

UT 04-8

Tax Type: Sales Tax

Issue: Machinery & Equipment Exemption – Manufacturing

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

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

v.

**ABC MARBLE & GRANITE
CO.,
Taxpayer**

**No. 02-ST-0000
IBT# 0000-0000
NTL# 00 00000000000000
00 00000000000000**

**Ted Sherrod
Administrative Law Judge**

RECOMMENDATION FOR DISPOSITION

Appearances: Special Assistant Attorney General George Foster on behalf of the Illinois Department of Revenue; Mark L. Rosenbloom, Esq. on behalf of ABC Marble & Granite Co.

Synopsis:

This matter comes for hearing following the timely protest by ABC Marble & Granite Co. (the “taxpayer”) of the Department’s Notices of Tax Liability number 00 00000000000000 and 00 00000000000000 covering the audit period July, 1999 through December, 2001. The Taxpayer was audited by the Department and as a result, was assessed use tax pursuant to the Illinois Use Tax Act (35 ILCS 105/1 *et seq.*) with respect to the purchase of machinery and equipment used in the production of custom made marble and granite countertops and on components used in the manufacture of these

countertops. During the hearing, the parties entered into joint stipulations wherein they agreed that the production of countertops constituted a manufacturing process and that the machinery and equipment at issue would qualify for the manufacturing machinery and equipment exemption authorized by 35 ILCS 105/3-5(18) if used to produce tangible personal property for retail sale. The parties also stipulated that components purchased for use in the production of countertops would be exempt components of tangible personal property intended for resale if the machinery and equipment qualified for exemption. At issue is whether the manufacturing machinery and equipment used to manufacture countertops qualified for exemption because used to produce tangible personal property for retail sale, and whether purchases of component parts used in this machinery and equipment were exempt purchases for resale. 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.

Findings of Fact:

1. The Department's prima facie case, inclusive of all jurisdictional elements was established by the admission into evidence of Notices of Tax Liability number 00000000000000 and number 0000000000000000, and the Audit Correction and/or Determination of Tax Due covering the audit period 7/1/99 through 12/31/01 showing total liability due and owing of \$55,588. Tr. pp. 21, 23; Department Group Ex. 1.¹

¹ Unless otherwise indicated, findings of fact apply to the audit period in controversy.

2. The taxpayer is an Illinois based subchapter S corporation having its place of business in Anywhere, Illinois. John Doe is the president of the taxpayer. Tr. p. 68; Department Group Ex. 1.
3. The taxpayer conducts business operations in Illinois by producing, selling, delivering and setting in place custom made granite and marble countertops for use primarily in bathrooms and kitchens to building contractors and sub-contractors, kitchen and bath shops and to the general public. Tr. pp. 18 - 20, 68 - 70.
4. The taxpayer employs between 20 and 25 persons including clerical employees and shop workers. Four of these employees are members of installation crews engaged in setting countertops on cabinets located at customer locations. Tr. pp. 135 - 137.
5. Each countertop produced by the taxpayer is custom designed according to the particular specifications and budget of each customer. Countertops range in price from \$100 to \$5,000 each and weigh up to 200 pounds. Employees of the taxpayer also discuss with the customer whether the customer wishes to have the countertop delivered and set in place on top of a pre-installed cabinet, which is an attachment to realty. Between 80% and 85% of the taxpayer's customers elect to have countertops delivered and set in place in this manner. The taxpayer describes this activity as "installation" on the taxpayer's estimate and proposal forms and invoices. Tr. pp. 69 -71, 75, 118, 119, 123, 124, 133, 134; Department Group Ex. 2.

6. When custom designing and producing countertops, the taxpayer takes into account plumbing and/or electrical work necessary to complete these items in accordance with customer specifications, and takes into account the location of sinks, faucets and other plumbing or electrical accessories necessary to accommodate the customer's intended use of the countertop. Accordingly, during production, holes are left in countertops for the affixation of these items. Plumbers usually supply plumbing accessories. Tr. pp. 68, 73 - 75, 81, 121, 123, 126, 145, 148, 149; Taxpayer's Ex. R-1.
7. The invoice for furnishing and installing countertops requires that the taxpayer pay a lump sum for delivery and installation of the countertops. 95% of countertops specified for installation at customer locations on estimate and proposal forms and invoices are placed in kitchens and bathrooms. Tr. p. 147; Department Group Ex. 2.
8. After the estimate and proposal has been agreed to, the taxpayer orders materials necessary to complete the countertops, including items for use in machinery and equipment used in the process of producing custom countertops. The taxpayer pays use tax to its vendors when it purchases materials used in the process of producing the countertops that are not used in countertop production machinery and equipment, and on materials that are unrelated to the production process. Tax is not paid on materials that are used in the production process and deemed incorporated into the countertops being sold, and the taxpayer gives resale certificates to its vendors covering these items. The Department's auditor determined that the tax should have been paid on these items because they were

not incorporated into countertops intended for retail sale as tangible personal property. The auditor also determined that the taxpayer did not make retail sales of countertops to customers. Tr. pp. 110, 149, 156, 157; Department Group Ex. 1; Taxpayer's Ex. R-8, R-9.

- 9.** After the estimate and proposal has been agreed to, the taxpayer has ordered all necessary materials, and has assembled them into a custom countertop in accordance with the customer's specifications, where taxpayer's estimate and proposal or invoice calls for installation, the taxpayer's installation crew delivers the countertop to the customer's location. Cabinets upon which countertops are to be placed at customer locations are attachments to realty. Tr. pp. 53, 69, 70, 118, 119, 122 - 125, 132, 134, 135, 136, 144, 145, 147.
- 10.** Upon delivery, the taxpayer's installation crew completes work designated as installation of the countertops on the customer's estimate and proposal or invoice by placing countertops on cabinets and using a shim to establish a level base line congruent with the cabinet dimensions to assure an exact fit between the countertop and the cabinet upon which it is placed. The taxpayer's installation crew then attaches the countertop with silicone and caulk to the top of the previously installed cabinet. When countertops become damaged, removal of damaged countertops prior to the installation of plumbing and /or electrical accessories takes up to fifteen minutes. Tr. pp. 69 - 72, 76, 118, 132, 137, 138, 145 - 147; Department Group Ex. 2.
- 11.** After all cabinet and countertop construction and installation is completed, the customer retains electricians and/or plumbers to make all necessary connections

for plumbing, lighting or kitchen appliances. The taxpayer is not responsible for, and does not arrange or perform any of these functions. Tr. pp. 68, 69, 126, 127, 131.

- 12.** The taxpayer uses machinery and equipment as part of the process of producing custom countertops. This machinery and equipment is used to cut grooves into stone. These grooves are essential to secure rods placed in the stone comprising the countertop to provide anchors for bolts which hold plumbing and accessories in place and secure plumbing to cabinets. The taxpayer's machinery and equipment also performs other functions necessary to install components that become integral parts of countertops. Tr. p. 123; Department Group Ex. 1.
- 13.** During the audit period at issue, the taxpayer purchased all or a portion of the aforementioned machinery and equipment at a cost price of \$507,392. The taxpayer did not pay Illinois use tax on its purchase of this machinery and equipment. Department Group Ex. 1.
- 14.** The Department conducted an audit of the taxpayer for the audit period at issue. As a result of this audit, the Department's auditor concluded that the aforementioned machinery and equipment purchased at a cost price of \$507,392 by the taxpayer on which tax was not paid, was not used to produce tangible personal property for retail sale and therefore did not qualify for the state's manufacturing machinery and equipment exemption. It therefore assessed the taxpayer for unpaid tax due on the purchase of this machinery and equipment. Accordingly, the Department issued a Notice of Tax Liability for use tax due on

these purchases. Department Group Ex. 1; Stipulations of Law and Fact, Taxpayer and Department Ex. 1 (hereinafter “Stip. 1”).

15. The taxpayer did not pay use tax on its purchase of consumable parts used in the aforementioned machinery and equipment to produce custom countertops. In lieu of paying tax on these items, the taxpayer issued resale certificates to its suppliers. The Department issued a Notice of Tax Liability for consumable parts used in the aforementioned machinery and equipment based on its audit finding that these parts were not used in machinery and equipment employed in the production of tangible personal property for retail sale and therefore could not be purchased tax free for resale. Department Group Ex. 1; Stipulations of Law and Fact, Taxpayer and Department Ex. 2 (hereinafter “Stip. 2”).

16. The Department and the taxpayer have stipulated that the production of countertops using the aforementioned machinery and equipment is a manufacturing process, and that the machinery and equipment used in this process qualifies for the manufacturing machinery and equipment exemption under Illinois sales and use tax law if it is used to produce tangible personal property for retail sale rather than items intended to be installed as attachments to realty by the taxpayer. Tr. pp. 15 – 17; Stip. 1.

17. The Department and the taxpayer have stipulated that consumable supplies used in the aforementioned machinery and equipment are exempt from Illinois use tax if the aforementioned machinery and equipment were used to produce tangible personal property for retail sale rather than items intended to be installed as attachments to realty by the taxpayer. Tr. pp. 15 – 17; Stip. 2.

Conclusions of Law:

The issue to be decided herein is whether machinery and equipment purchased at a cost price of \$507,392 used in the production of custom made countertops by the taxpayer are exempt from the imposition of Illinois use tax. The Department's determination that the taxpayer's purchases were not exempt, which is part of the record, is presumed correct. Masini v. Department of Revenue, 60 Ill. App. 3d 11 (1st Dist. 1978). Once the presumed correctness of the assessment is established, the burden shifts to the taxpayer to prove that the Department's determination is in error. Copilevitz v. Department of Revenue, 41 Ill. 2d 154 (1968); Central Furniture Mart v. Johnson, 157 Ill. App. 3d 907 (1st Dist. 1987); Vitale v. Department of Revenue, 118 Ill. App. 3d 210 (3rd Dist. 1983); Masini, *supra*.

The Use Tax Act imposes a tax "upon the privilege of using in this State tangible personal property purchased at retail from a retailer ... " 35 ILCS 105/3. There is no question that, unless expressly exempt by statute, the taxpayer's purchase of machinery and equipment at issue is, under the Use Tax Act, subject to the imposition of tax. The pertinent exemption claimed by the taxpayer reads as follows:

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

(18) Manufacturing and assembling machinery and equipment used primarily in the process of manufacturing or assembling tangible personal property for wholesale or retail sale or lease, whether that sale or lease is made directly by the manufacturer or by some other person, whether the materials used in the process are owned by the manufacturer or some other person, or whether that sale or lease is made apart from or as an incident to the seller's engaging in the service occupation of producing machines, tools, dies, jigs, patterns, gauges, or other similar items of no commercial value on special order for a particular purchaser.

35 ILCS 105/3-5 (18)

Statutes granting exemptions from taxation must be strictly construed and cannot be extended by judicial interpretation. Follett's Illinois Book and Supply Store, Inc. v. Isaacs, 27 Ill. 2d 600 (1963). In determining whether property is included within the scope of a tax exemption, all facts are to be construed and all debatable questions resolved in favor of taxation. Telco Leasing, Inc. v. Allphin, 63 Ill. 2d 305 (1976); Gas Research Institute v. Department of Revenue, 154 Ill. App. 3d 430 (1st Dist. 1987). Every presumption is against the intention of the state to exempt property from taxation. Follett's Illinois Book and Supply Store, Inc., *supra*. With respect to the manufacturing machinery and equipment exemption claimed by the taxpayer, by the very language of the statute, this exemption from the application of the use tax applies only when the machinery or equipment is used: 1) primarily to manufacture, 2) tangible personal property, 3) for wholesale or retail sale or lease. 35 ILCS 105/3-5 (18).

In this case, there is no dispute that the taxpayer purchased the machinery and equipment at issue for the sole purpose of assisting in the creation of custom made countertops from marble or granite and other raw ingredients. The parties have stipulated that using this machinery and equipment for such purposes is a manufacturing process. Stip. 1. Moreover, the record indicates that the countertops, prior to installation pursuant to estimate and proposal agreements with customers, are tangible personal property. Tr. pp. 68, 69; Taxpayer's Ex. R-1. At issue, then, is the requirement that machinery and equipment qualifying for exemption be used primarily to manufacture tangible personal property for wholesale or retail sale or lease. 35 ILCS 105/3-5 (18). It is this statutory

requirement that the taxpayer fails to meet, thus rendering the manufacturing machinery and equipment exemption inapplicable in this case.

The taxpayer engages in a business having at least two distinct components. First, it manufactures custom countertops, which it sells and delivers, but does not install. Tr. pp. 69 – 71, 126, 139, 140, 142, 143. In this respect, it functions similarly to the taxpayer in Van's Material Company, Inc. v. Department of Revenue, 131 Ill. 2d 196 (1989). In Van's Material the taxpayer combined raw material in the hollow of drum mixers on ready-mix concrete trucks. In so doing, ready-mix concrete was manufactured. *Id.* at 199, 205. The taxpayer then unloaded the produced concrete at the purchaser's delivery site. All that Van's Material did was manufacture, sell and deliver the concrete to its purchaser. Subsequently, the purchaser used the concrete to form part of real estate. *Id.* at 204. The Illinois Supreme Court held that the machinery and equipment at issue in Van's Material was exempt from the imposition of use tax and Retailers' Occupation Tax because the taxpayer proved that it used the machinery primarily to manufacture tangible personal property that it sold at retail.

During the audit, the taxpayer cited Van's Material as a basis for applying the manufacturing machinery and equipment exemption to the taxpayer in this case. Department Group Ex. 1. The record shows that the taxpayer sells only 15% to 20% of the custom countertops it manufactures without installation. Tr. pp. 71, 126, 139, 140, 142, 143. The taxpayer claims that it also sold the remaining 80% to 85% of custom countertops it manufactured without installing them to real property so as to become attachments to realty, which the Department disputes. Department Group Ex. 1. The taxpayer in Van's Material sold 100% of the product it manufactured without installation

to real property by the taxpayer. Accordingly, Van's Material is precedent for applying the manufacturing machinery and equipment exemption to the taxpayer only if the countertops remain tangible personal property after installation by the taxpayer.

The Department contends that the countertops that the taxpayer installs do not remain tangible personal property because the taxpayer is a “construction contractor” pursuant to regulation 86 Ill. Admin. Code, ch. I, sec. 130.1940.² Under Illinois case law, use tax is imposed upon any person purchasing building materials for installation into real property. G.S. Lyon & Sons Lumber and Manufacturing Company v. Department of Revenue, 23 Ill. 2d 180 (1961). Such persons constitute construction contractors under the aforementioned regulation. Construction contractors are deemed engaged in the sale of real estate rather than tangible personal property and, accordingly, their sales do not constitute retail sales of tangible personal property. Craftsmasters, Inc. v. Department of Revenue, 269 Ill. App. 3d 934 (4th Dist. 1995). This is true because the phrase “sale at retail” means a sale to a purchaser for final consumption. See 35 **ILCS** 120/1. A sale of building materials to a builder or installer for installation by the builder or installer is a sale to the builder or installer for final use or consumption by him, and not a sale to the builder’s or installer’s customer. G.S. Lyon, supra; Spurgeon v. Department of Revenue, 52 Ill. App. 3d 29 (3d Dist. 1977) (Recognizing the validity of Department rules deeming installers to be users or consumers of tangible personal property purchased for installation to realty by the installer).

² Administrative regulations have the force and effect of law and are construed under the same standards which govern the construction of statutes. Union Electric Co. v. Department of Revenue, 136 Ill. 2d 385, 391 (1990). Administrative interpretations by the agency charged with administering a statute are entitled to respect and deference from a reviewing court, but are not binding on the court. Such rules cannot limit or extend the scope of a statute. Van's Material Co. v. Department of Revenue, 131 Ill. 2d 196, 202, 203 (1989).

The taxpayer contends that an installer can be treated as a construction contractor only if it permanently installs tangible personal property to realty, citing in support of this claim Illinois Dept. of Rev. Letter Ruling No. ST 93-0150-PLR, 4/8/93 and Illinois Dept. of Rev. Letter Ruling No. ST 93-0532-PLR, 10/15/93. Tr. pp. 111, 112. See also Illinois Dept. of Rev. Letter Ruling No. ST 01-0027-PLR, 7/5/01. The taxpayer argues, moreover, that it does not permanently install custom countertops to cabinets and other types of real property because additional work, arranged for by customers independently, and performed by plumbers and others, is necessary to permanently secure these items to realty. Tr. pp. 19, 20. The Illinois case law makes it clear that custom made tangible property designed to be installed to realty can be sold as tangible personal property if the seller is not engaged in the actual installation of such items. Spurgeon v. Department of Revenue, 52 Ill. App. 3d 29 (3d Dist. 1977); Van's Material, *supra*. Accordingly, to resolve this case, it must be determined whether the activity engaged in by the taxpayer results in the installation of the countertops in a manner such that the taxpayer can be treated as a construction contractor for Illinois tax purposes.

The term “construction contractor” is defined at 86 Ill. Admin. Code, ch. I, sec. 1940(a)(1)³ as follows:

- (1) “Construction Contractor.” The word “construction contractor” when used in this Subpart includes general contractor, subcontractor and specialized contractor such as a landscape contractor. “Contractor” means any person who is engaged in the occupation of entering into and performing construction contracts for owners.

³ Regulation 86 Ill. Admin. Code, ch. I, sec. 130.1940 implements the Supreme Court’s decision in G.S. Lyon & Sons Lumber and Manufacturing Co. v. Department of Revenue, 23 Ill. 2d 180 (1961). In this case, the court ruled that building material incorporated into a structure loses its identity as personal property and is converted into real estate. Because the Retailers’ Occupation Tax applies only to retail sales of tangible personal property and not to real estate sales, the sale of material to the builder was held to be the final sale subject to tax and the builder was determined to be the user or consumer of the materials.

A “construction contract” is defined as follows:

(6) “Construction Contract” means a contract, written or oral, to “construct” ... a “structure” ... or to otherwise incorporate tangible personal property into real estate.

86 Ill. Admin. Code, ch. I, sec. 130.1940(a)(6)

The term “construct” is defined as follows:

(3) “Construct” means build, erect, construct, reconstruct, install, plant, repair, renovate or remodel.

86 Ill. Admin. Code, ch. I, sec. 1940(a)(3)

This regulation further provides as follows:

Certain sales of building materials purchased for incorporation into real estate located in an enterprise zone are exempt from Retailers’ Occupation Tax Liability (see Section 130.1951 of this Part). Certain sales of building materials purchased for incorporation into real estate located in an area designated by the Department of Commerce and Community Affairs under Section 5.5 of the Illinois Enterprise Zone Act are exempt from Retailers’ Occupation Tax liability. (see Section 130.1952 of this Part).

86 Ill. Admin. Code, ch. I, sec. 130.1940(e)

Regulation 86 Ill. Admin. Code, ch. I, sec. 130.1940 provides that a taxpayer is properly classified as a construction contractor if it enters into agreements or contracts with customers to incorporate tangible personal property into real estate. Again, while the taxpayer does enter into agreements with customers to install countertops, the taxpayer argues that this does not make it a construction contractor because the installation it performs does not incorporate tangible personal property (the countertops) into real estate.

The examples enumerated in subparts (b)(2) and (c)(1) of regulation 86 Ill. Admin. Code, ch. I, sec. 130.1940, and in regulation 86 Ill. Admin. Code, ch. I, sec.

130.1951 (crossed referenced in regulation 130.1940(e)) provide guidance regarding the classification of the taxpayer's countertops at issue in this case.⁴ Regulation 130.1940 (b)(2) lists as examples of items that remain tangible personal property after installation the following: "furniture and furnishings, curtains, drapes, (unattached) floor covering ... trade fixtures and machinery ... gas or electric stoves, refrigerators, washing machines, portable ventilating units and other portable equipment of this kind ..." Regulation (c)(1) lists as examples of items that ordinarily become attachments to realty when installed the following: "screen doors and windows; storm doors and windows; weather stripping; insulation material; Venetian blinds; window shades; awnings; cabinets built into the structure; (cemented) floor coverings ... plumbing systems or parts thereof, such as bathtubs, lavatories, sinks, faucets, water pumps, water heaters, water softeners, water pipes, etc.; heating systems or parts thereof, such as furnaces, stokers, boilers, heating pipes, etc. ; ventilation systems or parts thereof; commercial refrigeration systems or parts thereof; electrical systems or parts thereof; brick; lumber; sheet metal; roofing materials, and other similar items." Regulation 86 Ill. Admin. Code, ch. I, sec. 130.1951(e) also enumerates many of the aforementioned items in explaining what property becomes an attachment to realty upon installation.

While none of the foregoing regulations address the status of countertops (and this issue is not addressed by any other regulations or Illinois case law), 86 Ill. Admin. Code, ch. I, sec. 130.1940(b)(2) is particularly instructive. It provides in part as follows: "(A) construction contractor incurs Retailers' Occupation Tax liability when he sells ... floor

⁴ Retailers' Occupation Tax regulations enumerating exemptions, such as reg. 130.1940 also apply to the use tax at issue in this case. See 86 Ill. Admin. Code, ch. I, sec. 150.101; 86 Ill. Admin. Code, ch. I, sec. 150.301.

covering (except when he cements or otherwise permanently affixes the floor covering to a portion of the building)." (emphasis added) Identical, or substantially similar provisions are found at regulation 130.1940(c)(1) and at 86 Ill. Admin. Code, ch. I, sec. 130.1951(e)(8) ("floor coverings such as tile, linoleum and carpeting that are glued or otherwise permanently affixed to the real estate" [emphasis added] treated as attachments to realty under this regulation). Moreover, with the exception of machinery, the tax classification of which is governed by 35 **ILCS** 105/3-5(18), the examples in regulation 130.1940 (b)(2) indicate that tangible personal property that is not "cemented or otherwise permanently affixed" to realty such as furniture, curtains, drapes, trade fixtures,⁵ portable appliances and other portable equipment are properly classified as tangible personal property. Although the subparts of regulations quoted above address the classification of carpeting and floor coverings, the language used clearly equates the phrase "permanently affixed" with the affixation of tangible personal property to realty by cementing or gluing. Moreover, the Department's published letter rulings, which are cited as authority by the taxpayer for its position in this case, have applied this understanding of the phrase "permanently affixed" to tangible personal property other than floor coverings and carpeting. See Illinois Dept. of Rev. Letter Ruling No. ST 01-0022-GIL, 1/31/01 (signs affixed to real estate fixtures by gluing constitute attachments to realty); Illinois Dept. of Rev. Letter Ruling No. ST 91-0330-PLR, 4/17/91 (casings cemented to real estate constitute attachments to realty). While these rulings are not binding precedents, they offer insight into the Department's interpretation of its

⁵ The Department has defined trade fixtures as free-standing floor fixtures used in retailing and other facilities. See Illinois Dept. of Rev. Letter Ruling No. ST 95-0144-GIL, 3/15/95; Illinois Dept. of Rev. Letter Ruling No. ST 88-0698-PLR, 9/29/88.

governing statutes, a role that the courts have recognized. Container Corp. of America v. Wagner, 293 Ill. App. 3d 1089, 1096 (1st Dist. 1997); Oscar L. Paris Co. v. Lyons, 8 Ill. 2d 590, 598 (1956), *quoting* Skidmore v. Swift & Co., 323 U.S. 134 (1944) (“We consider the rulings, interpretations and opinions of the Administrator under this Act, while not controlling upon the courts by reason of their authority, do constitute a body of experience and informed judgment to which courts and litigants may properly resort for guidance”). Indeed, the Illinois courts have stated that substantial weight and deference should be accorded to the interpretations of laws by the agency charged with their administration and enforcement. King v. Industrial Commission, 189 Ill. 2d 167, 171 (2000); Central City Education Association v. Illinois Educational Labor Relations Board, 149 Ill. 2d 496, 510 (1992); City of Decatur v. American Federation of State, County and Municipal Employees, Local 268, 122 Ill. 2d 353, 361 (1988); Airey v. Department of Revenue, 116 Ill. 2d 528, 536 (1987). By statute, the authority to administer and enforce Illinois revenue laws is vested with the Department of Revenue. 20 ILCS 2505/2505-1 *et seq.*

The record in this case shows that the taxpayer attached the countertops to real estate using caulk and silicone. Tr. pp. 70, 72, 132, 138. The manner of affixation employed by the taxpayer is comparable to gluing or cementing tangible personal property to real estate. See Letter Ruling ST 91-0754-PLR, 10/3/91 (recognizes caulk as an adhesive similar to glue or cement). As a practical matter, caulk, like glue and cement, is ordinarily understood to provide permanent adhesion between surfaces to which it is applied. See Letter Ruling No. ST 97-0080-GIL, 2/11/97 (confirming that taxpayers in the business of fabricating and installing stone countertops to realty using

caulk and screws, are construction contractors when countertops are fabricated for the purpose of becoming attachments to real estate). Accordingly, the language used in the aforementioned regulations, and interpretations of the term “construction contractor” contained in Department rulings support the conclusion that the taxpayer was engaged in the installation of tangible property to realty when it caulked countertops to cabinets constituting real estate located at customer locations under agreements requiring it to install countertops.

The taxpayer argues that the degree of permanency with which tangible personal property is attached to realty should be used to determine whether the property is permanently affixed. Thus it argues that it did not permanently affix countertops by caulking them because it used only a thin layer of caulk or silicon to affix countertops to cabinets. Tr. pp. 70, 74, 132, 188, 189. First, I do not find testimony that the countertops were not firmly attached to cabinets to be credible. The taxpayer contends that the purpose for caulking or affixing the countertops in the manner testified to was to prevent damage due to inadvertent bumping or contact by workmen performing other functions. Tr. pp. 70, 132, 188, 189. However, the record also shows that countertops were all quite heavy items, weighing as much as 200 pounds and were solid rock. Tr. pp. 75, 76; Taxpayer’s Ex. R-1. It is difficult to imagine heavy marble or granite countertops of this nature being sufficiently at risk of damage from inadvertent contact by workmen to warrant any form of affixation primarily for this reason.

Furthermore, such risk of damage would be paramount if significant aspects of installation were left to plumbers and others over whom the taxpayer had no control, a risk I do not find it plausible to believe the taxpayer would assume. Consequently, I

cannot accept the taxpayer's explanation of why affixation during the countertop installation process was necessary. If affixation to protect the countertop was not necessary primarily for the reasons given by the taxpayer's witnesses, one can only conclude that caulking and affixing the countertop to the cabinet was designed to provide adherence after installation of plumbing or electrical devices was completed.⁶

Notably, the record contains conflicting evidence regarding whether countertops were routinely removed during plumbing and fixture installation. While Mr. Doe, the taxpayer's president, testified that removal was routine (Tr. pp. 72 – 75), this testimony is contradicted by the taxpayer's own expert witness (Tr. pp. 86 – 89). Disregarding Mr. Doe's anecdotal (Tr. pp. 72, 73) and obviously self-serving testimony, the record contains no credible evidence that countertops were removed or detached after installation. Moreover, the record contains no evidence that the taxpayer collected retailers' occupation tax on installed sales of countertops, even though tax collection would have been mandatory if these were indeed retail sales of tangible personal property as the taxpayer claims. See 86 Ill. Admin. Code, ch. I, sec. 130.101(d). The absence of credible evidence that countertops were to be removed before plumbing installation, or evidence that tax was collected on countertop sales lends credence to the Department's determination.

Finally, the record indicates that the removal of countertops from the cabinets could take up to fifteen minutes. Tr. p. 72. This suggests a degree of affixation far greater than the taxpayer's other testimony would have one believe.

⁶Note also that caulk used to affix countertops to cabinets was also used to waterproof the area surrounding the countertop. Tr. pp. 85, 86. This fact suggests that the caulk was intended to remain in place after installation of water fixtures by plumbers.

Even if the facts supported the taxpayer's claim that caulking was intended to lightly affix countertops to the cabinets, this evidence fails to support a finding that the taxpayer is not a construction contractor. This is true because the taxpayer's interpretation of regulation 86 Ill. Admin. Code, ch. I, sec. 130.1940 to base permanent installation on the degree of adherence between tangible personal property and real estate is without merit. The examples in this regulation make it clear that the manner of affixation itself is the controlling test. Thus carpeting is permanently attached if it is cemented to real property. It makes no difference whether it is lightly cemented with a thin layer of cement or not. Pursuant to the examples given in the regulations noted above, the act of cementing the carpeting to a floor surface is sufficient to render the carpeting an attachment to realty. 86 Ill. Admin. Code, ch. I, sec. 130.1940(b)(2), (c)(1). Conversely, portable tangible personal property that can be unplugged or similarly detached does not constitute an attachment to realty irrespective of the degree of attachment of the plug or other bond. 86 Ill. Admin. Code, ch. I, sec. 130.1940(b)(2). For example, a portable appliance that is installed by being plugged into a plumbing system would not constitute an attachment to realty for tax purposes even if plumbing connections were difficult to detach from realty because regulation 130.1940(b)(2) provides that such items remain tangible personal property after installation.

Accordingly, given the *de minimis* weight afforded testimony about the degree of affixation and the fact that countertops were caulked to real property, which appears to be a form of permanent affixation by analogy to the Department's regulations and letter rulings, and the lack of credible evidence that countertops were ordinarily removed after installation by the taxpayer, I conclude that the taxpayer was a construction contractor by

virtue of its installation of countertops. Since the taxpayer was installing tangible personal property to real property when it affixed countertops, it was not engaged in the production of tangible personal property for retail sale when it produced them primarily for this purpose using machinery and equipment at issue in this case. Accordingly, it cannot be deemed engaged in the production of tangible personal property primarily for retail sale using the machinery and equipment that it purchased. Since the machinery and equipment was not primarily used to produce tangible personal property for wholesale, or retail sale or lease as required to qualify for the manufacturing machinery and equipment exemption pursuant to 35 ILCS 105/3-5 (18), this exemption does not render the taxpayer's purchase of such tangible personal property immune from the imposition of use tax imposed by the Illinois Use Tax Act.

Moreover, the taxpayer's reliance upon Van's Material as a basis for treating countertops as tangible personal property is without merit. The record shows that the taxpayer used the machinery and equipment at issue to produce all of the countertops it sold. Even though 15% to 20% of the taxpayer's countertops were sold without installation to realty, the Van's Material case, where 100% of tangible personal property was sold without such installation, does not support the taxpayer's claim that it used machinery and equipment primarily to produce tangible personal property. The primary use of the taxpayer's machinery and equipment was to produce property for installation to realty by the taxpayer, which occurred in 80% to 85% of the taxpayer's countertop sales transactions. Accordingly, the taxpayer, not the taxpayer's customer, was the primary user or consumer of the countertops. G&S Lyon & Sons Lumber and Manufacturing Company, supra.

Sales of tangible personal property that, as an ingredient or constituent part, goes into and forms a part of manufactured tangible personal property subsequently sold at retail are exempt from sales and use tax as sales for resale. 35 ILCS 120/1; 35 ILCS 105/2; 86 Ill. Admin. Code, ch. I, sec. 130.210; 86 Ill. Admin. Code, ch. I, sec. 130.215. The taxpayer and the Department have jointly stipulated that component parts purportedly purchased for resale, on which no tax was paid at time of purchase by the taxpayer, constitute purchases for resale if the machinery and equipment in controversy was used to produce tangible personal property for retail sale. Stip. 2. However, as enumerated above, I find that the taxpayer's machinery and equipment at issue in this case was not used for this purpose. Accordingly, in accordance with the stipulation agreed to by both parties, I find that the Department properly assessed use tax on component parts used in the taxpayer's machinery and equipment on which no tax was paid at time of purchase.

WHEREFORE, for the reasons stated above, it is my recommendation that the Department's Notices of Tax Liability number 00 0000000000000 and 0000000000000 be upheld in their entirety.

Ted Sherrod
Administrative Law Judge

Date: 11/5/2004