

WSR 22-24-096

PERMANENT RULES

DEPARTMENT OF REVENUE

[Filed December 6, 2022, 1:53 p.m., effective January 6, 2023]

Effective Date of Rule: Thirty-one days after filing.

Purpose: The department of revenue is amending the below rules to recognize 2022 legislation (2SHB 1210), which changes the terminology referencing "marijuana" to "cannabis."

Citation of Rules Affected by this Order: Amending WAC 458-20-135 Extracting natural products, 458-20-136 Manufacturing, processing for hire, fabricating, 458-20-13601 Manufacturers and processors for hire—Sales and use tax exemptions for machinery and equipment, 458-20-209 Farming for hire and horticultural services performed for farmers, 458-20-210 Sales of tangible personal property for farming—Sales of agricultural products by farmers, and 458-20-244 Food and food ingredients.

Statutory Authority for Adoption: RCW 82.32.300, 82.01.060.

Adopted under notice filed as WSR 22-20-002 on September 21, 2022.

Number of Sections Adopted in Order to Comply with Federal Statute: New 0, Amended 0, Repealed 0; Federal Rules or Standards: New 0, Amended 0, Repealed 0; or Recently Enacted State Statutes: New 0, Amended 6, Repealed 0.

Number of Sections Adopted at the Request of a Nongovernmental Entity: New 0, Amended 0, Repealed 0.

Number of Sections Adopted on the Agency's own Initiative: New 0, Amended 6, Repealed 0.

Number of Sections Adopted in Order to Clarify, Streamline, or Reform Agency Procedures: New 0, Amended 0, Repealed 0.

Number of Sections Adopted using Negotiated Rule Making: New 0, Amended 0, Repealed 0; Pilot Rule Making: New 0, Amended 0, Repealed 0; or Other Alternative Rule Making: New 0, Amended 0, Repealed 0.

Date Adopted: December 6, 2022.

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Rules Coordinator

**OTS-4104.1**

AMENDATORY SECTION (Amending WSR 14-23-060, filed 11/17/14, effective 12/18/14)

**WAC 458-20-135 Extracting natural products. (1) Introduction.**

This rule explains the application of the business and occupation (B&O), retail sales, and use taxes to persons extracting natural products. Persons extracting natural products often use the same extracted products in a manufacturing process. This rule provides guidance for determining when an extracting activity ends and the manufacturing activity begins. In addition to all other taxes, commercial fishermen may be subject to the enhanced food fish excise tax levied by chapter 82.27 RCW (Tax on enhanced food fish).

Persons engaging in activities associated with timber harvest operations should refer to WAC 458-20-13501 (Timber harvest operations). Persons engaged in a manufacturing activity should also refer to WAC 458-20-136 (Manufacturing, processing for hire, fabricating) and 458-20-13601 (Manufacturers and processors for hire—Sales and use tax exemptions for machinery and equipment).

(2) **Who is an "extractor"?** RCW 82.04.100 defines the term "extractor" to mean 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 for the necessary labor or mechanical services, for sale or for commercial or industrial use mines, quarries, takes or produces coal, oil, natural gas, ore, stone, sand, gravel, clay, mineral, or other natural resource product. The term includes a person who fells, cuts, or takes timber, Christmas trees other than plantation Christmas trees, or other natural products. It also includes any person who takes fish, shellfish, or other sea or inland water foods or products.

(a) **Persons excluded from the definition of "extractor."** The term "extractor" does not include:

(i) Persons performing under contract the necessary labor or mechanical services for others (these persons are extractors for hire, see subsection (4) of this section); or

(ii) Persons who are farmers as defined in RCW 82.04.213. Refer to WAC 458-20-209 and 458-20-210 for tax-reporting information for farmers and persons selling property to or performing horticultural services for farmers; or

(iii) Persons producing (~~marijuana~~) cannabis.

(b) **When an extractor is also a manufacturer.** An extractor may subsequently take an extracted product and use it as a raw material in a manufacturing process. The following examples explain when an extracting process ends and a manufacturing process begins for various situations. These examples should be used only as a general guide. A determination of when extracting ends and manufacturing begins for other situations can be made only after a review of all of the facts and circumstances.

(i) **Mining and quarrying.** Mining and quarrying operations are extracting activities, and generally include the screening, sorting, and piling of rock, sand, stone, gravel, or ore. For example, an operation that extracts rock, then screens, sorts, and with no further processing places the rock into piles for sale, is an extracting operation.

(A) The crushing and/or blending of rock, sand, stone, gravel, or ore are manufacturing activities. These are manufacturing activities whether or not the materials were previously screened or sorted.

(B) Screening, sorting, piling, or washing of the material, when the activity takes place in conjunction with crushing or blending at the site where the materials are taken or produced, is considered a part of the manufacturing operation 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 a part of the manufacturing operation.

(ii) **Commercial fishing.** Commercial fishing operations, including the taking of any fish in Washington waters (within the statutory limits of the state of Washington) and the taking of shellfish or other sea or inland water foods or products, are extracting activities. These activities often include the removal of meat from the shell and the icing of fish or sea products.

(A) A person growing, raising, or producing a product of aquaculture as defined in RCW 15.85.020 on the person's own land or on land in which the person has a present right of possession is considered a farmer. RCW 82.04.213.

(B) Cleaning (removal of the head, fins, or viscera), filleting, and/or steaking fish are manufacturing activities. The cooking of fish or seafood is also a manufacturing activity. Refer to RCW 82.04.260 and WAC 458-20-136 for information regarding the special B&O tax rate/classification that applies to the manufacturing of seafood products that remain in a raw, raw frozen, or raw salted state.

(C) The removal of meat from the shell or the icing of fish or sea products, when the activity is performed in conjunction with and at the site where manufacturing takes place (e.g., cooking the fish or seafood), is considered a part of the manufacturing operation.

(3) **Tax-reporting responsibilities for income received by extractors.** Extractors are subject to the extracting B&O tax upon the value of the extracted products. (See WAC 458-20-112 regarding "value of products.") Extractors who sell the products at retail or wholesale in this state are subject to either the retailing or wholesaling B&O tax, as the case may be. In such cases, the extractor must report under both the "production" (extracting) and "selling" (wholesaling or retailing) classifications of the B&O tax, and claim a tax credit under the multiple activities tax credit (MATC). See also WAC 458-20-19301 (Multiple activities tax credits) for a more detailed explanation of the MATC reporting requirements. Extractors that manufacture tangible personal property that they sell to buyers who will either resell the tangible personal property without any intervening use, or will include the tangible personal property as a component or ingredient in another product for sale by the buyer to another customer, are making wholesale sales. To document the wholesale nature of any transaction, sellers making wholesale sales must obtain from the buyer a resale certificate for sales made before January 1, 2010, or reseller permit for sales made on or after January 1, 2010. See also WAC 458-20-102A (Resale certificates) and WAC 458-20-102 (Reseller permits) for a more detailed explanation of a seller's obligation to document its wholesale sales. Even though resale certificates are no longer used after December 31, 2009, they must be kept on file by the seller for five years from the date of last use or until December 31, 2014, whichever first occurs.

For example, Corporation quarries rock without further processing. Corporation sells and delivers the rock to Landscaper, who is located in Washington. Landscaper provides Corporation with a resale certificate (WAC 458-20-102A) for purchases made before January 1, 2010, or a reseller permit (WAC 458-20-102) for purchases made on or after January 1, 2010. Corporation should report under both the extracting and wholesaling B&O tax classifications, and claim a MATC per WAC 458-20-19301. Had Corporation delivered the quarried rock to an out-of-state location, Corporation would have incurred only an extracting B&O tax liability.

(a) **When extractors use their products in a manufacturing process.** Persons who extract products, use these extracted products in a manufacturing process, and then sell the products all within Washington are subject to both "production" taxes (extracting and manufacturing) and the "selling" tax (wholesaling or retailing), and may claim the appropriate credits under the MATC. (See also WAC 458-20-136 on manufacturing.)

For example, Company quarries rock (an extracting activity), crushes and blends the rock (a manufacturing activity), and sells the resulting product at retail. The taxable value of the extracted rock is \$50,000 (the amount subject to the extracting B&O tax). The taxable value of the crushed and blended rock is \$140,000 (the amount subject to the manufacturing B&O tax). The crushed and blended rock is sold for \$140,000 (the amount subject to the retailing B&O tax). Assume the tax rates for the extracting and manufacturing B&O taxes are .00484, and the tax rate for the retailing B&O tax is .00471. Company should compute its tax liability as follows:

(i) **Reporting B&O tax on the combined excise tax return:**

(A) Extracting B&O tax liability of \$242 ( $\$50,000 \times .00484$ );

(B) Manufacturing B&O tax liability of \$678 ( $\$140,000 \times .00484$ );

and

(C) Retailing B&O tax liability of \$659 ( $\$140,000 \times .00471$ ).

(ii) **Completing the multiple activities tax credit (Part II of Schedule C) :**

Activity which results in a tax credit	Taxable Amount	Business and Occupation Tax Reported					
		Extracting	Manufacturing	Wholesaling	Retailing	Total Credit	
Washington extracted products manufactured in Washington	50,000	242	242			242	
Washington extracted products sold in Washington							
Washington manufactured products sold in Washington	140,000		678		659	659	
					Multiple Activities Tax Credit Subtotal of taxes paid to Washington state		901
					Credit ID 800		901

Schedule C helps taxpayers calculate and claim the multiple activities tax credit provided by RCW 82.04.440. In the Schedule C example above, materials that a person extracts and then uses in a manufacturing process in Washington are entered at their value when extracting ceases and manufacturing begins (\$50,000 shown on the "Washington extracted products manufactured in Washington" line of the Schedule C). The taxable amount reported on the "Washington manufactured products sold in Washington" line of the Schedule C is the value of products at the point that manufacturing ceases (\$140,000), not simply the value added by the manufacturing activity. For more information and examples that are helpful in determining the value of products, refer to WAC 458-20-112 (Value of products).

(b) **When extractors sell their products at retail or wholesale.**

An extractor making retail sales must collect and remit retail sales tax on all sales to consumers, unless the sale is exempt by law (e.g., see WAC 458-20-244 regarding sales of certain food products). Extractors making wholesale sales must obtain resale certificates for sales made before January 1, 2010, or reseller permits for sales made on or after January 1, 2010, from their customers to document the wholesale nature of any transaction as provided in WAC 458-20-102A (Resale certificates) and WAC 458-20-102 (Reseller permits). Even though resale certificates are no longer used after December 31, 2009, they must be kept on file by the seller for five years from the date of last use or until December 31, 2014, whichever first occurs.

(4) **Tax-reporting responsibilities for income received by extractors for hire.** Persons performing extracting activities for extractors are subject to the extracting for hire B&O tax upon their gross income from those services.

For example, a person removing ore, waste, or overburden at a mining pit for the operator of the mining operation is an extractor for hire. Likewise, a person drilling to locate or provide access to a satisfactory grade of ore at the mining pit for the operator is also an extractor for hire. The gross income derived from these activities is subject to the extracting for hire B&O tax classification.

(5) **Mining or mineral rights.** Royalties or charges in the nature of royalties for granting another the privilege or right to remove minerals, rock, sand, or other natural resource product are subject to the service and other activities B&O tax. The special B&O tax rate provided by RCW 82.04.2907 does not apply because this statute specifically excludes compensation received for any natural resource. Refer also to RCW 82.45.035 and WAC 458-61-520 (Mineral rights and mining claims) for more information regarding the sale of mineral rights and the real estate excise tax.

Income derived from the sale or rental of real property, whether designated as royalties or another term, is exempt of the B&O tax.

(6) **Tax liability with respect to purchases of equipment or supplies and property extracted and/or manufactured for commercial or industrial use.** The retail sales tax applies to all purchases of equipment, component parts of equipment, and supplies by persons engaging in extracting or extracting for hire activities unless a specific exemption applies. If the seller fails to collect the appropriate retail sales tax, the buyer is required to remit the retail sales tax (commonly referred to as "deferred retail sales tax") or use tax directly to the department.

(a) **Exemption available for certain manufacturing equipment.** RCW 82.08.02565 and 82.12.02565 provide retail sales and use tax exemptions for certain machinery and equipment used by manufacturers and processors for hire. While this exemption does not extend to extractors or extractors for hire, persons engaged in both extracting and manufacturing activities should refer to WAC 458-20-13601 for an explanation of how these exemptions may apply to them.

(b) **Property manufactured for commercial or industrial use.** Persons manufacturing tangible personal property for commercial or industrial use are subject to both the manufacturing B&O and use taxes upon the value of the property manufactured, unless a specific exemption applies. (See also WAC 458-20-134 on commercial or industrial use.)

If the person also extracts materials used in the manufacturing process, the extracting B&O tax is due on the value of the extracted materials and a MATC may be taken. For example, Quarry extracts rock, crushes the rock into desired size, and then uses the crushed rock in its parking lot. The use of the crushed rock by Quarry in its parking lot is a commercial or industrial use. Quarry is subject to the extracting and manufacturing B&O taxes and may claim a MATC. Quarry is also responsible for remitting use tax on the value of the crushed rock applied to the parking lot.

[Statutory Authority: RCW 82.32.300, 82.01.060(2), and 82.04.100. WSR 14-23-060, § 458-20-135, filed 11/17/14, effective 12/18/14. Statutory Authority: RCW 82.32.300, 82.01.060(2), chapters 82.04, 82.08, 82.12 and 82.32 RCW. WSR 10-06-069, § 458-20-135, filed 2/25/10, effective 3/28/10. Statutory Authority: RCW 82.32.300 and 82.01.060(2). WSR

04-01-126, § 458-20-135, filed 12/18/03, effective 1/18/04. Statutory Authority: RCW 82.32.300. WSR 00-11-096, § 458-20-135, filed 5/17/00, effective 6/17/00; WSR 86-09-058 (Order ET 86-7), § 458-20-135, filed 4/17/86; WSR 83-07-034 (Order ET 83-17), § 458-20-135, filed 3/15/83. Statutory Authority: RCW 82.01.060(2) and 82.32.300. WSR 78-07-045 (Order ET 78-4), § 458-20-135, filed 6/27/78; Order ET 70-3, § 458-20-135 (Rule 135), filed 5/29/70, effective 7/1/70.]

## OTS-4105.1

AMENDATORY SECTION (Amending WSR 15-01-005, filed 12/4/14, effective 1/4/15)

### **WAC 458-20-136 Manufacturing, processing for hire, fabricating.**

(1) **Introduction.** This rule explains the application of the business and occupation (B&O), retail sales, and use taxes to manufacturers. It identifies the special tax classifications and rates that apply to specific manufacturing activities. The law provides a retail sales and use tax exemption for certain machinery and equipment (M&E) used by manufacturers. Refer to RCW 82.08.02565, 82.12.02565, and WAC 458-20-13601 (Manufacturers and processors for hire—Sales and use tax exemption for machinery and equipment) for more information regarding this exemption. Effective June 12, 2014, chapter 140, Laws of 2014 (SB 6505), machinery and equipment used directly in the manufacturing, research and development, or testing of (~~marijuana~~) cannabis, including related services, are not eligible for the M&E retail sales and use tax exemption. For purposes of this rule, "~~marijuana~~) cannabis" is any product with a THC concentration greater than .03 percent. Persons engaging in both extracting and manufacturing activities should also refer to WAC 458-20-135 (Extracting natural products) and 458-20-13501 (Timber harvest operations).

(2) **Manufacturing activities.** RCW 82.04.120 explains that the phrase "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 articles of tangible personal property is produced for sale or commercial or industrial use. The phrase includes the production or fabrication of special-made or custom-made articles.

(a) "To manufacture" includes, but is not limited to:

(i) The production or fabrication of dental appliances, devices, restorations, substitutes, or other dental laboratory products by a dental laboratory or dental technician;

(ii) The cutting, delimiting, and measuring of felled, cut, or taken trees;

(iii) The crushing and/or blending of rock, sand, stone, gravel, or ore;

(iv) The cleaning (removal of the head, fins, or viscera) of fish; and

(v) The production of compressed or liquefied natural gas for use as transportation fuel as defined in RCW 82.16.310.

(b) "To manufacture" does not include:

(i) The conditioning of seed for use in planting;

- (ii) The cubing of hay or alfalfa;
- (iii) The growing, harvesting, or producing of agricultural products;
- (iv) The cutting, grading, or ice glazing of seafood which has been cooked, frozen, or canned outside this state;
- (v) The packing of agricultural products, including sorting, washing, rinsing, grading, waxing, treating with fungicide, packaging, chilling, or placing in controlled atmospheric storage; and
- (vi) The repairing and reconditioning of tangible personal property for others.

(3) **Manufacturers and processors for hire.** RCW 82.04.110 defines "manufacturer" to mean every person who, either directly or by contracting with others for the necessary labor or mechanical services, manufactures for sale or for commercial or industrial use from his or her own materials or ingredients any articles, substances, or commodities. However, a nonresident of the state of Washington who is the owner of materials processed for it in this state by a processor for hire is not deemed to be a manufacturer in this state because of that processing. Additionally, any owner of materials from which a nuclear fuel assembly is fabricated in this state by a processor for hire is also not deemed to be a manufacturer because of such processing.

(a) The term "processor for hire" means a person who performs labor and mechanical services upon property belonging to others so that as a result a new, different, or useful article of tangible personal property is produced for sale or commercial or industrial use. Thus, a processor for hire is any person who would be a manufacturer if that person were performing the labor and mechanical services upon his or her own materials.

(b) If a particular activity is excluded from the definition of "to manufacture," a person performing the labor and mechanical services upon materials owned by another is not a processor for hire. For example, the cutting, grading, or ice glazing of seafood that has been cooked, frozen, or canned outside this state is excluded from the definition of "to manufacture." Because of this exclusion, a person who performs these activities on seafood belonging to others is not a "processor for hire."

(c) A person who produces aluminum master alloys, regardless of the portion of the aluminum provided by that person's customer, is considered a "processor for hire." RCW 82.04.110. For the purpose of this specific provision, the term "aluminum master alloy" means an alloy registered with the Aluminum Association as a grain refiner or a hardener alloy using the American National Standards Institute designating system H35.3.

(d) In some instances, a person furnishing the labor and mechanical services undertakes to produce an article, substance, or commodity from materials or ingredients furnished in part by the person and in part by the customer. Depending on the circumstances, this person will either be considered a manufacturer or a processor for hire.

(i) If the person furnishing the labor and mechanical services furnishes materials constituting less than (~~twenty~~) 20 percent of the value of all of the materials or ingredients which become a part of the produced product, that person will be presumed to be processing for hire.

(ii) The person furnishing the labor and mechanical services will be presumed to be a manufacturer if the value of the materials or ingredients furnished by the person is equal to or greater than (~~twen-~~

~~ty~~) 20 percent of the total value of all materials or ingredients which become a part of the produced product.

(iii) If the person furnishing the labor and mechanical services supplies, sells, or furnishes to the customer, before processing, (~~twenty~~) 20 percent or more in value of the materials or ingredients from which the product is produced, the person furnishing the labor and mechanical services will be deemed to be the owner of the materials and considered a manufacturer.

(e) There are occasions where a manufacturing facility and ingredients used in the manufacturing process are owned by one person, while another person performs the actual manufacturing activity. The person operating the facility and performing the manufacturing activity is a processor for hire. The owner of the facility and ingredients is the manufacturer.

(4) **Tax-reporting responsibilities for income received by manufacturers and processors for hire.** Persons who manufacture products in this state are subject to the manufacturing B&O tax upon the value of the products, including by-products (see also WAC 458-20-112 regarding "value of products"), unless the activity qualifies for one of the special tax rates discussed in subsection (5) of this rule. See also WAC 458-20-193 (Inbound and outbound interstate sales of tangible personal property).

For example, Corporation A stains door panels that it purchases. Corporation A also affixes hinges, guide wheels, and pivots to unstained door panels. Corporation B shears steel sheets to dimension, and slits steel coils to customer's requirements. The resulting products are sold and delivered to out-of-state customers. Corporation A and Corporation B are subject to the manufacturing B&O tax upon the value of these manufactured products. These manufacturing activities take place in Washington, even though the manufactured product is delivered out-of-state. A credit may be available if a gross receipts tax is paid on the selling activity to another state. (See also WAC 458-20-19301 on multiple activities tax credits.)

(a) Manufacturers who sell their products at retail or wholesale in this state are also subject to either the retailing or wholesaling B&O tax, as the case may be. In such cases, the manufacturer must report under both the "production" (manufacturing) and "selling" (wholesaling or retailing) classifications of the B&O tax, and claim a multiple activities tax credit (MATC). See also WAC 458-20-19301 for a more detailed explanation of the MATC reporting requirements. Manufacturers are making wholesale sales when their buyer will resell the tangible personal property without intervening use, or includes the tangible personal property as a component or ingredient in another product for sale by the buyer to another customer. Sellers in these wholesale sales must obtain a reseller permit from the buyer. Reseller permits replaced resale certificates effective January 1, 2010. Even though resale certificates are no longer used after December 31, 2009, they must be kept on file by the seller for five years from the date of last use or December 31, 2014, whichever first occurs. For additional information on reseller permits see WAC 458-20-102.

For example on January 1, 2010, Raw Fish Incorporated purchases raw fish that it manufactures into fillets. The resulting product is then sold at wholesale to its customer, Fish Distributor LLC. Fish Distributor LLC resells the fillets without intervening use to its customers and provides Raw Fish Incorporated with a copy of its reseller permit. Raw Fish Incorporated is subject to both the manufacturing raw seafood B&O tax upon the value of the manufactured product,



and the wholesaling B&O tax upon the gross proceeds of sale. Raw Fish Incorporated is entitled to claim a MATC.

(b) Processors for hire are subject to the processing for hire B&O tax upon the total charge made for those services, including any charge for materials furnished by the processor. The B&O tax applies whether the resulting product is delivered to the customer within or outside this state.

(c) The measure of tax for manufacturers and processors for hire with respect to "cost-plus" or "time and material" contracts includes the amount of profit or fee above cost received, plus the reimbursements or prepayments received on account of materials and supplies, labor costs, taxes paid, payments made to subcontractors, and all other costs and expenses incurred by the manufacturer or processor for hire.

(d) A manufacturing B&O tax exemption is available for the cleaning of fish, if the cleaning activities are limited to the removal of the head, fins, or viscera from fresh fish without further processing other than freezing. RCW 82.04.2403. Processors for hire performing these cleaning activities remain subject to the processing for hire B&O tax.

(e) Amounts received by hop growers or dealers for hops shipped outside the state of Washington for first use, even though the hops have been processed into extract, pellets, or powder in this state are exempt from the B&O tax. RCW 82.04.337. However, a processor for hire with respect to hops is not exempt on amounts charged for processing these products.

(f) Manufacturers and processors for hire making retail sales must collect and remit retail sales tax on all sales to consumers, unless the sale is exempt by law (e.g., see WAC 458-20-244 regarding sales of certain food products). A manufacturer or processor for hire making wholesale sales must obtain a reseller permit from the buyer. Reseller permits replaced resale certificates effective January 1, 2010. Even though resale certificates are no longer used after December 31, 2009, they must be kept on file by the seller for five years from the date of last use or December 31, 2014, whichever first occurs. For additional information on reseller permits see WAC 458-20-102.

(g) Effective July 1, 2015, a gas distribution business manufacturing or selling liquefied natural gas or compressed natural gas for use as transportation fuel is exempt from state and local public utility taxes. The sale of natural gas from which the buyer manufactures compressed natural gas or liquefied natural gas, where the compressed natural gas or liquefied natural gas is to be sold or used as transportation fuel, is also exempt from state and local public utility taxes. The gross receipts from these activities are subject to the manufacturing, wholesaling, or retailing B&O tax and local taxes, as applicable. The retail sale of compressed natural gas or liquefied natural gas is also subject to fuel taxes, if it is used in a motor vehicle. If the fuel is not used in a motor vehicle (off-road, boat, etc.) the fuel is subject to retail sales or use tax.

(5) **Manufacturing - Special tax rates/classifications.** RCW 82.04.260 provides several special B&O tax rates/classifications for manufacturers engaging in certain manufacturing activities. In all such cases the principles set forth in subsection (4) of this rule concerning multiple activities and the resulting credit provisions are also applicable.

Special tax classifications/rates are provided for the activities of:

(a) Manufacturing wheat into flour, barley into pearl barley, soybeans into soybean oil, canola into canola oil, meal, or canola by-products, or sunflower seeds into sunflower oil;

(b) Splitting or processing dried peas;

(c) Manufacturing seafood products, which remain in a raw, raw frozen, or raw salted state;

(d) Manufacturing by canning, preserving, freezing, processing, or dehydrating fresh fruits and vegetables ("fruits" and "vegetables" does not include (~~marijuana~~) cannabis);

(e) Slaughtering, breaking, and/or processing perishable meat products and/or selling the same at wholesale and not at retail; and

(f) Manufacturing nuclear fuel assemblies.

(6) **Repairing and/or refurbishing distinguished from manufacturing.** The term "to manufacture" does not include the repair or refurbishing of tangible personal property. To be considered "manufacturing," the application of labor or skill to materials must result in a "new, different, or useful article." If the activity merely restores an existing article of tangible personal property to its original utility, the activity is considered a repair or refurbishing of that property. (See WAC 458-20-173 for tax-reporting information on repairs.)

(a) In making a determination whether an activity is manufacturing as opposed to a repair or reconditioning activity, consideration is given to a variety of factors including, but not limited to:

(i) Whether the activity merely restores or prolongs the useful life of the article;

(ii) Whether the activity significantly enhances the article's basic qualities, properties, or functional nature; and

(iii) Whether the activity is so extensive that a new, different, or useful article results.

(b) The following example illustrates the distinction between a manufacturing activity resulting in a new, different, or useful article, and the mere repair or refurbishment of an existing article. This example should only be used as a general guide. The tax results of other situations must be determined after a review of all the facts and circumstances. In cases of uncertainty, persons should contact the department for a ruling.

(i) Corporation rebuilds engine cores. When received, each core is assigned an individual identification number and disassembled. The cylinder head, connecting rods, crankshaft, valves, springs, nuts, and bolts are all removed and retained for reassembly into the same engine core. Unusable components are discarded. The block is then baked to burn off dirt and impurities, then blasted to remove any residue. The cylinder walls are rebored because of wear and tear. The retained components are cleaned, and if needed straightened and/or reground. Corporation then reassembles the cores, replacing the pistons, gaskets, timing gears, crankshaft bearings, and oil pumps with new parts. The components retained from the original engine core are incorporated only into that same core.

(ii) Corporation is under these circumstances not engaging in a manufacturing activity. The engine cores are restored to their original condition, albeit with a slightly larger displacement because of wear and tear. The cores have retained their original functional nature as they run with approximately the same efficiency and horsepower. The rebuilding of these cores is not so extensive as to result in

a new, different, or useful article. Each engine core has retained its identity because all reusable components of the original core are re-assembled in the same core. Corporation has taken an existing article and extended its useful life.

(7) **Combining and/or assembly of products to achieve a special purpose as manufacturing.** The physical assembly of products from various components is manufacturing because it results in a "new, different, or useful" product, even if the cost of the assembly activity is minimal when compared with the cost of the components. For example, the bolting of a motor to a pump, whether bolted directly or by using a coupling, is a manufacturing activity. Once physically joined, the resulting product is capable of performing a pumping function that the separate components cannot.

(a) In some cases the assembly may consist solely of combining parts from various suppliers to create an entirely different product that is sold as a kit for assembly by the purchaser. In these situations, the manufacturing B&O tax applies even if the person combining the parts does not completely assemble the components, but sells them as a package. For example, a person who purchases component parts from various suppliers to create a wheelbarrow, which will be sold in a "kit" or "knock-down" condition with some assembly required by purchaser, is a manufacturer. The purchaser of the wheelbarrow kit is not a manufacturer, however, even though the purchaser must attach the handles and wheel.

(b) The department considers various factors in determining if a person combining various items into a single package is engaged in a manufacturing activity. Any single one of the following factors is not considered conclusive evidence of a manufacturing activity, though the presence of one or more of these factors raises a presumption that a manufacturing activity is being performed:

- (i) The ingredients are purchased from various suppliers;
- (ii) The person combining the ingredients attaches his or her own label to the resulting product;
- (iii) The ingredients are purchased in bulk and broken down to smaller sizes;
- (iv) The combined product is marketed at a substantially different value from the selling price of the individual components; and
- (v) The person combining the items does not sell the individual items except within the package.

(c) The following examples should be used only as a general guide. The specific facts and circumstances of each situation must be carefully examined to determine if the combining of ingredients is a manufacturing activity or merely a packaging or marketing activity. In cases of uncertainty, persons combining items into special purpose packages should contact the department for a ruling.

(i) Combining prepackaged food products and gift items into a wicker basket for sale as a gift basket is not a manufacturing activity when:

(A) The products combined in the basket retain their original packaging;

(B) The person does not attach his or her own labels to the components or the combined basket;

(C) The person maintains an inventory for sale of the individual components and does sell these items in this manner as well as the combined baskets.

(ii) Combining bulk food products and gift items into a wicker basket for sale as a gift basket is a manufacturing activity when:

(A) The bulk food products purchased by the taxpayer are broken into smaller quantities; and

(B) The taxpayer attaches its own labels to the combined basket.

(iii) Combining components into a kit for sale is not a manufacturing activity when:

(A) All components are conceived, designed, and specifically manufactured by and at the person's direction to be used with each other;

(B) The person's label is attached to or imprinted upon the components by supplier;

(C) The person packages the components with no further assembly, connection, reconfiguration, change, or processing.

(8) **Tax liability with respect to purchases of equipment or supplies and property manufactured for commercial or industrial use.** The retail sales tax applies to purchases of tangible personal property by manufacturers and processors for hire unless the property becomes an ingredient or component part of a new article produced for sale, or is a chemical used in the processing of an article for sale. If the seller fails to collect the appropriate retail sales tax, the buyer is required to remit the retail sales tax (commonly referred to as "deferred retail sales tax") or use tax directly to the department. Refer to WAC 458-20-113 for additional information about what qualifies as an ingredient or component or a chemical used in processing.

(a) RCW 82.08.02565 and 82.12.02565 provide a retail sales and use tax exemption for certain machinery and equipment used by manufacturers and/or processors for hire. Effective June 12, 2014, machinery and equipment used directly in the manufacturing, research and development, or testing of (~~marijuana~~) cannabis, including related services, are not eligible for the M&E retail sales and use tax exemption. Refer to WAC 458-20-13601 for additional information regarding how these exemptions apply.

(b) Persons manufacturing tangible personal property for commercial or industrial use are subject to both the manufacturing B&O and use taxes upon the value of the property manufactured, unless a specific exemption applies. (See also WAC 458-20-134 on commercial or industrial use.) Persons who also extract the product used as an ingredient in a manufacturing process should refer to WAC 458-20-135 for additional information regarding their tax-reporting responsibilities.

[Statutory Authority: RCW 82.32.300, 82.01.060(2), 82.04.120, 82.04.213, 82.04.260, 82.04.4266, 82.08.02565, 82.12.022, and 82.12.02565. WSR 15-01-005, § 458-20-136, filed 12/4/14, effective 1/4/15. Statutory Authority: RCW 82.32.300, 82.01.060(2), chapters 82.04, 82.08, 82.12 and 82.32 RCW. WSR 10-06-069, § 458-20-136, filed 2/25/10, effective 3/28/10. Statutory Authority: RCW 82.32.300. WSR 00-11-096, § 458-20-136, filed 5/17/00, effective 6/17/00; WSR 88-21-014 (Order 88-7), § 458-20-136, filed 10/7/88; WSR 86-20-027 (Order 86-17), § 458-20-136, filed 9/23/86; WSR 83-07-032 (Order ET 83-15), § 458-20-136, filed 3/15/83. Statutory Authority: RCW 82.01.060(2) and 82.32.300. WSR 78-07-045 (Order ET 78-4), § 458-20-136, filed 6/27/78; Order ET 71-1, § 458-20-136, filed 7/22/71; Order ET 70-3, § 458-20-136 (Rule 136), filed 5/29/70, effective 7/1/70.]

OTS-4109.1

AMENDATORY SECTION (Amending WSR 16-07-046, filed 3/14/16, effective 4/14/16)

**WAC 458-20-13601 Manufacturers and processors for hire—Sales and use tax exemptions for machinery and equipment. (1) Introduction.**

(a) This rule explains the retail sales and use tax exemptions provided by RCW 82.08.02565 and 82.12.02565 for sales to or use by manufacturers or processors for hire of machinery and equipment (M&E) used directly in a manufacturing operation or research and development operation. This rule explains the requirements that must be met to substantiate a claim of exemption. For information regarding the sales and use tax deferral for manufacturing and research/development activities in high unemployment counties, refer to WAC 458-20-24001 and chapter 82.60 RCW. For the high technology business sales and use tax deferral refer to chapter 82.63 RCW.

(b) Effective June 12, 2014, the retail sales and use tax exemptions provided by RCW 82.08.02565 and 82.12.02565 do not apply to:

(i) Sales of machinery and equipment used directly in the manufacturing, research and development, or testing of (~~marijuana~~) cannabis; and

(ii) Sales of or charges made for labor and services rendered in respect to installing, repairing, cleaning, altering, or improving such machinery and equipment.

(c) Effective August 1, 2015, an ineligible person, as defined in subsection (2)(e) of this rule, does not qualify for the retail sales and use tax exemptions provided by RCW 82.08.02565 and 82.12.02565, unless the taxpayer first used the qualifying machinery and equipment in this state prior to August 1, 2015.

(2) **Definitions.** For purposes of the manufacturing machinery and equipment tax exemptions, the following definitions apply:

(a) **Affiliated group.** "Affiliated group" means a group of two or more entities that are either:

(i) Affiliated as defined in RCW 82.32.655; or

(ii) Permitted to file a consolidated return for federal income tax purposes.

(b) **Cogeneration.** "Cogeneration" means the simultaneous generation of electrical energy and low-grade heat from the same fuel. See RCW 82.08.02565.

(c) **Device.** "Device" means an item that is not attached to the building or site. Examples of devices are: Forklifts, chainsaws, air compressors, clamps, free standing shelving, software, ladders, wheelbarrows, and pulleys.

(d) **Industrial fixture.** "Industrial fixture" means an item attached to a building or to land. Fixtures become part of the real estate to which they are attached and at the time of attachment are classified as real property, not personal property. Examples of "industrial fixtures" are fuel oil lines, boilers, craneways, and certain concrete slabs.

(e) **Ineligible person.** "Ineligible person" means all members of an affiliated group if all of the following apply:

(i) At least one member of the affiliated group was registered with the department of revenue (department) to do business in Washington state on or before July 1, 1981;

(ii) As of August 1, 2015, the combined employment in this state of the affiliated group exceeds (~~forty thousand~~) 40,000 full-time

and part-time employees, based on data reported to the employment security department by the affiliated group; and

(iii) The business activities of the affiliated group primarily include development, sales, and licensing of computer software and services.

(f) **Machinery and equipment (M&E).** "Machinery and equipment" means industrial fixtures, devices, and support facilities, and tangible personal property that becomes an ingredient or component thereof, including repair parts and replacement parts. M&E includes pollution control equipment installed and used in a qualifying operation to prevent air pollution, water pollution, or contamination that might otherwise result from the operation.

(g) **Manufacturer.** "Manufacturer" has the same meaning as provided in chapter 82.04 RCW. Manufacturer also includes a person that prints newspapers or other materials; and effective August 1, 2015, a person engaged in the development of prewritten computer software that is not transferred to purchasers by means of tangible storage media. RCW 82.08.02565, chapter 5, Laws of 2015 3rd sp. sess. (ESSB 6138).

(h) **Manufacturing.** "Manufacturing" has the same meaning as "to manufacture" in chapter 82.04 RCW.

(i) **Manufacturing operation.** "Manufacturing operation" means the manufacturing of articles, substances, or commodities for sale as tangible personal property. A manufacturing operation begins at the point where the raw materials enter the manufacturing site and ends at the point where the processed material leaves the manufacturing site. The operation includes storage of raw materials at the site, the storage of in-process materials at the site, and the storage of the processed material at the site. The manufacturing operation is defined in terms of a process occurring at a location. To be eligible as a qualifying use of M&E, the use must take place within the manufacturing operation, unless specifically exempted by law. Storage of raw material or other tangible personal property, packaging of tangible personal property, and other activities that potentially qualify under the "used directly" criterion, and that do not constitute manufacturing in and of themselves, are not within the scope of the exemption unless they take place at a manufacturing site. The statute specifically allows testing to occur away from the site.

The term "manufacturing operation" also includes that portion of a cogeneration project that is used to generate power for consumption within the manufacturing site of which the cogeneration project is an integral part. The term does not include the production of electricity by a light and power business as defined in RCW 82.16.010 or the preparation of food products on the premises of a person selling food products at retail.

(i) Neither duration or temporary nature of the manufacturing activity nor mobility of the equipment determine whether a manufacturing operation exists. For example, operations using portable saw mills or rock crushing equipment are considered "manufacturing operations" if the activity in which the person is engaged is manufacturing. Rock crushing equipment that deposits material onto a roadway is not used in a manufacturing operation because this is a part of the constructing activity, not a manufacturing activity. Likewise, a concrete mixer used at a construction site is not used in a manufacturing operation because the activity is constructing, not manufacturing. Other portable equipment used in nonmanufacturing activities, such as continuous gutter trucks or trucks designed to deliver and combine aggregate, or specialized carpentry tools, do not qualify for the same reasons.

(ii) Manufacturing tangible personal property for sale can occur in stages, taking place at more than one manufacturing site. For example, if a taxpayer processes pulp from wood at one site, and transfers the resulting pulp to another site that further manufactures the product into paper, two separate manufacturing operations exist. The end product of the manufacturing activity must result in an article, substance, or commodity for sale.

(j) **((Marijuana)) Cannabis.** "((Marijuana)) Cannabis" is any product with a THC concentration greater than ~~((-03))~~ .3 percent.

(k) **Processor for hire.** "Processor for hire" has the same meaning as used in chapter 82.04 RCW and as explained in WAC 458-20-136 Manufacturing, processing for hire, fabricating.

(l) **Qualifying operation.** "Qualifying operation" means a manufacturing operation, a research and development operation, or a testing operation.

(m) **Research and development operation.** "Research and development operation" means engaging in research and development as defined in RCW 82.63.010 by a manufacturer or processor for hire. RCW 82.63.010 defines "research and development" to mean: Activities performed to discover technological information, and technical and nonroutine activities concerned with translating technological information into new or improved products, processes, techniques, formulas, inventions, or software. The term includes exploration of a new use for an existing drug, device, or biological product if the new use requires separate licensing by the Federal Food and Drug Administration under chapter 21, C.F.R., as amended. The term does not include adaptation or duplication of existing products where the products are not substantially improved by application of the technology, nor does the term include surveys and studies, social science and humanities research, market research or testing, quality control, sale promotion and service, computer software developed for internal use, and research in areas such as improved style, taste, and seasonal design.

(n) **Sale.** "Sale" has the same meaning as "sale" in chapter 82.08 RCW, which includes by reference RCW 82.04.040. RCW 82.04.040 includes by reference the definition of "retail sale" in RCW 82.04.050. "Sale" includes renting or leasing, conditional sale contracts, leases with option to purchase, and any contract under which possession of the property is given to the purchaser but title is retained by the vendor as security for the payment of the purchase price.

(o) **Site.** "Site" means the location at which the manufacturing or testing takes place.

(p) **Support facility.** "Support facility" means a part of a building, or a structure or improvement, used to contain or steady an industrial fixture or device. A support facility must be specially designed and necessary for the proper functioning of the industrial fixture or device and must perform a function beyond being a building or a structure or an improvement. It must have a function relative to an industrial fixture or a device. To determine if some portion of a building is a support facility, the parts of the building are examined. For example, a highly specialized structure, like a vibration reduction slab under a microchip clean room, is a support facility. Without the slab, the delicate instruments in the clean room would not function properly. The ceiling and walls of the clean room are not support facilities if they only serve to define the space and do not have a function relative to an industrial fixture or a device.

(q) **Tangible personal property.** "Tangible personal property" has its ordinary meaning.

(r) **Testing.** "Testing" means activities performed to establish or determine the properties, qualities, and limitations of tangible personal property.

(s) **Testing operation.** "Testing operation" means the testing of tangible personal property for a manufacturer or processor for hire. A testing operation begins at the point where the tangible personal property enters the testing site and ends at the point where the tangible personal property leaves the testing site. The term also includes that portion of a cogeneration project that is used to generate power for consumption within the site of which the cogeneration project is an integral part. The term does not include the production of electricity by a light and power business as defined in RCW 82.16.010 or the preparation of food products on the premises of a person selling food products at retail. The testing operation is defined in terms of a process occurring at a location. To be eligible as a qualifying use of M&E, the use must take place within the testing operation, unless specifically excepted by law.

(3) **Retail sales and use tax exemptions.** The M&E exemptions provide retail sales and use tax exemptions for machinery and equipment used directly in a manufacturing operation or research and development operation, except for such sales or use relating to (~~marijuana~~) cannabis effective June 12, 2014. Sales of or charges made for labor and services rendered in respect to installing, repairing, cleaning, altering, or improving qualifying machinery and equipment are also exempt from sales tax, except for such sales or charges relating to (~~marijuana~~) cannabis effective June 12, 2014. However, because the exemption is limited to items with a useful life of one year or more, some charges for repair, labor, services, and replacement parts may not be eligible for the exemption. In the case of labor and service charges that cover both qualifying and nonqualifying repair and replacement parts, the labor and services charges are presumed to be exempt. If all of the parts are nonqualifying, the labor and service charge is not exempt, unless the parts are incidental to the service being performed, such as cleaning, calibrating, and adjusting qualifying machinery and equipment.

The exemption may be taken for qualifying machinery and equipment used directly in a testing operation by a person engaged in testing for a manufacturer or processor for hire, with the exception of such testing relating to (~~marijuana~~) cannabis effective June 12, 2014.

Sellers remain subject to the retailing B&O tax on all sales of machinery and equipment to consumers if delivery is made within the state of Washington, notwithstanding that the sale may qualify for an exemption from the retail sales tax.

(a) **Sales tax.** The purchaser must provide the seller with an exemption certificate. The exemption certificate must be completed in its entirety. The seller must retain a copy of the certificate as a part of its records. This certificate may be issued for each purchase or in blanket form certifying all future purchases as being exempt from sales tax. Blanket certificates are valid for as long as the buyer and seller have a recurring business relationship. A "recurring business relationship" means at least one sale transaction within a period of (~~twelve~~) 12 consecutive months. RCW 82.08.050 (7)(c).

The form must contain the following information:

- (i) Name, address, and registration number of the buyer;
- (ii) Name of the seller;
- (iii) Name and title of the authorized agent of the buyer/user;
- (iv) Authorized signature;



(v) Date; and

(vi) Whether the form is a single use or blanket-use form.

A copy of an M&E certificate form may be obtained from the department's website at [dor.wa.gov](http://dor.wa.gov), or by contacting the department's taxpayer services division at:

Taxpayer Services  
Department of Revenue  
P.O. Box 47478  
Olympia, WA 98504-7478  
1-800-647-7706

(b) **Use tax.** The use tax complements the retail sales tax by imposing a tax of like amount on the use within this state as a consumer of any tangible personal property purchased at retail, where the user has not paid retail sales tax with respect to the purchase of the property used. For additional information on use tax see chapter 82.12 RCW and WAC 458-20-178. If the seller fails to collect the appropriate retail sales tax, the purchaser is required to pay the retail sales tax (commonly referred to as "deferred sales tax") or the use tax directly to the department unless the purchase and/or use is exempt from the retail sales and/or use taxes. A qualifying person using eligible machinery and equipment in Washington in a qualifying manner is exempt from the use tax. If an item of machinery and equipment that was eligible for use tax or sales tax exemption fails to overcome the majority use threshold or is entirely put to use in a nonqualifying manner, use tax is due on the fair market value at the time the item was put to nonqualifying use. See subsection (9) of this rule for an explanation of the majority use threshold.

(4) **Who may take the exemption?** The exemption may be taken by a manufacturer or processor for hire who manufactures articles, substances, or commodities for sale as tangible personal property (excluding (~~marijuana~~) cannabis), and who, for the item in question, meets the used directly test and overcomes the majority use threshold. (See subsection (8) of this rule for a discussion of the "used directly" criterion and see subsection (9) of this rule for an explanation of the majority use threshold.) However, for research and development operations, there is no requirement that the operation produce tangible personal property for sale. A processor for hire who does not sell tangible personal property is eligible for the exemption if the processor for hire manufactures articles, substances, or commodities that will be sold by the manufacturer. For example, a person who is a processor for hire but who is manufacturing with regard to tangible personal property that will be used by the manufacturer, rather than sold by the manufacturer, is not eligible. For additional information on manufacturing, processing for hire, or fabricating, see WAC 458-20-136 and RCW 82.04.110. Persons who engage in testing for manufacturers or processors for hire are eligible for the exemption. To be eligible for the exemption, the taxpayer need not be a manufacturer or processor for hire in the state of Washington, but must meet the definition of manufacturer provided in subsection (2)(g) of this rule.

(5) **What is eligible for the exemption?** Machinery and equipment used directly in a qualifying operation by a qualifying person is eligible for the exemption, subject to overcoming the majority use threshold.

There are three classes of eligible machinery and equipment: Industrial fixtures, devices, and support facilities. Also eligible is tangible personal property that becomes an ingredient or component of

the machinery and equipment, including repair parts and replacement parts. "Machinery and equipment" also includes pollution control equipment installed and used in a qualifying operation to prevent air pollution, water pollution, or contamination that might otherwise result from the operation.

(6) **What is not eligible for the exemption?** In addition to items that are not eligible because they do not meet the used directly test or fail to overcome the majority use threshold, the following four categories of property are statutorily excluded from eligibility:

(a) **Hand-powered tools.** Screw drivers, hammers, clamps, tape measures, and wrenches are examples of hand-powered tools. Electric powered, including cordless tools, are not hand-powered tools, nor are calipers, plugs used in measuring, or calculators.

(b) **Property with a useful life of less than one year.** All eligible machinery and equipment must satisfy the useful life criterion, including repair parts and replacement parts. For example, items such as blades and bits are generally not eligible for the exemption because, while they may become component parts of eligible machinery and equipment, they generally have a useful life of less than one year. Blades generally having a useful life of one year or more, such as certain sawmill blades, are eligible. See subsection (7) of this rule for thresholds to determine useful life.

(c) **Buildings.** Buildings, other than machinery and equipment that is permanently affixed to or becomes a physical part of a building. Buildings provide work space for people or shelter machinery and equipment or tangible personal property. The building itself is not eligible, however some of its components might be eligible for the exemption. The industrial fixtures and support facilities that become affixed to or part of the building might be eligible. The subsequent real property status of industrial fixtures and support facilities does not affect eligibility for the exemption.

(d) **Building fixtures.** Building fixtures that are not integral to the manufacturing operation, testing operation, or research and development operation that are permanently affixed to and become a physical part of a building, such as utility systems for heating, ventilation, air conditioning, communications, plumbing, or electrical. Examples of nonqualifying fixtures are: Fire sprinklers, building electrical systems, or washroom fixtures. Fixtures that are integral to the manufacturing operation might be eligible, depending on whether the item meets the other requirements for eligibility, such as the used directly test.

(7) **The "useful life" threshold.** RCW 82.08.02565 has a per se exception for "property with a useful life of less than one year." Property that meets this description is not eligible for the M&E exemption. The useful life threshold identifies items that do not qualify for the exemption, such as supplies, consumables, and other classes of items that are not expected or intended to last a year or more. For example, tangible personal property that is acquired for a one-time use and is discarded after use, such as a mold or a form, has a useful life of less than one year and is not eligible. If it is clear from taxpayer records or practice that an item is used for at least one year, the item is eligible, regardless of the answers to the four threshold questions. A taxpayer may work directly with the department to establish recordkeeping methods that are tailored to the specific circumstances of the taxpayer. The following steps should be used to determine whether an item meets the "useful life" threshold. The series of questions progress from simple documentation to complex docu-

mentation. To substantiate qualification under any step, a taxpayer must maintain adequate records or be able to establish by demonstrating through practice or routine that the threshold is overcome. Catastrophic loss, damage, or destruction of an item does not affect eligibility of machinery and equipment that otherwise qualifies. Assuming the machinery and equipment meets all of the other M&E requirements and does not have a single one-time use or is not discarded during the first year, useful life should be determined by answering the following questions for an individual piece of machinery and equipment:

(a) Is the machinery and equipment capitalized for either federal tax purposes or accounting purposes?

- If the answer is "yes," it qualifies for the exemption.
- If the answer is "no,"

(b) Is the machinery and equipment warranted by the manufacturer to last at least one year?

- If the answer is "yes," it qualifies for the exemption.
- If the answer is "no,"

(c) Is the machinery and equipment normally replaced at intervals of one year or more, as established by industry or business practice? (This is commonly based on the actual experience of the person claiming the exemption.)

- If the answer is "yes," it qualifies for the exemption.
- If the answer is "no,"

(d) Is the machinery and equipment expected at the time of purchase to last at least one year, as established by industry or business practice? (This is commonly based on the actual experience of the person claiming the exemption.)

- If the answer is "yes," it qualifies for the exemption.
- If the answer is "no," it does not qualify for the exemption.

(8) **The "used directly" criteria.** Items that are not "used directly" in a qualifying operation are not eligible for the exemption. The statute provides eight descriptions of the phrase "used directly." The manner in which a person uses an item of machinery and equipment must match one of these descriptions. Examples of items that are not used directly in a qualifying operation are cafeteria furniture, safety equipment not part of qualifying M&E, packaging materials, shipping materials, or administrative equipment. Machinery and equipment is "used directly" in a manufacturing operation, testing operation, or research and development operation, if the machinery and equipment meets any one of the following criteria:

(a) **Acts on or interacts with.** It acts on or interacts with an item of tangible personal property. Examples include drill presses, concrete mixers (agitators), ready-mix concrete trucks, hot steel rolling machines, rock crushers, and band saws. Also included is machinery and equipment used to repair, maintain, or install tangible personal property. Computers qualify under this criterion if:

(i) They direct or control machinery or equipment that acts on or interacts with tangible personal property; or

(ii) If they act on or interact with an item of tangible personal property.

(b) **Conveys, transports, handles, or temporarily stores.** It conveys, transports, handles, or temporarily stores an item of tangible personal property at the manufacturing site or the testing site. Examples include wheelbarrows, handcarts, storage racks, forklifts, tanks, vats, robotic arms, piping, and concrete storage pads. Floor space in buildings does not qualify under this criterion. Also not eligible under this criterion are items that are used to ship the product or in

which the product is packaged, as well as materials used to brace or support an item during transport.

(c) **Controls, guides, measures, verifies, aligns, regulates or tests.** It controls, guides, measures, verifies, aligns, regulates, or tests tangible personal property at the site or away from the site. Examples of "away from the site" are road testing of trucks, air testing of planes, or water testing of boats, with the machinery and equipment used off site in the testing eligible under this criterion. Machinery and equipment used to take readings or measurements is eligible under this criterion.

(d) **Provides physical support.** It provides physical support for or access to tangible personal property. Examples include catwalks adjacent to production equipment, scaffolding around tanks, braces under vats, and ladders near controls. Machinery and equipment used for access to the building or to provide a work space for people or a space for tangible personal property or machinery and equipment, such as stairways or doors, is not eligible under this criterion.

(e) **Produces power or lubricates.** It produces power for or lubricates machinery and equipment. A generator providing power to a sander is an example of machinery and equipment that produces such power. An electrical generating plant that provides power for a building is not eligible under this criterion. Lubricating devices, such as hoses, oil guns, pumps, and meters, whether or not attached to machinery and equipment, are eligible under this criterion.

(f) **Produces another item.** It produces another item of tangible personal property for use in the manufacturing operation, testing operation, or research and development operation. Examples include machinery and equipment that make dies, jigs, or molds, and printers that produce camera-ready images.

(g) **Packs.** It places tangible personal property in the container, package, or wrapping in which the tangible personal property is normally sold or transported.

(h) **Is integral to research and development.** It is integral to "research and development" as it is defined in RCW 82.63.010.

(9) **The majority use threshold.**

(a) **M&E used both in a qualifying and nonqualifying manner.** Machinery and equipment used both directly in a qualifying operation and also in a nonqualifying manner is eligible for the exemption only if the qualifying use satisfies the majority use requirement. Examples of situations in which an item of machinery and equipment is used for qualifying and nonqualifying purposes include: The use of machinery and equipment in manufacturing and repair activities, such as using a power saw to make cabinets in a shop versus using it to make cabinets at a customer location; the use of machinery and equipment in manufacturing and constructing activities, such as using a forklift to move finished sheet rock at the manufacturing site versus using it to unload sheet rock at a customer location; and the use of machinery and equipment in manufacturing and transportation activities, such as using a mixer truck to make concrete at a manufacturing site versus using it to deliver concrete to a customer. Majority use can be expressed as a percentage, with the minimum required amount of qualifying use being greater than ((fifty)) 50 percent compared to overall use. To determine whether the majority use requirement has been satisfied, the person claiming the exemption must retain records documenting the measurement used to substantiate a claim for exemption or, if time, value, or volume is not the basis for measurement, be able to establish by demonstrating through practice or routine that the re-

quirement is satisfied. Majority use is measured by looking at the use of an item during a calendar year using any of the following:

(i) **Time.** Time is measured using hours, days, or other unit of time, with qualifying use of the M&E the numerator, and total time used the denominator. Suitable records for time measurement include employee time sheets or equipment time use logs.

(ii) **Value.** Value means the value to the person, measured by revenue if both the qualifying and nonqualifying uses produce revenue. Value is measured using gross revenue, with revenue from qualifying use of the M&E the numerator, and total revenue from use of the M&E the denominator. If there is no revenue associated with the use of the M&E, such as in-house accounting use of a computer system, the value basis may not be used. Suitable records for value measurement include taxpayer sales journals, ledgers, account books, invoices, and other summary records.

(iii) **Volume.** Volume is measured using amount of product, with volume from qualifying use of the M&E the numerator and total volume from use of the M&E the denominator. Suitable records for volume measurement include production numbers, tonnage, and dimensions.

(iv) **Other comparable measurement for comparison.** The department may agree to allow a taxpayer to use another measure for comparison, provided that the method results in a comparison between qualifying and nonqualifying uses. For example, if work patterns or routines demonstrate typical behavior, the taxpayer with the department's approval can satisfy the majority use test using work site surveys as proof.

(b) **Bundling similar M&E into classes.** Each piece of M&E does not require a separate record if the taxpayer can establish that it is reasonable to bundle M&E into classes. Classes may be created only from similar pieces of machinery and equipment and only if the uses of the pieces are the same. For example, forklifts of various sizes and models can be bundled together if the forklifts are doing the same work, as in moving wrapped product from the assembly line to a storage area. An example of when not to bundle classes of M&E for purposes of the majority use threshold is the use of a computer that controls a machine through numerical control versus use of a computer that creates a camera ready page for printing.

(c) **Industry-wide standards.** Typically, whether the majority use threshold is met is decided on a case-by-case basis, looking at the specific manufacturing operation in which the item is being used. However, for purposes of applying the majority use threshold, the department may develop industry-wide standards. For instance, the aggregate industry uses concrete mixer trucks in a consistent manner across the industry. Based on a comparison of selling prices of the processed product picked up by the customer at the manufacturing site and delivery prices to a customer location, and taking into consideration the qualifying activity (interacting with tangible personal property) of the machinery and equipment compared to the nonqualifying activity (delivering the product) of the machinery and equipment, the department has determined that concrete trucks qualify under the majority use threshold. Only in those limited instances where it is apparent that the use of the concrete truck is atypical for the industry would the taxpayer be required to provide recordkeeping on the use of the truck to support the exemption.

[Statutory Authority: RCW 82.32.300 and 82.01.060(2). WSR 16-07-046, § 458-20-13601, filed 3/14/16, effective 4/14/16. Statutory Authority: RCW 82.32.300, 82.01.060(2), 82.04.120, 82.04.213, 82.04.260,

82.04.4266, 82.08.02565, 82.12.022, and 82.12.02565. WSR 15-01-005, § 458-20-13601, filed 12/4/14, effective 1/4/15. Statutory Authority: RCW 82.32.300, 82.01.060(2), 82.08.02565, and 82.12.02565. WSR 08-14-024, § 458-20-13601, filed 6/20/08, effective 7/21/08. Statutory Authority: RCW 82.32.300. WSR 00-11-096, § 458-20-13601, filed 5/17/00, effective 6/17/00.]

## OTS-4106.1

AMENDATORY SECTION (Amending WSR 15-01-007, filed 12/4/14, effective 1/4/15)

**WAC 458-20-209 Farming for hire and horticultural services performed for farmers.** (1) **Introduction.** This rule provides tax reporting information for persons performing horticultural services for farmers. Persons providing horticultural services to persons other than farmers should refer to WAC 458-20-226 (Landscape and horticultural services). Farmers and persons making sales to farmers may also want to refer to the following rules:

(a) WAC 458-20-210 (Sales of tangible personal property for farming—Sales of agricultural products by farmers); and

(b) WAC 458-20-239 (Sales to nonresidents of farm machinery or implements, and related services).

(2) **Definitions.** For the purposes of this rule, the following definitions apply:

(a) "Farmer" means any person engaged in the business of growing, raising, or producing, upon the person's own lands or upon the lands in which the person has a present right of possession, any agricultural product to be sold. "Farmer" does not include a person growing, raising, or producing such products for the person's own consumption; a person selling any animal or substance obtained therefrom in connection with the person's business of operating a stockyard or a slaughter or packing house; or a person in respect to the business of taking, cultivating, or raising timber. RCW 82.04.213.

(b) "Agricultural product" means any product of plant cultivation or animal husbandry including, but not limited to: A product of horticulture, grain cultivation, vermiculture, viticulture, or aquaculture as defined in RCW 15.85.020; plantation Christmas trees; short-rotation hardwoods as defined in RCW 84.33.035; turf; or any animal including, but not limited to, an animal that is a private sector cultured aquatic product as defined in RCW 15.85.020, or a bird, or insect, or the substances obtained from such an animal. "Agricultural product" does not include animals defined as pet animals under RCW 16.70.020. Effective June 12, 2014, "agricultural product" may not be construed to include (~~marijuana. Marijuana~~) cannabis. Cannabis is any product with a THC concentration greater than (~~(.03)~~) .3 percent. RCW 82.04.213.

(c) "Horticultural services" include services related to the cultivation of vegetables, fruits, grains, field crops, ornamental floriculture, and nursery products.

(i) The term "horticultural services" includes, but is not limited to, the following:

(A) Soil preparation services such as plowing or weed control before planting;

(B) Crop cultivation services such as planting, thinning, pruning, or spraying; and

(C) Crop harvesting services such as threshing grain, mowing and baling hay, or picking fruit.

(ii) Effective June 12, 2014, horticultural services does not include services related to the cultivation of (~~marijuana. Marijuana~~) cannabis. Cannabis is any product with a THC concentration greater than (~~(.03)~~) .3 percent.

(3) **Business and occupation (B&O) tax.** Persons performing horticultural services for farmers are generally subject to the service and other business activities B&O tax upon the gross proceeds. However, if the person providing horticultural services also sells tangible personal property for a separate and distinct charge, the charge made for the tangible personal property will be subject to either the wholesaling or retailing B&O tax, depending on the nature of the sale. Persons making sales of tangible personal property to farmers should refer to WAC 458-20-210 to determine whether the wholesaling or retailing tax applies, and under what circumstances retail sales tax must be collected.

(a) A farmer who occasionally assists another farmer in planting or harvesting a crop is generally not considered to be engaged in the business of performing horticultural services. These activities are generally considered to be casual and incidental to the farming activity. For example, a farmer owning baling equipment which is used primarily for baling hay produced by the farmer, but who may occasionally accommodate neighboring farmers by baling small quantities of hay produced by them, is not considered to be in business with respect thereto.

(b) The extent to which horticultural services are performed for others is determinative of whether or not they are considered taxable business activities. Persons who advertise or hold themselves out to the public as being available to perform farming for hire will be considered as being engaged in business. For example, a person who regularly engages in baling hay or threshing grain for others is engaged in business and taxable upon the gross proceeds derived therefrom, irrespective of the amount of such business or that this person also does some farming of his or her own land.

(c) In cases where doubt exists in determining whether or not a person is engaged in the business of performing horticultural services, all pertinent information should be submitted to the department of revenue (department) for a specific ruling. The department may be contacted using the website [dor.wa.gov](http://dor.wa.gov) and selecting "contact us"; or by telephone at 1-800-647-7706.

(4) **Deferred sales or use tax.** If the seller fails to collect the appropriate retail sales tax, the purchaser is required to pay the deferred sales or use tax directly to the department.

(a) Purchases of machinery, machinery parts and repair, tools, and cleaning materials by persons performing horticultural services are subject to retail sales tax.

(b) Persons taxable under the service and other business activities B&O tax classification are defined as consumers of anything they use in performing their services. (Refer to RCW 82.04.190.) As such, these persons are required to pay retail sales or use tax upon the purchase of all items used in performing the service, such as fertil-

izers, spray materials, and baling wire, which are not sold separate and apart from the service they perform.

(5) **Examples.** The following examples identify a number of facts and then state a conclusion. These examples should be used only as a general guide. The tax results of other situations must be determined after a review of all of the facts and circumstances.

(a) John Doe is a wheat farmer owning threshing equipment which is generally used only for threshing his own wheat. Occasionally a neighbor's threshing equipment may break down and John will use his own equipment to assist the neighbor in completing the neighbor's wheat harvest. While John receives payment for providing the threshing assistance, this activity is considered to be a casual and isolated sale. John does not hold himself out as being in the business of performing farming (threshing) for hire. John Doe is not considered to be engaging in taxable business activities. The amounts John Doe receives for assisting in the harvest of his neighbors' wheat is not subject to tax.

(b) X Spraying applies fertilizer to orchards owned by Farmer A. The sales invoice provided to Farmer A by X Spraying reflects a "lump sum" amount with no segregation of charges for the fertilizer and the application. When reporting its tax liability, X Spraying would report the total charge under the service B&O tax classification. X Spraying must also remit retail sales or use tax upon the purchase of the fertilizer. The entire amount charged by X Spraying is for horticultural services, and X Spraying is considered the consumer of the fertilizer.

(c) Z Flying aerial sprays pesticides on crops owned by Farmer B. The sales invoice Z Flying provides to Farmer B segregates the charge for the pesticides and the charge for the application. When reporting its tax liability, Z Flying would report the charge for the application under the service B&O tax classification. The charge for the sale of the spray materials is subject to the wholesaling B&O tax provided it is properly documented by a reseller permit. Reseller permits replaced resale certificates effective January 1, 2010. For additional information on reseller permits see WAC 458-20-102. Z Flying's purchase of the pesticides is a purchase for resale and not subject to the retail sales tax. Even though resale certificates are no longer used after December 31, 2009, they must be kept on file by Z Flying for five years from the date of last use or December 31, 2014, whichever first occurs.

[Statutory Authority: RCW 82.32.300 and 82.01.060(2). WSR 15-01-007, § 458-20-209, filed 12/4/14, effective 1/4/15. Statutory Authority: RCW 82.32.300, 82.01.060(2), chapters 82.04, 82.08, 82.12 and 82.32 RCW. WSR 10-06-070, § 458-20-209, filed 2/25/10, effective 3/28/10. Statutory Authority: RCW 82.32.300. WSR 94-07-050, § 458-20-209, filed 3/10/94, effective 4/10/94; WSR 83-08-026 (Order ET 83-1), § 458-20-209, filed 3/30/83; Order ET 70-3, § 458-20-209 (Rule 209), filed 5/29/70, effective 7/1/70.]

**OTS-4107.1**



AMENDATORY SECTION (Amending WSR 19-02-057, filed 12/27/18, effective 1/27/19)

**WAC 458-20-210 Sales of tangible personal property for farming—Sales of agricultural products by farmers.** (1) **Introduction.** This rule explains the application of business and occupation (B&O), retail sales, and use taxes to the sale and/or use of feed, seed, fertilizer, spray materials, and other tangible personal property for farming. This rule also explains the application of B&O, retail sales, and litter taxes to the sale of agricultural products by farmers. Farmers should refer to WAC 458-20-101 (Tax registration and tax reporting) to determine whether they must obtain a tax registration endorsement or a temporary registration certificate from the department of revenue (department).

(a) **Examples.** This rule contains examples that identify a number of facts and then state a conclusion. These examples should be used only as a general guide. The tax results of other situations must be determined after a review of all facts and circumstances.

(b) **Other rules that may be relevant.** Farmers and persons making sales to farmers may also want to refer to rules in the following list for additional information:

(i) WAC 458-20-178 Use tax and the use of tangible personal property;

(ii) WAC 458-20-209 Farming for hire and horticultural services performed for farmers;

(iii) WAC 458-20-222 Veterinarians;

(iv) WAC 458-20-239 Sales to nonresidents of farm machinery or implements, and related services;

(v) WAC 458-20-243 Litter tax; and

(vi) WAC 458-20-262 Retail sales and use tax exemptions for agricultural employee housing.

(2) **Who is a farmer?** A "farmer" is any person engaged in the business of growing, raising, or producing, on the person's own lands or on the lands in which the person has a present right of possession, any agricultural product to be sold. Effective July 1, 2015, a "farmer" also includes eligible apiarists that grow, raise, or produce honey bee products for sale, or provide bee pollination services. A "farmer" does not include a person growing, raising, or producing agricultural products for the person's own consumption; a person selling any animal or substance obtained therefrom in connection with the person's business of operating a stockyard, slaughterhouse, or packing house; or a person in respect to the business of taking, cultivating, or raising timber. RCW 82.04.213.

(3) **What is an agricultural product?** An "agricultural product" is any product of plant cultivation or animal husbandry including, but not limited to: A product of horticulture, grain cultivation, vermiculture, viticulture, or aquaculture as defined in RCW 15.85.020; plantation Christmas trees; short-rotation hardwoods as defined in RCW 84.33.035; turf; or any animal, including, but not limited to, an animal that is a private sector cultured aquatic product as defined in RCW 15.85.020, a bird, an insect, or the substances obtained from such animals. Effective July 1, 2015, "agricultural product" includes honey bee products. An "agricultural product" does not include animals defined under RCW 16.70.020 as "pet animals." Effective June 12, 2014, RCW 82.04.213 excludes (~~marijuana~~) cannabis from the definition of

"agricultural product." ((Marijuana)) Cannabis is any product with a THC concentration greater than ((.03)) .3 percent. RCW 82.04.213.

(4) **Who is an eligible apiarist?** An "eligible apiarist" is a person who owns or keeps one or more bee colonies and who grows, raises, or produces honey bee products for sale at wholesale and is registered under RCW 15.60.021.

(5) **What are honey bee products?** "Honey bee products" are queen honey bees, packaged honey bees, honey, pollen, bees wax, propolis, or other substances obtained from honey bees. "Honey bee products" do not include manufactured substances or articles.

(6) **What is ((marijuana)) cannabis?** ((Marijuana)) Cannabis is any product with a THC concentration greater than ((.03)) .3 percent. For additional information on ((marijuana)) cannabis see RCW 69.50.101.

(7) **Sales to farmers.** Persons making sales of tangible personal property to farmers are generally subject to wholesaling or retailing B&O tax, as the case may be, on the gross proceeds of sales. Sales of some services performed for farmers, such as installing or repairing tangible personal property, are retail sales and subject to retailing B&O tax on the gross proceeds of such sales. Persons making retail sales must collect retail sales tax from the buyer, unless the sale is specifically exempt by law. Refer to subsection (9) of this rule for information about specific sales tax exemptions available for sales to farmers.

(a) **Documenting wholesale sales.** A seller must take and retain from the buyer a copy of the buyer's reseller permit, or a completed "Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions" to document the wholesale nature of any transaction.

(b) **Buyer's responsibility when the seller does not collect retail sales tax on a retail sale.** If the seller does not collect retail sales tax on a retail sale, the buyer must pay the retail sales tax (commonly referred to as "deferred sales tax") or use tax directly to the department, unless the sale is specifically exempt by law. The excise tax return does not have a separate line for reporting deferred sales tax. Consequently, deferred sales tax liability should be reported on the use tax line of the buyer's excise tax return. If a deferred sales tax or use tax liability is incurred by a farmer who is not required to obtain a tax registration endorsement from the department, the farmer must report the tax on a "Consumer Use Tax Return" and remit the appropriate tax to the department. For detailed information regarding use tax see WAC 458-20-178.

The Consumer Use Tax Return may be obtained by calling the department's telephone information center at 1-800-647-7706. The return may also be obtained from the department's website at dor.wa.gov.

(c) **Feed, seed, seedlings, fertilizer, spray materials, and agents for enhanced pollination.** Sales to farmers of feed, seed, seedlings, fertilizer, spray materials, and agents for enhanced pollination, including insects such as bees, to be used for the purpose of producing an agricultural product, whether for wholesale or retail sale, are wholesale sales.

However, when these items are sold to consumers for purposes other than producing agricultural products for sale, the sales are retail sales. For example, sales of feed to riding clubs, racetrack operators, boarders, or similar persons who do not resell the feed at a specific charge are retail sales. Sales of feed for feeding pets or work animals, or for raising animals for the purpose of producing agricultural products for personal consumption are also retail sales.

Sales of seed, fertilizer, and spray materials for use on lawns and gardens, or for any other personal use, are likewise retail sales.

(i) **What is feed?** "Feed" is any substance used as food to sustain or improve animals, birds, fish, bees, or other insects, including whole and processed grains or mixtures thereof, hay and forages or meals made therefrom, mill feeds and feeding concentrates, stock salt, hay salt, sugar, pollen patties, bone meal, fish meal, cod liver oil, double purpose limestone grit, oyster shell, and other similar substances. Food additives that are given for their beneficial growth or weight effects are "feed."

Hormones or similar products that do not make a direct nutritional or energy contribution to the body are not "feed," nor are products used as medicines.

(ii) **What is seed?** "Seed" is the propagative portions of plants commonly used for seeding or planting whether true seed, bulbs, plants, seed-like fruits, seedlings, or tubers. For purposes of this rule, "seed" does not include seeds or propagative portions of plants used to grow ((marijuana)) cannabis.

(iii) **What is fertilizer?** "Fertilizer" is any substance containing one or more recognized plant nutrients and is used for its plant nutrient content and/or is designated for use in promoting plant growth. "Fertilizer" includes limes, gypsum, and manipulated animal and vegetable manures. There is no requirement that fertilizers be applied directly to the soil.

(iv) **What are spray materials?** "Spray materials" are any substance or mixture of substances in liquid, powder, granular, dry flowable, or gaseous form, which is intended to prevent, destroy, control, repel, or mitigate any insect, rodent, nematode, mite, mollusk, fungus, weed, and any other form of plant or animal life normally considered to be a pest. The term includes treated materials, such as grains, that are intended to destroy, control, or repel such pests. "Spray materials" also include substances that act as plant regulators, defoliants, desiccants, or spray adjuvants.

(v) **Examples.**

(A) **Example 1.** Sue grows vegetables for retail sale at a local market. Sue purchases fertilizers and spray materials that she applies to the vegetable plants. She also purchases feed for poultry that she raises to produce eggs for her personal consumption. Because the vegetables are an agricultural product produced for sale, retail sales tax does not apply to Sue's purchases of fertilizers and spray materials, provided she gives the seller a copy of her reseller permit, or a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions. Retail sales tax applies to her purchases of poultry feed, as the poultry is raised to produce eggs for Sue's personal consumption.

(B) **Example 2.** WG Vineyards (WG) grows grapes that it uses to manufacture wine for sale. WG purchases pesticides and fertilizers that are applied to its vineyards. WG may purchase these pesticides and fertilizers at wholesale, provided WG gives the seller a copy of their reseller permit, or a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions.

(C) **Example 3.** Seed Co. contracts with farmers to raise seed. Seed Co. provides the seed and agrees to purchase the crop if it meets specified standards. The contracts provide that ownership of the crop is retained by Seed Co., and the risk of crop loss is borne by the farmers. The farmers must pay for the seed whether or not the crop meets the specified standard. The transfer of the possession of the

seed to each farmer is a wholesale sale, provided Seed Co. obtains a copy of their reseller permit, or a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions from that farmer.

(d) **Chemical sprays or washes.** Sales of chemical sprays or washes, whether to farmers or other persons, for the purpose of post-harvest treatment of fruit for the prevention of scald, fungus, mold, or decay are wholesale sales.

(e) **Farming equipment.** Sales to farmers of farming equipment such as machinery, machinery parts and repair, tools, and cleaning materials are retail sales and subject to retailing B&O and retail sales taxes, unless specifically exempt by law. Refer to subsections (7)(i) and (9) of this rule for information about sales tax exemptions available to farmers.

(f) **Packing materials and containers.** Sales of packing materials and containers, or tangible personal property that will become part of a container, to a farmer who will sell the property to be contained therein are wholesale sales, provided the packing materials and containers are not put to intervening use by the farmer. Thus, sales to farmers of binder twine for binding bales of hay that will be sold or wrappers for fruit and vegetables to be sold are subject to wholesaling B&O tax. However, sales of packing materials and containers to a farmer who will use the items as a consumer are retail sales and subject to retailing B&O and retail sales taxes. Thus, sales of binder twine to a farmer for binding bales of hay that will be used to feed the farmer's livestock are retail sales.

(g) **Purchases for dual purposes.** A buyer normally engaged in both consuming and reselling certain types of tangible personal property who is unable to determine at the time of purchase whether the particular property purchased will be consumed or resold must purchase according to the general nature of his or her business. RCW 82.08.130. If the buyer principally consumes the articles in question, the buyer should not give a copy of its reseller permit for any part of the purchase. If the buyer principally resells the articles, the buyer may provide a copy of its reseller permit for the entire purchase. For the purposes of this subsection, the term "principally" means greater than ((fifty)) 50 percent.

If a buyer makes a purchase for dual purposes and does not give a copy of their reseller permit for any of the purchase and thereafter resells some of the articles purchased, the buyer may claim a "taxable amount for tax paid at source" deduction. For additional information regarding purchases for dual purposes and the "taxable amount for tax paid at source" deduction see WAC 458-20-102.

(i) **Potential deferred sales tax liability.** If the buyer gives a copy of its reseller permit for all purchases and thereafter consumes some of the articles purchased, the buyer is liable for deferred sales tax and must remit the tax directly to the department. Refer to (b) of this subsection, WAC 458-20-102 and 458-20-178 for more information regarding deferred sales tax and use tax.

(ii) **Example 4.** A farmer purchases binder twine for binding bales of hay. Some of the hay will be sold and some will be used to feed the farmer's livestock. More than ((fifty)) 50 percent of the binder twine is used for binding bales of hay that will be sold. Because the farmer principally uses the binder twine for binding bales of hay that will be sold, the farmer may provide a copy of their reseller permit, or a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions to the seller for the entire purchase. The farmer is liable for deferred sales tax on the binder twine used for binding bales of

hay that are used to feed the farmer's livestock and must remit the tax directly to the department.

(h) **"Fruit bin rentals" by fruit packers.** Fruit packers often itemize their charges to farmers for various services related to the packing and storage of fruit. An example is a charge for the bins that the packer uses in the receiving, sorting, inspecting, and storing of fruit (commonly referred to as "bin rentals"). The packer delivers the bins to the grower, who fills them with fruit for eventual storage in the packer's warehouse. Charges by fruit packers to farmers for such bin rentals do not constitute the rental of tangible personal property to the farmer where the bins are under the control of the packer for use in the receiving, sorting, inspecting, and storing of fruit. These charges are income to the packer related to the receipt or storage of fruit. The packer, as the consumer of the bins, is subject to retail sales or use tax on the purchase or use of the bins. For information regarding the taxability of fruit packing by cooperative marketing associations and independent dealers acting as agents for others in the sales of fruit and produce see WAC 458-20-214.

(i) **Machinery and equipment used directly in a manufacturing operation.** Machinery and equipment used directly in a manufacturing operation by a manufacturer or processor for hire is exempt from sales and use taxes provided that all requirements for the exemptions are met. RCW 82.08.02565 and 82.12.02565. These exemptions are commonly referred to as the M&E exemption. Farmers who use agricultural products that they have grown, raised, or produced as ingredients in a manufacturing process may be entitled to the M&E exemption on the acquisition of machinery and equipment used directly in their manufacturing operation. For more information on the M&E exemption see WAC 458-20-13601.

(8) **Sales by farmers.** Farmers are not subject to B&O tax on wholesale sales of agricultural products. Effective July 1, 2015, bee pollination services provided to farmers by eligible apiarists also qualify for the exemption provided by RCW 82.04.330. Farmers who manufacture products using agricultural products that they have grown, raised, or produced should refer to (b) of this subsection for tax-reporting information.

Farmers are subject to retailing B&O tax on retail sales of agricultural products and retailing or wholesaling B&O tax on sales of nonagricultural products, as the case may be, unless specifically exempt by law. Also, B&O tax applies to sales of agricultural products that the seller has not grown, raised, or produced on the seller's own land or on land in which the seller has a present right of possession, whether these products are sold at wholesale or retail. Likewise, B&O tax applies to sales of animals or substances derived from animals in connection with the business of operating a stockyard, slaughterhouse, or packing house. Farmers may be eligible to claim a small business B&O tax credit if the amount of B&O tax liability in a reporting period is under a certain amount. For more information about the small business B&O tax credit see WAC 458-20-104.

(a) **Litter tax.** The gross proceeds of sales of certain products, including food for human or pet consumption, are subject to litter tax. RCW 82.19.020. Litter tax does not apply to sales of agricultural products that are exempt from B&O tax under RCW 82.04.330. RCW 82.19.050. Thus, farmers are not subject to litter tax on wholesale sales of agricultural products but are liable for litter tax on the gross proceeds of retail sales of agricultural products that constitute food for human or pet consumption. In addition, farmers that man-

ufacture products for use and consumption within this state (e.g., a farmer who produces wine from grapes that the farmer has grown) may be liable for litter tax measured by the value of the products manufactured. For more information about the litter tax see chapter 82.19 RCW and WAC 458-20-243.

**Example 5.** RD Orchards (RD) grows apples at its orchards. Most apples are sold at wholesale, but RD operates a seasonal roadside fruit stand from which it sells apples at retail. The wholesale sales of apples are exempt from both B&O and litter taxes. The retail sales of apples are subject to retailing B&O and litter taxes but are exempt from sales tax because the apples are sold as a food product for human consumption. Refer to subsection (9)(d) of this rule for more information about the retail sales tax exemption applicable to sales of food products for human consumption.

(b) **Farmers using agricultural products in a manufacturing process.** The B&O tax exemption provided by RCW 82.04.330 does not apply to any person selling manufactured substances or articles. Thus, farmers who manufacture products using agricultural products that they have grown, raised, or produced are subject to manufacturing B&O tax on the value of products manufactured. Farmers who sell their manufactured products at retail or wholesale in the state of Washington are also generally subject to the retailing or wholesaling B&O tax, as the case may be. In such cases, a multiple activities tax credit (MATC) may be available. Refer to WAC 458-20-136 (Manufacturing, processing for hire, fabricating) and WAC 458-20-19301 (Multiple activities tax credits), respectively, for more information about the manufacturing B&O tax and the MATC.

(i) **Manufacturing fresh fruits and vegetables.** RCW 82.04.4266 provides a B&O tax exemption to persons manufacturing fresh fruits or vegetables by canning, preserving, freezing, processing, or dehydrating fresh fruits or vegetables. For purposes of this rule, "fruits" and "vegetables" does not include (~~marijuana~~) cannabis.

Wholesale sales of fresh fruits or vegetables canned, preserved, frozen, processed, or dehydrated by the seller and sold to purchasers who transport the goods out of this state in the ordinary course of business are also eligible for this exemption. A seller must keep and preserve records for the period required by RCW 82.32.070 establishing that the purchaser transported the goods out of Washington state.

(A) A person claiming the exemption must file a complete annual tax performance report with the department under RCW 82.32.534. In addition, persons claiming this tax preference must report the amount of the exemption on their monthly or quarterly excise tax return. For more information on reporting requirements for this tax preference see RCW 82.32.808.

(B) RCW 82.04.4266 is scheduled to expire July 1, 2025, at which time the preferential B&O tax rate under RCW 82.04.260 will apply.

(ii) **Manufacturing dairy products.** RCW 82.04.4268 provides a B&O tax exemption to persons manufacturing dairy products, not including any (~~marijuana-infused~~) cannabis-infused product, that as of September 20, 2001, are identified in 21 C.F.R., chapter 1, parts 131, 133, and 135. These products include milk, buttermilk, cream, yogurt, cheese, and ice cream, and also include by-products from the manufacturing of dairy products such as whey and casein.

The exemption also applies to persons selling manufactured dairy products to purchasers who transport the goods out of Washington state in the ordinary course of business. Unlike the exemption for certain wholesale sales of fresh fruits or vegetables (see (b)(i) of this sub-

section), the exemption for sales of qualifying dairy products does not require that the sales be made at wholesale.

A seller must keep and preserve records for the period required by RCW 82.32.070 establishing that the purchaser transported the goods out of Washington state or the goods were sold to a manufacturer for use as an ingredient or component in the manufacturing of a dairy product.

(A) A person claiming the exemption must file a complete annual tax performance report with the department under RCW 82.32.534. In addition, persons claiming this tax preference must report the amount of the exemption on their monthly or quarterly excise tax return. For more information on reporting requirements for this tax preference see RCW 82.32.808.

(B) RCW 82.04.4268 is scheduled to expire July 1, 2025, at which time the preferential B&O tax rate under RCW 82.04.260 will apply.

(C) Effective October 1, 2013, the exemption provided by RCW 82.04.4268 expanded to include wholesale sales by a dairy product manufacturer to a purchaser who uses the dairy products as an ingredient or component in the manufacturing in Washington of another dairy product. The definition of dairy products was expanded to include products comprised of not less than (~~seventy~~) 70 percent dairy products measured by weight or volume.

(c) **Raising cattle for wholesale sale.** RCW 82.04.330 provides a B&O tax exemption to persons who raise cattle for wholesale sale provided that the cattle are held for at least (~~sixty~~) 60 days prior to the sale. Persons who hold cattle for fewer than (~~sixty~~) 60 days before reselling the cattle are not considered to be engaging in the normal activities of growing, raising, or producing livestock for sale.

**Example 6.** A feedlot operation purchases cattle and feeds them until they attain a good market condition. The cattle are then sold at wholesale. The feedlot operator is exempt from B&O tax on wholesale sales of cattle if it held the cattle for at least (~~sixty~~) 60 days while they were prepared for market. However, the feedlot operator is subject to wholesaling B&O tax on wholesale sales of cattle held for fewer than (~~sixty~~) 60 days prior to the sale.

(d) **B&O tax exemptions available to farmers.** In addition to the exemption for wholesale sales of agricultural products, several other B&O tax exemptions available to farmers are discussed in this subsection.

(i) **Growing, raising, or producing agricultural products owned by other persons.** RCW 82.04.330 exempts amounts received by a farmer for growing, raising, or producing agricultural products owned by others, such as custom feed operations.

**Example 7.** A farmer is engaged in the business of raising cattle owned by others (commonly referred to as "custom feeding"). After the cattle attain a good market condition, the owner sells them. Amounts received by the farmer for custom feeding are exempt from B&O tax under RCW 82.04.330, provided that the farmer held the cattle for at least (~~sixty~~) 60 days. Farmers are not considered to be engaging in the activity of raising cattle for sale unless the cattle are held for at least (~~sixty~~) 60 days while the cattle are prepared for market. (See (c) of this subsection.)

(ii) **Processed hops shipped outside Washington for first use.** RCW 82.04.337 exempts amounts received by hop growers or dealers for hops shipped outside the state of Washington for first use, if those hops have been processed into extract, pellets, or powder in this state.

However, the processor or warehouse of such products is not exempt on amounts charged for processing or warehousing such products.

(iii) **Sales of hatching eggs or poultry.** RCW 82.04.410 exempts amounts received for the sale of hatching eggs or poultry by farmers producing hatching eggs or poultry, when these agricultural products are for use in the production for sale of poultry or poultry products.

(9) **Retail sales tax and use tax exemptions.** This subsection provides information about a number of retail sales tax and corresponding use tax exemptions available to farmers and persons buying tangible personal property at retail from farmers. Some exemptions require the buyer to provide the seller with an exemption certificate. Refer to subsection (10) of this rule for additional information regarding exemption certificates.

(a) **Pollen.** RCW 82.08.0277 and 82.12.0273 exempt the sale and use of pollen from retail sales and use taxes.

(b) **Semen.** RCW 82.08.0272 and 82.12.0267 exempt the sale and use of semen used in the artificial insemination of livestock from retail sales and use taxes.

(c) **Feed for livestock at public livestock markets.** RCW 82.08.0296 and 82.12.0296 exempt the sale and use of feed to be consumed by livestock at a public livestock market from retail sales and use taxes.

(d) **Food products.** RCW 82.08.0293 and 82.12.0293 exempt the sale and use of food products for human consumption from retail sales and use taxes. These exemptions also apply to the sale or use of livestock for personal consumption as food. For more information about food products that qualify for this exemption see WAC 458-20-244.

(e) **Auction sales of farm property.** RCW 82.08.0257 and 82.12.0258 exempt from retail sales and use taxes tangible personal property, including household goods, which has been used in conducting a farm activity, if the property is purchased from a farmer, as defined in RCW 82.04.213, at an auction sale held or conducted by an auctioneer on a farm. Effective June 12, 2014, these exemptions do not apply to personal property used by a person in the production of (~~marijuana~~) cannabis.

(f) **Poultry.** RCW 82.08.0267 and 82.12.0262 exempt from retail sales and use taxes the sale and use of poultry used in the production for sale of poultry or poultry products.

**Example 8.** A poultry hatchery produces poultry from eggs. The resulting poultry are sold to egg producers. These sales are exempt from retail sales tax under RCW 82.08.0267. (They are also exempt from B&O tax. See subsection (8)(d)(iii) of this rule.)

(g) **Leases of irrigation equipment.** RCW 82.08.0288 and 82.12.0283 exempt the lease or use of irrigation equipment from retail sales and use taxes, but only if:

(i) The lessor purchased the irrigation equipment for the purpose of irrigating land controlled by the lessor;

(ii) The lessor has paid retail sales or use tax upon the irrigation equipment;

(iii) The irrigation equipment is attached to the land in whole or in part;

(iv) Effective June 12, 2014, the irrigation equipment is not used in the production of (~~marijuana~~) cannabis; and

(v) The irrigation equipment is leased to the lessee as an incidental part of the lease of the underlying land and is used solely on such land.



(h) **Beef and dairy cattle.** RCW 82.08.0259 and 82.12.0261 exempt the sale and use of beef and dairy cattle, to be used by a farmer in producing an agricultural product, from retail sales and use taxes.

**Example 9.** John operates a farm where he raises beef and dairy cattle for sale. He also raises other livestock for sale including hogs, sheep, and goats. John's sales of beef and dairy cattle for use on a farm are exempt from retail sales tax. However, John must collect retail sales tax on all retail sales of sheep, goats, and hogs unless the sales qualify for either the food products exemption described in (d) of this subsection, or the exemption for sales of livestock for breeding purposes described in this subsection (9)(i) of this rule.

(i) **Livestock for breeding purposes.** RCW 82.08.0259 and 82.12.0261 exempt the sale or use of livestock, as defined in RCW 16.36.005, for breeding purposes where the animals are registered in a nationally recognized breed association from retail sales and use taxes.

**Example 10.** ABC Farms raises and sells quarter horses registered in the American Quarter Horse Association (AQHA). Quarter horses are generally recognized as a definite breed of horse, and the AQHA is a nationally recognized breed association. Therefore, ABC Farms is not required to collect sales tax on retail sales of quarter horses for breeding purposes, provided it receives and retains a completed exemption certificate from the buyer.

(j) **Bedding materials for chickens.** RCW 82.08.920 and 82.12.920 exempt from retail sales and use taxes the sale to and use of bedding materials by farmers to accumulate and facilitate the removal of chicken manure, provided the farmer is raising chickens that are sold as agricultural products.

(i) **What are bedding materials?** "Bedding materials" are wood shavings, straw, sawdust, shredded paper, and other similar materials.

(ii) **Example 11.** Farmer raises chickens for use in producing eggs for sale. When the chickens are no longer useful for producing eggs, Farmer sells them to food processors for soup and stew meat. Farmer purchases bedding materials used to accumulate and facilitate the removal of chicken manure. The purchases of bedding materials by Farmer are exempt from retail sales tax as long as Farmer provides the seller with a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions. See subsection (10) of this rule for where to find an exemption certificate. The seller must retain a copy of the exemption certificate for its records.

The exemption merely requires that the chickens be sold as agricultural products. It is immaterial that Farmer primarily raises the chickens to produce eggs.

(k) **Propane or natural gas used to heat structures housing chickens.** RCW 82.08.910 and 82.12.910 exempt from retail sales and use taxes the sale to and use of propane or natural gas by farmers to heat structures used to house chickens. The propane or natural gas must be used exclusively to heat the structures, and the structures must be used exclusively to house chickens that are sold as agricultural products.

(i) **What are "structures"?** "Structures" are barns, sheds, and other similar buildings in which chickens are housed.

(ii) **Example 12.** Farmer purchases natural gas that is used to heat structures housing chickens. The natural gas is used exclusively to heat the structures, and the structures are used exclusively to house chickens. The chickens are used to produce eggs. When the chickens are no longer useful for producing eggs, Farmer sells the chickens

to food processors for soup and stew meat. The purchase of natural gas by Farmer is exempt from retail sales tax as long as Farmer provides the seller with a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions. See subsection (10) of this rule for where to find an exemption certificate. The seller must retain a copy of the exemption certificate for its records.

The exemption merely requires that the chickens be sold as agricultural products. It is immaterial that Farmer primarily houses these chickens to produce eggs.

(iii) **Example 13.** Farmer purchases natural gas that is used to heat structures used in the incubation of chicken eggs and structures used for washing, packing, and storing eggs. The natural gas used to heat these structures is not exempt from retail sales tax because the structures are not used exclusively to house chickens that are sold as agricultural products.

(l) **Farm fuel used for agricultural purposes.**

(i) **Diesel, biodiesel and aircraft fuels.** RCW 82.08.865 and 82.12.865 exempt from retail sales and use taxes the sale and use of diesel fuel, biodiesel fuel, and aircraft fuel, to farm fuel users for agricultural purposes. The exemptions apply to a fuel blend if all of the component fuels of the blend would otherwise be exempt if the component fuels were sold as separate products. The buyer must provide the seller with a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions. See subsection (10) of this rule for where to find an exemption certificate. The seller must retain a copy of the exemption certificate for its records.

(A) The exemptions apply to nonhighway uses for production of agricultural products and for providing horticultural services to farmers. Horticultural services include:

- (I) Soil preparation services;
- (II) Crop cultivation services;
- (III) Crop harvesting services.

(B) The exemptions do not apply to uses other than for agricultural purposes. Agricultural purposes do not include:

- (I) Heating space for human habitation or water for human consumption; or
- (II) Transporting on public roads individuals, agricultural products, farm machinery or equipment, or other tangible personal property, except when the transportation is incidental to transportation on private property and the fuel used for such transportation is not subject to tax under chapter 82.38 RCW.

(ii) **Propane and natural gas used in distilling mint on a farm.** Effective October 1, 2013, RCW 82.08.220 and 82.12.220 exempt from retail sales and use taxes sales to and use by farmers of propane or natural gas used exclusively to distill mint on a farm. The buyer must provide the seller with a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions. The seller must retain a copy of the exemption certificate for its records. See subsection (10) of this rule for where to find an exemption certificate. The seller must also report amounts claimed for exemption when electronically filing excise tax returns. This exemption is scheduled to expire July 1, 2017.

(m) **Nutrient management equipment and facilities.** RCW 82.08.890 and 82.12.890 provide retail sales and use tax exemptions for the sale to or use by eligible persons of:

- (i) Qualifying livestock nutrient management equipment;

(ii) Labor and services rendered in respect to installing, repairing, cleaning, altering, or improving qualifying livestock nutrient management equipment; and

(iii) Labor and services rendered in respect to repairing, cleaning, altering, or improving qualifying livestock nutrient management facilities, or to tangible personal property that becomes an ingredient or component of qualifying livestock nutrient management facilities in the course of repairing, cleaning, altering, or improving such facilities.

(iv) Nonqualifying labor and services. This subsection (9)(m)(iii) of this rule does not include the sale of or charge made for labor and services rendered in respect to the constructing of new, or replacing previously existing, qualifying livestock nutrient management facilities, or tangible personal property that becomes an ingredient or component of qualifying livestock nutrient management facilities during the course of constructing new, or replacing previously existing qualifying livestock nutrient management facilities.

(v) Nutrient management plan must be certified or approved. The exemptions provided by RCW 82.08.890 and 82.12.890 apply to sales made after the livestock nutrient management plan is:

(A) Certified under chapter 90.64 RCW;

(B) Approved as part of the permit issued under chapter 90.48 RCW; or

(C) Approved by a conservation district and who qualifies for the exemption provided under RCW 82.08.855. Effective June 12, 2014, the requirement for the department to issue exemption certificates was removed. A Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions should be completed and provided to the seller.

(vi) **Definitions. For the purpose of these exemptions, the following definitions apply:**

(A) **"Animal feeding operation"** means a lot or facility, other than an aquatic animal production facility, where the following conditions are met:

- Animals, other than aquatic animals, have been, are, or will be stabled or confined and fed or maintained for a total of (~~forty-five~~) 45 days or more in any (~~twelve-month~~) 12-month period; and

- Crops, vegetation, forage growth, or post-harvest residues are not sustained in the normal growing season over any portion of the lot or facility.

(B) **"Conservation district"** means a subdivision of state government organized under chapter 89.08 RCW.

(C) **"Eligible person"** means a person:

- Licensed to produce milk under chapter 15.36 RCW who has a certified dairy nutrient management plan, as required by chapter 90.64 RCW; or

- Who owns an animal feeding operation and has a permit issued under chapter 90.48 RCW; or

- Who owns an animal feeding operation and has a nutrient management plan approved by a conservation district as meeting natural resource conservation service field office technical guide standards and who qualifies for the exemption provided under RCW 82.08.855.

(D) **"Handling and treatment of livestock manure"** means the activities of collecting, storing, moving, or transporting livestock manure, separating livestock manure solids from liquids, or applying livestock manure to the agricultural lands of an eligible person other than through the use of pivot or linear type traveling irrigation systems.

(E) **"Permit"** means either a state waste discharge permit or a National Pollutant Discharge Elimination System permit, or both.

(F) **"Qualifying livestock nutrient management equipment"** means the tangible personal property listed below for exclusive use in the handling and treatment of livestock manure, including repair and replacement parts for the same equipment:

- Aerators
- Agitators
- Augers
- Conveyers
- Gutter cleaners
- Hard-hose reel traveler irrigation systems
- Lagoon and pond liners and floating covers
- Loaders
- Manure composting devices
- Manure spreaders
- Manure tank wagons
- Manure vacuum tanks
- Poultry house cleaners
- Poultry house flame sterilizers
- Poultry house washers
- Poultry litter saver machines
- Pipes
- Pumps
- Scrapers
- Separators
- Slurry injectors and hoses
- Wheelbarrows, shovels, and pitchforks.

(G) **"Qualifying livestock nutrient management facilities"** means the exclusive use in the handling and treatment of livestock manure of the facilities listed below:

- Flush systems
- Lagoons
- Liquid livestock manure storage structures, such as concrete tanks or glass-lined steel tanks
- Structures used solely for dry storage of manure, including roofed stacking facilities.

(n) **Anaerobic digesters (effective July 1, 2018).**

(i) RCW 82.08.900 and 82.12.900 provide retail sales and use tax exemptions for purchases and uses by eligible persons:

(A) In respect to equipment necessary to process biogas from a landfill into marketable coproducts including, but not limited to, biogas conditioning, compression, and electrical generation equipment, or to services rendered in respect to installing, constructing, repairing, cleaning, altering, or improving equipment necessary to process biogas from a landfill into marketable coproducts; and

(B) Establishing or operating anaerobic digesters or to services rendered in respect to installing, constructing, repairing, cleaning, altering, or improving an anaerobic digester. The exemptions include sales of tangible personal property that becomes an ingredient or component of the anaerobic digester. Anaerobic digester means a facility that processes organic material into biogas and digestate using microorganisms in a decomposition process within a closed, oxygen-free container as well as the equipment necessary to process biogas or digestate produced by an anaerobic digester into marketable coproducts in-

cluding, but not limited to, biogas conditioning, compression, nutrient recovery, and electrical generation equipment.

(ii) **Exemption certificate.** Effective July 24, 2015, eligible persons no longer need to apply for an exemption certificate. An "eligible person" is any person establishing or operating an anaerobic digester or landfill or processing biogas from an anaerobic digester or landfill into marketable coproducts.

(iii) **Records retention.** Persons claiming the exemptions under RCW 82.08.900 and 82.12.900 must keep records necessary for the department to verify eligibility. Sellers may make tax exempt sales only if the buyer provides the seller with a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions, and the seller retains a copy of the certificate for its files. See subsection (10) of this rule for where to find an exemption certificate.

(o) **Anaerobic digesters (effective until July 1, 2018).** RCW 82.08.900 and 82.12.900 provide retail sales and use tax exemptions for purchases and uses by eligible persons establishing or operating anaerobic digesters or to services rendered in respect to installing, constructing, repairing, cleaning, altering, or improving an anaerobic digester. The exemptions include sales of tangible personal property that becomes an ingredient or component of the anaerobic digester. The anaerobic digester must be used primarily (more than (~~fifty~~) 50 percent measured by volume or weight) to treat livestock manure. Anaerobic digester is a facility that processes manure from livestock into biogas and dried manure using microorganisms in a decomposition process within a closed, oxygen-free container.

(i) **Exemption certificate.** Effective July 24, 2015, eligible persons no longer need to apply for an exemption certificate. An "eligible person" is any person establishing or operating an anaerobic digester to treat primarily livestock manure.

(ii) **Records retention.** Persons claiming the exemptions under RCW 82.08.900 and 82.12.900 must keep records necessary for the department to verify eligibility. Sellers may make tax exempt sales only if the buyer provides the seller with a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions, and the seller retains a copy of the certificate for its files. See subsection (10) of this rule for where to find an exemption certificate.

(p) **Animal pharmaceuticals.** RCW 82.08.880 and 82.12.880 exempt from retail sales and use taxes the sale of and use of certain animal pharmaceuticals when sold to, or used by, farmers or veterinarians. To qualify for the exemption, the animal pharmaceutical must be administered to an animal raised by a farmer for the purpose of producing an agricultural product for sale. In addition, the animal pharmaceutical must be approved by the United States Department of Agriculture (USDA) or the United States Food and Drug Administration (FDA).

(i) **Who is a veterinarian?** A "veterinarian" means a person who is licensed to practice veterinary medicine, surgery, or dentistry under chapter 18.92 RCW.

(ii) **How can I determine whether the FDA or USDA has approved an animal pharmaceutical?** The FDA and USDA have an established approval process set forth in federal regulations. The FDA maintains a list of all approved animal pharmaceuticals called the "*Green Book*." The USDA maintains a list of approved biotechnology products called the "*Veterinary Biologics Product Catalogue*." Pharmaceuticals that are not on either of these lists have not been approved and are not eligible for the exemption.

(iii) **Example 17.** Dairy Farmer purchases sterilizing agents. The sterilizing agents are applied to the equipment and facilities where Dairy Farmer's cows are milked. Dairy Farmer also purchases teat dips, antiseptic udder washes, and salves that are not listed in either the FDA's *Green Book* of approved animal pharmaceuticals or the USDA's *Veterinary Biologics Product Catalogue* of approved biotechnology products. The purchases of sterilizing agents are not exempt as animal pharmaceuticals because the sterilizing agents are not administered to animals. The teat dips, antiseptic udder washes, and salves are likewise not exempt because they have not been approved by the FDA or USDA.

(iv) **What type of animal must the pharmaceutical be administered to?** As explained above, the exemptions are limited to the sale and use of animal pharmaceuticals administered to an animal that is raised by a farmer for the purpose of producing an agricultural product for sale. The conditions under which a farmer may purchase and use tax-exempt animal pharmaceuticals are similar to those under which a farmer may purchase and use feed at wholesale. Both types of purchases and uses require that the particular product be sold to or used by a farmer (or a veterinarian in the case of animal pharmaceuticals), and that the product be given or administered to an animal raised by a farmer for the purpose of producing an agricultural product for sale.

(v) **Examples of animals raised for the purpose of producing agricultural products for sale.** For purposes of the exemptions, the following is a nonexclusive list of examples of animals that are being raised for the purpose of producing an agricultural product for sale, presuming all other requirements for the exemption are met:

- (A) Horses, cattle, or other livestock raised by a farmer for sale;
- (B) Cattle raised by a farmer for the purpose of slaughtering, if the resulting products are sold;
- (C) Milk cows raised and/or used by a dairy farmer for the purpose of producing milk for sale;
- (D) Horses raised by a farmer for the purpose of producing foals for sale;
- (E) Sheep raised by a farmer for the purpose of producing wool for sale; and
- (F) "Private sector cultured aquatic products" as defined by RCW 15.85.020 (e.g., salmon, catfish, and mussels) raised by an aquatic farmer for the purpose of sale.

(vi) **Examples of animals that are not raised for the purpose of producing agricultural products for sale.** For purposes of the exemptions, the following nonexclusive list of examples do not qualify because the animals are not being raised for the purpose of producing an agricultural product for sale:

- (A) Cattle raised for the purpose of slaughtering if the resulting products are not produced for sale;
- (B) Sheep and other livestock raised as pets;
- (C) Dogs or cats, whether raised as pets or for sale. Dogs and cats are pet animals; therefore, they are not considered to be agricultural products. (See subsection (3) of this rule); and
- (D) Horses raised for the purpose of racing, showing, riding, and jumping. However, if at some future time the horses are no longer raised for racing, showing, riding, or jumping and are instead being raised by a farmer for the purpose of producing foals for sale, the exemption will apply if all other requirements for the exemption are met.

(vii) **Do products that are used to administer animal pharmaceuticals qualify for the exemption?** Sales and uses of products that are used to administer animal pharmaceuticals (e.g., syringes) do not qualify for the exemptions, even if they are later used to administer a tax-exempt animal pharmaceutical. However, sales and uses of tax-exempt animal pharmaceuticals contained in a product used to administer the animal pharmaceutical (e.g., a dose of a tax-exempt pharmaceutical contained in a syringe or cotton applicator) qualify for the exemption.

(q) **Replacement parts for qualifying farm machinery and equipment.** RCW 82.08.855 and 82.12.855 exempt from retail sales and use taxes sales to and uses by eligible farmers of replacement parts for qualifying farm machinery and equipment. Also included are: Labor and services rendered during the installation of repair parts; and labor and services rendered during repair as long as no tangible personal property is installed, incorporated, or placed in, or becomes an ingredient or component of the qualifying equipment other than replacement parts.

(i) **The following definitions apply to this subsection:**

(A) "Eligible farmer" as defined in RCW 82.08.855(4).

(B) "Qualifying farm machinery and equipment" means machinery and equipment used primarily by an eligible farmer for growing, raising, or producing agricultural products, and effective July 1, 2015, providing bee pollination services, or both.

(C) "Qualifying farm machinery and equipment" does not include:

- Vehicles as defined in RCW 46.04.670, other than farm tractors as defined in RCW 46.04.180, farm vehicles and other farm implements. "Farm implements" means machinery or equipment manufactured, designed, or reconstructed for agricultural purposes and used primarily by an eligible farmer to grow, raise, or produce agricultural products, but does not include lawn tractors and all-terrain vehicles;

- Aircraft;

- Hand tools and hand-powered tools; and

- Property with a useful life of less than one year.

(D) "Replacement parts" means those parts that replace an existing part, or which are essential to maintain the working condition, of a piece of qualifying farm machinery or equipment. Paint, fuel, oil, hydraulic fluids, antifreeze, and similar items are not replacement parts except when installed, incorporated, or placed in qualifying farm machinery and equipment during the course of installing replacement parts as defined here or making repairs as described above in (p) of this subsection.

(ii) **Exemption certificate.** Prior to June 12, 2014, the department was required to provide an exemption certificate to an eligible farmer or renew an exemption certificate when the eligible farmer applied for a renewal.

(A) Persons claiming the exemptions must keep records necessary for the department to verify eligibility. Sellers making tax-exempt sales must obtain, and retain in its files, a completed Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions from the farmer. In lieu of the exemption certificate, a seller may capture the relevant data elements as allowed under the streamlined sales and use tax agreement.

(B) The exemptions provided by RCW 82.08.890 and 82.12.890 do not apply to sales made from July 1, 2010, through June 30, 2013.

(10) **Sales tax exemption certificates.** As indicated in subsection (9) of this rule, certain sales of tangible personal property and retail services either to or by farmers are exempt from retail sales tax. A person claiming an exemption must keep records necessary for the department to verify eligibility for each claimed exemption. Effective June 12, 2014, the requirement for the department to issue certificates to qualified farmers was removed. Instead, farmers may complete and use the department's Farmers' Certificate for Wholesale Purchases and Sales Tax Exemptions. Refer to the department's website at dor.wa.gov for the exemption certificate. In lieu of an exemption certificate, a seller may capture the relevant data elements as provided under the streamlined sales and use tax agreement as allowed under RCW 82.08.050. Sellers must retain a copy of the exemption certificate or the data elements in their files. Without proper documentation, sellers are liable for payment of the retail sales tax on sales claimed as exempt.

[Statutory Authority: RCW 82.32.300 and 82.01.060(2). WSR 19-02-057, § 458-20-210, filed 12/27/18, effective 1/27/19. Statutory Authority: RCW 82.32.300, 82.01.060(2), 82.32.534, 82.32.585, 82.32.590, 82.32.600, 82.32.605, 82.32.607, 82.32.710, 82.32.790, 82.32.808, 82.04.240, 82.04.2404, 82.04.260, 82.04.2909, 82.04.426, 82.04.4277, 82.04.4461, 82.04.4463, 82.04.448, 82.04.4481, 82.04.4483, 82.04.449, 82.08.805, 82.08.965, 82.08.9651, 82.08.970, 82.08.980, 82.08.986, 82.12.022, 82.12.025651, 82.12.805, 82.12.965, 82.12.9651, 82.12.970, 82.12.980, 82.16.0421, 82.29A.137, 82.60.070, 82.63.020, 82.63.045, 82.74.040, 82.74.050, 82.75.040, 82.75.070, 82.82.020, 82.82.040, 84.36.645, and 84.36.655. WSR 18-13-094, § 458-20-210, filed 6/19/18, effective 7/20/18. Statutory Authority: RCW 82.32.300, 82.01.060(2), 2015 3rd sp.s. c 6 part XI and 2015 c 86 § 202. WSR 16-03-002, § 458-20-210, filed 1/6/16, effective 2/6/16. Statutory Authority: RCW 82.32.300 and 82.01.060(2). WSR 15-01-007, § 458-20-210, filed 12/4/14, effective 1/4/15; WSR 14-14-091, § 458-20-210, filed 6/30/14, effective 7/31/14. Statutory Authority: RCW 82.01.060(2), 82.32.300, and 34.05.230. WSR 03-18-024, § 458-20-210, filed 8/25/03, effective 9/25/03. Statutory Authority: RCW 82.32.300. WSR 94-07-048, § 458-20-210, filed 3/10/94, effective 4/10/94; WSR 86-21-085 (Order ET 86-18), § 458-20-210, filed 10/17/86; WSR 86-07-005 (Order ET 86-3), § 458-20-210, filed 3/6/86; WSR 83-08-026 (Order ET 83-1), § 458-20-210, filed 3/30/83. Statutory Authority: RCW 82.01.060(2) and 82.32.300. WSR 78-07-045 (Order ET 78-4), § 458-20-210, filed 6/27/78; Order ET 70-3, § 458-20-210 (Rule 210), filed 5/29/70, effective 7/1/70.]

#### OTS-4108.1

AMENDATORY SECTION (Amending WSR 22-14-014, filed 6/23/22, effective 7/24/22)

#### **WAC 458-20-244 Food and food ingredients. (1) Introduction.**

This rule provides guidelines for determining if food or food ingredients qualify for the retail sales tax and use tax exemptions under RCW 82.08.0293 and 82.12.0293 (collectively referred to in this rule as the "exemptions").



There is no corresponding business and occupation (B&O) tax exemption. Even if a sale of food or food ingredients is exempt from retail sales tax or use tax under the exemptions, gross proceeds from sales of food or food ingredients remain subject to the retailing B&O tax.

(2) **Other rules that may apply.** Rules in the following list may contain additional relevant information:

(a) WAC 458-20-119 Sales by caterers and food service contractors;

(b) WAC 458-20-124 Restaurants, cocktail bars, taverns and similar businesses;

(c) WAC 458-20-166 Hotels, motels, boarding houses, rooming houses, resorts, hostels, trailer camps, short-term rentals and similar lodging businesses;

(d) WAC 458-20-167 Educational institutions, school districts, student organizations, and private schools;

(e) WAC 458-20-168 Hospitals, nursing homes, assisted living facilities, adult family homes and similar health care facilities;

(f) WAC 458-20-169 Nonprofit organizations;

(g) WAC 458-20-229 Refunds; and

(h) WAC 458-20-243 Litter tax.

(3) **Items qualifying for the exemptions.**

(a) **In general.** The exemptions apply to food and food ingredients. "Food and food ingredients" means substances, whether in liquid, concentrated, solid, frozen, dried, or dehydrated form, that are sold for ingestion or chewing by humans and are consumed for their taste or nutritional value.

(b) **Items not used solely for ingestion or chewing.** Items that are commonly ingested or chewed by humans for their taste or nutritional value but which may also be used for other purposes are generally treated as food or food ingredients. For example, pumpkins are presumed to be a food or food ingredient unless the pumpkin is sold painted or is otherwise clearly for decorative purposes rather than consumption. This is true even though the purchaser may use an undecorated pumpkin for carving and display rather than for eating.

(4) **Items not qualifying for the exemptions.** The exemptions do not apply to the following items, which are not considered "food or food ingredients" or which are otherwise specifically excluded from the exemptions:

(a) **Items sold for medical or hygiene purposes.** Items commonly used for medical or hygiene purposes, such as cough drops, breath sprays, toothpaste, etc., are not ingested for taste or nutrition and are not considered a food or food ingredient. In contrast, breath mints are commonly ingested for taste and are considered a food or food ingredient.

(b) **Bulk sales of ice.** Ice sold in bags, containers, or units of greater than 10 pounds and blocks of ice of any weight are not considered a food or food ingredient. Ice sold in cubed, shaved, or crushed form in packages or quantities of 10 pounds or less is considered a food or food ingredient. Refer to WAC 458-20-120, Sales of ice, for additional guidance on the sale of ice.

(c) **Alcoholic beverages.** Alcoholic beverages are excluded from the definition of food and food ingredients. "Alcoholic beverages" means beverages that are suitable for human consumption and contain one-half of one percent or more of alcohol by volume.

(d) **Tobacco.** Tobacco is excluded from the definition of food and food ingredients. "Tobacco" includes cigarettes, cigars, chewing or pipe tobacco, or any other item that contains tobacco.

(e) (~~(**Marijuana.** Marijuana, useable marijuana, marijuana concentrates, or marijuana-infused)~~) **Cannabis.** Cannabis, useable cannabis, cannabis concentrates, or cannabis-infused products, as defined in RCW 69.50.101, are excluded from the definition of food and food ingredients. "~~(**Marijuana**)~~ **Cannabis**" means all parts of the plant *Cannabis*, whether growing or not, with a THC concentration greater than 0.3 percent on a dry weight basis.

(f) **Bottled water.** Bottled water is excluded from the exemptions for food and food ingredients. "Bottled water" means water that is placed in a safety sealed container or package for human consumption.

(i) Bottled water is calorie free and does not contain sweeteners or other additives except that it may contain:

- (A) Antimicrobial agents;
- (B) Fluoride;
- (C) Carbonation;
- (D) Vitamins, minerals, and electrolytes;
- (E) Oxygen;
- (F) Preservatives; and

(G) Only those flavors, extracts, or essences derived from a spice or fruit.

(ii) **Exemptions for tax on bottled water.** There are limited retail sales tax exemptions on bottled water. Sellers must collect the retail sales tax on all sales of bottled water, unless the bottled water is delivered to the buyer as described in (f)(ii)(C) of this subsection. Any buyer that has paid at least \$25.00 in state and local taxes on purchases of bottled water subject to the exemptions described in (f)(ii)(A) and (B) of this subsection may apply for a refund of the taxes directly from the department.

(A) **Prescription issued bottled water.** Bottled water prescribed to patients for use in the cure, mitigation, treatment, or prevention of disease or other medical condition is exempt. RCW 82.08.9994. The bottled water must be prescribed, through an order, formula, or recipe issued in any form of oral, written, electronic, or other means of transmission, by a licensed practitioner authorized by Washington law to prescribe.

(B) **Primary water source unsafe.** Bottled water for human use by persons whose primary source of drinking water is unsafe is exempt. RCW 82.08.99941. A person's primary source of drinking water is unsafe if:

(I) The public water system providing the drinking water has issued a public notification that the drinking water may pose a health risk, and the notification is still in effect on the date that the bottled water was purchased;

(II) Test results on the person's drinking water, which are no more than 12 months old, from a laboratory certified to perform drinking water testing show that the person's drinking water does not meet safe drinking water standards applicable to public water systems; or

(III) The person otherwise establishes, to the department's satisfaction, that the person's drinking water does not meet safe drinking water standards applicable to public water systems.

(C) **Bottled water delivered to the buyer in a reusable container not sold with the water.** Buyers claiming an exemption listed in (f)(ii)(A) or (B) of this subsection that have the qualifying water delivered in a reusable container that is not sold with the water must

complete a retail sales exemption certificate and provide it to the seller. The seller must retain a copy of the certificate.

(iii) For information regarding exemption certificates and refund requests, visit [dor.wa.gov](http://dor.wa.gov).

(g) **Soft drinks.** Soft drinks are excluded from the exemptions for food and food ingredients. "Soft drinks" means any nonalcoholic beverage that contains natural or artificial sweeteners, except beverages that contain:

(i) Milk or milk products;

(ii) Soy, rice, or similar milk substitutes; or

(iii) More than 50 percent by volume of vegetable or fruit juice.

For example, sweetened sports beverages are considered "soft drinks," but a sweetened soy beverage is a food or food ingredient.

Beverage mixes that are not sold in liquid form are not soft drinks even though they are intended to be made into a beverage by the customer. Examples include powdered fruit drinks, powdered tea or coffee drinks, and frozen concentrates. These items are food or food ingredients and are not subject to retail sales tax.

(h) **Dietary supplements.** Dietary supplements are excluded from the exemptions for food and food ingredients. "Dietary supplement" means any product intended to supplement the diet, other than tobacco, which meets all of the following requirements:

(i) Contains a vitamin; mineral; herb or other botanical; an amino acid; a substance for use by humans to increase total dietary intake; or a concentrate, metabolite, constituent, extract; or a combination of any of these ingredients;

(ii) Is intended for ingestion in tablet, capsule, powder, soft gel, gelcap, or liquid form, or if not intended for ingestion in such a form, is not represented as conventional food and is not represented for use as a sole item of a meal or of the diet; and

(iii) Is required to be labeled with a Food and Drug Administration "supplement facts" box. If a product is otherwise considered a food or food ingredient and labeled with both a "supplement facts" box and "nutrition facts" box, the product is treated as a food or food ingredient.

Nutrition products formulated to provide balanced nutrition as a sole source of a meal or of the diet are considered a food or food ingredient and not a dietary supplement. Refer to RCW 82.08.925 for information on the retail sales tax exemption applicable to dietary supplements dispensed under a prescription.

(i) **Prepared food.** Prepared food is excluded from the exemptions for food and food ingredients. Prepared food generally means heated foods, combined foods, or foods sold with utensils provided by the seller, as described in more detail in subsection (5) of this rule.

(5) **Items designated as prepared foods.** Food or food ingredients are "prepared foods" if any one of the following is true:

(a) **Heated foods.** Food or food ingredients are "prepared foods" if sold in a heated state or are heated by the seller, except bakery items. "Bakery items" include bread, rolls, buns, biscuits, bagels, croissants, pastries, donuts, Danish, cakes, tortes, pies, tarts, muffins, bars, cookies, and tortillas. Food is sold in a heated state or is heated by the seller when the seller provides the food to the customer at a temperature that is higher than the air temperature of the seller's establishment. Food is not sold in a heated state or heated by the seller if the customer, rather than the seller, heats the food in a microwave provided by the seller.

(b) **Combined foods.** Food or food ingredients are "prepared foods" if the item sold consists of two or more foods or food ingredients mixed or combined by the seller for sale as a single item, unless the food or food ingredients are any of the following:

- (i) Bakery items (defined in (a) of this subsection);
- (ii) Items that the seller only cuts, repackages, or pasteurizes;
- (iii) Items that contain eggs, fish, meat, or poultry, in a raw or undercooked state requiring cooking as recommended by the federal Food and Drug Administration in chapter 3, part 401.11 of *The Food Code*, published by the Food and Drug Administration, as amended or re-numbered as of January 1, 2003, so as to prevent foodborne illness; or
- (iv) Items sold in an unheated state as a single item at a price that varies based on weight or volume.

(c) **Food sold with utensils provided by the seller.** Food or food ingredients are "prepared foods" if sold with utensils provided by the seller. Utensils include plates, knives, forks, spoons, glasses, cups, napkins, and straws. A plate does not include a container or packaging used to transport the food.

(i) **Utensils are customarily provided by the seller.** A food or food ingredient is "sold with utensils provided by the seller" if the seller's customary practice for that item is to physically deliver or hand a utensil to the customer with the food or food ingredient as part of the sales transaction. If the food or food ingredient is pre-packaged with a utensil, the seller is considered to have physically delivered a utensil to the customer unless the food and utensil are prepackaged together by a food manufacturer classified under sector 311 of the NAICS. Examples of utensils provided by such manufacturers include juice boxes that are packaged with drinking straws, and yogurt or ice cream cups that are packaged with wooden or plastic spoons.

(ii) **Utensils are necessary to receive the food.** Individual food or food ingredient items are "sold with utensils provided by the seller" if a plate, glass, cup, or bowl is necessary to receive the food or food ingredient and the seller makes those utensils available to its customers. For example, items obtained from a self-serve salad bar are sold with utensils provided by the seller, because the customer must use a bowl or plate provided by the seller in order to receive the items.

(iii) **More than 75 percent prepared food sales with utensils available.** All food and food ingredients sold at an establishment, including foods prepackaged with a utensil by a manufacturer classified under sector 311 of the NAICS, are "sold with utensils provided by the seller" if the seller makes utensils available to its customers and the seller's gross retail sales of prepared food under (a), (b), and (c)(ii) of this subsection equal more than 75 percent of the seller's gross retail sales of all food and food ingredients, including prepared food, soft drinks, bottled water, and dietary supplements.

(A) **Exception for four or more servings.** Even if a seller has more than 75 percent prepared food sales, four servings or more of food or food ingredients packaged for sale as a single item and sold for a single price are not "sold with utensils provided by the seller" unless the seller's customary practice for the package is to physically hand or otherwise deliver a utensil to the customer as part of the sales transaction. Whenever available, the number of servings included in a package of food or food ingredients is to be determined based on the manufacturer's product label. If no label is available, the seller must reasonably determine the number of servings.

(B) **Determining total sales of prepared foods.** The seller must determine a single prepared food sales percentage annually for all the seller's establishments in the state based on the prior year of sales. The seller may elect to determine its prepared food sales percentage based either on the prior calendar year or on the prior fiscal year. A seller may not change its elected method for determining its prepared food percentage without the written consent of the department of revenue. The seller must determine its annual prepared food sales percentage as soon as possible after accounting records are available, but in no event later than 90 days after the beginning of the seller's calendar or fiscal year. A seller may make a good faith estimate of its first annual prepared food sales percentage if the seller's records for the prior year are not sufficient to allow the seller to calculate the prepared food sales percentage. The seller must adjust its good faith estimate prospectively if its relative sales of prepared foods in the first 90 days of operation materially depart from the seller's estimate.

(d) **Examples.** The following examples identify a number of facts and then state a conclusion. These examples should be used only as a general guide. The tax results of other situations must be determined after a review of all of the facts and circumstances.

(i) **Example 1.** Fast Cafe sells hot and cold coffee and mixed coffee and mixed milk beverages, cold soft drinks, milk and juice in single-serving containers, sandwiches, whole fruits, cold pasta salad, cookies and other pastries. Fast Cafe prepares the pasta salad on-site. It orders the pastries from a local bakery, including specialty cakes which it sells both as whole cakes and by the slice. It purchases its sandwiches from a local caterer. The sandwiches are delivered by the caterer prewrapped in plastic with condiments and a plastic knife. Fast Cafe makes straws, napkins and cup lids available for all customers by placing them on a self-service stand. In its first full year of operation, Fast Cafe's annual gross retail sales of all food and food ingredients, including prepared food, soft drinks, bottled water, and dietary supplements is \$100,000. Of this gross retail sales total, \$80,000 is from the sale of hot coffee and hot and cold mixed coffee and milk beverages, all sold in disposable paper or plastic cups with the Fast Cafe logo.

Because more than 75 percent of Fast Cafe's total retail sales of food and food ingredients, including prepared food, soft drinks, bottled water, and dietary supplements are sales of food or food ingredients that are heated or combined by the seller or sold with a utensil (cups) necessary to receive the food, Fast Cafe has more than 75 percent prepared food sales. Because Fast Cafe makes utensils available for its customers, all food and food ingredients sold by Fast Cafe are considered "prepared food," including the cold milk beverages, cookies and pastries, pasta salad, sandwiches and whole fruits. The only exception is the sale of whole specialty cakes. Because a whole cake contains four or more servings, it is not subject to retail sales tax unless Fast Cafe customarily hands a utensil to the customer as part of the sale transaction.

(ii) **Example 2.** Assume the same facts as in Example 1, but that only \$60,000 of Fast Cafe's Year 1 gross retail sales were sales of hot coffee and hot and cold mixed coffee and milk beverages. The remainder of its retail sales were sales of sandwiches, whole fruits, cookies and other pastries. Under these facts, Fast Cafe does not have more than 75 percent prepared food sales. Thus, the items sold by Fast Cafe are taxed as follows:

(A) Hot coffee and milk beverages are heated by the seller and are also sold by Fast Cafe with a utensil (a paper cup) necessary to receive the food. The hot coffee and milk beverages are "prepared food" for either reason and are subject to retail sales tax.

(B) Cold mixed milk beverages are a combination of two or more foods or food ingredients and are also sold by Fast Cafe with a utensil (a paper or plastic cup) necessary to receive the food. The cold milk beverages are "prepared food" for either reason and are subject to retail sales tax.

(C) Cold soft drinks are not exempt and are subject to retail sales tax.

(D) Sandwiches prepared by the caterer are subject to retail sales tax. Even though the caterer, rather than the seller, combines the ingredients and includes a utensil, Fast Cafe is considered to have provided the utensil because the caterer is not a food manufacturer classified under sector 311 of the NAICS.

(E) Pasta salad is combined by the seller and is subject to retail sales tax. Note that if the pasta salad was sold by the pound, rather than by servings, it would not be subject to retail sales tax.

(F) Milk and juice in single serving containers, whole fruit, cookies, pastries, slices of cake, and whole cakes are not subject to retail sales tax unless the seller's customary practice is to hand a utensil to the customer as part of the sales transaction. None of these items are heated by the seller, combined by the seller, or require a plate, glass, cup, or bowl in order to receive the item. Even if Fast Cafe heats the pastries for its customers, the pastries are not subject to retail sales tax.

(iii) **Example 3.** A pizza restaurant sells whole hot pizzas, hot pizza by the slice, and unheated ready-to-bake pizzas. The whole hot pizzas and hot pizza sold by the slice, including delivered pizzas, are "prepared food" because these items are sold in a heated state. If the unheated ready-to-bake pizzas are prepared by the seller, they are "prepared food" because the seller has mixed or combined two or more food ingredients. This is true even though some ingredients in the unheated pizzas are raw or uncooked, because those ingredients do not require cooking to prevent foodborne illness. If the unheated ready-to-bake pizzas are prepared by a manufacturer other than the seller, they will be taxable as "prepared food" only if sold with utensils provided by the seller.

(6) **Combined sales of taxable and exempt items.** Where two or more distinct and identifiable items of tangible personal property, at least one of which is a food or food ingredient, are sold for one nonitemized price that does not vary based on the selection by the purchaser of items included in the transaction:

(a) The entire transaction is taxable if the seller's purchase price or sales price of the taxable items is greater than 50 percent of the combined purchase price or sales price; and

(b) The entire transaction is exempt from retail sales tax if the seller's purchase price or sales price of the taxable items is 50 percent or less of the combined purchase price or sales price.

The seller may make the determination based on either purchase price or sales price, but may not use a combination of the purchase price and sales price.

**Example.** A combination wine and cheese picnic basket contains four items packaged together: A bottle of wine, a wine opener, single-serving cheeses, and the picnic basket holding these items. The seller's purchase price for the wine, wine-opener, and picnic basket to-

tals \$10.00. The seller's purchase price for the cheeses is two dollars. The seller must collect retail sales taxes on the entire package, because the seller's purchase price for the taxable items (\$10.00) is greater than 50 percent of the combined purchase price (\$12.00).

(c) **Incidental packaging.** "Distinct and identifiable items" does not include packaging which is immaterial or incidental to the sale of another item or items. For example, a decorative bag sold filled with candy is not the sale of "distinct and identifiable" items where the bag is merely ornamental packaging immaterial in the sale of the candy.

(d) **Free items.** "Distinct and identifiable items" does not include items provided free of charge. An item is only provided free of charge if the seller's sales price does not vary depending on whether the item is included in the sale.

(7) **Seller's accounting requirements.** All sales of food and food ingredients at an establishment will be treated as taxable unless the seller separately accounts for sales of exempt and nonexempt food and food ingredients. It is sufficient separation for accounting purposes if cash registers or the like are programmed to identify items that are not tax exempt and to calculate and assess the proper sales tax accordingly.

(8) **Other retail sales tax exemptions that may apply.**

(a) **Meals served to certain persons.** The exemptions apply to food and food ingredients furnished, prepared, or served as meals:

(i) Under a state-administered nutrition program for the aged as provided for in the Older Americans Act (Public Law 95-478 Title III) and RCW 74.38.040(6);

(ii) Provided to senior citizens, individuals with disabilities, or low-income persons by a nonprofit organization organized under chapter 24.03A or 24.12 RCW; or

(iii) Provided to residents, 62 years of age or older, of a qualified low-income senior housing facility by the lessor or operator of the facility. The sale of a meal that is billed to both spouses of a marital community or both domestic partners of a domestic partnership meets the age requirement in this subsection (a)(iii) if at least one of the spouses or domestic partners is at least 62 years of age. For purposes of this subsection, "qualified low-income senior housing facility" means a facility:

(A) That meets the definition of a qualified low-income housing project under Title 26 U.S.C. Sec. 42 of the federal Internal Revenue Code, as existing on August 1, 2009;

(B) That has been partially funded under Title 42 U.S.C. Sec. 1485 of the federal Internal Revenue Code; and

(C) For which the lessor or operator has at any time been entitled to claim a federal income tax credit under Title 26 U.S.C. Sec. 42 of the federal Internal Revenue Code.

(b) **Foods exempt under the Supplemental Nutrition Assistance Program (SNAP).** Under RCW 82.08.0297, eligible foods purchased with food benefits under the SNAP or a successor program are exempt from the retail sales tax. This is a separate and broader exemption than the retail sales tax exemption for food and food ingredients under RCW 82.08.0293. For example, bottled water, soft drinks, garden seeds, and plants which produce food for the household to eat are "eligible foods" but are not "food or food ingredients." If such items are purchased with food benefits under SNAP or a successor program, they are

exempt from the retail sales tax under RCW 82.08.0297, even though the items do not qualify for the exemption under RCW 82.08.0293.

(i) **Use of food benefits combined with other means of payment.**

When both food benefits and other means of payment are used in the same sales transaction, for purposes of collecting retail sales taxes, the other means of payment must be applied first to items which are food and food ingredients exempt under RCW 82.08.0293. The intent is to apply the benefits and other means of payment in such a way as to provide the greatest possible exemption from retail sales tax.

(ii) **Example.** A customer purchases the following at a grocery store: Meat for three dollars, cereal for three dollars, canned soft drinks for five dollars, and soap for two dollars for a total of \$13.00. The customer pays with seven dollars in benefits and six dollars in cash. The cash is applied first to the soap because the soap is neither exempt under RCW 82.08.0293 nor an eligible food under SNAP. The remaining cash (four dollars) is applied first to the meat and the cereal. The food benefits are applied to the balance of the meat and cereal (two dollars) and to the soft drinks (five dollars). Retail sales tax is due only on the soap.

(9) **Vending machine sales.** The exemptions do not apply to sales of food and food ingredients dispensed from vending machines. There are special requirements for reporting retail sales tax collected on vending machine sales, discussed in (a) of this subsection. "Honor box" sales (sales of snacks or other items from open display trays) are not considered vending machine sales.

(a) **Calculating and reporting retail sales tax collected on vending machine sales.** Vending machine owners do not need to state the retail sales tax amount separately from the selling price. See RCW 82.08.050 and 82.08.0293. Instead, vending machine owners must determine the amount of retail sales tax collected on the sale of food or food ingredients by using one of the following methods:

(i) **Food or food ingredients dispensed in a heated state, soft drinks, and bottled water.** For food or food ingredients dispensed from vending machines in a heated state (e.g., hot coffee, soups, tea, and hot chocolate) and vending machine sales of soft drinks and bottled water, a vending machine owner must calculate the amount of retail sales tax that has been collected ("tax in gross") based on the gross vending machine proceeds. The "tax in gross" is a deduction against the gross amount of both retailing B&O and retail sales. The formula is:

$$\text{gross machine proceeds} - [(\text{gross machine proceeds}) / (1 + \text{sales tax rate})] = \text{tax in gross}$$

(ii) **All other food or food ingredients.** For all other food and food ingredients dispensed from vending machines, a vending machine owner must calculate the amount of retail sales tax that has been collected ("tax in gross") based on 57 percent of the gross vending machine proceeds. The "tax in gross" is a deduction against the gross amount of both retailing B&O and retail sales. The formula is:

$$(\text{gross machine proceeds} \times .57) \times \text{sales tax rate} = \text{tax in gross}$$

The remaining 43 percent of the gross vending machine proceeds, less the "tax in gross" amount, is reported as an exempt food sales deduction against retail sales proceeds only calculated as follows:

$$(\text{gross machine proceeds} \times .43) - \text{tax in gross} = \text{exempt food deduction}$$

(b) **Example.** Jane owns a vending machine business with machines in Spokane and Seattle. In each location, she has a vending machine



selling candy and a second vending machine selling hot cocoa and coffee drinks. Her annual sales for the vending machines and the combined retail sales tax rates for Seattle and Spokane are as follows:

	Coffee Machine (cocoa & coffee)	Candy Machine	Combined Retail Sales Tax Rate
Seattle	\$2,500	\$10,000	.101
Spokane	\$3,000	\$6,000	.089

To determine the amount of retail sales tax she collected on the sale of cocoa and coffee (food dispensed in a heated state, subject to retail sales tax), Jane calculates the "tax in gross" deduction amount as follows:

$$\text{gross machine proceeds} - [(\text{gross machine proceeds}) / (1 + \text{sales tax rate})] = \text{tax in gross}$$

$$\begin{aligned} \$2,500 - (\$2,500 / 1.101) &= \$229.34 && \text{(Seattle coffee machine)} \\ \$3,000 - (\$3,000 / 1.089) &= \$245.18 && \text{(Spokane coffee machine)} \\ & \underline{\hspace{1.5cm}} && \\ & \$474.52 && \end{aligned}$$

Thus, for both retailing B&O and retail sales, Jane must report her total gross coffee machine proceeds of \$5,500 with a "tax in gross" deduction of \$474.52.

To determine the amount of retail sales tax she collected on the sale of candy, Jane calculates the "tax in gross" deduction amount as follows:

$$(\text{gross machine proceeds} \times .57) \times \text{sales tax rate} = \text{tax in gross}$$

$$\begin{aligned} \$10,000 \times .57 \times .101 &= \$575.70 && \text{(Seattle candy machine)} \\ \$6,000 \times .57 \times .089 &= \$304.38 && \text{(Spokane candy machine)} \\ & \underline{\hspace{1.5cm}} && \\ & \$880.08 && \end{aligned}$$

Thus, for both retailing B&O and retail sales, Jane must report her total gross candy machine proceeds of \$16,000 with a "tax in gross" deduction of \$880.08.

Jane must also report an exempt food sales deduction representing the remaining 43 percent of the gross candy machine proceeds.

$$(43\% \times \text{gross machine proceeds}) - \text{tax in gross} = \text{exempt food deduction}$$

$$(.43 \times \$16,000) - \$880.08 = \$5999.92$$

Jane reports the exempt food sales deduction only against the gross amount of her retail sales. The deduction does not apply to retailing B&O.

[Statutory Authority: RCW 82.32.300 and 82.01.060. WSR 22-14-014, § 458-20-244, filed 6/23/22, effective 7/24/22. Statutory Authority: RCW 82.32.300, 82.01.060(2), 82.08.0293, 82.12.0293, 82.08.9994, 82.08.99941, 82.12.9994, and 82.12.99941. WSR 19-20-061, § 458-20-244, filed 9/26/19, effective 10/27/19. Statutory Authority: RCW 82.32.300 and 82.01.060(2). WSR 15-01-006, § 458-20-244, filed 12/4/14, effective 1/4/15. Statutory Authority: RCW 82.32.300, 82.01.060(2), 82.08.0293 and 82.12.0293. WSR 12-01-027, § 458-20-244, filed 12/12/11, effective 1/12/12; WSR 10-21-010, § 458-20-244, filed 10/7/10, effective 11/7/10. Statutory Authority: RCW 82.32.300 and 82.01.060(2). WSR 07-24-038, § 458-20-244, filed 11/30/07, effective 12/31/07; WSR 07-11-066, § 458-20-244, filed 5/14/07, effective 6/14/07; WSR 03-24-031, § 458-20-244, filed 11/25/03, effective

1/1/04. Statutory Authority: RCW 82.32.300. WSR 88-15-066 (Order 88-4), § 458-20-244, filed 7/19/88; WSR 87-19-139 (Order 87-6), § 458-20-244, filed 9/22/87; WSR 86-21-085 (Order ET 86-18), § 458-20-244, filed 10/17/86; WSR 86-02-039 (Order ET 85-8), § 458-20-244, filed 12/31/85; WSR 83-17-099 (Order ET 83-6), § 458-20-244, filed 8/23/83; WSR 82-16-061 (Order ET 82-7), § 458-20-244, filed 7/30/82. Statutory Authority: RCW 82.01.060(2) and 82.32.300. WSR 78-05-041 (Order ET 78-1), § 458-20-244 (Rule 244), filed 4/21/78, effective 7/1/78.]

**Reviser's note:** The brackets and enclosed material in the text of the above section occurred in the copy filed by the agency and appear in the Register pursuant to the requirements of RCW 34.08.040.