Excise Tax Advisory

Excise Tax Advisories are interpretive statements authorized by RCW 34.05.230.

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Distributor Discounts/Allowances to Grocery Stores

Purpose

This Excise Tax Advisory explains the business and occupation (B&O) tax liability for grocery stores receiving distributor allowances or discounts.[1]

***Bona fide* vs. non *bona fide* discounts**

Per WAC 458-20-108, "selling price…does not include the amount of bona fide discounts actually taken by the buyer and the amount of such discount may be deducted from gross proceeds of sales providing such amount has been included in the gross amount reported." A *bona fide* discount is, for example, when the distributor grants the grocer either a discount or some form of payment for doing nothing more than purchasing products from the distributor.

The Department of Revenue's (Department) long standing position is that a discount is not *bona fide* if it is in exchange for a service or benefit, whether this is done pursuant to a written contract, business practice, or oral agreement.

Generally, a *bona fide* discount negotiated by the grocer upon purchase of the goods does nothing more than encourage the grocer to make sales they were already going to make. However, if a grocer performs a service in addition to selling the goods in exchange for the discount, then the discount is not *bona fide*.

Non *bona fide* discounts are subject to tax

Examples of discounts that are not *bona fide* because the person providing the allowance receives a service or benefit in return include, but are not limited to:

- Advertising allowance
  - An example of an advertising allowance is when a grocer receives some form of payment or credit from a distributor for advertising a distributor's products in print, on the Internet, or in the Taxpayer's place of business.

[1] For the purposes of this document only, the terms "allowance" and "discount" are used interchangeably.

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- Exclusivity allowance
  - An example of an exclusivity allowance is when a grocer receives some form of payment or credit from a distributor for carrying only the distributor's products to the exclusion of competitor's similar products. For example, a laundry detergent distributor provides a discount to a grocer if the grocer agrees not to stock laundry detergents sold by other distributors.

- Placement (slotting) allowance
  - An example of a placement allowance is when a grocer receives a payment or credit from a distributor for introducing a product line in the store or for placing a product in certain locations or in certain displays in the store.

The discounts described above are generally received in exchange for services and such income is reported as taxable gross income, generally subject to Service & Other B&O tax. See Det. No. 98-172E, 18 WTD 387 (1999).

***Bona fide* discounts are not subject to B&O tax**

Examples of discounts that are *bona fide* when the distributor providing the allowance does not receive a service or benefit from the grocer in return include, but are not limited to:

- Off-invoice allowance
  - An example of an off-invoice allowance is when a distributor reduces the price of a product by discounting the invoice price.

- Scan-down allowance
  - An example of a scan-down allowance is when a distributor gives the grocer a payment or credit for selling a specific volume of products during a specific timeframe.

- Volume discount allowance
  - An example of a volume discount allowance is when a distributor and a grocer agree in advance on a payment or discount on a per case/item basis and the grocer invoices the distributor for the discount based on the number of cases/items sold at the end of a particular period.

The discounts described above are generally not received in exchange for any service or benefit, and thus are not subject to B&O tax.

However, it is important to note that the name of the allowance alone will not determine that a discount is *bona fide*. For example, a scan-down allowance may also be provided to a grocery store by a distributor for a specific period for doing product advertising during that period. Such a scan-down allowance would also be in exchange for the advertising services, so it would not be a *bona fide* discount.

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What indicates services are provided in exchange for a discount?

Examples of indicators that suggest that the grocer is providing a service in exchange for a discount include:

Indicators of Service in Exchange
Written contract or enforceable right requiring performance by grocer
Ad copy is provided by vendor and vendor requests confirmation or other information about the use of the supplied ad copy, such as a copy of the ads run, be sent to the vendor
Invoice that contains a check box to indicate whether the grocer used the ad copy
Discount payments are accounted for as an income stream on the general ledger
Accounting entry lists the discount as an "advertising allowance," "promotional effort," or other term indicating a service was performed

This list of indicators is not complete. These are merely examples of the types of practices that indicate that an activity performed by a grocer may be a service performed in exchange for a discount. If there is no indicator showing a service was performed in exchange for a discount, the discount is presumed to be *bona fide*.

Contract example

Contractual Discount Example

Facts
A soft drink supplier enters into an agreement with a grocer that specifies what aspects of the supplier's advertising should be used in the store, in print ads, and online in exchange for discounts on the supplier's products.

Conclusion
The discount is not *bona fide*. Per the agreement, the advertising services are performed in exchange for the discount.

Membership example

Membership Discounts Example

Facts
Shoppers in a grocer's "Membership" program receive lower prices on specially marked items. A distributor enters into an agreement to sell its products to the grocer at a discount if the distributor's products will be included in the grocer's membership club program, which includes being listed in club program advertisements, in store notices and product displays, or aisle tags.

Conclusion
The allowance or discount is not *bona fide* because the grocer advertised the discounted items associated with its membership program in exchange for the discount per the agreement. The agreement is the indicator of the distributor's

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reason for providing the discount, in part, for the advertising services performed by the grocer.

Provided Ads example

Provided Ads Example

Facts
A distributor provides an ad sheet to the grocer with suggested ads that the grocer may use in its local advertising campaign. The distributor makes no effort to determine whether the grocer uses the ads. The distributor later sends the grocer an invoice for the items purchased by the grocer. Some of the items on the invoice are discounted by the distributor. Some of the discounted items were among those listed on the ad sheet. The discount is not listed on the invoice as an advertising discount, is booked as a reduction to the purchase price on the invoice, and is recorded in the accounting records of the grocer consistent with a bona fide purchase discount, such as a volume discount.

Conclusion
The discount is *bona fide* because there is no indicator that a link exists between the discount and the grocer's use of the provided ads.

Invoice Check Box example

Invoice Check Box Example

Facts
Same facts as the previous example, but the invoice that the distributor sends to the grocer includes a section with a check box that states, "Did you run the ad for this item for the week of December 19, 2011? Please attach a copy of the ad."

Conclusion
The discount is not *bona fide* because the invoice indicates that there is a link between the discount and the advertising services.

Advertising Discount Line Item example

Advertising Discount Line Item Example

Facts
Same facts as the Provided Ads Example, but the invoice that the distributor sends to the grocer includes a line item titled "Advertising Discount."

Conclusion
The discount is not *bona fide* because the line item on the invoice describing the discount as an "advertising discount" indicates that there is a link between the discount and the advertising services.

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Contract Number Reference example

Contract Number Reference Example

Facts
Same facts as the Provided Ads Example, but the invoice references promotional efforts and a contract number is referenced in relation to the promotional efforts.

Conclusion
The discount is not *bona fide* because the reference to a contract indicates that there is a link between the discount and the promotional services. The grocery store must have a copy of the contract referenced to show that there is no link between the discount and the promotional service. If the grocery store does not retain a copy of the referenced contract, then the discount is still not *bona fide*.

Scan Down With Ad example

Scan Down With Ad Example

Facts
Same facts as the Invoice Check Box Example, but the distributor requires the grocer send an invoice listing how many items were sold during the week of December 19, 2011, with the copy of the ad that was used.

Conclusion
The discount is not *bona fide* because the advertising services are performed in exchange for the discount. The scan down allowance alone would be a *bona fide* discount, but because it is linked to the advertising services, it is not *bona fide*.

Volume and Ad Discounts example

Volume Discount and Ad Discount Example

Facts
A distributor sends the grocery store an invoice for the purchase of cans of soup. The invoice includes a volume discount for the 50 cans of soup sold the previous month and lists a promotional allowance in the bottom corner of the invoice for the current month.

Conclusion
The volume discount is a *bona fide* discount because there is no indicator. The promotional allowance is not *bona fide* because the indicator on the invoice shows income for promotional services.

Store Ad example

Store Ad Example

Facts
A grocer holds a contest at a local elementary school soliciting art work for its weekly chocolate milk advertisement. A second grade student wins the contest with her depiction of a cow eating a chocolate candy bar. The distributor sells the grocer chocolate milk at a discount during the time that the grocer publishes an advertisement using the second grade student's art.

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Conclusion
The discount is *bona fide* because there is no indicator of a link between the advertising done by the grocer and the discount provided by the distributor.

Income Account on General Ledger example

Income Account on General Ledger Example

Facts
A grocery store receives a payment for a product discount from a distributor. The grocery store accounts for the payment in an income account on its general ledger.

Conclusion
The payment is not a *bona fide* discount because the grocery store's accounting for the payment in an income account is an indicator that the payment is in exchange for a service.

Rebuttal and Records Retention

Grocery stores receiving a *bona fide* discount when there is an indicator of a link between a service and the discount may rebut the presumption created by the indicator by producing the necessary records documenting that these transactions are unrelated to advertising services. Proper documentation to support any claimed deduction or exemption is required under the law. Under RCW 82.32.070, taxpayers must "keep and preserve…suitable records." If taxpayers do not keep accurate records and there are indicators that a service was provided in exchange for the discount, then additional information may be requested to determine if the discounts are *bona fide* and properly deducted from the gross proceeds of sales.

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