Cite as Det. No. 98-183, 18 WTD 220 (1999)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petitions For Correction of Assessments of	)	D E T E R M I N A T I O N
	)	No. 98-183
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[1] RCW 82.04.080; RCW 82.04.140: SERVICE B&O TAX – BUSINESS ACTIVITY – GROSS INCOME – SLOTTING FEES – PLACEMENT ALLOWANCES – SHELF SPACE. A grocer who provides shelf space for consideration is engaged in business. The grocer must include slotting fees or placement allowances for the shelf space in its gross income taxable under the service and other activities B&O tax classification.

[2] RULE 108; RCW 82.04.4283; ETA 34, ETA 494: DISCOUNTS – REBATES – MANUFACTURERS. Rebates paid by product manufacturers to grocers for shelf space to cover the grocers' costs of stocking the products were not deductible as discounts, but taxable as income.

[3] MISCELLANEOUS: B&O TAX -- SUBSTANCE OVER FORM. The doctrine of substance over form is not generally available to a taxpayer to eliminate the tax consequences of the taxpayer's structured form of the transaction. *See* Washington Sav-Mor Oil Co. v. State Tax Comm'n, 58 Wn.2d 518, 521, 364 P.2d 440 (1961).

[4] RCW 82.04.080 – RCW 82.04.090: B&O TAX -- VALUE PROCEEDING AND ACCRUING – FREE PRODUCT – CONSIDERATION. Product offered as consideration was not "free", but consideration for services. The value of consideration in the form of product accruing or proceeding to the taxpayer constituted gross income.

[5] MISCELLANEOUS: ESTOPPEL. The Department is not estopped from assessing tax based vague allegations of inconsistent treatment. *See* Kitsap-Mason Dairymen v. Tax Commission, 77 Wn.2d 812, 818, 467 P.2d 312 (1970).

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 ACTION:

A grocer protests the taxability of placement fees.[1]

FACTS:

M. Pree, A.L.J. – The taxpayers listed in the heading above operate grocery stores in Washington. The Department of Revenue (Department) reviewed their books and records. The Department's Audit Division assessed sales tax, use tax, and business and occupation tax, which the taxpayers protested. The sales and use tax issues for all of the taxpayers were discussed at the hearing. Following the hearing, the Audit Division prepared Post Audit Adjustments, which will resolve the sales and use tax issues. This determination addresses the only remaining issue -- business and occupation (B&O) tax.

Manufacturers paid[2] the taxpayers allowances to obtain shelf space for new products or to maintain shelf space for existing products. The taxpayer purchased the products from the manufacturers or distributors. The Audit Division found that generally, the taxpayers requested these fees to offset the costs of stocking products, including computer bar code charges. The Audit Division taxed the fees under the service and other activities B&O tax classification.

The taxpayers consider the fees or allowances, necessary means of reducing the costs of goods sold. The taxpayers state it is costly to introduce new items and they must maintain a larger profit margin on those items to purchase them. According to the taxpayers, the activities generating the allowances are an integral function of the negotiation for their purchase of goods at the lowest cost. The taxpayers consider the allowances to be trade discounts, not payments for separate taxable activities. The taxpayers do not consider the allowances within the contemplation of the tax statutes.[3]

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

[2] The consideration included both cash and "free products". The Audit Division included slotting and placement fees in the assessment regardless of the form of the consideration.

[3] The taxpayer's post-hearing brief states, "Detailed briefs addressing taxation of grocery industry allowances in general have heretofore been filed on behalf of other taxpayers in the retail grocery business, and those general arguments are incorporated herein by reference." This determination will only address the issues raised by the taxpayers to whom it's addressed. The taxpayers may wish to contact the grocers to whom they refer for our responses to other arguments.

ISSUES:

Are placement allowances or slotting fees, negotiated to increase the profit margin for new items, subject to B&O tax?

DISCUSSION:

[1] B&O tax is imposed upon receipts from business activities. See RCW 82.04.220. RCW 82.04.140 defines "business" as:

> "Business" 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.

Manufacturers pay the taxpayers to obtain shelf space from the taxpayers for new products or to maintain shelf space for existing products. The taxpayers negotiate the allowances and offer the shelf space and other services with the object of gain. The taxpayers' activities constituted business under RCW 82.04.140.

RCW 82.04.220 imposes B&O tax on business activities at stated rates for various activities. If the activity is not otherwise defined, the proper classification is service and other activities. RCW 82.04.290.[4] B&O tax under that classification is measured by the gross income of the business. Id. RCW 82.04.080 defines "Gross income of the business" 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.

The taxpayers receive cash or product for placement or slotting services. The taxpayers' placement or slotting activities for consideration constitute business transactions. Therefore, receipts to induce the taxpayers to provide shelf space for new products or to maintain shelf space for existing products are income to the taxpayer, unless otherwise deductible or excludable.

The taxpayers allege the negotiations for placement and slotting allowances, which included procurement of the products, were not taxable activities within contemplation of the tax statutes. We disagree. In Time Oil Co. v. State, 79 Wn.2d 143, 483 P.2d 628 (1971) , the Washington

[4] Effective July 1, 1993, this provision was recodified as RCW 82.04.290(4) and effective July 1, 1998 again recodified as RCW 82.04.290(2).

Supreme Court (Court) held that exchanges of goods between affiliates were subject to tax, even without the transfer of possession of the goods. Analyzing the statutory scheme of Chapter 82.04 RCW, the Court did not limit the activities upon which the tax could be imposed:

> RCW 82.04.140 defines "business" as:
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> "Business" 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.
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> For purposes of applying and measuring the tax, the statute then proceeds to classify various business activities, i.e., Extracting, RCW 82.04.230; Manufacturing, RCW 82.04.240; Retailing, RCW 82.04.250; Wholesaling grains, RCW 82.04.260; Wholesaling, RCW 82.04.270; Other business or service activities, RCW 82.04.290.
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> Viewing these broad provisions, and RCW 82.04 in its entirety, it is obvious that the legislature intended to impose the business and occupation tax upon virtually all business activities carried on within the state. Reynolds Metals Co. v. State, 65 Wn.2d 882, 400 P.2d 310 (1965).

Time Oil, at 146. The taxpayers' placement and slotting services clearly were business activities. The allowances were intended to be taxed.

The taxpayers sell groceries. The taxpayers also purchase products, promote them, and sell shelf space. Those activities, although related, are separate and distinct from selling the products. Persons engaged in multiple activities within the purview of the B&O tax provisions are taxable under each section applicable to each of their activities. RCW 82.04.440. For instance, J.C. Penney paid tax at the retailing rate on sales and the service rate for its financing charges from its charge accounts. See Department of Rev. v. J. C. Penney Co., 96 Wn.2d 38, 633 P.2d 870 (1981). In Impecoven v. Department of Rev., 120 Wn.2d 357, 364, 841 P.2d 752 (1992), the court stated:

> The statute, itself, allows a "person" who engages in separate but related activities to be taxed on each activity unless exempted. See RCW 82.04.440; see also Drury the Tailor v. Jenner, 12 Wn.2d 508, 510, 515, 122 P.2d 493 (1942) (prior to subsequent legislative exemption, tax properly imposed on activity of retail and on manufacture as each constitutes a separate activity).
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> In addition, we have refused to ignore the business structure of entities engaged in separate but related activities to avoid B&O taxation. See Washington Sav-Mor Oil Co. v. State Tax Comm'n, 58 Wn.2d 518, 364 P.2d 440 (1961).

Allowances in the form of cash or product constitute gross income of the taxpayer, unless other authority exists to exclude or deduct these amounts. "Taxation is the rule and exemption is the exception." O'Leary v. Department of Revenue, 105 Wn.2d 679, 682, 717 P.2d 273 (1986),

quoting Budget Rent-A-Car of Washington-Oregon, Inc. v. Department of Rev., 81 Wn.2d 171, 174, 500 P.2d 764 (1972).

[2] The Department allows deductions for bona fide discounts. Deductible discounts include cash discounts and trade discounts offered by sellers. RCW 82.04.4283 allows a deduction for cash discounts taken by purchasers. 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.

From the evidence provided by the taxpayer, the allowances were not dependent upon dates when the taxpayer paid the suppliers. Therefore, the allowances were not cash discounts. The fees for slotting and placement services are not deductible under RCW 82.04.4283.

Other discounts may not be subject to tax. Rule 108 provides in part:

> (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.

The Department has been uniform and consistent in its position that bona fide discounts never include situations where the purchaser is required to provide any service or benefit to the seller in return for the price reduction. Det. No 83-180, 11 WTD 5, 7 (1983). Discounts do not include advertising allowances from wholesalers to retailers. Id. Similarly, manufacturers' payments to dealers for "make-ready" services on equipment sold by the manufacturers to the dealers are taxable to the dealers. ETA 034.04.108[5]. Manufacturers are not granting discounts to the taxpayers. They are paying the taxpayers for services performed by the taxpayers for them.

Other rebates are subject to B&O tax. For instance, car dealers must include automobile manufacturers' rebates assigned to the dealers in their measure of B&O tax as well as in the measure of retail sales tax. See ETA 494.08.108 (ETA 494, copy attached). Manufacturers pay consumers rebates on cars that they purchase from dealers. Manufacturers' rebates are not a discount in the buyer's purchase price. See Det. No. 89-107, 7 WTD 189 (1989) and Det. No. 87-365, 4 WTD 357 (1987). We require consumer-buyers to pay retail sales tax on the full price. Sellers must include the full price in their measure of tax. Since we do not treat manufacturers' rebates as discounts, the payments received from the manufacturers must be accounted for as income.

[5] Formerly, ETB 034.04.108. All Excise Tax Bulletins have been cancelled and reissued as Excise Tax Advisories to be consistent with RCW 34.05.230(4).

Payments to entice particular purchases or other behavior regarding transactions are taxable. For instance, builders who construct energy efficient structures for new homebuyers include payments from electric companies in their measure of tax. Det. No. 93-078, 12 WTD 599 (1993). In our case, the manufacturers paid the grocers with allowances to obtain shelf space and to cover the costs of stocking products to encourage the taxpayers to stock products in a particular manner.

No legal authority exists in the statutory scheme permitting a deduction of the allowances at issue.[6] The allowances must be included in the taxpayer's measure of tax.

[3] The taxpayers state there is no difference in substance when these transactions are compared to discounts. The taxpayers ask that we disregard the form and observe the substance of the transactions. When asked to disregard the form of transactions structured by a taxpayer, the Court refused. See Washington Sav-Mor Oil Co. v. State Tax Comm'n, 58 Wn.2d 518, 521, 364 P.2d 440 (1961). In Sav-Mor Oil, the plaintiff challenged the assessment of B& O tax on sales to its parent corporation. Sav-Mor argued as a wholly owned subsidiary, it was actually a part of the parent company. If part of the same company, it could not make a sale to itself. The court rejected the argument. The Court will not "import an exemption into the tax statutes" where none existed. Time Oil at 147.

[4] The taxpayers state other audits do not include tax on free product. The product was not free, but consideration for its placement and slotting services. Payment for services regardless of the form of the consideration is taxable. "Gross income of the business" means "the value proceeding or accruing by reason of the transaction of the business engaged in". RCW 82.04.080. RCW 82.04.090 defines "Value proceeding or accruing":

> "Value proceeding or accruing" means the consideration, whether money, credits, rights, or other property expressed in terms of money, actually received or accrued.

The taxpayer received value in the form of the property as consideration for its placement and slotting services. Under these circumstances, we do not consider the product "free".

[5] We are not aware of the specific instance(s) referred to by the taxpayer where the Audit Division exempted product for placement or slotting services. Equitable relief to the taxpayer under the doctrine of estoppel is not the remedy even if allowed in another audit. The Department has not changed its position regarding the issues raised by the taxpayer.

In Kitsap-Mason Dairymen v. Tax Commission, 77 Wn.2d 812, 818, 467 P.2d 312 (1970), the Washington Supreme Court addressed audit inconsistencies stating:

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[6] For instance, RCW 82.04.4283 specifically permits a deduction for cash discounts. Offering rebates has been a business practice for years. No statutory deduction exists for business rebates.

> . . . This is not a case in which auditors changed their interpretation of a statute or rule. It is one in which they overlooked through ignorance, neglect or inadvertence Kitsap's error in computing the tax. The fact that the oversight only recently has been discovered does not relieve Kitsap of its liability for the correct tax during the audit period now under consideration.

The taxpayer has not provided any evidence that it received any misinformation from the Department. Further, if the taxpayer has received any misinformation from another source, we note:

> A failure to pay taxes because of misinformation received from others, including the DOL [Department of Licensing], is not a defense to a later assessment for delinquent taxes under case law or any statute. To create an estoppel, three elements must be present: (1) an admission, statement, or act inconsistent with the claim afterwards asserted, (2) action by the other party on the faith of such admission, statement, or act, and (3) injury to such other party resulting from allowing the first party to contradict or repudiate such admission, statement, or act. Harbor Air Service, Inc. v. Board of Tax Appeals, 88 Wn.2d at 359, 366-67 (1977).

Det. No. 87-298, 4 WTD 087, 93 (1987). The taxpayer has failed to establish a basis for relief under the doctrine of estoppel.

DECISION AND DISPOSITION:

Taxpayer's petition is denied.

Dated this 29th day of October, 1998.