

Ohio: Supreme Court rules that manufacturer's purchases of natural gas do not qualify for sales and use tax exemption



David M. Kall | Thursday, August 2, 2018

The Ohio Supreme Court handed down its latest decision on the manufacturing exemption for sales and use tax on July 26, 2018. In [East Manufacturing Corp. v. Testa](#), the court ruled that a manufacturer of custom aluminum truck trailers could not claim the exemption for purchases of natural gas used to heat its manufacturing plant.

The manufacturer, East Manufacturing, argued that the natural gas purchases were essential to the manufacturing process because the manufacturing operation required them to maintain the temperature at 50 degrees Fahrenheit or higher. Specifically, East Manufacturing maintained that the temperature must be at least 50 degrees inside the plant to prevent condensation during its welding process.

The tax commissioner contested this factual premise, arguing that higher, not lower, temperatures would create condensation. By analogy to a soda can, the tax commissioner argued that condensation would form around the can upon being pulled from a cold environment in a refrigerator and subject to a warmer room temperature. By this line of reasoning, the heat produced by the natural gas may have been used not so much as to protect the welding and manufacturing operations, but instead to keep plant workers warm during cold winter temperatures in northeast Ohio, namely Randolph, Ohio.

East Manufacturing's legal argument centered on a statutory provision that allows exemption for "tangible personal property that totally regulates the environment in a special and limited area of the manufacturing facility where the regulation is essential for production to occur." Generally, materials used in regulating temperature in a facility are not exempt, but there is an exclusion that allows exemption for regulating "special and limited areas." But the court ruled that this exemption provision did not apply because the natural gas was not used in a special and limited area of the facility. Rather, East Manufacturing's plant consisted of several buildings that generally did not have walls and the natural gas was used to heat the entire area in each building.

East Manufacturing additionally claimed exemption pursuant to the general manufacturing exemption for items used in a manufacturing process. However, the court held that the general manufacturing exemption may not apply because it had already ruled out the specific exclusions to the taxability of materials used in temperature regulation. The general exemption provisions could not be used to circumvent the general assembly's specific directions on when the manufacturing exemption applied to temperature regulation.

For these reasons, the Ohio Supreme Court rejected East Manufacturing's claim to tax exemption for its natural gas purchases and affirmed the decision of the Ohio Board of Tax Appeals.



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