

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition :

of :

JOSAL FOODS, INC. :

DECISION

for Revision of a Determination or for Refund  
of Sales and Use Taxes under Articles 28 and 29 :  
of the Tax Law for the Period September 1, 1977 :  
through December 31, 1983. :

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Petitioner, Josal Foods, Inc., 8845 Main St., Harris Hill, Williamsville, New York 14221, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1977 through December 31, 1983 (File No. 52238).

A hearing was held before James J. Morris, Jr., Hearing Officer, at the offices of the State Tax Commission, State Office Building, 65 Court Street, Buffalo, New York, on January 14, 1986 at 1:15 P.M., with additional evidence to be submitted by February 14, 1986. Petitioner appeared by Gary Glowish. The Audit Division appeared by John P. Dugan, Esq. (Deborah J. Dwyer, Esq., of counsel).

#### ISSUES

I. Whether the Audit Division's denial of exemption from imposition of sales and use taxes with respect to certain purchases of electricity consumed in the operation of petitioner's supermarket was proper.

II. Whether the method used by the Audit Division to determine the amount of exempt kilowatt-hours of electricity consumed by certain equipment in petitioner's supermarket was proper.

FINDINGS OF FACT

1. On September 29, 1980, petitioner, Josal Foods, Inc., filed an Application for Credit or Refund of State and Local Sales or Use Tax claiming credit of \$1,365.00 for sales tax paid on certain purchases of electricity used by petitioner during the period September 1, 1977 through September 1, 1980.<sup>1</sup> The claimed credit was premised upon petitioner's contention that the electricity at issue was consumed in production and was therefore exempt from sales tax. On its sales tax returns filed subsequent to the period covered by its refund claim, commencing with the period ended February 28, 1981, and continuing through the period ended December 31, 1983, petitioner took credit for sales tax paid on similar purchases of electricity which petitioner determined had been consumed in production. Petitioner took \$2,990.00 in tax credits on its sales tax returns for the aforementioned periods. As a result, the total amount claimed herein by petitioner, including both credit sought by petitioner in its refund application and credits taken by petitioner on its sales tax returns, is \$4,355.00.

2. On March 9, 1984 the Audit Division advised petitioner that its claims for refund or credit of sales tax paid on utilities had been reduced from \$4,355.00, as claimed by petitioner, to \$2,101.70, following a review of petitioner's application and documentation submitted in support thereof. The Audit Division deducted the amount of credit computed to be due petitioner for the entire period (9/1/77 - 12/31/83) from the amount of credit for sales tax

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1 On its refund claim, petitioner excluded \$135.00 in tax paid on purchases relating to hot water production from the total paid, thus claiming a credit of \$1,230.00. The Audit Division treated the entire amount of \$1,365.00 as the refund claim, however, and based all its calculations on the larger amount.

paid on utilities actually taken by petitioner on its sales tax returns for the period December 1, 1980 through December 31, 1983. This resulted in an assertion of additional sales tax due in the amount of \$888.30. Based upon this determination, the Audit Division issued to petitioner on March 9, 1984 two notices of determination and demands for payment of sales and use taxes due which granted petitioner credit of \$887.86 for the period September 1, 1977 through November 30, 1980 and for the quarters ended August 31, 1982 and August 31, 1983. The Audit Division also asserted additional tax due of \$1,776.16 for the period December 1, 1980 through December 31, 1983. The net amount of additional tax due from petitioner as asserted by the Audit Division was therefore \$888.30, plus interest.

3. At all times during the period at issue herein, petitioner owned and operated a supermarket in Williamsville, New York which was open daily from 7:00 A.M. to 10:00 P.M., a total of 15 hours per day. Included among the store's operations were meat, produce, deli and bakery departments. Petitioner's claimed exemptions were premised upon purchases of electricity used to operate some 21 separate pieces of equipment in use throughout the store. The Audit Division granted exemption from imposition of sales tax for purchases of electricity with respect to 13 of the items in question. The Audit Division disallowed, in full, exemption from sales tax with respect to electricity purchases for four pieces of equipment in petitioner's produce department and disallowed, in part, exemption for electricity purchases for two items in petitioner's meat department and also two items in petitioner's deli and bakery departments.

4. The Audit Division's denial of petitioner's claimed credit with respect to its purchases of electricity for the equipment in petitioner's

produce department was premised upon the Audit Division's position that such electricity was not consumed directly in the production process. Specifically, electricity consumed in operating the scale, wrapper, pricer and produce cooler in petitioner's store's produce department was deemed nonexempt.

5. The scale in petitioner's produce department was used to weigh customers' purchases of produce. The pricer was used in conjunction with the scale and was used to price items. The wrapper was located behind a customer service counter and was used to package various products before such products were placed in open cases for sale. The produce cooler was located in petitioner's produce preparation room, an area removed from the customer shopping area. The produce cooler was a closed case used to store produce at proper temperatures both prior to placing such produce out for sale and, during periods when the store was closed, to store produce which had previously been placed out for sale.

6. The Audit Division also reduced the length of average daily exempt usage of petitioner's meat cooler and meat preparation room from petitioner's claimed 20 hours per day of usage to the Audit Division's assertion of 18 hours per day of exempt usage<sup>2</sup>. This reduction was premised upon the Audit Division's contention that the electricity consumed by those two items was used partly for nonexempt purposes.

7. Petitioner's meat cooler was used to store meat prior to placing such meat out for sale. Petitioner's meat preparation room was used to prepare meats to be placed out for sale. Both of these items were in use 24 hours per

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2 Both the meat cooler and the meat preparation room were in use 24 hours per day. The motors used to cool these areas, however, were not running for 24 hours. This resulted in petitioner's claim of 20 hours of usage.

day. The meat cooler was also used when the store was closed to store meat which had previously been placed out for sale. Both the meat cooler and the meat preparation room were cooled to temperatures necessary to preserve the meat purchased by petitioner until such time as it was sold to customers.

8. Regarding petitioner's store's deli department, the Audit Division reduced the length of average daily exempt usage of the scale and wrapper used in the deli department from 15 hours per day of exempt usage to 12 hours per day of exempt usage. As with petitioner's meat cooler and meat preparation room, this reduction was premised upon the Audit Division's contention that the electricity consumed by these two items was used partly for nonexempt purposes.

9. The scale in petitioner's deli department was used to weigh retail portions of deli meats and cheeses after slicing portions of such meats and cheese for retail sale. Petitioner's wrapper in its deli department was used to wrap all items which had been sliced and weighed and also to re-wrap those larger portions of the deli meats and cheeses which were returned to petitioner's coolers for storage.

10. In support of its refund claim, petitioner submitted to the Audit Division a survey of the electricity consumption of each of the 21 pieces of equipment for which petitioner claimed exemption with respect to its purchases of electricity. The survey was prepared on petitioner's behalf by Energy & Value Consultants, Inc., and set forth a description of each of the 21 items together with its respective make and model number. For eight of the items, the survey set forth figures indicating each item's horsepower, voltage, and amperage. For two of the items, the survey set forth figures indicating each item's horsepower and voltage. With respect to four of the items, only voltage and amperage figures were provided, and with respect to seven of the items,

only voltage figures were provided. Finally, with respect to all 21 items, the survey set forth kilowatt-hours of use, length of average daily usage and kilowatt-hours of use per day. The survey did not indicate the manner in which the figures indicating kilowatt-hours of use were determined.

11. After making its determination as to which equipment consumed electricity directly in production, the Audit Division sought to determine the proportion of petitioner's purchases of electricity which qualified for exemption from sales tax. To make this determination, the Audit Division first calculated kilowatt-hours for each piece of equipment which it had determined was used in production. With respect to each of the nine allowed items for which the survey listed a horsepower figure, the Audit Division used that horsepower figure to calculate kilowatt-hours by the following formula:

$$\frac{\text{Horsepower} \times 746}{1,000} = \text{Kilowatt-hours}$$

12. With respect to those items for which horsepower figures were not set forth in the survey, but for which voltage and amperage figures were set forth, the Audit Division used such voltage and amperage figures to determine kilowatt-hours by the following formula:

$$\frac{\text{Volts} \times \text{Amperes}}{1,000} = \text{Kilowatt-hours}$$

13. With respect to the six allowed items for which neither horsepower nor amperage figures were provided, the Audit Division accepted the kilowatt-hours figure set forth in the survey in making its determinations.

14. The formula set forth in Finding of Fact "11" was derived from information furnished to the Audit Division by the New York State Energy Office and the United States Department of Energy and was based upon a study of electric

motors ranging from 1 to 125 horsepower and having an average efficiency of 85 percent.

15. Having made its determination as to kilowatt-hours of exempt usage consumed by petitioner's equipment and the hours per day of such exempt usage, the Audit Division then calculated the ratio of kilowatt-hours of exempt usage to total kilowatt-hours of usage. This ratio was then applied to the total amount of petitioner's purchases of electricity to determine the amount of such purchases qualifying for exemption. The Audit Division used petitioner's utility bills to determine petitioner's total kilowatt-hours of usage and its total purchases of electricity.

16. The horsepower figures for the allowed pieces of equipment which listed such information ranged from 0.33 horsepower to 10.0 horsepower.

17. At hearing petitioner contended that its equipment was older than the equipment upon which the Audit Division's formula (as set forth in Finding of Fact "11") was based. Petitioner stated that the motors in its equipment were therefore less efficient than those upon which the Audit Division's formula was based. Petitioner claimed that, given the small size and inefficiency of the motors used in the equipment at issue, the kilowatt-hour calculations which were made using the formula set forth in Finding of Fact "11" were inaccurate. Petitioner further contended that calculations utilizing the formula set forth in Finding of Fact "12" would result in a more accurate determination of kilowatt-hours of electricity consumed by the equipment in question. Petitioner failed to substantiate its claim regarding the age and relative inefficiency of its equipment.

18. Of the 21 pieces of equipment for which petitioner submitted data regarding kilowatt-hours in its survey, petitioner used the formula set forth

in Finding of Fact "12" to determine kilowatt-hours for four of the items. Of the 17 remaining items, petitioner's data did not indicate the basis for its kilowatt-hour determinations.

20. At hearing petitioner submitted photocopies of its electric bills for the period September 1, 1983 through December 31, 1983. These bills had not previously been submitted by petitioner and had not been utilized by the Audit Division in making its determination in this matter.

CONCLUSIONS OF LAW

A. That section 1115(c) of the Tax Law provides for an exemption from the sales and use taxes imposed under sections 1105 and 1110 of the Tax Law as follows:

"Fuel, gas, electricity, refrigeration and steam, and gas, electric, refrigeration and steam service of whatever nature for use or consumption directly and exclusively in the production of tangible personal property, gas, electricity, refrigeration or steam, for sale, by manufacturing, processing, assembling, generating, refining, mining, extracting, farming, agriculture, horticulture or floriculture, shall be exempt from the taxes imposed under subdivisions (a) and (b) of section eleven hundred five and compensating use tax imposed under section eleven hundred ten."

B. That 20 NYCRR 528.22(c)(1) provides the following with respect to section 1115(c) of the Tax Law:

"(c) Directly and exclusively. (1) Directly means the fuel, gas, electricity, refrigeration and steam and like services, and must during the production phase of a process, either:

- (i) operate exempt production machinery or equipment,  
or
- (ii) create conditions necessary for production, or
- (iii) perform an actual part of the production  
process.



(2) Usage in activities collateral to the actual production process is not deemed to be used directly in production.

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(3)(i) Exclusively means that fuel, gas, electricity, refrigeration and steam and like services are used in total (100%) in the production process.

(ii) Because fuel, gas, electricity, refrigeration and steam when purchased by the user are normally received in bulk or in a continuous flow and a portion thereof is used for purposes which would make the exemption inapplicable to such purchases, the user may claim a refund or credit for the tax paid only on that portion used or consumed directly and exclusively in production."

C. That in view of the aforecited statute and regulations, the Audit Division properly denied exemption from sales tax for petitioner's purchases of electricity consumed in its produce department by the equipment described in Finding of Fact "5". Petitioner's scale is and was a convenience for its customers, aiding petitioner in the selling and distribution of produce. The scale is in no way related to the production process. Similarly, the wrapper and pricer also serve petitioner in the distribution and selling of produce. In no way do the wrapper or pricer effect a change in the nature, shape or form of the produce (see 20 NYCRR 531.2[e]). As to petitioner's produce cooler, this facility was at all times used for storage and therefore does not meet the exclusivity requirements of 20 NYCRR 528.22(c)(3)(i) and (ii). Consequently, the Audit Division properly denied exemption for purchases of electricity consumed by this equipment.

D. That petitioner's claimed average daily exempt usage of 20 hours for its meat preparation room and 15 hours for its deli scale and deli wrapper was proper. Inasmuch as the meat preparation room was used exclusively in production, the Audit Division's contention that this item was used for nonexempt purposes

when the store was closed is without merit. Accordingly, the Audit Division improperly reduced the hours of exempt usage for this item from 20 hours per day to 18 hours per day. As for the deli scale and deli wrapper, inasmuch as the Audit Division did not contest that the electricity consumed by such equipment was used for exempt purposes, and given the fact that this equipment was in use for 15 hours per day, the Audit Division's reduction of exempt usage from 15 hours per day to 12 hours per day was improper.

E. That with respect to petitioner's meat cooler, in view of the use of the equipment, when the store was closed, to store meat which had previously been placed out for sale (see Finding of Fact "7", supra), clearly nonexempt use, the Audit Division properly reduced the hours of daily exempt usage from 20 hours per day of exempt usage to 18 hours per day of exempt usage.

F. That the Audit Division properly recalculated the kilowatt-hours of exempt electrical use consumed by the equipment in petitioner's store. While petitioner submitted a survey with apparent kilowatt-hours figures for each item of equipment at issue, petitioner failed to set forth the basis of its calculations. Petitioner failed to establish its contention that the motors operating the equipment at issue were older and less efficient than the motors upon which the Audit Division's formula was based. In addition, petitioner failed to establish the validity of its survey. Finally, at hearing petitioner argued for use of the formula set forth in Finding of Fact "12" as the most reasonable means by which to calculate kilowatt-hours, yet a review of petitioner's calculations reveals that petitioner only used the aforementioned formula in calculating kilowatt-hours for 4 of the 21 items of equipment for which petitioner sought exemption herein. Petitioner has thus failed to show wherein the Audit

Division's calculations were improper or unreasonable and has further failed to establish the reasonableness or accuracy of its own calculations.

G. That with respect to the electric bills submitted by petitioner at hearing, the Audit Division is hereby directed to utilize such bills to compute the amount of tax credit to which petitioner is entitled in accordance with this decision.

H. That the petition of Josal Foods, Inc., is granted to the extent indicated in Conclusions of Law "D" and "G"; that the Audit Division is hereby directed to recompute the notices of determination and demands for payment of sales and use taxes due dated March 9, 1984 in accordance therewith; and that, except as so granted, the petition is in all respects denied.

DATED: Albany, New York

STATE TAX COMMISSION

OCT 15 1986

Rodriguez-Clema  
PRESIDENT

Francis D. Koernig  
COMMISSIONER

[Signature]  
COMMISSIONER