Cite as Det. No. 01-072, 22 WTD 193 (2003)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of Assessment of	)	D E T E R M I N A T I O N
	)	No. 01-072
. . .	)	Registration No. . . .
	)	FY . . . /Audit No. . . .
	)	Docket No. . . .

[1] RULE 134, RULE 136, RULE 170: MANUFACTURING B&O TAX – USE TAX – STEVEDORING COMPANY – DOCKSIDE RAMP. Where a stevedoring company that leases a port facility adjacent to a navigable body of water builds a large ramp on the leased property, moves the ramp to the water's edge, and attaches it to the realty, it has not engaged in a taxable manufacturing activity. Use tax is due only on the materials used to construct the ramp.

[2] RULE 115, RULE 117, RULE 178, & RULE 211: USE TAX – DUNNAGE – PACKING MATERIALS – STEVEDORING COMPANY – BAILMENT TO. Where water-borne interstate carriers bail dunnage and packing materials to a stevedoring company that applies the items to secure outbound cargo, the stevedoring company is liable for use tax on the bailed items, based on their reasonable rental value, which will be pro-rated if the items are also used by others.

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:

Stevedoring company protests use tax assessed on a dockside ramp and dunnage/packing materials.[1]

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

FACTS:

Dressel, A.L.J. -- [The taxpayer] is a stevedoring company. Its books and records were examined by the Department of Revenue (Department) for the period January 1, 1995 through December 31, 1998. As a result a tax assessment, identified by the above-captioned numbers, was issued in the amount of $ . . . . The taxpayer appeals portions of the assessment.

The taxpayer is engaged in the business of marine cargo handling and stevedoring at a leased, port facility on the [body of water]. To facilitate its vessel-loading activities, the taxpayer constructed a very large ramp, which it dubbed the "Super Ramp." The ramp *per se* or *girder span* was built by the taxpayer's own employees on an area of the leased premises some . . . distan[ce] from the [body of water], where it would, eventually, be located. Around the construction area, the taxpayer built a temporary structure to shield the ramp and the workers from the elements. Once the ramp was built, the taxpayer used forklifts and dollies to nudge it . . . from its building site to the edge of the [body of water]. There, one end was placed on "batter pilings," which the taxpayer had constructed by a contractor in the [body of water] itself. The other end of the ramp was attached to the beach to a significant concrete foundation, also built by a contractor. The ramp is bolted and welded to the foundation. Considerable work was undertaken at the [body of water] to secure the ramp and get it ready for its intended purpose, which was to allow forklifts to transfer cargo platforms from land to ship or barge. Among other things, the ramp was paved, following its attachment to the foundation on one end and the pilings on the other.

The Audit Division (Audit) assessed use tax on what it calculated to be the value of the ramp. Not only did it assess tax on the value of the materials that went into constructing the ramp, but also it included in the measure of tax labor and overhead expended in its fabrication. Consistent with such a pattern of use taxation, Audit also assessed manufacturing business and occupation (B&O) tax on the construction of the ramp. It reasoned that the ramp, *per se*, was tangible personal property, which would be used by the taxpayer for commercial or industrial purposes.

Contrary to that position, the taxpayer contends the ramp was part of an overall improvement to real property and that, therefore, use tax should only be assessed on the physical components of the ramp and that no B&O tax is owed, because the Super Ramp was more appropriately classified as real property. Manufacturing B&O tax, it says, only applies to personal property. Although aware the Department has distinguished items incorporated into real estate based on whether they were built at or away from a construction site, the taxpayer claims, in essence, that [its ramp was built] close enough to [the body of water to] be considered "on site."

A second bone of contention in this appeal is use tax assessed on dunnage and/or packing materials. The taxpayer has a sister company, [Cargo Co.], that is a waterborne carrier-for-hire, whose destinations include [State A and B]. The largest portion of the taxpayer's business is packing and loading cargo for [Cargo Co.]. [Cargo Co.] requests of the taxpayer that it pack its

loads using various dunnage-type items. Included are "V guards,"[2] wooden "timbers," banding, and tarpaulins.[3]

At the hearing the taxpayer explained the use of each of these items. The timbers are large pieces of wood, measuring four by six by eight.[4] According to the taxpayer, they are used to separate barge loads, not to protect them. When loads arrive at the taxpayer's facility, they are relatively small and sit on two by four wood pieces. The taxpayer takes a small "unit" off a truck and creates a large packing unit for a barge. It places the small units on large, metal platforms that are loaded onto barges and ships. The timbers are used to separate loads, presumably, by type and destination but, most importantly, to separate the large platforms. The platforms are stacked and the timbers separate the platforms. This allows the taxpayer to pack a larger load and facilitates offloading at the destination site. The timbers make it easier for large forklifts to pick the platforms off the ship and transport them to shore. These timbers are, by far, the most valuable item vis-à-vis the issue of dunnage.

V boards are, simply, two timbers nailed together in an "L" shape. They protect loads from "lashing" chains and furnish a base to which tarps may be attached. Tarps are used to protect cargo from sea spray en route and for storage at the destination end of the cargo's journey. Metal banding helps, slightly, to secure a unit as it is being loaded onto a barge, but its primary use is to secure cargo for the ocean voyage.

The dunnage items are not the property of the taxpayer. They are purchased by [Cargo Co.] and other carrier customers of the taxpayer to be applied to the cargo by the taxpayer. Deliveries of dunnage are made, approximately, once a month to the taxpayer's facility and, simply, stored in a pile until needed for a shipment. Typically, the dunnage is in and out of the taxpayer's premises in one month's time.

Some of the dunnage is returned to the taxpayer and reused. Some is not. The taxpayer hesitated to give an estimate as to how frequently the dunnage came back.

Audit reasoned that the carriers had bailed the dunnage items to the taxpayer and assessed use tax against the taxpayer on 25 percent of the dunnage. Its basis for that percentage was its estimate that 25 percent of the items was applied to the loads or units on land, whereas 75 percent was applied aboard the barges. Of the four items mentioned above, however, Audit considered only the timbers to be dunnage. V guards, banding, and tarps were considered by Audit to be "packing materials," as opposed to dunnage. One hundred percent of these packing materials were subjected to use tax by Audit. Any item subjected to use tax was taxed based on its full purchase price from a vendor.[5]

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[2] Also known as "V boards."
[3] Also known as "tarps."
[4] Inches, we presume.
[5] It should be understood that the purchase price was the price paid by [Cargo Co.] and the other carriers for the dunnage/packing materials. Again, these items were not purchased by the taxpayer. They were bailed to the taxpayer by the carriers. Audit did a companion audit of [Cargo Co.] and was able to identify the purchase price of dunnage and packing materials from that examination.

The taxpayer doesn't attempt to make a large point about whether the items should be labeled dunnage or packing materials. Regardless of their proper category, inasmuch as they are bailed to the taxpayer, any use tax on them, says the taxpayer, should be calculated, based on their reasonable rental value. The taxpayer argues, however, that it doesn't have possession of the items long enough to establish any rental value. It argues further that there isn't even a bailment in this situation because the taxpayer doesn't have dominion and control of the items, purportedly, bailed. Thirdly, the taxpayer claims that the carriers and the parties on the destination end of the shipment are the primary beneficiaries of the dunnage and the packing materials and are, therefore, the *consumers*. As such, the taxpayer argues, *they* ought to be the parties liable for any use tax.

ISSUES:

1. Was the construction of a ramp at an export dock the construction of real property such that Manufacturing B&O and use tax should not apply?

2. Is a stevedoring company liable for use tax on dunnage materials bailed to it by its waterborne carrier customer?

3. If the stevedoring company is liable for use tax on dunnage, should the measure of tax be the purchase price or rental value?

DISCUSSION:

Super Ramp

Those engaged in business in this state as manufacturers are subject to B&O tax under the Manufacturing classification. RCW 82.04.240. "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, and shall include: (1) The production or fabrication of special made or custom made articles . . . .

RCW 82.04.120. (Italics ours.) At issue in the instant case is the construction of a ramp, which became attached to *real* property. So, the *real* question here is whether the ramp should be considered real or personal property. If it is the latter and, otherwise, fits the other statutory requirements,[6] it is subject to Manufacturing B&O tax. If it's real property, it doesn't fit the above-quoted definition of "to manufacture," and its fabrication would *not* be subject to Manufacturing B&O tax.

[6] *See* RCWs 82.04.110, .120, .130, and .240.

In *Morrison-Knudsen Co. v. State*, 64 Wn.2d 86, 390 P.2d 712 (1964), use tax was affirmed against a contractor who had constructed bridge pontoons and anchor shells in Seattle, many miles from the Hood Canal bridge, where they were, eventually, installed. The court reasoned that the contractor had produced tangible personal property for commercial or industrial use and that, therefore, Manufacturing B&O tax and use tax were due on the fabrication of the mentioned large construction components.

Vis-à-vis the matter of use tax, the court also found that the contractor used the pontoons and anchor shells as a consumer and was, thus, liable for use tax based on the value of the several bridge components. *Id*. at 92-93. The statutory authority for use tax is RCW 82.12.010, which reads, in part:

> **Use tax imposed.** (1) There is hereby levied and there shall be collected from every person in this state a tax or excise for the privilege of using within this state as a consumer: (a) Any article of *tangible personal property* purchased at retail, or acquired by lease, gift, repossession, or bailment, or extracted or *produced or manufactured by the person so using the same*, or otherwise furnished to a person engaged in any business taxable under RCW 82.04.280 (2) or (7) . . . .

[Italics ours.] As to both use tax and Manufacturing B&O tax, the Board of Tax Appeals arrived at a conclusion similar to that of the court in *Morrison-Knudsen v. State, supra*, in *United Builders of Washington, Inc. v. Dept. of Revenue*, BTA Docket No. 193 (1968). In the BTA case, a builder of homes constructed roof trusses, wall panels, and cabinets in Yakima and then transported them by truck to building sites elsewhere in Eastern Washington, as well as in Idaho and Oregon. The Board's theory was the same, that United Builders manufactured these articles at one location and then submitted them to its own industrial use at another location.

This holding of the BTA was adopted by the Department when it issued ETB 404.04.134 on July 24, 1970. This excise tax bulletin was based on the holding in *United Builders v. Dept., supra*.[7] At the same time, this ETB noted an exception where it said:

> *Note that where components are fabricated at the job site for incorporation into the structure at that site, they are considered as becoming a part of the real property in the course of fabrication and so are not subject to the state's excise taxes.* The state has, however, held that work performed at locations other than the job site should be distinguished for tax purposes under the provisions of the tax laws. This distinction was upheld in Morrison-Knudsen, Inc. v. State of Washington, 64 Wn. 2d 86 (1964), where a contractor was held liable for the same taxes involved here. These were assessed upon the construction and use of concrete pontoons and shells which were produced for a floating bridge. These components were built at a site many miles from the bridge site, stored for a period of time, and then floated to the bridge site where they were installed. (Italics ours.)

. . .

[7] ETB 404.04.134 is now Excise Tax Advisory (ETA) 404.04.134.

In the instant case the ramp, or girder span, was assembled [a distance] from where it was committed to the ground as real property. The logical question, then, is is the assembly site at the job site or away from the job site. While it, precisely speaking, was not at the place of the ramp's ultimate fixation to the real estate, it was on the same work site in a more general sense. Both the actual attachment to the real property and assembly of the ramp took place on the same piece of property, the port facility leased by the taxpayer. It is reasonable to say that the ramp was constructed at the job site.

Such a conclusion is fortified when one considers . . . ETA 404 says that when components are fabricated at the job site for incorporation into the structure at that job site, the components are not subject to the state's excise taxes. It is notable that in its last paragraph, the ETA states further, "Here the items of personal property which were fabricated were completed as individual components and were separate items of personal property when they left the taxpayer's headquarters." The component at issue in the instant case, the ramp, it should be remembered, *never* left the taxpayer's headquarters. It was built *and* permanently located at the taxpayer's headquarters.

. . .

Considering the cited authority, we find that the ramp, in the instant case, *was* constructed at the job site. Its fabrication took place adjacent to the site of the real property improvement. . . . We conclude, for taxation purposes, the ramp is . . . not the proper subject of either Manufacturing B&O or use tax. Use tax does apply, however, to the materials used to construct the ramp, to the extent sales tax was not paid upon their acquisition. RCW 82.12.020.

On the first issue, the Super Ramp, the taxpayer's petition is granted.

Dunnage and Packing Materials

Dunnage is defined in WAC 458-20-117 (Rule 117) as:

> (a) The term "dunnage" means any material used for the purpose of protecting or holding in place cargo or freight during transportation by any carrier of property, and which is not an integral part of the carrier itself. Dunnage includes, but is not limited to, *wood blocks*, stakes, *separating strips*, *timber*, double decks, false floors, door shields, bulkheads, and *other bracing*. Dunnage generally does not remain with the cargo that is being transported and will not be delivered to the person who will ultimately receive the cargo. On the other hand, packing materials are generally part of the total package containing the cargo and are ultimately delivered to the customer as part of the cargo or merchandise. (Italics ours.)

Packing materials, on the other hand, is defined in WAC 458-20-115 (Rule 115) as follows:

> (2) Definitions. 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. [Italics ours.]

The four items in question are timbers, V-blocks, banding, and tarps. Timbers and V-blocks[8] are, certainly, dunnage. Banding qualifies as packing material. Tarps aren't as easily categorized, based on the quoted rule definitions, but we find them to be dunnage as well, in that their primary purpose appears to be protection of cargo during its actual transportation period.

According to Audit[9] 100 percent of steel banding and V-blocks was subjected to use tax, and at 100 percent of value of the items. Only 25 percent of timbers were taxed but, again, at 100 percent of value. It is not clear what percentage of tarps was taxed, but there is no indication in the Audit file that they were taxed on anything less than 100 percent of value.

As Audit acknowledges, the dunnage and packing materials were bailed to the taxpayer, principally, by [Cargo Co.]. They were also used by the taxpayer in that the taxpayer applied them to outbound shipments of water-borne goods. Those using tangible personal property as a consumer in this state are liable for use tax, including those who acquire such property through bailment. RCW 82.12.020. WAC 458-20-211(7)(a) discusses bailment and use tax.[10] It reads:

> (a) Bailment. The value of tangible personal property held or used under bailment is subject to use tax if the property was purchased or acquired under conditions whereby the retail sales tax was not paid by the bailor. Tax liability is that of the bailor, or of the bailee if the bailor has not paid the tax. The measure of the tax to the bailor is the fair market value of the article at the time the article was first put to use in Washington. The measure of the use tax to the bailee for articles acquired by bailment is the reasonable rental with the value to be determined as nearly as possible according to the rental price at the place of use of similar products of like quality and character. In the absence of rental prices for similar products, the reasonable rental may be computed by prorating the retail selling price over the period of possession had by a bailee and payable in monthly installments. No further use tax is due upon property acquired by bailment after tax has been paid by the bailee or any previous bailee upon the full original value of the article.

Having received the dunnage and packing materials from [Cargo Co.], the taxpayer is the bailee in this situation. Thus, any liability it might have for use tax on those items should be based on their reasonable rental value. The Audit Division, however, did not assess use tax based on reasonable rental value. Instead, anything it taxed was at 100 percent of its retail value. It did exclude 75 percent of dunnage, reasoning that it was applied on board a barge or ship.

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[8] Formed by timbers attached in an "L" shape.
[9] *See* Auditor's Detail of Differences and Instructions to Taxpayer, page 4.
[10] *See also* WAC 458-20-178(13).

"Transporting across the state's boundaries is exempt, whereas supplying such transporters with facilities, arranging accommodations, providing funds and the like, by which they engage in such commerce is taxable." WAC 458-20-193D. Interstate commerce may be made to pay its fair share of local tax burdens. *National Can Corp. v. Department of Rev.*, 109 Wn.2d 878, 749 P.2d 1286 (1988). *See also Complete Auto Transit v. Brady*, 430 U.S. 274 (1977); and *Dept. of Revenue v. Association of Washington Stevedoring Cos.*, 435 U.S. 734 (1978). In terms of exacting that local tax, it makes no difference whether this stevedoring taxpayer applies dunnage and packing materials on the shore or on the boat next to shore. Either way, it is providing a local service in the state of Washington.

As indicated in WAC 458-20-211 (Rule 211), *supra*, use tax in a bailment situation should be based on a reasonable rental value of the item bailed. "In the absence of rental prices for similar products, the reasonable rental may be computed by prorating the retail selling price over the period of possession had by a bailee and payable in monthly installments." *Id.*; s*ee also* Det. No. 91-322, 11 WTD 521, 528-529 (1992). Furthermore, the reasonable rental value of articles used by only one user is the full value of the article. ETA 108.12.178. If an article is shared among several bailees, use tax may be pro-rated among those bailees. *See* Det. No. 92-218, 14 WTD 145 (1995); and Det. No. 91-322, *supra*.

Applying this rationale to the instant case, use tax on dunnage and packing materials bailed to the taxpayer should be pro-rated such that the taxpayer is taxed based only on its period of possession, as opposed to the time the items are possessed by all users. As the taxpayer correctly points out, the dunnage and the packing materials are also applied for the benefit of and used by the water-borne carriers and the buyers and receiving entities on the other end of the journey. In fact, at the time the dunnage and packing materials are loaded aboard an [Cargo Co.] barge, they are returned to their bailor. The taxpayer's bailment terminates at that moment. [Cargo Co.], at that point, commences the direct use of its own dunnage and packing materials for the benefit of its own water-borne cargo shipment.

The taxpayer's period of use should include the time the items are kept on its premises, awaiting application to loads of cargo. This is because "[t]he terms 'use,' 'used,' 'using,' or 'put to use' include any act by which a person takes or assumes dominion or control over the article and shall include installation, storage, withdrawal from storage, or any other act preparatory to subsequent actual use or consumption within the state." WAC 458-20-178(3).

In terms of pro-rating reasonable rental value, the burden is placed on taxpayers to provide proper documentation. Det. No. 91-322, *supra*, at 529. Therefore, we will give the taxpayer 60 days from the date of this Determination, or such other period upon which it and Audit may agree, to provide documentation or other evidence suitable for pro-rating the use tax. If such information is forthcoming, Audit will adjust the assessment, as it relates to use tax on dunnage and packing materials, in conformity with this Determination. In the absence of this evidence, we cannot say that Audit's assessment, vis-à-vis dunnage and packing materials, was unreasonable, in that it taxed only 25 percent of what it considered dunnage. Roughly speaking, that accomplishes a pro-ration and accounts for the fact that other parties used the bailed items as well. The burden is on the taxpayer to produce documentation to establish its tax liability, and, if it fails to do so, it may

not, successfully, complain about an ensuing tax assessment. RCW 82.32.070. To summarize, if the taxpayer doesn't, within 60 days, produce credible evidence to support a different pro-ration of use tax on packing materials and dunnage, the present one, as contained in the current assessment, will be reinstated.

With respect to the taxpayer's argument that, based on *Active Moving & Storage Co. v. Department. of Rev.*, BTA Docket No. 203 (1968), it didn't have dominion and control of the items bailed, we note that, as to the Department, Board of Tax Appeals decisions are not precedential. Det. No. 94-152, 15 WTD 41 (1995). The Board, in the cited case, declined to assess use tax, on a bailment theory, against a moving company that used lumber and nails to make crates for the federal government. We choose not to adopt the rationale of the BTA case.

Measure of Use Tax

This issue has already been addressed in the discussion of the second issue.

DECISION AND DISPOSITION:

The taxpayer's petition is granted, conditionally. This matter is remanded to Audit for an amended assessment, consistent with this Determination.

DATED this 31st day of May, 2001