

Business tax tip #9

Sales and Use Tax Exemptions for Production Activities

The Maryland sales and use tax does not apply to sales of tangible personal property used directly and predominantly in production activities, or to sales of tangible personal property for resale or incorporation as material or part of tangible personal property produced for sale.

What constitute “production activities” for the sales and use tax exemption?

Exemption production activities include:

- Assembling, manufacturing, processing, or refining tangible personal property for sale or resale;
- Generating electricity for sale or for use in another production activity;
- Laundering, maintaining, or preparing textile products in providing the taxable service of commercial cleaning or laundering of textiles for a buyer who is engaged in a business that requires recurring service of commercial cleaning or laundering of the textiles;
- Establishing or maintaining clean rooms or clean zones required by federal laws pertaining to manufacture of drugs, medical devices, or biologics;
- Producing, repairing and maintaining machinery or equipment used in a production activity;
- Providing for the safety of employees (including safety glasses, hard hats and breathing apparatus); and
- Providing for quality control on a production activity site.

Servicing, maintaining, or repairing tangible personal property other than production machinery or equipment, or providing for the health and comfort of employees is not a production activity.

Processing food or beverages by a food vendor is also not production activity. See below for a specific exemption relating to food preparation.

What items are exempt?

- Any tangible personal property used directly and predominantly in a production activity at any stage of operation on the production activity site, from handling raw materials or components to moving finished product;
- Foundations to support other machinery or equipment or an item required to conform to air or water pollution laws and normally considered part of real property;
- Safety equipment used in production activity;
- Tangible personal property for quality control purposes used on a production activity site;
- Equipment and supplies used to remove finished goods on a production activity site;
- Machinery or equipment used to produce bituminous concrete; and
- Certain specified equipment used in aluminum production.

Do equipment leases qualify?

Yes. Lease payments for tangible personal property for use in production activities qualify for the exemption.

What about equipment used for both taxable and exempt purposes?

If machinery or equipment is used both in a production activity and administrative, managerial, sales or any other non-operational activity, the exemption may apply if it is used at least 50 percent of the time, *i.e.* predominantly, in a production activity.

What is meant by used "directly and predominantly"?

To meet the "directly" test, the use of the property must be integral and essential to the production activity, occurring where the production activity is carried on, and occurring during the production activity.

The "predominantly" test is met if the property is used more than 50 percent of the time directly in production activities.

Does food preparation by restaurants and food retailers qualify for exemption?

Generally, items used to process food for sale by grocery stores, bakeries, and other food retailers do not qualify for exemption.

However, there is a specific exemption for the sale of equipment to be used by a retail food vendor to manufacture or process bread or bakery goods for resale. To qualify for the exemption, the vendor must operate a "substantial grocery or market business" (see [Business tax tip #5 - How are Sales of Food Taxed in Maryland?](#)) at the same location where the food is sold, and the taxable price of each piece of qualified equipment must be at least \$2,000.

Can utilities and fuel qualify for exemption from sales tax?

Yes. Sales of utilities and fuel consumed directly and predominantly in a production activity is exempt. However, a sale of utilities and fuel for use in operating administrative, commercial and storage facilities and in providing plant heating and air conditioning is not exempt. When utilities are sold through a single meter for both taxable and exempt uses, taxability is controlled by the majority usage. The taxability of oil and coal is also controlled by the majority use where it is impractical to separate qualifying and non-qualifying usage. To claim the exemption for utilities and fuel, complete **Form ST 206 - Exemption Certification for Utilities or Fuel Used in Production Activities** and forward it directly to the vendor. You can request a copy of Form ST 206 by calling Taxpayer Service at 410-260-7980 in Baltimore or 1-800-638-2967 from elsewhere in Maryland.

How are the production activities exemptions claimed?

No special forms are needed to claim the machinery and consumable exemptions, other than Form ST206 for utilities and fuel. If a vendor requires documentation to support a claim for the machinery exemption, a signed form certifying use directly and predominantly in a production activity may be provided. A statement in the form of a resale certificate stating that the property will qualify may also be provided.

How are resale and incorporation exclusions claimed?

Vendors may not recognize the resale and incorporation exclusions unless provided with a resale certificate with a signed statement that the purchases are for resale, incorporation or otherwise used in a production activity, and including the buyer's name and address. For more information on the use of resale certificates, see **Business Tax Tip #4 - If You Make Purchases for Resale**. You can also request a copy by calling Taxpayer Service at 410-260-7980 in Baltimore or 1-800-638-2967 from elsewhere in Maryland.

Are purchases for research and development exempt?

Yes. The tax does not apply to purchases of tangible personal property for use or consumption in research and development. No special forms are required to claim the research and development exemption. If entitlement to exemption is not evident from the documents of sale, a vendor should obtain a certificate from the purchaser stating that the property will qualify.

What is considered research and development?

"Research and development" means basic and applied research in the sciences and engineering, and the design, development, and governmentally mandated pre-market testing of prototypes, products, and processes. Research and development does not include market research, research in the social sciences or psychology, and other non-technical activities, routine product testing, sales services, or technical and non-technical services.

Does the law have any special provisions for printers?

Yes. The tax does not apply to the sale of photographic materials used to produce an item (such as a photographic plate) used in composing, printing, or production of another item used in printing. Sales of artwork, electrodes, electrotypes, composition, lithographic plates or negatives, mats, photo engravings, stereotypes or typographies for direct use by a person engaged in printing tangible personal property for sale are also exempt. A person selling an item referred to above, other than those that are photographic in nature, must pay the tax on all materials used to produce them. A printer who produces these items for self use also must pay tax on all materials.

If I am due a refund of taxes previously paid, how do I get a refund or credit?

You may apply for a refund within four years from the date of payment of the tax by completing **Form ST 205 - Sales and Use Tax Refund Application**. You can also request a copy by calling 410-260-7980 in Baltimore or 1-800-638-2967 from elsewhere in Maryland. For assistance or information on filing refund claims, contact the refund office at 410-767-1538 within the Baltimore area.