

**UT 16-04**

**Tax Type: Use Tax**

**Tax Issue: Agricultural Machinery/Feed/Products/Exemptions**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
SPRINGFIELD, ILLINOIS**

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<b>THE DEPARTMENT OF REVENUE OF THE STATE OF ILLINOIS</b>	)	<b>XXXX</b>
	)	<b>Agricultural Equipment Exemption</b>
<b>v.</b>	)	
	)	
<b>ABC BUSINESS,</b>	)	<b>Kelly K. Yi</b>
<b>TAXPAYER</b>	)	<b>Administrative Law Judge</b>

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**RECOMMENDATION FOR DISPOSITION**

**Appearances:** Mr. Matthew Crain, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; Mr. John McMillan of March, McMillan, DeJoode & Duvall on behalf of ABC Business.

**Synopsis:**

On September 2, 2014, the Department of Revenue of the State of Illinois (“Department”) issued a Notice of Tax Liability (“NTL”) for Form EDA-94, Auditor-prepared Use Tax Report to ABC Business (“Taxpayer”) assessing sales and use taxes for the purchase of a tractor. Taxpayer timely protested the Department’s assessment and requested an administrative hearing. In lieu of a hearing, the parties subsequently submitted a “Stipulation of Facts and Issues” (“Stipulation”) along with Joint Exhibits 1-9, and expressly waived their respective rights to an oral hearing. The issue is whether the Taxpayer’s purchase of a tractor qualifies for the farm machinery and equipment exemption pursuant to Section 3-5(11) of the Use Tax Act, 35 ILCS 105/1 *et seq.* Following the submission of all evidence and a review of

the record, it is recommended that this matter be resolved in favor of the Department. The following Findings of Fact and Conclusions of Law are made in support of this recommendation.

**Stipulated Facts Not In Dispute:**

1. The Department's case, inclusive of all jurisdictional elements, is established by the admission into evidence of the Department's NTL issued to Taxpayer on September 2, 2014.
2. Taxpayer is a self-employed farmer and has no secondary occupation or source of income.  
Stip. 1.
3. Taxpayer raises corn and soybeans and is the owner or operator of XXX acres of cropland.  
Stip. 2.
4. On or about February 8, 2012, the Taxpayer purchased a tractor from January Implement Company and claimed the agricultural equipment exemption from Illinois sales and use taxes. Stip. 3.
5. On or about September 2, 2014, the Department issued an NTL for Form EDA-94, Auditor prepared Use Tax Report, Letter ID XXXX to the Taxpayer. Stip. 4; Joint Ex. 1.
6. Taxpayer protested the Notice of Tax Liability, asserting that the tractor is used for farming and spraying around corn and soybean fields, farm buildings and farm lots; handling crop seeds and grains; snow removal; maintaining waterways and drainage ditches; cutting waterways and road banks; and seeding. Stip. 5.
7. Taxpayer responded to the Department's farm machinery & equipment questionnaire (Department of Revenue Equipment Activity List) indicating a percentage usage for each of seven different activities in the following:

15%	Applying farm chemicals (insecticide, pesticide, fertilizer, weed prevention) to crops
15%	Snow removal/management on property
30%	Mowing fence rows or ditches adjacent to crops
5%	Planting, cultivating, irrigating crops
10%	Using attached hydraulic loader to clean & push fallen trees & brush around fields
14%	Using hydraulic 3pt LandPride cutter to cut waterways
<u>11%</u>	<u>Blading passage to fields &amp; filling smaller eroded ditches in fields</u>
100%	Total

Stip. 6; Joint Ex. 3.

8. Taxpayer has submitted the Department of Revenue Audit Questionnaire form and has stated under penalty of perjury that the use of the tractor in question to be the following: “Farming, spraying around fields, farm buildings and farm lot, use attached hydraulic loader for handling of crop grains, snow removal around farm buildings, filling ditches, use three point hydraulic cutter for cutting waterways and road banks[,] Land pride Hydraulic Blade used in farm maintenance, PTO seeder used in seeding waterways.” Stip. 7; Joint Ex. 4.
9. Taxpayer’s farmland is enrolled in the USDA farm programs administered by the United States Department of Agriculture. Stip. 8.
10. Taxpayer’s eligibility for participation in all USDA farm programs is contingent upon Taxpayer’s compliance with the USDA Farm Service Agency and the Natural Resources Conservation Service and “Continuous AD-1026 Certification” with the USDA. Stip. 9-10.

**Conclusions of Law:**

Under the Use Tax Act (“Act”), Illinois imposes a tax upon the privilege of using in Illinois tangible personal property purchased at retail from a retailer. 35 ILCS 105/3. The use tax is a corollary to the retailers’ occupation tax (“ROT”), which is a tax on persons engaged in the business of selling at retail tangible personal property. 35 ILCS 120/2. The use tax is imposed at the same rate as the ROT. 35 ILCS 105/3-10; 120/2-10. The purpose of the use tax

is to prevent avoidance of the ROT by people who make purchases in states that do not impose the ROT and to protect Illinois merchants from the diversion of business to retailers outside Illinois. Brown's Furniture, Inc. v. Wagner, 171 Ill.2d 410, 418 (1996). If the person who uses the property does not pay the use tax to the retailer, it must be paid directly to the Department. 35 ILCS 105/3-45.

Section 12 of the Use Tax Act, 35 ILCS 105/12, incorporates by reference Section 5 of the Retailers' Occupation Tax Act ("ROTA"), 35 ILCS 120/1 *et seq.*, which provides that if the taxpayer fails to file a return, the Department shall determine the amount of tax due "according to its best judgment and information." 35 ILCS 105/12; 35 ILCS 120/5. A certified copy of the Department's determination of the amount of tax due "shall, without further proof, be admitted into evidence...and shall be prima facie proof of the correctness of the amount of tax due, as shown therein." *Id.* Once the Department has established its *prima facie* case by submitting the certified copy of the Department's determination into evidence, the burden shifts to the taxpayer to overcome this presumption of validity. Clark Oil & Refining Corp. v. Johnson, 154 Ill.App.3d 773, 783 (1<sup>st</sup>Dist. 1987). To prove his case, a taxpayer must present more than testimony denying the Department's assessment. Sprague v. Johnson, 195 Ill.App.3d 798, 804 (4<sup>th</sup> Dist. 1990). The taxpayer must present sufficient documentary evidence to support his claim. *Id.*; Balla v. Department of Revenue, 96 Ill.App.3d 293, 295 (1<sup>st</sup> Dist. 1981). It is well settled that tax exemption provisions are strictly construed in favor of taxation. Heller v. Fergus Ford, Inc., 59 Ill.2d 576, 579 (1975). The party claiming the exemption has the burden of clearly proving that he is entitled to the exemption and all doubts are resolved in favor of taxation. *Id.*

Section 3-5 of the Use Tax Act provides a list of items that are exempt from the use tax and provides, in relevant part, as follows:

Sec. 3-5. Exemptions. Use of the following tangible personal property is exempt from the tax imposed by this Act:

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(11) Farm machinery and equipment, both new and used, including that manufactured on special order, certified by the purchaser to be used primarily for production agriculture or State or federal agricultural programs.\*\*\* Farm machinery and equipment shall include precision farming equipment that is installed or purchased to be installed on farm machinery and equipment including, but not limited to, tractors, harvesters, sprayers, planters seeders or spreaders.\*\*\* 35 ILCS 105/3-5 (11).

Section 3-35 of the Act defines “production agriculture” as follows:

Sec. 3-35. Production agriculture. For purposes of this Act, “production agriculture” means the raising of or the propagation of livestock; crops for sale for human consumption; crops for livestock consumption; and production seed stock grown for the propagation of feed grains and the husbandry of animals or for the purpose of providing a food product, including the husbandry of blood stock as a main source of providing a food product. “Production agriculture” also means animal husbandry, floriculture, aquaculture, horticulture and viticulture. 35 ILCS 105/3-35.

The Illinois General Assembly authorized the Department to make, promulgate, and enforce reasonable rules and regulations relating to the administration and enforcement of the provisions of the UTA and ROTA. 35 ILCS 105/12; 35 ILCS 120/12. Pursuant to that authority, the Department has adopted a regulation defining “production agriculture,” in relevant part, as follows:

Production Agriculture, with respect to crops, is limited to activities necessary in tilling the soil, planting, irrigating, cultivating, applying herbicide, insecticide or fertilizer, harvesting and drying of crops.\*\*\***Activities such as the clearing of land, mowing of fence rows, creation of ponds or drainage facilities are not included,** nor are the operations involved in the storing or transporting of crops and produce. \*\*\* (emphasis added). 86 Ill.Admin.Code §130.305(f).

The Department acknowledges that applying farm chemicals and planting, cultivating and irrigating crops, assigned to 20% of the tractor’s use, qualify as production agriculture, but argues that the remaining 80% of use is expressly excluded from exemption under the Department regulation, 86 Ill.Admin.Code §130.305(f). Dept’s Brief, p. 4. Taxpayer takes a

broad view of what “production agriculture” means and argues that “so long as the tractor is used for various purposes on the real estate that is tillable farmland used for production of corn and soybeans,” it falls under the definition of production agriculture. Taxpayer’s Brief, p. 3.

Citing Mid-American Growers, Inc. v. Department of Revenue, 143 Il.App.3d 600 (3<sup>rd</sup> Dist. 1986), Taxpayer asserts that the courts have interpreted the definition of ‘Farm machinery and equipment’ broadly. Taxpayer’s Brief, p. 1. Mid-American Growers is distinguishable from the instant case. It primarily addressed the grouping of single units of lighting and heating system to meet the threshold exemption requirement of \$1,000. Whether the specialty lighting or heating equipment used for production agriculture was exempt from taxation was not in dispute. Also, Taxpayer’s point that the court in Mid-American Growers granted exemption for the carts, partially used for non-exempt use, is consistent with the statute requiring that farm equipment be used *primarily* for production agriculture; there is no broad interpretation of the statute.

The determining issue in the instant case is whether the Department’s regulations expressly excludes from exemption the activities devoted to 80% of the tractor’s use and whether the regulations are consistent with the enabling statute. The Department has defined the statutory phrase “production agriculture” by expressly including and excluding a class of activities from exemption. 86 Ill.Admin.Code § 130.305(f); Mid-American Growers at 605-06 (citing the definition of production agriculture in 86 Ill.Admin.Code §130.305(f)). With respect to crops, “[a]ctivities necessary in tilling the soil, planting, irrigating, cultivating, applying herbicide, insecticide or fertilizer, harvesting and drying of crops” are expressly included in the exemption. 86 Ill.Admin.Code § 130.305(f). Conversely, “[a]ctivities such as the clearing of land, mowing of fence rows, [and] creation of ponds or drainage facilities ...” are expressly excluded from exemption under the regulation. *Id.*

Taxpayer's core argument is that the regulation defines "production agriculture" too narrowly, so it is inconsistent with the enabling statute. It argues that the regulation cannot change the plain meaning of the enabling statute. Indeed, that is the settled law. If an administrative regulation is inconsistent with the statute under which it was adopted, the regulation will be held invalid. Hadley v. Illinois Department of Corrections, 224 Ill.2d 365, 385 (2007). Administrative regulations can neither expand nor limit the statute they enforce. Outcom, Inc. v. Department of Transportation, 233 Ill.2d 324, 340 (2009). However, an agency's interpretation of its regulations and enabling statute are "entitled to substantial weight and deference," given that "agencies make informed judgments on the issues based upon their experience and expertise and serve as an informed source for ascertaining the legislature's intent." Provena Covenant Medical Center v. Department of Revenue, 236 Ill.2d 368, 387, 339 (2010). Where an agency has been charged with a statute's administration and enforcement, a court will not substitute its own construction of a statutory provision where the agency has provided a reasonable interpretation. Hadley at 371. However, courts are not bound by an agency's interpretation that conflicts with the statute, is unreasonable, or is otherwise erroneous. *Id.*

Taxpayer generally argues that the activities in dispute are a necessary part of the production agriculture of corn and soybeans. Taxpayer's Brief p. 2. Specifically, it claims that one cannot operate the field cultivator or planter until the tree limbs and branches are removed.<sup>1</sup> I understand its argument, but Taxpayer failed to show how the Department's definition of "production agriculture" is unreasonable. The cited case authority establishes that to declare the regulation invalid, it is insufficient to simply argue that an interpretation is just as or even more

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<sup>1</sup> Taxpayer failed to address the issue of snow removal in the brief but previously argued that snow removal qualifies as production agriculture. *See* Taxpayer's Brief; Joint Ex. 4.

reasonable than that of the Department's; it must show that the Department's interpretation is unreasonable. As long as the Department provides a reasonable definition, the regulation is valid. Hadley at 371. In giving substantial weight and deference to the Department's definition, *supra*, I conclude that the applicable regulation is reasonable, thus, valid.

The next issue is whether the activities in dispute are expressly excluded from exemption under the regulation. Taxpayer argues that "clearing of land" is defined too widely and argues that the type of farm equipment used should be considered in determining whether an activity qualifies as production agriculture. It claims that "clearing of land by a bulldozer is not an integral part of production farming, while clearing fallen branches and brush prior to planting is." Taxpayer's Brief, p. 2. "Clearing of land" is a general and expansive phrase, inclusive of all objects removed in the clearing of land, which would include snow removal, representing 15% of use, and clearing of fallen trees and brush, representing 10% of use. There is no qualifier language in the regulation to except or limit the definition of "clearing of land," thus, it is immaterial which farm equipment, tractor or bulldozer, was used to clear the land of whatever objects. Mowing of fence rows, assigned to 30% of the use, is likewise expressly excluded from exemption. 86 Ill.Admin.Code §130.305(f).

As to the waterways maintenance and erosion control, assigned to 25% of the use, Taxpayer offered no evidence as to how the activities are necessary for tilling the soil, planting, irrigating, cultivating, applying herbicide, insecticide or fertilizer, harvesting and drying of crops. 86 Ill.Admin.Code §130.305(f). While stated differently, the activities are akin to creating ponds or drainage facilities, which are expressly excluded from exemption in the regulation. Even if making waterways and erosion control is not just another way of saying that the tractor was used to create ponds or drainage facilities, there is insufficient evidence to conclude that Taxpayer's

making of waterways and erosion control is included within the regulation's definition of production agriculture. 86 Ill.Admin.Code §130.305(f). Rules adopted by an administrative agency pursuant to statutory authority have the force of law and the administrative agency is bound by its rules. Department of Corrections v. Illinois Civil Service Commission, 187 Ill. App. 3d 304, 308 (1<sup>st</sup> Dist. 1989).

Taxpayer lastly argues that both State and Federal laws require correction of naturally occurring erosion from the tillage of highly erodible land. Taxpayer claims that to be in compliance with the laws, it has to maintain the waterways within the tillable acreage used for the production of corn and soybeans. Taxpayer's Brief, p. 3. In support of the argument, Taxpayer cites, without directing to a specific provision, Agricultural Areas Conservation and Protection Act ("AACPA"), 505 ILCS 5/3.01 *et seq.* My research does not indicate that there is a specific mandate in the AACPA for erosion control of highly erodible land. It generally addresses a creation of an "agricultural area" to protect farmlands from urban expansion, not of excessive soil erosion. *See* 505 ILCS 5/2 and 5/5. There is, however, as the Taxpayer argues, a federal mandate of erosion control of highly erodible land for the participants in the USDA Farm Program. Taxpayer is enrolled in the program and its eligibility is contingent upon continuous compliance with the USDA Farm Service Agency ("FSA") and the Natural Resources Conservation Service ("NRCS"). Stip. 8-10. Taxpayer has produced Form AD-1026, Highly Erodible Land Conservation (HELIC) and Wetland Conservation (WC) Certification,<sup>2</sup> signed by Taxpayer, dated August 2009. Joint Ex. 8. According to an Appendix to Form AD-1026, the signed certification means that a participant agrees to protect highly erodible land from excessive soil erosion by applying an approved conservation system. Joint Ex. 5. The certification, however, does not necessarily represent that a participant's farmland is

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<sup>2</sup> As there is no claim that Taxpayer's farmland is wetland, only the discussion of highly erodible land is applicable.

designated as highly erodible. The USDA's compliance brochure indicates that "Consult your FSA maps or contact your local FSA or NRCS Office to determine if any of your fields are designated as highly erodible land." Joint Ex. 6. The compliance certification, therefore, merely means that a participant agrees to apply an approved conservation system to the farmland *if* that farmland were designated as highly erodible. Taxpayer offered no evidence that its farmland is designed as highly erodible.<sup>3</sup> Accordingly, there is no evidence that the tractor at issue is used in State or Federal agricultural programs. I conclude that Taxpayer has failed to prove by clear and convincing evidence that the activities devoted to 80% of the tractor's use qualify as "production agriculture" under 35 ILCS 105/3-5 (11).

**Recommendation:**

For the foregoing reasons, I recommend that the Director finalize the Notice of Tax Liability as issued, with penalties and interest to accrue pursuant to statute.

December 14, 2015

Kelly K. Yi  
Administrative Law Judge

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<sup>3</sup> Page two of Form AD-1026 refers to Form AD-1026A for a declaration of NRCS designation of highly erodible land. Taxpayer did not offer into evidence a completed Form AD-1026A to establish that its farmland is designed as highly erodible by NRCS. Taxpayer's Report of Commodities Farm and Tract Detail Listing admitted into the record reports of no such designation. *See* Joint Exs. 5, 7.