

STATE OF COLORADO



DEPARTMENT OF REVENUE
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PLR-12-005

John W. Hickenlooper
Governor

October 16, 2012

Barbara J. Brohl
Executive Director

XXXXXXXXXXXXXXXXXX
ATTN: XXXXXXXXXXXX
XXXXXXXXXXXXXXXXXX
XXXXXXXXXXXXXXXXXX
XXXXXXXXXXXXXXXXXX

Re: Private Letter Ruling

Dear XXXXXXXXXXXX,

You submitted on behalf of XXXXXXXXXXXX ("Company") a request for a private letter ruling to the Colorado Department of Revenue ("Department") pursuant to Regulation 24-35-103.5. This letter is the Department's private letter ruling.

Issues

1. Is the sale of welding gases that produces energy for welding and that are directly used in the manufacturing process exempt pursuant to §39-26-102(21)(a), C.R.S. from Colorado sales tax?
2. Is the sale of inert and semi-inert welding gases that do not produce energy but are necessary to the welding process exempt from Colorado sales taxes when the suspension of the exemption §39-26-102(21)(a) and (b)(I), C.R.S. expires on July 1, 2012?
3. Is the sale of welders and related machinery sold to a manufacturer in Colorado whose welding is a direct part of its manufacturing process exempt from sales tax pursuant to §39-26-709(1)(a), C.R.S. if the sale price is greater than \$500 or the items are included in an invoice or purchase order of machinery or machine tools totaling more than \$500?
4. Is the sale of welding attachments, parts, or machine tools exempt from Colorado sales tax pursuant to §39-26-709(1)(a), C.R.S. if these items have a sales price greater than \$500 or the item is included in an invoice or purchase order of machinery or machine tools totaling more than \$500?

Conclusion

1. The sale of acetylene used in manufacturing is exempt¹ from state sales tax (some local sales tax may apply), but the sale and use of oxygen used in conjunction with the acetylene is not exempt from state or state-administered local taxes.
2. The sale of inert and semi-inert gases do not qualify for the exemption of fuel used in the manufacturing process pursuant to §39-26-102(21)(a), C.R.S. because they are not a fuel.
3. Hand-held torches and similar tools sold to a manufacturer in Colorado whose welding is a direct part of its manufacturing process are not exempted from sales tax under the manufacturing machinery exemption of §39-26-709(1)(a), C.R.S.
4. Welding attachments, parts, and tools are not exempt from Colorado sales and use tax pursuant to §39-26-709(1)(a), C.R.S.

Background

Welding Gases

Company sets forth the following background. Company sells industrial, medical, and specialty gases and various goods, including welding machinery and associated tools, parts, and attachments to manufacturers in Colorado. The welding gases include, but are not limited to, argon, acetylene, oxygen, and carbon dioxide.

Welding gases are used to weld metals and to cut metals. Gas welding involves the use of a hand held gas-fed flame torch to heat the metal and the filler material to create a weld. The gases generally used are a mixture of fuel gases and shielding gases to create a clean, hot flame. Fuel gases, such as acetylene and oxygen (used for cutting metal) provide the energy. Shielding gases, such as argon, helium, and carbon dioxide are inert or semi-inert gases. The purpose of these inert gases is to protect the weld area from atmospheric gases, such as oxygen, nitrogen, and water vapor.

To perform a weld, a hand held welding gun utilizes heat supplied by the combustible gas (acetylene) along with welding wire and the gases carbon dioxide and argon. The wire is fed through a tube in the gun. The gases flow from storage tanks through a hollow tube that surrounds the wire. Acetylene is lit producing a flame and heat. The flame is applied to the area sought to be welded. The carbon dioxide and argon act as a shielding agent to keep oxygen and the outside atmosphere away from the weld. The weld is made by the wire melting onto the metal pieces sought to be joined.

A metal cutting process uses an oxyfuel cutting torch. In this process, two hoses run to the torch: one hose supplies acetylene and the other supplies oxygen. The torch is lit and the acetylene heats the area to be cut. Once heated, the oxygen is applied and

¹ The exemptions for industrial fuels and manufacturing machinery that we discuss in this ruling apply to both state taxes and state-administered local sales taxes.

the cut is made by a chemical reaction. The acetylene is the power source, which produces the heat to create the cut. In the metal cutting process, the manufacturer cannot cut steel without the high temperature from the acetylene and the oxygen.

Company posits that because acetylene and oxygen produce energy and are used in a welding or cutting process that is directly part of manufacturing, these gases qualify for the fuel exemption used in manufacturing. Additionally, Company states that while the inert and semi-inert gases do not provide energy/burn, these gases are instrumental in creating the surface necessary to perform a clean, quality weld and, as such, fall under the definition of "gas" in the fuel exemption.

Welding Machinery Attachments, Machine tools and Machine Parts

In addition to welding gases and welders, Company sells welding tools, attachments, and parts. The following is a list of items sold by Company:

1. Spool Guns: Spool guns are used for smooth feeding of aluminum during the welding process when the material being welded is aluminum. Spool guns are used in metal inert gas welding and are attached to the hoses running from the shielding gases, wire feeder and power source. Spool guns provide smoother bead appearance and minimize post weld grinding. Without the spool guns, the aluminum would easily bind up and create poor quality welds.
2. Torches: Company sells water cooled TIG (tungsten and inert gas) torches (requires a water cooler), water coolers and air cooled torches. To prevent the power cable, torch or gun from overheating from high temperature welds, cooling torches are required.
3. Regulators and Flowmeters: Regulators control the pressure of the gas from the cylinder to the torch. Flowmeters control the amount of gas from the cylinder to the torch. The pressure and amount of gas used during the welding process requires adjustment based on the type of welding to be completed. Regulators and flowmeters also maintain a steady flame during the welding process, which is required to obtain quality welds.
4. Flash Back Arrestors: Flash back arrestors prevent the ignition of the mixed gases and prevent damage to the welding machinery. They are also required by Occupational Safety and Health Administration regulations.

Company states that these items have a direct impact on the welding process and are all constituent parts of the welding process used directly and predominantly in the manufacturing process. Company also states that the welding attachments, tools, and parts they sell should qualify for the manufacturing equipment exemption (§39-26-709(1)(a), C.R.S.) if sold to a manufacturer where welding is a direct and critical part of the manufacturing process. Although some of the welding items are priced in excess of \$500, others are less than \$500 but may be included on invoices or purchase orders of machinery and machine tools totaling more than \$500.

Discussion

Welding Gases

Colorado imposes sales and use tax on the sale, use, storage, and consumption of tangible personal property.² There are exemptions that apply to certain gases, although not all gases are exempt.

Sales and purchases of electricity, coal, gas, fuel oil, steam, coke or nuclear fuel, for use in processing, manufacturing, mining, refining, irrigation, construction, telegraph, telephone and radio communication, street and railroad transportation services, and all industrial uses, ... shall be deemed to be wholesale sales and shall be exempt from taxation under this part 1 [sales taxes].

§39-26-102(21)(a), C.R.S. "Gas" is not defined by statute. However, the other items listed do provide a context in which this term can and should be understood. All the items listed in this section are sources of energy. This context indicates that the legislature intended to exempt items that are at least fuel sources. This interpretation is consistent with a similar exemption for fuels for residential use, which defines "gas" either as natural, manufactured, and liquefied petroleum gas. See, §39-26-715(1)(a)(II), C.R.S.

Acetylene used for welding qualifies as a "gas" under this exemption because it is a source of energy. On the other hand, oxygen itself is not an energy source but rather a catalyst for combustion. As such, it is not exempt under this statute. Similarly, inert gases that are used to create a proper environment for the welding process are not energy sources themselves and, therefore, do not qualify under this exemption.

We note that these combustible welding gases must be used in at least one of the enumerated industries, such as manufacturing, construction, mining, and other industrial uses, which include the agricultural industry.³ Therefore, the sale of fuel used for welding within the agricultural industry and used to repair machinery and equipment used in the agricultural industry is exempt. However, welding gases used in a non-commercial setting, such as acetylene gas sold by a hobby store, do not qualify.

Exemption for machinery used in manufacturing

Purchases of machinery or machine tools and parts in excess of five hundred dollars are exempt from Colorado sales and use tax when the machinery is used directly and

² §39-26-104 and 202, C.R.S. (sales and use tax apply to the sale, use, storage, or consumption of tangible personal property). You can view this and other statutes, regulations, and Department publications by visiting our web site at www.colorado.org/revenue/tax > Tax Library.

³ Effective March 10, 2010, the legislature suspended this exemption for fuel used for industrial purposes until July 1, 2012. See, 39-26-102(21)(b), C.R.S.

predominantly in manufacturing tangible personal property in Colorado. §39-26-709(1)(a)(II) C.R.S. For purposes of this statute, "machinery" means:

"any apparatus consisting of interrelated parts used to produce an article of tangible personal property. The term includes both the basic unit and any adjunct or attachment necessary for the basic unit to accomplish its intended function."

§39-26-709(1)(c)(II), C.R.S.

As an initial matter, we note that exemptions from tax are narrowly construed. *Security Life & Accident Co. v. Heckers*, 177 Colo. 455, 495 P.2d 225, 226 (1972). Unless the exemption clearly applies, the exemption must be denied. Machinery connotes an apparatus of some complexity. For example, we would not classify a lug wrench or hand saw as "machinery" even though, in some sense, it is an "apparatus" consisting of various parts. At the other extreme, we would classify a hydraulic press as machinery because it possesses a significant degree of complexity. We believe a hand-held acetylene torch is more akin to a hand-held tool than it is to "machinery."

We have used this hand tool distinction in related contexts. For example, Colorado exempts "machinery" used in "cleanrooms" where a pollutant-free environment is critical to the manufacturing process. There, we exclude from the definition of "machinery" hand held tools.

The [cleanroom] exemption applies only to "machinery." Therefore, tangible personal property that is not "machinery" is not exempt. Non-machinery items include, but are not limited to, chemicals or catalysts; gases and liquids; energy; safety or work apparel; standard janitorial supplies; *hand tools*; office equipment; furniture and supplies; replacement and repair parts that do not constitute machinery; and the building in which the cleanroom is housed.

FYI Publication Sales 73, "Cleanroom Equipment Exemption."⁴

Other states have similarly concluded that simple mechanical devices, such as hand tools, do not constitute "machinery." See, e.g., Ark. Regs. GR-55 Exemptions From Tax — Manufacturers; Illinois Dept. of Rev. General Information Letter No. ST 96-0493-GIL, 12/12/1996. Other states have reached a contrary conclusion. See, In the Matter of the Petition of Reynolds Metals Co., N.Y. Division of Tax Appeals, DTA No. 814694, 7-31-97 (hand torches qualify as machinery used in production of aluminum.)

In some cases, welding devices are complex. For example, longitudinal and circumferential welding machines used for manufacturing of storage tanks would likely qualify as "machinery" because of the complexity of the welding device. However, in contrast, the welding torches at issue here are the typical hand-held torch, tank, and

⁴ This Publication is available on the Department's web site at www.colorado.gov/revenue/tax > Tax Library > FYI Publications > Sales > Sales 73.

regulator. These do not possess the degree of complexity that we normally associate with "machinery" and, therefore, they are not exempt as "machinery."

Hand-held torches also do not qualify as "machine tools." Although not defined by statute, the Department interprets this machine tool exemption to apply to those tools primarily used in conjunction with machinery. For example, jigs, molds, and patterns which are used in conjunction with machinery (e.g., molds used in a machine press) are exempt as machine tools. See, FYI Sales 53 - Special Regulation: Tools, Jigs, Dies, Patterns, and Molds ("Molds or similar machine tools are exempt when held and used [in manufacturing]"). On the other hand, hammers, wrenches and other tools are not primarily used in connection with machinery and, therefore, do not qualify for the machine tool exemption. Hand-held torches are not primarily used in connection with exempt machinery and, therefore, do not qualify as machine tools.

Miscellaneous

This ruling applies only to sales and use taxes administered by the Department. Please note that the Department administers state and state-collected city and county sales taxes and special district sales and use taxes, but does not administer sales and use taxes for self-collected home rule cities and counties. You may wish to consult with local governments which administer their own sales or use taxes about the applicability of those taxes. Visit our web site at www.colorado.gov/revenue/tax for more information about state and local sales taxes.

This ruling is premised on the assumption that Company has completely and accurately disclosed all material facts. The Department reserves the right, among others, to independently evaluate Company's representations. This ruling is null and void if any such representation is incorrect and has a material bearing on the conclusions reached in this ruling. This ruling is subject to modification or revocation in accordance to Department Regulation 24-35-103.5.

Enclosed is a redacted version of this ruling. Pursuant to statute and regulation, this redacted version of the ruling will be made public within 60 days of the date of this letter. Please let me know in writing within that 60 day period whether you have any suggestions or concerns about this redacted version of the ruling.

Sincerely,

Neil L. Tillquist
Colorado Department of Revenue
Tele: (303)866-5627
Email: neil.tillquist@state.co.us
(Please note that my email has changed)