

Cite as Det. No. 19-0005, 40 WTD 100 (2021)

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

In the Matter of the Petition for Correction of) D E T E R M I N A T I O N
Assessment of)
 No. 19-0005
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 Registration No. . . .
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)

RULE 108; RCW 82.08.010: BONA FIDE DISCOUNT DEDUCTION. Taxpayer is not entitled to a bona fide discount deduction for amounts it receives from special price agreement rebate policies intended to promote inventory purchases since the special price agreement rebates are not part of a single transaction with the purchase of that inventory by third parties.

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 THE CASE

Gabriella Herkert, T.R.O. – An out-of-state manufacturer of industrial enclosure and cooling solution products protests inclusion of special price agreement rebates in its measure of selling price subject to wholesaling business and occupation (B&O) tax. Taxpayer contends that the special price agreement rebates are bona fide discounts excluded from the definition of selling price and, therefore, the measure of gross proceeds subject to B&O tax. We . . . deny Taxpayer's petition . . .¹

ISSUE

Under RCW 82.08.010(1)(b), and WAC 458-20-108 are special price agreement rebates bona fide discounts excluded from the definition of "selling price" and therefore not part of the measure of gross proceeds subject to wholesaling B&O tax?

FINDINGS OF FACT

A manufacturer of industrial enclosure and cooling solution products . . . (Taxpayer), headquartered [out-of-state], sells its products to distributors throughout the country including in Washington. Taxpayer provides inventory pricing adjustments to its distributors. Taxpayer issued a . . . rebate policy controlling the inventory pricing adjustments. The rebate policy is written and

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

controlled solely by Taxpayer and may be changed at any time without the approval or participation of distributors. Taxpayer may alter the amount of the rebate at any time. Any change to the amount of the rebate means that Taxpayer's products held by distributors in inventory are no longer subject to the rebate amounts included in the . . . rebate policy at the time distributors purchased such inventory from Taxpayer.

Taxpayer contends that the [rebate policy] is designed to allow it to adjust distributor pricing when necessary to account for subsequent competitive market conditions.² Taxpayer concedes that while in most cases the ultimate amount of the discount is not determined until the distributor subsequently sells to its customers, the existence of the [rebate policy] is known and relied upon by distributors at the time of purchase from Taxpayer.³ Taxpayer also concedes that while it may make payments under the [rebate policy] to distributors, those distributors are free to price their products independently. As a result, Taxpayer is not actually adjusting distributor pricing by making payments under the [rebate policy].

....

Distributors must provide information and documentation to Taxpayer to receive payment. Distributors have no other obligation to perform services, including marketing services, to qualify for the [rebate] payments. Taxpayer reviews rebate requests to determine if they "align with the product scope, timing, and other parameters of the [specific rebate policy]."⁴ Taxpayer's distributors are entitled to the [rebate] amount included in Taxpayer's [rebate policy] program on the date that the distributor sells to the end user.⁵

Distributors hold inventory of Taxpayer's products for sale to third parties For products held in inventory, the distributor does not know the amount of the [rebate] for the products until it sells to an end user at a later date. The [rebate] amount listed by Taxpayer on the date a distributor purchases for inventory can change before the distributor sells to a third party Taxpayer pays the rebate directly to distributors.

The Department of Revenue's Audit Division (Audit) reviewed Taxpayer's books and records from January 1, 2013, through December 31, 2016. The Department issued an assessment to Taxpayer in the amount of \$⁶ The assessment is the result of Audit not treating payments made under Taxpayer's [rebate policy] as bona fide discounts from the sales price offered to distributors purchasing products from Taxpayer. Taxpayer timely requested review of the assessment.

² Petition, p. 4.

³ *Id.*

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⁵ *Id.*

⁶ Document No. . . . includes \$. . . in wholesaling B&O tax, \$. . . in interest, and \$. . . in a substantial underpayment penalty.

ANALYSIS

Washington State imposes a B&O tax upon every person that has a substantial nexus with this state for the act or privilege of engaging in business activities. RCW 82.04.220(1). Washington imposes the B&O tax on various tax classifications, including making retail sales under RCW 82.04.250 and wholesale sales under RCW 82.04.270. A “wholesale sale” is defined as “any sale, which is not a sale at retail.” RCW 82.04.060(1). The wholesaling B&O tax is imposed on the “gross proceeds of sales.” RCW 82.04.270.

“Gross proceeds of sales” is defined as the following:

[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 82.04.070.

RCW 82.08.010(1)(b) exclude[s] from the [definition of] selling price any “[d]iscounts, including cash, term, or coupons that are not reimbursed by a third party that are allowed by a seller and taken by a purchaser on a sale.”

WAC 458-20-108 (Rule 108) is the Department’s administrative rule that addresses discounts and allows for a B&O tax deduction for bona fide discounts. Rule 108 explains the criteria for bona fide discounts, as follows:

(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. . . .

(Emphasis provided.) Rule 108(7) clarifies that a “bona fide discount” is one whose terms are contemplated at the time of sale, and applies at time of sale or within a time as determined by both parties. Therefore, under Rule 108, in order to be a bona fide discount not included in gross proceeds from sales, the discount must be part of a single transaction.

We note that, in general, “[t]axation is the rule and exemption is the exception.” *Budget Rent-A-Car*, 81 Wn.2d 171, 174, 500 P.2d 764 (1972). “The taxpayer has the burden of establishing eligibility for an exemption.” *Stroh Brewing Co. v. Dep’t of Revenue*, 104 Wash. App. 235, 240, 15 P.3d 692 (2001).

“Selling price” or “sales price” does not include discounts, including cash, term, or coupons that are not reimbursed by a third party that are allowed by a seller and taken by a purchaser on a sale.

RCW 82.08.010(1)(b). Taxpayer asserts that the [rebate policy] payments are bona fide discounts that are not subject to B&O tax pursuant to RCW 82.08.010(1)(b) and Rule 108(7). We disagree.

For any discount to be deductible from the measure of B&O tax pursuant to Rule 108, whether it is called a cash discount, trade discount, volume discount, or bears another name, the underlying sale must have the characteristics of a single transaction, i.e., a contract of sale that is expressly made “subject to” the discount at the time of sale. *See Rule 108(7).* Rule 108(7) indicates that for purposes of calculating the gross proceeds of a sale, we look to the transaction when it is “finally completed.” This implies that a bona fide discount is a discount that is part of an original contract of sale whose terms are contemplated by both parties at the time of sale, and one that takes effect at the time of sale, or at a different time contemplated and specified by both parties.

The Washington State Supreme Court in *Steven Klein, Inc. v. Dep’t of Revenue*, 183 Wn.2d 889, 357 P.3d 59 (2015) considered bona fide discounts. In *Klein*, the Court held that “dealer cash,” which is an incentive program where manufacturers make payments to car dealerships on each car sale made during a specified period of time, does not constitute a bona fide discount. *Id.* at 901. The Court indicated that dealer cash payments are not bona fide discounts to the wholesale purchase price of vehicles because Klein did not purchase the vehicles from the manufacturer **subject to** the dealer cash savings. *Id.* The Court explained its rationale as follows:

[D]ealer cash payments are not necessarily quantified or even knowable at the time Klein Honda purchases vehicles from Honda, and the invoices for cars do not list amounts for dealer cash savings. Also, Klein Honda is not automatically entitled to dealer cash when it purchases vehicles at wholesale; rather, Klein Honda must earn dealer cash by accepting Honda’s conditional offer and complying with various terms and conditions. Klein Honda could sell a car eligible for dealer cash but not earn dealer cash depending on the timing and the manner in which it sold the car.

Id.

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Like the taxpayer in *Klein*, Taxpayer has not demonstrated that most of its sales to distributors were “subject to” the later payments from the [rebate policy]. Taxpayer conceded in its petition that in most cases the ultimate amount of the discount/rebate is not determined until the distributor subsequently sells to its customers. Like the dealer cash in *Klein*, [rebate policy] payments to distributors “are not necessarily quantified or even knowable” at the time distributors purchase products from Taxpayer. *See Klein*, 183 Wn.2d at 901. As such, the selling price does not include the [rebate policy] payments made at a later time as bona fide discounts.

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[W]e deny Taxpayer’s petition.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 8th day of January 2019.