

Cite as Det. No. 13-0050, 34 WTD 443 (2015)

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. 13-0050
	)	
...	)	Registration No. ...
	)	

[1] RCW 82.64.050(1); Rule 255(4) – WHOLESALE TO COLLECT CARBONATED BEVERAGE SYRUP TAX FROM BUYER. The taxpayer is liable for the syrup tax for syrup sales made to the federal government regardless of whether it is obligated to collect from the federal government.

[2] RCW 82.64.030(2); Rule 255(5) - CARBONATED BEVERAGE SYRUP TAX EXEMPTION FOR SYRUP TRANSFERRED OUTSIDE THE STATE FOR USE OUTSIDE THE STATE. The Certificate of Tax Exempt Export Carbonated Beverage Syrup, or other certificate with substantially the same information required under RCW 82.64.030(2) and Rule 255(5), must contain the type and volume of the syrup of the taxpayer’s customers purchased in order for the taxpayer to claim the exemption.

[3] RCW 82.04.080(1); RCW 82.04.4283; RCW 82.04.160; Rule 108(5) – BONA FIDE DISCOUNTS. When the taxpayer provides to its customer an amount off of the wholesale price of the products in exchange for the customer to advertise the taxpayer’s products in specific orders and specific quantity, the amount is not a bona fide discount. The amount represents the taxpayer’s cost of doing business and the taxpayer may not exclude the amount from the measure of its gross income.

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.

Callahan, A.L.J. – A syrup manufacturer (Taxpayer) protests a syrup tax assessment alleging that it is not required to collect the syrup tax for sales to the federal government . . . in Washington. Taxpayer also contests the wholesaling business and occupation (B&O) tax assessment arguing that it should be allowed to deduct from its gross income as volume discounts certain payments to its customers. We deny . . . the petition.<sup>1</sup>

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

## ISSUES

1. Is Taxpayer liable for the syrup tax, under RCW 82.64.050 and WAC 458-20-255 (Rule 255), when it failed to collect the syrup tax from the federal government. . .
2. Has Taxpayer produced documents to establish some of the syrup sales are exempt from the syrup tax, under RCW 82.64.030(2) and WAC 458-20-255 (Rule 255), because the syrup was transferred to a point outside Washington for use outside the state?
3. Can Taxpayer exclude payments or allowances to its customers for sales of its products from its “gross income of the business,” under RCW 82.04.080, as cash discounts under RCW 82.04.4283 and WAC 458-20-108(5)(c) (Rule 108)?

## FINDINGS OF FACT

Taxpayer manufactures and makes wholesale and retail sales of syrup and other products. Taxpayer has bottling plants located in . . . [Washington]. The Department of Revenue’s (the Department’s) Audit Division examined Taxpayer’s books and records for the period of . . . (the audit period). On February 24, 2011, Audit issued assessment number . . . <sup>2</sup> and assessment number . . . <sup>3</sup> The original assessed amount of assessment number . . . was \$ . . . . Audit issued a post assessment adjustment (PAA) for assessment number . . . based on the additional information Taxpayer subsequently submitted. The PAA for assessment number . . . was in the amount of \$ . . . , which consisted of retail sales tax of \$ . . . , retailing business and occupation (B&O) tax of \$ . . . , wholesaling B&O tax of \$ . . . , a credit for use tax/deferred sales tax of \$ . . . , manufacturing B&O tax of \$ . . . , a credit for multiple activities tax credit (MATC) of \$ . . . , litter tax of \$ . . . , syrup tax of \$ . . . , audit interest of \$ . . . , and additional interest from March 29, 2011 to April 18, 2012 of \$ . . . .

Taxpayer did not pay the assessment and timely petitioned for correction of assessment. Taxpayer is not disputing the retail sales tax, retailing B&O tax, use tax/deferred sales tax credit, manufacturing B&O tax, MATC credit, or the litter tax in the assessment. At issue are the syrup tax and the wholesaling B&O tax. We will first address the syrup tax issue.

Taxpayer makes wholesale sales of syrup to several extensions of the federal government. . . located in Washington. . . . Taxpayer did not collect the syrup tax from . . . the federal government . . . when it sold its syrup to them during the audit period. Taxpayer argues that it is not required to collect the syrup tax from them because these entities are exempt from the syrup tax under RCW 82.64.050(1). Taxpayer asserts that the Department’s Rule 255 exceeds its statutory authority and is invalid because it “shifts the incidence of the syrup tax to the wholesaler instead of the buyer.”

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<sup>2</sup> While the appeal was pending, Taxpayer submitted additional information for Audit to review. As a result, Audit issued a PAA for assessment number . . . and Taxpayer paid this assessment in full. At hearing, Taxpayer stated that it agreed with the PAA for assessment number . . . and this assessment is not in dispute.

<sup>3</sup> Two auditors worked on the audit on different issues, which resulted in two assessments issued with the respective issues.

The syrup tax assessment<sup>4</sup> also included the disallowed syrup tax exemptions Taxpayer took, under RCW 82.64.030(2), for wholesaling sales to businesses where the syrup was allegedly used outside Washington. Audit disallowed the syrup tax exemptions because Taxpayer did not produce a Certificate of Tax Exempt Export Carbonated Beverage Syrup, or another certificate with substantially the same information required under RCW 82.64.030(2) and Rule 255. When the appeal was pending, Taxpayer produced copies of Certificates of Tax Exempt Export Carbonated Beverage Syrup issued by the buyers.<sup>5</sup> Only the certificate issued by [Customer A] contained the type and volume of the syrup Taxpayer's customers purchased. The "Syrup Purchased" portions of the other certificates were left incomplete.<sup>6</sup>

With respect to the wholesaling B&O tax,<sup>7</sup> Taxpayer enters into agreements with its customers, under which Taxpayer agrees to pay its customers incentives to purchase its products. There are two types of incentives, one is labeled as a "funding." Taxpayer provided a copy of the agreement named [Customer Agreement] that it entered with [Customer B] as an example. The agreement in relevant part, provided:<sup>8</sup>

#### COMPLIANCE

The Account [Customer B] agrees and acknowledges funding hereunder is earned in response to the terms of this Agreement over the Term of the Agreement and that in order to receive the funding set forth herein, the Account must: (1) be in full compliance with the terms and conditions of this Agreement,<sup>9</sup> and (2) have paid, without offsets, auto or

<sup>4</sup> There are two items that are [not at issue] in the syrup tax assessment. The first one is the sales of generic syrup. Taxpayer argued in its petition that the sales of generic syrup are not subject to the syrup tax under RCW 82.64.020. Audit agrees that the sales of generic syrup are not taxable under RCW 82.64.020. However, this is [not an] issue because Audit did not assess generic syrup in its assessment during the audit period. The second one is the wholesale sales to businesses in Washington, other than to the federal government . . . , where Taxpayer did not collect and remit the syrup tax. Audit assessed syrup tax for these unreported sales, which is not in dispute. The undisputed amount of the syrup tax was \$ . . . out of the total assessed syrup tax of \$ . . . .

<sup>5</sup> The export certificates Taxpayer provided were issued by . . . [customers].

<sup>6</sup> Audit reviewed the certificates and determined only the certificate issued by [Customer A] conformed to the requirements under Rule 255. Audit will make the adjustment to the syrup tax assessment regarding [Customer A] in accordance with the certificate Taxpayer provided. Audit rejected the certificate issued by [Customer C] as a valid certificate because it was issued for purchase order . . . where the assessment for the syrup tax sale was for purchase order . . . .

<sup>7</sup> There are two [items not at] issue in the wholesaling B&O tax assessment. The first one is the syrup Taxpayer sells through vending machines located in Washington. Taxpayer claimed that it collected retail sales tax for these sales. Audit included the retail sales tax amount in the measure of Taxpayer's wholesaling B&O tax liability. On appeal, Taxpayer argues that the vending machines syrup retail sales should be excluded from the measure of its wholesaling B&O tax because they were not wholesale sales and it collected retail sales tax for those sales. Audit agrees with Taxpayer's proposed adjustment. Audit will exclude the retail sales tax collected for the vending machines syrup sales from the wholesaling B&O tax liability measurement providing that Taxpayer will submit documentation to prove that retail sales tax was collected and remitted to the Department. The second issue is the "customer short-pays" where Taxpayer deducted the amount its customer paid less the amount invoiced for its purchase. On Appeal, Taxpayer provided documents to demonstrate the gross receipts of the short-pays sales. Audit agrees and will make adjustment to the assessment to exclude the short-pays amount from Taxpayer's wholesaling B&O tax liability.

<sup>8</sup> That agreement covered the period from . . . .

<sup>9</sup> The terms and condition were: . . . .

other deductions, all invoices for products delivered to the Account in accordance with the payment terms set out above. (Emphasis added).

If any of the Account's stores fail to comply with the provisions of this Agreement, the Bottlers will provide the Account with five (5) days notice of such non-complying stores prior to the withholding of funds. . . . The Bottler also reserves the right to suspend all funds indefinitely to stores with consistent compliance issues. . . .

The [Customer Agreement] provided that Taxpayer would provide funding to [Customer B] per case of Taxpayer's products sold when [Customer B] reached a certain volume level of sales.<sup>10</sup>

. . .

Taxpayer deducted funding . . . payments or allowances to its customers when it reported its wholesaling B&O tax during the audit period. Audit disallowed the deductions because they were Taxpayer's costs of doing business. Taxpayer relies on Rule 108(5)(c) and argues that the payments or allowances were bona fide discounts that it offered to its customers based on the volume of product sold and are not subject to the wholesaling B&O tax.

## ANALYSIS

### [1. Liability for Syrup Tax]

The syrup tax is imposed upon the wholesaling and retailing sale of syrup sold in Washington. RCW 82.64.020.<sup>11</sup> There is no dispute that Taxpayer's syrup is "a concentrated liquid added to carbonated water to produce a carbonated beverage" as defined in RCW 82.64.010(3). RCW 82.64.050 provides that a wholesaler making wholesaling sales in Washington must collect the syrup tax from the buyer:

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<sup>10</sup> The agreement provided that Taxpayer would pay "a growth fund of \$ . . . per case on all incremental . . . Cases purchased by the Customer during the term in excess of the 2005 Cases from +2% +10% growth."

<sup>11</sup> Before 1994, RCW 82.64.020 imposed the "Carbonated beverage tax" on wholesale or retail sales of carbonated beverages or syrup in Washington. However, effective July 1, 1995, RCW 82.64.020, now commonly referred to as the "Syrup tax," was revised to impose a tax on the wholesale or retail sale of syrup. Carbonated beverages were excluded upon the revision of RCW 82.64.020. RCW 82.64.020 provides:

(1) A tax is imposed on each sale at wholesale of syrup in this state. The rate of the tax shall be equal to one dollar per gallon. Fractional amounts shall be taxed proportionally.

(2) A tax is imposed on each sale at retail of syrup in this state. The rate of the tax shall be equal to the rate imposed under subsection (1) of this section.

(3) Moneys collected under this chapter shall be deposited in the state general fund.

(4) Chapter 82.32 RCW applies to the taxes imposed in this chapter. The tax due dates, reporting periods, and return requirements applicable to chapter 82.04 RCW apply equally to the taxes imposed in this chapter.

- (1) The tax imposed in RCW 82.64.020(1) shall be paid by the buyer to the wholesaler and each wholesaler shall collect from the buyer the full amount of the tax payable in respect to each taxable sale, unless the wholesaler is prohibited from collecting the tax from the buyer under the Constitution of this state or the Constitution or laws of the United States. **Regardless of the obligation to collect the tax from the buyer, the wholesaler is liable to the state for the amount of the tax.** The tax imposed in RCW 82.64.020(2) shall be paid by the retailer. The buyer is not obligated to pay or report to the department the taxes imposed in RCW 82.64.020.

(Emphasis added).

Under RCW 82.64.050, a wholesaler must collect syrup tax from the buyer unless the wholesaler is prohibited from collecting the tax from the buyer under the Washington Constitution or the laws of the United States. In other words, a wholesaler cannot collect syrup tax from the buyer if the buyer is exempt from such tax either under the Washington Constitution or the laws of the United States. However, the statute provides that the **wholesaler is liable to the state** for the syrup tax **regardless of its obligation** to collect the tax from the buyer. Rule 255 is the Department's administrative rule implementing RCW 82.64.020. Rule 255(4)(a) explains that under RCW 82.64.020, a wholesaler is liable for the syrup tax if the buyer is exempt from the tax:

A wholesaler making a wholesale sale of syrup in this state must collect the tax from the buyer and report and pay the tax to the department. If, however, the wholesaler is prohibited from collecting the tax under the Constitution of this state or the Constitution or laws of the United States, the wholesaler is liable for the tax.

(Emphasis added).

Taxpayer's argument that "the Department shifts the incidence of the syrup tax to the wholesaler instead of the buyer" is not supported by statute or rule. The plain meaning of the language in RCW 82.64.050 clearly provides that the wholesaler is liable for the syrup tax regardless of whether it is obligated to collect from the buyer. Absent ambiguity, we rely on the plain language of the statute. *City of Spokane v. Dep't of Revenue*, 104 Wn. App. 253, 258, 17 P.3d 1206 (2001). The Department's interpretation of RCW 82.64.050 in Rule 255 is consistent with the statute. Taxpayer is a wholesaler when it makes sales to the buyers in Washington for resale, and it is liable for the syrup tax if the buyers are exempt from the syrup tax. RCW 82.64.050; Rule 255. Accordingly, we conclude that Taxpayer is liable to [remit] the syrup tax for sales made to the federal government . . . . We deny Taxpayer's petition and affirm the assessment on this issue.

[2. Exemption for Syrup Transferred Outside the State for Use Outside the State]

RCW 82.64.030(2) provides an exemption for syrup tax if the syrup "is transferred to a point outside the state for use outside the state. The department shall provide by rule appropriate procedures and exemption certificates for the administration of this exemption." (Emphasis added). Rule 255(5)(b)(i) provides the required documentation for the syrup tax exemptions:

The prior approval of the department is not required to claim an exemption from the syrup tax for exported syrup. The seller, at the time of sale, must retain in its records an exemption certificate completed by the buyer to document the exempt nature of the sale. This requirement may be satisfied by using the department's "Certificate of Tax Exempt Export Carbonated Beverage Syrup," or another certificate with substantially the same information.

(Emphasis added).

RCW 82.32.070 requires a taxpayer to preserve records, which provides in part:

Every person liable for any fee or tax imposed by chapters 82.04 through 82.27 RCW shall keep and preserve, for a period of five years, suitable records as may be necessary to determine the amount of any tax for which he may be liable, which records shall include copies of all federal income tax and state tax returns and reports made by him. All his books, records, and invoices shall be open for examination at any time by the department of revenue.

The Department's administrative rule WAC 458-20-254, provides additional details regarding this record keeping requirement. Further, RCW 82.32A.030(3) imposes the responsibility upon a taxpayer to "keep accurate and complete business records." Where a taxpayer fails to keep or provide adequate records from which the Department can ascertain the taxpayer's liability, the Department may obtain information from which it may reasonably determine or estimate the taxpayer's liability. Det. No. 89-53, 7 WTD 137 (1989).

Taxpayer argues that some of its syrup sales are exempt from the syrup tax, under RCW 82.64.030, because the syrup was transferred to a point outside the state for use outside Washington. In determining whether the syrup sales at issue are exempt from the syrup tax under the law, we must follow several long-accepted general rules of statutory construction. Taxation is the rule; exemption is the exception. *Spokane County v. City of Spokane*, 169 Wash. 355, 13 P.2d 1084 (1932). Exemptions from a taxing statute are to be narrowly construed. *Budget Rent-A-Car, Inc. v. Dep't. of Revenue*, 81 Wn.2d 171, 500 P.2d 764 (1972), *Evergreen-Washelli Mem'l Park Co. v. Dep't. of Revenue*, 89 Wn.2d 660, 574 P.2d 735 (1978).

In this case, Taxpayer did not produce evidence to demonstrate that the syrup was transferred to a point outside the state for use outside Washington. The exempt certificates Taxpayer provided did not contain the required type and volume of syrup that its customers purchased. We cannot determine the type and volume of syrup that Taxpayer's customers purchased that was transferred to a point outside Washington to qualify for the syrup tax exemption. Therefore, we deny Taxpayer's petition because Taxpayer failed to meet its burden to show that the disputed syrup sales are exempt from the syrup tax. We affirm the assessment on this issue.<sup>12</sup> Syrup tax is a separate tax from the wholesaling B&O tax that is also in dispute.

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<sup>12</sup> We remand the case to Audit for an assessment adjustment with respect to the sales to [Customer A], in accordance to the exempt certificate [Customer A], issued. See FN5 above.

[3. Bona Fide Discounts]

Washington's B&O tax is imposed on every person "for the act or privilege of engaging in business activities" and applies to the gross income of the business. RCW 82.04.220. "Business" for B&O tax purposes includes "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or to another person or class, directly or indirectly." RCW 82.04.140 (emphasis added). "Gross income of the business" similarly is broadly defined as:

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.

RCW 82.04.080(1) (emphasis added). Likewise, "value proceeding or accruing" is defined in pertinent part as the consideration, whether money, credits, rights, or other property expressed in terms of money, actually received or accrued." RCW 82.04.090 (emphasis added).

The Legislature "intended to impose the business and occupation tax upon virtually all business activities carried on within the state." *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 149, 3 P.3d 741 (2000) (quoting *Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971)). The B&O tax is not a tax on profit, net gain, capital gain, or sales "but a tax on the total money or money's worth received in the course of doing business." *Budget Rent-A-Car of Wash.-Oregon*, 81 Wn.2d 171, 172, 500 P.2d 764 (1972). The B&O tax provisions "leave practically no business and commerce free of the business and occupation tax." *Id.* at 175. As a result, unless an exception or deduction applies, a taxpayer owes B&O tax on all income received.

RCW 82.04.4283 allows a deduction for cash discounts taken by purchasers. RCW 82.04.160 defines "cash discount" as "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." The Department's administrative rule, Rule 108 provides guidance on discounts that are not subject to the B&O tax:

(5) **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.

WAC 458-20-108(5) (emphasis added).

The Department issued Excise Tax Advisory 3173.2013 (ETA 3173), titled "Distributor Discounts/Allowances to Grocery Stores," on January 7, 2013, which provides further guidance on bona fide discounts. ETA 3173 in pertinent part, provides:

Examples of discounts that are not bona fide because the person providing the allowance receives a service or benefit in return include, but are not limited to:

- Advertising allowance

An example of an advertising allowance is when a grocer receives some form of payment or credit from a distributor for advertising a distributor’s products in print, on the Internet, or in the Taxpayer’s place of business.

- Exclusivity allowance

An example of an exclusivity allowance is when a grocer receives some form of payment or credit from a distributor for carrying only the distributor’s products to the exclusion of competitor’s similar products. For example, a laundry detergent distributor provides a discount to a grocer if the grocer agrees not to stock laundry detergents sold by other distributors.

- Placement (slotting) allowance

An example of a placement allowance is when a grocer receives a payment or credit from a distributor for introducing a product line in the store or for placing a product in certain locations or in certain displays in the store.

The discounts described above are generally received in exchange for services and such income is reported as taxable gross income, generally subject to Service & Other B&O tax.

(Emphasis added).

In this case, in order for Taxpayer’s customers to receive the fees through the funding program, they have to perform specific services described in the [Customer Agreements]. These services include advertising Taxpayer’s products in specific orders and specific quantity; exclusively advertising Taxpayer’s products in the customers’ newspaper advertisement during Taxpayer’s promotional weeks; and placing Taxpayer’s products in certain locations or in certain displays in their stores. Taxpayer’s customers earn the fees by performing these services and they are not bona fide discounts Taxpayer provides to its customers [off of the wholesale price of the products]. These services Taxpayer receives from its customers are the consideration in exchange for the fees labeled as “funding” it gives to its customers. . . . Taxpayer must not deduct these fees from its [“gross proceeds of sales”]. RCW 82.04.070 [(prohibiting any deduction for expenses)]. To [do so] is contrary to the longstanding recognition that the B&O tax is “a tax on the total money or money’s worth received in the course of doing business.” *Budget Rent-A-Car of Wash.-Oregon*, 81 Wn.2d at 172.

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DECISION AND DISPOSITION

Taxpayer's petition is denied . . . . We deny Taxpayer's petition for the syrup tax assessment and the exclusion from its gross income of funding payments or allowances.. . .

Dated this 22nd day of February, 2013.