

STATE OF FLORIDA DEPARTMENT OF REVENUE
TALLAHASSEE, FLORIDA

DOR 2013-003 - FOF
FILED

TARGET CORPORATION,

Petitioner,

vs.

FLORIDA DEPARTMENT OF REVENUE,

Respondent.

Department of Revenue – Agency Clerk

Date Filed: March 7, 2013

By: April Warner

DOAH Case Number: 12-2690

Audit Number: 200033531

FINAL ORDER

This cause came before the State of Florida, Department of Revenue (the Department) for the purpose of issuing a Final Order. The Administrative Law Judge assigned by the Division of Administrative Hearings heard this cause and submitted a Recommended Order to the Department. A copy of the Recommended Order, issued on December 7, 2012, by Administrative Law Judge F. Scott Boyd, is attached to this order and incorporated by reference as if fully set forth herein as Exhibit 1. No exceptions to the Recommended Order were filed. The Department has jurisdiction in this cause.

FINDINGS OF FACT

The Department adopts and incorporates in this Final Order the Findings of Fact set forth in the Recommended Order as if fully set forth herein.

CONCLUSIONS OF LAW

The Department adopts and incorporates in this Final Order the Conclusions of Law set forth in the Recommended Order as if fully set forth herein.

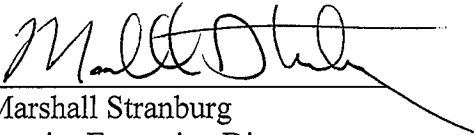
Accordingly, it is ORDERED that the Administrative Law Judge's finding that Petitioner is entitled solely to a refund of use tax on the \$11,658,000.00 portion of the sales price allocated to the design, purchase, and installation of the racking element of the Swisslog contract is adopted.

NOTICE OF RIGHT TO JUDICIAL REVIEW

Any party to this Order has the right to seek judicial review of the Order pursuant to Section 120.68, Florida Statutes, by filing a Notice of Appeal pursuant to Rule 9.110 Florida Rules of Appellate Procedure, with the Agency Clerk of the Department of Revenue in the Office of the General Counsel, P.O. Box 6668, Tallahassee, Florida 32314-6668 [FAX (850) 488-7112], **AND** by filing a **copy** of the Notice of Appeal accompanied by the applicable filing fees with the appropriate District Court of Appeal. **The Notice of Appeal must be filed within 30 days from the date this Order is filed with the Clerk of the Department.**

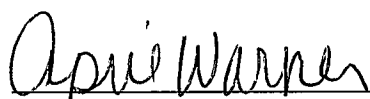
DONE AND ENTERED in Tallahassee, Leon County, Florida this 7th day of March, 2013.

STATE OF FLORIDA
DEPARTMENT OF REVENUE


Marshall Stranburg
Interim Executive Director

CERTIFICATE OF FILING AND SERVICE

I HEREBY CERTIFY that the foregoing FINAL ORDER has been filed in the official records of the Department of Revenue and that a true and correct copy of the Final Order has been furnished by United States mail, both regular first class and certified mail return receipt requested, to Petitioner C/O Scott A. Browdy at Ryan Law Firm, LLP, 22 West Washington, Suite 1500, Chicago, Illinois 60602 this 7th day of March, 2013.



Agency Clerk

Copies furnished to:

F. Scott Boyd
Administrative Law Judge
Division of Administrative Hearings
The DeSoto Building
1230 Apalachee Parkway
Tallahassee, FL 32399-3060

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STATE OF FLORIDA
DIVISION OF ADMINISTRATIVE HEARINGS

TARGET CORPORATION,)
)
 Petitioner,)
)
 vs.) Case No. 12-2690
)
 DEPARTMENT OF REVENUE,)
)
 Respondent.)
 _____)

RECOMMENDED ORDER

Upon joint request, this matter was submitted for Recommended Order upon a Joint Stipulation of Facts and Exhibits, in lieu of hearing, to F. Scott Boyd, an administrative law judge assigned by the Division of Administrative Hearings.

APPEARANCES

For Petitioner: Scott A. Browdy, Qualified Representative
Ryan Law Firm, LLP
22 West Washington, Suite 1500
Chicago, Illinois 60602

For Respondent: John Mika, Esquire
Office of the Attorney General
The Capitol, Plaza Level 01
Tallahassee, Florida 32399

STATEMENT OF THE ISSUE

The issue to be decided is whether Petitioner was making improvements to real property or purchasing tangible personal property when it entered into a contract for the furnishing and

installation of the Swisslog System in its Lake City facility.

PRELIMINARY STATEMENT

The Florida Department of Revenue conducted an audit of Target Corporation's sales and use tax compliance for the period December 1, 2004, through November 30, 2007. A Notice of Proposed Assessment was issued on December 6, 2010. After Petitioner filed a Petition for Redetermination on January 14, 2011, Notice of Decision was issued on or about January 6, 2012.

A Petition under chapter 120 to challenge a Denial of Refund was filed on February 28, 2012. The Petition was referred to the Division of Administrative Hearings on March 28, 2012. An Order Closing File and Relinquishing Jurisdiction was entered on May 22, 2012, for the purpose of furthering informal discovery and settlement discussions, based upon the parties' joint request. A Joint Motion to Reopen File was filed on June 22, 2012. The file was re-opened with the same case number, and was set for hearing on November 14, 2012. Pursuant to joint request, the parties were permitted to file a joint stipulation of facts and separate proposed recommended orders in lieu of hearing, the parties agreeing upon all facts except for certain ultimate facts to be derived from stipulated facts.

The parties timely filed Proposed Recommended Orders on October 15, 2012. An Order Granting Joint Motion to Supplement Record and File Replies to Proposed Recommended Orders was

granted on October 15, 2012. The parties filed replies to each other's Proposed Recommended Order on October 25, 2012. The Proposed Recommended Orders and Replies were considered in the preparation of this Recommended Order.

FINDINGS OF FACT

1. Respondent conducted an audit of Petitioner's sales and use tax compliance for the period December 1, 2004, through November 30, 2007 (the "Refund Period").

2. Petitioner presented refund schedules to Respondent requesting a refund of \$2,179,484.84 in sales and use tax accrued and remitted on the design and construction of a perishable-food storage and handling system.

3. Respondent issued a Notice of Proposed Assessment denying the requested refund on December 6, 2010.

4. Petitioner timely filed a Petition for Redetermination on January 14, 2011, which ultimately resulted in a Notice of Decision upholding Respondent's December 6, 2010, denial of Petitioner's requested refund.

5. Petitioner timely filed a Formal Protest on February 28, 2012, challenging the Notice of Decision. The Protest was referred to the Division of Administrative Hearings to conduct a section 120.57 hearing.

6. Petitioner is a national retailer of discounted, high-quality general merchandise and grocery products.

7. Petitioner owns and operates over 120 stores in Florida.

8. Over the past ten years, Petitioner has been increasing the number and quality of grocery offerings in its stores. Petitioner constructed new perishable-food distribution centers to support its grocery operations.

9. Petitioner has built a 420,000 square-foot Dedicated Perishable-Food Distribution Center ("Distribution Center") in Lake City, Florida.

10. The Distribution Center supplies Petitioner's grocery operations in the Southeastern United States.

11. Petitioner entered into two separate contracts with two different contractors relating to the construction and equipping of the Distribution Center.

12. One contract, between Petitioner and Ryan Corporation, for approximately \$60 million, was for construction of a building (the "Building"). The second contract, between Target Corporation and Swiss-Log, for approximately \$40 million, was for the material handling and distribution system inside the Building (the "Swisslog System").

13. The Swisslog System functions as an automated system for storing, inventorying, and distributing approximately 8,000 different items of perishable food products. The two

contractors and Petitioner worked together on the planning and design of the Building to accommodate the Swisslog System.

14. The Building has 34 receiving docks and 38 shipping docks. The docks are connected by conveyors that run throughout the Building. The Building was designed to take into consideration the conveyors, lifts, cranes, and "Caddy Picks" of the Swisslog System. The Swisslog System is physically attached to the Building, intended to be a permanent addition, and required for the facility to serve its intended purpose.

15. The Distribution Center has five major storage areas. They are:

- a. 83,000 sq. ft. freezer chamber
- b. 73,000 sq. ft. cooler chamber
- c. 57,000 sq. ft. dry produce area
- d. 8,500 sq. ft. meat area
- e. 8,600 sq. ft. wet produce area.

16. The contract with Swisslog was for the design, purchase, and installation of the entire integrated material handling and distribution system. The system included conveyors, cranes, de-pallet equipment, Caddy Picks, shelving, and the software and hardware to operate the warehouse management and distribution system's equipment and machinery to move food from the receiving docks to the designated storage areas and then to the appropriate shipping docks.

17. The Distribution Center's general contractor hired several sub-contractors and suppliers to erect the Building and install the Swisslog System. The vast majority of the Swisslog System and its racking is attached to the floor or walls of the Building, or moves along tracks in the floor, or hangs from I-beams in the ceiling. The Building, including the cold and frozen temperature chambers, was designed and constructed to the specifications of the Swisslog System. During construction, the walls of the Building were not enclosed until the framework for the Swisslog System was complete.

18. The freezer section of the Swisslog System is over 68 feet tall and 261 feet long. This section contains two floors and 25,040 merchandise "slots." The cooler section is 53 feet tall and 261 feet long. The cooler section contains two floors and 12,720 merchandise slots.

19. The building that envelops the Swisslog System contains approximately 1,800 tons of structural steel.

20. The Swisslog System's racking component includes 3,000 tons of steel.

21. The Swisslog System has its own set of fixtures, including lighting fixtures and components, a fire protection sprinkler system consisting of piping and sprinkler heads, and an electrical system.

22. To accommodate the Swisslog System, the Building foundation contains increased steel reinforcement and footing depths necessary to support the Swisslog System's weight and design loads. In addition, the foundation contains 24" deep pits in certain areas to support the weight and design height the Swisslog System's pallet jack inducts.

23. Petitioner paid use tax on the entire contract price for the Swisslog System contract.

24. Petitioner records the Swisslog System as tangible personal property on its ad valorem returns filed with Lake County, Florida.

25. For federal tax purposes, Petitioner depreciates the Swisslog System as (***) year property, under the Modified Accelerated Cost Recovery System.

26. Attached and incorporated into the Joint Stipulation of Facts was a brochure produced by *Accalon*, which further describes the Swisslog System. The brochure is a fair and accurate representation of the Swisslog System installed at the Distribution Center.

27. The following is a general description of how the distribution system works, and the method of its attachment and incorporation into the Building:

Order Receiving

a. Employees, driving forklifts, unload pallets from the semi tractor trailers at the receiving docks.

b. The pallets are then label-scanned into the Work Management System (WMS) and the pallet moves to a pallet de-layering station. The WMS processes data and issues instructions, so that most of the steps necessary to move merchandise within the Swisslog System are automated.

c. If the pallets require de-layering, the pallets are de-layered and the cases from the pallet are loaded onto a split tray and travel by conveyor to the SRM aisle and pick up station.

d. Freezer load units are transferred in to the freezer chamber on conveyors that drive the loads through and cause the automated air-door on the refrigerated chambers to open.

e. Once in the freezer or cooler chambers, one of the 16 automated cranes will pick up the pallets from the conveyors.

f. These cranes, several stories tall and traveling on railroad-like tracks mounted to the floor, will travel down the aisles behind the racks to the appropriate storage rack locations, where the crane will lift the pallet and slide the pallet into the storage rack.

g. Like the crane, the 75-foot tall storage racks are physically bolted to the building's floor or walls.

h. The pallet-size conveyors are bolted to the floor or walls of the facility.

i. Pallets are stored in specific locations using WMS logic.

Order Picking

j. The WMS receives orders from the store and groups the orders, allocates, and releases batches of orders for efficient pickup.

k. During allocation, the WMS separates full-pallet picks from partial picks.

l. The WMS virtually guides pallets from individual store orders based on cubic volume of the quantity of cases selected.

m. The WMS maps the picking locations for the Caddy Picks and allocates orders for the Caddy Picks.

n. There are 70 Caddy Picks in the aisles in front of the racks. Each Caddy Pick may carry up to 2,800 pounds of merchandise.

o. The Caddy Picks hang from ceiling I-beams and travel down the aisles to pick containers and boxes from pallets on the racks and load onto outgoing pallets.

p. An employee is required to follow the Caddy Pick as it travels down the aisles and manually pick the containers and boxes and load onto the outgoing pallets.

q. This picking process will continue until the outgoing order of mixed products is fulfilled.

r. These pallets are then transferred via conveyors and lifts (mechanical elevators) to ground level where the pallets are wrapped in shrink wrap on the conveyor.

s. The pallets are then conveyed to a double-shuttle car interface station where the pallet is transferred to the double shuttle, also mounted to the floor.

t. This car can carry two pallets simultaneously and transfer them to allocated conveyor shipping lanes.

u. Employees driving forklifts pick up the pallets from the conveyor shipping lanes and load them into the semi-tractor trailers parked in the shipping docks.

v. The entire process (excepting where human interaction is required) is performed by the WMS, and automated computer and software system.

w. The system reads bar code labels on the pallets and determines where incoming inventory should be stored, manages store re-supply orders, determines product pulls to optimize time resources and pallet configuration, and determines which shipping dock the pallet of inventory being pulled should be routed to.

28. Mr. Scott Browdy had the necessary qualifications to responsibly represent Petitioner's interests in a manner which

would not impair the fairness of the proceeding or the correctness of the action to be taken.

29. The parties filed a package of electronic documents that was agreed to be a true copy of the December 7, 2006, contract between Petitioner and Swisslog Logistics, Incorporated.

30. The term "System" was described in the contract as "all Plant to be provided and the installation services or other work to be done by the Contractor or any permitted Subcontractors under the Contract, which shall include delivery, installation, testing and commissioning of an order fulfillment system with all required software, hardware, racking, mezzanines, conveyors, cranes, Caddy Picks as specified in the Specifications."

31. The contract did not specifically describe and itemize each item of tangible personal property to be provided. However, in the "Investment Summary," which was originally a December 5, 2006, proposal from Swisslog to Petitioner, that was part of the package of electronic documents that was agreed to be a "true copy" of the December 7, 2006, contract, the various elements of the contract were priced. Racking was priced at \$11,658,000.00, the warehouse management system was priced at \$2,441,000.00, and project and implementation services were priced at \$2,691,000.00. The stacker cranes, pallet conveyors,

and Caddy Picks for the cooler and freezer were priced at a total of \$22,656,000.00. The prices for all of these elements totaled \$39,446,000.00, which was the price of the final contract when executed.

32. The contract did not charge Petitioner for items of tangible personal property as they were delivered, but charged the lump sum amount of \$39,446,000.00 for all services, tangible personal property, and improvements to real estate. It provided for various percentages of this total contract price to be paid at certain milestone events leading toward the completion of the contract.

33. The Swisslog contract was a mixed contract providing for sale of tangible personal property such as perishable food transport and handling equipment; improvements to real property such as permanent storage racks; electrical, computer control, and plumbing components which were not described sufficiently in the contract to classify; and project and implementation services, which were not associated in the contract with either improvements to real property or sale of tangible personal property.

34. The contract clearly allocated the contract price among these various elements of the contract. It indicated that \$11,658,000.00 was allocated for the permanent storage racks. This allocation was bona fide and reasonable in terms of their

great size and the large amount of steel used in their construction.

35. The permanent storage racks installed as part of the Swisslog System were not industrial machinery or equipment but were instead improvements to real property.

36. Petitioner failed to prove which, if any, of the remaining elements of the contract were improvements to real property. It was unclear if any of the electrical, computer, or plumbing components were integrated into the Building's systems, or which services related to the improvement to real property.

CONCLUSIONS OF LAW

37. The Division of Administrative Hearings has jurisdiction over the subject matter and the parties in this case pursuant to sections 72.011(1), 120.569, 120.57(1), and 120.80(14), Florida Statutes (2012).

38. Section 120.80(14)(b)3.b. provides that the requirement of section 72.011(2) that an action contesting denial of refund may not be filed in circuit court more than 60 days after a final decision is equally applicable to administrative proceedings and is "jurisdictional."

39. Section 72.011(2)(b)1. requires the Department of Revenue to adopt a rule establishing the date on which a denial of refund becomes final.

40. Florida Administrative Code Rule 12-6.003(3)(b) provides that if the taxpayer does not file a petition for reconsideration, the Notice of Decision regarding a denial of refund becomes final on the date it is issued. The Notice of Decision here was issued on January 6, 2012. Petitioner timely filed its Formal Protest in Response to Notice of Decision on March 2, 2012.

41. The request of Petitioner in the Notice of Appearance filed on May 14, 2012, that Mr. Scott Browdy be authorized to represent Petitioner in this matter is approved. Mr. Browdy is a qualified representative.

42. Pursuant to section 120.80(14)(b) 2., Respondent's burden of proof in a taxpayer contest proceeding is limited to a showing (1) that an assessment was made against the taxpayer; and (2) the factual and legal grounds for making that assessment. Once Respondent has met this initial burden of proof, the burden then shifts to Petitioner to demonstrate by a preponderance of evidence that the denial of refund was incorrect. IPC Sports v. Dep't of Rev., 829 So. 2d 330, 332 (Fla. 3rd DCA 2002). See also Dep't of Rev. v. Nu-Life Health and Fitness Ctr., 623 So. 2d 747, 751-52 (Fla. 1st DCA 1992).

43. Any ambiguities or doubts in the interpretation of the statute are to be resolved in favor of the taxpayer, however. Taxes may be collected only within the clear definite boundaries

recited by the statute. Maas Bros., Inc. v. Dickinson, 195 So. 2d 193 (Fla. 1967); Dep't of Rev. v. Ray Constr., 667 So. 2d 859, 865 (Fla. 1st DCA 1996).

44. Section 212.05, Florida Statutes, has provided in pertinent part throughout the Refund Period:^{1/}

It is hereby declared to be the legislative intent that every person is exercising a taxable privilege who engages in the business of selling tangible personal property at retail in this state, including the business of making mail order sales, or who rents or furnishes any of the things or services taxable under this chapter, or who stores for use or consumption in this state any item or article of tangible personal property as defined herein and who leases or rents such property within the state.

(1) For the exercise of such privilege, a tax is levied on each taxable transaction or incident, which tax is due and payable as follows:

* * *

(b) At the rate of 6 percent of the cost price of each item or article of tangible personal property when the same is not sold but is used, consumed, distributed, or stored for use or consumption in this state
. . . .

45. Under section 212.06(13), the activities of altering or improving real property is considered an "improvement to real property." An improvement to real property is not a sale of tangible personal property subject to use tax.

46. The issue here is whether the contract for the furnishing and installation of the Swisslog System in the Lake City facility was an improvement to real property, and so not subject to use tax, or a purchase of tangible personal property taxable under the above statute. The question of whether property is personal property or a fixture is a question of fact for determination by the trier of fact. Sears v. Bay Bank & Trust Co., 537 So. 2d 1041, 1042 (Fla. 1st DCA 1989).

47. Petitioner's argument that the Swisslog System constitutes an improvement to real property seems well supported by common law cases involving the transfer of property. In 1929, Justice Ellis of the Florida Supreme Court cited to English land law, itself citing still more ancient authority: "According to Lord Chancellor Hardwicke, 'in the old cases they go a great way upon the annexation to the freehold, and so long ago as Henry the Seventh's time the courts of law construed even a copper and furnace to be part of the freehold.'" Comm. Fin. Co. v. Brooksville Hotel Co., 98 Fla. 410 (Fla. 1929) (citing 8 Am. and Eng. Ency. Law, p. 42, note). Justice Ellis went on to describe three criteria which the courts have generally applied: actual annexation to the realty or something appurtenant thereto; second, appropriateness to the use or purpose of that part of the realty with which it is connected; and third, the

intention of the party making the annexation that it shall be a permanent accession to the freehold. Brooksville Hotel at 415.

48. Similar criteria have been utilized in tort cases involving product liability. The issue arises because Florida courts impose principles of strict liability with respect to "products" as personal property but not when structural improvements to real property are involved. A case cited by Petitioner, Plaza v. Fisher Development, Inc., 971 So. 2d 918 (Fla. 3d DCA 2007), is one of these. In that case, the court, after an extensive review of cases from Florida, other states, and several Federal Circuits, concluded that the conveyor at issue was a structural improvement to real property. The court noted specifically that the conveyor system was installed when the store was first constructed, that its purpose was to move merchandise from one part of the property to another, and that the system was affixed to the building. Petitioner correctly notes that all of these factors also are present in the instant case.

49. Tax law is statutory, however. To the extent a statute uses terms such as "improvement to real property" and "fixture" without elaboration, these traditional common law definitions would be very persuasive because the Legislature is presumed to be aware of such constructions. However, if the statute deviates from common interpretations, the statutory

language must control. Baskerville-Donovan Eng'rs v. Pensacola Exec. House Condo. Ass'n, 581 So. 2d 1301, 1303 (Fla. 1991) (courts may presume Legislature has specified any innovation to common law).

50. The language of the tax statute therefore guides the inquiry here. Throughout the Refund Period, section 212.06(14) provided in relevant part:

For the purpose of determining whether a person is improving real property, the term:

(a) "Real property" means the land and improvements thereto and fixtures and is synonymous with the terms "realty" and "real estate."

(b) "Fixtures" means items that are an accessory to a building, other structure, or land and that do not lose their identity as accessories when installed but that do become permanently attached to realty. However, the term does not include the following items, whether or not such items are attached to real property in a permanent manner: . . . industrial machinery or equipment. For purposes of this paragraph, industrial machinery or equipment is not limited to machinery and equipment used to manufacture, process, compound, or produce tangible personal property.

51. The statute thus invokes traditional definitions to an extent, but specifically modifies these definitions by providing that "industrial machinery and equipment" is not to be considered as a fixture to real estate, regardless of whether it is attached to real property in a permanent manner.

52. Petitioner argues that even if the Swisslog System is found not to be a fixture because it is industrial machinery or equipment, it might otherwise be an improvement to real estate. This contention is rejected. Legislative modification of the common law definition of "fixture" by the exclusion of industrial machinery and equipment evinces a clear intent that such tangible personal property not be considered an improvement to real property for purposes of the Tax Code. The statute cannot reasonably be construed contrary to this intent to find that industrial machinery and equipment, though not a fixture, is nevertheless still an improvement to real property. Such an interpretation would be absurd and undermine the very purpose of the statutory modification. Fla. Dep't of High. Saf. & Motor Veh. v. Hernandez, 74 So. 3d 1070, 1079 (Fla. 2011) (statutes not to be interpreted so as to yield absurd result). If the Swisslog System is "industrial machinery or equipment" then, it is not an improvement to real estate under the statute.

53. The Department of Revenue has been granted rulemaking authority in section 212.17(6), which provides, "The department has authority to adopt rules pursuant to ss. 120.536(1) and 120.54 to enforce the provisions of this chapter."

54. Pursuant to this authority DOR has adopted a rule entitled "Sales to or by Contractors Who Repair, Alter, Improve

and Construct Real Property." Rule 12A-1.051(2)(e) provides in relevant part:

1. "Machinery or equipment" means and includes property that:

a. Is intended to be used in manufacturing, producing, compounding, processing, fabricating, packaging, moving, or otherwise handling personal property for sale or other commercial use, in the performance of commercial services, or for other purposes not related to a building or other fixed real property improvement; and

b. May, on account of its nature, be attached to the real property but which does not lose its identity as a particular piece of machinery or equipment.

2. "Machinery or equipment" generally does not include junction boxes, switches, conduits, wiring, valves, pipes, and tubing incorporated into the electrical, cabling, plumbing, or other structural systems of fixed works, buildings, or other structures, whether or not such items are used solely or partially in connection with the operation of machinery and equipment.

3. "Machinery or equipment" serves a particular commercial activity that is carried on at a location rather than serving general uses of land or a structure. Examples of machinery or equipment include conveyor systems, printing presses, drill presses, or lathes. Examples of items that are not machinery or equipment because they are integrated into the structure or realty and retain their usefulness no matter what activity is carried on at the site include heating and air conditioning system components or water heaters. Any property that would be classified as machinery or equipment under Section 212.08(5), F.S., or any other provision of Chapter 212, F.S., is

considered to be machinery or equipment for purposes of this rule. In the case of property used in the production of electrical or steam energy, any item that would qualify as exempt machinery or equipment under Section 212.08(5)(c), F.S., is considered to be machinery or equipment for purposes of this rule.

55. In reviewing the statutory definition, it should be initially noted that there was no suggestion that the Swisslog System could be classified as the machinery or equipment that is described in section 212.08(5), which relates to machinery or equipment used to increase productive output, in production of electrical or steam energy, or under federal procurement contract.

56. It was stipulated that the Swisslog System functions as an automated system for storing, inventorying, and distributing perishable food products. Several different elements are identified in the contract. Racking was to be erected in the storage areas; stacker cranes, conveyors, Caddy Picks, and other equipment to move the food was to be constructed; a Warehouse Management System was to be installed to automate control of the operations; and project and implementation services were to be provided. Each of these elements of the contract will be considered in light of the applicable statute and rule.

Storage Racking

57. The Distribution Center has five large storage areas, including areas for wet produce, dry produce, a meat area, and cooler and freezer chambers. The Swisslog System includes 3,000 tons of steel racking with merchandise "slots" for food storage in these areas. The 75-foot tall storage racks are physically bolted to the Building's floor and walls. The Building foundation contains increased steel reinforcement and footing depths necessary to support the Swisslog System's weight and design loads. It was stipulated that the Swisslog System is physically attached to the Building, intended to be a permanent addition, and is required for the facility to serve its intended purpose. If this permanently attached steel racking does not come under the statutory exclusion of machinery and equipment, it is clearly a fixture and is an improvement to real property. Cf. Plaza v. Fisher Dev., Inc., 971 So. 2d 918 (Fla. 3d DCA 2007) (conveyor system installed as initial construction to move merchandise around building and permanently affixed was improvement to real property in liability case).

58. The rule definition of "machinery and equipment" includes any equipment "intended to be used in manufacturing, producing, compounding, processing, fabricating, packaging, moving, or otherwise handling personal property for sale or other commercial use." This description does not by its terms

include mere storage structures, which do not move, handle, or otherwise perform any action on property for sale. Permanent storage racks are not industrial machinery or equipment within the plain language of the statute or the rule definition. Extension of the rule language beyond the clear definite boundaries of the statute to also encompass storage areas, shelving, or racks which serve the general uses of land or a building is not warranted. A taxing statute should always be construed in the light most favorable to the taxpayer. Mikos v. Ringling Bros.-Barnum & Bailey Combined Shows, 497 So. 2d 630, 632 (Fla. 1986). Any doubt should be resolved in the taxpayer's favor. Fla. Hi-Lift v. Dep't of Rev., 571 So. 2d 1364, 1368 (Fla. 1st DCA 1990).

59. This interpretation is consistent with Respondent's treatment of similar permanently-fixed storage structures as improvements to real property serving the general uses of land or a building, and not as industrial machinery or equipment. T.A.A. 8A-029 Sales and Use Tax - Refrigeration Equipment, 2008 Fla. Tax LEXIS 51, 3-4 (Fla. Tax 2008) ("refrigeration equipment when installed will become a part of realty"); T.A.A. 1A-060 Food Service Equipment Installation, 2001 Fla. Tax LEXIS 104, 24-25 (Fla. Tax 2001) (stainless steel wall shelves to be permanently attached in lounge were real property improvements, although predominate nature of mixed contact was sale of

tangible personal property); T.A.A. 97A-037 Real Property v. Tangible Personal Property, 1997 Fla. Tax LEXIS 67, 3 (Fla. Tax 1997) (underground fuel storage tanks and pumps connected to them are improvements to real property).

60. Conversely, if the storage racks had not been permanently fixed to the real property, they would remain tangible personal property. Pamperin v. Interlake Cos., 634 So. 2d 1137, 1140 (Fla. 1st DCA 1994) (storage rack system that could be disassembled and resold was not a permanent fixture).

Warehouse Management System

61. The Swisslog System is an integrated material handling and distribution system. It includes a Warehouse Management System that tracks which food products are stored in what locations and issues instructions to automatically move these products. It controls the movement of food products from the receiving docks to the designated storage areas, and subsequently, the movement of selected food products from the storage areas to appropriate shipping docks.

62. Under rule 12A-1.051(2)(e)2., quoted above, switches, wiring, valves, pipes, and tubing incorporated into the structural systems of a building do not constitute "machinery and equipment" under the statute, whether or not such items are used solely or partially in connection with the operation of machinery and equipment. However, Petitioner presented no

evidence to indicate the extent to which computer control components or electrical components were in fact incorporated or integrated into the structural systems of the Building. In light of Petitioner's failure to meet its burden, the Warehouse Management System element would therefore have to be considered as tangible personal property.

Project and Implementation Services

63. The contract also included various project and implementation services. Section 212.06(1)(a) provides that sales and use tax is levied at the rate of six percent of the sales price. The term "sales price" is defined in section 212.02(16) to include the amount paid for tangible personal property, including any services that are part of the sale.

64. Installation services related to the performance of a real property improvement contract are not taxable. Fla. Admin. Code R. 12A-1.016(3)(a). Again, however, no evidence was presented to indicate the value of services, if any, associated with improvements to real property. In light of Petitioner's failure to meet its burden, the project and implementation services would have to be considered associated with the sale of tangible personal property.

Distribution

65. The primary function of the Swisslog System is to automatically distribute perishable food products from receiving

docks to appropriate storage areas and ultimately to shipping docks. It utilizes a series of conveyors, lifts, cranes, depalleting equipment, Caddy Picks, and shuttle cars to accomplish this task. The vast majority of this elaborate distribution equipment is permanently attached to the floor, walls, or ceiling of the building. If this permanently attached distribution system does not come under the statutory exclusion for machinery and equipment, it is a fixture and is clearly an improvement to real property. Plaza v. Fisher Dev., Inc., 971 So. 2d 918 (Fla. 3d DCA 2007) (conveyor system installed as initial construction to move merchandise around building and permanently affixed was improvement to real property in liability case).

66. As noted earlier, the statute does not limit industrial machinery or equipment only to actual manufacturing equipment, and the rule clarifies that equipment to "move" or "handle" personal property for sale is also included within the definition. Fla. Admin. Code R. 12A-1.051(2)(e)1.a. If considered separately, the cranes, conveyors, Caddy Picks and other equipment which move perishable food would, therefore, not be fixtures, but would be industrial machinery and equipment, and so tangible personal property.

67. The various elements of the Swisslog System were not contracted for separately, however, but were furnished under a

single contract. The Swisslog System contract was thus a mixed contract, containing elements of a real property contract as well as elements of a sale of tangible personal property. Rule 12A-1.051(8).

68. The determination as to the taxability of a mixed contract is normally based on the predominant nature of the contract. If the predominant nature of the contract is that of a real property improvement contract, then the entire contract will be taxed as a real property improvement. Likewise, if the predominant nature of the contract is that of a sale of tangible personal property, then the entire contract will be taxed as a sale of tangible personal property. Fla. Admin. Code R. 12A-1.051(8). The Swisslog contract predominantly involves industrial machinery and equipment, and so is a contract for the sale of tangible personal property.

69. However, rule 12A-1.051(8)(d) also provides in relevant part:

(d) If a mixed contract clearly allocates the contract price among the various elements of the contract, and such allocation is bona fide and reasonable in terms of the costs of materials and nature of the work to be performed, taxation will be in accordance with the allocation.

70. On its face, the Investment Summary appears to be part of a negotiating proposal from Swisslog, to be considered only as Swisslog's explanation of how it arrived at its proposed

price, not an actual part of the contract. However, it was submitted as a part of the package of electronic documents that the parties formally agreed was a "true copy" of the December 7, 2006, contract. This critical agreement of the parties is accepted. Sapp v. Berman Bros., 884 So. 2d 1080, 1081-1082 (Fla. 1st DCA 2004) (unrefuted stipulation should be followed unless there is a showing of fraud, overreaching, or misrepresentation).

71. The Investment Summary, and hence the contract, clearly allocated the contract price among the various elements of the contract. Racking was priced at \$11,658,000.00, the warehouse management system was priced at \$2,441,000.00, and project and implementation services were priced at \$2,691,000.00. The stacker cranes, pallet conveyors, and Caddy Picks for the cooler and freezer were priced at a total of \$22,656,000.00. The prices for all of these elements totaled \$39,446,000.00, which was the price of the final contract when executed.

72. The \$11,658,000.00 contract price allocated to the racking is bona fide and reasonable in terms of the costs of materials and nature of the work to be performed.

73. Section 212.06(14), Florida Statutes, sets clear and definite boundaries subjecting industrial machinery and equipment to sales and use taxation.

74. Respondent showed that it made an assessment of use tax against Petitioner for the full sales price of the Swisslog System because it constituted industrial machinery and equipment and, therefore, was a sale of tangible personal property, not an improvement to real property.

75. Petitioner proved by a preponderance of evidence that the Swisslog contract was a mixed contract and that the racking element was not industrial machinery or equipment, but was an improvement to real property. The contract clearly allocated \$11,658,000.00 to the racking element.

76. Petitioner failed to prove by a preponderance of evidence that any other elements of the Swisslog System installed in the Lake City facility constituted an improvement to real property or otherwise did not come within the definition of tangible personal property subject to taxation.

RECOMMENDATION

Upon consideration of the above findings of fact and conclusions of law, it is

RECOMMENDED that the Department of Revenue enter a final order: (1) finding that Target Corporation is entitled to a refund of use tax on the \$11,658,000.00 portion of the sales price allocated to the design, purchase, and installation of the racking element of the Swisslog contract; and (2) otherwise denying refund.

DONE AND ENTERED this 7th day of December, 2012, in
Tallahassee, Leon County, Florida.

F. Scott Boyd

F. SCOTT BOYD
Administrative Law Judge
Division of Administrative Hearings
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Filed with the Clerk of the
Division of Administrative Hearings
this 7th day of December, 2012.

ENDNOTE

^{1/} Citation to statutes and administrative rules, except as
otherwise indicated, are to the versions in effect at the time
of the contract.

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NOTICE OF RIGHT TO SUBMIT EXCEPTIONS

All parties have the right to submit written exceptions within 15 days from the date of this Recommended Order. Any exceptions to this Recommended Order should be filed with the agency that will issue the Final Order in this case.