

Excise Tax Advisory

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Manufacturers' Machinery and Equipment Exemption — Buildings, Fixtures, and Support Facilities

The Department has issued a series of excise tax advisories (ETAs) to address questions regarding the retail sales and use tax exemption provided by RCW 82.08.02565 and 82.12.02565, commonly referred to as the manufacturers' machinery and equipment exemption (M&E exemption). This ETA is issued to address the application of the M&E exemption to buildings, fixtures, and support facilities. Please refer to ETA 3117.2009 for a current list of the issues covered by this series.

In addition to the issues discussed in this ETA series, machinery and equipment must also meet the other requirements of the statutes to be eligible for the exemption. For example, some of the requirements include:

- Purchaser/User must be a manufacturer, processor for hire, or a tester for a manufacturer or processor for hire,
- Must purchase machinery or equipment (devices, industrial fixtures, support facilities, pollution control equipment),
- The machinery or equipment must be used directly in a manufacturing, research and development, or testing operation,
- The machinery or equipment must have a useful life of one year or more, and
- The machinery or equipment must be used more than 50% of the time on an eligible activity.

Therefore, readers are advised that RCW 82.08.02565, RCW 82.12.02565, and WAC 458-20-13601 should also be referenced when making determinations about taxability.

The Department has been asked to give more guidance on the meaning of the words and phrases "buildings," "fixtures," and "support facilities."

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The M&E exemption defines “machinery and equipment” as “industrial fixtures, devices, and support facilities.” In addition to setting forth criteria for eligibility of machinery and equipment, the statute describes four classes of property that are not eligible for the exemption. These are:

- (1) Hand-powered tools;
- (2) Property with a useful life of less than one year;
- (3) Buildings, other than machinery and equipment that is permanently affixed to or becomes a physical part of a building; and
- (4) Building fixtures that are not integral to the manufacturing operation, testing operation, or research and development operation that are permanently affixed to and become a physical part of a building, such as utility systems for heating, ventilation, air conditioning, communications, plumbing, or electrical.

Buildings

A building cannot qualify for the M&E exemption. The statute specifically excludes buildings from eligibility using the following language: “Buildings, other than machinery and equipment that is permanently affixed to or becomes a physical part of a building.”

Because fixtures and support facilities are considered to be a “physical part of a building” it is necessary to distinguish between eligible and ineligible physical parts.

Those parts of buildings that serve a building function do not qualify for the exemption. Walls, roofs, and floors of buildings are designed on a case by case basis to accommodate a particular building use, whether that use is by a manufacturer, retailer, or professional service provider. Walls, roofs, and floors are also designed differently on the basis of external elements such as stability of the underlying earth, winter and summer temperature, and precipitation levels. Walls, roofs, and floors thus serve a general building function, even if designed and constructed differently.

For instance, floors are designed to bear weight. A floor that is designed to bear the weight of raw materials, such as lead bars, is not a support facility, even though a rack designed to store the bars may qualify as a fixture or device. Similarly, a basic function of walls is to control the environment. Insulated wall panels, which make a building’s refrigeration system more efficient do not “control or regulate” tangible personal property for purposes of the “used directly” requirement of the M&E exemption. On the other hand, a refrigeration unit that cools air is a fixture or device and it may qualify for the M&E exemption if it is used directly in the manufacturing operation.

The M&E exemption does not extend to buildings and this restriction applies even if the building is specially designed and unique. For example, an earth-sheltered storage facility is a building, as is an above ground facility, even though to achieve identical ambient air temperatures in the two buildings requires the installation of HVAC fixtures and extra insulation in the above ground facility.

Fixtures

The word “fixture” is a term of art in that it has particular meaning in the context of tax. For purposes of the M&E exemption, the Department uses the common law definition of “fixture” as it is commonly understood in Washington State. A fixture is an item of personal property that has been converted to

real property by being permanently affixed to the realty. The actual tax classification of the fixture does not impact taxability under the M&E exemption. In other words, the fact that a fixture might be classified as real property or personal property has no bearing on eligibility under the statute.

The word “fixture” denotes a type of property that can be distinguished from a “building” per se. A fixture does not lose its identity when installed. Examples of fixtures are air conditioning units, furnaces, boilers, and heating units, plumbing fixtures, conveyors, electric generators, transformers, elevators, and cranes. In addition, the M&E exemption recognizes “utility systems” as fixtures. Property outside of buildings also qualifies as “industrial fixtures.” Examples are tanks, pipes, pads, and lined ponds.

Building construction materials are not fixtures, nor do they normally become fixtures when combined to make walls, floors, and other building components. Examples of construction materials are steel, bricks, lumber, caulking material, tile, cement, mortar, wallboard, doors, paint, coating, flooring, weather stripping, glass, windows, gravel, insulation, and roofing. Fixtures may be made from some of these same materials and fixtures potentially qualify for the exemption regardless of the material from which they are made.

Building fixtures

Building fixtures can qualify for the M&E exemption if integral to the manufacturing, testing, or research and development operation.

Support Facilities

Support facilities, unlike industrial fixtures, are often made from construction materials. The phrase “support facilities” is not defined in the statute nor is it a term of art. Machine foundations act as part of the machine itself, and are the type of property targeted by the existing definition of “support facility” in Rule 13601.

The Department has defined “support facilities” to be property constructed as a machine foundation. Rule 13601 defines the phrase as “a part of a building, or a structure or improvement, used to contain or steady an industrial fixture or device.” The definition further requires that a support facility “must be specially designed and necessary for the proper functioning of the industrial fixture or device and must perform a function beyond being a building or a structure or an improvement...” What this means is that a structure or improvement that functions as a floor, wall, door, roof, or other building component does not qualify for the exemption.

In addition to machine foundations, the phrase “support facilities” includes constructed items such as trenches, gutters, pits, and other property similar in nature that do not have a building function and that are separately identifiable, subject to meeting a used directly test.

Physical parts of buildings that cannot be differentiated and that are not separately identifiable from surrounding construction material do not qualify as a support facility. In order to qualify under the

M&E exemption, these differentiated and separately identifiable parts must meet a used directly test and must not serve a building function.

The Department distinguishes buildings from support facilities, based on the notion of “purpose and function.” For example, a reinforced wall that is designed to bear the weight of the roof trusses does not qualify as a support facility. Roof trusses are part of the building and as such are not machinery and equipment. A portion of the reinforced wall specifically designed and constructed to provide physical support for a fixture or device as a machine foundation could be a support facility if (1) a taxpayer could show that its design is necessary for the operation of the machinery and equipment, and (2) that the reinforced wall can be shown to be differentiated and identifiable from the building. Floors are subject to the same analysis. In order for a part of a floor to qualify as a support facility it has to be differentiated and separately identified and must be a machine foundation. Floors as such do not qualify for the M&E exemption.

Documentation necessary for qualification would include an engineering study, design, or plan, confirming that the reinforced portion of the wall or floor was designed and constructed to support the machinery and equipment, and that it did in fact separately and differently support the machinery and equipment. In determining what qualifies for exemption, the portion of the construction that would be there regardless of the support facility does not qualify. Only the additional construction qualifies.
