



COLORADO

Department of Revenue

Taxation Division

Office of Tax Policy
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PLR 23-008

December 27, 2023

XXXXXXXXXX
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Via Electronic Mail: XXXXXXXXXXXX

Re: Applicability of the Manufacturing Machinery Exemption to Certain Bakery Equipment

Dear XXXXXXXXXXXX:

You submitted a request for a private letter ruling on behalf of XXXXXXXXXXXX (“Company”), to the Colorado Department of Revenue (“Department”) pursuant to 1 CCR 201-1, Rule 24-35-103.5. This letter is the Department’s private letter ruling. This ruling is binding on the Department to the extent set forth in 1 CCR 201-1, Rule 24-35-103.5. It cannot be relied upon by any taxpayer other than the taxpayer to whom the ruling is made.

Issue

Whether Company’s purchase and use of certain tangible personal property used in Company’s bakeries is exempt from Colorado sales and use tax pursuant to section 39-26-709(1)(a)(II) and (2), C.R.S., and related state-administered local taxes.

Conclusion

Company’s purchase and use of the bakery equipment detailed herein is exempt from Colorado sales and use tax pursuant to section 39-26-709(1)(a)(II) and (2), C.R.S. This exemption applies to related state-administered local taxes except when the bakery equipment is purchased or used in a locality that has not adopted the optional manufacturing machinery and machine tools exemption.

Background¹

Company operates retail stores worldwide, most of which are in the United States. Within these stores, Company sells varied merchandise, including packaged food and sundries (such as dry grocery, frozen foods, drinks, candy, liquor, and tobacco); non-food items (such as electronics,

¹ Paragraph (4)(b)(ii) of 1 CCR 201-1, Rule 24-35-103.5 requires the request for a private letter ruling to include a statement of facts. This section generally recites the statement of facts provided in the initial request or in any supplement or amendment thereto, which is not an indication that the Department found such facts relevant to its analysis. Some relevant facts may be redacted or omitted to ensure confidentiality as required by section 24-35-103.5(5), C.R.S. The terms used in this section to describe the factual background are generally those of the requester.

major appliances, apparel, health and beauty aids, garden and patio, furniture, office supplies, housewares, and jewelry); and fresh foods (such as meat, produce, and bakery items). Company also sells goods and services ancillary to its primary retail business.

Almost all of Company's stores include a bakery. Company's typical bakery occupies 2,700-3,000 square feet. Each bakery's production facilities are segregated within a portion of the store that is physically inaccessible to customers, and typically, only a portion of the production facilities is visible to customers. The bakeries generally begin operations each morning at 4 a.m., hours before the store opens to customers.

Each day the store is open, each bakery produces, from raw ingredients, thousands of units of freshly baked products, including muffins, croissants, rolls, bagels, bread, cookies, danishes, cakes, mini-cakes, pound cakes, and pies. By way of example, a typical individual Company bakery will sell, in a given week, approximately 2,000 "units" of croissants (with one dozen croissants in each unit) and approximately 1,000 units of cookies (two dozen cookies in each unit). The bakeries' largest raw ingredient needs include flour, milk, eggs, sugar, oil, shortening, yeast, butter, salt, chocolate, cream cheese, lemon juice, and an assortment of natural fillings such as apples, pumpkin, and pecans. Company sources these raw ingredients from national and local vendors. Its bakeries receive shipments of the raw ingredients 6 days per week.

Company produces many of its baked goods from scratch, using individual raw ingredients. For example, it produces its cakes, muffins, pound cakes, mini-cakes, and many of its fillings and icings, among others, entirely from scratch. For other of its baked goods, Company purchases partially prepared materials from vendors, such as the dough for its bagels and artisan rolls.

All baked products are packaged for sale in large quantities (e.g., a minimum of one dozen croissants or two dozen cookies) and/or large sizes (e.g., 4-pound, 12-inch pies). For many of these products, the Company produces multiple varieties or flavors. For example, the bakeries produce up to 4 different varieties of bagels, 4 varieties of bread, and 5 types of cookies at any given time. Almost all of the baked goods are labeled and sold under Company's proprietary brand. All of the baked goods are packaged and sold for off-premises consumption.

A majority of the freshly baked goods are displayed in the store shopping area for selection and purchase by customers. Customers wishing to purchase particularly large quantities of baked goods may call in advance to place an order for pick-up.

Customers purchasing from Company's bakeries may be end consumers or wholesale customers. Many restaurants, coffee shops, and similar businesses purchase Company baked goods, under exemption certificates, for resale in their own establishments. By way of example, a cursory review of resale transactions in one recent week at one Company location revealed that a coffee shop purchased 8 six-packs of muffins and 6 four-packs of danishes; a cafe purchased 4 six-packs of muffins, 5 dozen croissants, and two dozen bagels; and a third customer purchased for resale 4 six packs of muffins, two dozen bagels, and 8 four-packs of danishes.

Each bakery requires substantial industrial baking equipment to satisfy its largescale production needs. This equipment is used by Company solely for the production of baked goods. The principal types of equipment purchased by Company for its bakeries—often found in multiple

quantities at any bakery—include the following:

- Mixers: Motorized mixers, generally 80-quart or 140-quart in volume, mix large quantities of raw ingredients to create a dough, filling, or glaze.
- Bowl Lifts: Mechanical lifts raise the heavy bowls coming from the mixers to facilitate pouring of mixed ingredients into the dough dividers and presses.
- Dough Dividers, Bread Rollers, and Presses: Dividers cut mixed dough into desired sizes. Bread rollers and presses manipulate the dough into desired thicknesses and shapes (e.g., for bread loaves and pie crusts).
- Depositors: Release prescribed quantities of mixed ingredients in precise locations on or into baking sheets, muffin tins, or molds.
- Unifillers: Deposit prescribed quantities of filling ingredients or icing on or into pies and cakes.
- Proofing Ovens and Baking Ovens: Proofing ovens introduce warm air and moisture to dough mixtures to promote rising. Large ovens bake the risen dough.
- Oven Racks: Racks are filled with unbaked goods and rolled into an oven, where a clamp lifts the rack slightly off the ground to permit rotation during the baking process. The racks turn throughout the baking process, ensuring an even distribution of heat across the baked items. When the baking is completed, the racks are dropped back to the ground and removed from the ovens. The baked goods will remain on the racks to cool (before packaging). For certain items (e.g., cheesecakes), the racks may be placed temporarily in the industrial refrigerator to speed the cooling process. Once the goods are cooled, the racks are moved to “production tables,” where the individual items are transferred, by employees, into containers for sale. The racks are never used to store finished goods or to display them on the retail floor.
- Glaze Sprayers: Spray liquified coatings, in consistent amounts and in precise locations, generally onto baked goods.
- Labeling Machines: Print labels for each of the packaged items, showing such information as nutritional content, weight, and price. These machines only print labels for individual packages for sale to Company’s customers.

For purposes of this PLR request, please assume the following: (1) that Company purchases each of the foregoing items of equipment for a price in excess of \$500; (2) that all of the subject equipment would have qualified for the federal investment tax credit that was provided in section 38 of the Internal Revenue Code of 1954; and (3) that Company purchases all of the subject equipment new (and therefore, the purchases would not have been subject to the former investment tax credit limitation for used equipment).

Discussion

Company's purchase and use of the bakery equipment detailed above is exempt from Colorado sales and use tax pursuant to section 39-26-709(1)(a)(II) and (2), C.R.S. This exemption applies to related state-administered local taxes except when the bakery equipment is purchased or used in a locality that has not adopted the optional manufacturing machinery and machine tools exemption.

Colorado imposes a sales tax on most sales of tangible personal property at retail, as well as certain services.² Tangible personal property embraces all tangible or corporeal things and substances which are dealt in, capable of being possessed, and exchanged.³ Retail sales include all sales made within the state except wholesale sales.⁴ A wholesale sale is a sale by a wholesaler to a retail merchant, jobber, dealer, or other wholesaler for resale and does not include a sale by a wholesaler to a user or consumer not for resale.⁵ Colorado also imposes a use tax upon the storage, use, or consumption of tangible personal property in this state purchased at retail.⁶

The bakery equipment is tangible personal property, as all the items listed above are corporeal goods that are dealt in, capable of being possessed, and exchanged. Company's purchases of the bakery equipment are purchases at retail because Company uses and does not resell the bakery equipment.

Nevertheless, section 39-26-709(1)(a)(II), C.R.S., exempts from sales tax purchases of machinery or machine tools, or parts thereof, in excess of \$500 to be used in Colorado directly and predominantly in manufacturing tangible personal property, for sale or profit. In order to qualify for exemption, the purchase of the machinery must be of such nature that it would have qualified for the investment tax credit pursuant to section 38 of the Internal Revenue Code.⁷ Section 39-26-709(2), C.R.S., provides a corresponding use tax exemption.

Each of the types of bakery equipment described above is machinery. "Machinery" means any apparatus consisting of interrelated parts used to produce an article of tangible personal property.⁸ That term includes both the basic unit and any adjunct or attachment necessary for the basic unit to accomplish its intended function.⁹ Therefore "machinery" encompasses, for example, a baking oven—which is used to produce baked rolls from raw dough. "Machinery" also encompasses the oven racks described above because they are an adjunct or attachment used by the oven to accomplish its intended function.

Company's bakeries are engaged in manufacturing. "Manufacturing" means the operation of producing a new product, article, substance, or commodity different from and having a distinctive name, character, or use from the raw or prepared materials.¹⁰ Company's bakeries

² Section 39-26-104, C.R.S.

³ Section 39-26-102(15), C.R.S.; 1 CCR 201-4, Rule 39-26-102(15), paragraph (1).

⁴ Section 39-26-102(9), C.R.S.

⁵ Section 39-26-102(19)(a), C.R.S.

⁶ Section 39-26-202(1)(b), C.R.S.

⁷ Section 39-26-709(1)(e), C.R.S.

⁸ *Id.* at (1)(c)(II).

⁹ *Id.*

¹⁰ *Id.* at (1)(c)(III).

operate daily to mass produce goods for sale at retail and wholesale. The process begins with raw and prepared ingredients, which Company receives six days per week. These ingredients are moved in a continuous and systematic flow through a series of steps using the industrial machinery described above. In totality, this system of mass production, including the space and machinery that comprise it, can properly be described as an “operation of producing.” Company uses both raw and prepared ingredients. These ingredients are altered by this process resulting in new products that are different from the raw and prepared ingredients.

The machinery is used directly in this operation of producing these new products. Although it does not explicitly define the term “directly,” the statute instructs:

For purposes of this subsection (1), direct use in manufacturing is deemed to begin for items normally manufactured from inventoried raw material at the point at which raw material is moved from plant inventory on a contiguous plant site and to end at a point at which manufacturing has altered the raw material to its completed form, including packaging, if required. Machinery used during the manufacturing process to move material from one direct production step to another in a continuous flow and machinery used in testing during the manufacturing process is deemed to be directly used in manufacturing.¹¹

The building space, the machinery, and the other fixtures dedicated to this operation of producing constitute a contiguous plant site. The bakeries are segregated areas within the store where this manufacturing operation takes place. This space, and the equipment therein, is employed exclusively for largescale production of goods, which makes these bakeries “plants” within the common meaning of that term.¹² Each piece of machinery (along with its adjuncts or attachments, if any) either acts upon and has a positive effect on the baked goods being produced,¹³ or it moves material from one direct production step to another in a continuous flow through the packaging process. The labeling machine is used in this final step of packaging to print labels for each package. The use of the bakery equipment as described is direct use in manufacturing.

The bakery equipment is used predominantly (in fact, exclusively) for manufacturing as described above. The oven racks, for example, are never used to store finished goods or to display them in Company’s stores. The label machines only print labels for individual packages for sale to Company’s customers.

As requested, we assume that Company purchases each of the foregoing items of equipment for a price in excess of \$500 and that Company purchases all of the subject equipment new. We do not rule on whether the subject equipment would have qualified for the federal investment tax credit that was provided in section 38 of the Internal Revenue Code of 1954 because you asked us to assume that it would have so qualified. If any of the bakery equipment

¹¹ *Id.* at (1)(d).

¹² *See Plant*, Merriam-Webster.com Dictionary, <https://www.merriam-webster.com/dictionary/plant> (last visited Dec. 26, 2023) (defining “plant” to mean, “the land, buildings, machinery, apparatus, and fixtures employed in carrying on a trade or an industrial business,” or, “a factory or workshop for the manufacture of a particular product.”). When a statute does not define an integral term, one may refer to a dictionary to determine the common usage of the term. *Breckenridge v. Egencia, LLC*, 442 P.3d 969, 976 (Colo. App. 2018).

¹³ *See Coors Brewing Co. v. Fagan*, 949 P.2d 110, 113 (Colo. App. 1997).

above would not have qualified, it is not exempt. Subject to this caveat, we rule that Company's purchase and use of the bakery equipment detailed above is exempt from Colorado sales and use tax pursuant to section 39-26-709(1)(a)(II) and (2), C.R.S.

Finally, you requested a ruling confirming the application of this exemption to certain state-administered local taxes, specifically, those imposed by the Regional Transportation District and the Scientific and Cultural Facilities District. The Colorado Revised Statutes authorize cities, towns, counties, and certain types of special districts to impose a sales tax.¹⁴ These sales taxes are collected, administered, and enforced by the Department in the same manner as the state sales tax.¹⁵ Certain special districts, namely the Regional Transportation District,¹⁶ the Scientific and Cultural Facilities District,¹⁷ and certain regional transportation authorities,¹⁸ also impose general use taxes applicable to the property at issue in this ruling. This ruling will refer to the taxes imposed by these cities, towns, counties, and special districts collectively as state-administered local sales or use taxes.

In addition to these state-administered local sales taxes, certain self-collecting home-rule cities may impose sales and use taxes under the independent authority allowed to them by the state constitution.¹⁹ This ruling does not extend to the sales taxes imposed by those cities.

In most cases, state-administered local sales taxes are imposed upon the same property and services subject to the state sales tax.²⁰ Cities, towns, and counties are, however, permitted to deviate from the state sales tax base with respect to certain optional exemptions.²¹ Importantly, the exemption for sales of machinery and machine tools allowed by section 39-26-709(1), C.R.S. will not apply to the sales taxes imposed by state-administered cities, towns, and counties unless their local ordinances or resolutions expressly include the exemption.²² Therefore, our ruling with respect to the bakery equipment will only apply to those state-administered cities, towns, and counties that have expressly adopted the exemption. Department publication DR 1002 details which jurisdictions have done so.

Special district sales taxes differ in very limited respects, and those deviations are normally

¹⁴ Section 29-2-102, C.R.S. (regarding incorporated towns and cities); 29-2-103, C.R.S. (regarding counties). The taxing authority for those entities that the Department refers to generally as "special districts" is found in the statutes establishing or permitting the establishment of the entity. See, e.g., section 32-9-119(2)(a), C.R.S. (empowering the board of the Regional Transportation District to impose a sales tax); 32-13-107(1)(a), C.R.S. (same with respect to the board of the Scientific and Cultural Facilities District); 43-4-605(1)(j)(I) (same with respect to regional transportation authorities).

¹⁵ Section 29-2-106, C.R.S. For special districts, refer to the enabling statutes as described in note 14, above.

¹⁶ Section 32-9-119(2), C.R.S.; *Howard Elec. & Mech. v. Dept. of Revenue*, 748 P.2d 1321, 1323–24 (Colo. App. 1988).

¹⁷ Section 32-13-107(1)(a), C.R.S.

¹⁸ Section 43-4-605(1)(j), C.R.S. Refer to Department publication DR 1002 for a list of regional transportation authorities that impose a use tax.

¹⁹ Colo. Const. art. XX, § 6. Section 29-2-106(4) permits the Department to collect the sales taxes of home-rule cities at their request. The Department generally does not distinguish these state-administered home-rule cities from other state-administered cities and towns because subsection (4)(a)(I)(A) of that section requires them to conform their ordinances to the requirements under article 2 of title 29 applicable to statutory cities and towns. This ruling applies to state-administered home-rule cities accordingly.

²⁰ Section 29-2-105, C.R.S. (with respect to cities and towns). For special districts, refer to the enabling statutes as described in note 14, above.

²¹ Section 29-2-105(1)(d), C.R.S.

²² *Id.* at (1)(d)(I)(A) and (1)(d)(III).

mandatory.²³ Neither the Regional Transportation District nor the Scientific and Cultural Facilities District may deviate with respect to the exemption for machinery and machine tools.²⁴ Therefore, our ruling applies to the sales and use taxes imposed by those special districts.

Miscellaneous

This ruling is premised on the assumption that Company has completely and accurately disclosed all material facts, that all representations are true and complete, and that Company has otherwise complied with the requirements of section 24-35-103.5, C.R.S., and the rules promulgated pursuant thereto. The Department reserves the right, among others, to independently evaluate Company's facts, representations, and assumptions. The ruling is null and void if any such fact, representation, or assumption is incorrect and has a material bearing on the conclusions reached in this ruling. This ruling is binding on the Department and is subject to modification or revocation, in accordance with 1 CCR 201-1, Rule 24-35-103.5.

Thank you for your request.

Sincerely,

Office of Tax Policy
Colorado Department of Revenue

This ruling cannot be relied upon by any other taxpayer other than the taxpayer to whom the ruling is made.

²³ The most common deviation requires special districts to exempt sales of cigarettes from the districts' sales taxes. *E.g.*, 29-1-204.5(3)(f.1), C.R.S. (regarding multi-jurisdictional housing authorities); 32-1-1003.5(5) (health assurance districts).

²⁴ See, section 32-9-119(2)(a), C.R.S.; 32-13-107(1)(a), C.R.S.