

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 Correction of Assessment of)
) No. 89-490
)
) Registration No. . . .
) Assessment No. . . .

[1] RULE 136 AND RULE 112: B&O TAX - MANUFACTURING -
VALUE OF PRODUCTS - OUT-OF-STATE LEASE - TAXPAYER
LEAVES WASHINGTON. When a taxpayer which has
manufactured a product in this state for lease out-
of-state subsequently removes itself from this
state, that taxpayer will be required to continue to
report the manufacturing tax measured by the lease
payments as long as this state has any taxing
jurisdiction over it. If jurisdiction over the
taxpayer is to cease before the taxpayer has paid
manufacturing tax on a measure equalling at least
the product's "cost of production," the taxpayer
will owe manufacturing tax on the balance of that
measure.

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: . . .
 . . .

NATURE OF ACTION:

Petition concerning manufacturing tax liability related to the
manufacture of tangible personal property leased out-of-state
when the taxpayer removes itself from the state.

FACTS:

Bauer, A.L.J. -- The taxpayer's business records were examined for the period April 1, 1981 through March 31, 1985. The above-referenced assessment was issued on December 26, 1985 in the amount of \$

The taxpayer manufactured three vessels in the state of Washington. These vessels were then leased to out-of-state customers. Since the rental of tangible personal property is considered a sale under the Revenue Act, these out-of-state leases were considered exempt interstate sales. Thus, the manufacturing tax was imposed on the measure of rental payments as they were received.

The taxpayer has moved from the state of Washington. At the time the taxpayer left the state, manufacturing taxes on the vessels at issue had not been collected on a measure equalling their capitalized values. The auditor, in the Department's final audit, assessed the manufacturing tax, as of November 30, 1983 - the date the taxpayer left the state - on the remaining untaxed capitalized values of the vessels.

TAXPAYER'S EXCEPTIONS:

The taxpayer originally appealed numerous portions of the assessment of a factual nature, which issues were remanded to the Audit Section under separate correspondence. These issues will not be addressed.

The remaining issue involves the manufacturing tax liability relating to the three vessels leased out-of-state. The taxpayer has not objected to the measure of the tax, but to the timing of its payment.

The taxpayer's petition argues, in pertinent part, as follows:

The audit assessment has substantially changed and reinterpreted WAC 458-20-136 and WAC 458-20-211 as to when tax becomes due on interstate or foreign lease income from vessels manufactured in the State of Washington. Per WAC 458-20-136:

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 the retailing or wholesaling-
all other in respect to such sales.

Leases or rentals of tangible personal property are
under WAC 458-20-211:

The term "leasing" and "renting" are used
interchangeably and refer generally to the
act of granting to another the right of
possession to and use of tangible personal
property for a consideration....

Business and Occupation tax - The renting
or leasing of tangible personal property
constitutes a 'sale' (RCW 82.04.040) and
persons engaged in renting or leasing such
property to users or consumers are taxable
under the retailing classification upon
gross income from rentals as of the time of
the rental payments fall due.

The lease of the [three vessels at issue] are
interstate sales and the vessels were manufactured
by [the taxpayer]. The total rental payments did
not fall due at November 30, 1983 when [the
taxpayer] moved out of state (as shown in the audit
assessment). They continued to fall due according
to the contractual conditions of the Bareboat
Charter Party Agreements which are still in effect.

The adjustments required to correctly reflect the
lease revenue as the payments fall due is as
follows: 1983 revenues are decreased from
\$2,654,033.00 to \$372,483.00 and tax decreases from
\$12,845.52 to \$1,802.82, net change in revenue is a
decrease of \$2,281,550.00 and a decrease in tax of
\$11,042.70; 1984 revenues increase \$666,390 and tax
increases \$3,225.33; 1985 revenue increases
\$121,500.00 and tax increases \$588.06. The net
effect in tax is a decrease of \$7,229.31 (see note
#4).

[Petition paragraphed for reading ease.]

ISSUE:

The sole issue before us is the correct timing of
manufacturing tax due on the remaining untaxed value of

tangible personal property originally manufactured in Washington and then leased out-of-state, when the taxpayer has moved out-of-state.

DISCUSSION:

RCW 82.04.240 imposes the Manufacturing classification of business and occupation tax measured by the "value of the products" manufactured.

RCW 82.04.450 provides that the "value of products" manufactured shall be determined by the gross proceeds for the "sale" thereof.

RCW 82.04.040 defines the term "sale" to include renting or leasing. Also the Supreme Court of Washington State has ruled that leases or rentals of tangible personal property constitute a services of consecutive individual sales of such property for excise tax purposes. See Gandy v. State, 57 W.2d 690 (1961).

Moreover, WAC 458-20-112 implements the foregoing statutes and provides the method for determining the "value of Products" under certain circumstances. When, as here, products are transported out of the state without prior sale, the value of products shall correspond as nearly as possible to the gross proceeds from other sales in this state. Clearly this rule contemplates what the measure of tax must be for Manufacturing business tax because it is the only business tax which can apply to goods manufactured here and sold or rented outside this state.

There is simply no provision or contemplation of law within the Revenue Act for distinguishing the Manufacturing tax measure based upon whether the property is sold outright outside this state or leased outside this state. In either instance the tax measure is gross proceeds. In the case before us, assuming the taxpayer's continuing contacts with this state, the appropriate tax measure is the gross proceeds from out-of-state leases of tangible personal property.¹

¹ In passing, we note that the ultimate effect from using continuing rental payments as the tax measure might ultimately result in a greater tax burden than a one-time tax on the property's actual fair market value following manufacture. That is, the gross income from an out-of-state rental will presumably

[1] However, when a taxpayer manufactures equipment in this state for lease out of state, but then subsequently removes itself from the state, that taxpayer will be required to continue to report the manufacturing tax measured by the lease payments as long as this state maintains any taxing jurisdiction over it. If jurisdiction over the taxpayer is to cease before the taxpayer has paid manufacturing tax on a measure at least equalling the product's "cost of production," the taxpayer will owe manufacturing tax on the balance of that measure. Although this is a situation which was clearly not contemplated by statutory law, the legislature could not have intended that the manufacturing activity itself escape its fair measure of tax.

In this case, the taxpayer moved from the state of Washington before manufacturing tax was paid on a measure equalling the cost of the vessels which had been rented out-of-state. The taxpayer, however, still leases tangible personal property in the state of Washington, and will thus remain subject to this state's taxing jurisdiction. Accordingly, the taxpayer will be permitted to continue paying manufacturing tax on the value of the vessels at issue as lease payments are received. Should all taxing jurisdiction cease, the taxpayer will owe manufacturing tax on a measure equalling the balance of the product's "cost of production."

DECISION AND DISPOSITION:

The taxpayer's petition is granted. The Audit Section will issue a new assessment after completing a review of the factual matters which have already been referred to it, and issue a new assessment, payment of which will be due on the date thereon.

DATED this 20th day of October 1989.

exceed its capitalized value. Nonetheless, this is the proper tax reporting measure under the law.