

Cite as Det. No.15-0223, 35 WTD 217 (2016)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of)	<u>D E T E R M I N A T I O N</u>
Assessment of)	
)	No. 15-0223
)	
...)	Registration No. . . .
)	

[1] WAC 458-20-178; WAC 458 20 102; RCW 82.12.010: USE TAX – FREE SAMPLES – WINERY – WINE TASTING. A winery is liable for use tax on the value of wine samples it provides for free to the public.

[2] RCW 82.08.0273 – RETAIL SALES TAX – SALES TAX EXEMPTION FOR NONRESIDENTS – DOCUMENTATION & RETENTION – A winery that shows that it has complied with the documentation and retention requirements under RCW 82.08.0273(6)(a) is entitled to the sales tax exemption for qualified nonresidents with regard to its sales of wine to nonresidents for use outside of Washington State.

[3] RCW 82.32A.020: THIRD PARTY ADVICE – RELIANCE. The Department lacks authority under RCW 82.32A.020 to waive assessed taxes based on erroneous instructions from a third party. RCW 82.32A.020 provides authority to waive taxes only based upon reliance on specific, official written advice or written reporting instructions from the Department to the taxpayer.

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.

LaMarche, A.L.J. – A winery objects to the assessment of use tax on wine it provided free of charge for wine tasting and on items it gave free of charge to its wine-making class participants. The winery also protests the disallowance of the sales tax exemption it took for sales of wine to qualified nonresidents. The winery further asserts that tax should be waived because it relied on the erroneous tax advice and services of its accountant. We grant the petition in part and deny it in part.¹

¹ Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

ISSUES

1. Under RCW 82.12.010, WAC 458-20-178 (Rule 178), and WAC 458-20-102 (Rule 102), is use tax due on wine that Taxpayer provided for no charge to its customers for purposes of wine tasting?
2. Did the Department properly disallow the sales tax exemption on sales of wine to nonresidents where Taxpayer followed the documentation and retention requirements under RCW 82.08.0273?
3. . . .
4. In accordance with RCW 82.32A.020, does the Department have the authority to waive or cancel assessed taxes resulting from Taxpayer's reliance on the erroneous advice of its professional accountant?

FINDINGS OF FACT

[Taxpayer] manufactures and sells wine and wine-making materials, and conducts wine-making classes at its location in . . . , Washington.

The Audit Division (Audit) of the Department of Revenue (Department) conducted an audit of Taxpayer's business records for the period of January 1, 2010 through December 31, 2013 (Audit Period). Taxpayer did not pay use tax and/or deferred sales tax on wine it provided free of charge for wine tasting during the Audit Period, and did not pay use tax and/or deferred sales tax on items it gave to participants of wine-making classes. Audit based its assessment of use tax on the retail sales prices that Taxpayer provided for its products.

For each of its retail sales to nonresidents of Washington State, Taxpayer examined the purchaser's proof of nonresidence, determined whether the proof was acceptable (i.e., whether it had a photograph of the purchaser, showed a nonresidential address in a qualifying state, and was issued by the out-of-state jurisdiction in part for the purpose of showing residency in the out-of-state jurisdiction). Taxpayer maintained these records and was able to produce them for the audit.

Audit allowed the nonresident sales tax exemption claimed for sales of items other than wine; however, Audit disallowed the Qualified Non-Resident deduction Taxpayer claimed on sales of wine to nonresidents. Audit presumed that sales of single bottles of wine were non-exempt because purchasers were more likely to consume single bottles within the state, but stated that cases of wine qualified for the exemption because the purchasers were more likely to use the wine outside of the state.

Because Taxpayer was unable to differentiate between wine sales and sales of other tangible personal property, Audit estimated that 30 percent of Taxpayer's sales were sales of items other than wine, and allowed the exemption for those sales.

Because Taxpayer could not differentiate between sales of single bottles and sales of cases, Audit presumed that all wine sales were subject to retail sales tax as sales of single bottles, and on that basis, denied 70 percent of Taxpayer's claimed nonresident sales tax exemptions.

...

Taxpayer states that many of the errors and omissions that led to additional tax liability in the assessment were the result of Taxpayer's reliance on the erroneous advice of its professional accountant, and asks the Department for waiver or cancellation of assessed tax liability for that reason.

Audit issued an assessment on July 10, 2014 totaling \$² Taxpayer timely filed an appeal.

ANALYSIS

1. Use Tax on Wine Tastings

A use tax is imposed under RCW 82.12.020 for the privilege of using within this state, as a consumer, any article of tangible personal property acquired by the user in any manner. RCW 82.12.020. The use tax supplements the retail sales tax by imposing a tax of like amount upon the use within this state as a consumer of any article of tangible personal property purchased or otherwise acquired, where the user has not paid retail sales tax under chapter 82.08 RCW with respect to the property used. *See* WAC 458-20-178(1) (Rule 178).³ A "consumer" is defined under RCW 82.12.010(1) to include "...any person who distributes...any article of tangible personal property,...the primary purpose of which is to promote the sale of products...." *Id.* Liability for the use tax arises at the time the property is first put to use in this state. RCW 82.12.020; Rule 178(3). The tax is levied and collected on an amount equal to the value of the article used by the taxpayer. Rule 178(13); RCW 82.12.020(4); *see* Det. No. 13-0237R, 33 WTD 349 (2014).

RCW 82.12.010(7)(a) defines "value of the article used" as follows:

"Value of the article used" is the purchase price for the article of tangible personal property, the use of which is taxable under this chapter. . . . In case the article used is acquired by lease or by gift or is extracted, produced, or manufactured by the person using the same or is sold under conditions wherein the purchase price does not represent the true value thereof, the value of the article used is determined as nearly as possible according to the retail selling price at place of use of similar products of like quality and character under such rules as the department may prescribe.

² The assessment, Document No. . . . , issued on July 10, 2014, totaled \$. . . , which comprised \$. . . retail sales tax, \$. . . Retailing Business and Occupation (B&O) tax, \$. . . use tax and/or deferred sales tax, and a small business credit of \$

³The Department promulgated an updated version of Rule 178. The changes to the rule do not affect the outcome in this case. The citations in this determination are to the prior version of the rule.

Rule 178 essentially mirrors the statute, and it states in reference to the “value of the article used,”

[T]he value of the article used must be determined as nearly as possible according to the retail selling price, at the place of use, of similar products of like quality, quantity and character.

Rule 178(13) (emphasis added). *See* 33 WTD 349, *supra*.

Here, Taxpayer owes use tax on the wine that it manufactured and used in Washington State as free wine samples to its customers and on the items it gave to its wine-making class participants. Because Taxpayer provided the wine samples and items in the classes for free, no sales tax was paid on the wine or free items. Therefore, use tax liability arose when Taxpayer used wine that it had manufactured as free samples for its customers, and when it gave the free items to its class participants. RCW 82.12.020; Rule 178; *see* Det. No. 13-0234, 33 WTD 409 (2014). Here, where Taxpayer manufactured the wine it used, use tax was based on the value of the wine used, i.e., the “retail selling price, at the place of use, of similar products of like quality, quantity and character.” Rule 178(13); RCW 82.12.010(7)(a). Use tax on the items given to class participants is similarly based on their retail value. *Id.*

Taxpayer argues that use tax on the wine should be based on the wholesale or manufacturing cost, rather than the retail value. However, the statute clearly states that “the value of the article used is determined as nearly as possible according to the retail selling price at place of use of similar products of like quality and character” RCW 82.12.010(7)(a) (emphasis added). Here, for purposes of calculating use tax, Audit used the retail sales prices that Taxpayer provided for its own products of like quality and character. Therefore, Audit made the calculations in accordance with the statute and rule.⁴

Taxpayer further argues that it should not be taxed for free wine samples it provided using wine not in its inventory, which came from its owner’s private reserve of 200 gallons, which he is allowed annually for personal use tax-free under federal law.⁵ However, use tax is imposed under RCW 82.12.020 for the privilege of using within this state, as a consumer, “any article of tangible personal property acquired by the user in any manner.” *Id.* (Emphasis added.) Therefore, the broad scope of RCW 82.12.020 encompasses the wine reserved for personal use

⁴ *See also* Department of Revenue, Taxability of Wine Industry, Common sales tax exemptions (Taxability of Wine Industry), <http://dor.wa.gov/content/doingbusiness/business/types/industry/wine/wine-sales.aspx> (accessed August 6, 2015).

⁵ Taxpayer refers to 27 CFR 24.75, which states, “Any adult may, without payment of tax, produce wine for personal or family use and not for sale.” *Id.* However, 27 CFR 24.75 falls under 27 CFR Part 24, Subpart A, which sets forth federal regulations that “relate to the establishment and operation (including incidental activities) of wine premises and to the treatment and classification of wine.” 27 CFR 24.1. The authority for 27 CFR 24.75 derives from 26 U.S. Code § 5041, which imposes federal taxes on wines; the tax exemption Taxpayer refers to is for certain federal taxes on wine, and is not applicable to the use tax imposed in this state under RCW 82.12.020. In essence, Taxpayer is arguing that it is using for free samples the wine that its owner reserves for personal use. However, as we discuss, use tax is imposed on “any article of tangible personal property acquired by the user in any manner.” RCW 82.12.020.

of Taxpayer's owner, when the owner used that wine for the purpose of providing free samples to Taxpayer's customers. RCW 82.12.010(1); RCW 82.12.020; Rule 178.

Taxpayer also argues that it used the wine for advertising. However, use tax is also due on promotional material, which is defined as "any article of tangible personal property, except newspapers, displayed or distributed in the state of Washington for the primary purpose of promoting the sale of products or services. Examples of promotional material include, but are not limited to, . . . free gifts, or samples . . ." WAC 458-20-17803. A taxpayer who distributes or displays such promotional material is the "consumer" of the promotional material. RCW 82.12.010(1); *Activate, Inc. v. Dep't of Revenue*, 150 Wn. App. 807, 815-16, 209 P.3d 524 (2009) (seller who distributed "free" cellular phones to promote the sale of cellular phone service contracts was a "consumer" of those phones). Therefore, use tax was due on free wine that Taxpayer used as samples, or any items that Taxpayer gave to class participants for promotional purposes.

We conclude that Taxpayer has not shown that Audit erred when it assessed use tax on wine that Taxpayer provided to its customers free of charge, or on items Taxpayer gave to its wine-making class participants.

2. Sales of Wine to Nonresidents of Washington State

Washington State imposes retail sales tax on each retail sale in this state. RCW 82.08.020. Washington State also imposes a Retailing B&O tax on [the activity of engaging in making] retail sales in this state. RCW 82.04.250. RCW 82.04.050 defines "retail sale" to include sales of tangible personal property and sales of certain services.⁶

However, RCW 82.08.0273(1) provides a sales tax exemption for nonresidents of Washington State on purchases of tangible personal property, when:

- (a) The property is for use outside this state;
- (b) The purchaser is a bona fide resident of a province or territory of Canada or a state, territory, or possession of the United States, other than the state of Washington; and
 - (i) Such state, possession, territory, or province does not impose, or have imposed on its behalf, a generally applicable retail sales tax, use tax, value added tax, gross receipts tax on retailing activities, or similar generally applicable tax, of three percent or more; or
 - (ii) If imposing a tax described in (b)(i) of this subsection, provides an exemption for sales to Washington residents by reason of their residence; and
- (c) The purchaser agrees, when requested, to grant the department of revenue access to such records and other forms of verification at his or her place of residence to assure that such purchases are not first used substantially in the state of Washington.

⁶ . . .

RCW 82.08.0273(1)(a)-(c).

RCW 82.08.0273(3) requires that any person claiming exemption from retail sales tax under RCW 82.08.0273 must display proof of his or her current nonresident status, such as a valid driver's license for the jurisdiction claimed, and a valid identification card with a photograph of the purchaser issued by the out-of-state jurisdiction, which shows the purchaser's residential address and that the document was issued, in part, for the purpose of establishing purchaser's residency. A purchaser also has the option to provide proof of nonresidency to the seller using a properly completed exemption certificate authorized by the Department in compliance with the multistate Streamlined Sales and Use Tax Agreement. RCW 82.08.0273(3)(a)-(c).

RCW 82.08.0273(4)(a) states that the vendor is not required to make tax exempt retail sales to nonresidents, but that if vendors choose to do so, they "must examine the purchaser's proof of nonresidence, determine whether the proof is acceptable under [RCW 82.08.0273(3)], and maintain records for each nontaxable sale which must show the type of proof accepted, including any identification numbers where appropriate, and the expiration date, if any." *Id.*

Audit does not claim that Taxpayer failed to obtain and maintain the records required under the statute, but argues that sales of single bottles of wine are presumptively not sales of property "for use outside this state" as required by RCW 82.08.0273(1)(a). Under the specific facts here, we disagree with the premise that Taxpayer's single bottles are presumptively sold for in-state consumption. As Taxpayer asserts in its petition, each bottle of wine was sealed with a cork and shrink-wrapped, and was sold without a corkscrew or other means to open the bottle. We take notice of Taxpayer's assertion that wine has a shelf-life considerably longer than the time it takes to reach the Washington border, and that some wine is purchased with the intent to let it age for some time prior to consumption. We also note that it is not uncommon to purchase wine as a gift or to purchase bottles of a local wine as a souvenir of a visit to that locale. Moreover, Taxpayer's location right off of a major interstate highway relatively close to the state border supports Taxpayer's assertion that its sales of wine were largely to non-residents whose purchases were not for the purpose of in-state consumption.

The Department's industry guide entitled "Taxability of Wine Industry" contemplates a retail sales tax exemption on wine sold to qualifying nonresidents, and states, "Sales of wine and other tangible goods to residents of certain qualifying states, US possessions, or Canadian provinces *for use outside the state* may be exempt from sales tax."⁷ The on-line materials make no distinction between sales of cases or bottles, and do not discuss that single bottle sales are presumptively for use within the state and, are therefore, ineligible for the tax exemption. The site also refers the user to ETA 3054.2014 which was issued on November 4, 2014. (During the Audit Period, the previous version of the advisory, ETA 3054.2011, issued August 12, 2011, was in effect; however, there is no difference in the language pertinent to our discussion here.) ETA 3054.2011 addresses exempt sales to certain nonresidents, pursuant to RCW 82.08.0273. Like the Department's website, the ETA emphasizes that the tax exemption only applies to sales to qualifying nonresidents of tangible personal property for use *outside this state*. *Id.* Thus:

⁷ Taxability of Wine Industry, see note 4.

The exemption also does *not* apply to sales of articles substantially used or consumed within Washington. This includes, but is not limited to, sales of:

- Meals or refreshments prepared for immediate consumption.
- Articles to persons in the military stationed within Washington.
- Articles to nonresident students attending schools in this state.
- Articles to any other nonresident temporarily residing in Washington.

Id. We do not agree that Taxpayer's sales of single bottles of wine are comparable to sales of meals or refreshments prepared for immediate consumption, or the other examples listed, where the nature of the goods or circumstances of the buyer make it extremely likely that the items will be used or consumed within Washington.⁸ To the contrary, Audit's assumption that qualifying nonresidents purchasing sealed single bottles of wine in a gift store at a Washington winery intend to consume the wine in Washington is not supported by the objective evidence in this case.

We conclude that Taxpayer has met its burden under RCW 82.08.0273(6)(a), and we remand to the operating division to make adjustments to the assessment in accordance with this determination.

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3. Reliance on erroneous statements of a third party.

RCW 82.32A.020 provides the Department the authority to waive tax only based upon reliance on specific, official written advice or written reporting instructions from the Department to that taxpayer. *See* Det. No. 02-0039, 21 WTD 318 (2002); Det. No. 00-001, 19 WTD 681 (2000); *see also* Det. No. 87-130, 3 WTD 59 (1987); Det. No. 96-114, 16 WTD 188 (1996); Det. No. 92-004, 11 WTD 551 (1992); ETA 3065.2009.

Here, Taxpayer has not shown that it relied on specific, official written advice or written reporting instructions from the Department. RCW 82.32A.020. Here, the tax reporting advice, instructions, and tax services Taxpayer received were not from the Department but from a third party individual. Reliance on written or oral reporting instructions given by a third party is not a circumstance under which the Department has authority to cancel an assessment for taxes due. RCW 82.32A.020; Det. No. 14-0201, 33 WTD 612 (2014).

Taxpayers have the duty to know their own reporting obligations, to ensure the accuracy of their returns, and when they are uncertain, to seek instructions from the Department. RCW

⁸ *See also* Det. No. 14-0325, [34 WTD 225 (2015),] involving sales to nonresident students by a Washington community college bookstore, where we concluded, "that it is reasonable to conclude that nonresident students attending school in Washington substantially use their textbooks and other course materials in Washington, and the sale of such articles are, therefore, subject to retail sales tax."

82.32A.030. The Washington tax system is largely based on voluntary compliance and taxpayers have a responsibility to inform themselves about applicable laws. RCW 82.32A.005. Because of the nature of Washington's tax system, the burden of becoming informed about tax liability also falls upon the taxpayer, and it is the taxpayer who bears the consequences of a failure to be correctly informed. Det. No. 01-165R, 22 WTD 11 (2003).

In conclusion, while we understand that Taxpayer relied on an individual it viewed as a tax expert, we do not have authority on that basis to grant relief under RCW 82.32A.020.

DECISION AND DISPOSITION

Taxpayer's petition is granted in part and denied in part.

We are remanding the case to the Audit Division (Operating Division) for adjustment to the assessment in regard to the Qualified Nonresident Sales deduction.

Dated this 18th day of August, 2015.