

Cite as Det. No. 99-325, 19 WTD 515 (2000)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of)	<u>D E T E R M I N A T I O N</u>
Assessment of)	
)	No. 99-325
)	
...)	Registration No. . . .
)	FY. . . /Audit No. . . .
)	

[1] RULE 135; RULE 13601; RCW 82.08.02565; RCW 82.12.02565: MANUFACTURING EQUIPMENT AND MACHINERY EXEMPTION – EXTRACTING. Machinery and equipment used for the crushing, and/or blending of rock, sand, stone, gravel, or ore is machinery and equipment used in a manufacturing operation. See RCW 82.04.100. Machinery and equipment used in a manufacturing operation is exempt from retail sales tax if it meets the “used directly” and “majority use” requirements.

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:

The taxpayer protests use tax assessment on machinery and equipment used in its [rock crushing] activities.¹

ISSUE:

Whether [machinery and equipment] used in the taxpayer’s [rock crushing] business is exempt from retail sales tax as machinery and equipment used directly in a manufacturing operation.

FACTS:

S. Thomas, A.L.J. -- The taxpayer, . . . , is engaged in the business of operating a sand and gravel pit in Washington. The taxpayer’s activities involve extracting sand and aggregate rock from the pit, and manufacturing concrete. The taxpayer separates and sells, wholesale and retail,

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

materials extracted from the ground. The taxpayer also operates a concrete batch plant on site where concrete is loaded into concrete trucks and delivered to construction sites. The Audit Division examined the taxpayer's books and records for the period January 1, 1994 through December 31, 1997.

A tax assessment, Document No. FY. . . , was issued as a result of this audit. Document No. FY. . . included use tax assessed on machinery and equipment which at the time of the audit was deemed to have been used in an extracting operation. The taxpayer protests the assessment of use tax on purchases of M & E claiming the M & E is used in a manufacturing and, therefore, the M & E is exempt from retail sales tax and/or use tax.

The taxpayer protests the Audit Division's conclusion that the majority of its sales receipts were from the sale of rock, sand, etc., extracted by the taxpayer. Rather, the taxpayer claims, the majority of its sales receipts were from sales of concrete, manufactured by the taxpayer. The taxpayer asserts because the Audit Division erred when it classified the income as arising from an extracting activity, the assessment of retail sales tax on M & E is incorrect. The taxpayer asserts the M & E is put to a majority use in the taxpayer's concrete manufacturing operation. Pursuant to the discretion granted by the Legislature, RCW 82.32.160 and RCW 82.32.170, the Appeals Division, elected not to hold a hearing. See also WAC 458-20-100(4)(a).

DISCUSSION:

During the audit period, persons removing ore, stone, sand, and/or gravel from their land, or another's land, under a right of license were extractors. RCW 82.04.100; WAC 458-20-135² (Former Rule 135). As extractors, persons such as the taxpayer, are not entitled to the manufacturing M&E retail sales tax and use tax exemptions for equipment used in their extracting business. RCW 82.08.02565; RCW 82.12.02565; Former Rule 135; WAC 458-20-13601 (Emergency Rule 13601).

However, the 1999 Legislature approved and the Governor signed Engrossed Substitute House Bill 1887. H.B. 1887, 56th Leg., 1st Sess., 1999 Washington Laws 211 (hereinafter ESHB 1887). ESHB 1887 clarified the legislative intent for the application of the manufacturing M&E exemption from retail sales and use tax. ESHB 1887 is retroactive to the date of the original 1995 M&E exemption legislation, July 1, 1995. The statutory sections affected by ESHB 1887 were RCW sections 82.08.02565, 82.12.02565, and 82.04.120. RCW 82.08.02565 and 82.12.02565 provide the M&E exemptions.

RCW 82.04.120 defines "to manufacture." ESHB 1887 amended RCW 82.04.120 to include the "crushing, and/or blending of rock, sand, stone, gravel, or ore" in the definition of "to manufacture."

² WAC 458-20-135 was amended after the audit period to reflect statutory changes. WAC 458-20-135 was amended at the 2nd Emergency rulemaking (CR 103) and filed September 23, 1999, effective immediately. The amended version of Rule 135 will be referred to as "Emergency Rule 135." References to the previous version of Rule 135 will be cited as "Former Rule 135."

Emergency Rule 135, the Department's administrative rule implementing 82.04.100 (the statute section entitled "Extractor"), was amended September 23, 1999, to be effective immediately. Emergency Rule 135(2)(b)(ii) states:

Mining and quarrying operations are extracting activities, including the screening, sorting, piling, and washing of rock, sand, stone, or gravel if the extractor does not directly or by contracting with others crush or blend the materials at the site where the materials were taken or produced.

The crushing and/or blending of rock, sand, stone, or gravel are not extracting activities. These are manufacturing activities. (See WAC 458-20-136 on manufacturing.) Likewise, any screening, sorting, piling, or washing of the material, when the activity takes place in conjunction with crushing or blending, is considered a part of the manufacturing activity if it takes place after the first screen. If there is no separate first screen, only those activities subsequent to the materials being deposited into the screen are considered manufacturing activities.

The taxpayer removes the sand, gravel, aggregate rock and dirt from the ground, an extracting activity. Then the taxpayer washes, screens, and sorts the extracted materials. To the extent the washing, screening, sorting and piling of the materials occurs in conjunction with the crushing and blending activities, and subsequent to the first screening, the activities are part of a manufacturing process. In operations where there is no first screen process, activities taking place after the materials have been deposited into the screen will be considered manufacturing activities. Therefore, the M & E used directly in the manufacturing operation, which includes the rock crushing and blending procedure, is exempt from retail sales tax and/or use tax, if it meets the useful life and majority use requirements. RCW 82.08.02565; RCW 82.12.02565; Emergency Rule 13601.

The Audit Division did not have the benefit of ESHB 1887 and the amended administrative rules when it issued the tax assessment. We believe this determination addresses the concerns of the taxpayer without deciding whether the taxpayer's income was properly characterized. We are remanding this matter to the Audit Division for re-examination of the taxpayer's activities in light of the legislative clarifications decisions discussed herein and to issue, as appropriate, a post assessment adjustment (PAA) consistent with ESHB 1887 and this determination.

DECISION AND DISPOSITION:

The taxpayer's petition is dismissed and remanded to the Audit Division to re-examine the taxpayer's activities and to issue, as appropriate, a PAA consistent with ESHB 1887 and this determination.

Dated this 13th day of December, 1999.