

FINDINGS OF FACT

[Taxpayer] is located in . . . Washington. Taxpayer's business activities in Washington include providing logging services on a contract basis for timber harvesters. Occasionally Taxpayer purchases timber of its own, and logs that timber. Taxpayer owns and operates logging trucks in connection with its logging activities.

The Department's Audit Division (Audit) examined Taxpayer's books and records for the period January 1, 2006, through June 30, 2007. On June 2, 2010, the Department issued Taxpayer an assessment . . . totaling \$. . ., including a retail sales tax credit of \$. . . for machinery and equipment parts and repair used in manufacturing, use tax and/or deferred sales tax of \$. . ., extracting/extracting for hire B&O tax totaling \$. . ., extracting timber B&O tax totaling \$. . ., a 5 percent assessment penalty of \$. . ., and interest of \$. . . .

Schedule 4 of the Assessment imposed deferred retail sales and/or use tax on a piece of equipment called a feller buncher that Taxpayer purchased without payment of sales tax. The taxable amount of the feller buncher that the Department included in the Assessment was less an allowable trade-in. When Taxpayer purchased the feller buncher, it gave the seller an M&E exemption certificate.

Audit concluded that the feller buncher performs the function of cutting/severing the standing tree from the stump, an extracting/extracting for hire activity that occurs prior to the manufacturing/processing for hire activity. Therefore, Audit found that Taxpayer's purchase of the feller buncher was not exempt from retail sales tax, and Taxpayer owed deferred retail sales and/or use tax on the feller buncher.

Taxpayer disagrees with Audit, and argues that the feller buncher is exempt from retail sales tax because Taxpayer used it the majority of the time to sort trees and forward them, so that they can be reached by other forwarding machines. Taxpayer explains that feller bunchers are used to cut trees in riparian zones,² where only a few trees are allowed to be harvested, due to state and federal regulations. Consistent with taxpayer's description, one website describes a feller buncher as follows:

Feller Buncher

A *feller buncher* is a large logging machine designed to cut trees in place without letting them fall. It provides a very controlled way to cut a tree in tight quarters. The feller buncher also allows us to prevent damage from a tree falling and preserve fragile forest areas. It consists of a standard heavy equipment base with a tree-grabbing device furnished with a saw. There is also a pinching device designed to cut small trees off at the base. The machine then places a cut tree in a stack suitable for a skidder or other means of transport.

² A riparian zone or riparian area is the interface between land and a river or stream. See http://en.wikipedia.org/wiki/Riparian_zone (last visited January 25, 2011).

<http://www.gamblebaytimber.com/equipment.html> (last visited January 18, 2011). Dual function machines, like feller bunchers, are able to fell a tree and move the cut stem to a pile.³ The feller buncher replaces the work that lumberjacks or fallers historically did, namely falling and piling trees into bunches.⁴ The feller buncher removes a tree from its stump, and bunches this tree and other trees in a pile. A majority of the time, a log loader (shovel loader) then pulls the cut trees out of the forest and brings them to the landing site where the processor, which delimbs the trees and cuts them to length, is located.⁵

ANALYSIS

In general, all sales in the state of Washington of tangible personal property to consumers are subject to retail sales tax unless the sales are otherwise exempt from taxation. RCW 82.08.020; RCW 82.04.050. Use tax complements the retail sales tax by imposing a tax of like amount upon the privilege of using within this state as a consumer any article of tangible personal property acquired without payment of retail sales tax. *See* RCW 82.12.020(1), (2).

However, sales to a manufacturer or processor for hire of machinery and equipment (M&E) used directly in a manufacturing operation is exempt from retail sales tax. RCW 82.08.02565. In addition, a manufacturer or processor for hire is exempt from use tax on M&E used directly in a manufacturing operation. RCW 82.12.02565.⁶

RCW 82.04.120 establishes that the cutting, delimbing, and measuring of felled, cut, or taken trees is a manufacturing activity, not an extracting activity:

“To manufacture” embraces all activities of a commercial or industrial nature wherein labor or skill is applied, by hand or machinery, to materials so that as a result thereof a new, different or useful substance or article of tangible personal property is produced for sale or commercial or industrial use, and shall include: . . . (3) cutting, delimbing, and measuring of felled, cut, or taken trees;

RCW 82.04.120.⁷ Rule 13501(1)(c) elaborates on the statutory standard, and reads:

The cutting into length (bucking), delimbing, and measuring (for bucking) of felled, cut (severed), or taken trees is a manufacturing activity. RCW 82.04.120.

³ See <http://www.forestencyclopedia.net/p/p2276> (last visited January 18, 2011). Several videos on the internet show feller bunchers at work. See <http://wn.com/feller-buncher> (last visited January 18, 2011).

⁴ See http://www.ritchiewiki.com/wiki/index.php/Feller_Buncher (last visited January 18, 2011).

⁵ If hills or mountains are involved, then a yarder is used to bring the trees to the landing site. Sometimes in smaller logging operations, and where the land is fairly flat, a skidder is used to move logs to the landing site.

⁶ See also WAC 458-20-135(6)(a); WAC 458-20-13501(7)(a); and WAC 458-20-13601(3).

⁷ Det. No. 00-138, 20 WTD 167 (2001) explains that a 1999 statutory amendment of RCW 82.04.120 clarified that “to manufacture” includes the “cutting, delimbing, and measuring of felled, cut, or taken trees.”

See also WAC 458-20-136(2)(a) (Rule 136(2)(a)) (“To manufacture” includes . . . “(ii) The cutting, delimbing, and measuring of felled, cut, or taken trees;”)

Extraction differs from manufacturing, however, by statute. The term “extractor” is defined by statute as:

[E]very person who from the person’s own land or from the land of another under a right or license granted by lease or contract, either directly or by contracting with others for the necessary labor or mechanical services, for sale or for commercial or industrial use . . . fells, cuts or takes timber. . . . “Extractor” does not include persons performing under contract the necessary labor or mechanical services for others . . .

RCW 82.04.100. *See also* WAC 458-20-13501(2)(b) (“The felling, cutting (severing from the land), or taking of trees is an extracting activity.”); WAC 458-20-135(2) (“The term includes a person who fells, cuts, or takes timber.”)

Persons who perform extracting activities (labor and mechanical services) for timber harvesters are subject to the extracting for hire B&O tax upon the gross income from those services. Rule 13501(3). The rule gives the following example of an extractor for hire:

[A] person severing trees owned by a timber harvester is performing an extracting activity, and is considered an extractor for hire with respect to those services. . . .
Extracting activities commonly performed by extractors for hire include, but are not limited to:

(a) Cutting or severing trees;

Rule 13501(3).

An extractor may subsequently take an extracted product and use it as a raw material in a manufacturing process. Rule 135(2)(b). A determination of when extracting ends and manufacturing begins can be made only after a review of all the facts and circumstances. *Id.* Generally, a manufacturing operation begins at the point where the raw materials enter the manufacturing site and ends at the point where processed material leaves the manufacturing site. RCW 82.08.02565(2)(d) (“For purposes of this section and RCW 82.12.02565”); Rule 13601(2)(g). The operation includes storage of raw materials at the site, the storage of in-process materials at the site, and the storage of the processed material at the site. *Id.* To be eligible as a qualifying use of M&E, the use must take place within the manufacturing operation. *Id.*

Det. No. 00-138, 20 WTD 167 (2001) involved a taxpayer that manufactured, repaired, and sold logging equipment, including feller bunchers. The Department’s Audit Division assessed taxpayer retail sales tax on taxpayer’s sales of such equipment to its customers. 20 WTD 167 affirmed the assessment as to the feller bunchers, concluding that the feller bunchers did not

qualify for the M&E exemption because they were used to cut trees, which is an extracting activity, not a manufacturing activity.

The only stage of the logging process at which manufacturing under RCW 82.04.120 occurs is when felled, cut, or taken trees are cut into length (bucked), delimbed, or measured (for bucking). This only occurs when the trees are processed.⁸ A feller buncher does not process the trees. A feller buncher simply fells, cuts (severs from the land), and takes trees and bunches them into piles, so that another machine (e.g., log loader/shovel loader) can remove them from the forest. This is an extraction activity under RCW 82.04.100. If Taxpayer uses a feller buncher to perform such services for other timber harvesters, it does so as an extractor for hire under Rule 13501(3). If it does so with regard to its own timber, it is merely an extractor.

Since the feller buncher merely extracts trees, it is not used directly in a manufacturing operation, and taxpayer is *not* exempt from paying retail sales and/or use tax on the feller buncher (M&E) under RCW 82.08.02565 and RCW 82.12.02565. 20 WTD 167 supports this conclusion. Taxpayer's argument that the feller buncher spends the majority of its time sorting and moving trees equates bunching logs (which a feller buncher does) with subjecting them to a manufacturing process. This is not correct.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 17th day of March 2011.

⁸ E.g., the mere removal of bark from logs is not a manufacturing activity. Rule 13501(2)(c)(iii).