MV 97-2
Tax Type: MOTOR VEHICLE USE TAX
Issue: Rolling Stock (Vehicle Used Interstate For Hire)
Machinery and Equipment Exemption - Manufacturing

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

THE DEPARTMENT OF REVENUE	)	**No.**
OF THE STATE OF ILLINOIS	)	**No.**
	)	**IBT No.**
v.	)	**IBT No.**
	)	**NTL:**
	)	**NTL:**
TAXPAXYER,	)	**NTL:**
	)	**Charles E. McClellan**
Taxpayer	)	**Administrative Law Judge**
	)	

RECOMMENDATION FOR DISPOSITION

APPEARANCES: John D. Alshuler, Special Assistant Attorney General, for the Department of Revenue; James Jacobson and Joanne Giger, Griffith & Jacobson, for TAXPAYER.

Synopsis:

This matter came on for hearing pursuant to the taxpayers' timely protest of Notices of Liability issued by the Department on August 21, 1992, May 4, 1993, and June 24, 1994, to TAXPAYER ("taxpayer") for Illinois Use Tax for the months of June 1989, March 1990, and May 1991. An evidentiary hearing was held on September 28, 1995, at 100 West Randolph, Chicago, Illinois. The issue is whether the taxpayer is liable for Illinois Use Tax in connection with the purchase of a Mack truck tractor and two Heilbilt trailers it purchased during the audit period for use in its business. Taxpayer contends that the vehicles are exempt either as rolling stock used in interstate commerce or as manufacturing equipment. Following the submission of all evidence and a review

of the record, I recommend that this matter be resolved in favor of the Department.

Findings of Fact:

1. By stipulation of the taxpayer and the Department at the hearing in this matter, Notice of Tax Liability XXXXX dated September 23, 1992, was withdrawn in the consolidation of case numbers MV970001 and MV970002, and, at the request of the taxpayer, Notice of Tax Liability XXXXX was consolidated with these cases. (Tr. p. 6).

2. The Department audited the books and records of the taxpayer for the months of June 1989, March 1990, and May 1991. (Dept. Group Ex. No. 1).

3. The Department's prima facie case, including all jurisdictional elements, was established by the admission into evidence of the Correction of Returns showing additional tax due of $9,937. (Dept. Group Ex. No. 1).

4. Taxpayer is an asphalt paving contractor. (Tr. pp. 17-19).

5. Taxpayer's offices are located in La Grange, Illinois. (Tr. p. 15).

6. Taxpayer has an asphalt plant in Hodgkins, Illinois and another one in Elgin, Illinois. (Tr. p. 17).

7. Taxpayer makes asphalt for paving roadways, driveways and parking lots, etc., in these plants by mixing aggregate with liquid asphalt which functions as glue to hold the aggregate together. (Tr. p. 18).

8. During the mixing process, the asphalt and the aggregate are heated to approximately 300 degrees. (Tr. p. 18).

9. The hot asphalt is then dumped into taxpayer's trucks and hauled to the construction site where it is dumped into a paver which spreads and compacts the asphalt into the proper thickness and grade on the road or other construction site. (Tr. p. 19).

10. After the asphalt paving material has cooled to the appropriate temperature, it is rolled to compact it further. (Tr. p. 20).

11. The Illinois Department of Transportation (IDOT) accounts for about half of taxpayer's business with surrounding municipalities accounting for another 25%. (Tr. p. 16).

12. IDOT specifies the formulas for the asphalt mixtures used on its road projects. (Tr. p. 23).

13. For IDOT projects, taxpayer is required to purchase sand, aggregate, liquid asphalt and other ingredients from suppliers approved by IDOT. (Tr. p. 23).

14. To make roadways more skid resistant, one of the ingredients IDOT specifies is slag which is material left over from steel production. (Tr. p. 24).

15. Taxpayer obtains liquid asphalt from an CORPORATION plant in Whiting, Indiana. (Tr. p. 24).

16. Taxpayer obtains the slag material from sources in Indiana. (Tr. p. 33).

17. In the case of asphalt roadways that taxpayer is resurfacing, IDOT requires taxpayer to recycle the existing asphalt by tearing it up with machines called "grinders", hauling it to its asphalt plants and using it as an ingredient in the asphalt mix. (Tr. pp. 54, 55).

18. The trailers at issue in this case are used to haul slag from the vendors in Indiana to taxpayer's asphalt plants. (Tr. pp. 38, 52).

19. The Mack truck and the trailers involved in this case are used generally in taxpayer's business to haul liquid asphalt in tankers, slag, ground up asphalt to be recycled in taxpayer's asphalt plants, and hot asphalt to construction sites.. (Tr. pp 32, 38, 52, 53, 55, 61).

20. Taxpayer also does asphalt paving work for the Indiana Department of Transportation. (Tr. p. 51).

Conclusions of Law:

The evidence on record in this case, consisting of the hearing transcript and exhibits, establishes that the taxpayer has failed to overcome the Department's *prima facie* case of tax liability under the assessment in question. Accordingly, by such failure, and under the reasoning set forth below, the determination by the Department that TAXPAYER owes the tax liability set forth in Notices of Tax Liability XXXXX, XXXXX, and XXXXX must stand as a matter of law. In support thereof, the following conclusions are made:

ISSUE No. 1

The first issue is whether the two trailers and the truck tractor are exempt as rolling stock used in interstate commerce. Section 3-55(b) of the Illinois Use Tax Act (35 ILCS 105/3-55(b)) exempts tangible personal property used in Illinois by an interstate carrier for hire as rolling stock moving in interstate commerce. The exemption does not apply to vehicles which a taxpayer is using to transport its own employees or property or property which it is selling and delivering to its customers. (86 Admin. Code ch. I § 130.340). Taxpayer alleges that it never takes title to the slag, liquid asphalt or the ground up asphalt it hauls between Indiana and Illinois and is, therefore an interstate carrier for hire. (Tr. pp. 7-9). The record does not support this argument, however. Taxpayer's exhibits indicate that it is the owner of the liquid asphalt and the slag that it hauls. Taxpayer's group exhibit number 1 consists of two bills of lading for loads of liquid asphalt it obtained from CORPORATION, in Whiting, Indiana. It lists taxpayer as both the shipper and the consignee. Taxpayer's group exhibit number 2 consists of three material allowance affidavits by which taxpayer billed IDOT for slag and freight. (Tr. p. 35). It stands to reason that IDOT would not allow itself to be billed for slag it already owns. Taxpayer's group exhibit number 3 consists of a number of trip tickets for slag sold by Hecket Slag Sales in Whiting, Indiana. Taxpayer is listed as the customer on each one. In addition, taxpayer's controller testified

that the billing procedure is for the slag and liquid asphalt suppliers to invoice taxpayer and that taxpayer then invoices IDOT. (Tr. pp. 68, 71). This testimony coupled with taxpayer's first three exhibits lead to the conclusion that the equipment in question was used by taxpayer to haul its own slag and liquid asphalt for use in fulfilling its road paving contracts.

Taxpayer alleged further that the ground up asphalt that it hauled to its asphalt plants for recycling belonged to IDOT which made taxpayer an interstate carrier for hire. A taxpayer can overcome the Department's *prima facie* case by producing competent evidence identified with the taxpayer's books and records. Vitale v. Department of Revenue, 118 Ill.App.3d 210 (3d Dist. 1983). In this case taxpayer did not introduce any contracts it had with IDOT or any other evidence that would support the allegation that it was hired by its customers to grind up asphalt and haul it for them across state lines. Nor did it introduce any evidence that any ground up asphalt was hauled across state lines. In any case, conducting business as a paving contractor is not the same as being an interstate carrier for hire. Accordingly, taxpayer has failed to prove that it used the equipment in question as an interstate carrier for hire.

ISSUE No. 2

The second issue is whether the equipment in question is exempt as machinery and equipment used in manufacturing. Taxpayer argues that the process of manufacturing asphalt for paving highways, parking lots, etc., does not end until all of the processes at the construction site are done. (Tr. p. 11). Taxpayer argues further that the asphalt roads are not permanently affixed to real estate but remain personal property. (Tr. p. 12).

The statutory provision at issue is Section 3-5(18) of the Illinois Use Tax Act which provides an exemption for "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 . . .." (35 ILCS 105/3-5(18)). Equipment used to deliver tangible personal property does not qualify

for the exemption, nor does equipment used to produce personal property manufactured for personal use. (86 Admin. Code ch. I, § 130.330.

First, in this case, the record indicates that taxpayer is manufacturing tangible personal property, asphalt, primarily for its own use in fulfilling its road construction contracts. IDOT and most of taxpayer's other customers are not purchasing asphalt, but, rather, they hire taxpayer to undertake asphalt paving contracts. Taxpayer uses the asphalt that it manufactures to fulfill its own contractual obligations.

In addition, taxpayer argues that the hot asphalt is still being "manufactured" when it is kept hot in the trailers as it is transported to the job sites. However, nothing happens to the slag, the liquid asphalt or the ground up asphalt as it is being transported to taxpayer's asphalt plants. It is only when this raw material is placed in an asphalt plant and mixed and heated that manufacturing of tangible personal property takes place. Taxpayer then loads the hot asphalt in trailers for transport to the construction site where it is used by the taxpayer in improving real estate. Nothing happens to the hot asphalt while it is in transport. When it arrives at the construction site, it is dumped into a paver which spreads and compacts the asphalt into the proper thickness and grade on the road or other construction site. (Tr. p. 19).

This process at the construction site and the subsequent compacting are not processes that manufacture tangible personal property. These processes are converting tangible personal property, the asphalt, into a real property improvement, a roadway. Grading, paving and repaving roadways constitute making improvements to real property. Billman v. Crown-Trygg Corp., 205 Ill. App. 3d 916 (1st Dist. 1990). See also, Thomas M. Madden and Company v. Department of Revenue, 272 Ill.App.3d 212 (2nd Dist. 1995).

Taxpayer argues that the issue in this case is determined by the court's decision in Van's Material Co. v. Dept. of Revenue, 131 Ill.2d 196 (1989) which held that ready-mix concrete trucks qualified for exemption as manufacturing

equipment that produced tangible personal property for sale. This case is factually distinguishable from Van's. First of all, the ready-mix trucks involved in the Van's case did the manufacturing. Raw materials were placed in the truck mounted mixing drums, powered by the truck engine, which turned the raw materials into ready-mix concrete as the trucks traveled to the construction sites. In this case, raw materials are converted into paving asphalt in taxpayer's asphalt plants. When that manufacturing process is completed, the asphalt is transferred to trailers for transport to the construction site. To qualify as a manufacturing process, existing materials must be changed into materials with a different form, use or name. (35 ILCS 105/3-50, 86 Admin. Code ch. I, § 130.330). In addition, the process must be commonly regarded as manufacturing. *Id.* Nothing happens to the asphalt while it is in the trailers at issue in this case. Although taxpayer's controller testified that to haul hot asphalt, the trailers must be specially treated, be equipped with a tarpaulin to keep the asphalt hot while in transport, and be equipped with a special rear end for dumping asphalt (Tr. p. 18) that is not evidence of any manufacturing taking place on the trucks because there is no change to the form, use or name of the asphalt. It arrives as hot asphalt at the construction site in the same form, for the same use and with the same name as it had when it was loaded on the trailer at the asphalt plant.

The trailers and the truck in question do not manufacture anything. They function to transport asphalt to construction sites, where the asphalt is converted to roadways, parking lots, etc., all of which are real property, not tangible personal property.

Second, the taxpayer in Van's did not convert tangible personal property to real property as the taxpayer does in this case. The taxpayer in Van's sold tangible personal property, ready-mix concrete, to road contractors who, in turn, converted the concrete into real property. The taxpayer in this case does not sell tangible personal property in connection with its paving contracts. It

converts it into real property. On this point, taxpayer argues that the asphalt remains tangible personal property after it is made into a roadway because it can be torn up with a grinder and recycled. Taxpayer argues that an asphalt roadway is different from a concrete roadway because it is less permanent. Even if that is true, an asphalt roadway is still permanently affixed to land. It is not readily moveable, and it cannot be removed without grinding it up. In summary, the truck and the two trailers at issue in this case do not qualify for the manufacturing equipment exemption because they are not used primarily in the manufacture or assembly of tangible personal property for sale or resale.

It is well established in Illinois that "[a] person claiming an exemption from taxation has the burden of proving clearly that he comes within the statutory exemption. Such exemptions are to be strictly construed and doubts concerning the applicability of the exemptions will be resolved in favor of taxation." United Air Lines, Inc. v. Johnson, 84 Ill.2d 446, 455 (1981). In addition, there is the presumption in Illinois against the intent to exempt property from taxation. *Id* at 456. For these reasons, the truck and trailers at issue do not qualify for the exemption for rolling stock used by an interstate carrier for hire, or for the manufacturing machinery and equipment exemption.

WHEREFORE, for the reasons stated above, it is my recommendation that the Department's assessment be upheld in full.

Date

Charles E. McClellan
Administrative Law Judge