Cite as Det. No. 00-106, 20 WTD 84 (2001)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Ruling of	)	D E T E R M I N A T I O N
	)	
	)	No. 00-106
. . .	)	
	)	Registration No. . . .
	)	Appeal of Ruling

[1] RULE 111; RULE 122; RULE 159; RULE 160; RCW 82.04.050; RCW 82.04.213; RCW 82.04.120: WHOLESALING B&O TAX -- SALES OF SPRAY TO FARMERS -- FARMER DEFINED. Sales of spray materials to farmers for the purpose of producing for sale any agricultural product are classified as wholesale sales. However, if a person uses agricultural products as ingredients in a manufacturing process, the person does not qualify as a farmer. A person will qualify as a farmer, provided: 1) the person grows or produces an agricultural product on the person's own land or land in which the person has a present right of possession; and 2) the person does not use such products as ingredients in a manufacturing process (however packing such products is not considered to be manufacturing).

[2] RULE 122; RCW 82.04.050(8): SALES OF CHEMICAL SPRAYS FOR THE POSTHARVEST TREATMENT OF FRUIT – SALES TAX – USE TAX – DEDUCTION --POTATOES. The exception from the definition of a retail sale set forth in RCW 82.04.050(3) applies to sales of spray for *fruit* and not *vegetables* As such, it does not apply to sales of spray for potatoes.

[3] RULE 102; RULE 113; RCW 82.04.050: SALES TAX – USE TAX – DEDUCTION --CHEMICAL USED IN PROCESSING – SPRAY MATERIALS. Even if spray materials qualified as a "chemical" for purposes of the exemption, in this case their use appears to occur prior to any processing taking place because the potatoes are sprayed at the time of harvest, when they are put into storage.

[4] RULE 115; RCW 82.08; RCW 82.12.0311; RCW 82.04.4287; RCW 82.08.0311; RCW 82.12.0311; SALES TAX – USE TAX –DEDUCTION -- SPRAY MATERIALS – PACKING MATERIALS. The definition of "packing materials" does not encompass spray materials. The definition of packing

> materials is limited to "materials in which tangible personal property may be contained or protected within a container, for transportation or delivery to a purchaser." Because the spray materials do not contain or protect the potatoes, nor are they used for transportation or delivery, spray materials do not qualify for the deduction

NATURE OF ACTION:

A dealer and applicator of chemicals used in agriculture appeals a ruling that its provision of spray materials is subject to service B&O tax and that its purchase or use of such materials is subject to retail sales or use tax.[1]

FACTS:

C. Pree, A.L.J. –The taxpayer, . . ., is a licensed dealer and applicator of chemicals used in agriculture. Its customers include farmers, packing sheds, and potato processors. The taxpayer either sells its chemicals to its customers (and the customers themselves apply the chemicals) or the taxpayer itself applies the chemicals. Only the latter transactions are at issue in this appeal. When the taxpayer applies the chemicals, it segregates the charge for application of the chemicals from the charge for the chemicals.

On April 21, 1999, the taxpayer requested a ruling from the Taxpayer Information and Education Division ("TI&E") of the Department of Revenue. In the ruling request, the taxpayer stated:

> [In prior rulings, the Department] indicated that [the taxpayer is] taxable under the service & other activities B&O classification on sales to farmers and packing sheds, and [it] must pay sales or use tax on the chemicals [it] purchases[s]. . . .
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> Since [the taxpayer] segregates the charge for chemicals and the charge for application . . . [its] situation would parallel the example cited in WAC 458-20-209 paragraph (5)(c). The charge for the application would be reported under the service B&O tax classification. The charge for the sale of the chemicals would be reported under the wholesaling B&O classification, provided that [the taxpayer] obtains a resale certificate from its farmer customers. No sales tax is required to be collected from the customer. The purchase of the chemical is a purchase for resale and is not subject to retail sales tax or use tax.
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> For sales to packing sheds, since the application charge is segregated from the chemical charge, the application would be reported under the service B&O tax classification, and the sale of the chemical would be reported under the wholesaling classification, provided that [the taxpayer] obtains a resale certificate from the packing shed. No sales tax is required to be collected under WAC 458-20-115(3)(d)(i) which refers to the statutory

[1] Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

> exemptions for persons performing packing of fresh perishable horticultural products for the grower. The purchase of the chemical is a purchase for resale and is not subject to retail sales or use tax.

On April 29, 1999, TI&E responded to the taxpayer's request, ruling that when the taxpayer sells sprout inhibitor spray to its customers (along with the application services), other than farmers, and such spray is separately invoiced in the sales to the customers, the taxpayer is liable for service B&O tax on such receipts. Further, TI&E ruled, when the taxpayer purchases the spray to perform spray services for non-farmers, it must pay sales or use tax. The ruling quoted WAC 458-20-209 (Rule 209) and explained:

> It is clear that **when [the taxpayer] performs its spray service for farmers**, rule 209 applies. That is, **if the charges are segregated**, the charge for spray materials are taxable under wholesaling B&O tax (with a resale certificate from the farmer) and the charges for labor are taxable under service B&O tax. In this case [the taxpayer] does not owe tax on the materials and is not required to collect tax from the farmers.
>
> However, **packing sheds and potato processors are not defined as farmers.** In addition, **post harvest activities performed by or for persons not defined as farmers,** do not qualify as horticultural services. Horticultural cultivation is caring for growing agricultural products. Accordingly, when [the taxpayer] performs its spray services for **packing sheds and potato processors**, its total charge is taxable under service B&O tax[,] and [the taxpayer] is considered the consumer of the spray materials. [The taxpayer] is not allowed to bifurcate its charge between spray materials and labor with respect to the taxation of the activity. [The taxpayer] may not accept a resale certificate from these customers for relief from its sales or use tax liability on the materials.

(Emphasis original.) In its appeal of the ruling, the taxpayer argues that TI&E's ruling is "contrary to the intent of rules WAC 458-20-122, 458-20-209, 458-20-113, and other related rules." The taxpayer explains:

> [TI&E's] ruling attempts to narrow and limit the scope of the definition of farming and horticultural services. It focuses on who the person the farming or horticultural services activities are performed for, instead of the farming or horticultural activities themselves, as being the basis for the wholesale treatment. By putting emphasis on the one word, 'cultivation' contained in WAC 458-20-209, you remove it from its context and change the meaning of the phrase in which it is contained. The point is, by taking the word out of its context you are viewing the meaning of farming and horticultural services more narrowly. The phrase also includes the words " . . . related to cultivation." The work of a farmer and the activity of farming clearly extend from pre-field cultivation to the final disposition of the crop.
>
> This is true from its general meaning and also is clear from the context of the above . . . rules. WAC 458-20-102, Paragraph 4(g), makes it clear that sale[s] of feed, seed, seedlings, fertilizer, spray materials or agents for enhanced pollination, including insects

such as bees, used by a farmer for producing for sale any agricultural product is considered a sale at wholesale. The definition of "producing for sale" includes all farming activities, starting at pre-cultivation and ending at the ultimate disposition of the crop. WAC 458-20-122, relating to sales to farmers, adds the restriction that to qualify for wholesale treatment, the sale of the spray material must be invoiced separately from the service.

We believe there are several situations which are part of [the taxpayer's] normal activity to which [the TI&E] ruling erroneously applies use tax.

Situation 1 – Sales of spray applied in a custom, fresh-pack potato operation. In this case, the fresh-pack operation sorts, washes and packages the farmer's potatoes in bags and boxes. Prior to packaging, the potatoes are treated with sprout inhibitor to keep them from rotting and to enhance and preserve quality. The packer then sells and ships the potatoes, collects the money and remits it to the farmer less its sales commission and charges for washing, packing and sprout inhibiting the potatoes. In this situation, the packing company custom packs the potatoes owned by the farmer. The owner of the potatoes is the farmer. He has the risk of loss on the potatoes. He receives the net amount after the packing charges are posted back to him. It is not uncommon in poor years for the farmer to actually have to pay the processor's charges posted to his account because the price of potatoes was not sufficient to pay them. One of these charges is the sprout inhibitor charge. In this situation, the sprout inhibitor is merely a part of custom packing service[s] provided to the farmer. The custom sprout inhibitor company is acting together with the packer to assist the farmer in his farming activity.

Situation 2 – [TI&E's ruling] erroneously applies use tax to sprout inhibitor applied to potatoes by or for farmers under processors' grower storage contracts. These contracts provide that the grower deliver the crops grown under such contracts to a storage facility until the processor (i.e., french fry processor) removes the potatoes for its use in making french fries or hashbrowns. The storage facility is either owned or rented by the farmer. The potatoes are sprout inhibited at the time the potatoes are harvested and delivered to the storage. The cost of the sprout inhibitor is paid directly by the farmer in some cases; or it is paid by the french fry processor, who charges the sprout inhibitor cost back to the farmer. Under these contracts, the farmer is at risk with regard to the crop until the processor removes the crop from the storage. He is paid for the usable potato based on processor grading procedures. Under the storage contract, if the potatoes are rotten when the processor comes to remove them, the farmer gets paid nothing, and the farmer has the expense of getting rid of the rotten potatoes. Under this circumstance, sprout inhibitor applied to the potatoes is a charge for spray used "by a farmer for producing for sale an agricultural product." Again, this is clearly defined in WAC 458-20-102, under resale certificates as a wholesale sale. It is also defined under WAC 458-20-209 as spraying performed for a farmer.

> Situation 3 – [TI&E's ruling] erroneously applies use tax to the sprout inhibitor applied to potatoes for the processor who grows the potatoes. In this situation, the processor is the farmer to which WAC 458-20-209 applies. Again, sales of sprout inhibitor to the farmer processor in connection with sprout inhibiting the potatoes grown by the farmer processor is not subject [to] use or sales tax.
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> Situation 4 – [TI&E's ruling] erroneously applies use tax to the situation in which sprout inhibitor is applied to potatoes after being purchased by the processor. Again WAC 458-20-102 indicates this is a sale at wholesale. Paragraph 4(b) defines situations when a buyer may issue a resale certificate to include property to be used as an ingredient or component part of a new article of tangible personal property to be produced for sale, or paragraph (c), a chemical to be used in processing an article to be produced for sale. This refers to WAC 458-20-113, related to chemicals used for processing. The imposition of use tax on the sprout inhibitor is a double tax on the french fries or hashbrowns sold at McDonalds for example. The first tax is on the sprout inhibitor, a component added to the french fry during processing and the second tax is on the ultimate sale to the buyer of the french fry.
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> Another indication of the law's intent not to tax sprays used in processing is found in the clear example contained in WAC 458-20-122 paragraph 3(a), Wholesaling. Wholesaling includes "sales of chemical sprays or washes to persons for the purpose of post-harvest treatment of fruit for the prevention of scald, fungus, mold or decay." It is clear that this rule exempts the sale of the spray materials needed to prevent rot of fruit during the post-harvest processing of the fruit. When taken in the context of the broader rule 458-20-102, this exemption also applies to sprout inhibitor for potatoes, which serves the same purpose. It prevents potatoes from rotting.

(Emphasis the taxpayer's.)

In summary, the taxpayer and TI&E agree that where the taxpayer performs its spray services for a farmer, the taxpayer's charges for applying the spray materials are subject to tax under the service B&O tax classification.[2] Further, the taxpayer and TI&E agree that the taxpayer's segregated charges for providing the spray materials to farmers are subject to wholesaling B&O tax, and the taxpayer is not liable for retail sales or use tax on its purchase or use of such materials (provided the taxpayer takes a resale certificate from the farmer).[3]

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[2] WAC 458-20-209 (Rule 209) provides:

> Persons performing horticultural services for farmers are generally subject to the service and other business activities B&O tax upon the gross proceeds.

[3] Rule 209 provides:

> [I]f the person providing horticultural services also sells tangible personal property for a separate and distinct charge, the charge made for the tangible personal property will be subject to either the wholesaling or retailing B&O tax, depending on the nature of the sale.

Further, the taxpayer and TI&E agree that the taxpayer's charges for applying the spray are subject to subject to service B&O tax regardless of whether the person for whom the services are performed qualifies as a farmer.

However, the taxpayer and TI&E disagree regarding which situations involve the provision of spray services to a farmer. As indicated in the "situations" set forth above, the taxpayer interprets the term "farmer" more broadly than does TI&E. Further, the taxpayer argues that, even where it performs these services for persons who do not qualify as "farmers," the spray materials qualify as a chemical used in processing under WAC 458-20-113 (Rule 113). In addition, the taxpayer argues that the exemption set forth in WAC 458-20-122 (Rule 122), regarding sprays used for the treatment of fruit implies that the use of spray materials with respect to potatoes is similarly exempt. Finally, the taxpayer argues that the spray materials qualify as sales of packing materials under WAC 458-20-115 (Rule 115).

Thus, the taxpayer asserts that its sales of spray materials in the four situations set forth above qualify as sales at wholesale, and it is entitled to purchase and use the spray materials without payment of sales or use tax. TI&E, on the other hand, ruled that none of the four situations qualifies as a wholesale situation, and the taxpayer is, therefore, liable for sales or use tax on its purchase or use of the spray materials.

ISSUES:

1. Whether the taxpayer is performing its spray services for a "farmer" when it provides such services:
   - To a packing operation,
   - Under a processor's grower storage contract,
   - To a processor/grower, or
   - To a processor after its purchase of the potatoes.
2. Whether the specific exception to the definition of "retail sale" for spray materials for fruit supports the taxpayer's argument that its purchase or use of spray materials for potatoes is similarly exempt from retail sales or use tax.
3. If the taxpayer provides it services to a person who does not qualify as a farmer, whether the taxpayer's purchase or use of spray materials is exempt from retail sales or use tax as "chemicals used in processing."
4. If the taxpayer provides its services to a person who does not qualify as a farmer, whether taxpayer's purchase or use of spray materials is exempt from retail sales or use tax as packing materials.

DISCUSSION:

1. Whether the taxpayer performed its spray services for farmers. The first issue is whether the taxpayer sold its spray materials to farmers. Absent the availability of the exemptions discussed below in sections three and four, resolution of this issue will dictate whether the

taxpayer's sales of spray materials are subject to wholesaling B&O tax (and its purchase or use of such materials therefore exempt from retail sales or use tax), as the taxpayer contends, or whether the taxpayer's sales of spray materials are subject to service B&O tax (and therefore its purchase or use of such materials subject to retail sales or use tax), as TI&E contends.[4]
RCW 82.04.050(8) provides in pertinent part as follows:

> The term ["retail sale"] shall . . . not include . . . sales of. . . spray materials to: . . . farmers for the purpose of producing for sale any agricultural product. . . .[5]

(Footnote added.) WAC 458-20-122 (Rule 122).explains: "Sales to farmers of . . . spray materials . . . for the purpose of producing an agricultural product for wholesale or retail sale" are subject to wholesaling B&O tax."[6]

RCW 82.04.213(2) defines "farmer" as follows:

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[4] RCW 82.04.270 imposes the B&O tax under the wholesaling classification with respect to persons engaged in the business of making sales at wholesale. RCW 82.04.290 imposes the B&O under the service classification with respect to persons "engaging within this state in any business activity other than or in addition to those enumerated" in other sections of RCW 82.04.

RCW 82.08.020 imposes the retail sales tax with respect to purchases of tangible personal property at retail. Generally, RCW 82.12.020 imposes the use tax with respect to the use of property purchased at retail, without payment of retail sales tax. Retail sales tax applies to sales to persons engaged in any business classified under the service classification. See RCW 82.04.050; Rule 209. However, neither retail sales tax nor use tax applies to the purchase or use of property for resale, without intervening use. See RCW 82.04.060. Rule 102 explains that all sales are treated as retail sales unless the seller takes from the buyer a properly executed resale certificate. Examples of sales that are not at retail include chemicals to be used in processing an article to be produced for sale and spray materials for use by a farmer for producing for sale any agricultural product. Rules 102 and 122.

[5] There is no dispute that potatoes are an "agricultural product." See RCW 82.04.213(1) ("'Agricultural product' means any product of plant cultivation . . . including, but not limited to: A product of horticulture.")

Neither the taxpayer nor TI&E question whether the sprout inhibitor spray is a "spray material," and we have insufficient facts to make an independent determination of this issue. Thus, for purposes of this ruling, it is assumed that the sprout inhibitor spray qualifies as a spray material. See WAC 458-20-122(2)(d) ("'Spray materials' means any substance or mixture of substances in liquid, powder, granular, dry flowable, or gaseous form, which is intended to prevent, destroy, control, repel, or mitigate any insect, rodent, nematode, mollusk, fungus, weed, and any other form of plant or animal life which is normally considered to be a pest. . . . 'Spray materials' also includes substances which act as plant regulators, defoliants, desiccants, or spray adjuvants.")

[6] Initially, we note that the taxpayer argues that TI&E erroneously "focuses on who the person the farming or horticultural services activities are performed for, instead of the farming or horticultural activities themselves, as being the basis for the wholesale treatment." However, we note that the statutes and rule are clear in their requirement that the sale be to a *farmer* for the sale of spray materials to qualify as a wholesale sale. As such, we disagree with the taxpayer's argument that TI&E erroneously "focuses on who the person the farming or horticultural services activities are performed for."

> "Farmer" means any person engaged in the business of growing or producing, upon the person's own lands or upon the lands in which the person has a present right of possession, any agricultural product whatsoever for sale. "Farmer" does not include a person using such products as ingredients in a manufacturing process . . . .

Thus, if a person uses agricultural products as ingredients in a manufacturing process, the person does not qualify as a farmer. RCW 82.04.120 defines manufacturing as follows:

> "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. . . .
>
> "To manufacture" shall not include: . . . the growing, harvesting, or producing of agricultural products; or packing of agricultural products, including sorting, washing, rinsing, grading, waxing, treating with fungicide, packaging, chilling, or placing in controlled atmospheric storage.

Thus, pursuant to the above statutes and rule, a person will qualify as a farmer, provided: 1) the person grows or produces an agricultural product on the person's own land or land in which the person has a present right of possession; and 2) the person does not use such products as ingredients in a manufacturing process (however packing such products is not considered to be manufacturing). Thus, we will apply these requirements to the four situations the taxpayer presented.

a. Packing operations. As described by the taxpayer, the packing operation sorts, washes and packages the farmer's potatoes in bags and boxes. The spray is applied prior to packaging. The taxpayer notes that the packing operation sells the potatoes, collects the money, and remits it to the farmer less its sales commission and charges for washing, packing and spraying the potatoes. Thus, the taxpayer argues, the packing company custom packs the potatoes owned by the farmer, and the farmer has the risk of loss on the potatoes. The taxpayer concludes that the spray service is "merely a part of custom packing service[s] provided to the farmer."

The packing operation does not qualify as a farmer because the packing operation did not grow the potatoes on its own land (or land in which it had a present right of possession); the farmer is the person who grew the potatoes. However, if the packing operation purchased the spray materials and services as an agent of the farmer, those sales would qualify as a sale to a farmer. See WAC 458-20-111 (Rule 111); WAC 458-20-159 (Rule 159); WAC 458-20-160 (Rule 160) regarding the requirements for agency status. Thus, if the packing operation purchased the spray services solely as an agent of the farmer, the taxpayer's charges for the spray materials would be subject to wholesaling B&O tax (provided the taxpayer receives a resale certificate), and the taxpayer would not be liable for retail sales tax or use tax on its purchase or use of the spray materials.

On the other hand, absent the availability of another exemption, if the packing operation is not an agent of the farmer, the taxpayer's provision of the spray materials would properly be subject to tax under the service classification, and the taxpayer would be liable for retail sales or use tax on its purchase or use of such materials because the sales would not qualify as sales to a farmer.

b. Processors' grower storage contracts. As described by the taxpayer, these contracts require the farmer to deliver the potatoes grown under such contracts to a storage facility, owned or rented by the farmer, where they are held until the processor uses the potatoes in making french fries or hashbrowns. According to the taxpayer, the potatoes are sprayed when they are harvested and delivered into storage. The taxpayer explains that the cost of the spray is paid either directly by the farmer or by the processor, who then charges the cost back to the farmer. The taxpayer further explains that under these contracts, the farmer is at risk with regard to the potatoes until the processor removes the potatoes from storage.

We note that it appears from the taxpayer's description of these contracts that the farmer is the owner of the potatoes at the time the spray is applied and that the processor is the owner of the potatoes at the time they are processed. If this is the case, the taxpayer's sales of spray would qualify as sales to a farmer because the service would be provided for a person who grew the potatoes, and that person does not use the potatoes in a manufacturing operation. In this case; the taxpayer would be liable for wholesaling B&O tax on its receipts from providing the spray materials, but would not be liable for retail sales tax or use tax on its purchase or use of the spray materials (provided it obtains a resale certificate.

On the other hand, if the farmer is the owner of the potatoes at the time they are processed, the farmer would not qualify as a farmer (for purposes of the issue addressed in this determination) because the farmer would have used the agricultural products in a manufacturing process, as will be discussed further below. A farmer's use of an agricultural product in a manufacturing process disqualifies the farmer from such definition for Washington tax purposes. See RCW 82.04.213; RCW 82.04.120, discussed above. Similarly, if the processor owns the potatoes at the time they are sprayed, the sales would not qualify as sales to a farmer because the processor does not grow the potatoes and because (as will be discussed below) the processor uses the potatoes in a manufacturing operation. Under these circumstances, the taxpayer's receipts from providing the spray materials would be subject to service B&O tax, and the taxpayer would be liable for retail sales or use tax on its purchase or use of the materials (provided another exemption is not available).

c. Processor/growers. According to the taxpayer, these transactions involve sales to processors, who also grow the potatoes. The taxpayer argues that the processor is the farmer. Provided the processor grows the potatoes on its own land (or land in which it has a present interest), the first requirement for qualification as a farmer is met. See RCW 82.04.213. With respect to the second requirement, the growers will qualify as farmers provided they do not use the potatoes in a manufacturing process. See RCW 82.04.120; RCW 82.04.213. In this case, the taxpayer's sales of spray materials to them will qualify as wholesale sales (provided the taxpayer

takes a resale certificate), and the taxpayer will not be liable for sales or use tax on its purchase or use of those materials.

However, if the grower's processing activities involve "manufacturing" processes, the sales of spray materials to these growers will not qualify as sales to farmers; the taxpayer's charges for the spray materials will be taxed under the service classification, and the taxpayer will be liable for sales or use tax on its purchase or use of the spray materials (unless another exemption applies).

The ruling request did not recite specifically what activities the processor performs with respect to the potatoes. As noted above, RCW 82.04.120 provides that manufacturing does not include "the growing, harvesting, or producing of agricultural products; or packing of agricultural products, including sorting, washing, rinsing, grading, waxing, treating with fungicide, packaging, chilling, or placing in controlled atmospheric storage." Thus, if the grower/processor engages only in the above activities, it would qualify as a farmer.

On the other hand, if the grower/processor makes hashbrowns or french fries with the potatoes it would be engaging in a manufacturing activity that disqualifies it from the definition of "farmer." We note that RCW 82.04.120 broadly defines manufacturing to include "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." This definition has been applied in a number of different factual situations, where the courts have concluded that the taxpayers' activities constituted manufacturing. See, e.g., Continental Coffee Co. v. State, 66 Wn.2d 194, 384 P.2d 862 (1965)(changing green coffee beans to a roasted and blended coffee); McDonnell & McDonnell v. State, 62 Wn.2d 553, 383 P.2d 905 (1963)(splitting peas); Bornstein Sea Foods, Inc. v. State, 60 Wa.2d 169, 373 P.2d 483 (1962)(cutting whole fish into fish fillets); Stokely-Van Camp, Inc. v. State, 50 Wn.2d 492 312 P.2d 816 (1957)(freezing food); J & J Dunbar & Co. v. State, 40 Wn.2d 763, 245 P.2d 1164 (1952)(screening and filtering raw whiskey). See also WAC 458-20-136 (Rule 136)("[Manufacturing] 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 . . . .").

Under the statutory definition and case law, it is clear that changing whole potatoes into hashbrowns or french fries constitutes manufacturing. Such a process involves the application of labor to the potatoes so that as a result thereof a new, different, or useful produce is produced for sale. We note that the changes to the potatoes in these processes are at least as significant as splitting peas and making fish fillets, both of which were deemed by the courts to constitute manufacturing.

d. Processors. Processors are the final type of customer to whom the taxpayer sells its spray services. Because these processors do not grow the potatoes, they do not qualify as farmers. As such, unless another exemption applies, the taxpayer is liable for service B&O tax

on its receipts from these customers, and it must pay retail sales or use tax on its purchase or use of spray materials used in performing these contracts.

2. Whether the specific exemption for spray materials for fruit supports the taxpayer's argument that spray materials for potatoes are exempt.

RCW 82.04.050(8) provides the following exception from the definition of "retail sale":

> (8) The term ["retail sale"] shall . . . not include sales of chemical sprays or washes to persons for the purpose of postharvest treatment of fruit for the prevention of scald, fungus, mold, or decay, nor shall it include sales of feed, seed, seedlings, fertilizer, agents for enhanced pollination including insects such as bees, and spray materials to: (a) Persons who participate in the federal conservation reserve program, the environmental quality incentives program, the wetlands reserve program, and the wildlife habitat incentives program, or their successors administered by the United States department of agriculture; (b) farmers for the purpose of producing for sale any agricultural product; and (c) farmers acting under cooperative habitat development or access contracts with an organization exempt from federal income tax under 26 U.S.C. Sec. 501(c)(3) or the Washington state department of fish and wildlife to produce or improve wildlife habitat on land that the farmer owns or leases.

(Emphasis added.) See also Rule 122. The taxpayer argues that the portion of the statute highlighted above (and repeated in Rule 122) is "another indication of the law's intent not to tax sprays used in processing" regardless of whether the person for whom the services are provided is a farmer. We disagree with this broad statement. As explained above, the statutes and rules make it clear that the taxpayer's sales of spray materials to farmers (who provide resale certificates) qualify as wholesale sales. However, although we note that under the portion of the statute highlighted above, the exception from the definition of a retail sale applies to sales of spray to *persons,* without limiting application to *farmers* only, this exception applies only to spray for *fruit* and not *vegetables.*[7]

The highlighted portion of the statute has been included as an exception to the definition of "retail sale" since 1967. *See* Laws of 1967 Ex. Sess. Ch. 149. Additional agricultural exceptions were added in subsequent years. In 1993, the word "farmers" was substituted for "persons" regarding "any agricultural product," while the word "persons" remained in the highlighted portion. *See* Laws of 1993, 1st Sp. Sess., Ch. 25, sec. 301. It is evident, particularly with the 1993 amendment, that the drafters realized the distinction between "farmers" and "persons" and that they intended to have different terms be applied to different exceptions.

The highlighted portion applies to sales of *fruit*; unlike the provision in subsection (b), it does not apply to sales of *any agricultural product.* If the legislature uses certain statutory language in one instance (fruit) and different language in another (any agricultural product), there is a

[7] It is clear that a potato is a vegetable, not a fruit. See, e.g., Webster's Third New International Dictionary (Unabridged) (1993) at p. 1774.

difference in legislative intent. *United Parcel Service, Inc. v. Department of Rev.*, 102 Wn.2d 355, 687 P.2d 186, (1984). As such, contrary to the taxpayer's argument, we find that this statute supports our conclusion (and that of TI&E) that the customer must be a farmer for the sale of spray materials for potatoes to qualify for wholesale treatment (unless another exemption applies).

3. If the taxpayer provides its services to a person who does not meet the definition of a farmer, whether its purchase or use of the spray materials is exempt from retail sales or use tax because the spray materials constitute a "chemical used in processing." The taxpayer argues that, even if its sales are not to farmers, it is not liable for sales or use tax on its purchase or use of the spray materials because they are a "a chemical to be used in processing an article to be produced for sale.

Initially, we note that this exemption is not available with respect to the taxpayer's sales to potato packing operations because the packers do not engage in any manufacturing or processing activities.

RCW 82.04.050 defines "retail sale" as excluding sales to a person who presents a resale certificate and who:

> Purchases for the purpose of consuming the property purchased in producing for sale a new article of tangible personal property or substance, of which such property . . . is a chemical used in processing, when the primary purpose of such chemical is to create a chemical reaction directly through contact with an ingredient of a new article being produced for sale . . . .

See also Rule 102. WAC 458-20-113 (Rule 113) provides:

> (6) "Chemicals used in processing" carries its common restricted meaning in commercial usage. It includes only chemical substances which are used by the purchaser to unite with other chemical substances, present as ingredients or components of the articles or substances being processed, to produce a chemical reaction therewith, as contrasted with merely a physical change therein. A chemical reaction is one in which there takes place a permanent change of certain properties, with the formation of new substances which differ in chemical composition and properties from the substances originally present, and usually differ from them in appearance as well. It is not necessary that all of the new substances which are formed be present in the final completed article or substance which is sold; one or more of such new substances resulting from the chemical reaction may be removed or drawn off in the processing.

We do not have sufficient facts to determine whether the spray materials cause the type of chemical reaction necessary to qualify as a chemical used in processing. However, even if the spray materials qualified as a "chemical" for purposes of the exemption, we note that their use appears to occur prior to any processing taking place. According to the taxpayer, the potatoes are sprayed at the time of harvest, when they are put into storage, and it appears that the storage facility is at a

separate site from the hashbrown or french fry processing site. At this point, the manufacturing process has not begun. See WAC 458-20-13601 (Rule 13601) ("A manufacturing operation begins at the point where the raw materials enter the manufacturing site and ends at the point where the processed material leaves the manufacturing site. 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.") As such, we disagree with the taxpayer's argument that the spray materials qualify as a chemical used in processing. The taxpayer's petition is denied as to this issue.

4. If the taxpayer provides its services to a person who does not qualify as a farmer, whether taxpayer's purchase or use of spray materials is exempt from retail sales or use tax as packing materials. The taxpayer's final argument is that its purchase or use of the spray materials is not subject to retail sales tax or use tax because the taxpayer's sale of the spray materials constitutes the sale of packing materials.

RCW 82.08.0311 provides the following retail sales tax exemption:

> The tax levied by RCW 82.08.020 shall not apply to sales of materials and supplies directly used in the packing of fresh perishable horticultural products by any person entitled to a deduction under RCW 82.04.4287 either as an agent or an independent contractor.

RCW 82.12.0311 provides a similar use tax deduction. The B&O tax deduction under RCW 82.04.4287 referenced in these statutes applies to "amounts derived by any person as compensation for the receiving, washing, sorting, and packing of fresh perishable horticultural products and the material and supplies used therein when performed for the person exempted in RCW 82.04.330, either as agent or as independent contractor."

WAC 458-20-115 (Rule 115) explains that sales of packing materials qualify as sales at wholesale.

However, the rule provides the following definition of "packing materials":

> The term "packing materials" means and includes all boxes, crates, bottles, cans, bags, drums, cartons, wrapping papers, cellophane, twines, gummed tapes, wire, bands, excelsior, waste paper, and all other materials in which tangible personal property may be contained or protected within a container, for transportation or delivery to a purchaser.

The definition of "packing materials" does not encompass the taxpayer's spray materials. We note that the definition of packing materials is limited to "materials in which tangible personal property may be contained or protected within a container, for transportation or delivery to a purchaser." Because the spray materials do not contain or protect the potatoes, nor are they used for transportation or delivery, we conclude that the taxpayer's spray materials do not qualify for the

deductions set forth in RCW 82.08.0311 or 82.12.0311. The taxpayer's petition is denied with respect to this issue.

DECISION AND DISPOSITION:

Taxpayer's petition is granted in part and denied in part. Specifically, with respect to sales to a packing operation, the taxpayer's petition is granted, provided the packing operation meets the requirements to qualify as an agent of the farmer when it purchases the spray. If the packing operation does not qualify as an agent of the farmer, the taxpayer's petition is denied. With respect to processors' grower storage contracts, the taxpayer's petition is granted, provided the farmer is the owner of the potatoes at the time the spray is applied and the processor is the owner of the potatoes at the time they are processed. If the farmer is the owner of the potatoes at the time they are processed or if the processor owns the potatoes at the time they are sprayed, the taxpayer's petition is denied. With respect to sales to a processor/grower, the taxpayer's petition is granted, provided the processor/grower does not use the potatoes in a manufacturing process. If the processor/grower's processing activities involve manufacturing processes, the taxpayer's petition is denied. The taxpayer's petition is denied with respect to sales to processors, as well as to its arguments that the spray materials qualify as chemicals used in processing or packing materials.

Dated this 9th day of June, 2000.