Cite as 2 WTD 143 (1986)

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

In the Matter of the Petition For Correction of Assessment of	)	D E T E R M I N A T I O N
	)	No. 87-17
. . .	)	Registration No. . . .

[1] **RULES 112 and 135**: RCW 82.04.450 -- EXTRACTING TAX -- SELLING PRICE -- VALUE -- TIMBER -- ETB 302. The value of products extracted is determined by the gross proceeds of sales, not the price paid for similar logs.

[2] **RULE 193C**: B&O TAX -- COMMERCE -- EXPORTS -- LOGS -- STORAGE YARD --COAST PACIFIC TRADING, INC., cited. Tax upheld where the taxable transaction--the sale of the logs--was completed before the logs were towed from storage to be loaded aboard ship. Logs found not to have entered "export stream" even though they were sold to foreign purchasers and delivered to the towing company with instructions to transport the logs to a particular port for shipment on a named carrier. Tax on foreign sales is valid unless logs are delivered to the foreign buyer at shipside.

[3] **RULE 106**: RULE 109 -- RCW 82.04.080 -- B&O TAX -- SERVICE -- INTEREST CASUAL SALE. The purchase of items for resale falls within the definition of a business activity, even if a taxpayer's primary business is not buying and selling inventory. Sales of items that were purchased for resale are not casual and isolated sales, and the interest earned from the sale of such items is subject to the Service business and occupation tax.

[4] **RULE 178**: RCW 82.12.010 -- USE TAX -- VALUE -- ETB 302.

In most cases, the taxable value of property for use tax purposes is the consideration paid by the purchaser to the seller for the property. Assessment of use tax on a truck will be reduced if taxpayer's records show that amount on its books listed as purchase price of truck also included cash received.

[5] **RULE 178**: USE TAX -- CONSUMABLE SUPPLIES -- TEST PERIOD.
A correlation generally exists between a taxpayer's purchases of consumable supplies and its income. If a taxpayer believes a test period used by an auditor to arrive at a percentage to use for computing amounts subject to tax is not representative of other periods, it may compute the amount of use tax owing for another period. The assessment will be reduced if the taxpayer can show the percentage used by the auditor resulted in a higher tax than was due.

Headnotes are provided as a convenience for the reader and are 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 HEARING: September 30, 1986

NATURE OF ACTION:

The taxpayer petitions for a correction of a tax assessment as it relates to extracting tax on timber harvested and sold in interstate or foreign commerce, disallowed wholesale export sales deductions, service tax on interest income, and use tax on capital assets and consumable supplies.

FACTS AND ISSUES:

Frankel, A.L.J. -- The taxpayer operates a log sorting yard. . . . . The taxpayer also extracts timber, buys timber, manufactures chips and sells timber and chips.

The taxpayer's records were examined for the period March 17, 1983 through September 30, 1985. The examination disclosed taxes and interest owing in the amount of $. . . . A tax assessment (No. . . .) in that amount was issued on May 20, 1986.

The taxpayer protests the following portions of the assessment:

1. Schedule II, extracting tax on timber harvested and sold in interstate or foreign commerce. The taxpayer contends it was overcharged the sum of $2,710. It states it used normally accepted accounting principles and WAC 458-20-112 and WAC 458-20-135 to arrive at the figure for the amount of tax due.

The auditor determined the value of the extracted timber by the selling price of the logs. The average export selling price per thousand board feet was applied against the board footage of extracted timber sold for export to determine the value of the extracted timber. The taxpayer contends the extracting tax should be reported on the purchase price which it pays for similar logs rather than the selling price of the logs.

2. Schedule IV, disallowed wholesale export sale deductions. Deductions were disallowed for those sales in which the taxpayer delivered logs to a rafting or towing company. The taxpayer contends the logs had entered the "export stream," and thus the sales are exempt from the business and occupation tax.

3. Schedule VI, service tax on unreported interest income on notes receivable. The interest income was from inventory items which the taxpayer sold on account which earn interest on the unpaid balance. The taxpayer contends the items which were sold were casual sales and that none of the income from the sales should be subject to the business and occupation tax.

4. Schedule VIII, use tax on capital assets on which sales or use tax was not paid. The taxpayer contends the assessment of use tax on a flatbed truck should be reduced. The taxpayer's books indicated a value of $4,400 for the truck. The taxpayer contends that figure was not the value of the truck alone, as it included additional cash received. The taxpayer contends the true value of the truck was only $1,200 and that the assessment should be reduced approximately $278.

5. Schedule IX, use tax on recurring purchases. The auditor reviewed the taxpayer's purchases for the test period of July 1984 to June 1985 to determine the amount of purchases on which the retail sales tax was not paid to the taxpayer's suppliers. This amount was compared to the total income for

the corresponding period to arrive at a percentage to apply to other periods. The percentage was applied to reported income for all of the audit to arrive at the amounts subject to tax.

The taxpayer objects to the auditor's assumption that consumable purchases are related to the amount of sales. Instead, the taxpayer contends the amount of consumables remains fairly constant, but the income from sales varies.

DISCUSSION:

[1] Extracting tax: The auditor assessed the extracting tax against the selling price of the extracted timber. The taxpayer contends the proper measure should be the price that it pays for similar logs rather than the selling price. It states its purchase price includes, inter alia, the cost of the log, yarding and logging, transportation from the woods to the logging landing, and from the landing to the sorting yard. The taxpayer contends the "value" of the exported logs should not include the additional price to the export buyer for the taxpayer's built-in charges for sorting and bucking.

Logging operations are included within the extracting classification definition of an "extractor" in RCW 82.04.100. RCW 82.04.450 provides for a business tax upon extractors upon the value of the products extracted for sale. See also WAC 458-20-135 (persons who extract products in this state and sell them in interstate commerce are taxable under the extracting classification upon the value of the products so sold).

The term "value of products" is statutorily defined by RCW 82.04.450 which provides in pertinent part as follows:

> The value of products . . . extracted . . . shall be determined by the gross proceeds derived from the sale thereof whether such sale is at wholesale or at retail, . . . (Emphasis supplied.)

WAC 458-20-112 (Rule 112) is the Department's rule which contains the principles set forth in RCW 82.04.450. The rule provides that in all cases of bona fide sales, the value of products extracted shall be determined by the gross proceeds of sales.

Where bona fide sales have not occurred, Rule 112 provides:

> ALL OTHER CASES. The law provides that where products extracted or manufactured are
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> 1. For commercial or industrial use (by the extractor or manufacturer--see WAC 458-20-134); or
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> 2. Transported out of the state, or to another person without prior sale; or
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> 3. Sold under circumstances such that the stated gross proceeds from the sale are not indicative of the true value of the subject matter of the sale: the value shall correspond as nearly as possible to the gross proceeds from other sales at comparable locations in this state of similar products of like quality and character, in similar quantities, under comparable conditions of sale, to comparable purchasers, and shall include subsidies and bonuses.
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> In the absence of sales of similar products as a guide to value, such value may be determined upon a cost basis. In such cases, there shall be included every item of cost attributable to the particular article or article extracted or manufactured, including direct and indirect overhead costs.

The taxpayer contends its sales fall under subsection (3), contending the stated gross proceeds from the exports are not indicative of the true value of the logs.

We disagree. The taxpayer has not shown that the export sales were not "bona fide sales"; thus the measure of the tax is the selling price. The taxpayer's additional costs for sorting and bucking were factors in establishing the selling price, and RCW 82.04.450 contemplates that the value of products shall correspond to the gross proceeds from sales. See ETB 302.04.112.

As Rule 112 provides, all of the taxpayer's costs, except actual transportation costs from the point at which the shipment originates in this state to the point of delivery outside the state, must be included in determining the value of the logs. Accordingly, the assessment in Schedule II is upheld.

[2] The auditor disallowed wholesale export sale deductions where the logs were sold to a foreign buyer but were delivered to a Washington towing company. The purchaser was responsible

for moving the logs from the towing area to the ship and paid the towing company for the transportation.

The taxpayer contends that it delivered all of the logs to the towing company with instructions to transport the logs to a particular port for shipment on a named carrier. In some cases, the purchaser paid the towing company directly and in other cases the taxpayer did. In substance, the taxpayer contends all of the transactions were the same and that it was its obligation to see that the logs were shipped.

Both the taxpayer and the auditor rely on WAC 458-20-193C (Rule 193C) and Coast Pacific Trading, Inc. v. Department of Rev., 105 Wn.2d 912 (1986). States are not prohibited from taxing sales to foreign buyers, but are prohibited from taxing goods that have entered the "export stream." See Kosydar v. National Cash Register Company, 417 U.S. 62, 70-71 (1974); Coe v. Errol, 116 U.S. 517, 526-27 (1886).

Rule 193C was enacted to codify the requirements for immunity established by United States Supreme Court decisions. See, Coast Pacific, 105 Wn.2d at 916-17. Rule 193C states the requirements for a tax exempt export sale as follows:

> EXPORTS. A deduction is allowed with respect to export sales when as a necessary incident to the contract of sale the seller agrees to, and does deliver the goods (1) to the buyer at a foreign destination; or (2) to a carrier consigned to and for transportation to a foreign destination; or (3) to the buyer at shipside or aboard the buyer's vessel or other vehicle of transportation under circumstances where it is clear that the process of exportation of the goods has begun, and such exportation will not necessarily be deemed to have begun if the goods are merely in storage awaiting shipment, even though there is reasonable certainty that the goods will be exported. The intention to export, as evidenced for example, by financial and contractual relationships does not indicate "certainty of export" if the goods have not commenced their journey abroad; there must be an actual entrance of the goods into the export stream.
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> In all circumstances there must be (a) a certainty of export and (b) the process of export must have started.

It is of no importance that title and/or possession of the goods pass in this state so long as delivery is made directly into the export channel. To be tax exempt upon export sales, the seller must document the fact that he placed the goods into the export process. That may be shown by the seller obtaining and keeping in his files any one of the following documentary evidence:

(1) A bona fide bill of lading in which the seller is shipper/consignor and by which the carrier agrees to transport the goods sold to the foreign buyer/consignee at a foreign destination; or

(2) A copy of the shipper's export declaration, showing that the seller was the exporter of the goods sold; or

(3) Documents consisting of:

(a) Purchase orders or contracts of sale which show that the seller is required to get the goods into the export stream, e.g., "f.a.s. vessel;" and

(b) Local delivery receipts, tripsheets, waybills, warehouse releases, etc., reflecting how and when the goods were delivered into the export stream; and

(c) When available, United States export or customs clearance documents showing that the goods were actually exported; and

(d) When available, records showing that the goods were packaged, numbered, or otherwise handled in a way which is exclusively attributable to goods for export.

Thus, where the seller actually delivers the goods into the export stream and retains such records as above set forth, the tax does not apply. It is not sufficient to show that the goods ultimately reached a foreign destination; but rather, the seller must show that he was required to, and did put the goods into the export process.

Coast Pacific Trading, Inc. v. Department of Rev., supra, upheld the Department's denial of export deductions for logs held in floating storage yards pending shipment to a foreign purchaser. The court held that the logs had not yet entered

the export stream, even though the logs had been set aside to fill a specific order from a foreign purchaser. In that case, the Department taxed sales with "F.O.B." ("free on board") delivery locations that were not alongside or on board a ship, but not those with "F.A.S." ("free alongside ship") delivery points or those with shiploading or imminent-loading F.O.B. delivery points. 105 Wn.2d at 914. The taxpayer has not contended that its sales were either "F.A.S." or "F.O.B" with shiploading or imminent-loading delivery points.

In Coast Pacific, the court found the taxable transaction--the sale of the logs--was completed before the logs were towed from storage to be loaded aboard ship for export. In that case, as here, the logs were reasonably certain to be exported and their "final movement" overseas had begun before the logs reached the F.O.B. delivery point. 105 Wn.2d at 919-20. As the court noted, however, "courts repeatedly have rejected these grounds for tax immunity." 105 Wn.2d at 920.

We find the facts in Coast Pacific are apposite to the present case. Accordingly, the assessment in Schedule IV is upheld.

[3] The taxpayer purchased the assets of another corporation from a bank which had repossessed them. It did not pay sales tax on the items at the time of acquisition. The taxpayer stated it purchased the items to supply a new service shop; it sold those items it did not want to use. The taxpayer contends those sales were "casual sales" and the interest income should be exempt from the business and occupation tax.

The business and occupation tax is imposed "for the act or privilege of engaging in business activities" in this state. RCW 82.04.220. "Business" includes "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or to another person . . ." RCW 82.04.220. The business and occupation tax is calculated on the "gross income of the business" unless otherwise exempted. RCW 82.04.290. "Gross income of the business" includes proceeds received from interest. RCW 82.04.080. Interest is taxable under RCW 82.04.290, which imposes the Service classification business and occupation tax.

A "casual sale" is one made by a person who is not engaged in the business of selling the type of property involved. RCW 82.04.040. The business and occupation tax does not apply to casual or isolated sales. WAC 458-20-106.

The auditor found that the taxpayer did not pay sales tax on the items when it acquired them from the bank because it told the bank the items were being purchased for resale. RCW 82.04.050 provides an exemption from the retail sales tax for a sale to a person who "purchases for the purpose of resale as tangible personal property in the regular course of business without intervening use by such person." (Empahsis added.) The purchase of items for resale falls within the definition of a business activity. Accordingly, although the taxpayer's primary business may not be buying and selling inventory, we do not agree that the sales at issue meet the definition of "casual or isolated." The auditor found the taxpayer had paid business and occupation tax on the proceeds from the sales of the inventory items, except the amount received for interest. We find the assessment of Service business and occupation on the interest was proper. The assessment in Schedule VI is upheld.

[4] The use tax supplements the retail sales tax by imposing a tax of like amount upon the use of tangible personal property, the sale or acquisition of which has not been subject to the Washington retail sales tax. WAC 458-20-178; RCW 82.12.020. In most cases, the taxable value is the consideration paid by the purchaser to the seller. RCW 82.12.010.

The taxpayer objects to the amount of use tax assessed on the flatbed truck (. . .). The taxpayer agrees that use tax is owing, but objects to the amount of the tax. The taxpayer's books indicated that it received $4,400 for the truck, but it stated that the $4,400 represents a cash payment as well as the truck. The taxpayer contends that the true value of the truck was only $1,200 -- the amount stated as the true value of the truck when it was licensed.

We agree that the assessment of use tax should be reduced, if the taxpayer can document that the $4,400 amount listed for the truck included a payment of cash. Acceptable evidence would be a copy of a receipt which stated the amount of the cash received, or a copy of a deposit slip or the taxpayer's records identifying the cash received from this transaction. The $4,400 amount will be reduced by the amount of cash received.

If the taxpayer is unable to produce such evidence, the value will be reduced if the taxpayer's federal tax returns show a depreciable value of the truck at less than $4,400. Such evidence should be submitted to the auditor to receive a

corrected assessment. The taxpayer's statement that a taxable value of $1,200 was used when registering the vehicle, however, is not sufficient evidence by itself to reduce the assessment.

[5] The last item at issue is the amount of deferred sales tax/use tax assessed on consumable supplies on which the taxpayer had not paid retail sales tax. The auditor reviewed all purchases for July 1984 to June 1985, a test period selected jointly by the auditor and the taxpayer's representative. The purchases were primarily for parts and supplies, but also included carbonated beverages.

The taxpayer does not dispute that tax is due, but objects to the method used by the auditor in calculating the amount of tax due. The taxpayer contends that the amount of consumable supplies remains fairly constant; thus the use of a percentage is inaccurate. The taxpayer also contends that the auditor should have deleted the two invoices for the largest and smallest payments during the test period to arrive at a more accurate statistical sample.

The taxpayer apparently agreed to the sampling method at the time of the hearing and at the supervisor's conference. If it now feels the test period is not representative of other periods, however, it may compute the amount of use tax owing for another period. It should, however, total all invoices for that period for which sales tax was not paid and not delete the "high" and "low" invoice to arrive at the taxable amount. If the evidence shows that the percentage relationship is lower than the percentage for the period used by the auditor, that evidence can be presented to the Audit Section and the assessment will be recalculated.

DECISION AND DISPOSITION:

The taxpayer's petition for correction of Assessment No. . . . is denied as to the assessments in Schedules II, IV and VI.

The taxpayer shall have 20 days from the date of this Determination (February 11, 1987) to present evidence to the Audit Section which would support a reduction of the assessments in Schedules VIII and IX, as discussed herein. That section, after performing any adjustments permitted by this Determination, shall issue an amended assessment due on the date shown. If the taxpayer does not present evidence supporting an adjustment, the amount remaining owing, plus extension interest of shall be due by February 11, 1987.

Any evidence which the taxpayer is unable to identify within the 20-day period, but which it believes meets the guidelines for exclusion, may be presented to the Audit Section with a petition for refund. A petition for refund must be within the four-year limitation period provided by RCW 82.32.060.

DATED this 22nd day of January 1987.