



Explanation of Industrial Development Bond Manufacturing Definition Provision

The Technical and Miscellaneous Revenue Bond Act of 1988 (TAMRA) added the term “manufacturing facility” to Section 144 of the Internal Revenue Code of 1986, as amended (the “Code”). The term focuses only on the manufacture of tangible products, and does not clearly include the development or production of products in a knowledge-based economy (e.g., computer software and intellectual property associated with the bio-tech and pharmaceutical industries). **The proposed language would broaden the definition of “manufacturing” to include the creation of intangible property, specifically, patents, copyrights, formulas, processes, designs, patterns, know-how, format, or other similar items**, as set forth in section 197(d)(1)(C)(iii) of the Code.

Language has also been added to clarify that a “manufacturing” facility includes “functionally related and subordinate facilities,” and to differentiate between the phrases “functionally related and subordinate facilities” and “directly related and ancillary facilities.” The inclusion of “functionally related and subordinate facilities” as part of a facility is similar to a long-standing regulatory standard used since 1972 in the area of tax-exempt bonds for exempt facilities. See Treas. Reg. § 1.103-8(a)(3). To qualify under this standard, functionally related and subordinate facilities generally must be of a character and size commensurate with the primary manufacturing facility. The House Report on TAMRA states that activities that are subordinate to the manufacturing process, such as short-term warehousing of raw materials, temporary warehousing of finished products, and labs for testing raw materials, are all integral to the manufacturing process and therefore not subject to the 25% limitation. H. Rep. No 100-795. Directly related and ancillary facilities, on the other hand, are activities carried on at the facility that are not integral to the manufacturing process. They are activities that, as the statute provides, are directly related to manufacturing, but are, as the dictionary provides, secondary, supplementary or extra. These activities are not so necessary to the actual manufacturing process that they would in all cases be located in the plant. Unfortunately, the Conference Report on TAMRA, Con. Rep. No. 100-1104, p. 2004, and subsequent Internal Revenue Service private letter rulings, have combined these two phrases, thus blurring the distinction between “functionally related and subordinate” and “directly related and ancillary.”