



# INTERIM AUDIT GUIDELINE

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Interim Audit Guidelines are interpretive statements issued by the Department of Revenue under authority of RCW 34.05.230. These guidelines explain the Department's policy regarding how tax law applies to a specific issue or specific set of facts and are intended to communicate timely guidance of tax issues important to the public and agency staff where no published guidance exists. They are advisory for taxpayers; however, the Department is bound by these guidelines until superseded by Court action, Legislative action, rule adoption, or an amendment to or cancellation of the interim audit guideline.

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~~Interim Audit Guideline 01.01~~ **PLEASE SEE** [ETA 2008](#)

## Deferred Sales Tax

The purpose of this interim audit guideline is to instruct Department personnel on the proper use of the term "deferred sales tax." This guideline also explains the difference between deferred sales tax and use tax and provides instructions on proper reporting and audit procedures.

The retail sales tax is imposed on persons who purchase nonexempt items of tangible personal property within the state as consumers. Sellers who make retail sales in the state are required to collect the retail sales tax from buyers and remit the tax to the Department. Any seller required to collect retail sales tax who fails to do so is liable for the full amount of the uncollected tax. The retail sales tax is measured by the selling price of the item sold, including any freight or handling charges imposed by the seller regardless of whether such charges are separately stated in the contract of sale or sales invoice.

Generally, there are two situations where a seller may be relieved of the duty to collect retail sales tax:

Situation 1: The seller receives a properly documented claim for tax exemption from the buyer; or

Situation 2: The seller takes a properly executed resale certificate from a buyer who normally engages in both consuming and reselling nonexempt items of tangible personal property, and the buyer cannot determine at the time of purchase whether the property will be consumed or resold.

If the seller fails to collect retail sales tax that is later determined to be due, the Department may proceed directly against the buyer to collect the tax. The retail sales tax may become due from the buyer under Situation 1 if events occurring after the sale fail to meet the requirements for tax exemption. In Situation 2 the buyer is required to maintain records of the items consumed and remit the retail sales tax directly to the Department. The Department sometimes refers to the sales tax that may become due from the buyers in both situations as "deferred sales tax." The tax is deferred because at the time of sale the facts giving rise to the tax liability are not yet known. Deferred sales tax does not refer to sales tax that is properly due at the time of sale that the seller mistakenly or purposefully fails to collect.

Deferred sales tax is not the same as use tax. Use tax is imposed on the use by a consumer of nonexempt tangible personal property within the state. The tax does not apply when the acquisition or

sale of the property has been previously subjected to the retail sales tax. "Use" for this purpose means the first act within the state by which a person first takes or assumes dominion and control over an item of tangible personal property as a consumer, and includes installation, storage, withdrawal from storage, or any other act preparatory to subsequent actual use or consumption within the state. The use tax is based on the value of property at the time of first taxable use within the state. Normally, the value of an item of property acquired by purchase will be the price paid by the buyer less any freight charges separately identified in the contract of sale or sales invoice.

The following examples illustrate the difference between deferred sales tax and use tax:

Example A: A buyer provides a resale certificate to a seller under Situation 2 and later withdraws an item from inventory for use in the buyer's business. The buyer will be liable for retail sales tax on the selling price paid for the item at the time the item is withdrawn from inventory. The sales tax applies regardless of whether the item withdrawn from inventory is used inside or outside the state. The local tax rate would be determined under WAC 458-20-145 based on the place of sale.

Example B: The buyer in Example A acquires inventory under circumstances where the seller does not have a duty to collect tax in the first instance (e.g. its seller is not required to register with the Department). The buyer later withdraws several items from inventory for use within the state. In this example the buyer is liable for use tax based on the value of the withdrawn items at the time they are first used in the state. The local tax rate is determined based on the place of first taxable use under WAC 458-20-145. If the items are immediately sent outside the state for use, no tax would be due because storage preparatory to use outside the state is not a taxable use.

Because the Combined Excise Tax Return does not have a special line for reporting deferred or unpaid sales taxes on purchases, taxpayers should be instructed to report these amounts on the use tax line of the return. The retail sales tax line on the return is designed for persons who make retail sales (sellers) and not for persons making taxable purchases. Therefore, in most instances the total sales subject to retail sales tax must agree with total retail sales reported for business and occupation tax purposes. If sales reported for sales tax and B&O tax purposes do not agree, the return will be out of balance and may generate an error notice from the Department. The local tax component of deferred or unpaid sales tax should be reported in the local use tax area of the return using the appropriate location code corresponding to the place of sale determined under WAC 458-20-145.

If an auditor discovers untaxed purchases that are properly subject to the retail sales tax, these items should be assessed and coded as sales tax and not as use tax. The local tax component of deferred or unpaid sales tax should be assigned to the correct local jurisdiction corresponding to the place of sale under WAC 458-20-145.

When sampling purchases to project underpayments or overpayments of tax it may not be practical to distinguish between use tax and deferred sales tax. In such cases, auditors should identify any resulting underpayment or overpayment as "deferred sales and/or use tax" and provide an explanation to the taxpayer of how the amount was calculated. The explanation should note that the computed amount may

include both deferred sales and use taxes. The evaluation of each item in the sample should be based on the total tax properly due with respect to the item according to the applicable tax and local tax coding.

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