

Georgia Letter Ruling: LR SUT-2017-07

Dated: February 24, 2017

Topic: Manufacturing Exemptions, Energy

This letter is in response to your request for guidance on the application of Georgia sales and use tax to energy necessary and integral to manufacturing.

Facts Presented by Taxpayer

[Redacted] (“Taxpayer”) purchases and uses biomass fuel, tire derived fuel, electricity, natural gas, and coal to produce steam. The steam is produced for two purposes: to be sold to one entity and for using the remaining steam to generate electricity.

Taxpayer sells a contractually limited amount of electricity which does not include a base amount. Despite the flexibility provided in the contract, it is financially advantageous for Taxpayer to deliver almost all of its declared capacity.

Taxpayer’s steam turbine generator has limited condensing capacity. This design configuration depends on large amounts of steam being extracted: Taxpayer cannot generate the current declared capacity without steam extracted. Thus, it is necessary to maintain steam sales to achieve power production at or near capacity, and Taxpayer would not be financially viable without steam sales. In practice, Taxpayer normally provides the maximum steam possible and, consequently, maintains its current power sales rate near production capacity.

In addition to the process description above, Taxpayer states the following:

- The value of the capital assets and investments used to produce steam far exceed those used to produce electricity for resale.
- Approximately [redacted amount (more than 50%)] of the energy derived from the combustion of solid fuels within the boiler is used to produce (sold) steam. The remainder of this energy goes to condensing steam or other processes in power production.
- On average, [redacted amount (less than 50%)] of Taxpayer’s gross revenue results from the sale of steam and [redacted amount (more than 50%)] Taxpayer’s gross revenue results from the sale of electricity. By contract, power revenue fees are set for [redacted] years with a [redacted] annual adjustment. The steam fees are adjusted annually based on a neutral index, with a cap of [redacted] per year.
- It takes approximately [redacted] hours to produce electricity with the same heat value as the amount of steam produced in one hour. It takes approximately [redacted] minutes to produce electricity with the same resale value as the amount of steam produced in one hour.
- Taxpayer considers its facility to be classified under the 2012 North American Industrial Classification System (NAICS) code 221117 (Biomass electric power generation). This industry comprises establishments primarily engaged in operating biomass electric power generation facilities. These facilities use biomass to produce electric energy. The electric energy produced in these establishments is provided to electric power transmission systems or to electric power distribution systems.¹

Much of the biomass fuel purchased by Taxpayer meets the definition of “biomass material” under the sales and use tax exemption contained in O.C.G.A. § 48-8-3(83)(A). However, in addition to biomass material, Taxpayer also purchases other fuels to burn to produce steam. Since Taxpayer classifies these products as materials necessary and integral for heat, Taxpayer seeks clarification on whether Taxpayer is eligible for a partial energy exemption.

Issue

Is Taxpayer “primarily engaged in producing electricity for resale” as used in the definition of the term “energy” in O.C.G.A. § 48-8-3.2(a)(3)?

¹ “North American Industry Classification System: 221117 Biomass Electric Power Generation.” *United States Census Bureau*. <http://www.census.gov/cgi-bin/sssd/naics/naicsrch?code=221117&search=2012> (August 23, 2016). This code is comprised of part of the facilities in 2007 NAICS code 221119 (Other electric power generation), and it is a subset of 22111 (Electric Power Generation).

Analysis

Georgia levies and imposes a tax (subject to certain specific exemptions) on the retail purchase, retail sale, storage, use, or consumption of tangible personal property, certain enumerated services, and utilities.²

The sale and use of energy are exempt from sales and use tax (except certain sales and use taxes for educational purposes) if the energy is necessary and integral to the manufacture of tangible personal property and sold, used, stored, or consumed at a manufacturing plant in Georgia.³ “Energy” means natural or artificial gas, oil, gasoline, electricity, solid fuel, wood, waste, ice, steam, water, and other materials necessary and integral for heat, light, power, refrigeration, climate control, processing, or any other use in any phase of the manufacture of tangible personal property. However, the term “energy,” as used in the exemption at issue, excludes energy purchased by a manufacturer that is primarily engaged in producing electricity for resale.⁴

Here, Taxpayer is purchasing materials to burn for heat, which is necessary to produce steam and electricity. Therefore, it seems that the purchased materials would be considered energy unless Taxpayer, the manufacturer, is primarily engaged in producing electricity for resale.

Exemptions from taxation are strictly construed, and an exemption will not be granted unless the relevant statute clearly and distinctly shows that such was the plain and unambiguous intention of the General Assembly.⁵ The phrase “primarily engaged in producing electricity for resale” is not defined, so the Department assumes that the words are used in their ordinary senses. “Primarily” means “for the most part” or “in the first place.”⁶ “Engaged” means “involved in activity,” “being used,” or “busy with some activity.”⁷

The Department considers Taxpayer’s whole operation to understand what Taxpayer is primarily engaged in producing.⁸ Taxpayer must produce steam before producing electricity. Given Taxpayer’s limited condensing capacity, Taxpayer could not efficiently produce electricity without selling steam. Taxpayer must repurpose steam and sell electricity.⁹

Although there is no minimum production requirement for steam or electricity, Taxpayer entered into a long-term power purchase agreement with a power company. Because of the production design, Taxpayer would not be financially viable without producing electricity for resale. In fact, with [redacted amount (more than 50%)] of Taxpayer’s gross revenue resulting from the sale of electricity, Taxpayer earns more revenue from electricity production than from steam production.

Moreover, Taxpayer classifies itself as primarily engaged in operating a biomass electric power generation facility. Taxpayer considers its facility to be classified under the 2012 NAICS code 221117, the code for facilities that primarily use biomass to produce electric energy. It is under the general industry code of electric power generation. While there is a different code for steam production establishments, Taxpayer did not identify itself under that category.¹⁰

² O.C.G.A. §§ 48-8-1, 48-8-2(31)(A), and 48-8-30(a).

³ O.C.G.A. § 48-8-3.2; Ga. Comp. R. & Regs. r. 560-12-2-.64.

⁴ O.C.G.A. § 48-8-3.2; Ga. Comp. R. & Regs. r. 560-12-2-.64.

⁵ Ga. Comp. R. & Regs. r. 560-12-1-.18.

⁶ “Primarily,” *Merriam-Webster.com*. <http://www.merriam-webster.com/dictionary/primarily> (August 23, 2016).

⁷ “Engaged,” *Merriam-Webster.com*. <http://www.merriam-webster.com/dictionary/engaged> (August 23, 2016).

⁸ Because Taxpayer’s steam and electricity production is a united operation, a more traditional review of production time is not indicative of the primary activity of Taxpayer.

⁹ Taxpayer urged consideration of capital and heat inputs, but inputs are not determinative of what the Taxpayer is primarily engaged in producing. Such measures are misleading since inputs for steam are required for electricity.

¹⁰ See “North American Industry Classification System: 221330 Steam and Air-Conditioning Supply.” *United States Census Bureau*. [http://www.census.gov/cgi-bin/sssd/naics/naicsrch?code=221330&search=2012 NAICS Search](http://www.census.gov/cgi-bin/sssd/naics/naicsrch?code=221330&search=2012%20NAICS%20Search) (January 13, 2017).

In light of Taxpayer's relationship with its steam purchaser, business model, self-classification, and production methods, the facts presented in this case indicate that Taxpayer is primarily engaged in producing electricity for resale.

Ruling

In view of the totality of Taxpayer's description of its current operations, Taxpayer is "primarily engaged in producing electricity for resale" as used in the definition of the term "energy" in O.C.G.A. § 48-8-3.2(a)(3).

The opinions expressed in this ruling are based upon the information contained in your request and limited to the specific transactions, facts, circumstances, and taxpayer in question. Should the circumstances regarding the transactions change or differ materially from those represented, this ruling may become invalid. Subsequent statutory or administrative rule changes or judicial interpretations of the statutes or rules upon which this ruling is based may subject similar future transactions to different tax treatment than that expressed in this ruling.