

Memorandum

To: Ms. Susan Wengel
Assistant Chief Counsel - MIC:85

Date: October 31, 1996

From: Gary J. Jugum
Assistant Chief Counsel

Subject: REDACTED TEXT

The referenced matter is scheduled for Board hearing on November 20, 1996. The issue in this case is whether wood chips obtained from burnt forests constitute waste by-products from forest production operations, the sale of which are exempt under Revenue and Taxation Code section 6358.1, where the forest fire is caused by natural means, accident or arson.

Revenue and Taxation code section 6358.1 provides an exemption for "waste by-products from agricultural or forest products operations. . . ." which are used for certain specified purposes. The term "forest products operations" is not defined.

This taxpayer contracts as an independent contractor with land owners for salvage operations on timberland. The scope of taxpayer's employment is typically described as follows:

"Removal, cutting, and chipping of wood products and non-merchantable timber from Client's real property as described herein. Contractor shall not cut or remove merchantable timber, nor shall Contractor cut so many trees that the property will not meet stocking requirements of the Department of Forestry of the State of California."

These salvage operations occur after the land has been subject to a controlled burn, or where a forest fire is caused by natural means, accident, or arson. Taxpayer chips out stumps and other materials not consumed in the burn. Taxpayer then sells the chips. The question is whether the sale of the chips qualifies for exemption from tax.

The staff has previously concluded that if a controlled fire is set by the forest service, wood chips made from the stumps and other tree parts in the burned area constitute waste by-products from forest products operations.

Taxpayer's sale of wood chips salvaged following an unplanned burn is nontaxable if the chips constitute "waste by-products from. . . forest products operations." It is not clear that taxpayer itself is engaged in "forest products operations," either when it salvages and sells chips following a planned burn, or when it salvages and sells chips following an unplanned burn. This analysis is irrelevant, however. The statute does not specify that the "forest products operations" must be conducted by the person selling the "waste by-products." Such a limited interpretation would make no sense. If the section were given such limited application, then the exemption would apply only if the retailer of the chips was the person conducting the "forest products operations." There is no reason, however, that the person conducting the "forest products operations" cannot sell the "waste by-products" in a sale for resale to another person who will make the retail sale. We think it is the meaning and intention of section 6358.1 that such subsequent retail sale would qualify for exemption under section 6358.1.

Here the chips are a "waste by-product" with respect to the "forest products operations" conducted by the owner of the land. There is no material difference between the case where the wood chips are harvested following a planned burn versus an unplanned burn. Clearing of undergrowth to prevent fires and thinning for new growth or promotion of growth are "forest products operations." Management of the forest includes both the conducting of planned burns and the conducting of operations in response to fires caused by natural means, accident, or arson. It is thus our opinion that this taxpayer's sales of wood chips qualify for exemption as sales of "waste by-products" resulting from "forest products operations" within the meaning of section 6358.1.

This interpretation is consistent with the intent of section 6358.1 that there should be a tax incentive to promote the salvaging of waste by-products from agricultural or forest products operations, to be used as a fuel source in lieu of oil, natural gas, and coal.

It is our recommendation that this matter be taken off calendar and that the petition be granted.

GJJ:sr

cc: Mr. Glenn A. Bystrom - MIC:43
Ms. Mary Armstrong - MIC:83
Ms. Janice Masterton - MIC:81

bc: Ms. Sophia Chung