Cite as Det. No. 17-0233, 38 WTD 52 (2019)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of Assessment of	)	D E T E R M I N A T I O N
	)	No. 17-0233
. . .	)	Registration No. . . .

RCW 82.04.4283; WAC 458-20-108: CASH AND TRADE DISCOUNT DEDUCTION. Taxpayer is not entitled to a cash and trade discount deduction for amounts of "off invoice" discounts by which Taxpayer reduced the sale price of its products for its retailer customers where Taxpayer failed to prove that the retailer customers were not required to do anything in exchange for receiving the "off invoice" discounts.

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.

Yonker, T.R.O. – A distributor (Taxpayer) that sells pre-packaged snacks to retailer customers protests the disallowance of cash and trade discount deductions Taxpayer originally claimed for "off invoice" discounts that it gave to its retailer customers when selling products to such customers. Taxpayer argues that the discounts were given to its customers without the expectation of anything in return from those customers. We deny the petition.[1]

ISSUE

Under RCW 82.04.4283 and WAC 458-20-108, has Taxpayer proven that it is entitled to a cash and trade discount deduction for amounts of "off invoice" discounts by which Taxpayer reduced the sale price of its products for some of its retailer customers?

FINDINGS OF FACT

. . . (Taxpayer) is [an out-of-state] partnership that makes wholesale sales of snack products to retailers from various distribution outlets located in Washington. Typically, Taxpayer enters into contracts with retailers in which such retailers agree to purchase Taxpayer's products in exchange for such retailers agreeing to resell such products to consumers. As part of its contracts with retailers, Taxpayer often agreed to pay the retailer certain "rebates" that are not at issue here. In

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

addition to the "rebates," Taxpayer represented that it often gave a price discount off the selling price of its products to the retailer, called "off invoice" discounts.

Once Taxpayer had executed contracts with its retailer customers, Taxpayer's representatives then made regular visits to those retailers and delivered products as needed. When the representatives delivered such products, Taxpayer would issue a "ticket," or invoice, to the retailer customer that would include the gross sale price of each product sold, and an "off invoice" discount, if applicable, was subtracted from the sale price of each discounted product. In other words, Taxpayer gave its retailer customers the discounts up front at the time Taxpayer sold the products to those retailers.

Throughout the relevant time period, Taxpayer reported its gross sales of its products to Washington retailers under the wholesaling business and occupation (B&O) tax classification. Taxpayer also claimed a deduction for the amount of discount given for each product it sold to its contracted retailers in Washington.

In 2013, the Department's Audit Division commenced a review of Taxpayer's books and records for the time period of January 1, 2009, through December 31, 2012 (audit period). As part of its review, the Audit Division made a number of findings, including finding that Taxpayer had not adequately supported its claimed deductions for the discounts given to Taxpayer's retailer customers.

On October 21, 2016, as a result of the Audit Division's review, the Department issued a tax assessment for $ . . . , which included $ . . . in wholesaling B&O tax, $ . . . in use tax and/or deferred sales tax, and $ . . . in interest. On April 19, 2017, after reviewing additional records submitted by Taxpayer, the Audit Division issued a post assessment adjustment (PAA), reducing the amount of use tax due on the tax assessment to $ . . . , although the total amount due on the PAA increased to $ . . . as a result of additional interest accrued. Taxpayer subsequently sought review of only the wholesaling B&O tax amount, and the associated interest. The tax assessment, as adjusted by the PAA, remains unpaid.

On review, Taxpayer produced a number of documents, including a contract it entered into on February 10, 2012, with . . . (Customer A), which operates convenience stores. In that contract, Taxpayer agreed to pay Customer A "the 'Rebate Pricing' described on Schedule B attached" to the contract. Schedule B, in turn, states that Taxpayer "[a]grees to" (1) take a . . . discount off "all Purchases everyday as off invoice," (2) give a "Space Rebate" of . . . of "ticket sales" paid quarterly to each "division," and (3) an additional . . . space rebate off "ticket sales" paid quarterly to each "division" that participates in at least three of the "menu choices."

In exchange for all of those discounts and rebates, Schedule B states that Customer A "[a]grees to" (1) place merchandise in specific display arrangements and in certain distances from the cash register, the "cold vault," or other store features in the stores, (2) participate in various promotions throughout the year, and (3) complete at least three "menu choices" of various merchandise placement strategies "to assist in driving sales and profits" if Customer A opts to earn the additional . . . space rebate.[2] Schedule B states that "[a]ll funds are conditioned upon actual performance and

[2] Regarding merchandise placement, Schedule B required the following:

- . . . position no further than 6 ft from the register

verification in accordance with your Customer Merchandising Agreement with [Taxpayer]. Proof of Performance is required for distribution of funds." Taxpayer produced invoices issued to Customer A that indicate Taxpayer reduced the price of the products it sold to Customer A by . . . percent.

Taxpayer also produced three additional sample "Merchandising Program Descriptions and General Information" forms it entered into with other retailer customers that generally describe various "rebate" programs such as "Flex," "Space," "Growth," and "Other," in which those retailer customers opted to participate. Each of those additional forms contain language stating that the various rebates are paid quarterly, semiannually, or annually, depending on the specific terms of each retailer customer's "Customer Merchandising Agreement." Taxpayer produced the corresponding "Customer Merchandising Agreements," which each reference the various "rebate" programs in which each retailer customer chose to participate. None of those additional documents include any terms stating that Taxpayer agreed to give those retailer customers "off invoice" discounts like the terms contained in Schedule B of Taxpayer's contract with Customer A.

On review, Taxpayer represented that in cases other than large national retailer customers like Customer A, the "off invoice" discounts are not part of a written contract. Instead, the "off invoice" discounts are given to retailer customers for a variety of sales promotions, such as "buy one, get one," at various discount rates depending on the promotion.[3] In such situations, Taxpayer represented that, even in the absence of a contractual agreement, retailer customers who purchase products subject to the various discounts agree to resell those products in compliance with the terms of the promotion. We requested, but did not receive, a description of the various promotions offered during the audit period, the terms of those promotions, and the associated "off invoice" discount percentages.

ANALYSIS

Every person in the business of making "sales at wholesale" within Washington generally owes wholesaling B&O tax equal to the gross proceeds of sales of the business, multiplied by the applicable tax rate. RCW 82.04.270. "Gross proceeds of sales" is defined in RCW 82.04.070 as follows:

- . . . end cap facing cold vault. Or shop around like in the Midwest.
- . . . This unit will hold Pre-packed weekender, shipper, and monthly take home promotion.
- Minimum of 75% of the gondola. (Up to 95% space to sales)
- Authorize all new items sold by [Taxpayer] while maintaining current authorizations
- Prepacked weekenders/Shippers authorized for all stores. (75% stores to participate)
- Complete . . . Promotion in all Divisions
- Division . . . Program 2 per year in all Divisions
- All Divisions will participate under this Program

Regarding promotions, Schedule B stated that "[p]romotional activities require participation in monthly take-home promotions calendar mutually agreed with [Taxpayer]." Schedule B also included ten separate "menu choices" from which Customer A could choose three or more. The menu choices generally appear to relate to additional product placement strategies within the store, and other promotional programs that are not defined in detail.

[3] Taxpayer represented that the "buy one, get one" promotion would require a retailer customer to sell the products purchased from Taxpayer consistent with that phrase, so that a consumer would purchase one snack product and receive a second one free.

> [T]he value proceeding or accruing from the sale of tangible personal property, . . . and or/for other services rendered, without any deduction on account of the cost of property sold, the cost of materials used, labor costs, interest, discount paid, delivery costs, taxes, or any other expense whatsoever paid or accrued . . . .

RCW 82.04.090, in turn, defines "value proceeding or accruing" as "the **consideration**, whether money, credits, rights, or other property expressed in terms of money actually received or accrued." (Emphasis added). Thus, generally, a taxpayer is liable for wholesaling B&O tax on the consideration, or full selling price, of the property sold, unless some specific deduction or exemption applies. The taxpayer has the burden of showing qualification for any tax deduction, exemption or credit. *Budget Rent-A-Car of Wash.-Oregon, Inc. v. Dep't of Revenue*, 81 Wn.2d 171, 174-175, 500 P.2d 764 (1972); *Group Health Co-Op v. Tax Comm'n*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967).

Here, Taxpayer argues that it is entitled to claim a cash and trade discount deduction to reduce its taxable gross proceeds of sales. RCW 82.04.4283 states that, "[i]n computing tax there may be deducted from the measure of tax the amount of cash discount actually taken by the purchaser." RCW 82.04.160 defines "cash discount" as "a deduction from the invoice price of goods or charge for services which is allowed if the bill is paid on or before a specified date." WAC 458-20-108 (Rule 108) further explains the deduction for cash discounts:

> (7) **Bona fide discounts.** When a sale is made subject to cash or trade discount, the gross proceeds actually derived from the selling price are determined by the transaction as finally completed. A sale is made subject to a discount when the sales price is reduced under terms known to the buyer and seller at the time of the sale, and the price reduction occurs at the time of the sale or within a time agreed and understood by the parties at the time of the sale.
>
> The selling price or sales price of a service or article of tangible personal property does not include bona fide discounts actually taken by the buyer. The amount of bona fide discounts may be deducted only if the amount has been included in the gross amount reported.

Therefore, only "bona fide" discounts are deducted from the selling price. The Department has long recognized that discounts are "bona fide" when they are "reduced prices" and the buyer is not required to do anything in return for that reduced price. *See* Det. No. 14-0159, 34 WTD 257 (2015); Det. No. 05-0142, 26 WTD 256 (2007); Det. No. 83-180, 11 WTD 5 (1983).

[. . .] Essentially, if a seller expects something in return for a discount, the amount of the discount constitutes a business cost as opposed to a bona fide discount because the seller is receiving something of value to the business for giving up that portion of the selling price. [*See Steven Klein, Inc. v. Dep't of Revenue*, 183 Wn.2d 889, 901, 357 P.3d 59 (2015) (auto manufacturer payments to auto dealers not bona fide discounts off wholesale price where dealer must sell specific cars at specific times to earn the payment).]

Here, Taxpayer claims the "off invoice" discounts that it took off the price of its products at the time of sale to its retailer customers constitute 'bona fide" discounts, and are, therefore, deductible

from the gross sales of its products. We conclude, however, that Taxpayer has failed to meet its burden of proving that the retailer customers were not required to do anything in exchange for receiving the "off invoice" discounts.

The only documentation in the record specifically addressing the "off invoice" discounts relates to Customer A. Schedule B of the contract with Customer A identifies a number of obligations with which Customer A must comply to get either the "off invoice" discounts or any of the other rebates. Specifically, Schedule B states that Customer A "[a]grees to" employ certain merchandising, displaying, and marketing strategies that were clearly aimed at maximizing the resale of Taxpayer's products by Customer A to its consumers. In exchange, Taxpayer "[a]grees to" give the . . . "off invoice" discount. To the extent that Taxpayer suggests the strategies Customer A agreed to employ were required only for the "Space Rebate," we find no distinction in Schedule B between Customer A's performance requirements for obtaining the "off invoice" discount and its performance for obtaining the "Space Rebate." Simply put, Schedule B appears to require Customer A to perform certain tasks to obtain the "off invoice" discount.

Taxpayer has offered no other evidence tending to prove that it gave the "off invoice" discount to Customer A without expectation that Customer A comply with the clear terms of Schedule B. Further, Taxpayer has offered no evidence at all regarding the "off invoice" discounts it gave to its other retailer customers. The other sample documents contained no mention of "off invoice" discounts. Indeed, on review, Taxpayer represented that there were no written contractual terms governing these discounts for its other retailer customers. At the same time, Taxpayer represented that there were promotional obligations that a retailer customer was expected to abide by in order to take advantage of the "off invoice" discounts. Even in the absence of a written contract governing the "off invoice" discounts, Taxpayer's own representations are consistent with a discount given in return for some action on the part of the retailer customer. . . .

Based on the record before us, we conclude that Taxpayer has failed to meet its burden to prove that the "off invoice" discounts constitute "bona fide" discounts eligible for deduction from gross sales under RCW 82.04.4283 and Rule 108. Accordingly, we affirm the Audit Division's disallowance of the deductions originally claimed by Taxpayer.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 14th day of September, 2017.