

Cite as Det. No.21-0180, 41 WTD 430 (2022)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS 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. 21-0180
)	
... )	Registration No. ...
)	

[1] WAC 458-40-610; RCW 84.33.041; EXCISE TAXES – TIMBER TAX – DEDUCTIONS. When a real property owner that harvested timber from its real property did not produce records that distinguish between its qualifying and non-qualifying harvesting and marketing activities, the owner is eligible for a harvesting and marketing costs deduction of thirty-five percent of the gross receipts from the sale of the logs.

[2] WAC 458-20-228; RCW 82.32.105; TAXES – PENALTIES – WAIVER OR CANCELLATION OF PENALTIES. When a real property owner incurred delinquent penalties for failing to timely pay all the timber tax that was due because it incorrectly calculated its harvesting and marketing costs deduction, the penalties were not the result of any circumstances that were beyond the owner’s control and may not be waived.

[3] WAC 458-20-228; RCW 82.32.105; TAXES – INTEREST – WAIVER OR CANCELLATION OF INTEREST. When a real property owner did not rely upon specific written instructions from the Department in failing to timely report and pay its timber tax liability and the Department did not grant any extension of the due date, the owner is not eligible for any waiver or cancellation of interest.

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.

McCormick, T.R.O. – A real property owner that harvested timber from his property disputes the Department’s disallowance of claimed harvesting and marketing deductions, and assessment of additional timber tax liability, delinquent penalty, and interest. The owner asserts that the Department incorrectly disallowed the claimed deductions as charges for land clearing or stump removal. Because the owner did not provide records from which the Department may separate Taxpayer’s costs for qualifying and non-qualifying activities, the Department correctly determined

that the owner was eligible to claim a 35 percent deduction for harvesting and marketing costs. We deny in part and grant in part, the petition.<sup>1</sup>

### ISSUES

1. Whether, under RCW 84.33.041 and WAC 458-40-610, a real property owner that contracted with a timber harvester to harvest timber from the owner's real property is eligible for claimed harvesting and marketing deductions, when the owner has not provided records that state separate costs for qualifying and non-qualifying harvesting activities.
2. Whether, under RCW 82.32.105 and WAC 458-20-228, a real property owner is eligible for a waiver of delinquent penalties included in the Department's tax assessment.
3. Whether, under RCW 82.32.105 and WAC 458-20-228, a real property owner is eligible for a waiver of interest included in the Department's tax assessment.

### FINDINGS OF FACT

. . . (Taxpayer) is an owner of real property located in . . . , WA. Taxpayer registered with the Department [in] 2019. During the Quarter 3 2019 period, Taxpayer harvested and marketed timber from his real property. Payment of timber tax is due by the last day of the month following the quarterly period in which the timber is harvested. *See* RCW 84.33.086. Payment of Taxpayer's timber tax liability was due October 31, 2019.

During 2019, Taxpayer contracted with . . . (Consultant) to assume responsibility for harvesting and marketing the timber located on Taxpayer's real property. In turn, Consultant engaged the services of . . . (Harvester) to harvest the subject timber. During August and September 2019, Harvester harvested the subject timber from Taxpayer's real property.

On November 4, 2019, Taxpayer filed his Quarter 3 2019 combined excise tax return and reported his timber tax liability to the Department. Taxpayer reported \$. . . in gross income from sale of 18,000 board feet of timber and claimed harvesting and marketing deductions in the amount of \$. . . Taxpayer did not submit any payment with his Quarter 3 2019 tax return.

During April 2021, the Department's Audit Division (Audit) investigated Taxpayer's timber harvesting activities and reviewed Taxpayer's Quarter 3 2019 combined excise tax return to verify that Taxpayer correctly reported his timber tax liability. In completing its investigation, Audit inquired whether Taxpayer had invoices that established Taxpayer's various harvesting and marketing activities, including qualifying and non-qualifying harvesting and marketing costs. Taxpayer informed Audit that it did not have separate invoices to distinguish between his logging, clearing, grading, and stump removal, costs. Audit determined that Taxpayer was subject to timber tax on the total stumpage value of the harvest and was eligible to take the standard harvesting and marketing costs deduction of 35 percent of his gross receipts.

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

On April 30, 2021, the Department issued Letter ID . . . , a notice of balance due (Assessment) in the amount of \$ . . . , which is comprised of \$ . . . in timber tax, a 29 percent delinquent penalty of \$ . . . , and \$ . . . in interest. Payment of the Assessment was due June 2, 2021. The Assessment remains unpaid.

On May 17, 2021, Taxpayer petitioned for administrative review of the Assessment. Taxpayer asserts that the Department incorrectly disallowed his claimed harvesting and marketing costs deductions. Taxpayer asserts that Audit informed him that stump removal is not an allowable deduction. Taxpayer asserts that he engaged Consultant to arrange for harvesting of the subject timber from his real property, and Consultant in turn engaged Harvester to perform the actual harvesting of the subject timber. Taxpayer asserts that Harvester removed the subject timber from his real property by pushing over and removing each entire tree and that none of Taxpayer's asserted harvesting costs were for stump removal.

As part of this review, Taxpayer provided additional records, including: a spreadsheet containing a summary of the relevant invoices; Harvester's invoice nos. 119, 120, 121, and 122; vouchers from lumber mills evidencing the amount of timber sold and prices paid; and logging permit preparation and permit cost. Invoice nos. 119 and 120 include charges for excavation/logging and cutting. Invoice nos. 121 and 122 include charges for excavation, logging, piling brush, moving logs, hauling brush, stoking fire-burning stumps, and moving debris offsite. The information contained in the vouchers is limited to weight or size of the timber purchased, the price the lumber mills paid for the timber, and the amounts the lumber mills paid to both Taxpayer and the hauler of the timber.

In reviewing the additional records, Audit noted that the spreadsheet containing the summary of relevant invoices does not include any author or origination information. In its Division Response, Audit states that, in an effort to substantiate Taxpayer's assertions, Audit contacted Harvester to inquire if the invoices it provided to Taxpayer were sufficient to distinguish between the various harvesting activities Harvester performed. Harvester indicated that its invoices did not include separate costs for each of the specific harvesting activities it performed. "The only documentation [Harvester] provided were [Harvester's] invoices and that there wasn't a way to differentiate between fall, buck, yard, load and the other activities [Harvester] did onsite." Division Response at 2.

## ANALYSIS

1. Taxpayer is eligible to claim the standard 35 percent harvesting and marketing costs deduction from his timber tax liability because Harvester's invoices do not separate the costs of qualifying and non-qualifying activities.

### *Timber Excise Tax*

A timber tax is imposed on every person engaging in the business of harvesting timber on privately or publicly owned land. RCW 84.33.041(1). "Harvester" means "every person who from the person's own land or from the land of another under a right or license granted by lease or contract, either directly or by contracting with others . . . , fells, cuts, or takes timber for sale or for

commercial or industrial use. . . .” RCW 84.33.035(7) (emphasis added). “Timber” means all “forest trees, standing or down, on privately and publicly owned land.” RCW 84.33.035(18). There is no dispute here that Taxpayer was a harvester of timber, which he cut from his own land using a hired third-party contractor.

The tax is equal to the stumpage value of timber harvested for sale or for commercial or industrial use, multiplied by specified rates. RCW 84.33.041(1). A landowner selling timber is making commercial use of that timber. WAC 458-40-626. Timber tax is imposed on timber harvested during the previous calendar quarter and due on the last day of the month following the quarter in which the timber is harvested. RCW 84.33.086; WAC 458-40-626.

Qualified small harvesters, such as Taxpayer here,<sup>2</sup> are permitted to deduct harvesting and marketing costs from the gross receipts of a timber sale to arrive at the taxable value, as follows:

When timber is sold after it has been harvested, the taxable value is the actual gross receipts from sale of the harvested timber minus the costs of harvesting and marketing the timber. When the taxpayer is unable to provide documented proof of harvesting and marketing costs, this deduction for harvesting and marketing costs shall be a percentage of the gross receipts from sale of the harvested timber as determined by the department of revenue but in no case less than twenty-five percent.

RCW 84.33.074(3)(b) (emphasis added); *see also* WAC 458-40-610(11). Here, according to Taxpayer’s timber sale report, Taxpayer received \$. . . in gross receipts from the sale of 18,000 board feet of timber and reported under the Small Harvester option.

### *Harvesting and Marketing Costs*

The Department’s rules administering the timber tax statutes, RCW 84.33.010 through 84.33.096, are contained in Chapter 458-40 WAC. RCW 84.33.074(3)(b) directs the Department to determine the allowable harvesting and marketing costs deduction where the taxpayer is unable to provide documented proof of its costs. The Department interprets the term “harvesting and marketing costs” in WAC 458-40-610(11) as:

Only those costs directly and exclusively associated with harvesting merchantable timber from the land and delivering it to the buyer. The term includes the costs of piling logging residue on site, and costs to abate extreme fire hazard when required by the department of natural resources. Harvesting and marketing costs do not include the costs of other consideration (for example, reforestation, permanent road construction), treatment to timber or land that is not a necessary part of a commercial harvest (for example, precommercial thinning, brush clearing, land grading, stump removal), costs associated with maintaining the option of land conversion (for example, county fees, attorney fees, specialized site assessment or

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<sup>2</sup> Under RCW 84.33.035 and WAC 458-20-13501(14), a “small timber harvester” is a harvester who takes two million board feet of timber or less for sale in a calendar year. Small harvesters, such as Taxpayer here, are granted limited exemption from B&O tax under RCW 82.04.333. However, they must still register and pay timber tax.

evaluation fees), or any other costs not directly and exclusively associated with the harvesting and marketing of merchantable timber. The actual harvesting and marketing costs must be used in all instances where documented records are available. When the taxpayer is unable to provide documented proof of such costs, or when harvesting and marketing costs cannot be separated from other costs, the deduction for harvesting and marketing costs is thirty-five percent of the gross receipts from the sale of the logs.

(Emphasis added.) *See also* Det. No. 15-0355, 35 WTD 296 (2016); Det. No. 16-0131, 35 WTD 573 (2016); Det. No. 08-0097, 28 WTD 105 (2008).

Here, Taxpayer provided records in support of the claimed deduction for his harvesting and marketing costs in the amount of \$ . . . , including Harvester's invoices and the lumber mills' vouchers. Invoice nos. 119 and 120 include charges for excavation, logging, and cutting. Invoice nos. 121 and 122 include charges for excavation, logging, piling brush, moving logs, hauling brush, stoking fire-burning stumps, and moving debris offsite. The information contained in the vouchers is limited to weight or size of the timber purchased, the price the lumber mills paid for the timber, and the amounts the lumber mills paid to both Taxpayer and the hauler of the timber.

Neither the invoices nor the vouchers establish separate costs for each of the specific harvesting activities Harvester performed, such as brush clearing, land grading, and stump removal. Because Taxpayer has not provided records from which the Department may separate the costs of his qualifying and non-qualifying harvesting and marketing activities, the Department correctly determined that Taxpayer is eligible to claim a deduction for his harvesting and marketing costs of 35 percent of the gross receipts from the sale of the timber. We deny the petition as to this issue.

2. Taxpayer is eligible for a waiver of the delinquent penalty because Taxpayer registered with the Department before engaging in taxable timber harvesting.

Payment of the timber tax is due on or before the last day of the month following the end of the quarterly period in which the tax accrues. RCW 84.33.086. Payment of Taxpayer's timber tax liability was due by October 31, 2019. [Taxpayer filed his timber tax return on November 4, 2019, but did not pay any tax.]

Taxpayers are responsible to know their tax reporting obligations, and when they are uncertain about their obligations, seek instructions from the Department. RCW 82.32A.030(2); *see also* Det. No. 01-165R, 22 WTD 11, 15-16 (2003). Because of the nature of Washington's tax system, the burden of becoming informed about tax liability falls upon the taxpayer, and it is the taxpayer who bears the consequences of a failure to be correctly informed. RCW 82.32A.030(2); 22 WTD at 15.

The Department operates under a progressive delinquent penalty scheme, outlined in RCW 82.32.090(1):

If payment of any tax due on a return to be filed by a taxpayer is not received by the department of revenue by the due date, there is assessed a penalty of nine

percent of the amount of the tax; and if the tax is not received on or before the last day of the month following the due date, there is assessed a total penalty of nineteen percent of the amount of the tax under this subsection; and if the tax is not received on or before the last day of the second month following the due date, there is assessed a total penalty of twenty-nine percent of the amount of the tax under this subsection.

Assessment of the delinquent payment penalty is mandatory. Det. No. 01-193, 21 WTD 264 (2002); Det. No. 99-279, 20 WTD 149 (2001); Det. No. 87-235, 3 WTD 363 (1987). When Taxpayer did not pay his timber tax liability by the last day of the second month following the due date, the Department was required to assess a 29 percent delinquent penalty.

Having determined that the Department properly imposed the assessed penalties, we now turn to whether the Department can waive them.

The Department has limited authority to waive or cancel penalties. RCW 82.32.105. The Department can cancel penalties in the following situations: (1) the penalties were the result of “circumstances beyond the control of the taxpayer;” or (2) in the case of the late payment penalty, the Department may also waive the penalty [for late payment of timber tax owed under RCW 84.33.086] if the taxpayer has a good payment history. RCW 82.32.105(1); RCW 82.32.105(2).

WAC 458-20-228 (Rule 228) explains that “[c]ircumstances beyond the control of the taxpayer are generally those which are immediate, unexpected, or in the nature of an emergency. Such circumstances result in the taxpayer not having reasonable time or opportunity to obtain an extension of the due date or otherwise timely file and pay.” Rule 228(9)(a)(ii). The circumstances must directly cause the late payment. Rule 228(9)(a)(i).

Rule 228(9)(a)(ii) lists examples of circumstances that are generally considered beyond a taxpayer’s control sufficient to cancel penalties:

- Erroneous written information from the Department;
- An act of fraud or conversion by the taxpayer’s employee or contract helper which the taxpayer could not immediately detect or prevent;
- Emergency circumstances around the time of the due date, such as the death or serious illness of the taxpayer or a family member or accountant; or
- Destruction of the business or records by fire or other casualty.

Rule 228(9)(a)(iii) also lists examples of situations that are generally *not* considered beyond the control of a taxpayer:

- Financial hardship;
- A misunderstanding or lack of knowledge of a tax liability; or
- Mistakes or misconduct on the part of employees or other persons contracted with the taxpayer.

Here, Taxpayer disputes the Department's assessment of delinquent penalty because Taxpayer asserts that Audit incorrectly disallowed his claimed harvesting and marketing deduction. Taxpayer asserts that he has provided records sufficient to establish his claimed harvesting and marketing deduction. As explained above, Taxpayer is mistaken in his assertion because Taxpayer's records do not separate the costs of qualifying and non-qualifying activities. Taxpayer's failure to correctly determine his qualifying harvesting and marketing costs deduction directly caused Taxpayer's late payment of his assessed timber tax liability, resulting in the delinquent penalty at issue. Taxpayer's failure was due to either a mistake or lack of knowledge of a tax liability and was not a circumstance that was beyond Taxpayer's control.

Rule 228 also explains that a taxpayer may qualify for waiver of the delinquent penalty for having a good payment history under RCW 82.32.105(2). The rule explains that a taxpayer is eligible for this provision when it requests a penalty waiver and "has timely filed and paid all tax returns due for that specific tax program for a period of twenty-four months immediately preceding the period covered by the return for which the waiver is being requested." Rule 228(9)(b)(i)(B). Rule 228 explains that this provision allows waiver of the late payment penalty on "the taxpayer's very first return due" so long as they obtained a tax registration endorsement with the Department before conducting business in the state. *Id.*

Here, Taxpayer registered with the Department on May 10, 2019. Taxpayer's first return due was for the Quarter 3 2019 period. Because Taxpayer registered with the Department before engaging in taxable timber harvesting activities, Taxpayer is eligible under Rule 228(9)(b)(i)(B) for a waiver of the delinquent penalty included in the Assessment. We grant the petition as to this issue.

3. Taxpayer is not eligible for a cancellation or waiver of interest.

When the Department determines that a taxpayer has paid less tax than is properly due, it is required to assess the amount of unpaid taxes and include interest thereon. RCW 82.32.050(1). When the Department issued the Assessment to Taxpayer, it was required to include interest on the assessed tax amount.

RCW 82.32.105(3) provides the two circumstances under which the Department will waive or cancel interest:

- (a) The failure to timely pay the tax was the direct result of written instructions given the taxpayer by the department; or
- (b) The extension of a due date for payment of an assessment of deficiency was not at the request of the taxpayer and was for the sole convenience of the department.

As explained above, Taxpayer did not rely upon specific written instructions from the Department in failing to timely report and pay its tax liabilities. There is also no indication that the due date for the Quarter 3 2019 period was extended at the Department's request. Since neither circumstance under RCW 82.32.105(3) is present in this case, Taxpayer is not eligible for cancellation of interest. We deny the petition as to this issue.

DECISION AND DISPOSITION

Taxpayer's petition is granted in part and denied in part.

Dated this 9th day of November 2021.