Cite as Det. No. 13 WTD 138 (1993).

BEFORE THE INTERPRETATION AND APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of Assessment of	)	F I N A L D E T E R M I N A T I O N
	)	No. 92-249ER
. . .	)	Registration No. . . .
	)	REAL ESTATE EXCISE TAX
	)	No. . . .

[1] RCW 82.45.010, WAC 459-61-660, and ETB 541.04/45/33.135: REAL ESTATE EXCISE TAX -- SALES OF STANDING TIMBER -- WHAT CONSTITUTES. A stumpage contract found to be a sale of standing timber and subject to the real estate excise tax where the agreement provided: (1) description of timber to be cut and removed; (2) the unit price and terms of payment; (3) purchaser assumed risk of loss for the timber; and (4) purchaser was to sign DNR Forest Practices Application as "Timber Owner."

This headnote is provided as a convenience for the reader and is not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

TAXPAYER REPRESENTED BY: . . .

DATE OF TELEPHONE CONFERENCE: . . .

NATURE OF ACTION:

The taxpayer petitioned for executive level reconsideration of Determination 92-249 with respect to the finding a "stumpage contract" was a contract for the sale of timber and subject to the real estate excise tax.

FACTS AND ISSUES:

Roys, Sr. A.L.J. -- [The taxpayer] is a limited partnership which owns forest land . . . . The taxpayer entered into a stumpage

contract with . . . [purchaser]. The Department's Miscellaneous Tax Division reviewed the contract and determined that it conveyed the ownership of standing timber to the purchaser. The Department assessed real estate excise tax on the gross sales price.

The taxpayer petitioned for a correction of the assessment. The taxpayer contended title to the logs did not pass until payment, and, therefore, the contract was not a sale of "standing timber" and not subject to the REET.

Determination 92-249 sustained the assessment. The decision set forth the facts relating to the contract at issue as follows:

1. The contract was described as a "stumpage contract."
2. The taxpayer desired to sell the timber and the contractor-buyer desired to purchase the timber.
3. The contractor-buyer was to pay the taxpayer stumpage based on the amount of timber harvested.
4. Payment for the timber was to be made within 10 days of receipt of a scale certificate or twenty days of scaling whichever was the earlier. The price to be paid was determined by the type of tree and the quantity per a schedule attached to the contract.
5. All logs were to be branded and tagged with the taxpayer's brand prior to leaving the property. The brands and tags were to remain on the logs until payment was made to the taxpayer.
6. The taxpayer retained an "economic interest" in the logs until the payment was made.
7. The contractor-buyer assumed all risk of loss of the timber and timber products.
8. The contractor-buyer provided the taxpayer with a cash deposit in the amount of $200,000.
9. The contractor-buyer granted to the taxpayer "a security interest in all of the timber which was cut or harvested by the [contractor-buyer] under this contract."
10. If, at the end of the contract period, there had been timber remaining on the property, the taxpayer would have received damages and the right to sell the remaining timber to third parties.
11. The contract was cancelable only for cause.
12. The contractor-buyer was obligated to pay any Washington State timber tax as the "harvester."

In sustaining the assessment, the administrative law judge relied, in part, on the following:

1) The contract is entitled "Stumpage Contract." ETB 541 states that the terms "standing timber" and "stumpage" are synonymous. The contractor-buyer is referred to as the "purchaser" who "shall pay stumpage to" the taxpayer.

2) The purchaser bore the risk of loss.

3) The purchaser was entitled to the gross proceeds from the eventual sale of the harvested timber and bore the risk that timber prices would fluctuate.

The Determination concluded that requiring the purchaser to brand the logs with the taxpayer's brand was to create a security interest only.

The taxpayer petitioned for reconsideration of the Determination. The taxpayer contends the Administrative Law Judge (1) relied on two administrative rules--WAC 458-40-620 and WAC 458-61-660(3)--that are invalid, (2) relied on aspects of the transaction that have no legal significance, and (3) ignored the evidence and legal arguments that demonstrate the parties' intent to pass title to the timber after severance.

In its petition for reconsideration the taxpayer stated the central question was "whether, under the specific terms of this contract, [the purchaser] acquired title to or ownership of the timber before it was cut." . . . .

DISCUSSION:

For purposes of the real estate excise tax, a "sale" includes the transfer of the ownership of or title to real property, including standing timber. RCW 82.45.010. Persons who harvest timber are required to obtain a Forest Practice Application (cutting permit) from the Department of Natural Resources. This document is used by the Department's Forest Tax Division to identify and register harvesters for payment of the Timber Excise Tax. The cutting permit is also the primary source for determining tax liabilities of the landowner and the timber owner.

If the landowner and the timber owner are the same, the transaction is assumed to be a sale of logs and subject to the B&O tax. If the landowner is different from the timber owner, the Department assumes that there was a sale of standing timber. Excise Tax Bulletin 541.04\45\33.135\259 [ETB 541] explains the tax liabilities that arise from the sale of standing timber and/or the sale of logs.

In this case, the cutting permit showed the taxpayer as the landowner and the purchaser as the timber owner. The taxpayer contends, however, that the "stumpage contract" was not a

contract for the sale of standing timber and that title to the timber had not passed to the purchaser prior to scaling.

The taxpayer had argued that the industry does not consider a stumpage or cutting rights agreement to be a sale of standing timber. (. . . .) The taxpayer distinguished its "stumpage" contracts from "lump-sale" contracts which it agrees are for the sale of standing timber. In lump-sum contracts, the standing timber is identified and the price is established up front. The buyer accepts all risk if the timber is blown down prior to sale.

WAC 458-40-630 equates the term "standing timber" with the term "stumpage" and defines the term as including standing or fallen trees having commercial value, which have not yet been severed from the stump. Webster's New Universal Unabridged Dictionary, second edition at page 1809, defines stumpage as:

1. standing timber.
2. the value of standing timber as figured from the price per stump.
3. the right to cut such timber.
4. a tax levied on cut timber.

Equating the terms stumpage and standing timber, therefore, is in accord with a common dictionary meaning of the two terms. Furthermore, several Washington decisions dealing with contracts for the sale of standing timber referred to the contracts as "cutting rights" contracts. See, e.g. Layman v. Ledgett, 89 Wn.2d 906, 577 P.2d 970 (1978) and Leuthold v. Davis, 56 Wn.2d 710, 355 P.2d 6 (1960).

We find that the "stumpage contract" at issue was a contract to sell standing timber. That finding is not based on the title of the contract, however, but on the contract terms.

The first recital in the contract stated:

> [The taxpayer] owns certain timber situated on the real property legally described in Schedule "A". [The taxpayer] desires to sell the timber identified in Schedule "A" to Purchaser and Purchaser desires to purchase the same.

As the timber identified in Schedule "A" was standing at the time the contract was executed, that provision supports the conclusion reached in Determination No. 92-249 that the taxpayer sold standing timber.

The contract set a price per unit for each species and grade that was to be cut. The fact that the parties to the contract did not

know the total amount the taxpayer would receive for the timber at the time they executed the contract does not negate a finding that the contract was for a sale of standing timber. The contract provision regarding payment is the standard method for stating the price and terms of payment in a contract for the sale of standing timber. See, 12 Am.Jur Legal Forms § 168:15, Contract for the sale of standing timber; 54 C.J.S Logs and Logging § 15. ETB 541 also notes that sales of standing timber may be for a lump sum amount or a unit price may be specified for each species.

In Paulus v. Yarbrough, 219 Or. 611, 347 P.2d 620 (1959), the Oregon Court held that a timber contract which provided that the sellers agreed to sell and buyer agreed to purchase all standing merchantable timber created a sale of the timber. In that case, as in the present case, the agreement called for payment per unit for poles and logs removed. The Court construed this provision to describe only the method of payment and not the buyer's obligation to pay. The court stated:

> The agreement obligates the buyer to purchase "all" of the merchantable timber upon the described land. The buyer also obligates himself to begin logging operations promptly and to continue such operations "until such time as all the timber herein agreed to be purchased has been removed. . .." If plaintiff had failed to proceed diligently with the logging operation, or if at the termination of the removal period he should fail to cut all or any of the timber agreed to be purchased he would be subject to an action for breach of contract.

Id. at 624.

Furthermore, in the contract at issue in Paulus the sellers had retained the power of designating some trees which could not be cut. The Court stated:

> The question is whether the power of designation reserved in the sellers could be regarded as postponing the passage of title until the designation was made. The contract embraced all of the merchantable timber on the land except those trees the removal of which would cause unreasonable damage to the unmatured trees. As we have already stated, the designation of the trees capable of removal without serious damage could be made in accordance with objective standards. That being true the title could be regarded as passing upon the execution of the contract.

347 P.2d at 634.

That analysis refutes the taxpayer's additional argument that the fact it could identify the timber to be cut and logged by marking was inconsistent with a transfer of title prior to severance. . . . . The taxpayer stated it had required the purchaser to leave certain trees to protect and control streams and water courses. We assume designating trees which needed to be retained for riparian management zones could also be done in accordance with objective standards. Accordingly, title could pass upon the execution of the contract.

ETB 541 states that a sale of standing timber occurs when title transfers to the buyer before harvesting; a sale of logs takes place when the landowner retains title until the logs are delivered to the buyer and scaled. The taxpayer's "Stumpage Contract" does not say when title passes to the buyer.
The taxpayer argued that because the buyer granted it a security interest only in cut timber, the buyer must have obtained title only to the cut logs. We disagree.

> As a general proposition, the vendor of standing timber to be cut and removed from his land by the vendee has a common law lien, known as the seller's lien, on the timber and lumber manufactured, as long as it remains upon his premises, unless it is otherwise stipulated in the contract.

In re Eakin Lumber Co., 34 F.Supp. 460 (1940). Furthermore, if the purchaser left standing timber, the purchaser was required to make payment to the taxpayer and the taxpayer could sell the timber to another party.

The taxpayer also asserted that the contract provisions for the branding/tagging of logs indicated the sale of cut logs rather than standing timber. We agree with the conclusion reached in Determination 92-249, however, that the branding and tagging was to protect [taxpayer's] security interest in those logs removed from its property until payment.

Schedule C of the contract provided a date by which the timber was to be cut and logged. The fact that a contract provides that the timber must be removed within a definite time does not prevent the title from vesting in the purchaser. 52 Am Jur2d, Supra, at § 34.

> By an unbroken line of decisions, the law is that, when an owner sells timber and conveys the same by deed, commonly called "cutting rights," if the conveyance fixes a time within which the timber must be removed,

> and the timber is not removed within such period, the ownership of the timber reverts to the grantor.

Leuthold v. Davis, 56 Wn. 2d at 712-13 (citations omitted).

In Heybrook v. Beard, 75 Wash. 646, 135 P. 626 (1913), the Court held that the timber grantee was liable under the contract for the value of cut logs destroyed by fire before removal. This holding was based on the court's conclusion that present title to the timber passed when the contract was executed. In that case, the contract provided that the purchasers had seven years to cut and remove the described timber. The Court interpreted the contract to mean that the title to the timber passed subject to a reversion if the timber had not been cut and removed from the land within the contract period. The Court reasoned there could be no reversion if title had not previously passed from the grantor to the vendee. 75 Wash. at 649.

In this case, upon termination of the contract, the purchaser had no further right to the timber and the taxpayer could sell the timber to another party. This provision would not be necessary if the ownership of the standing timber never transferred to the purchaser.

In Layman v. Ledgett, supra, the Court discussed the nature of the grantor's and the grantee's rights in a contract for the sale of standing timber. The Court stated:

> The grantor of timber (including cutting rights) retains a reversionary interest in the timber which is part of his estate in the land. These timber rights are considered as a profit a prendre, a right to take the profits of the land by entering onto it and cutting and removing the timber. This right is an interest in real property to which the timber grantee has title. The grantor has parted only with his right to appropriate that part of his land, i.e., timber, for a period of time; he has not parted with any part of his estate. The trees remain a part of the land until severed, at which time they are converted into personalty. Id. quoting Luccock, Timber Deeds--A case for the Restatement of the Law of Property, 20 Wash. L. Rev. 199, 207 (1945).

(Emphasis added.) 89 Wn.2d at 911.

In a contract for the sale of timber, the purchaser becomes the beneficial owner of the timber even though the purchaser has not paid the whole purchase price. The seller holds the title as trustee to be conveyed to the purchaser upon compliance with the

terms of the contract. Contract for the sale of standing timber; 54 C.J.S Logs and Logging § 15. See also, Cascade Security Bank v. Butler, 88 Wn.2d 777, 567 P.2d 631 (1977), overruling Ashford v. Reese, 132 Wn. 649 (1925) (Executory contract of sale conveys an equitable title to the vendee, bare legal title remaining in the vendor until the completion of the contract, whereupon legal title vests in the vendee.)

In Dierks Lumber & Coal Co. v. Fry, 203 Okla. 467, 223 P.2d 113 (1950), the Oklahoma Supreme Court described timber contracts as analogous to oil and gas mining leases. The court noted such contracts convey only a qualified title to the oil and gas. The title becomes absolute when the oil and gas is produced and reduced to the possession of the lessee. 223 P.2d at 115.

Standing timber sold separately from the fee is owned, for purposes of personal property taxation assessments, by the party enjoying the right to possess, use, or convey such forest products as well as suffering the risk of loss in the event of their damage or destruction. See Wasser & Winters v. Jefferson County, 84 Wn.2d 597, 528 P.2d 471 (1974); 71 Am.Jur.2d State and Local Taxation sections 194-196 and cases cited therein.

In Wasser & Winters, the Washington Supreme Court examined the question of whether the plaintiff was properly the owner of logs under a contract entitled "Bill of Sale and Contract to Pay For and Remove Forest Products from State Lands." The Court stated:

> We have identified the chief incidents of ownership of property as the right to its possession, use and enjoyment and to sell or otherwise dispose of it according to the will of the owner. [Citation omitted.] In Sloan Shipyards Corp. v Thurston County, 111 Wash. 361 (1920), we held that the person assessed need not have a perfect and unencumbered title to the property but only that he should be vested with the apparent legal title, or with the possession coupled with such claims and evidence of ownership as will justify the assumption that he is the owner.

(Emphasis supplied.) 84 Wn.2d at 599.

In the present case, the purchaser had not only the right but the obligation to cut and sell all merchantable timber. We find the purchaser was properly the "owner" of the timber. As "timber owner" the purchaser owned the right to cut and remove all merchantable timber. Layman v. Ledgett, 16 Wn.App 733, 738-39 (1977), aff'd. 89 Wn.2d 906 (1978).

Section five of the legal form for the Contract for the sale of standing timber in 12 AM. JUR. LEGAL FORMS 2d, Logs & Timber, § 168:15, provides:

> Title to timber designated for removal shall pass to buyer at the time of scaling. Risk of loss to timber subject to removal and an insurable interest in such timber shall pass to buyer at the time of felling.

As in the form contract for a sale of standing timber, the taxpayer's stumpage contract provided that the purchaser assumed the "risk of loss" of the timber. The taxpayer's representative testified that this only made the purchaser liable to the taxpayer for any losses occurring after severance. The taxpayer contended that in the event of destruction of timber prior to harvesting, loss would be borne by both parties. The fact that the purchaser, not the taxpayer, had the risk of any loss to the timber at the time of felling, however, supports the finding that the purchaser had acquired ownership of the timber prior to scaling.

Finally, the taxpayer had argued that the Administrative Law Judge had relied on two administrative rules which are invalid. The taxpayer contended the definition of "harvester" in RCW 84.33.035(3) does not state that the "harvester" is the person who owns the timber. The taxpayer argued that the Department's meaning of "harvester" to be the owner of the timber in WAC 458-40-620 has no statutory authority.
We believe the fact the contract at issue required the purchaser to sign the Forest Practices Application as "Timber Owner" supports, but does not require, a finding that the contract transferred ownership of the timber to the purchaser. The finding that the taxpayer's stumpage contract was a contract for the sale of standing timber, however, would be the same whether or not Rule 620 is valid or invalid.

The taxpayer also argued that WAC 458-61-660(3) is invalid. That section provides that "a contract to transfer the ownership of timber after it has been cut and removed from land by the grantee is a taxable transaction." We agree that section three should state that such a contract is not a taxable transaction. However, even if 660(3) is invalid, it would not change the result in this case. We find that the contract transferred ownership of the timber before it was cut and removed. This case fits within subsections one and two of Rule 660.

We find that the Administrative Law Judge properly expressed the position of the Department. The contract required the purchaser to go upon described land and remove designated timber, set the price and terms of payment, provided that the buyer assumed the

risk of loss for the timber, and provided that the purchaser was the "timber owner" and liable for the timber excise tax--all factors which support the finding that the contract was for a sale of timber.

DECISION AND DISPOSITION:

The taxpayer's petition is denied. This is the last action the Department will take in this matter. However, the taxpayer may choose to continue its appeal, either through the provisions of RCW 82.03, which governs appeals to the Board of Tax Appeals, or by petition to the Superior Court of Thurston County, pursuant to the provisions of RCW 82.32.180.

DATED this 28th day of May 1993.