

AWK note: The Dept. ultimately withdrew these rules!

6-2700-9730-1

STATE OF MINNESOTA  
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT OF REVENUE

In the Matter of Proposed Adoption  
of the Rule Relating to Sales and Use  
Tax on Capital Equipment and  
Replacement Capital Equipment,  
Minnesota Rules, Part 8130.2200.

REPORT OF THE  
ADMINISTRATIVE LAW JUDGE

The above-entitled matter came on for hearing before Administrative Law Judge Allan W. Klein on July 18, 1995, in St. Paul, Minnesota.

This Report is part of a rulemaking proceeding held pursuant to Minn. Stat. §§ 14.131 to 14.20, to hear public comment, determine whether the Minnesota Department of Revenue ("the Department") has fulfilled all relevant substantive and procedural requirements of law or rule applicable to the adoption of the rule, evaluate whether the proposed rule is needed and reasonable, and assess whether or not modifications to the rule proposed by the Department after initial publication are substantially different from the rule as originally proposed.

The Department's hearing panel consisted of Gregory Heck, Attorney, and Mary Blackburn, Revenue Sales and Use Tax Specialist. Approximately seventy persons attended the hearing. Forty-four persons signed the hearing register. The Administrative Law Judge ("ALJ" or "the Judge") received eighteen agency exhibits during the hearing. The hearing continued until all interested persons, groups, and associations had an opportunity to be heard concerning the adoption of this rule.

The record remained open for the submission of written comments until August 7, 1995, twenty calendar days following the date of the hearing. Pursuant to Minn. Stat. § 14.15, subd. 1 (1994), five working days were allowed for the filing of responsive comments. At the close of business on August 14, 1995, the rulemaking record closed for all purposes.

The Department must wait at least five working days before it takes any final action on the rule; during that period, this Report must be made available to all interested persons upon request.

Pursuant to the provisions of Minn. Stat. § 14.15, subds. 3 and 4, this Report has been submitted to the Chief Administrative Law Judge for his

approval. If the Chief Administrative Law Judge approves the adverse findings of this Report, he will advise the Department of actions which will correct the defects and the Department may not adopt the rule until the Chief Administrative Law Judge determines that the defects have been corrected. However, in those instances where the Chief Administrative Law Judge identifies defects which relate to the issues of need or reasonableness, the Department may either adopt the Chief Administrative Law Judge's suggested actions to cure the defects or, in the alternative, if the Department does not elect to adopt the suggested actions, it must submit the proposed rule to the Legislative Commission to Review Administrative Rules for the Commission's advice and comment.

If the Department elects to adopt the suggested actions of the Chief Administrative Law Judge and makes no other changes and the Chief Administrative Law Judge determines that the defects have been corrected, then the Department may proceed to adopt the rule and submit it to the Revisor of Statutes for a review of the form. If the Department makes changes in the rule other than those suggested by the Administrative Law Judge and Chief Administrative Law Judge, then it shall submit the rule, with the complete hearing record, to the Chief Administrative Law Judge for a review of the changes before adopting it and submitting it to the Revisor of Statutes.

When the Department files the rule with the Secretary of State, it shall give notice on the day of filing to all persons who requested that they be informed of the filing.

Based upon all the testimony, exhibits, and written comments, the Administrative Law Judge makes the following:

### FINDINGS OF FACT

#### Procedural Requirements

1. On July 18, 1994, the Department published a Notice of Solicitation of Outside Opinion at 19 State Register 172 regarding its proposal to adopt rules relating to the capital equipment and replacement capital equipment sales tax exemption or reduction.

2. On May 23, 1995, the Department filed the following documents with the Chief Administrative Law Judge:

- a. a copy of the proposed rule certified by the Revisor of Statutes;
- b. the Order for Hearing;
- c. the Notice of Hearing proposed to be issued;
- d. the Statement of Need and Reasonableness ("SONAR");

- e. a statement by the Department of the anticipated duration and attendance at the hearing; and
- f. a notice of discretionary additional public notice pursuant to Minn. Stat. §14.14, subd. 1a.

3. On June 12, 1995, the Department mailed the Notice of Hearing and a copy of the proposed rule to all persons and associations who had registered their names with the Department for the purpose of receiving such notice, all persons who requested a hearing on this rule, and all persons to whom additional discretionary notice was given by the Department.

4. On June 12, 1995, the Department published the Notice of Hearing and the proposed rule at 19 State Register 2366.

5. On June 21, 1995, the Department filed the following documents with the Administrative Law Judge:

- a. a photocopy of the pages of the State Register containing the Notice of Hearing and the proposed rule;
- b. the Notice of Hearing as mailed;
- c. the Department's certification that its mailing list was accurate and complete as of June 12, and the Affidavit of Mailing the Notice to all persons on the Department's mailing list;
- d. the Affidavit of Mailing the Notice to those persons to whom the Department gave discretionary notice; and
- e. all materials received in response to the Notice of Solicitation of Outside Opinion published on July 18, 1994.

#### Nature of the Proposed Rule and Statutory Authority

6. In 1984, the Minnesota Legislature adopted a reduced rate in the sales tax for capital equipment. Since that time, various policies and guidelines have been adopted and amended by the Department to implement the statute. The only formal rulemaking occurred in 1993, when the Department sought to adopt a comprehensive rule concerning capital equipment. The proposed rule was ultimately withdrawn. In 1994, the Minnesota Legislature again amended the sales tax exemption statute, Minn. Stat. § 297A.01. In response to that amendment, the Department initiated this rulemaking. The proposed rule defines terms and establishes eligibility criteria for the capital equipment exemption and the replacement capital equipment tax reduction.

In its SONAR and Notice of Hearing, the Department cites Minn. Stat. § 270.06, clause 14 (1994), as granting the Commissioner of Revenue the

authority to promulgate this rule. Minn. Stat. § 270.06, clause 14, provides that the Commissioner of Revenue shall:

[a]dminister and enforce the assessment and collection of state taxes and, from time to time, make, publish, and distribute rules for the administration and enforcement of assessments and fees administered by the commissioner and state tax laws. The rules have the force of law.

The Judge finds that the Department has statutory authority to adopt this rule.

#### Impact on Agricultural Land

7. Minn. Stat. § 14.11, subd. 2 (1994), imposes additional statutory requirements when rules are proposed that have a "direct and substantial adverse impact on agricultural land in this state." The statutory requirements referred to are found in Minn. Stat. §§ 17.80 to 17.84. The rule proposed by the Department will have no substantial adverse impact on agricultural land within the meaning of Minn. Stat. § 14.11, subd. 2 (1994).

#### Fiscal Note

8. Minn. Stat. § 14.11, subd. 1, requires state agencies proposing rules that will require the expenditure of public funds in excess of \$100,000 per year by local public bodies to publish an estimate of the total cost to local public bodies for the two years immediately following adoption of the rules. There will be no cost to local public bodies imposed by the rule.

#### Small Business Considerations in Rulemaking

9. Minn. Stat. § 14.115, subd. 2 (1994), requires state agencies proposing rules that may affect small businesses to consider methods for reducing adverse impact on those businesses. In its SONAR and Notice of Hearing, the Department indicated that it considered the impact of the rule on small businesses. The Department noted that the rule does not impose any reporting or payment requirements on small businesses. SONAR, at 2. The only filing requirement relating to capital equipment is the application for a refund and supporting documentation. *Id.* These requirements predate the proposed rule and arise from the statutory scheme for requiring payment of the sales or use tax and then applying for a refund. The proposed rule sets no deadline for compliance. The Department noted that it has simplified its reporting requirements for all businesses by not requiring cancelled checks or purchase orders and not requiring invoices for replacement capital equipment. SONAR, at 2. There are no performance standards being set by this rule. The Department considered that any exemptions for small business would be contrary to the capital equipment exemption statute. The Department has adequately considered the impact of the rule on small businesses as required under Minn. Stat. § 14.115, subd. 2.

## Analysis of the Proposed Rule

10. The Administrative Law Judge must determine, inter alia, whether the need for and reasonableness of the proposed rule has been established by the Department by an affirmative presentation of facts. The Department prepared a Statement of Need and Reasonableness ("SONAR") in support of the adoption of each of the proposed rule. At the hearing, the Department thoroughly supplemented the SONAR in making its affirmative presentation of need and reasonableness for each provision. The Department also made written post-hearing comments.

11. The question of whether a rule is reasonable focuses on whether it has a rational basis. The Minnesota Court of Appeals has held a rule to be reasonable if it is rationally related to the end sought to be achieved by the statute. Broen Memorial Home v. Minnesota Department of Human Services, 364 N.W.2d 436, 440 (Minn. App. 1985); Blocher Outdoor Advertising Company v. Minnesota Department of Transportation, 347 N.W.2d 88, 91 (Minn. App. 1984). The Supreme Court of Minnesota has further defined the burden by requiring that the agency "explain on what evidence it is relying and how the evidence connects rationally with the agency's choice of action to be taken." Manufactured Housing Institute v. Pettersen, 347 N.W.2d 238, 244 (Minn. 1984). An agency is entitled to make choices between possible standards as long as the choice it makes is rational. If commentators suggest approaches other than that selected by the agency, it is not the proper role of the Administrative Law Judge to determine which alternative presents the "best" approach.

12. This Report is generally limited to the discussion of the portions of the proposed rule that received significant critical comment or otherwise need to be examined. Accordingly, the Report will not discuss each comment or rule part. Persons or groups who do not find their particular comments referenced in this Report should know that each and every submission has been read and considered. Moreover, because some sections of the proposed rule were not opposed and were adequately supported by the SONAR, a detailed discussion of each section of the proposed rule is unnecessary. The Administrative Law Judge specifically finds that the Department has demonstrated the need for and reasonableness of the provisions of the rule that are not discussed in this Report, that such provisions are specifically authorized by statute, and that there are no other problems that prevent their adoption.

13. Where changes are made to the rule after publication in the State Register, the Administrative Law Judge must determine if the new language is substantially different from that which was originally proposed. Minn. Stat. § 14.15, subd. 3 (as amended by Minn. Laws 1995, ch. 233). The standards to determine if the new language is substantially different are found in Minn. Stat. § 14.05, subd. 2 (as amended by Minn. Laws 1995, ch. 233). Any language proposed by the Department which differs from the rule as published in the State

Register and is not discussed in this Report is found not to be substantially different.

## Proposed Rule Part 8130.2200 - Capital Equipment; Replacement Capital Equipment

The Department's proposal consists of only one rule, which has ten subparts. The subparts will be discussed individually.

### Subpart 1 - General Information

14. Item A of subpart 1 restates the statutory standards for capital equipment to qualify for the sales tax exemption. Item B restates the standards for the replacement capital equipment sales tax reduction. Item C sets out the possibility that capital equipment not qualifying for the exemption could qualify for the replacement capital equipment reduction. Item D states:

“Sold ultimately at retail,” as required under subpart 3, item B, includes the situation where an article is made and sold to either be used in producing a different product or to become incorporated into another product.

Daniel F. Peterson, of Larson, Allen, Weishair & Co. on behalf of some members of the Tax Section of the Minnesota Society of Certified Public Accountants (MSCPA), and others, suggested that the use of “includes” seemed to be inclusive in some places, but exclusive in others. He noted that this is confusing and proposed “includes but not limited to” where that is the intent of the Department. The Department agreed with the comments and altered this rule accordingly. What the Department is attempting to say here is that the phrase “sold ultimately at retail” is not limited to the traditional concept of a retail sale to an ultimate consumer, but also includes more indirect sales. Normally, the phrase “includes but not limited to” is objectionable when it attempts to give unbridled discretion to administrators. That is not the case here. Instead, the Department is attempting to add somewhat unusual circumstances to a more traditional one. In this situation, the proposed rule does not violate any substantive provision of law. The new language does not constitute a substantial change.

### Subpart 2 - Definitions

#### Item A - Accessories

15. Item A of subpart 2 defined “accessories” in three sentences. The first sentence purports to be a definition and the following two sentences “include” nonessential attachments and devices incapable of acting independently into the definition of accessories. The second paragraph contains a treatment of accessories as qualifying for the exemption if the accessory is: a) purchased prior to the operation of the qualifying equipment, and b) essential to

the operation of the integrated production process. Examples of the treatment of a newsprint roll holder, injection molds, and equipment installed after the process is put into operation are included in the item.

16. David A. Olsen, Vice President of Manufacturing for Potlatch Corporation, urged the Department to clarify that equipment added that is “essential to the control, regulation or operation of the equipment” be eligible for the exemption. Potlatch maintains that such equipment should not be excluded because the equipment is acquired “to correct defects in the quality of the product being produced or improve the production capacity of the initial equipment.”

Barbara Dunham of Refund Investigators objected to the accessory definition for failing to identify when equipment ceased to qualify for the exemption or reduction. William A. Blazar, Vice President of Government Affairs and Policy Development for the Minnesota Chamber of Commerce (MCC or the Chamber), urged clarification of the accessories definition to include only that equipment “not essential to the cost-effective operation of an integrated production process.” John V. Stowe, Tax Manager for Coopers & Lybrand, urged that all machinery be treated as exempt capital equipment. The Department responded that the exemption was not dependent upon whether the final product could be produced to provide an adequate profit. The Department relies upon the function of the machinery and its relation to the production process to determine the tax status of the item. MCC also suggested that equipment purchased to replace essential equipment qualify for the exemption. Minn. Stat. § 297A.01, subd. 20, defines “replacement capital equipment” and the statutory definition includes the equipment mentioned by the commentator. MCC’s suggestion goes beyond the statutory scheme.

17. West Publishing Company (West), and Coopers & Lybrand objected to the portion of the definition limiting qualifying equipment to that machinery purchased prior to the operation of an integrated production process. The Department cited the statutory definition of replacement capital equipment to support the rule. Minn. Stat. § 197A.01, subd. 20. The Department asserts that an integrated production process cannot begin without all essential components in place. Anything added afterward is, by definition, not essential. The Department has shown the prior purchase language to be needed, reasonable, and authorized by statute.

18. Gregg A. Mensing, Sales Tax Manager for 3M, objected to the one-month reference in the example of installing a pick and put machine. 3M maintains that a manufacturer should be able to get some production out of its equipment when it arrives and not wait for the delivery of other machines. The argument overlooks the statutory scheme, however. The Department cannot ignore the two statutory requirements, that only equipment essential to the production be afforded the exemption and any capital equipment obtained afterward be characterized as replacement capital equipment, even if it increases

the speed, efficiency or production capacity of the process. The Department did eliminate the one-month reference as potentially misleading. The example, as modified, correctly states the effect of initiating production before all the components of an integrated production process are in place.

19. MSCPA suggested that the newsprint roller example was unclear as to whether the equipment was nonexempt due to its relation to the integrated process or because the equipment was purchased after the integrated process was put into production. As the rule is written, either ground appears to be a proper basis for denying the exemption in the roller example. However, the rule would be improved if the Department specified why the example yields the conclusion which it does. The example is not unacceptably vague, but an explanation would assist taxpayers and should be added.

#### Item B - Equipment

20. Item B defines “equipment” as “independent devices separate from machinery but essential to an integrated production process.” It then goes on to list items that are included and give examples.

21. MCC suggested the language of the item could be confusing because of the use of the term “basic machinery.” The commentator pointed out that the term is not used in the statute and not defined in the rule. The Department agreed with the comment and replaced the term “basic machinery” with “integrated production process.” The new language clarifies the rule, is needed and reasonable, and does not constitute a substantial change.

22. The example in item B explicitly excludes electrical transformers and substations not directly connected to a generating plant from qualifying for the capital equipment sales tax exemption. Sue Ann Nelson, of Dougherty, Rumble & Butler, on behalf of Northern States Power Co. and United Power Association (“the Utilities”), objected to the classification of transformers as non-qualifying equipment. The Utilities maintain that the proposed definition of equipment is unduly restrictive by excluding transformers and substations. Coopers & Lybrand characterized transformers as “indirectly operating or controlling the machines.” These devices reduce the voltage of electricity to the level usable by the ultimate consumer. The Utilities argue that the reduction of voltage is an integral part of the production process. The commentators assert that the process of reducing voltage is a step in the manufacturing of electricity and under the definition of manufacturing, transformers cannot be excluded. Utilities’ Comment, at 10. The Department responded that a change in voltage is not a fundamental change in the electricity produced and thus, does not qualify for the capital equipment sales tax exemption or replacement capital equipment reduction. The Department analogized the delivery of electricity to the delivery of tangible personal property by a vehicle. The Utilities also compared transformers to the ready-mix mixing unit placed upon a delivery truck. When bought separately, the mixing unit is capital equipment, the truck is not.

Applying the “mixing truck” analogy, transformers are not capital equipment. The mixing unit takes constituent parts of concrete: aggregate, water, and cement, and processes them en route to a location. The action of processing the constituent parts into something new qualifies the mixing unit as exempt capital equipment. But in the case of transformers, there is nothing “new” that is produced. Transformers alter the voltage, either up or down, but what comes out is still electricity. A watt of electricity at 1,000 volts is fundamentally the same as a watt of electricity at 100 volts. Here, the statutory provision on manufacturing only includes the generation of electricity, not the distribution or delivery of that electricity. Transformers and substations are delivery devices that do not generate electricity within the meaning of Minn. Stat. § 297A.01, subd. 16(d)(4). The Department’s rule and example are needed and reasonable, as proposed.<sup>1</sup>

### Item C - Essential

23. A number of commentators at the hearing urged the Department to clarify what the term “essential” means in the context of this rule. The Department responded by proposing a definition of “essential” to be added as item C (relettering all subsequent items). The new language defines the term as “items indispensable to the integrated production process” and excludes “equipment or machinery which upgrade, enhance, modernize, or replace existing equipment.” The definition goes on to note that a company’s conclusion that economic viability cannot be maintained without the equipment or machinery does not render the equipment or machinery “essential to the original and/or existing integrated production process.” An example is given of a more efficient drill press replacing an existing drill press, concluding that the new press is not essential.

The new language meets the needs of the commentators who want clarification of the term “essential.” Stylistically, the term “and/or” is in the dictionary (American Heritage Dictionary, Second Edition, at 108 (1985)), but the term is described there as “stilted.” The use of the term could cause confusion, but not to a level that constitutes a defect. The Judge suggests modifying the wording to the first portion of that sentence to render the language less idiomatic. The Judge suggests the following language:

That a company deems equipment or machinery to be essential to increasing the company’s economic viability does not render that equipment or machinery “essential” to the existing integrated production process. . . .

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<sup>1</sup>There is litigation pending on this issue. The Utilities expressed concern that adoption of this rule would be an improper infringement on the judicial process. The Judge disagrees. The rule is prospective only, while the litigation deals with past transactions. The two are not mutually exclusive.

The suggested language is not required to be adopted and is merely offered as an alternative to the Department's proposed language. The proposed rule, is needed and reasonable with or without the modification.

#### Item D - "Fabricating"

24. The Department has chosen to duplicate statutory language in order to provide the basis for an example. As originally proposed, the example did not state a conclusion, in the sense that it did not indicate whether or not those facts resulted in the item qualifying as capital equipment or not. The Tax Section of the Minnesota State Bar Association pointed out that this example should state a conclusion and the grounds for it so that it can provide guidance to taxpayers. In response to this comment, the Agency proposes to add a sentence to indicate that the equipment used in the fabrication "may qualify" as capital equipment. The Administrative Law Judge finds that this choice of words does not cure the problem raised by the Tax Section. If the example is to be of any benefit at all, taxpayers need to know whether the equipment qualifies, or does not. To say that it "may" qualify does not answer the question. The Administrative Law Judge concludes that this is so vague as to constitute a defect which must be remedied. In order to cure the defect, the Department must state, with clarity, whether or not the equipment in the example does qualify. If the Department is concerned that there are a number of other tests which must be met in order for the equipment to qualify, it can cure the defect by using language such as:

The equipment used in the fabrication of the compact disc player qualifies as capital equipment, so long as it meets all of the other tests in statute or rule.

#### Item E - Generation of Electricity or Steam

25. Item E defines the term "generation of electricity or steam" as the "creation of electrical energy or steam" and limits the process to the activity at the production facility. Transmission and distribution of the electricity or steam is expressly excluded from the definition. The arguments surrounding this issue were discussed earlier. Item E is consistent with the statutory inclusion of generation of electricity and steam as a manufacturing activity. The statutory definition does not include transmission or distribution equipment or machinery. Item E is needed and reasonable, as proposed.

#### Item F - Integrated Production Process

26. Minn. Stat. § 297A.01, subd. 16(b) extends the definition of capital equipment to all equipment "essential to the integrated production process." Item F defines "integrated production process" by using four discrete sentences with different concepts. The language in the rule is unclear. The Judge suggests using the operative language in each sentence in an itemized list. The rule would then read:

“Integrated production process” means:

- (1) a process in which a number of distinct devices are joined or linked together in some manner so that they operate or function as a unit to provide for the manufacturing, fabricating, mining, or refining of tangible personal property; or
- (2) a coordinated group of fixed assets, which may include land, buildings, machinery, and equipment, that are essential to and used in an integrated manufacturing, fabricating, mining, or refining process; or
- (3) an economic unit in which qualifying business activity is conducted; or
- (4) an economic unit in which manufacturing or other industrial operations are performed; or
- (5) outside fabrication services contracted for by a manufacturer provided those services are essential to and an integral part of the production of tangible personal property to be ultimately sold at retail; or
- (6) research, development, and design activities conducted by a manufacturer of tangible personal property; or
- (7) storage of work in progress.

The language has been adjusted to retain coherence in the concepts underlying the proposed rule. Particularly with subitem 3, the word “qualifying” was added to ensure the rule definition as originally proposed did not purport to extend the exemption to non-qualifying business enterprises. The suggested language renders the proposed rule more readable. The rule is needed and reasonable with or without the suggested modifications. The new language does not constitute a substantial change.

#### Item G - Machinery

27. “Machinery” was originally is defined in item G as a mix of definitions and exclusions that suffered from readability problems. This was noted by the Tax Section, among others. In order to better focus the definition, the Agency proposes to take some of the language that was originally part of the definition of “machinery” and move it so that it becomes part of the definition of “essential” which was added as well. The Administrative Law Judge finds that this solution is appropriate. In addition, the Agency proposes to change the words “quality control” to “monitoring” in response to criticisms from IBM and the Minnesota Chamber of Commerce. The rule, as modified, has been demonstrated to be needed and reasonable.

#### Item H - Manufacturing

28. The term “manufacturing” is defined by proposed item H. The definition contains the nonexclusive language “may” in describing the end product of the manufacturing process. This language is defective, since the language is too vague to describe the limits on what the end product must be to qualify the manufacturing process. To cure this defect, the Judge suggests that the word “either” be inserted into the sentence, so that it is clear what the sentence means.

29. The proposed rule sets forth definitions of what the word “manufacturing” does mean, as well as a definition of what it does not mean. Those are followed by examples of businesses which are “considered to be engaged in manufacturing”, as well as examples of businesses which are “not considered to be engaged in manufacturing”. The MSCPA objected to the examples, pointing out that whether any given business is performing a qualifying type of activity needs to be determined on a case-by-case basis. They used an example of a law firm or accounting firm (typically not a “manufacturer”) which purchases a copy machine and uses it primarily for making copies for which it charges its clients and collects sales tax. MSCPA believes that the copy machine ought to be treated as capital equipment. The Department responded that if the equipment were used primarily to manufacture a tangible personal property item that is sold at retail, then the equipment or machinery could qualify as capital equipment. The Administrative Law Judge questions whether ordinary taxpayers (for whom the examples are, after all, intended) would grasp this distinction between the type of business and what it is doing at the time. MSCPA suggested that another approach would be to use examples of “activities” that qualify or do not qualify, rather than “businesses”. The Administrative Law Judge agrees that this would be an improvement. It does solve the problem which exists. Another solution would be to add a sentence to the rule that read something like the following:

Any of these businesses, however, might engage in some activities which involve the use of capital equipment which would be eligible for a refund.

While the Administrative Law Judge does not believe that the rule, as a whole, is so misleading that there is a defect, he urges the Department to rewrite the rule, or at least add the sentence for the benefit of taxpayers.

#### Item J - Mining

30. “Mining” is defined in item J in two sentences. Both sentences suffer from the “includes” problem discussed earlier. While not a defect, the Judge suggests that the rule be clarified by using the following language:

“Mining means the process of extracting ore, minerals, or peat from the earth for commercial purposes through underground, surface, and open-pit operations; and

extracting building stone, limestone, gravel, sand, or other surface materials from surface operations.

The suggested language more clearly states the limits to the rule. The rule is needed and reasonable, either with or without the change. The suggested language does not constitute a substantial change.

#### Item K - On-line Data Retrieval System

31. "On-line data retrieval system" is defined in proposed item K. The definition sets out the following qualifying "factors," all of which must be present, according to the rule, for the on-line data retrieval system (ODRS) to be exempt:

- (1) the equipment must be used as an ODRS;
- (2) data retrieval must be done by the customer;
- (3) all of the information in the system must be equally available and accessible to all the customers;
- (4) the provider must use the system to gather and refine information in the database
- (5) the provider must maintain the database; and
- (6) the system must accept electronically transmitted queries from customers about the contents of the database, identify and retrieve the data, format the data, and electronically transmit the data to the customer.

The rule specifically excludes any ODRS that retrieves information that "was solely gathered from third-party sources (such as bond or stock market prices)." The rule also specifically excludes on-line bulletin boards or networks. The rule also excludes any system on which any information is not made available to any customer due to data privacy restrictions.

West Publishing, the Chamber, the Tax Section and MSCPA all objected to the proposed rule as overly restrictive and inconsistent with the statutory provisions concerning ODRS. The statute states in pertinent part:

- (a) Capital equipment means machinery and equipment purchased or leased for use in this state and used by the purchaser or lessee primarily for manufacturing, fabricating, mining, or refining tangible personal property to be sold ultimately at retail and for electronically transmitting results retrieved by a customer of an on-line computerized data retrieval system.

\* \* \*

(d) For purposes of this subdivision:

\* \* \*

(6) “On-line data retrieval system” means a system whose cumulation of information is equally available and accessible to all its customers.

Minn. Stat. § 297A.01, subd. 16.

The Department maintains that the wording of the statute demonstrates the Legislature intended that the “manufacturing, fabricating, mining, or refining” requirements be incorporated in the data transmitted by an ODRS for it to qualify as capital equipment. Department August 14, 1995 Comment, at 11. The commentators noted above all disagree, and read the ODRS language as completely separate. The Administrative Law Judge finds that the language of the statute -- the wording and verbs used -- indicate that the Legislature intended to treat ODRS as a separate piece of equipment and the act of “electronically transmitting” as the action which qualifies the ODRS as capital equipment. The terms “manufacturing, fabricating, mining, or refining” are defined in the statute and none of those definitions makes reference to ODRS. The statute’s treatment of ODRS is similar to the statutory treatment of power generation in that the process is recognized as qualifying, despite the incongruity of the process in relation to the traditional definition of capital equipment. Even the wording of the Department’s proposed subpart 3B recognizes the difference between “manufacture, fabricate, . . .” and “electronically transmit.”

The Department cited a recent tax court case<sup>2</sup> in which West Publishing Company successfully appealed the disallowance of its equipment. SONAR, at 17. The Department opined that the statutory provisions regarding ODRS are in response to that court ruling, and that therefore we must read into the statute the salient facts of what West was doing at the time. The Judge believes that the plain language of the statute must control. There is no basis in the language of that statute to disqualify an ODRS based on the source of the information contained therein. Nor is there any basis to exclude bulletin board systems or networks if they meet the other standards. The fourth “factor” is found to be a defect in the proposed rule for improperly limiting a statutory provision. The factor must be deleted to cure the defect.

32. West further asserts that the Department is unduly restricting the exemption for ODRS by limiting the exemption to those systems whose information is completely accessible to all its customers. The Department correctly points out that the statutory definition requires that the total cumulation

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<sup>2</sup> West Publishing Co. v. Commissioner of Revenue, Dkt. No. 5346 (Minn. Tx. Ct., July 11, 1990), aff’d, 464 N.W.2d 512 (Minn. 1991).

of information in an ODRS be “available and accessible to all its customers.” Minn. Stat. § 97A.01, subd. 16(d)(6). In its proposed rule, the Department has restated the statutory definition and taken an “all or nothing” approach to the existence of any non-accessible information in the system. West questions how that position is reconciled with the concept of “primarily”, as used both in the statute and the rule, to suggest that equipment must be used 50% or more of the time in an exempt activity in order to be qualified. For example, if a company used its equipment 51% of the time for an ODRS, but used it 49% of the time for internal payroll, personnel, and other non-qualifying activities, the concept of “primarily” would suggest that the equipment could still qualify, while the Department’s rule would disqualify the equipment. The Administrative Law Judge finds that there is no statutory basis for deleting the concept of “primarily” in the case of an ODRS. Therefore, the third “factor” listed above must be recast to incorporate the concept of “primarily”. Language which would accomplish this result could read as follows:

- (3) A system must be used, primarily, to provide access to information. The information must be equally available and accessible to all the customers.

33. It is clear from the wording of the proposed rule that “all of the following factors must be present”. The Administrative Law Judge would suggest, however, that the word “elements” would be preferable to “factors”, because the former implies that all are required, while the latter suggests that not all need be present. This is merely a suggestion, because the context clearly indicates that all must be present, but there is no reason not to pick the best language to avoid problems if the rule is edited or otherwise changed in the future to obscure the clarifying context.

#### Item L - Refining

34. “Refining” is defined in item L in three sentences. The third sentence contains an addition definition for refining as applied to ODRS. Due to the preceding Finding, there is no basis for applying a definition of refining to ODRS. To correct this defect, the third sentence must be deleted.

#### Item N - Special Purpose Buildings

35. Item N defines “special purpose buildings” for the purpose of determining if a building qualifies as replacement capital equipment. IBM objected to the definition as lacking a distinction between the building and any capital equipment within the building. The Department responded that the only equipment that would have its status altered would be that equipment attached to the building so as to be a fixture.

36. Subitem 2 limits the qualification of special purpose buildings for the replacement capital equipment exemption to those buildings dedicating at least

80 percent of the floor space to the special purpose and at least 50 percent of the time in the integrated production process. MSCPA suggested using a 70 percent figure on the use of floor space. The Department pointed out that the MSCPA did not introduce any hard information to support its figure. In the SONAR, the Department offers its opinion that 80 percent is reasonable, but offered nothing more than common sense to support its figure. There is no statutory definition of “special purpose building.” The Department could require, consistent with the statute, that 100 percent of the floor space be used for the special purpose.

Clearly, some space is needed for bathrooms, break rooms, etc. The 80 percent figure is needed and reasonable to allow for inclusion of these amenities.

37. Coopers & Lybrand and IBM urged that the rule be expanded to incorporate large storage tanks and processes outside the integrated production process, respectively. The Department declined to make those changes, citing statutory limitations and longstanding agency practices. The Administrative Law Judge finds that the Department’s proposal has been justified and may be adopted.

#### Item O - Support Operations and Administrative Purposes

38. MSCPA and DTED urged that “tool rooms” and other such maintenance expenses be included in the definition of capital equipment and excluded from the definition of “support operations and administrative purposes” in item O. Unisys maintains that not providing capital equipment treatment to tool rooms and other such operations affords inequitable treatment to manufacturers who maintain such facilities, compared with manufacturers who do not. The Department declined to make that change, citing the statutory limitations on capital equipment. The Department’s analysis is correct.

Item O suffers from the “includes but not limited to” problem. The Judge suggests (but does not require) that the second sentence be change to read as follows:

The following activities are deemed to be examples of “support operations” or “administrative purposes:

[remainder of the rule unchanged]

The suggested language retains the benefits of a nonexclusive itemized list without using language that creates a status outside the general definitional language not contained in the rule. The rule is needed and reasonable. The suggested language is not a substantial change.

#### Subpart 3 - Qualifying Capital Equipment

39. Proposed subpart 2, discussed above, contained definitions. Proposed subpart 3 sets out the standards an item must meet to qualify for the sales tax exemption for capital equipment.

40. Item A requires that the equipment or machinery must be “used by the purchaser.” The Department made an important modification to the original proposal in response to public comments. MSCPA, SMARCA, Inc., the Minnesota Electrical Association, Seagate and others recommended that the Department allow machinery and equipment purchased by a contractor, under various circumstances. In response, the Department proposed an addition to the language at the end of item A that allows for a principal-agent relationship to “pass-through” the capital equipment exemption if: a) the written contract authorizes the contractor to bind the principal; b) the purchase is in the principal’s name; c) the purchase contract identifies the principal as obligated to pay; d) all of the capital equipment is used by the principal; e) title vests in the principal at the time of delivery; and f) all risks of ownership are with the principal. The new language goes a long way toward meeting the needs of the commentators, is consistent with the longstanding practices of the Department, and clarifies the standards that apply to principal-agent relationships. The item is needed and reasonable, as modified. The new language is not a substantial change. However, in light of earlier Findings which do not accept the Department’s treatment of ODRS as “refiners”, the Department should add a reference to ODRS in the first sentence of the new rule.

41. Item B requires the equipment or machinery be used to “manufacture, fabricate, mine, or refine tangible personal property to be sold ultimately at retail.” Grant Thornton and DTED objected to the rule because items or products manufactured for use by the manufacturer itself are not included in the “ultimately at retail” part of the rule. Grant Thornton maintained that a taxable use is equivalent to a taxable sale and therefore the rule inappropriately limits the statutory exemption. In the case of ready-mix concrete contractors or asphalt contractors, the machinery to manufacture the product (concrete or asphalt) qualifies if the product is purchased from another, but does not qualify if the product is manufactured by the user to perform its jobs. The commentators maintain that this puts them at a competitive disadvantage against manufacturers who purchase items from others, rather than manufacture the items themselves.

The Department acknowledged the different treatment of the machinery and equipment and asserts that this outcome is required by the statutory language of the capital equipment statute. The Legislature has made a distinction between service industries who produce their own supplies and industries who sell goods to service industries. The Legislature can make distinctions between differently situated groups. Since an independent manufacturer of supplies will presumably add a profit margin to its product, the cost savings to making one’s own product for use in its service business can act as an independent incentive. The statute is clear that, for machinery or equipment to qualify, the product must be “ultimately sold at retail.”

42. Refund Investigators, the Tax Section, Coopers & Lybrand, and others raised questions about the Department's attempt to define when the manufacturing, fabricating, or refining process ends. The Department has defined it as ending when "the completed state is achieved", including packaging and placing of the completed product into finished good inventory. The proposed rule goes on to state that if the tangible personal property is not placed into finished goods inventory prior to shipment or transport, then the process ends when the last process prior to loading for shipment or transportation has been completed. Equipment or machinery used to palletize or otherwise prepare the completed produce for shipment or transport, regardless of when it occurs, is not deemed to qualify as capital equipment.

Commentators took issue with this demarcation of when the process ends. Coopers & Lybrand noted that manufacturing companies typically acquire equipment such as strapping machines, stretch film wrappers, palletizers, and lifts to package bulk groups of products for shipment. They thought this equipment should be treated as part of the manufacturing process. Refund Investigators focused on palletizing equipment, pointing out that palletizing occurs in-line and prior to the product being placed into finished goods inventory. The Tax Section argued that the exclusion of palletizing equipment was inconsistent with the statute and that it was part of the packaging process. The Section pointed out that in a different statute (industrial production exemption contained in Minn. Stat. § 297A.25, subd. 9 (1994)), the Department's own rule determined that the taxability of skids and pallets depended on whether they are returnable to the vendor, and if they are returnable, they are treated as industrial production equipment, whereas if they are not returnable, they are not.

In the SONAR, the Department bases its exclusion on the theory that machinery used to handle, transport, palletize or otherwise prepare the completed product for shipment occurs after the integrated production process. The Department notes that packaging of the individual product is considered part of the production process, but that assembly and palletizing of numerous individual products into bulk shipments is not.

The statute at issue here, Minn. Stat. § 297A.01, subd. 16, limits capital equipment to equipment essential to the integrated production process. While the statute explicitly recognizes packaging as a legitimate activity for capital equipment machinery, the Department has drawn the line between placing a package around an individual product and assembling a number of individual products into a convenient unit for shipment, such as a pallet. The Department does have a rational basis for drawing the line where it did, and there is no statutory requirement that requires that the line be drawn somewhere else. Therefore, this portion of the rule is found to have been justified as needed and reasonable.

43. Item C contains the statutory requirement that the machinery or equipment, to qualify for the exemption, must be "essential to the integrated

44. Another of the examples listed deals with environmental control devices. The rule would include environmental control devices that are needed to maintain conditions which “are essential to and are part of the production process”. An example is given of a “clean room” which is “necessary for the manufacture of a product”. However, the rule goes on to exclude environmental control equipment needed to maintain conditions in an area merely to provide for optimum operation of qualifying equipment or machinery, “since such equipment is not essential to the integrated production process”. The Department is drawing a line between environmental control equipment which is necessary as opposed to that which is merely desirable. The Tax Section described this as ambiguous, confusing, and without basis in statute. The Department responds that the statute requires that the equipment maintain conditions which are “essential to” the production process, but excludes devices used in “space heating, lighting, or safety”. Therefore, the Department argues, the concept of “essentialness” is an appropriate part of the rule. The Department did agree to withdraw language denying coverage for items that provided for optimum operation, but it was unwilling to withdraw the entire item. The Administrative Law Judge agrees with the Department’s position because of the statutory language which requires that the devices be used to maintain conditions which are “essential to” the production process. As modified, the rule comports with the statute, and may be adopted.

#### Subpart 4 - Non-qualifying Capital Equipment

45. Subpart 4 identifies equipment or machinery which due to its status as replacement parts or spares; motor vehicles; receiving or storing raw materials; building materials; being used for non-production purposes; and farm, aquaculture, and replacement equipment, does not qualify for the exemption from sales tax for capital equipment.

Grant Thornton and the Aggregate & Ready Mix Association, Hard Drives, Inc., and others objected to the inclusion of the already taxable portion of accessories to motor vehicles in the list of non-qualifying equipment. This is based upon a ready-mix truck, where a mixer is attached to a truck. The

commentators indicate that the mixing units qualify for the exemption independent of the vehicle and should, therefore, be exempt when purchased with the vehicle. The statute specifically excludes “motor vehicles taxed under chapter 297B”. That statute, in turn, taxes both the truck and the ready mix unit if they are purchased together, as a unit, but not if they are purchased separately. Department August 14, 1995 Comment, at 16. The inclusion of motor vehicles is needed and reasonable, and consistent with the statute.

46. Item C identifies “just-in-time inventory control systems” as non-qualifying capital equipment. Unisys objected this treatment and suggested that such a system is part of the integrated production process and should, therefore, be exempt. The Department responded that such equipment is for handling raw materials and the statute specifically excludes such equipment.

Minn. Stat. § 297A.01, subd. 16(d)(3), defines “machinery” as beginning with the “removal of raw materials from inventory.” Excluding “just-in-time inventory control systems” is consistent with the statute. While careful examination of the rule will allow a person to find out what is or is not excluded, the wording of the rule is unnecessarily difficult to understand. The Judge suggests that Item C should be reorganized to better allow persons to understand what is excluded and what is allowed. From the second sentence down to “However,” semicolons and reorganizing fourth sentence will improve the readability of the rule. “However” can be deleted from the fourth sentence and “as capital equipment” can added at the end of that sentence. The fifth sentence can be clarified by deleting the sentence from “Also” to “are” and adding “does not constitute capital equipment” to the end. While the item, as proposed, has been demonstrated to be needed and reasonable, and could be adopted, the clarifications outlined above are recommended.

#### Subpart 5 - Replacement Capital Equipment

47. Replacement capital equipment is subject to taxation, at a sliding rate between four and two percent, to at least June 30, 1998. While it is not as desirable (to the purchaser) as pure capital equipment, it is better than totally non-qualifying equipment, which would be subject to a 6.5% tax. The Department has proposed a rule which explains the Department’s view of a number of items discussed in the statute. It also provides two examples. Both the rule and the examples drew criticism.

Refund Investigators criticized the rule as unnecessary, stating that the statute did not need clarification. The Administrative Law Judge disagrees. Even though the statute is full of terms which have been defined, either in statute or rule, there are still numerous questions which will arise. It is appropriate for the Department to try to answer some of these questions in advance.

48. Refund Investigators also criticized an example where the burden is on the taxpayer to prove that the machinery is used primarily (50% or more) to

produce new products, and asks how the taxpayer would ever be able to prove this fact. Refund Investigators said this was an impossible burden to place on a taxpayer. The Department pointed out that the statute presumes that all gross receipts are subject to the sales tax until the contrary is established. Minn. Stat. § 297A.09. Moreover, the general rule relating to statutory exemptions is that the burden of proof is upon the person claiming the exemption. The Judge finds that the example is needed and reasonable.

49. The Minnesota Society of CPAs suggested that the proposed rule does not treat “back up” equipment as being either qualified capital equipment or replacement equipment. The Department responded that the purpose of “back up” equipment is to replace existing equipment until such time as the original equipment can be placed back into production. The Administrative Law Judge does not understand how that answers the question. For example, if a business determines that it cannot withstand being out of production awaiting the repair of a particular piece of equipment, and therefore, purchases a “back up” machine to keep in reserve and be put into place only if the original machine breaks down, and if it meets all of the other tests, that machine ought to qualify as replacement capital equipment. The Administrative Law Judge does not discern anything in the rule which would deny that treatment, and thus no change needs to be made.

50. MSCPA also requested that if a new machine can perform the same function as an older machine, but yet do it in a manner that is so much more efficient, faster or of higher quality that it bears little or no resemblance to the former equipment, then that new machine ought to be treated as capital equipment, and an example which suggested it would be replacement capital equipment should be modified. The Department disagreed, pointing out that the statute quite clearly included within the definition of “replacement capital equipment” equipment which served fundamentally or essentially the same purpose or function or produced the same or similar end product as did the old equipment, even though it may increase speed, efficiency, or production capacity. If the Society disagrees with this matter, it must prevail upon the Legislature to change the statute, rather than ask the Department to change the rule.

The Department did make two minor changes to rule, at the prompting of the Tax Section and 3M. Neither of the changes are substantial. The Administrative Law Judge concludes that the Department has demonstrated the need for and reasonableness of this proposed rule on replacing capital equipment, and that, with the changes as made by the Department, it can be adopted.

#### Subpart 6 - Local Taxes

51. Some taxpayers pay sales or use tax to a locality as well as to the State. The Department asserts that under local city or county tax programs, a sale is exempt if it is fully exempt from Minnesota sales and use tax. The

proposed rule provides that claims for local taxes “should” be included on the same claim form as the corresponding claim for the state sales tax for purposes of the two-claim per year limitation. While this provision is not totally clear, it is not so vague as to constitute a defect. The Administrative Law Judge recommends, however, that the rule be rewritten so that the third sentence reads as follows:

A claim for a local tax capital equipment refund filed with the state capital equipment refund is deemed to be one claim for the purposes of the two-claim per year limitation.

The remainder of the rule is unobjectionable, and the Administrative Law Judge finds that it has been demonstrated to be both needed and reasonable. The new language would not be a substantial change.

#### Subpart 7 - Leases

52. Leased equipment is eligible for the capital equipment sales tax exemption. Subpart 7 sets out standards for leases to qualify. One standard is for the contract to have a option for re-leasing or purchase by the lessee in order for the re-lease or purchase to qualify for the sales tax exemption. Beckwith, Refund Investigators, and MSCPA urged that re-leases or purchases of leased equipment be allowed for the capital equipment exemption, without regard to whether the original contract allowed it. The Department responded that the normal treatment of such a transaction, absent a prior contract, would be to allow only the replacement capital equipment reduction. The Department believes it is extending the statute as far as it can by treating a clause in a contract allowing the option of re-lease or purchase to validate the treatment of equipment or machinery as exempt capital equipment. To go further would conflict with the statutory obligation to afford only a tax reduction to replacement capital equipment. The Administrative Law Judge agrees.

The only defect in the original rule was the word “generally” in the third sentence. The Department accepted a comment that it be deleted. With “generally” deleted, the rule is needed and reasonable. The new language is not a substantial change.

#### Subpart 8 - Research, Development, and Design

53. The statute, in subdivision 16(b)(2), explicitly includes “machinery and equipment used for research and development, design, quality control, and testing activities” within the definition of “capital equipment”. The proposed rule attempts to clarify under what conditions research, development and design equipment qualifies for either the capital equipment exemption or the replacement capital equipment reduction. The Department takes the position (which the Administrative Law Judge accepts) that this equipment is also subject to the limitations on all other forms of capital equipment, including the basic

limitation that it be used by the purchaser or lessee primarily for manufacturing, fabricating, mining or refining tangible personal property to be sold ultimately at retail. This creates a problem because manufacturers, for example, may engage in general research, as well as specific product-oriented research. Or, they may contract out their research to outside consultants. This contracted research may be either of the general type, or of the product-specific type. These various permutations and combinations do require a rule to explain the applicability of the exemption or reduction.

54. The Department's proposal, however, has problems. The Department did accept a number of suggestions for improvements proposed by IBM, Unisys, the Society of CPAs and the Tax Section. None of those are substantial changes, and all of them do improve the precision of the rule. Nevertheless, a number of defects still remain. The first sentence contains the word "may", used in such a way as to make the sentence be a non-rule. The way the sentence is written, the equipment may qualify, or it may not qualify. This problem continues into the second sentence, which begins with the word "generally", without specifying the limitations imposed by the word. These are defects. The remainder of the first paragraph is fine. The Judge suggests the following language to cure the vagueness defects noted above:

Equipment or machinery used primarily to provide research and development services to a manufacturer, fabricator, miner or refiner for a specific product is eligible for the capital equipment exemption or the replacement capital equipment reduction to the extent that such research and development is essential to the integrated production process of a specific product. Equipment or machinery used for general product development, for another, where no specific product is offered for sale at retail, is not eligible for the capital equipment exemption.

This language cures the vagueness defects and incorporates the change suggested by MSCPA and agreed to by the Department, from "solely" to "primarily." The language as modified is needed and reasonable, and does not constitute a substantial change.

55. After the initial paragraph in subpart 8, the rule lists activities which qualify machinery and equipment for the capital equipment exemption. Item A lists equipment used in research, development, and design as eligible if that equipment meets the definition of "capital equipment" in subpart 3, whether a product is produced or not. The item uses the word "may" to indicate that eligibility is conditional on the equipment meeting the definition. This is a defect. It is unduly vague, since the language suggests that the eligibility condition is not exclusive. To cure it, the Judge suggests replacing "may" with "provided that". Item A, as modified, is needed and reasonable. The new language is not a substantial change.

56. Item B governs exemption eligibility for equipment used in research activities by consultants. Item B uses “may” in the same way as item A and must be changed. The Judge suggests either “qualifies” or “is eligible for” as language to cure the defect. The Department agreed with the suggestion by Unisys to replace “and/or” with simply “or.” The conditions specified in the proposed rule have been demonstrated to be needed and reasonable. The modifications are not a substantial change.

#### Subpart 9 - Mining or Production of Taconite

57. The taconite industry has been singled out for special treatment in the statute. Minn. Stat. § 297A.01, subd. 16, which is the basic capital equipment subdivision, ends with the following paragraph:

- (f) Notwithstanding prior provisions of this subdivision, machinery and equipment purchased or leased to replace machinery and equipment used in the mining or production of taconite shall qualify as capital equipment.

The Department has proposed a rule which provides that equipment which is purchased to replace existing equipment used in the taconite industry qualifies as capital equipment, but that the special treatment does not extend to replacement and repair parts, spare parts, accessories, upgrades, modifications, foundations or special purpose buildings.

Coopers & Lybrand and the Iron Mining Association of Minnesota both challenged the Department’s exclusion of capital equipment treatment for parts, accessories, upgrades, etc. The thrust of their argument is that those items are excluded from the definition of capital equipment by subdivision 16(c), which is part of the subdivision that is negated by the special provisions in the above-quoted subpart (f). The Department responds that the precise wording of the statutory provision at issue extends only to machinery and equipment purchased to replace machinery and equipment, and does not extend to replacement capital equipment, which would include repair and replacement parts, accessories, etc. The Department indicates that at the time that the taconite industry received the exemption for machinery and equipment which replaced existing machinery and equipment, the industry also sought to gain an exemption for repair and replacement parts, but that the Legislature granted the former, but not the latter. While the Department offers no evidence to support this version of the legislative history, it tends to corroborate the language of the statute itself.

The Administrative Law Judge concludes that the proposed subpart does comport with the statute and has been justified as both needed and reasonable. It may be adopted.

Based upon the foregoing Findings of Fact, the Administrative Law Judge makes the following:

### CONCLUSIONS

1. The Minnesota Department of Revenue ("the Department") gave proper notice of this rulemaking hearing.

2. The Department has substantially fulfilled the procedural requirements of Minn. Stat. §§ 14.14, subds. 1, 1a and 14.14, subd. 2 (1992), and all other procedural requirements of law or rule so as to allow it to adopt the proposed rule.

3. The Department has demonstrated its statutory authority to adopt the proposed rule, and has fulfilled all other substantive requirements of law or rule within the meaning of Minn. Stat. §§ 14.05, subd. 1, 14.15, subd. 3, and 14.50 (i) and (ii) (1992), except as noted at Findings 31, 32 and 34.

4. The Department has demonstrated the need for and reasonableness of the proposed rule by an affirmative presentation of facts in the record within the meaning of Minn. Stat. §§ 14.14, subd. 2 and 14.50 (iii) (1992), except as noted at Findings 24, 28, 54, 55 and 56.

5. The additions or amendments to the proposed rule suggested by the Department after publication of the proposed rule in the State Register do not result in rules which are substantially different from the proposed rule as published in the State Register.

6. The Administrative Law Judge has suggested action to correct the defects cited in Conclusions 3 and 4, as noted at Findings 24, 28, 31, 32, 34, 54, 55 and 56.

7. Due to Conclusions 3, 4 and 6, this Report has been referred to the Chief Administrative Law Judge for his approval pursuant to Minn. Stat. § 14.15, subd. 3 (1994).

8. Any Findings which might properly be termed Conclusions are hereby adopted as such.

9. A Finding or Conclusion of need and reasonableness in regard to any particular rule subsection does not preclude and should not discourage the Department from further modification of the proposed rule based upon an examination of the public comments, provided that no substantial change is made from the proposed rule as originally published, and provided that the rule finally adopted is based upon facts appearing in this rule hearing record.

Based upon the foregoing Conclusions, the Administrative Law Judge makes the following:

RECOMMENDATION

IT IS HEREBY RECOMMENDED that the proposed rule be adopted except where otherwise noted above.

Dated this \_\_\_\_\_ day of September, 1995.

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ALLAN W. KLEIN  
Administrative Law Judge

Reported: Taped, No Transcript Prepared