

FINANCE AND ADMINISTRATION CABINET
Department of Revenue
(Amended at ARRS Committee)

103 KAR 30:120. Machinery for new and expanded industry.

RELATES TO: KRS 139.010, 139.470, 139.480, 241.010, 243.030, 243.040

STATUTORY AUTHORITY: KRS 131.130(1)

NECESSITY, FUNCTION, AND CONFORMITY: KRS 131.130(1) authorizes the Department of Revenue to promulgate administrative regulations for the administration and enforcement of Kentucky tax laws. KRS 139.480 exempts specified property from sales and use taxes. This administrative regulation interprets the sales and use tax law as it applies to exemption qualification for "machinery for new and expanded industry."

Section 1. Definitions.

- (1) "Directly used in the manufacturing or industrial processing process" is defined by KRS 139.010(12).
- (2) "Industrial processing" is defined by KRS 139.010(17).
- (3) "License" is defined by KRS 241.010(34).
- (4) "Machinery" means machines, in general, or collectively; also, the working parts of a machine, engine, or instrument; such as, the machinery of a watch. (Webster's New International Dictionary). This definition does not require machinery to have working parts and be able to perform a function in and of itself, as a "machine" would. The machinery of a manufacturing operation is composed of all the components making up the process, including the fixed and nonmoving parts as well as the moving parts. This is illustrated in the example of the machinery of a watch.
- (5) "Machinery for new and expanded industry" is defined by KRS 139.010(19).
- (6) "Manufacturing" is defined by KRS 139.010(20).
- (7) "Plant facility" is defined by KRS 139.010(28).
- (8) "Premises" is defined by KRS 241.010(44).
- (9) "Recycled materials" is defined by KRS 139.010(31).

Section 2. Requirements for Exemption. The machinery and the appurtenant equipment necessary to the completed installation of the machinery, together with the materials directly used in the installation of the machinery and appurtenant equipment, which are incorporated for the first time into new or existing plant facilities or licensed premises as provided in KRS 139.010(19), or which are installed in the place of existing machinery having a lesser productive capacity, and which are directly used in a manufacturing or industrial processing operation shall be exempt from the sales and use tax. In summary, the following four (4) specific requirements shall be met before machinery qualifies for exemption:

- (1) It shall be machinery.
- (2) It shall be used directly in the manufacturing or industrial processing process.
- (3) It shall be incorporated for the first time into:
 - (a) Plant facilities established in this state; or
 - (b) The premises of alcohol beverage producers in this state that include a retail establishment licensed under KRS 243.030 or KRS 243.040.
- (4) It shall not replace other machinery.

Section 3. Analysis of Requirements.

- (1) It shall be machinery.
- (2) It shall be used directly in the manufacturing or industrial processing process. Machinery shall be intimately involved in production in order to be considered used "directly" in the manufacturing or industrial processing process. The fact that machinery

is necessary for a manufacturing or industrial processing process shall not automatically qualify it for exemption. A single manufacturer may, within its primary manufacturing process, have more than one (1) production activity.

(a) Primary manufacturing process.

1. The primary manufacturing process is the production operation resulting in a finished product which will be transferred from the producing plant for distribution to customers or for further processing at another plant site. Production begins at a point where the raw material enters a process and is acted upon to change its size, shape, or composition or is transformed in some manner. Production ends when the finished goods are packaged or ready for sale. Packaging is considered complete when the product is in the container in which it is normally received by the purchaser.

2. All activities preceding the point of introduction of the raw material into the manufacturing process and following the point at which the finished product is packaged or ready for sale are not production activities and the machinery used therein shall be subject to tax.

3. Storage facilities, including those provided for the storage of in-process materials which have been removed from the production line to await further processing, are not used directly in the manufacturing process and shall be subject to tax. Proximity of storage facilities to the production line is immaterial.

(b) Contributory or secondary manufacturing process. This activity generally falls into one (1) of four (4) categories:

1. The manufacture of industrial tools to be used in the manufacturing process. Examples include the manufacture of dies, patterns, rolls, molds, cutters and cutter blades, and like property. The exemption for machinery used shall be determined by the same criteria used for determining the exemption provided in the primary manufacturing process.

2. The processing of materials which do not become an ingredient of the finished product but are consumed as industrial supplies directly in the primary manufacturing process. Examples include water cooling systems, bottle washing preparatory to filling, and chemical processes whereby the chemical is used as a catalyst directly on the product being manufactured. This machinery exemption begins at the point where the material is acted upon to condition it for use in the manufacturing process or at the point where it performs a function itself, if it is not acted upon prior to that point. The exemption ends when the material leaves the process.

3. Electrical machinery and similar equipment used directly in the operation of other machinery which is used directly in the manufacturing process.

4. Machinery used exclusively for quality control of in-process material or the efficient operation of machinery. Examples are air cooling or air conditioning systems, control panels, exhaust systems, and similar activities.

(3) It shall be incorporated for the first time into plant facilities or licensed premises established in this state. To meet this requirement, the machinery shall be installed in this state for the first time and it shall be incorporated into plant facilities or licensed premises in this state. Machinery which has been once installed into manufacturing facilities or licensed premises in this state may be subject to tax when subsequently sold by that manufacturer. Machinery purchased and delivered in Kentucky shall be subject to tax when the machinery is not acquired for installation in Kentucky.

(4) It shall not replace other machinery. New machinery purchased to replace other machinery in the plant or licensed premises shall be subject to tax unless the new machinery increases the consumption of recycled materials at the plant facility or licensed premises by not less than ten (10) percent, performs a different function,

manufactures a different product, or has a greater productive capacity, measured by units of production, than the machinery replaced.

(a) Modification of existing machinery may qualify for exemption if the modification is to perform a different function or manufacture a different product. Modification of existing machinery is not replacement machinery but maintenance of existing machinery; therefore, modifications that merely provide a greater productive capacity as measured by units of production shall not qualify for exemption.

(b) Modification of existing machinery that results in automation of non-automated functions without performance of a different function or manufacture of a different product shall not qualify for exemption.

Section 4. Pursuant to KRS 139.470(22), charges for labor or services to apply, install, repair, or maintain tangible personal property directly used in manufacturing or industrial processing process shall not be subject to sales and use tax if the charges for labor or services are separately stated. Purchasers may issue a fully completed "Certificate of Exemption Labor or Services on Manufacturing Equipment," Form 51A360, or "Streamlined Sales and Use Tax Agreement-Certificate of Exemption," Revenue Form 51A206, to claim the applicable exemption for the labor or service charges on tangible personal property directly used in the manufacturing or industrial processing process.

Section 5. In all cases where a question arises concerning the exemption of machinery for new and expanded industry, the burden of proof that each qualification has been met shall be on the one seeking the exemption.

Section 6. Forms. The forms referenced herein may be inspected, copied, or obtained, subject to applicable copyright law, at:

- (1) The Kentucky Department of Revenue, 501 High Street, Frankfort, Kentucky 40601;
 - (2) A Kentucky Taxpayer Service Center, Monday through Friday, 8:00 a.m. to 4:30 p.m.;
- or
- (3) The Department or Revenue Web site at <http://revenue.ky.gov>.

(SU-6-1; 1 Ky.R. 469; eff. 3-12-1975; TAM eff. 6-22-2016; 48 Ky.R. 501, 1514; eff. 2-1-2022.)

CONTACT PERSON: Gary Morris, Executive Director, Office of Tax Policy and Regulation, Department of Revenue, 501 High Street, Station 1, Frankfort, Kentucky 40601, phone (502) 564-0424, fax (502) 564-3875, email Gary.Morris@ky.gov.