Cite as 5 WTD 41 (1988)

BEFORE THE DIRECTOR
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of Assessment of)	F I N A L D E T E R M I N A T I O N
)	No. 87-75A
. . .)	Registration No. . . .

[1] **RULE 119:** RETAIL SALES TAX -- EMPLOYEE MEALS. Retail sales tax is due upon the selling price of employee meals supplied by an employer measured by the selling price rather than by a minimal charge which does not represent the value of the consideration received. Under Rule 119 the cost of the food in employees' meals is the appropriate tax measure.

[2] **RCW 82.08.050:** RETAIL SALES TAX -- TAX SEPARATELY ITEMIZED -- EVIDENCE -- BUYER'S DUTY. A buyer who pays tax separately itemized on a retail sale billing has no further obligation to assure that the seller remits such tax to the state. Payment by the buyer of the amount billed as tax goes to the weight of the evidence that sales tax has been paid and is not overcome by supposition that the amount could be something other than sales tax.

TAXPAYER REPRESENTED BY: . . .
. . .

HEARING CONDUCTED BY DIRECTOR'S DESIGNEES:
Garry G. Fujita, Assistant Director, I&A
Edward L. Faker, Sr. Administrative Law Judge

DATE AND PLACE OF HEARING: July 15, 1987 -- Teleconference,
. . . , Washington

NATURE OF ACTION:

The taxpayer appeals from the findings and conclusions of Determination No. 87-75 which was issued on March 18, 1987 after an

original appeal conference conducted on November 8, 1985. That Determination sustained the assessment of retailing business tax and retail sales tax measured by the value of food provided to employees in the form of meals. It also sustained the assessment of retail sales tax measured by lease payments made by the taxpayer to its lessor of business equipment.

FACTS AND ISSUES:

Faker, Sr. A.L.J. -- The facts of this case, to the extent that they are known, are not disputed. As to the first issue stated below, the taxpayer has challenged a factual statement in Determination No. 87-75 that the reason it charged its employees only one percent (1%) of the menu price for meals was because the cash registers used by the taxpayer were incapable of backing out one hundred percent (100%) of the entered price. This is not a dispositive fact pertinent to this issue and it is referenced here for purposes of precision and clarity.

With regard to the second issue stated below, the factual history of the equipment lease transaction is not fully known by the taxpayer or discoverable by the Department. Some parties (lessors) are gone and records are not available. The known background of the lease transaction is fully and properly reported in Determination 87-75 and is not restated here. The "Facts" portion of Determination 87-75 is incorporated herein by this reference.

There are two independent issues for our resolution.

> 1) Was the taxpayer's per meal charge to its employees (1% of the meal price) the appropriate tax measure for "employee provided meals" under WAC 458-20-119 or should the tax measure be the average cost, to the taxpayer, of the food served?
>
> 2) Was the taxpayer, as a lessee/consumer of operating equipment, entitled to a credit or offset for retail sales tax paid by its lessor to a third party provider and passed through to the taxpayer on its lease billings as "tax as charged by financing company?"

A third issue originally involved in the audit and tax assessment has been resolved by the Department's field agents.

TAXPAYER'S EXCEPTIONS:

The taxpayer asserts that WAC 458-20-119 (Rule 119) which covers the tax liability attendant to providing employees with meals as part of their compensation does not provide that the specific charge made for such meals has to be reasonable or sufficient to cover the cost of the meal. Rather, the rule simply provides that where a specific charge is made, the sales tax must be collected

and accounted for on the selling price. The taxpayer asserts that its charge to employees of 1% of the meal menu price was purposely established and included in its employees' handbook, rather than simply being the result of cash register incapabilities. The taxpayer does not consider itself to be seeking a "loophole" in the rule, or to be consciously avoiding tax liability, but asserts that its methodology was simply the easiest way to administer the rule and calculate tax due.

The taxpayer's records and employees' handbook, copies and excerpts from which were provided for our review, reflect that its 99% employee meals discount program was an established and consistently followed system. It resulted in employees paying five cents (.05 cents) for a meal priced at $3.75. The taxpayer asserts that its charge to employees was "quite precise and specific." Thus, the conclusion in Determination 87-75 that, ". . . there was no specific charge within the meaning and intent of Rule 119" was incorrect.

The taxpayer's petition includes the following argument.

> Here, the taxpayer charged his employees a price equal to 1 percent of the normal cost of the meal. Retail sales tax was collected and accounted for on that selling price.
>
> However, the Determination held that such selling price did not constitute a "specific charge," because, in Judge . . . 's opinion, the price was too low. Instead, he ruled that, where the price is "much less than the actual cost of the food . . . the proper measure of the tax is the cost of the food. . . ." Determination 87-75, p. 4.
>
> Nowhere does this reasoning find any support in the language of the Rule itself. The WAC specifically acknowledges that persons in the restaurant business customarily furnish their employees meals, and sometimes impose a charge and sometimes don't. It does not require that the charge be any minimum amount, such as "greater than or equal to any amount which is 'much less than' actual cost." Instead, it simply says that, where a charge is made, that price is used; where no charge is made, the actual cost is used.
>
> There is a very good reason why the Rule is written in the way it is. It provides a "bright line" that is simple for both the employer and the Department to compute and administer.
>
> If the logic of the Determination were adopted, then how would an employer or the Department know whether the discount is "too low," so as to trigger this suggested

> enforcement mechanism that would ignore the specific language of the WAC? How would this be applied in various types of restaurants with different markup rates?
>
> Under the reasoning of the Determination, an employer would presumably be able to impose a selling price somewhat below actual cost, but not too far below actual cost. If the price were "much less than" actual cost, sales tax would be imposed not on the Minimum Acceptable Discounted Price, but on the actual cost itself. However, if the price were to be only "a little less than" the actual cost, the sales tax could be imposed on that price. Such inequities, and the related administrative complexities, are the reason why the Rule itself was quite clear in permitting tax to be imposed against whatever price the employer decided to charge.

Regarding the second issue, again the facts and taxpayer's arguments are reported fully in Determination 87-75. The taxpayer's petition on this issue includes the following.

> The taxpayer leased certain equipment from . . . Equipment Company. A copy of that lease is attached hereto as Exhibit "B".[1] . . . Equipment Company, in turn, leased that equipment from . . . Credit Corp., which is now a subsidiary of . . . Corporation in Stamford, Connecticut. . . . has either gone out of business or may have been merged into " . . . Holding Co." of Denver, Colorado. The taxpayer is not sure about this.
>
> The correct way for this transaction to have been handled would have been for . . . Equipment Company to give . . . Credit Corp. a certificate of resale, since . . . intended to make no use of the property other than to re-lease it. WAC 458-20-102. . . . then should have collected and paid the sales tax itself. WAC 458-20-211. If . . . had paid some amount of sales or use tax to the state of Colorado, in which . . . was located, it would have been entitled to a credit against Washington's sales and use tax for that amount. RCW 82.56.010 (Article V).
>
> Instead, . . . did not give a certificate of resale to . . . , but simply passed along to . . . the amount of tax that was charged to it by . . . . . . then paid the tax to the Washington Department of Revenue. This is perfectly understandable inasmuch as neither . . . nor . . . were residents of Washington, and therefore may not

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[1] Exhibits referred to in the taxpayer's petition are not appended as exhibits to this Final Determination.

have been familiar with the WAC regarding Resale Certificates. . . . should not have to suffer for this however.

The Auditor's Report indicated that $ . . . was due as sales tax on these lease payments. In fact, . . . paid a total of $ . . . as tax on those payments, as indicated by the separately stated amounts for tax on the invoices. . . . should therefore be entitled to a credit in that amount.

. . .

After tracing through the documentation described below, it will become apparent that . . . did in fact pay tax to the Washington Department of Revenue. Such amounts were based on the amount of its rental charged to . . .. That rental amount varied from the rental amount charged by . . . to . . . . That is the reason the percentages don't match up, as noted in footnote 2 on page 5 of the Determination. The following facts need to be kept in mind:

- The invoices received by the taxpayer from . . . included a separately stated amount for tax, as required by RCW 82.08.050

- The taxpayer paid these amounts.

Nowhere does the statute or WAC impose on the buyer some kind of duty to audit all the seller's transactions with the Department of Revenue and make sure that every vendor with whom the taxpayer deals does in fact pay to the Washington Department of Revenue the amounts stated on the invoices received by the taxpayer from each such seller. It does not require buyers to act like private enforcement agencies. Yet, that is precisely what kind of burden this Determination would impose on . . . .

Nonetheless, taxpayer can in fact show,for a sample month, how the amounts shown on the invoices eventually traced their way back to the Washington Department of Revenue.

. . .

A taxpayer should not have to go through the labor of tracing transactions between its different vendors and the Washington Department of Revenue, as . . . has had to do in this case. Instead, a buyer's burden is removed after he pays the amount indicated as "tax" on the sales invoice to his vendor. RCW 82.08.050. See Exhibit "E".

> Nonetheless, the taxpayer has gone through this exercise for the period for which . . . sent it data, pursuant to Mr. . . . 's April 24, 1987, letter (Exhibit "G").
>
> The Determination suggested that the Rule of RCW 82.08.050 and WAC 458-20-221, which requires the invoices to separately state the tax and requires the buyer to pay such amount is inapplicable here to give the buyer a credit for the amount shown as "tax." The reasoning was that the invoice did not specifically state "sales or use" tax, and therefore could theoretically have been some other form of tax (such as property tax). This is unreasonable for several reasons, including:
>
> (a) Neither Rule 221 nor RCW 82.08.050 specifically require reference to the words "sales or excise," but only refer to separately stating the amount of "the tax";
>
> (b) Standard commercial practice is to show excise taxes on sales invoices, whereas personal property taxes are "1-shot" items which are paid when the assessment comes out; and
>
> (c) The fact that we have shown through the Exhibits that this was in fact an excise tax.

At the July 15, 1987 Director's level hearing the taxpayer relied upon its petition statements. It emphasized that, based upon the full explanation of what transpired in connection with the lease, and based upon the meaning of "tax as charged by finance company" supported in its documents and exhibits, it is clear that the taxpayer did remit Washington's sales tax to its lessor.

DISCUSSION:

There are certain specific statutory definitions and other statutory tax provisions which prevail in this case and which are fully referenced and explained in Determination 87-75. They are correctly applied in that Determination. The crux of these statutory applications is that, whatever cash charge may have been paid for meals by the employees, the taxable selling price consisted of the total consideration paid. That was a combination of both cash and employee labor. It was because of this very realization by the Department that Rule 119 was originally developed and periodically amended with the cooperation and assistance of the private business sector (Washington Restaurant Association). There is no express statutory tax treatment governing restaurants which provide meals to employees at reduced prices or free of charge. Through Rule 119, however, the Department has taken administrative notice of the business reality that such employee meals are commonly used to compensate employees as benefits in addition to salary. Rule 119 is a necessary rule of

procedure which provides uniform and equitable methods for use in situations where restaurants (and other situations not pertinent here) provide meals to employees and the precise tax measure is unclear because the consideration is not simply cash paid. As such, this rule has the same force and effect as the statutes it administers. (See RCW 82.32.300.)

[1] It is not the intent of Rule 119 that restaurants may arbitrarily establish a minimal cash charge which employees will pay for employer provided meals and thereby avoid consumer taxes (sales tax or use tax) upon the value of such things. The Department has no authority to provide such tax exemptions or deductions by administrative rule. See Budget Rent-A-Car v. State, 81 Wn.2d 171 (1972). Thus, an attempted technical application of the precise wording of the rule for the sole purpose of avoiding the tax liability which the rule seeks to administer in a uniform manner makes the rule provision a nullity and defeats its very purpose. Moreover, even when the rule statement about employee meals is technically construed; it does not provide that the tax is due only on the cash charge made to the employee. The rule expressly states:

> Where a specific charge is made, the retail sales tax must be collected and accounted for on the selling price. (Emphasis supplied.)

The statutory term "selling price," as explained in Determination 87-75, includes both the cash payment and any other rights delivered by a buyer (the employee here) to a seller (the employer here). Thus, the rule statement cannot be misconstrued to artificially lower the tax measure to .05 cents on a $3.75 meal provided to employees as part of employee benefits.

Determination 87-75 properly resolves this employee meals issue and the findings and conclusions of that Determination on this issue are hereby sustained.

[2] Regarding the second issue before us, we have thoroughly reviewed the lease billing documents and other exhibits submitted and referenced in the taxpayer's petition. We are now satisfied that the taxpayer paid to its lessor, . . . Equipment Company, a line itemized amount which the parties recognized was the Washington State retail sales tax due on the lease payments. Determining whether the lessor improperly paid these amounts over to its seller, . . . , and whether that seller, in turn, fully remitted this sales tax to this state, are not legal obligations which the lessee/taxpayer must satisfy.

While there maybe valid concerns and questions about these happenings, there is no evidence whatever that the amount line itemized as "tax as charged by financing company" was anything other than the sales tax due on the lease payments. Moreover, the

taxpayer has satisfactorily explained the disparity between the amounts it paid to its lessor and the amounts computed by the auditor to be due on the lease payments by applying the prevailing tax rates in Washington at those times. This differential arose because the taxpayer's lessor, . . . , was an equipment leasing company exclusively leasing to the taxpayer and other of its franchised restaurants. Thus, the retail lease payments and length of lease terms were different from the terms upon which the lessor acquired the equipment at wholesale. Nonetheless, whether or not the amount of tax actually paid to its lessor by the taxpayer was precisely the amount which would have been due if this transaction had been properly structured from the outset, it is now apparent that the amount actually paid did constitute sales tax and should be entitled to the credit offset sought by the taxpayer.

It is important to fully understand that no other state had jurisdiction to tax the lease payments or income from the lease of equipment located in this state during the periods of the lease. It is inappropriate and unsupported by the best available evidence to assume that the line itemized tax payments could be some other state's tax or anything other than the sales tax due. RCW 82.08.050 which requires the buyer (lessee) to pay sales tax over to the seller (lessor) imposes no further duty on the buyer to somehow assure that the seller properly remits the tax to this state.

In its final analysis, this issue raises a question of fact. There was a close association between the taxpayer and its equipment leasing company. The taxpayer possibly should have known that the two-level leasing transaction should have been structured differently so that the leasing company was acquiring the equipment for resale (release) to the taxpayer and, therefor, there should have been no retail sales tax being charged by the wholesale lessor, . . . , to the retail lessor, ... Nevertheless, the wholesale lessor was registered with the Department and was remitting retail sales tax to this state on its regular combined excise tax returns. There is no evidence in support of any disbelief that this tax remitted was not the tax paid by the taxpayer to its lessor and, in turn, paid through to the wholesale lessor.

We have concluded that his question should be resolved in the taxpayer's favor at the administrative level, so that it may be credited with the amounts it paid designated "tax as charged by financing company" against the sales tax assessment in issue here. However, we are not convinced that the taxpayer could establish such credit entitlement strictly as a matter of law. Accordingly, we have referred Tax Assessment No. . . . to the Audit Section for the purpose of recomputing the tax and interest due after the application of the credit offset. If the amount found to be due is timely paid, the balance of Tax Assessment . . . will be cancelled.

DECISION AND DISPOSITION:

The taxpayer's petition is qualifiedly sustained in part. The Audit Section will proceed with recomputations of tax and interest due and effect payment thereof as explained here.

DATED this 10th day of February 1988.