Cite as Det. No. 00-150R, 20 WTD 442 (2001)

BEFORE THE APPEALS DIVISION
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. 00-150R[1]
. . .	)	Registration No. . . .
	)	FY. . ./Audit No. . . .
	)	Docket No. . . .

[1] RULE 102; RCW 82.08.130: RETAIL SALES TAX – "DEFERRED SALES TAX" – PURCHASES FOR DUAL PURPOSES. While WAC 458-20-102(11), dealing with purchases for dual purposes, instructs the buyer to report the "deferred sales tax liability" under the use tax classification on its excise tax return, the rule does not classify the tax liability as use tax. The term "deferred sales tax" as used in Rule 102 means retail sales tax.

[2] RULE 102; RCW 82.08.130: RETAIL SALES TAX – "DEFERRED SALES TAX" – PURCHASES FOR DUAL PURPOSES. In a purchase for dual purposes situation in which a buyer gives a resale certificate as allowed by RCW 82.08.130 and WAC 458-20-102(11), and subsequently consumes some of the articles, the taxable event with respect to the articles consumed is the sale on which the buyer gave the resale certificate, not the subsequent use of the articles. The measure of the tax is the [selling] price of the articles purchased with a resale certificate and subsequently consumed.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

NATURE OF ACTION:

Taxpayer is a distributor of educational publications who gave resale certificates on all acquisitions of inventory, and regularly withdrew some articles from inventory and distributed them as free samples. It requests reconsideration of Determination No. 00-150, which sustained

[1] The original determination, Det. No. 00-150, is published at 20 WTD 432 (2001).

an assessment of "deferred sales tax" on articles the taxpayer removed from inventory and distributed out of state as free samples.[2]

FACTS:

Prusia, A.L.J. -- We repeat the facts as set out in Det. No. 00-150:

> The taxpayer is engaged in business in Washington as a distributor of textbooks and educational materials (hereinafter referred to as "publications").[3] The taxpayer buys the publications at wholesale from a number of Washington-registered vendors, and resells the publications to school districts and other buyers, using a catalog distribution model. The taxpayer has customers both in and outside Washington. The taxpayer has its office and warehouse facilities in [Washington].
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> The taxpayer provides resale certificates to its vendors on 100% of purchased inventory. It resells the great majority of the publications it purchases. However, it distributes some as free samples. The samples are used to introduce products to the taxpayer's buyers. This occurs when a potential buyer of a publication requests a sample for purposes of comparing it with other publications. The samples are identical to the items the taxpayer sells in the regular course of its business. At the time it purchases the inventory, the taxpayer is not able to determine whether particular property purchased will be used as a sample or resold. For 1996, 1997, and 1998, samples as a percentage of purchased inventory were 8.79%, 9.02%, and 18.88% respectively.
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> The Audit Division of the Department of Revenue (Department) examined the taxpayer's business records for the period January 1, 1995 through December 31, 1998. As a result of this audit, the Department issued Tax Assessment No. FY. . . on November 17, 1999, in the amount of $. . . plus $. . . statutory interest. Schedule 7 of the assessment is for "deferred sales tax/use tax" on publications the taxpayer took from inventory and sent as free samples to potential buyers in Washington. Schedule 8 is for "deferred sales tax" on publications the taxpayer took from inventory and sent as free samples to potential buyers out-of-state.
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> The taxpayer contests Schedule 8 of the assessment, which assesses $. . . in additional tax, as well as statutory interest related to Schedule 8. The taxpayer agreed to the remainder of the assessment, including the Schedule 7 portion, and in December 1999 paid $. . . on the assessment.
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> The Audit Division based the Schedule 8 assessment upon its interpretation of RCW 82.08.130 and WAC 458-20-102 (Rule 102). It interprets those provisions as requiring

[2] Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

[3] The taxpayer is a "publisher" in that it owns the copyrights or distribution rights to the materials. It generally is the sole source of titles it distributes. The taxpayer does not physically produce books. Most of the books and materials it distributes are for the elementary school level.

> that the taxpayer account for the value of any articles it purchased with a resale certificate that it subsequently used rather than resold, and to remit retail sales tax on the articles. The taxpayer also relies upon RCW 82.08.130 and Rule 102 in contesting the assessment. The taxpayer contends its purchases of publications were exempt from retail sales tax under RCW 82.08.130 and Rule 102, the only tax the Department can assess on the taxpayer's subsequent use of the samples is use tax, and use tax does not apply to samples distributed outside Washington.

Relevant statutes and rules

RCW 82.08.020 imposes a retail sales tax on each retail sale in this state. RCW 82.04.050 defines the term "retail sale" for excise tax purposes. Subsection (1)(a) of RCW 82.04.050 excludes from the definition of "retail sale" a sale to a person who presents a resale certificate under RCW 82.04.470,[4] and who "[p]urchases for the purpose of resale as tangible personal property in the regular course of business without intervening use by such person."

There is no exemption from the sales tax for Washington residents who purchase articles in this state for their own use in Washington or outside Washington.

In general, the use tax applies upon the use within Washington, as a consumer, of any tangible personal property the sale or acquisition of which has not been subjected to the Washington retail sales tax. It supplements the retail sales tax by imposing a tax of like amount. WAC 458-20-178 (Rule 178); RCW 82.12.020; RCW 82.12.0252. Liability arises upon first use in this state. Washington use tax is not imposed on use outside Washington.

RCW 82.08.130, entitled "Resale certificate--Purchase and resale--Rules," provides tax alternatives to Washington buyers who engage in both consuming and reselling certain types of tangible personal property, as follows:

> If a buyer normally is engaged in both consuming and reselling certain types of articles of tangible personal property and is not able to determine at the time of purchase whether the particular property acquired will be consumed or resold, the buyer may use a resale certificate for the entire purchase if the buyer principally resells the articles according to the general nature of the buyer's business. The buyer shall account for the value of any articles purchased with a resale certificate that are used by the buyer and remit the sales tax on the articles to the department.
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> A buyer who pays a tax on all purchases and subsequently resells an article at retail, without intervening use by the buyer, shall collect the tax from the purchaser as otherwise provided by law and is entitled to a deduction on the buyer's tax return equal to the cost to the buyer of the property resold upon which retail sales tax has been paid. The deduction is allowed only if the taxpayer keeps and preserves records that show the

[4] RCW 82.04.470 sets out the information required in a resale certificate, and absolves a seller who has accepted a resale certificate in good faith from the burden of proving a sale was not a sale at retail.

> names of the persons from whom the articles were purchased, the date of the purchase, the type of articles, the amount of the purchase, and the tax that was paid. The department shall provide by rule for the refund or credit of retail sales tax paid by a buyer for purchases that are later sold at wholesale without intervening use by the buyer.

WAC 458-20-102 (Rule 102) is the administrative rule governing the issuance of resale certificates. It explains the conditions under which a buyer may furnish a resale certificate to a seller, provides tax reporting information to persons who purchase articles for resale and subsequently withdraw them from inventory for their own use, and provides information to persons who purchase types of articles for dual purposes (i.e., for both resale and consumption).

Regarding purchases that are for both consumption and resale (dual purposes), Rule 102 states, in pertinent part:

> (11) **Purchases for dual purposes.** A buyer normally engaged in both consuming and reselling certain types of tangible personal property, and not able 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 resale certificate for any part of the purchase. If the buyer principally resells the articles, the buyer may issue a resale certificate for the entire purchase. For the purposes of this subsection, the term "principally" means greater than fifty percent.
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> (a) **Deferred sales tax liability.** If the buyer gives a resale certificate for all purchases and thereafter consumes some of the articles purchased, the buyer must set up in his or her books of account the value of the article used and remit to the department of revenue the applicable deferred sales tax. The deferred sales tax liability should be reported under the use tax classification on the buyer's excise tax return.
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> (i) Buyers making purchases for dual purposes under the provisions of a resale certificate must remit deferred sales tax on all products or services they consume. If the buyer fails to make a good faith effort to remit this tax liability, the penalty for the misuse of resale certificate privileges may be assessed. This penalty will apply to the unremitted portion of the deferred sales tax liability.

RCW 82.04.190 defines the term “consumer” for excise tax purposes as “[a]ny person who purchases . . . any article of tangible personal property . . . other than for the purpose (a) of resale as tangible personal property in the regular course of business . . . .”

Determination No. 00-150

Determination No. 00-150 found that the taxpayer is normally engaged in both consuming (using as samples) and reselling the publications, and is not able to determine at the time of purchase whether particular items acquired will be consumed or resold. It concluded the taxpayer's circumstances bring it within the provisions of RCW 82.08.130 and Rule 102(11), and under Rule 102(11) the taxpayer was required to report and remit sales tax on any articles purchased with a resale certificate that it later consumed (distributed as samples).

Det. No. 00-150 concluded that RCW 82.08.130 does not provide an exemption from the retail sales tax, but rather permits certain taxpayers to defer determination of which items are subject to sales tax, and defer payment of sales tax until it is certain which items it acquired will not be resold. Det. No. 00-150 cited Det. No. 88-311A, 9 WTD 293 (1990), and Det. No. 89-309, 8 WTD 13 (1989), in support of that conclusion. Det. No. 00-150 concluded that RCW 82.08.130 does not change the fact that sales tax was due at the time of purchase, or convert the tax that is due, when the articles are used by the buyer, into use tax. It is a statute that, for the common convenience of the Department, vendors, and dual-purpose buyers, allows dual-purpose buyers to present resale certificates for all articles purchased, and defer payment of retail sales tax until the final status of the goods is known.

Petition for Reconsideration

The petition for reconsideration asserts that Det. No. 00-150 erred as follows: (1) "The determination erred in concluding that the assessment's assertion of 'deferred sales tax' could be upheld on the theory that retail sales tax was due." (2) "The published determinations relied upon in the determination are consistent with [Taxpayer's] position and are not precedent for assessing 'deferred sales tax' on items that were not purchased in retail sales and were not used in Washington." (3) "The determination asserts a policy that has not been previously articulated in published authorities, as a matter of taxpayer fairness adoption of new policy positions should not be enacted prospectively, not applied retroactively to audit periods predating the publication of written guidance to the taxpayer." Taxpayer argues each assertion.

ANALYSIS:

We will address each assertion made on reconsideration in turn.

1. Contention that Det. No. 00-150 erred in concluding that the assessment's assertion of "deferred sales tax" could be upheld on the theory that retail sale tax was due.

The taxpayer correctly asserts that Det. No. 00-150 accepts the taxpayer's basic premises that there are only two potentially applicable taxes, either retail sales tax or use tax, and "deferred sales tax" is not a separate type of tax.

The taxpayer further argues Det. No. 00-150 failed to analyze whether the sales to the taxpayer were "retail sales." It argues this issue is key, because under RCW 82.08.020 retail sales tax was due only if the sales to the taxpayer were "retail sales." It argues the sales were not "retail sales" as that term is defined in RCW 82.04.050(1). Its definitional argument is as follows (emphasis the taxpayer's):

> The term "retail sale" is defined by statute:
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> > "retail sale means every sale of tangible person property . . . to all persons . . . other than a sale to a person who presents a resale certificate . . . and who:
> > (a) Purchases for the purpose of resale as tangible personal property in the regular course of business without intervening use by such person;
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> RCW 82.04.050. (emphasis added). Thus, where the purchaser presents a resale certificate and purchases for the purpose of resale in the regular course of business, the transaction is not a retail sale and is not subject to sales tax.

The taxpayer argues Det. No. 00-150 erroneously added to the definition's exception for purchases for the purpose resale, a requirement that the items purchased for the purpose of resale actually be resold. It argues the Department has no authority to impose additional requirements beyond those contained in the express language of the statute.

We do not agree that Det. No. 00-150 failed to analyze whether the sales were "retail sales," nor do we agree that it added a requirement to RCW 82.04.050(1).

Det. No. 00-150 found that the sales of articles that that taxpayer later distributed as free samples were retail sales. It found that the taxpayer is normally engaged in both consuming (using as samples) and reselling the publications it purchases. The nature of its business requires that it withdraw some textbooks from inventory to send to prospective buyers as free samples. It knows, at the time of purchase, that it will be consuming rather than reselling some of the textbooks. The evidence shows that for 1996, 1997, and 1998, samples as a percentage of purchased inventory were 8.79%, 9.02%, and 18.88%, respectively. It is not able to determine at the time of purchase whether particular items purchased will be resold or consumed (used as samples). Thus, the taxpayer is not purchasing all of the items for the purpose of resale in the normal course of business. The purchases that are not for the purpose of resale are retail sales. RCW 82.04.050.

[1] RCW 82.08.130 and Rule 102(11) classify such sales as "retail sales." The statute and rule allow a buyer normally engaged in consuming and reselling certain types of tangible personal property, and not able to determine at the time of purchase whether the particular property purchased will be consumed or resold, to defer its sales tax liability on the items it later consumes. While the rule instructs the buyer to report the "deferred sales tax liability" under the use tax classification on its excise tax return, the rule does not classify the tax liability as use tax.

The definition of "retail sale" in RCW 82.04.050(1) does not tell us how to handle the situation where a buyer normally is engaged in both consuming and reselling certain types of articles, and is

unable to determine at the time of purchase whether the particular property will be consumed or sold. RCW 82.08.130 is a specific statute that addresses that situation. RCW 82.08.130 is applicable under the facts of this case.

The taxpayer argues on reconsideration that the textbooks are purchased solely for the purpose of reselling them in the regular course of business, not for a dual purpose, and that RCW 82.08.130 and Rule 102(11) are not applicable in its case. It cites the following definition of "purpose," from *The American Heritage College Dictionary*, Third Ed. 1997:

> 1. The object toward which one strives or for which something exists; an aim or goal; 2. A result or an effect that is intended or desired. See synonyms at intention.

The taxpayer argues there is no question its aim, goal, and intent are to resell the textbooks it purchases. It argues that although a small portion of the textbooks it purchases are not in fact resold, it is not the taxpayer's aim or goal, or intention, to give away free books.

The taxpayer's analysis would have us consider only the taxpayer's primary purpose in purchasing a category of articles. RCW 82.04.050(1)(a) does not require that treatment, and that treatment is contrary to RCW 82.08.130.

2. Contention that Det. No. 00-150 erred in that it relied on post-sale events to support a re-characterization of the tax imposed, and that whether a sale is a retail sale is determined at the time of the sale.

On reconsideration, the taxpayer argues that Det. No. 00-150 erred in that it imposed tax based on an event that occurred after the sale had been completed, the subsequent consumption of the articles for which the taxpayer had given a resale certificate. It argues that in Det. No. 00-150, both the incident of the tax and the measure of the tax result from a use tax analysis, not a retail sales tax analysis.

[2] Det. No. 00-150 did not impose tax based on an event that occurred after the sale. It applied RCW 82.08.130 and Rule 102(11), which allow a buyer to defer the retail sales tax that is due on the sale. The taxable event is the sale on which the buyer used the resale certificate. If Det. No. 00-150 is unclear as to the measure of the tax, we will attempt clarification. The measure of the tax is the [selling] price of the articles purchased with a resale certificate that are subsequently used by the buyer. RCW 82.08.130; Rule 102(11).

3. Contention that published determinations relied upon in Det. No. 00-150 are consistent with the taxpayer's position.

The taxpayer argues that Det. No. 88-311A, 9 WTD 293 (1990), a portion of which Det. No. 00-150 quoted and characterized as a correct interpretation of the statute and rule, addresses a different situation, and actually supports the taxpayer's position in the present case.

We do not read Det. No. 88-311A as supporting the taxpayer's position, which is that purchases of articles purchased with a resale certificate, which are later withdrawn from inventory and used (rather than resold) out of state, are not subject to either sales or use tax. Quite the contrary. Det. No. 88-311A concerned a buyer who fit the profile set out in RCW 82.08.130 and Rule 102(11). The articles purchased were materials the buyer used in printing insurance forms for its own use and for sale to affiliates, both inside and outside Washington. Det. No. 88-311A held:

> Accordingly, sales tax was not due at the time the printing materials were purchased by the taxpayer and used in the printing of insurance forms. Sales tax is due, however, on the materials which were not resold. To the extent that the taxpayer pays a use tax [to the other state] on the forms which it uses out of state, it should be entitled to a credit for the Washington sales tax paid on the materials used to print those forms.

The taxpayer argues with Det. No. 00-150's reliance on Det. No. 89-309, 8 WTD 13 (1989), in the determination's rejection of the taxpayer's suggestion that if the taxpayer gave a valid resale certificate, retail sales tax is never owed on the sale. The taxpayer appears to argue that Det. No. 89-309 only stands for the principle that if the buyer gave an improperly completed and executed resale certificate, the Department can assess the buyer deferred sales tax in a subsequent audit.

We agree that the issue in Det. No. 89-309 was different from the issue before us in the present appeal. Rather than rely on dictum in Det. No. 89-309, we will rely on the language of RCW 82.08.130. The statute allows a taxpayer who normally purchases for dual purposes, to use a resale certificate for the entire purchase, and to later remit "the sales tax" on articles it actually uses. The taxpayer's suggestion that the nature of the transaction is forever fixed with respect to the entire purchase if the resale certificate is complete and properly executed, is contrary to the plain language of the statute.

4. Contention that Det. No. 00-150 asserts a policy that has not been previously articulated, and as a matter of fairness the policy should be applied prospectively only.

The taxpayer argues:

> As discussed above, the determination's re-characterization of "deferred sales tax" as retail sales tax is incorrect. Even if there were merit to the determination's position, it implements a construction of the tax statutes that has not been articulated by the department in published authorities. Given the confusion that the department has long acknowledged flows from the practice of characterizing assessments as imposing "deferred sales tax" it is unfair to implement the policy position asserted in the determination retroactively to an audit period predating the department's promulgation of written guidelines. The best place to implement new construction is by administrative rule.

We do not agree that the rule applied in Det. No. 00-150 has not previously been articulated by the Department. It is clearly articulated in Rule 102(11).

We concede that Department personnel have not always used the term "deferred sales tax" properly in other contexts. The term has sometimes been used as though it were interchangeable with use tax. However, that has nothing to do with this appeal. RCW 82.08.130 clearly identifies the tax due in this context as "the sales tax." Rule 102(11) labels the tax due "deferred sales tax."[5] Det. No. 00-150 did not articulate a new rule. This is not a case of first impression requiring an interpretation of the statute or rule. The statute and rule are clear, and the Audit Division correctly applied them. We find no basis for limiting our decision in Det. No. 00-150 to future periods.

For the taxpayer's future guidance, we note the Audit Division recently issued Interim Audit Guideline 01.01, effective January 1, 2001, for the purpose of instructing Department personnel on the proper use of the term "deferred sales tax." We attach a copy of the interim guideline.

In sum, we find no error in Det. No. 00-150's conclusion that the assessment correctly assessed deferred sales tax on the taxpayer's purchases of articles it purchased with resale certificates and later distributed out of state as free samples. We hold the determination properly applied RCW 82.08.130 and Rule 102(11), which allow a buyer to use a resale certificate and defer payment of the retail sales tax, under specified circumstances. We find no basis for limiting the determination's holding to future reporting periods. We sustain Det. No. 00-150, and deny the petition for reconsideration.

DECISION AND DISPOSITION:

The taxpayer's petition for reconsideration is denied.

Dated this 20th day of June, 2001.

[5] The Auditor's Detail of Differences and Instructions to Taxpayer, dated September 30, 1999, also correctly labeled the tax due on purchases of publications later sent out of state as samples as "deferred sales tax."