

UT 10-01

Tax Type: Use Tax

Issue: Machinery & Manufacturing Equipment Exemption (Agricultural)

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

THE DEPARTMENT OF REVENUE)	Docket No.	00-ST-0000
OF THE STATE OF ILLINOIS)	IBT No.	0000-0000
v.)	NTL No.	00 00000000000000
ABC FARMS,)	John E. White,	
Taxpayer)	Administrative Law Judge	

RECOMMENDATION FOR DISPOSITION

Appearances: David Shockey, Shockey & Cox, appeared for ABC Farms, Mehpara Suleman, Special Assistant Attorney General, appeared for the Illinois Department of Revenue.

Synopsis:

This matter arose when ABC Farms (Taxpayer) protested a Notice of Tax Liability (NTL) the Illinois Department of Revenue (Department) issued to it to assess use tax regarding its purchase of a bulldozer for use in Illinois. The issue is whether Taxpayer's use of the bulldozer was exempt from tax pursuant to § 3-5(11) of the Illinois Use Tax Act (UTA), which exempts farm machinery and equipment primarily used in production agriculture. 35 ILCS 105/3-5(11).

The hearing was held at the Department's offices in Chicago. Taxpayer presented evidence through two witnesses. I have reviewed that evidence, and I am including in this recommendation findings of fact and conclusions of law. I recommend that the issue be resolved in favor of the Department.

Findings of Fact:

1. Taxpayer is owned by John Doe (ABC). Hearing Transcript (Tr.) p. 29 (ABC).¹
2. On July 20, 2005, Taxpayer purchased a 1998 John Deere 450G LPG dozer from XXX, Inc., a retailer doing business in Illinois. Department Ex. 2, p. 1 (copy of invoice for dozer). On the invoice the retailer prepared to document that sale, the purchaser is identified as Taxpayer. *Id.*
3. When Taxpayer purchased the dozer, its agent signed a Department form titled, Equipment Exemption Certificate, which identified the retailer and the purchaser, and which contained the Taxpayer's sworn statement that the equipment purchased would be used primarily in production agriculture. Department Ex. 2, p. 2 (copy of exemption certificate); *see also* 35 ILCS 120/7. On that form, the purchaser is identified as "John Doe (ABC Farms)." Department Ex. 2, p. 2.
4. Taxpayer's exemption certificate was forwarded to a Department auditor, Annette Simmons (Simmons), who was assigned to review the correctness of Taxpayer's claim of exemption. Tr. pp. 12-14 (Simmons). Simmons conducted the audit of Taxpayer's purchase and use of the dozer via correspondence, which she referred to as a desk or office audit. *Id.* p. 12.
5. Simmons has been employed by the Department as an auditor for about 21 years, and has conducted about 50 audits relating to the farm machinery and equipment

¹ The record is unclear whether Taxpayer, ABC Farms, is a sole proprietorship owned by ABC, or whether ABC Farms has some corporate existence that is separate from ABC. Thus, even though I refer to Taxpayer and ABC separately in this recommendation, they may well be the same person. 35 ILCS 105/1 ("person" defined).

exemption. Tr. pp. 10-11 (Simmons).

6. Simmons sent Taxpayer a letter, dated August 7, 2008, notifying it that the Department had initiated an audit of its purchase of the dozer. Department Ex. 3 (copy of August 7, 2008 letter).
7. Attached to that letter was a form questionnaire requesting the following items of information from Taxpayer:
 1. Please briefly describe your farming operations.
 2. Please give a complete description of the equipment's use.
 3. List by activity, the percentage of use that applies to that activity.
 4. List accessories and/or additional equipment used in conjunction with this equipment.
 5. List your FEIN#/SSN#
List your Illinois Sales Tax# (if applicable)

Department Ex. 3.

8. Taxpayer responded to Simmon's letter, and provided answers to the questionnaire. Department Ex. 1C (copy of Taxpayer's responses to questionnaire).
9. In response to question number 2, Taxpayer responded, "We use the dozer for making water ways, building terraces and cleaning out fence rows." Department Ex. 1C.
10. After reviewing Taxpayer's responses to the questionnaire and the provisions of the Department's retailers' occupation tax regulation § 130.305, Simmons determined that Taxpayer's use of the dozer was not exempt. Tr. p. 17 (Simmons).
11. Simmons notified Taxpayer of that determination in a letter dated August 14, 2008, which provided, in pertinent part:

Dear Taxpayer:

In your response to our letter dated August 7, 2008 you stated that the John Deere Dozer was used for making water ways, building terraces and cleaning out fence rows.

86 Illinois Administrative Code, Section 130.305(f) states the following:

“activities such as the clearing of land, mowing of fence rows, creation of ponds or drainage facilities are not included”. Based on this information the activities for which you use your John Deere Dozer do not qualify as tax exempt under the provisions of the farm machinery and equipment exemption.

Department Ex. 4 (copy of Department’s August 14, 2008 letter).

12. Simmons also reviewed the Wikipedia web site to obtain a definition of a bulldozer, which described a bulldozer as being a piece of equipment that is used to push large quantities of soil during construction work. Tr. pp. 22-23 (Simmons).
13. After taking into account the definition of a bulldozer, Simmons understood that Taxpayer’s dozer was being used to move soil around in preparation for construction. Tr. pp. 23-24 (Simmons).
14. Thereafter, the Department issued the NTL to Taxpayer, assessing tax in the amount of \$1,969, a late filing penalty of \$39, and a late payment penalty of \$394. Department Ex. 1, p. 1.

Conclusions of Law:

The UTA imposes a tax “upon the privilege of using in this State tangible personal property purchased at retail from a retailer ...” 35 ILCS 105/3. The Illinois General Assembly incorporated into the UTA certain provisions of the complementary Retailers’ Occupation Tax Act (ROTA). 35 ILCS 105/11. Among them is § 4 of the ROTA, which provides that the Department’s determination of tax due constitutes prima facie proof that tax is due in the amount determined by the Department. 35 ILCS 105/12; 35 ILCS 120/4. In this case, the Department established its prima facie case when it introduced Department Exhibit 1, consisting of a copy of the NTL and of the auditor’s determination of tax due, under the certificate of the Director. Department Ex. 1. That

exhibit, without more, constitutes prima facie proof that Taxpayer owes Illinois use tax in the amount determined by the Department. 35 ILCS 105/12; 35 ILCS 120/4.

The Department's prima facie case is overcome, and the burden shifts to the Department to prove its case, only after a taxpayer presents evidence that is consistent, probable and identified with its books and records, to show that the Department's determinations were not correct. Copilevitz v. Department of Revenue, 41 Ill. 2d 154, 157-58, 242 N.E.2d 205, 207 (1968). Additionally, when a taxpayer claims that a transaction is exempt from a particular tax, the burden of proof is on the taxpayer. 35 ILCS 105/12; 35 ILCS 120/7; Balla v. Department of Revenue, 96 Ill. App. 3d 293, 296, 421 N.E.2d 236, 238 (1st Dist. 1981) (citing Telco Leasing, Inc. v. Allphin, 63 Ill. 2d 305, 347 N.E.2d 729 (1976); Bodine Electric Co. v. Allphin, 81 Ill. 2d 502, 410 N.E.2d 828 (1980)).

Section 3-5 of the UTA provides exemptions from use tax based on the nature of the property's use, or based on the nature of the user. 35 ILCS 105/3-5. The exemption claimed by Taxpayer here is described in § 3-5(11), which provides:

Sec. 3-5. Exemptions. Use of the following tangible personal property is exempt from the tax imposed by this Act:

(11) Farm machinery and equipment, both new and used, including that manufactured on special order, certified by the purchaser to be used primarily for production agriculture or State or federal agricultural programs, including individual replacement parts for the machinery and equipment, including machinery and equipment purchased for lease, and including implements of husbandry defined in Section 1-130 of the Illinois Vehicle Code, farm machinery and agricultural chemical and fertilizer spreaders, and nurse wagons required to be registered under Section 3-809 of the Illinois Vehicle Code, but excluding other motor vehicles required to be registered under the Illinois Vehicle Code. Horticultural polyhouses or hoop houses used for propagating, growing, or overwintering plants shall be considered farm machinery and equipment under this item (11). Agricultural chemical tender tanks and dry boxes shall include units sold

separately from a motor vehicle required to be licensed and units sold mounted on a motor vehicle required to be licensed if the selling price of the tender is separately stated.

Farm machinery and equipment shall include precision farming equipment that is installed or purchased to be installed on farm machinery and equipment including, but not limited to, tractors, harvesters, sprayers, planters, seeders, or spreaders. Precision farming equipment includes, but is not limited to, soil testing sensors, computers, monitors, software, global positioning and mapping systems, and other such equipment.

Farm machinery and equipment also includes computers, sensors, software, and related equipment used primarily in the computer-assisted operation of production agriculture facilities, equipment, and activities such as, but not limited to, the collection, monitoring, and correlation of animal and crop data for the purpose of formulating animal diets and agricultural chemicals. This item (11) is exempt from the provisions of Section 3-90.

35 ILCS 105/3-5(11). This exemption is substantively identical to the exemption set forth in § 2-5 of the Retailers' Occupation Tax Act (ROTA). 35 ILCS 120/2-5.

Section 3-35 of the UTA defines the term "production agriculture," as follows:

Production agriculture. For purposes of this Act, "production agriculture" means the raising of or the propagation of livestock; crops for sale for human consumption; crops for livestock consumption; and production seed stock grown for the propagation of feed grains and the husbandry of animals or for the purpose of providing a food product, including the husbandry of blood stock as a main source of providing a food product. "Production agriculture" also means animal husbandry, floriculture, aquaculture, horticulture, and viticulture.

35 ILCS 105/3-35.

The Illinois General Assembly authorized the Department to make, promulgate and enforce reasonable rules and regulations relating to the administration and enforcement of the provisions of the UTA and ROTA. 35 ILCS 105/12; 35 ILCS 120/12. Pursuant to that authority, the Department has adopted a regulation in which it announced how it will administer the farm machinery and equipment exemption. 86 Ill. Admin. Code § 130.305. That regulation is codified at § 130.305 of the Department's retailers'

occupation tax regulations, and was in effect when Taxpayer purchased the dozer at issue here. 86 Ill. Admin. Code § 130.305. That particular regulation provides, in pertinent part:

Production Agriculture, with respect to crops, is limited to activities necessary in tilling the soil, planting, irrigating, cultivating, applying herbicide, insecticide or fertilizer, harvesting and drying of crops. Specialized food production operations which produce plants under controlled environments in growing media other than soil, qualify as production agriculture. **Activities such as the clearing of land, mowing of fence rows, creation of ponds or drainage facilities are not included,** nor are the operations involved in the storing or transporting of crops and produce. The processing of crops into food or other products is not production agriculture. With respect to the raising of or propagation of livestock and husbandry of animals, the animals must be domestic farm animals raised for profit. The raising of wild animals, game birds and house pets would not be considered to be production agriculture.

86 Ill. Admin. Code § 130.305(f) (emphasis added).

After the Department rested, ABC testified that the dozer was too small to be used in construction. Tr. pp. 29-30. He said it was used to push snow away from driveways in the winter time, and repeated that it was used to make terraces and waterways, and to take out fence lines. Tr. pp. 30, 33. He said that since he farms about 5,000 acres, there are always ditches to close up. Tr. p. 30. He also explained that some of the waterways he maintains with the dozer are on land that he farms and which he rents from others. Tr. p. 31. He said that he maintained such waterways to keep the landlady happy. *Id.* He said he also uses the dozer to close up washouts in the fields. Tr. p. 32. He said that he closed them himself because it was cheaper than hiring someone else, and that a lighter dozer, like the one he had, does not damage the fields. *See id.* He concluded by saying that 100% percent of his use of the dozer was for the production of agriculture. *Id.*

On cross-examination, ABC contested the Department regulation's exclusion of making terraces and waterways as being within the definition of production agriculture. Tr. p. 34. When asked how many weeks the dozer was used to clear fences, he answered that there were times when it sat for a couple of months at a time, and other times when it may be used every day for a month straight. Tr. pp. 34-35. He said that it was used to terrace, to stop erosion, and for waterways for a short time in the spring and for a short time in the fall. Tr. pp. 34-35. He acknowledged that the dozer was not used for harvesting crops or spraying chemicals. Tr. p. 35. He also acknowledged that the photos of the dozer do not reflect how it was used. *Id.*

On redirect, ABC said that if he did not have the dozer, he would use a tractor with a loader on it to perform the same tasks. Tr. p. 36. ABC explained that the dozer does a nicer, neater job on the tasks he uses it for than a tractor would, because the dozer is more level. *Id.*

After ABC testified, Taxpayer offered the testimony of Mr. Smith (Smith). Smith owns XYZ Equipment, Inc., a retailer of farm and other equipment, and is also a member of the Illinois General Assembly. Tr. pp. 37, 43-46. He testified regarding the nature and characteristics of the John Deere dozer that Taxpayer purchased, and said that such a dozer could be used for light construction purposes or for production agriculture purposes. Tr. pp. 49-50. He acknowledged that he had no personal knowledge of how Taxpayer used the dozer. Tr. pp. 50-51. Smith said that he has sold equipment similar to the dozer at issue here, and has never been subject to question or audit when a purchaser claimed the farm machinery and equipment exemption. Tr. p. 51.

Prior to resting, Taxpayer adopted Department Exhibit 6, ABC's photos of the dozer, as Taxpayer Exhibit 1. Tr. p. 49.

During closing arguments, counsel for Taxpayer first argued that, while dozers may be and are used in construction, they can also be used for production agriculture purposes, as Taxpayer used the one at issue here. Tr. pp. 53-54. Counsel also argued that the Department's reading of the definition of production agriculture to include only equipment used in planting or harvesting was an overly narrow construction of the farm machinery exemption statute. Tr. p. 54. Counsel asserted that cleaning fence rows and maintaining waterways with a piece of equipment that is not defined as a tractor or combine is part of modern production agriculture. *Id.* Finally, counsel argued that the spirit of the exemption statute was to include equipment like the dozer Taxpayer used. Tr. pp. 54-55.

In response, Department counsel argued that the Department had established its prima facie case, and that the evidence Taxpayer offered was not sufficient to rebut it. Tr. pp. 55-56. Counsel asserted that the evidence Taxpayer offered did not rebut the Department's case because it consisted only of testimony, with no corroborating documentary evidence to support Taxpayer's claim that the Department's determination was incorrect. *See* Tr. pp. 56-57. Counsel also argued that the activities Taxpayer used the dozer for were excluded from the regulation's definition of production agriculture. *See* Tr. pp. 58-59.

After considering the parties' arguments and the evidence, I agree that Taxpayer has not rebutted the Department's presumptively correct determination that the dozer was subject to tax.

The Department has adopted an administrative regulation in which it defined the statutory phrase “production agriculture,” by expressing a class of activities that are included within that phrase, and by expressing other activities that are excluded from that phrase. 86 Ill. Admin. Code § 130.305(f); Mid-American Growers, Inc. v. Department of Revenue, 143 Ill. App. 3d 600, 605-06, 493 N.E.2d 1097, 1101 (3rd Dist. 1986) (citing the definition of production agriculture in 86 Ill. Admin. Code § 130.305(f)). Specifically, that applicable regulation defines production agriculture, with respect to crops, as being “limited to activities necessary in tilling the soil, planting, irrigating, cultivating, applying herbicide, insecticide or fertilizer, harvesting and drying of crops.” 86 Ill. Admin. Code § 130.305(f). That same subsection also expressly provides that “[a]ctivities such as the clearing of land, mowing of fence rows, [and] creation of ponds or drainage facilities are not included ... [in production agriculture.]” *Id.*

Here, Taxpayer has consistently acknowledged that it used the dozer to make waterways, to build terraces, and to clean out fence rows. Department Ex. 1C; Tr. pp. 30, 33. During hearing, ABC also testified that he used the dozer in the winter to clear away snow from a yard and from driveways. Tr. pp. 30, 33.

Regarding the first use, Taxpayer offered no evidence to show that the waterways it made with the dozer were necessary for irrigating its crops. Thus, even if making waterways is not just another way of saying that the dozer was used to create ponds or drainage facilities, there is insufficient evidence to conclude that Taxpayer’s making of waterways is included within the regulation’s definition of production agriculture. 86 Ill. Admin. Code § 130.305(f).

Taxpayer also used the dozer to clean out fence rows. The specific meaning of “cleaning out” was never explained, although from the testimony and other evidence it appears that what ABC meant was that he used the dozer to tear down old fences and/or to clear land to make it ready for putting up new fence rows. Tr. pp. 33-35 (ABC); Department Ex. 5; Tr. p. 20 (Simmons). Since, however, the regulation excludes clearing land from the definition of production agriculture, I conclude that Taxpayer’s use of the dozer to clean out fence rows is also excluded from the definition of production agriculture. 86 Ill. Admin. Code § 130.305(f). But even if that conclusion is not correct, Taxpayer offered no evidence to show that cleaning out fence rows was necessary for tilling, planting, irrigating, or cultivating the soil being farmed, or for applying herbicide, insecticide or fertilizer, or for harvesting or drying Taxpayer’s corn and bean crops. *Id.*

The remaining two activities that ABC testified he used the dozer for include making terraces and plowing snow during the winter. Tr. pp. 30, 33. The latter activity is not a use that is necessary for tilling soil, planting, irrigating, cultivating, applying herbicide, insecticide or fertilizer, or for harvesting or drying crops. 86 Ill. Admin. Code § 130.305(f). Using an item of equipment to make terraces is not expressly referred to in the regulation. However, and as indicated by ABC’s testimony, farmers may make terraces to help avoid soil erosion, often caused by heavy rains. *See* Tr. pp. 30-35. If Taxpayer made terraces for this purpose, it is not unreasonable to conclude that its making of terraces is an activity that is akin to creating drainage facilities, which is expressly excluded from the definition of production agriculture. 86 Ill. Admin. Code 130.305(f). And again, there was no evidence offered to show that making terraces was necessary for tilling, planting, irrigating, or cultivating the soil Taxpayer farmed, or for

applying herbicide, insecticide or fertilizer, or for harvesting or drying its corn and bean crops.

As a final note, I want to make clear that my conclusion that Taxpayer did not rebut the Department's prima facie case is not based on a determination that a bull dozer can only be used for construction purposes. Rather, it is based on the determination that the claimed uses here do not come within the applicable regulation's definition of production agriculture.

Rules adopted by an administrative agency pursuant to statutory authority have the force of law and the administrative agency is bound by its rules. Department of Corrections v. Illinois Civil Service Commission, 187 Ill. App. 3d 304, 308, 543 N.E.2d 190, 194 (1st Dist. 1989). While an administrative regulation does not bind a court charged with reviewing an agency's application of an administrative regulation to a particular set of facts (*see, e.g., Wesko Plating Inc. v. Department of Revenue*, 222 Ill. App. 3d 422, 584 N.E.2d 162 (1st Dist. 1991)), the regulation at issue here certainly binds this administrative law judge on the question of which activities are included within the statutory phrase, production agriculture, as well as which activities are excluded from that phrase. 86 Ill. Admin. Code § 130.305(f); Department of Corrections, 187 Ill. App. 3d at 308, 543 N.E.2d at 194.

Conclusion:

I recommend that the Director finalize the NTL as issued, with penalties and interest to accrue pursuant to statute.

January 8, 2010
Date

John E. White, Administrative Law Judge