

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

In The Matter of the Petition     )     D E T E R M I N A T I O N  
For Determination of Tax         )  
Liability of                     )     No. 89-393  
                                  )  
                                  )  
                                  )     Registration No. . . .

RULE 136:     MANUFACTURING -- DEBARKING OF LOGS.     The debarking of logs is a manufacturing activity.     The fact that this activity does not meet the federal definition of "manufacturing" for the export of logs does not alter the tax consequences in Washington state.

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.

NATURE OF ACTION:

Taxpayer requests a ruling regarding whether the debarking of logs is considered a manufacturing activity.

FACTS AND ISSUES:

Hesselholt, A.L.J. -- Taxpayer received a telephone call from the Department of Revenue auditor who performed its last audit.     The auditor informed taxpayer that the Department was currently taking the position that the debarking of logs was a manufacturing activity.     Taxpayer disagreed with this position and has requested a determination in this matter.     Taxpayer explains its business as follows:

[Taxpayer] operates a log export facility . . . .

Log sales are made F.A.S. vessels.     Mates receipts, bills of lading, original invoices are available for sales transactions.     The majority of sales have qualified as export sales under State and City of . . . audit scrutiny.

In late 1988 the company installed a log debarker at its export facility.     The purpose of the debarker is to

remove remaining bark from logs prior to shipping. (up to 70% of bark may fall off of the log through normal handling) The advantages of bark removal are (1) maximization of capacity on ships (Bark is a waste product and reduces volume capacity for wood cargo) and (2) there is no demand for bark waste product such as Beauty Bark overseas. Therefore, the additional cost of disposal at the foreign destination reduces the F.A.S. sales price.

The ultimate use of the log is not altered by removing the remaining bark. The item exported is neither new nor different. The item exported is still a log. Debarking is not unlike "the mere cleaning of whole fish" which under WAC 458-20-136 is specifically identified as not a manufacturing process.

Taxpayer further explained that it has an arrangement with a person who takes the bark. If he makes over a certain amount of money turning the waste bark into Beauty Bark, he must rebate it to the taxpayer. Taxpayer states that this seldom, if ever, happens. Taxpayer also explained that the U.S. Forrest Service does not permit the export of logs grown on federal land unless they are manufactured, and that debarking does not meet their strict definition of manufacturing. Logs grown on non-federal land are not required to be manufactured before being exported.

#### DISCUSSION:

WAC 458-20-136 (Rule 136) provides, in relevant part, as follows:

(1) "The term 'to manufacture' embraces all activities of a commercial or industrial nature wherein labor or skill is applied, by hand or machinery, to materials, to 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 the production or fabrication of special made or custom made articles." (RCW 82.04.120.) It means the business of producing articles for sale, or for commercial or industrial use from raw materials or prepared materials by giving these matters new forms, qualities, properties, or combinations. It includes such activities as making, fabricating, processing, refining, mixing, slaughtering, packing, curing, aging, canning, etc. It includes also the preparing, packaging and freezing of fresh fruits, vegetables, fish, meats and other food products, the making of custom made suits, dresses, coats, awnings, blinds, boats, curtains, draperies, rugs, and tanks, and other articles constructed or made to order, and the curing of animal hides and food products.

(7) Manufacturing--interstate or foreign sales. Persons who manufacture products in this state and sell the same in interstate or foreign commerce are taxable under the classification manufacturing upon the value of the products so sold, and are not taxable under retailing or wholesaling--all others in respect to such sales. . . .

Taxpayer argues that its activities are akin to the "mere cleaning of fish" (Rule 136(4)) and therefore not subject to the manufacturing tax. The "cleaning of fish" is not manufacturing because there is a specific statutory exemption for it. The general question of what constitutes manufacturing has been considered by the Department of Revenue many times over the years. The case law on the subject is conclusive as authority for imposition of the tax even when there is a minimal amount of physical change in the product. See McDonnell & McDonnell v. State, 52 Wn.2d 553 (1963), (splitting peas is a manufacturing activity); Continental Coffee Company v. State, 66 Wn.2d 194 (1965) (the changing of green coffee beans into roasted and blended coffee is manufacturing); Bornstein Sea Foods, Inc. v. State, 60 Wn.2d 169 (1962), (the process of changing fish into fish filet is manufacturing); Stokeley-Van Camp, Inc. v. State, 50 Wn.2d 492 (1957), (the packaging and freezing of fruits and vegetables held to be manufacturing); and J.J. Dunbar & Company v. State, 40 Wn.2d 763 (1952), (the screening and filtering of raw whiskey constitutes manufacturing).

In this case, taxpayer takes a "raw" log and removes the remaining bark from it. This process results in waste bark, which is turned into Beauty Bark, a product used in landscaping, and a smooth log, which is exported. The debarking of the log has resulted in the production of a new substance (waste bark, which becomes Beauty Bark), and a debarked log, which takes up less space on a ship. This is sufficient to meet the statutory definition of manufacturing. The fact that this definition does not meet the U.S. Forest Service's definition is irrelevant.

RULING:

The debarking of logs is considered a manufacturing activity. Taxpayer shall report it as such as of the date of this determination.

DATED this 27th day of July 1989.