The can machines are used at all times in the handling of the cans. In addition, the can machines are used at all times to determine the metallic content of the cans in order to ensure that aluminum and bimetallic cans are not recycled together. There is no break in the materials handling network from the bins at one end of the can machines through to the crusher/compactors.

Electrical Transformer. All of Petitioner's recycling equipment is powered by electricity. The machines specifically require different voltage and amperage than the standard service provided by the local utilities. To meet these needs, Petitioner purchased a transformer on an installed basis. The sole purpose of the transformer is to convert Petitioner's standard electrical service which it receives from the local utility to a voltage and amperage compatible with the recycling equipment's operating specifications. Electrical service of standard

voltage and amperage used by Petitioner to power conventional lighting and climate control equipment is removed from Petitioner's utility stream before the current enters the transformer. All electricity that flows out of the transformer is used to power equipment actively engaged in the recycling of containers.

The transformer is a single piece of equipment welded to a structural steel frame. The frame extends downwards to form two horizontal support footings which run the length of the unit. As installed, the extended support footings that make up part of the structural frame are embedded in concrete. The transformer cannot be removed from the facility without either: (1) taking a jackhammer to the concrete in which it sits; or (2) taking a blowtorch or other device to the frame and cutting off the support footings. Petitioner intended the transformer to be a permanent installation.

Recycling of Used Plastic Bags. It is noted that on various occasions Petitioner picks up used plastic bags from the premises of various retail establishments. Petitioner compacts these plastic bags and sells them to third parties for recycling. Petitioner charges its customers a fixed fee per pound of plastic bags retrieved. The charge is less than the charge that would be imposed if Petitioner picked up the plastic bags for disposal rather than recycling.

Applicable Law and Regulations

Section 1101(b)(9) of the Tax Law defines a "capital improvement," in part, as follows:

Capital improvement. (i) An addition or alteration to real property which:

(A) Substantially adds to the value of the real property, or appreciably prolongs the useful life of the real property; and

(B) Becomes part of the real property or is permanently affixed to the real property so that removal would cause material damage to the property or article itself; and

(C) Is intended to become a permanent installation.

Section 1105(a) of the Tax Law imposes tax on "[t]he receipts from every retail sale of tangible personal property, except as otherwise provided in this article."

Section 1105(c) of the Tax Law imposes tax upon the receipts from every sale, except for resale, of the following services:

* * *

(3) Installing tangible personal property ... not held for sale in the regular course of business, whether or not the services are performed directly or by means of coin-operated equipment or by any other means, and whether or not any tangible personal property is transferred in conjunction therewith, except:

* * *

(iii) for installing property which, when installed, will constitute an addition or capital improvement to real property, property or land, as the terms real property, property or land are defined in the real property tax law as such term capital improvement is defined in paragraph nine of subdivision (b) of section eleven hundred one of this chapter

* * *

(5) Maintaining, servicing or repairing real property, property or land, as such terms are defined in the real property tax law, whether the services are performed in or outside of a building, as distinguished from adding to or improving such real property, property or land, by a capital improvement as such term capital improvement is defined in paragraph nine of subdivision (b) of section eleven hundred one of this chapter, but excluding services rendered by an individual who is not in a regular trade or business offering his services to the public.

Section 1105-B of the Tax Law provides, in part:

* * *

(b) Notwithstanding any other provisions of this article, but not for the purposes of the taxes imposed by section eleven hundred seven or eleven hundred eight or authorized pursuant to the authority of article twenty-nine of this chapter, the taxes imposed by subdivision (c) of section eleven hundred five on receipts from every sale of the services of installing ... the tangible personal property described in paragraph twelve of subdivision (a) of section eleven hundred fifteen, including the parts with a useful life of one year or less, tools and supplies described in subdivision (a) of this section, to the extent subject to such tax ... shall be exempt from the tax on sales imposed under subdivision (c) of section eleven hundred five on and after March first, nineteen hundred eighty-one.

* * *

(d) Notwithstanding any other provisions of this section or this article to the contrary, on and after September first, nineteen hundred ninety-six, the exemptions provided by subdivisions (a), (b) and (c) of this section shall apply for purposes of the sales and compensating use taxes imposed by section eleven hundred seven of this article.

Section 1115(a) of the Tax Law provides:

Receipts from the following shall be exempt from the tax on retail sales imposed under subdivision (a) of section eleven hundred five and the compensating use tax imposed under section eleven hundred ten:

* * *

(12) Machinery or equipment for use or consumption directly and predominantly in the production of tangible personal property ... for sale, by manufacturing, processing, generating, assembling, refining, mining or extracting

Section 527.7(a) of the Sales and Use Tax Regulations provides, in part:

Definitions. (1) *Maintaining, servicing and repairing* are terms which are used to cover all activities that relate to keeping real property in a condition of fitness, efficiency, readiness or safety or restoring it to such condition. Among the services included are services on a building itself such as painting; services to the grounds, such as lawn services, tree removal and spraying; trash and garbage removal and sewerage service and snow removal.

Section 527.7(b) of the regulations provides, in part:

Imposition. (1) The tax is imposed on receipts from every sale of the services of maintaining, servicing or repairing real property, whether inside or outside of a building.

* * *

(2) All services of trash or garbage removal are taxable, whether from inside or outside of a building or vacant land.

Section 528.13 of the regulations provides, in part:

(b) Production. (1) The activities listed in paragraph (a)(1) of this section are classified as administration, production or distribution.

(i) *Administration* includes activities such as sales promotion, general office work, credit and collection, purchasing, maintenance, transporting, receiving and testing of raw materials and clerical work in production such as preparation of work, production and time records.

(ii) *Production* includes the production line of the plant starting with the handling and storage of raw materials at the plant site and continuing through the last step of production where the product is finished and packaged for sale.

(iii) *Distribution* includes all operations subsequent to production, such as storing, displaying, selling, loading and shipping finished products.

(2) The exemption applies only to machinery and equipment used directly and predominantly in the production phase. Machinery and equipment partly used in the administration and distribution phases does not qualify for the exemption, unless it is used directly and predominantly in the production phase.

(3) The determination of when production begins is dependent upon the procedure used in a plant. If on receiving raw materials, the purchaser weighs, inspects, measures or tests the material prior to placement into storage, production begins with placement into storage, and the prior activities are administrative. If the materials are unloaded and placed in storage for production without such activities, the unloading is the beginning of production.

* * *

(4) Production ends when the product is ready to be sold.

* * *

(c) Directly and predominantly. (1) *Directly* means the machinery or equipment must, during the production phase of a process:

(i) act upon or effect a change in material to form the product to be sold, or

(ii) have an active causal relationship in the production of the product to be sold, or

(iii) be used in the handling, storage, or conveyance of materials or the product to be sold, or

(iv) be used to place the product to be sold in the package in which it will enter the stream of commerce. (2) Usage in activities collateral to the actual production process is not deemed to be used directly in production.

* * *

(4) Machinery or equipment is used predominantly in production, if over 50 percent of its use is directly in the production phase of a process.

Opinion

Issue 1

As indicated by Petitioner, containers constitute the "raw materials" from which Petitioner generates its revenue. The facts presented by Petitioner are not materially distinguishable from those presented in Marisol, Inc. (Tax App Trib, January 4, 1996, TSB-D-96(2)S). In Marisol, the Tax Appeals Tribunal concluded that, under the circumstances, the petitioner's receipts from the service of removal of used or spent industrial chemicals for recycling and sale by the petitioner were not subject to tax under Section 1105(c)(5) of the Tax Law. Accordingly, we conclude that the receipts received by Petitioner from the service of picking up and recycling full containers are not subject to sales tax as receipts from the sale of the service of maintaining real property, property or land pursuant to Section 1105(c)(5) of the Tax Law. Similarly, Petitioner's receipts from picking up and recycling plastic bags are not subject to sales tax under Section 1105(c)(5) of the Tax Law. (It is noted that Petitioner does not inquire, and from the facts presented we do not address, whether any of Petitioner's services may be taxable under another provision of the Tax Law. A previous Advisory Opinion issued to Petitioner [Adv Op Comm T&F, April 15, 1985, TSB-A-85(3)S] indicated, among other things, that certain services provided by Petitioner were not subject to tax under Section 1105(c)(2) of the Tax Law. The facts presented in the Petition for this Advisory Opinion do not appear to be the same as those addressed in the earlier Opinion.)

Issue 2

The can machines that make up part of Petitioner's material handling and testing system constitute production equipment and are eligible for the exemption from sales tax that is provided by Section 1115(a)(12) of the Tax Law. Petitioner is in the business of recycling containers, including cans, for sale to third parties and in this regard is engaged in the production of tangible personal property for sale.

Cans are collected by Petitioner, unloaded and placed directly into storage pending recycling. No actions are taken on the cans before they are placed in storage. Pursuant to Section 528.13(b)(3) of the regulations, the unloading of the cans constitutes the beginning of production. When the cans are removed from storage, the first pieces of equipment that they encounter are the can machines. Each machine is an integrated unit. The cans are separated into individual runways and moved by internal conveyors in the machines past laser scanners. The scanned information provides Petitioner with the specific type of metal cans and the cans' metallic content. After being identified for metallic content, the cans are sent by conveyor to the appropriate crusher/compactor for recycling. The can machines are used at all times in the handling of the cans, in order to determine the metallic content of the cans and to ensure that unlike cans are not recycled together. Thus, the can machines have an active causal relationship in production and are used in the storage, handling and conveyance of the cans. Accordingly, as provided in the regulations and based on the procedures used at

Petitioner's recycling facility, the can machines are used directly and predominantly in production of tangible personal property for sale. (See, Lindemann Recycling Equipment, Inc., Adv Op Comm T&F, January 31, 1989, TSB-A-89(3)S; Vigliotti Recycling Corp., Adv Op Comm T&F, December 24, 1990, TSB-A-90(58)S.)

The fact that the scanned information also provides Petitioner with the means to account for the cans' deposits, a function that can arguably be classified under "administration" (20 NYCRR 528.13(b)(1)(i)), does not negate the fact that the can machines are used directly and predominantly in production. Each can machine as a whole (including its laser scanner) makes up part of Petitioner's continuous and integrated material handling and testing system. There is no reason to apply the subject exemption from tax on a component-by-component basis (see, B.R. DeWitt, Inc., Tax App Trib, September 19, 1991, TSB-D-91(77)S). Nor is it necessary under the Tax Law or regulations to discern whether the primary function of a can machine's laser scanner is to account for deposits or to identify the cans for metallic content so that the cans may be sent to the appropriate crusher/compactor for recycling (see, National Fuel Gas Distribution Corporation, Tax App Trib, March 14, 1991, TSB-D-91(15)S). Both of these functions occur simultaneously during the production phase; it is not an "either/or" situation or otherwise quantifiable. That is, all of the time that a can machine is operating it is accomplishing both of these tasks.

Issue 3

Petitioner's electrical transformer is also eligible for the exemption from sales tax under Section 1115(a)(12) of the Tax Law.

"The determination as to whether a particular piece of machinery [or equipment] qualifies for the exemption depends upon the peculiarities of a taxpayer's operation and must be individually assessed on its own fact pattern." (See, Deco Builders, Inc., Tax App Trib, May 9, 1991, TSB-D-91(39); Matter of Rochester Independent Packer v Heckelman, 83 Misc.2d 1064.) Where transformers are used in the transmission and distribution of electricity rather than in its production (see, Matter of Niagara Mohawk Power Corp. v Wanamaker, 286 AD 446, affd 2 NY2d 764; ABB Power Transmission, Inc., Adv Op Comm T&F, July 17, 1990, TSB-A-90(34)S) and where transformers are used to regulate or transmit electricity throughout a plant or mine (see, Gernatt Asphalt Products, Inc., Adv Op Comm T&F, December 5, 1985, TSB-A-85(64)S; Akzo Salt, Inc., Adv Op Comm T&F, January 25, 1993, TSB-A-93(8)S), the transformers do not qualify for the exemption from tax.

However, Petitioner's transformer is more akin to the motor starters and frequency inverters which were the subject of the Advisory Opinion in Leprino Foods Company, April 28, 1994, TSB-A-94(17)S. In that matter the Commissioner opined:

All electrical parts actually attached to a qualifying piece of production machinery or equipment are deemed to assume the identity of such machinery and equipment and are therefore entitled to the same exemption as the machinery and equipment. All other electrical components are not used directly in production and therefore are not entitled to the exemption contained in Section 1115(a)(12) of the Tax Law. (See, New York State and Local Sales Tax Information for Manufacturers, New York State Department of Taxation and Finance Publication 852 (9/86) at page 11.)

In the instant matter, the motor starters and the frequency inverters which are designed to be used specifically with individual pieces of machinery and equipment and which are directly wired to the individual pieces of machinery or equipment are considered to assume the identity of such machinery or equipment and are entitled to the same exemption afforded the machinery or equipment.

Similar to Leprino Foods, Petitioner's transformer is integral to Petitioner's production equipment. The transformer was purchased by Petitioner for the sole purpose of converting standard electricity to a voltage and amperage compatible with the production equipment's operating specifications. Without the transformer, the production equipment would not have power, and production could not take place. Electrical service of standard voltage and amperage that is used by Petitioner for nonproduction purposes is removed before the electricity enters the transformer. All electricity that flows out of the transformer is used to power equipment actively engaged in the recycling of containers. Thus, Petitioner's transformer is considered to assume the identity of the production equipment and is entitled to the same exemption. (See, also, Finch, Pruyn & Co. Inc., Adv Op Comm T&F, September 4, 1996, TSB-A-96(51)S.)

The service of installing the transformer is exempt from New York State sales tax in accordance with Section 1105-B of the Tax Law (L 1996, ch 366, as amended). However, as provided in Section 1105-B(b), there is no exemption from the local sales taxes authorized pursuant to the authority of Article 29 of the Tax Law on this installation service. Accordingly, it is necessary to address whether the transformer as installed constitutes a capital improvement to real property, property or land and whether such installation falls within the exclusion from tax under Section 1105(c)(3)(iii) of the Tax Law.

Petitioner's electrical transformer, as installed, is a capital improvement to real property, property or land within the meaning and intent of Section 1101(b)(9)(i) of the Tax Law. The transformer satisfies each of the requirements of the statutory definition of "capital improvement." The installation of the transformer substantially adds to the value of Petitioner's real property. It was originally purchased and installed for the sole purpose of converting the voltage and amperage of electricity that is used in recycling. Without the installation of the transformer, Petitioner's production equipment would not have the power necessary to operate and Petitioner's facility could not be used for recycling. In addition, the transformer, as installed, is a single piece of equipment welded to a structural steel frame that runs the length of the unit and

is embedded in a concrete foundation. This degree of affixation is permanent in nature and any attempt to remove the transformer from its welded station would cause material damage to the transformer itself. Lastly, Petitioner has indicated and the circumstances support the fact that the installation of the transformer was intended to be permanent. Accordingly, the installation of the transformer is excluded from both the State and local taxes under Section 1105(c)(3)(iii) of the Tax Law.

DATED: July 23, 1997

/s/
John W. Bartlett
Deputy Director
Technical Services Bureau

NOTE: The opinions expressed in Advisory Opinions are limited to the facts set forth therein.