

JURISDICTION: OKLAHOMA TAX COMMISSION
CITE: 2010-10-14-04 / NON-PRECEDENTIAL
ID: P-10-208-K
DATE: OCTOBER 14, 2010
DISPOSITION: DENIED
TAX TYPE: SALES
APPEAL: NO APPEAL TAKEN

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Protestant, COMPANY d/b/a BUSINESS is represented by MANAGER, Office Manager. The Taxpayer Assistance Division of the Oklahoma Tax Commission (hereinafter "Division") is represented by OTC ATTORNEY, Assistant General Counsel, Office of the General Counsel, Oklahoma Tax Commission.

STATEMENT OF THE CASE

On or about April 9, 2010, Protestant filed an *Oklahoma Business Registration Application for Manufacturers* ("Application") indicating it sought a manufacturers sales tax exemption permit. As the result of the answers provided on the *Application*, the Division by letter dated April 26, 2010, denied Protestant's *Application*. Protestant filed a timely written protest to the denial of the *Application* with the Office of the Administrative Law Judges ("ALJ's Office").

On May 24, 2010, the Division referred its file to the ALJ's Office for the institution of proceedings consistent with the Uniform Tax Procedure Code¹ and the Rules of Practice and Procedure before the Office of Administrative Law Judges². The protest was docketed as Case No. P-10-208-K and assigned to ALJ, Administrative Law Judge.³

A pre-hearing conference was scheduled in this cause for July 7, 2010, by *Prehearing Conference Notice* issued May 26, 2010.⁴ On May 27, 2010, Protestant requested that the pre-hearing conference be conducted by telephone which request was granted. On the date and time scheduled for the pre-hearing conference Protestant did not call. By *Prehearing Conference Order* ("Order") issued July 8, 2010, the Division was directed to file a verified response to protest no later than thirty (30) days from the date of the *Order* and Protestant was advised that a reply could be filed within thirty (30) days of the filing date of the verified response. The *Order* further directed that if an oral hearing was not requested, the record would be closed and the protest submitted for decision upon completion of the announced procedural schedule⁵. Protestant did not respond to the *Order*.

¹ 68 O.S. 2001, § 201 et seq., as amended.

² Rules 710:1-5-20 through 710:1-5-47 of the *Oklahoma Administrative Code* ("OAC").

³ OAC, 710:1-5-22(a) and (b).

⁴ OAC, 710:1-5-28(a).

⁵ OAC, 710:1-5-28(b).

The *Division's Verified Response* (“*Response*”) was filed July 15, 2010. Exhibits A through C were attached to the *Response*. Protestant did not file a reply to the *Response*. On August 20, 2009, the record was closed and the protest was submitted for decision.⁶

FINDINGS OF FACT

Upon review of the file and records, including the *Response* and exhibits attached thereto, the undersigned finds:

1. On or about April 9, 2010, Protestant filed an *Oklahoma Business Registration Application for Manufacturers* (“*Application*”) indicating it sought a manufacturers sales tax exemption permit (“MSEP”). Exhibit A.

2. Protestant manufactures “signage, custom plastic, metal & film products” through the process of “[r]ough cut and forming, both metal and plastic, into custom shapes and configurations, sanding, polishing and painting, electrical wiring and lighting layout.” Exhibit A.

3. Protestant’s North American Industry Classification System (“NAICS”) classification is “[o]ther services related to advertising” which is defined as “[t]his industry comprises establishments primarily engaged in providing advertising services (except advertising agency services, public relations agency services, media buying agency services, media representative services, display advertising services, direct mail advertising services, advertising material distribution services, and marketing consulting services).” The corresponding index entries for Protestant’s classification include “[s]ign lettering and painting services.” <http://www.census.gov/cgi-bin/sssd/naics/naicsrch>.⁷

4. Eighty percent (80%) of the product produced by Protestant is “[o]ne of a kind product for individual customer”, ten percent (10%) is “[s]tandard design available to all customers” and ten percent (10%) is “[s]ervice and repair”. Exhibit A.

5. Protestant produces product based on a customer’s order whereby the customer’s specifications is not a variation to a standard product, but the entire production process is based on the customer’s specifications. Exhibit A.

6. Protestant maintains a finished goods inventory. Exhibit A.

7. The primary machinery and equipment used in Protestant’s production process are: “[p]aint booth, air compressor, heater, welder, panel saw, table saw, grinders, sanders, band saws, large format printer, plotters, computers, shear, brake, chop saw, pop-rivet gun, laser, CNR router, drill press, hand-held plunge router, forklift, drills, paint gun, [and] polishing wheel.” Exhibit A.

8. The Division reviewed the *Application* and based on the answers denied Protestant’s MSEP application. The Division reasoned that “[c]ustom order operations are not commonly

⁶ OAC, 710:1-5-39(a).

⁷ OAC, 710:1-5-36.

regarded as a manufacturing process”, citing § 1359 of the Oklahoma Sales Tax Code and *OAC*, 710:65-19-60. Exhibit B.

9. Protestant filed a timely written protest to the denial of the MSEP. Exhibit C.

ISSUE

The issue presented for decision is whether custom order operations are commonly regarded as manufacturing operations and eligible for a MSEP.

CONCLUSIONS OF LAW

1. Jurisdiction of the parties and subject matter of this proceeding is vested in the Oklahoma Tax Commission. 68 O.S. 2001, §§ 207(c) and 212(b).

2. The collection and remittance of sales tax is governed by the Oklahoma Sales Tax Code (“Code”).⁸ An excise tax is levied upon the gross receipts or gross proceeds of all sales, not otherwise exempted by the Code. 68 O.S. 2001, § 1354(A). The sale of “tangible personal property”⁹ is expressly made subject to sales tax. 68 O.S. 2001, § 1354(A)(1).

3. “Sales of goods, wares, merchandise, tangible personal property, machinery and equipment to a manufacturer for use in a manufacturing operation” is specifically exempted from the levy of sales tax. 68 O.S. Supp. 2003, § 1359(1)¹⁰.

4. “Manufacturing” for purposes of the Code is defined in pertinent part to mean and include “the activity of converting or conditioning tangible personal property by changing the form, composition, or quality of character of some existing material or materials, including natural resources, by procedures commonly regarded by the average person as manufacturing, compounding, processing or assembling, into a material or materials with a different form or use.” 68 O.S. Supp. 2007, § 1352(14).¹¹ See *OAC*, 710:65-13-150.1(a)(4).

⁸ 68 O.S. 2001, § 1350 et seq., as amended.

⁹ Defined by the Code to mean “personal property which may be seen, weighed, measured, felt, or touched or which is in any other manner perceptible to the senses”. 68 O.S. 2001, § 1352(17). Amended and renumbered by Laws 2003, c. 413, § 1, eff. Nov. 1, 2003, to include within the meaning “electricity, water, gas, steam and prewritten computer software” and to provide that “[t]his definition shall be applicable only for purposes of the Oklahoma Sales Tax Code”. See 68 O.S. Supp. 2004, § 1352(23). See also *OAC*, 710:65-1-2. Amended at 21 Ok Reg 2581, eff 6-25-04.

¹⁰ Amended by Laws 2003, c. 472, § 15, to include the second sentence which provides:

Goods, wares, merchandise, property, machinery and equipment used in a nonmanufacturing activity or process as set forth in paragraph 9 [now 14] of Section 1352 of this title shall not be eligible for the exemption provided for in this subsection by virtue of the activity or process being performed in conjunction with or integrated into a manufacturing operation.

¹¹ Laws 2007, c. 155, § 4, which redesignated former paragraphs 1 through 27 as paragraphs 2 through 28. See Laws 2004, c. 5, § 64, which amended then paragraph 13 by inserting “including natural resources” and “by the average person” in the relevant language.

5. A “Manufacturing Operation” is defined to mean “the designing, manufacturing, compounding, processing, assembling, warehousing, or preparing of articles for sale as tangible personal property” and does not include “administration, sales, distribution, transportation, site construction, or site maintenance.” 68 O.S. 2007, § 1352(15); and *OAC*, 710:65-13-150.1(a)(5).

6. *OAC*, 710:65-19-60 provides:

Made-to-order and custom sales

Where persons contract to manufacture, compound, process or fabricate their materials into articles of tangible personal property according to the special order of their customers, the total receipts from the sales of such articles are subject to tax. The seller may not deduct any of his costs, nor can he deduct any of his charges for labor or services, which are an item of the production or fabrication costs of the article, to arrive at the amount of gross receipts subject to tax. Articles commonly made to order are curtains, draperies, tents, awnings, clothing, and slipcovers. The person making sales of made-to-order and custom made articles may purchase the materials which become a component or ingredient of their products tax exempt pursuant to a valid sales tax permit. The equipment, tools and supplies directly used or consumed in the production of such articles and not becoming a part thereof are subject to tax. (Emphasis added).¹²

7. Rules promulgated pursuant to the Administrative Procedures Act¹³, are presumed to be valid until declared otherwise by a court of competent jurisdiction. 75 O.S. 1991, § 306(C). They are valid and binding on the persons they affect, have the force of law and are prima facie evidence of the proper interpretation of the matter to which they refer. 75 O.S. 1991, § 308.2(C). Further, the legislature is deemed to adopt an administrative construction of a statute when, subsequent to such construction, it amends the statute or reenacts it without overriding such construction. *Branch Trucking Co. v. Oklahoma Tax Commission*, 1990 OK 41, 801 P.2d 686 (Okla. 1990).

8. In all administrative proceedings the burden of proof is on the taxpayer to show in what respect the action or proposed action of the Tax Commission is incorrect. *OAC*, 710:1-5-47. See *Enterprise Management Consultants, Inc. v. State ex rel. Oklahoma Tax Commission*, 1988 OK 91, 768 P.2d 359.

9. *OAC*, 710:65-19-60 specifically recognizes that the producer of made-to-order and custom made articles is a manufacturer by definition, but denies the status of a manufacturer by subjecting the “equipment, tools and supplies directly used or consumed in the production of such articles and not becoming a part thereof” to tax.

¹² Promulgated as Rule 13.016.24 of the Oklahoma Tax Commission Permanent Rules (June 30, 1990).

¹³ 75 O.S. 2001, § 250 et seq., § 301 et seq.

10. Protestant has failed to come forward with any evidence to show it is not primarily engaged in producing made-to-order and custom made articles. Accordingly, Protestant's protest to the denial of a MSEP should be denied.

DISPOSITION

Based on the above and foregoing findings of fact and conclusions of law, it is ORDERED that the protest to the denial of the application for a Manufacturers Sales Exemption Permit of Protestant, COMPANY d/b/a BUSINESS, be denied.

OKLAHOMA TAX COMMISSION

CAVEAT: This decision was NOT deemed precedential by the Commission. This means that the legal conclusions are generally applicable or are limited in time and/or effect. Non-precedential decisions are not considered binding upon the Commission. Thus, similar issues may be determined on a case-by-case basis.