Cite as Det. No. 93-316, 16 WTD 1 (1993)

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

In the Matter of the Petition For Correction of Assessment	)	D E T E R M I N A T I O N
	)	No. 93-316
. . .	)	Registration No. . . .
	)	FY. . ./Audit No. . . .

RULE 193C: B&O TAX - DEDUCTION - EXPORT - ENTRY INTO EXPORT STREAM. For there to have been "entry into the export stream" and "unbroken continuity of movement" for purposes of the export deduction, any delay in shipping goods must be "reasonable and in furtherance of the intended transportation."

1 RULE 193C: B&O TAX - DEDUCTION - EXPORT - ENTRY INTO EXPORT STREAM - STORAGE. Goods have not entered the export stream - or acquired tax immunity - when they have been delivered to an entity for storage prior to actual overseas shipment to specified buyers.

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:

Petition concerning the applicability of the export deduction to sales of logs to a Washington export company, which further sold them to Japanese buyers, when delivery was made by the taxpayer to the buyer's export packer in this state.[1]

FACTS:

Bauer, A.L.J.-- The taxpayer's business records were audited for the period from January 1, 1988 to December 31, 1991. As a

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

result, an assessment was issued. The taxpayer seeks a correction of this assessment. The taxpayer buys and sells lumber at wholesale. The sales here at issue were made to a single unrelated foreign sales company[2] (hereinafter, "Customer Corp") whose sole purpose was to buy lumber in the United States and resell to purchasers in Japan.

When Customer Corp issued a purchase order to the taxpayer, it described the specific types and amounts of lumber sought. Customer Corp also specified that the lumber (2-by-4's) were to be packed in 216-piece bundles.[3]

The purchase order also stated that delivery was to be made "F.O.B. Dock-[Washington port]." This term implied that the traditional delivery point was alongside the ship, ready for loading. However, Customer Corp's Japanese customers always specified that the lumber could not be shipped in open bulk because they required dry, clean, finished goods. Moreover, lumber could not be shipped in open bulk on container vessels. Therefore, the lumber had to be packaged in containers and then moved to the vessel. Customer Corp and the taxpayer thus used the term "F.O.B. Dock-[Washington port]" to mean delivery at an export packaging facility of a trucking company at a Washington port location (hereinafter, the "export packer").

Customer Corp's purchase order also specified the mark to be placed on the lumber at the mill[4], and provided the stencil to do so. All the lumber in the lot was marked with the same mark. The lumber was packed in the special 216-piece bundles for export. The strapping used for these bundles was also different from the strapping used for domestic shipping. Finally, the bundles were end-painted at the mill, which did not occur in domestic sales.

The mill arranged for shipping the lumber by truck to the export packer at the taxpayer's expense. Per the taxpayer's contracts with Customer Corp, title and risk of loss to the lumber passed from the taxpayer to Customer Corp upon acceptance of delivery by the export packer.

The taxpayer asserts that the sole business activity of the export packer's facility was packaging goods in containers for export. It did such packing at the direction of Customer Corp, which determined, according to the known or anticipated needs of its buyers, whether to break up the lots among different shipments. Single lots would often be broken up into two or more shipments to a single buyer at different locations, or into two or more shipments to Customer Corp's different buyers. Nevertheless, all lumber sold by the taxpayer to Customer Corp and delivered to the export packer was certain to be exported.

The packing for export done by the export packer was a necessary, preliminary part of the export of the lumber. After packing, Customer Corp instructed the export packer when to deliver specific containers to dockside for loading on their designated vessels.

Representative documentation submitted by the taxpayer, which is included in the audit jacket, concerns two deliveries to the export packer:

The first set of documents demonstrates that the taxpayer delivered one lot of lumber to the export packer on April 8, 1991. This lot was further divided by the export company, and portions thereof were included in shipments which were "laden on board" vessels destined for the port at [Port 1], Japan on the following dates:

May 3, 1991 (for ultimate delivery to [Port 2], Japan);

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[2] Although some invoices reflected sales to the export company's corporate parent instead of to the export company, we will, for the sake of this determination, accept the assertion that the sales were made to the export company itself.

[3] This was a special export-sized bundle designed to fit export containers. Domestic shipping, almost without exception, goes either by flat-bed truck in standard bundles that contain 208 pieces or by rail in standard bundles that contain 294 pieces.

[4] The taxpayer purchased all the lumber involved in these sales from the same mill.

June 7, 1991 (for delivery to [Port 3], Japan);
September 8, 1991 (for delivery to [Port 2], Japan); and
September 8, 1991 (for delivery to [Port 3], Japan).

Actual delays in overseas shipment of this original April 8, 1991, delivery by the taxpayer to the export packer thus ranged from 24 days to approximately five months.

A second lot of lumber was delivered to the export packer on January 29, 1991. This lot was further divided and included in shipments which were "laden on board" vessels destined for the port at [Port 1], Japan on the following dates:

February 20, 1991 (for delivery to [Port 4], Japan);
March 17, 1991 (for delivery to [Port 3], Japan); and
April 26, 1991 (delivery to [Port 4], Japan).

Actual delays in overseas shipment of this January 29, 1991, order thus ranged from 22 days to almost three months.

A letter dated November 16, 1992, from Customer Corp provided in support of the taxpayer's appeal states:

At times, when [Customer Corp] issues a purchase order for lumber in the United States, our buyer in Japan has already been identified. At other times, the Japanese buyer is identified later, between the time that [Customer Corp] places the purchase order and the date of shipment to Japan. At other times, the shipment to Japan is made before our ultimate buyer has been identified. . . .

TAXPAYER'S EXCEPTIONS:

The taxpayer argues that its sales to Customer Corp were deductible export sales, citing the following provision of WAC 458-20-193C (Rule 193C):

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 . . . (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. . .

Emphasis the taxpayer's.)

In this case, the taxpayer feels it meets the Rule 193C test because Customer Corp's purchase orders required the taxpayer to deliver the goods to Customer Corp at a trucking company, which specialized as an export packing facility, for packing into an "other vehicle of transportation," and the circumstances surrounding the trucking company's packing operations made it clear that the process of exportation of goods had begun.

The taxpayer argues that the general rule further provides that "there must be an actual entrance of the goods into the export stream." This requirement was satisfied by delivery to the export packer because, once there, the lumber was necessarily packed into containers according to the instructions of Customer Corp, and those instructions were geared to satisfy specific needs of foreign customers. None of the lumber delivered to the export packer was re-bundled for domestic shipment. The process of packing for export by the export packer was an absolutely essential part of the export process, because direct delivery to the vessel would not be acceptable to the vessel owner.

The taxpayer further contends that its documentation regarding its delivery "into the export stream" are in order and satisfy the criteria set out by Rule 193C.

In support of its argument that local delivery of a product to an export packer designated by a local buyer for specialized packing prior to overseas shipment is not an interruption of the export process, the taxpayer has particularly cited two cases: Carrington Co. v. Department of Revenue, 84 Wn.2d 444, 527 P.2d 74 (1974) (hereinafter, "Carrington"), and the California Supreme Court decision Gough Industries, Inc. v. State Board of Equalization, 336 P.2d 161 (1959) (hereinafter, "Gough").

ISSUE:

Whether lumber delivered to an export packer designated by a domestic purchaser constituted placement "into the export stream," when, at the time of such delivery, ultimate overseas buyers or particular overseas destinations had not been established and the packer held the taxpayer's deliveries - or portions thereof - until ultimate overseas buyers, destinations, and packing and shipping instructions could be determined.

DISCUSSION:

Generally, under Rule 193C and applicable case law, a transaction will qualify as an export sale so long as it can be established that at the time of sale there is (1) certainty of export, and (2) actual entrance into the export stream. See Det. No. 87-36, 2 WTD 183 (1986).

It appears, and the Department will concede for purposes of resolving this case that the first element - certainty of export -has been established. The question which then remains is whether the taxpayer placed the lumber into the "export stream" by delivering it to Customer Corp's designated export packer.

As stated in Carrington, on which the taxpayer relies:

Entry into the export stream must be the start of a continuity of movement. . . . Yet the journey may be interrupted if the purpose of the interruption is "reasonable and in furtherance of the intended transportation." . . . The point has been otherwise stated as allowing interruption to "promote the safe or convenient transit" of the goods. . . . In application the following situations have been deemed to be permissible interruptions: (1) holding of logs in a boom in a river to await subsidence of high water, . . . ; (2) shipment to an independent export packer for preparation for ocean travel, . . . ; (3) accumulation and storage for convenient and efficient loading of ships. . . ; Some of these cited cases involved the commerce clause, but the rationale is pertinent here. (Citations omitted, emphasis added.)

Carrington, at 446.

[1] Thus, for there to have been "entry into the export stream" and unbroken continuity of movement for purposes of the export exemption, any delay in shipping goods must be "reasonable and in furtherance of the intended transportation" and "to promote the safe or convenient transit of the goods."

In Carrington, the original purchase orders identified the overseas recipients and the foreign destinations of the goods. In Carrington, the buyer's facility which packed the goods kept them an average of only 7 or 8 days before they were actually loaded on a ship or airlifted overseas, and the longest any equipment remained at the packing facility was 18 days.

Similarly, in Gough[5], original purchase orders designated the ultimate overseas buyers and the respective destinations of the electrical products to be shipped. The goods were delivered to the export packer designated by the buyers along with specific shipping instructions, a required date of export, and a special export number. Ocean transport had already been arranged. The packer merely "packed and crated the goods according to the purchaser's specifications and forwarded them by truck carrier to the ocean carrier, which transported them to Saudi Arabia." The California Supreme Court stated:

The trial court specifically found that the export journey started when the goods left plaintiff's plant in Los Angeles; that it was a continuous journey from Los Angeles to Saudi Arabia; that there was no stoppage in transit or attempt to cause one, or any delay for an unreasonable length of time; that any delay (if any there were) did not break the continuous stream of foreign commerce; and that all packing and crating by the export packer "was an incidental part of the total export journey rather than the primary station of commencing an export journey to Saudi Arabia."

From the foregoing, it appears that; (a) the agreement of sale contemplated shipment of the goods in export, that is, from a seller in the United States to a buyer in a foreign country; (b) from the beginning of the transaction, the goods were committed to go all the way to the foreign country; (c) the movement of the goods had actually started when the tax was sought to be imposed; and (d) the journey was continuous and unbroken by any action or delay taken for a purpose independent of the transportation of the goods.

[5] Gough, being a California case, is not controlling in Washington. We agree with the taxpayer, however, that it is instructive.

Therefore, it is immaterial that the goods were shipped to the packer in Wilmington and there packed for ocean travel, such being incidental and necessary for the safe transportation of the goods . . . . (Emphasis added.)

Unlike the facts in Carrington and Gough, the facts in this case do not favor a finding that a continuous export journey had begun when the taxpayer delivered the lumber to the export packer designated by Customer Corp, or that this delivery was part of a continuous unbroken journey with no delays unrelated to the lumber's safe or convenient transportation.

Of the sales documents available, the taxpayer's invoices did not reflect Customer Corp's ultimate overseas buyers, the specific composition of particular orders to be packed for those foreign customers, actual ultimate destinations (other than the general intent to export to Japan), or arrangements as to overseas transportation. In fact, in many cases, ultimate customer information was unknown at the time of the taxpayer's delivery to the export packer. The export packer in this case routinely held entire lots of lumber - or portions thereof - until Customer Corp actually obtained orders from its own foreign customers or gave it further shipping instructions, in some instances resulting in a delay in further overseas shipment of up to five months. Only on receiving further instructions from Customer Corp could orders be made up in the required amounts, packed, and containerized from entire lots or portions thereof, and export shipments arranged for specific destinations.

Instead, we think the facts and holding of Coast Pacific v. Department of Rev., 105 Wn.2d 912, 719 P.2d 541 (1986) are controlling. In that case, the taxpayers, having standing orders from its overseas customers, delivered logs to a local independent towing company which was under contract to the taxpayers' overseas purchasers. The towing company sorted, rafted, and moved the logs into a fresher-water, protected holding area, primarily near the mouth of the Snohomish River. By agreement, the logs were held by the towing company in storage until they were paid for by the taxpayers' overseas purchasers, at which time they were released for overseas shipment. At no time was there any doubt that all logs in storage were destined for overseas destinations. The court nonetheless held the logs' delivery to the towing company for storage to precede their actual entrance into the export stream. In so holding, the Court noted, "our decision in Carrington Co. v. Department of Rev., supra, does not provide compelling authority for this case." Coast, supra, at 919.

The Coast court further reasoned:

We understand Coast Pacific's argument that these logs were reasonably certain to be exported and that their "final movement" overseas had begun before the logs reached the F.O.B. delivery point. However, courts repeatedly have rejected these grounds for tax immunity. The Sumitomo[6] court specifically responded that "[c]ertainty of export evidenced by financial and contractual relationships does not by itself render goods `exports' before the commencement of their journey abroad." 504 F.2d at 608. . . .

. . . The framers of the import-export clause intended to allow the states to impose sufficient taxes to defray the expenses of providing local services to the importers and exporters of goods. Abamson, State Taxation of Exports: The Stream of Constitutionality,, 54 N.C. L. Rev. 59, 61-62 (1975). In 1949, Justice Frankfurter wrote in Joy Oil Co. v. State Tax Com'n, 337 U.S. 286, 93 L. Ed. 1366, 69 S. Ct. 1075 (1949) that "[t]he Export-Import Clause was meant to confer immunity from local taxation upon property being exported, not to relieve property eventually to be exported from its share of the host of local services." 337 U.S. at 288. Justice Hale of this court agreed:

The billions of dollars worth of goods piled on the docks of the nation's ports, or within nearby warehouses and storage depots, can hardly be said to be exports at that stage of the journey, even though documented for overseas shipment and ultimate delivery. They and the business activities connected with them are at that point still drawing all of the beneficial and protective services of the state and municipality in which they are kept, including those provided by police, firemen, inspectors and all of their equipment and paraphernalia. They have the use of the public streets, highways, utilities and ports. . . . the goods and the transactions affecting them should, therefore, bear their fair share of the taxes imposed upon them or the businesses connected with them to support the state and local services precisely as do all other goods and businesses so taxed within the state.

Carrington Co. v. Department of Rev., 84 Wn.2d at 466-67 (Hale, C.J., dissenting).

Coast, supra, at 920-21.

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[6] Sumitomo Forestry Co. v. Thurston Cy., 504 F.2d 604 (9th Cir. 1974).

[2] The Washington Supreme Court in Coast thus affirmed the trial court's conclusion that Coast Pacific's logs had not entered the export stream - or acquired tax immunity - when they were delivered to the towing company for storage prior to actual shipment.

Based on the documentation and facts presented in this case, we must similarly hold that actual export of the lots of lumber delivered by the taxpayer to Customer Corp's export packer had not begun, since the subsequent delay and storage at the export packer's awaiting further instructions was not merely incidental and necessary for the lumber's safe or convenient transportation.

DECISION AND DISPOSITION:

Taxpayer's petition is denied.

DATED this 30th day of November, 1993.