

Cite as 5 WTD 379 (1988)

BEFORE THE INTERPRETATION AND APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition)	<u>D E T E R M I N A T I O N</u>
For Refund of)	
)	No. 88-202
)	
. . .)	Registration No. . . .
)	Tax Assessment No. . . .
)	

[1] **RULE 108:** B&O TAX -- SERVICE -- DEDUCTIONS -- DISCOUNTS -- SALES COMMISSIONS. Cash discounts from the selling price of tangible personal property may not be deducted from sales commissions taxed under the Service B&O category when calculating the measure of the sales agent's tax.

[2] **RULE 108, RULE 159, RCW 82.04.080, AND RCW 82.04.090:** B&O TAX -- SERVICE -- EXCLUSION -- SALES COMMISSIONS -- DISCOUNTS. Where a sales agent contracts with its principal for a full commission but does not receive such a commission because it allows a discount on the sale of its merchandise, only the actual or partial commission received by the agent will be subjected to Service B&O tax.

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.

TAXPAYER REPRESENTED BY: . . .

DATE OF HEARING: May 28, 1987

NATURE OF ACTION:

Petition for reduction of Service B&O tax on commissions based on discounted wholesale prices.

FACTS AND ISSUES:

Dressel, A.L.J. -- . . . (taxpayer) is a cooperative organization which sells orchard supplies on a wholesale basis. Its books and

records were examined by the Department of Revenue (Department) for the period January 1, 1982 through December 31, 1985. As a result the above-referenced tax assessment was issued which actually was a credit in the amount of \$ In this action the taxpayer is requesting an additional credit on the basis stated above.

The taxpayer sells fruit packing supplies directly as a wholesaler and also as an agent-representative of packing supply manufacturers. The matter at issue has to do with the latter activity. In a typical sales scenario, a fruit packing company will order packing supplies either through the taxpayer or directly from the manufacturer who is represented locally by the taxpayer. The supplies are sent directly from the manufacturer to the packer. The packer is invoiced by the taxpayer. That invoice will reflect a 2-1/2% discount from the suggested wholesale price. The taxpayer also allows an additional discount for prompt payment. The packer remits payment to the taxpayer. The taxpayer, in turn, sends 95% of the manufacturer's listed wholesale price to the manufacturer. Of the manufacturer's suggested wholesale price (list price), the taxpayer is entitled to a 5% selling commission for its services. In actuality, however, the taxpayer only realizes a 2-1/2% commission. This is because it has reduced the list price on the invoice by 2-1/2% but is obligated to pay 95% of the list price to the manufacturer. That only leaves 2-1/2% of the list price, which is the taxpayer's actual commission.

In the assessment the auditor has subjected 5% of the list price to Service B&O tax as the taxpayer's commission. According to the auditor's report, the taxpayer contends the measure of that tax should be cut in half as a sales discount pursuant to WAC 458-20-108 (Rule 108) which does allow bona fide discounts to be deducted from the selling price when determining business and occupation tax liability. The auditor has countered by saying that cash discounts are deductible but only for purposes of calculating the measure of Retailing or Wholesaling B&O tax. This taxpayer is an agent of the vendor of the merchandise and, as such, it earns a selling commission. That commission is subject to Service B&O tax rather than the Retailing or Wholesaling selling taxes, so, therefore, the discounts given the purchasers may not be deducted from the taxpayer's measure of tax.

Whether the taxpayer is subject to Service B&O tax on the whole 5% commission to which it is entitled according to its agreement with the manufacturer is the issue to be decided herein.

DISCUSSION:

[1] In this case the auditor is claiming that the discount deduction allowed under Rule 108 cannot be applied for purposes of calculating the Service B&O tax payable on the taxpayer's commissions. The taxpayer claims otherwise, saying that under Rule 108 if it first reports the 5% gross commission, it may deduct the

2-1/2% discount. Actually, both parties are right, and both parties are wrong.

First of all, the auditor is correct in saying that discounts may not be utilized to reduce Service B&O tax. Rule 108 reads in part:

DISCOUNTS. The *selling price* of a service or of an article of tangible personal property 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. (Emphasis added.)

The above-quoted portion of Rule 108 permits a discount deduction from the "selling price," not from a sales commission. Rule 108 is, therefore, of no aid to the taxpayer in its quest to have the measure of its B&O tax reduced.

[2] Not only has the taxpayer misplaced its reliance in this matter on Rule 108, but also the Department has done so as well. The taxpayer here has acted as a *selling agent* for manufacturers of fruit packing supplies. The administrative rule which discusses agency is WAC 458-20-159 (Rule 159). The rule states in part:

SERVICE AND OTHER BUSINESS ACTIVITIES. Every consignee, bailee, factor, agent or auctioneer who makes a sale in the name of the actual owner, as agent of the actual owner, or who purchases as agent of the actual buyer, is taxable under the service and other business activities classification upon the gross income derived from such business.

The Department has interpreted that paragraph to mean that salespeople are B&O taxable on their commissions. The reference in the rule to "gross income" is further explained in RCW 82.04.080 which reads:

"Gross income of the business" means the *value proceeding or accruing* by reason of the transaction of the business engaged in and includes gross proceeds of sales, compensation for the rendition of services, gains realized from trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, *commissions*, dividends, and other emoluments however designated, all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses. (Emphasis added.)

"Value proceeding or accruing" is defined in the immediately succeeding statute, RCW 82.04.090, as "the consideration, whether money, credits, rights, or other property expressed in terms of money, actually received or accrued" (Emphasis added.) The 2-1/2% discount afforded purchasing packers is never "actually received" by the taxpayer. The taxpayer's statement to the packer specifically excludes that amount. The packer's payment to the taxpayer, therefore, consists of 97.5% of the manufacturer's wholesale price.

RCW 82.04.090 also speaks in terms of money actually accrued to the taxpayer. While the taxpayer may be entitled to a 5% commission under the terms of its agreement with the manufacturers it represents, we do not believe that it can accurately be said that in the situations at hand a full 5% commission accrues to the taxpayer. If the taxpayer billed its customer at 100% of the list price, such a full commission could properly be said to have accrued to the taxpayer's benefit. But here, where the customer (packer) has been billed at 97-1/2% of the list price and, by agreement, the taxpayer owes 95% of the list price to the manufacturer, it is only a 2-1/2% commission, in actuality, that accrues to the benefit of the taxpayer.

We see no good reason to subject something other than the taxpayer's actual commission of 2-1/2% to the Service B&O tax. As explained above, this is the gross income that it derives from its business as a manufacturer's representative. The 2-1/2% figure is the value which actually proceeds or accrues to the taxpayer's benefit. The full 5% commission is never received by the taxpayer, nor is the taxpayer entitled to it when one considers the structure of these transactions.

It is our conclusion that only the 2-1/2% commission actually received is taxable. Henceforth, on its excise tax returns the taxpayer is directed to report only that amount. It should not first report 5% and then attempt to deduct half of that because it was never entitled to 5% in the first place. It is suspected that the taxpayer adopted that policy after mistakenly believing that Rule 108 applied to its situation.

DECISION AND DISPOSITION:

The taxpayer's petition is granted. An amended assessment will be issued reflecting the proper credit.

DATED this 27th day of April 1988.