

Cite as Det. No. 05-0023, 24 WTD 388 (2005)

BEFORE THE APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

In the Matter of the Petition For )	<u>D E T E R M I N A T I O N</u>
Reconsideration of Assessment of )	
)	No. 05-0023
)	
... )	
)	Registration No. . . .
)	. . . /Audit No. . . .
)	Docket No. . . .
)	

RULE 190(9)(b); RCW 82.04.263: B&O TAX – CLEANUP OF RADIOACTIVE WASTE – QUALIFICATION FOR THE SPECIAL TAX RATE. Qualification for the special tax classification is based solely on the activity performed with the activity being “integral and necessary to the direct performance of the cleanup.” The design of equipment to sample nuclear waste and procedures to vitrify nuclear waste qualifies when the design work is both indispensable and directly precedes the performance of the qualifying activity.

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.

Lewis, A.L.J. -- Taxpayer receives income from providing design services to prime contractors involved in the cleanup of hazardous radioactive waste. Specifically, Taxpayer designs procedures to test, alter, and handle nuclear waste. We conclude Taxpayer’s income qualifies for the “cleaning up radioactive waste and other byproducts of weapons production and nuclear research and development” (“radioactive waste cleanup”) B&O tax. The design work is “integral and necessary” to a qualifying activity, the “handling, storing, treating, immobilizing, stabilizing, or disposing of radioactive waste.”<sup>1</sup>

ISSUE:

Whether Taxpayer’s income derived from the design of procedures for the cleanup of hazardous nuclear substances qualifies for the radioactive waste cleanup B&O tax classification?

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

### FINDINGS OF FACT:

The United States Department of Energy, the State of Washington, and the United States Environmental Protection Agency have a detailed program that governs the cleanup of hazardous nuclear substances at Hanford, Washington. The cleanup program is long-term and complex and requires significant scientific and engineering study, planning, and design prior to undertaking the actual physical cleanup activities.

The Federal Government awarded cleanup contracts to prime contractors. Each prime contractor uses both its own employees and subcontractors to accomplish the task. Taxpayer operated as a subcontractor for three prime contractors during the audit period. The prime contractors and their role in the cleanup program include:

[Prime #1] has the responsibility for the safe storage, characterization, and retrieval of high level radioactive waste from underground storage tanks. The responsibility includes transfer of high level radioactive waste to a waste treatment facility that is currently being designed and constructed.

[Prime #2] has the responsibility to design, construct, and operate the waste treatment facility that will treat the high level radioactive waste currently stored in underground tanks. The waste treatment facility will vitrify<sup>2</sup> waste to produce a waste form that can be shipped off site and disposed of in an underground repository, currently planned to be constructed [outside Washington].

[Prime #3] is responsible for retrieval and packaging of spent nuclear fuel currently stored underwater in storage basins, treatment of the contaminated water in the storage basins, and retrieval and treatment of radioactive sludge from the basins. [Prime #3] also is responsible for decontamination and decommissioning of facilities and retrieval and packaging of transuranic and mixed waste for shipment [outside Washington].

Each prime contractor hired Taxpayer to design procedures and policies necessary to accomplish the cleanup. Taxpayer relates that the Hanford nuclear reservation contains almost two hundred tanks containing radioactive nuclear waste. The tanks are massive; some contain over a million gallons of liquid waste. In most instances, the exact nature of the waste contained in the tank is unknown. To further complicate matters, the forty foot deep tanks may contain different types of nuclear waste that has settled at different levels in the tanks. Before any cleanup can occur, the exact nature of the waste must be determined. The contractors hire Taxpayer to design a methodology to test the contents of the tanks. Taxpayer's responsibility includes both the design of a testing methodology to determine what hazardous substances are in the tanks and the design of the equipment necessary to do the testing.

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<sup>2</sup> Vitrification turns the nuclear waste into a glass-like substance.

Equally important is Taxpayer's design work related to the vitrification of the hazardous liquid, which is necessary for the waste's safe transportation and storage.

Taxpayer reported the revenues derived from its design contracts discussed above under the radioactive waste cleanup B&O tax classification. The Department's Audit Division audited Taxpayer's books and records for the period January 1, 1999 through March 31, 2003. On October 3, 2003, the Department issued a \$ . . . assessment. Most of the tax arose from the Audit Division's reclassification of Taxpayer's income from the radioactive waste cleanup to the service and other B&O tax classification.

In reclassifying Taxpayer's income, the Audit Division reasoned that Taxpayer's income did not qualify for the radioactive waste cleanup B&O tax classification because Taxpayer "perform[s] engineering work, but do[es] not actually do the cleanup operations." Taxpayer disagreed and on January 7, 2004 filed a petition requesting correction of the assessment. Taxpayer maintains that the design work it performs is integral and necessary to the cleanup activity and that the income it receives should be reported under the radioactive waste cleanup B&O tax classification.

#### ANALYSIS:

RCW 82.04.263 provides a special B&O tax classification for the income derived from the clean up of radioactive waste and other byproducts of weapons production and nuclear research and development. Specifically RCW 82.04.263 states:

Upon every person engaging within this state in the business of cleaning up for the United States, or its instrumentalities, radioactive waste and other byproducts of weapons production and nuclear research and development; as to such persons the amount of the tax with respect to such business shall be equal to the value of the gross income of the business multiplied by the rate of 0.471 percent

Under this provision, only those activities that meet the definition of "cleaning up radioactive waste and other byproducts of weapons production and nuclear research and development" are entitled to the preferential tax rate. RCW 82.04.263 defines "cleaning up radioactive waste and other byproducts of weapons production and nuclear research and development" to mean:

the activities of handling, storing, treating, immobilizing, stabilizing, or disposing of radioactive waste, radioactive tank waste and capsules, nonradioactive hazardous solid and liquid wastes, or spent nuclear fuel; spent nuclear fuel conditioning; removal of contamination in soils and ground water; decontamination and decommissioning of facilities; and activities integral and necessary to the direct performance of cleanup.

(Emphasis added.)

Here, Taxpayer's activities are not of themselves directly involved in the clean up. To qualify for the special rate, they would have to qualify as "activities integral and necessary to the direct performance of cleanup."

On January 5, 2005 the Department adopted a revision to WAC 458-20-190 (Rule 190) that helps to explain RCW 82.04.263.<sup>3</sup> Rule 190(9)(b) explains that to be considered an activity "integral and necessary to the direct performance of the cleanup" the activity must be "directly connected to and essential for the furtherance" of the earlier enumerated activities.

Rule 190(9)(b) also explains that "[d]irectly connected to and essential to the direct performance of the cleanup" requires both a "necessity relationship" and "sequential relationship" with one of the earlier enumerated activities. "Necessity relationship" means that the activity "must take place in order for the direct cleanup to take place." Rule 190(9)(b)(ii). In other words, the activity must be more than just highly desirable; the activity must be "indispensable" to the direct cleanup. Rule 190(9)(b). In addition, the activity must also have a "sequential relationship" with one of the earlier enumerated activities. Here, "sequential relationship" means that "the activity directly precedes, directly follows, or is concurrent with" one of the previously enumerated activities." Rule 190(9)(b)(i).

Here, Taxpayer receives income for the design of equipment to sample the nuclear waste; procedures to determine the composition of the nuclear waste; and methods to vitrify the liquid waste for ease and safety of moving, storage, or disposal. Income derived from such activities qualifies for the radioactive waste cleanup B&O tax classification because the design work is both indispensable and directly precedes the performance of a qualifying activity, *i.e.*, the "handling, storing, treating, immobilizing, stabilizing, or disposing of radioactive waste."

In this case, Taxpayer's activities are similar to those identified in an example in the rule as qualifying for the special rate:

(iii) Company E is an environmental engineering company which contracts with Prime Contractor to develop a plan on how best to decontaminate the soil at a tank farm and will monitor the cleanup/decontamination as it progresses. Company E's activities qualify for the preferential tax rate under RCW 82.04.263 because the activities are directly connected to and essential for removing contamination in soils.

Rule 190(c)(iii). Qualification for the tax classification is based solely on the activity performed, *i.e.*, the cleanup of radioactive waste and other byproducts of weapons production and nuclear research and development, and not on the status of the contractor. Thus, subcontractors as well as prime contractors may qualify for the tax classification. Rule 190(9). Accordingly, we grant Taxpayer's petition.

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<sup>3</sup> The revision to Rule 190 becomes effective February 5, 2005. Prior to the revision, the Rule did not address the qualifications for the preferential nuclear cleanup B&O tax classification.

**DECISION AND DISPOSITION:**

Taxpayer's petition is granted.

Dated this 31<sup>st</sup> day of January, 2005.