

Title 12—DEPARTMENT OF REVENUE
Division 10—Director of Revenue
Chapter 110—Sales/Use Tax—Exemptions

PROPOSED AMENDMENT

12 CSR 10-110.600 Electrical Energy as defined in Section 144.030, RSMo. The director proposes to amend the Title, the purpose, and sections (1) through (4).

PURPOSE: This rule is being amended due to TAFP HCS SCS SB 196, enacted by the 93rd General Assembly, 2005, and TAFP CCS HCS SB30, enacted by the 94th General Assembly, 2007.

*PURPOSE: Section 144.030.2.(12), RSMo exempts from tax certain purchases of electrical energy used in primary or secondary manufacturing, processing, compounding, mining or producing a product, [or used in material recovery processing] **or processing of raw materials that contain recovered materials.** Section 144.030.2.(31), RSMo, exempts from tax, electricity used in connection with the manufacturing of cellular glass products or in any material recovery processing plant. Section 144.030.2.(33), RSMo, exempts from tax utilities used or consumed directly or exclusively in the research and development of agricultural biotechnology products and plant genomics products and prescription pharmaceuticals consumed by humans or animals. This rule explains when [this] **these** exemptions apply[ies] and how a taxpayer may claim the exemptions at the time of purchase of the electrical energy.*

(1) In general, electrical energy used in facilities owned or leased by the taxpayer in the actual primary manufacturing, processing, compounding, mining or producing of a product is exempt from tax if the cost of the electrical energy used exceeds ten percent (10%) of the total cost of the primary manufacturing, processing, compounding, mining or producing, exclusive of the cost of electrical energy so used. Electrical energy used in facilities owned or leased by the taxpayer in the actual secondary manufacturing, processing, compounding, mining or producing of a product is exempt from tax if the cost of the electrical energy used exceeds ten percent (10%) of the total cost of the secondary manufacturing, processing, compounding, mining or producing, exclusive of the cost of electrical energy so used. Electrical energy used in a material recovery processing plant owned or leased by the taxpayer **or in manufacturing cellular glass products** is exempt from tax [if the total cost of electric energy used in such processing exceeds ten percent (10%) of the total cost of the processing, exclusive of the cost of electrical energy so used]. **Utilities used or consumed directly or exclusively in the research and development of agricultural biotechnology products and plant genomics products and prescription pharmaceuticals consumed by humans or animals are exempt from tax.** Electrical energy used in facilities owned or leased by the taxpayer in [manufacturing,] processing [, compounding, mining or producing a product or in a material recovery processing plant is exempt if the raw materials used in

such processing] **raw materials that** contain at least twenty-five percent (25%) recovered materials **is exempt from tax.**

(2) Definition of Terms.

(A) Compounding—Producing a product by combining two (2) or more ingredients or parts.

(B) Fabrication—See 12 CSR 10-111.010[(2)(C)].

(C) Manufacturing—See 12 CSR 10-111.010[(2)(E)].

(D) Material recovery processing plant— *[A facility that has as its primary purpose the recovery of materials into a useable product or a different form that is used in producing a new product. It includes facilities or equipment used exclusively for the collection of recovered materials for delivery to a material recovery processing plant but does not include motor vehicles used on highways. This applies only to the original conversion of recovered materials. Material recovery is not the reuse of materials within a manufacturing process or the use of a product previously recovered. A facility that uses materials that have previously been recovered is not a material recovery processing plant.]* **See 12 CSR 10-111.060.**

(E) Mining—See 12 CSR 10-111.010[(2)(F)].

(F) Primary **processing**—Manufacturing, processing, compounding, mining or producing that results in the first marketable product.

[(G) Processing—Any mode of treatment, act or series of acts performed upon materials to transform and reduce them into an article with a use, identity and market value different from the use, identity and market value of the materials, and includes treatment necessary to maintain or preserve such processing by the producer at the production facility.]

[(H)] **(G) Producing**—See 12 CSR 10-111.010[(2)(H)].

[(I)] **(H) Product**—An item with a new identity, use and market value produced by the taxpayer's efforts which is intended at the time of the production activity to be sold ultimately for final use or consumption. A product may be tangible personal property or a service, if the property or service is subject to state or local sales or use taxes, or any tax that is substantially equivalent thereto, in this state or any other state.

[(J)] **(I) Production activity**—Manufacturing, processing, compounding, mining, producing or fabricating.

(J) Raw material – any ingredient or component that becomes part of, or is made into a finished product.

(K) Recovered materials— **See 12 CSR 10-111.060. In order for an item to be a recovered material, a facility must recover it from the solid waste stream. An item used in processing for its original intended purpose is not a recovered material.** *[Materials that have been diverted or removed from the solid waste stream for sale, use, reuse or recycling, whether or not they require subsequent separation or processing.]*

(L) Secondary **processing**—Further processing or fabricating of a marketable product that results in another marketable product.

(M) Solid waste-See 12 CSR 10-111.060.

[(M)] **(N) Total cost**— All allocated costs incurred in producing the product, including all elements of production cost in accordance with generally accepted accounting principles.

(3) Basic Application of Exemption.

(A) A taxpayer may claim this exemption at the time of purchase of the electrical energy by presenting the seller with a direct pay certificate issued by the department. In order to obtain a direct pay certificate, the taxpayer must submit **[annually]** an electrical energy direct pay authorization application. The application must demonstrate, by the use of the previous calendar year's data, a probable entitlement to the electrical energy exemption for the coming year. The taxpayer must file and remit the appropriate tax on energy purchases that do not qualify for this exemption on its sales tax return.

(B) Every transformation of materials does not constitute a separate production activity. In order to be a separate production activity, the activity must create a new marketable product. If a taxpayer produces only one (1) marketable product, there can only be primary production activity. All production costs must be included in calculating the total cost of production. Secondary production activity can only exist when an already marketable product produced by the taxpayer undergoes subsequent production activity that produces a second marketable product. When there is secondary production activity, the production costs attributable to the primary production activity are not included in the total cost of production of the secondary production activity.

(4) Examples.

(A) A manufacturing firm produces extruded sheet plastic. The automated production line is a closed system connected together by use of vacuum feed-pipe. When an order is received, the computer controlled production line first blends the necessary raw materials. After blending, the mix is conveyed through vacuum pipe to be dried, and then to the extruder, where the mix is heated to meltdown and rolled into sheets by the extruder rollers. These sheets are the end product. The cost of raw materials is 95% of the total cost of producing the end product. The cost of electrical energy is 99% of the cost of drying and extruding the blended raw materials. The plastic sheet is the only marketable product produced by this continuous, indivisible operation. *[None of the electrical energy is exempt because it does not exceed 10% of the total cost of producing the end product.]* **Because the cost of electricity does not exceed 10% of the total cost of producing the product, the purchase of the electricity does not qualify for the exemption.**

(B) A manufacturer produces glass bottles to be used as packaging. The manufacturer combines raw materials, including recycled glass **obtained from recyclers**, which is then melted under extreme heat. The molten glass is then formed into bottles, which are the manufacturer's only product. The electrical energy costs exceed 10% of the total cost of production; therefore the manufacturer qualifies for the exemption. If the manufacturer's raw materials include at least 25% *[recycled]* **recovered** material, the manufacturer may avoid the time and cost involved in the calculations necessary to support the exemption under the 10% threshold and claim the exemption based on its use of *[recycled]* **recovered** materials.

(C) A business contracts with manufacturers of frozen food products to receive fresh or partially frozen food products, reduce the temperature to zero degrees or below, and release the fully frozen food product back to the manufacturer for distribution. The

frozen food products that the business produces have a new and different identity from the fresh or partially frozen products that it receives.

Frozen foods have a longer shelf life and a broader distribution system than refrigerated foods. The business qualifies for the exemption if the electricity used in the freezing process exceeds 10% of the cost of producing the fully frozen food products from the fresh or partially frozen food products. The business does not have to include the cost of its customer's production of the fresh or partially frozen products because the fresh or partially frozen food is a separate marketable product from the frozen food.

(D) A frozen food manufacturer uses \$100,000 of electricity in manufacturing its products. The manufacturer also uses \$150,000 of electricity in its on-premises, refrigerated warehouse to maintain its products at the necessary temperature prior to shipping. Total cost of producing the products, excluding electricity, is \$2,000,000. The combined electricity cost of \$250,000 exceeds 10% of the \$2,000,000 cost of production. The manufacturer qualifies for the exemption because processing includes any treatment by the producer at the production facility that is necessary to maintain the product.

(E) A paper manufacturer uses recycled paper *[to produce]* in its **primary processing of producing** rolls of newsprint. The newsprint includes *[more than 25%]* **50%** recovered paper, *[and qualifies]* **qualifying the manufacturer** for the electrical energy exemption **from state and local taxes**. The newsprint is subsequently cut into sheets **during secondary processing** for sale to a book printer. The cost of electricity *[to cut the sheets]* **used during the secondary processing** does not exceed 10% of the total cost of producing the cut sheets. **However, [T]**the electrical energy used to produce the final product is **also** exempt because the *[manufacturer]* **secondary process** uses at least 25% recovered materials.

AUTHORITY: section 144.270, RSMo 2000. Original rule filed July 25, 2001, effective Feb. 28, 2002. This emergency amendment filed Aug. ____, 2007, effective Aug. 28, 2007, expires Feb. 23, 2008. Amended: Filed Aug. ____, 2007.

PUBLIC COST: This proposed amendment will not cost state agencies or political subdivisions more than five hundred dollars (\$500) in the aggregate.

PRIVATE COST: This proposed amendment will not cost private entities more than five hundred dollars (\$500) in the aggregate.

*NOTICE TO SUBMIT COMMENTS: Anyone may file a statement in support of or in opposition to this proposed amendment with the Missouri Department of Revenue, Legal Services Division, Governmental Affairs Bureau, PO Box 475, Jefferson City, MO 65105-0475. To be considered, comments must be received within thirty (30) days after publication of this notice in the **Missouri Register**. No public hearing is scheduled.*