

701—17.3(422,423) Processing exemptions. Carbon dioxide in a liquid, solid or gaseous form, electricity, steam, or other taxable services to be used in the processing of tangible personal property intended to be sold ultimately at retail are exempt from sales tax.

17.3(1) Services used in processing. Electricity, steam, or any other taxable service is used in processing only if the taxable service is used in any operation which subjects raw material to some special treatment which changes, by artificial or natural means, the form, context, or condition of the raw material and results in a change of the raw material into marketable tangible personal property intended to be sold ultimately at retail. The following are nonexclusive examples of what would and would not be considered electricity, steam or other taxable services used in processing:

a. The gross receipts from the sale of electricity or steam consumed as power or used in the actual processing of tangible personal property intended to be sold ultimately at retail would be exempt from tax. The gross receipts are to be distinguished from those of electricity or steam consumed for the purpose of lighting, ventilating, or heating manufacturing plants, warehouses, or offices. These latter gross receipts would be taxable.

b. The gross receipts from electricity used in the freezing of tangible personal property, ultimately to be sold at retail, to make the property marketable would be exempt from sales tax, *Fischer Artificial Ice & Cold Storage Co. v. Iowa State Tax Commission*, 81 N.W.2d 437 (Iowa 1957).

c. Electricity used merely in the refrigeration or the holding of tangible personal property for the purpose of preventing spoilage or to preserve the property in its present state would not be “used in processing” and, therefore, its gross receipts would be subject to tax, *Fischer Artificial Ice*, supra.

d. Prior to July 1, 1995, electricity or other fuel used by greenhouses and their related facilities for the purposes of growing plants is not under any circumstances fuel which is used in processing, and the gross receipts from its sales would be subject to tax. On and after July 1, 1995, electricity or other fuel used for heating or cooling of a building used in the commercial production of flowering, ornamental, or vegetable plants, is exempt from tax. See 701—subrule 18.57(2) for more information.

17.3(2) Carbon dioxide in a liquid, solid, or gaseous form, electricity, steam, and other taxable services used in processing. An expanded definition of “processing” is allowed to manufacturers of food products for human consumption using carbon dioxide in a liquid, solid, or gaseous form, electricity, steam, and other taxable services. The definition of processing applicable to persons who are not manufacturers of food products but who are using taxable services is found in subrule 17.3(1).

a. “Manufacturer” characterized. A manufacturer is a person or entity different from a merchant, dealer, or retailer. See *Commonwealth v. Thackara Mfg. Co.*, 27 A. 13 (Pa. 1893). In order for a business to be a manufacturer the principal business of that business must be manufacturing. See *Associated General Contractors v. State Tax Commission*, 123 N.W.2d 922 (Iowa 1963). Another distinction is that a merchant or retailer sells in order to earn a profit and a manufacturer sells to take profits already earned from prior activity. See *State v. Coastal Petrol Inc.*, 198 So. 610 (Ala. 1940). A person primarily engaged in selling tangible personal property in order to earn a profit and only incidentally engaged in creating products suitable for use from raw materials is not a manufacturer. A retail grocery store, incidentally and not primarily engaged in manufacturing activities such as meat cutting or production and packaging of baked goods, is not a “manufacturer of food products for human consumption” and not entitled to claim the special processing exemption allowed to those manufacturers. Retail food stores, restaurants, and other persons incidentally engaged in food manufacturing activities can, however, continue to claim on their incidental processing activities the processing exemption allowed to persons who are not manufacturers of food products for human consumption. See subrule 17.3(1).

b. For sales occurring on and after July 1, 1985, the following activities constitute processing when performed by a manufacturer to create food products for human consumption. Any carbon dioxide in a liquid, solid, or gaseous form, electricity, steam, or other taxable services primarily used in the performance of these activities is exempt from tax.

(1) Treatment of material that changes its form, context, or condition in order to produce a marketable food product for human consumption. “Special” treatment of the material to change its form, context, or condition is not necessary. Examples of “treatment” which would not be “special” are the following: washing, sorting and grading of fruits or vegetables; the washing, sorting, and grading

of eggs; and the mixing or agitation of liquids. By way of contrast, sterilization would be “special treatment.”

(2) Maintenance of quality or integrity of the food product and the maintenance or the changing of temperature levels necessary to avoid spoilage or to hold the food in marketable condition. Any carbon dioxide in liquid, solid, or gaseous form, electricity, steam, or other taxable service used in freezers, heaters, coolers, refrigerators, or evaporators used in cooling or heating which holds the food product at a temperature necessary to maintain quality or integrity or avoid spoilage of the food or to hold the food product in marketable condition is exempt from tax. It is not necessary that the taxable service be used to raise or lower the temperature of the food. Also, processing of food products for human consumption does not cease when the food product is in marketable form. Any carbon dioxide in liquid, solid, or gaseous form, electricity, steam, or other taxable service used to maintain or to change a temperature necessary to keep the product marketable is exempt from tax.

(3) Any carbon dioxide in liquid, solid, or gaseous form, electricity, steam, or other taxable service primarily used in the maintenance of environmental conditions necessary for the safe or efficient use of machinery or material used to produce the food product is exempt from tax. For example, electricity used to air-condition a room in which meat is stored is exempt from tax if the purpose of the air conditioning is to maintain the meat in a condition in which it is easy to slice rather than for the comfort of the employees who work in the room.

(4) Any carbon dioxide in liquid, solid, or gaseous form, electricity, steam, or other taxable service primarily used in sanitation and quality control activities is exempt from tax. Nonexclusive examples exempt from tax include taxable services used in pH meters, microbiology counters and incubators used to test the purity or sanitary nature of a food product. For example, electricity used in egg-candling lights would be exempt from tax. Also, electricity, steam, or any other taxable service used to power equipment which cleans and sterilizes food production equipment would be exempt from tax. Electricity used to power refrigerators used to store food samples for testing would be exempt from tax. Finally, electricity used to power “bug lights” or other insect killing equipment used in areas where food products are manufactured or stored would be exempt from tax.

(5) Any carbon dioxide in liquid, solid, or gaseous form, electricity, steam, or other taxable service used in the formation of packaging for marketable food products for human consumption is exempt from tax. For example, electricity used by a food manufacturer in plastic bottle forming machines is exempt from tax if the plastic bottles will be used to hold a marketable food product, such as milk. Any electricity, steam or other taxable service used in the heating, compounding, liquefying and forming of plastic pellets into these plastic bottles is exempt.

(6) Any carbon dioxide in liquid, solid, or gaseous form, electricity, steam, or other taxable service used in placement of the food product into shipping containers is exempt from tax. For example, electricity used by a food manufacturer to place food products into packing cases, pallets, crates, shipping cases, or other similar receptacles is exempt.

(7) Any carbon dioxide in liquid, solid, or gaseous form, electricity, steam, or other taxable service used to move material which will become a marketable food product or used to move the marketable food product itself until shipment from the building of manufacture is exempt from tax. This includes, but is not limited to, taxable services used in pumps, conveyors, forklifts, and freight elevators moving the material or food product and taxable services used in door openers which open doors for forklifts or other devices moving the material or product. Any loading dock which is attached to a building of manufacture is a part of that building. Any electricity, steam, or other taxable service used to move any food products to a loading dock is exempt from tax. If a food product is carried outside its building of manufacture by any conveyor belt system, electricity used by any portion of the system located outside the building is taxable.

17.3(3) *Measurement of taxable and nontaxable use of electricity and steam.* The exemption provided in the case of electricity or steam applies only upon the gross receipts from the sale of electricity or steam when the energy is consumed as power or is used in the processing of food products or other tangible personal property intended to be sold ultimately at retail, as distinguished from electricity or steam which is consumed for taxable purposes. When practical, electricity or steam consumed as

power or used directly in processing must be separately metered and separately billed by the supplier thereof to clearly distinguish energy so consumed from electricity or steam which is consumed for purposes or under conditions where the exemption would not apply. If it is impractical to separately meter electricity or steam which is exempt from that electricity or steam upon which tax will apply, the purchaser must furnish an exemption certificate to the supplier with respect to what percentage of electricity or steam in the case of each purchaser is subject to the exemption. See 701—subrule 15.3(2). The exemption certificate must be supported by a study showing how the percentage was developed. When a certificate and study are accepted by the supplier as a basis for determining exemption, any changes in the processing method, changes in equipment or alterations in plant size or capacity affecting the percentage of exemption will necessitate the filing of a new and revised statement by the purchaser. When the electric or steam energy is separately metered, enabling the supplier to accurately apply the exemption in the case of processing energy, the purchaser need only file an exemption certificate since the supplier, under such conditions, will separately record and compute the consumption of energy which is exempt from tax apart from that energy which is subject to tax.

This rule is intended to implement Iowa Code sections 422.42(3) and 423.1.