

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition)	<u>D E T E R M I N A T I O N</u>
For Correction of Assessment of)	
)	No. 96-048
)	
. . .)	Registration No. . . .
)	FY. . ./Audit No. . . .
)	
)	

RULE 660; RCW 82.45.010; and ETB 541.04/45/33.135: REAL ESTATE EXCISE TAX -- SALES OF STANDING TIMBER -- TITLE AND OWNERSHIP -- TRANSFER OF TITLE. When title or ownership to standing timber passes prior to the timber's severance from the land, the sale is subject to real estate excise tax. A landowner's retention of bare legal title to the timber does not otherwise alter the imposition of the tax.

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:

Landowner protests the assessment of real estate excise tax (REET) on the sale of standing timber.¹

FACTS :

Mahan, A.L.J. -- The taxpayers own land in Eastern Washington that contained marketable timber. On October 8, 1994, they entered into a Timber Sale Agreement with a purchaser of the timber. Under the terms of this agreement, the sellers agreed "to

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

sell to Purchaser and Purchaser agrees to buy, under the terms and conditions hereafter stated, merchantable timber" on the property. The taxpayers were paid a deposit by the purchaser and, after the application of the deposit to the timber first cut and removed by the purchaser, they were paid by the board foot following the delivery of logs to a scaling yard. The purchaser was granted the right of ingress and egress from the property and the taxpayers reserved the right to inspect the scales of cutters and of sorting and scaling yards. The agreement further provided that "Title to said timber and forest products from said timber shall remain in seller until paid for by Purchaser."

According to the taxpayers, the purchaser hired a cutting contractor and entered into a contract with a mill for the sale of the logs. The taxpayers were not parties to any contract with the cutting contractor or the mill. The Forest Practices Application, completed by the purchaser, identified the purchaser as the owner of the timber and the taxpayers as the landowner.

According to the taxpayers, they paid business and occupation (B&O) tax on the income received under the Timber Sale Agreement, but they did not pay REET on the sale price. The purchaser also paid the timber tax on their behalf.

Based on the information contained in the Forest Practices Application and the Timber Sale Agreement, the Department of Revenue issued a REET assessment. The taxpayers paid the assessment and filed a timely appeal. In their appeal, they contend that they retained the title to the timber and, as a consequence, they sold a crop, not real estate.

ISSUE:

Whether REET is owed where language in a timber sale contract reserves title in the landowner until after payment is received for the severed timber.

DISCUSSION:

RCW 82.45.060 imposes the REET upon the "sale" of real property. RCW 82.45.010(1) defines the term "sale" to mean:

As used in this chapter the term "sale" shall have its ordinary meaning and shall include any conveyance, grant, assignment, quitclaim, or transfer of the ownership of or title to real property, including standing timber, or any

estate or interest therein for a valuable consideration,

(Emphasis supplied.)

The amount of the tax is based on the selling price. The seller of the property is obligated to pay the tax. RCW 82.45.080.

With respect to the sale of standing timber, the Department adopted WAC 458-61-660 (Rule 660) in 1982. As with the statute, the rule provides that the tax is imposed if the ownership of the timber is transferred while the timber is still standing. Prior to a recent amendment, and during the period of the transaction at issue here, it read in pertinent part:

The application of the real estate excise tax to the sale of timber is based upon whether or not the ownership of the timber transferred while the timber was standing.

(1) The sale of standing timber is a taxable transaction.

(2) The seller's irrevocable agreement to sell timber and pass ownership to it as it is cut is a taxable transaction if the total amount of the sale is specified in the original contract.

(Emphasis supplied.)²

With respect to the liability of landowners for the sale of standing timber, the Department has also promulgated Excise Tax Bulletin 541.04/45/33.135 (ETB 541). It summarizes the tax liability of an owner and purchaser as follows:

The tax liabilities that apply to each party for a sale of standing timber versus a sale of logs are summarized as follows:

	SELLER (Landowner)	PURCHASER (logger/Contractor)
TYPE OF TRANSACTION	PAYS:	PAYS:
I. Sale of standing timber	REET	Timber tax and B&O tax

²We are bound to follow the rules adopted by the Department. Rules promulgated by the Department have the force and effect of law, unless declared invalid by the judgment of a court of record not appealed from. RCW 82.32.300.

II. Sale of logs	Timber tax	B&O Tax
	and B&O tax	

ETB 541 further provides that the liability for the REET depends upon whether ownership and/or title to timber was transferred while the timber was standing. In relevant part it provides:

There are a number of ways in which timber is sold, and the timing of the transfer of ownership and/or title to the timber determines which taxes are due and who is liable for paying them. The two most common sale arrangements and the taxes that apply in each situation are described below:

(1) Sale of Standing timber (stumpage sales): Title to the timber transfers to the buyer before harvesting takes place.

(Emphasis supplied.)

In general, contracts of the type at issue here, also referred to as stumpage contracts or cutting rights contracts, have been found to involve a transfer of ownership or title. This is true even if the landowner retains bare legal title pending completion of the contract. See Det. No. 92-249ER, 13 WTD 138 (1993). As we explained in that determination:

In a contract for the sale of timber, the purchaser becomes the beneficial owner of the timber even though the purchaser has not paid the whole purchase price. The seller holds the title as trustee to be conveyed to the purchaser upon compliance with the terms of the contract.

Legal title does not have to be transferred in order for the timber buyer to be recognized as the owner of the timber. As explained in Wasser & Winters Co. v. Jefferson Cty., 84 Wn.2d 597, 599, 528 P.2d 471 (1974):

We have identified the chief incidents of ownership of property as the right to its possession, use and enjoyment and to sell or otherwise dispose of it according to the will of the owner the person assessed need not have a perfect and unencumbered title to the property but only that he should be vested with the apparent legal title, or with the possession coupled with such claims and evidence of ownership as will justify the assumption that he is the owner.

In this case, before the timber was severed from the land, all incidents of ownership were transferred to the buyer except for bare legal title. For example, the purchaser appeared to have the full right to possess and to sell or otherwise dispose of the timber according to its will, as shown by the cutting and sale contracts. It also represented itself as the owner of the timber in the Forest Practices Application. Under such circumstances, REET was due upon the transfer of such ownership rights.

This holding is also consistent with this state's Uniform Commercial Code (UCC), RCW 62A.1-101, et seq. Under most circumstances, a contract for the sale of timber is governed by the UCC. Syrov v. Alpine Resources, Inc., 122 Wn.2d 544, 549, 859 P.2d 51 (1993). Section 2-107 of the UCC, in relevant part, provides:

(2) A contract for the sale apart from the land . . . of timber to be cut is a contract for the sale of goods within this Article whether the subject matter is to be severed by the buyer or by the seller even though it forms part of the realty at the time of contracting, and the parties can by identification effect a present sale before severance.

(3) The provisions of this section are subject to any third party rights provided by law relating to realty records, and the contract for sale may be executed and recorded as a document transferring an interest in land and shall then constitute notice to third parties of the buyer's rights under the contract for sale.

RCW 62.2-107. Although the UCC is not determinative of what constitutes a transfer of real property for REET purposes (See Det. No. 90-372, 10 WTD 159 (1990)), we recognize that it generally describes the rights of the parties to a timber sale contract.

The fact that a party retains legal title is not conclusive evidence that the party remained the owner of the property as well. Under the UCC, the reservation of title by the seller does not prohibit the vesting of title in the buyer, but only reserves a security interest in the property. RCW 62A.2-401 (the "retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest"); In re R & R Contracting, Inc., 4 B.R. 626, 632 (E.D. Wash. 1986).

Under the facts of this case, the taxpayers' reservation of a title interest had the effect of only a reservation of a security interest in the timber sold to the purchaser. In all other respects the ownership of the standing timber was transferred prior to the severance of the timber from the land, and the landowner became liable for the REET at the time of the transfer.

DECISION AND DISPOSITION:

The taxpayers' petition is denied. This decision is without prejudice to the taxpayers' timely request for a refund of B&O tax, should such a request be appropriate.

DATED this 26th day of March, 1996.