

Cite as 9 WTD 149 (1990)

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

In the Matter of the Petition)	<u>D</u> <u>E</u> <u>T</u> <u>E</u> <u>R</u> <u>M</u> <u>I</u> <u>N</u> <u>A</u> <u>T</u> <u>I</u> <u>O</u>
<u>N</u>		
For Correction of Assessment)	
of)	No. 90-83
)	
. . .)	Registration No. . . .
)	. . ./Audit No. . . .
)	

- [1] **RULE 112 & RCW 82.04.450:** MANUFACTURING TAX -- VALUE OF THE PRODUCT -- TRANSFERRED OUT OF STATE PRIOR TO SALE -- COMPARABLE SALES -- COST. Where a manufactured product is transferred outside the state prior to sale, the value of the product shall correspond as nearly as possible to the gross proceeds from sales in this state of similar products of like quality and character, and in similar quantities by other taxpayers. Valuation based on the cost of production is appropriate only after the Department has made a finding that there are no "similar" or "comparable" sales.
- [2] **RULE 106:** B&O TAX -- CASUAL OR ISOLATED SALE -- SALE OF BUSINESS. The sale of unsold inventory as part of the liquidation of the entire business is not a casual or isolated sale and therefore subject to B&O taxes.
- [3] **RULE 19301 & RCW 82.04.440:** MATC -- GROSS RECEIPTS TAX -- DEFINITION -- TAX SEPARATELY STATED. Because as a matter of custom, the New Mexico gross receipts tax is separately stated from the sales price, it does not meet the definition of a "Gross receipts tax" under the RCW 82.04.440. [Accord: ETB 543.04.19301]

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 TELEPHONE CONFERENCE: . . .

NATURE OF ACTION:

The taxpayer protests additional taxes and interest assessed in an audit report.

FACTS:

Okimoto, A.L.J. -- [The taxpayer]'s books and records were examined for the period . . . through An audit resulted in additional taxes and interest owing in the amount of \$. . . and Assessment No. . . . was issued in that amount on

The taxpayer manufactures . . . devices at plants located both within and without the state of Washington. At its Washington plant the taxpayer primarily manufactures electronic [products]. A normal sales scenario of this product is as follows:

1. The [product] is manufactured at one of the taxpayer's plants in Washington.
2. 100% of the finished [products] are shipped from the plant to the taxpayer's distribution warehouse in . . . , Oregon.
3. The [products] are then stockpiled at the warehouse until a customer orders a [product] and other related equipment. At that time the [product] is packaged with various options, accessories, and additional equipment which may or may not have been manufactured at the taxpayer's Washington plant. The entire order is then consolidated and shipped to the taxpayer's customers at their business locations both within and without the state of Washington.
4. No additional manufacturing is done to the [products] after it leaves the Washington plant.
5. The [products] are not custom made or unique, but are generic in the sense that all products in an individual product line are basically the same.

The taxpayer protests the following items:

Future Instructions to Report Mfg tax computed on Selling Price

In the prior audit, the Department of Revenue's chief of audit instructed the taxpayer to report manufacturing tax on [the products] manufactured at its Washington plant and transferred to its Oregon distribution warehouse prior to sale based on the cost of producing these items at the time of transfer. In the current audit, the auditor rescinded those instructions and told the taxpayer to report those items based on the selling price of the manufactured items. The taxpayer argues as follows:

1. The taxpayer was instructed to use cost during the last audit and there has been no material change in the taxpayer's Washington operations during the interim.
2. It is not practical to report based on selling price because the taxpayer does not know what the selling price will be until an order is received. In addition, some sales apply charges or allow discounts to the entire order and it is difficult to apportion these discounts or charges to any given product.
3. There has been no material change in B&O tax laws since the last audit. Under RCW 82.04.450 where products are transported outside the state prior to sale, the value of the goods shall correspond as nearly as possible to the gross proceeds from sales of similar products of like quality and character, and in similar quantities by other taxpayers. The taxpayer further argues that since there are no comparable sales, Rule 112 allows them to report at cost.

B&O tax on Inventory sold as part of the sale of the entire business

In the audit report, Wholesaling B&O tax was assessed on amounts received by the taxpayer for plastics inventory sold as part of the sale of the entire plastics business to . . . in September of 1987. The taxpayer argues as follows:

1. The plastics inventory was not sold in the regular course of business because the nature of the transaction (ie. selling the entire business) is not a regular part of the taxpayer's business. The taxpayer argues that this sale was neither routine nor continuous.

2. The taxpayer argues that WAC 458-20-106, (Rule 106) is not applicable because it contemplates situations where the seller of the property is selling the property before and after the infrequent sale in question. The taxpayer distinguishes it from its own situation where the taxpayer is completely out of the business after the sale.

3. The auditor's interpretation results in a windfall to the state because it subjects the same inventory to two taxes, once by the taxpayer and again when it is sold by

Disallowance of Multiple Activities Tax Credit (MATC) on New Mexico Gross Receipts tax

In the audit report no MATC was allowed for selling taxes paid to New Mexico under its gross receipts tax. The taxpayer argues that this disallowance was in error. The taxpayer states that the New Mexico tax is a qualifying gross receipts tax because:

1. It is measured by the gross volume of the business.

2. The tax is imposed on the seller of the goods and not on the buyer. Although the New Mexico statutes allow the seller to separately state the tax and to pass it on to the customer, it does not require the customer to pay the tax. Therefore if the customer does not pay it, the seller must absorb the tax itself.

3. The taxpayer also argues that the purpose of the MATC is to prevent double taxation of persons engaged in interstate commerce, and that to disallow the credit merely because the tax is separately itemized defeats its purpose.

The taxpayer does concede that by custom, the New Mexico gross receipts tax is separately stated on the invoice. The taxpayer stated at the teleconference that this is done

primarily so that it is allowed to exclude from the measure of the New Mexico tax that portion of the sales price received that is attributable to the New Mexico tax.

ISSUES:

1. If a product is manufactured in Washington and transferred to a point outside the state prior to sale, upon what value is the manufacturing tax to be computed?
2. Does the Wholesaling B&O tax apply to the amount received for inventory items if they are sold as part of the liquidation of the entire business?
3. Is the New Mexico gross receipts tax a qualifying "gross receipts" tax for purposes of RCW 82.04.440?

DISCUSSION:

Future Instructions to Report Mfg tax computed on Selling Price

[1] RCW 82.04.240 imposes upon the privilege of manufacturing a product within this state, a B&O tax under the Manufacturing tax classification measured by the "value of the product." RCW 82.04.450(1) provides that the "value of the product" is to be determined by the "gross proceeds of sale" with three exceptions. These exceptions include:

(a) Where such products, including byproducts, are extracted or [1] manufactured for commercial or industrial use;

(b) Where such products, including byproducts, are shipped, transported or [2] transferred out of the state, or to another person, without prior sale or are [3] sold under circumstances such that the gross proceeds from the sale are not indicative of the true value of the subject matter of the sale.
(Emphasis and numbers, ours)

Because the taxpayer ships its products out of state without prior sale, it clearly falls within the above exception. We therefore agree that the measure of the manufacturing tax is not "gross proceeds of sale" of the product manufactured, but is determined by the second provision of RCW 82.04.450 which states:

...(2) In the above cases the value shall correspond as nearly as possible to the gross proceeds from sales in this state of similar products of like quality and character, and in similar quantities by other taxpayers, plus the amount of subsidies or bonuses ordinarily payable by the purchaser or by any third person with respect to the extraction, manufacture, or sale of such products:... The department of revenue shall prescribe uniform and equitable rules for the purpose of ascertaining such values. (Emphasis ours)

Rule 112, the lawfully promulgated regulation interpreting this statute states in part:

ALL OTHER CASES. The law provides that where products extracted or manufactured are...

(2) Transported out of the state, or to another person without prior sale;

... the value shall correspond as nearly as possible to the gross proceeds from other sales at comparable locations in this state of similar products of like quality and character, in similar quantities, under comparable conditions of sale, to comparable purchasers, and shall include subsidies and bonuses.

In the absence of sales of similar products as a guide to value, such value may be determined upon a cost basis.

Rule 112 clearly requires that before a cost basis valuation is used, the Department must make a finding that there are no similar or comparable sales. Although the taxpayer argues that this is the case, we are not convinced. The taxpayer readily concedes that its [products] are neither unique nor unusual but that it produces and sells many such [products] each year. It nevertheless contends that there are no comparable sales because other sales do not meet the like quality and character, and similar quantities test mandated by the statute. We believe that the taxpayer confuses the word "similar" with "identical." The statute does not contemplate identical sales, but merely requires similar sales upon which to base a reasonable estimate of the value of the products sold. To this extent we would consider the sales by other taxpayers of similar products within this state; sales by this taxpayer of similar products located within this state; or even some average sales price by this taxpayer of prior months

sales of similar products sold within this state; as constituting "sales in this state of similar products of like quality and character, and in similar quantities" within the meaning of the statute. Because the audit section has not addressed the question of comparable sales, this issue will be remanded for further investigation. If upon remand, the audit section finds that there are no comparable sales, cost valuation may be used.

[2] B&O tax on Inventory sold as part of the sale of the entire business

WAC 458-20-106, (Rule 106) states in part:

A casual or isolated sale is defined by RCW 82.04.040 as a sale made by a person who is not engaged in the business of selling the type of property involved. Any sales which are routine and continuous must be considered to be an integral part of the business operation and are not casual or isolated sales.

Furthermore, persons who hold themselves out to the public as making sales at retail or wholesale are deemed to be engaged in the business of selling, and sales made by them of the type of property which they hold themselves out as selling, are not casual or isolated sales even though such sales are not made frequently. (Emphasis ours)

Prior to the liquidation of the business, the taxpayer was engaged in the business of selling the type of property that was taxed by the auditor. Therefore under RCW 82.04.040 and Rule 106 the sale of that inventory, even though part of the liquidation of the business, is not a casual or isolated sale. As such it is fully subject to Washington B&O taxes. The taxpayer's petition is denied on this issue.

[3] Disallowance of MATC on New Mexico Gross Receipts tax

RCW 82.04.440(4) allows persons taxable under the Manufacturing tax classification a credit against those taxes for any "gross receipts taxes paid to another state with respect to the sales of the products so extracted or manufactured in this state." It further defines "Gross receipts tax" to mean a tax:

(i) Which is imposed on or measured by the gross volume of the business, in terms of gross receipts on in other terms, and in the determination of which the deductions allowed would not constitute the tax an income tax or value added tax: and

(ii) Which is also not, pursuant to law or custom, separately stated from the sales price. (Emphasis ours)

Because the New Mexico tax is separately stated from the sales price as a matter of custom, it does not meet the definition of a "Gross receipts tax" under the statute. We note that this interpretation is consistent with the recently published Excise Tax Bulletin, 543.04.19301 (. . .). Accordingly, the taxpayer's petition is denied on this issue.

DECISION AND DISPOSITION:

The taxpayer's petition is denied in part, and remanded in part. This matter will be remanded to the audit section for adjustments consistent with this determination.

DATED this 22nd day of February 1990.