

SENATE BILL REPORT

SB 5407

As Reported by Senate Committee On:
Ways & Means, February 18, 2019

Title: An act relating to providing that scan-down allowances on food and beverages intended for human and pet consumption are bona fide discounts for purposes of the business and occupation tax.

Brief Description: Providing that scan-down allowances on food and beverages intended for human and pet consumption are bona fide discounts for purposes of the business and occupation tax.

Sponsors: Senators Mullet, Conway, Braun, Rolfes and Schoesler.

Brief History:

Committee Activity: Ways & Means: 1/30/19, 2/18/19 [DP, w/oRec].

Brief Summary of Bill

- Provides a business and occupation tax deduction for scan-down allowances.

SENATE COMMITTEE ON WAYS & MEANS

Majority Report: Do pass.

Signed by Senators Rolfes, Chair; Frockt, Vice Chair, Operating, Capital Lead; Mullet, Capital Budget Cabinet; Braun, Ranking Member; Brown, Assistant Ranking Member, Operating; Honeyford, Assistant Ranking Member, Capital; Bailey, Becker, Billig, Carlyle, Conway, Darneille, Hasegawa, Hunt, Keiser, Liias, Palumbo, Rivers, Schoesler, Van De Wege, Wagoner and Warnick.

Minority Report: That it be referred without recommendation.

Signed by Senator Pedersen.

Staff: Jeffrey Mitchell (786-7438)

Background: Washington State's major business tax is the business and occupation (B&O) tax. The B&O tax is imposed on the gross receipts of business activities conducted within

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the state, without any deduction for the costs of doing business. A business may have more than one B&O tax rate, depending on the types of activities conducted. Major tax rates are 0.471 percent for retailing; 0.484 percent for manufacturing, wholesaling, and extracting; and 1.5 percent for services, and activities not classified elsewhere. Several lower rates also apply to specific business activities.

A B&O tax deduction reduces the amount of taxable income subject to tax.

A bona fide discount negotiated by a grocer from a distributor upon purchase of goods is not subject to B&O tax. However, if a grocer performs a service, such as advertising, in addition to selling goods in exchange for the discount, then the discount is subject to B&O tax. As provided in an Excise Tax Advisory, the Department of Revenue (DOR) has historically taken the position a payment or credit by a distributor to a grocer exclusively for the grocer selling a specific volume of products during a specific timeframe is not subject to B&O tax on the value of the payment or credit. These payments or credits are often referred to as scan-down allowances. In a 2014 court ruling (*Klein Honda v. State*), the court concluded under a dealer cash program, where a car manufacturer offers dealers a specified amount of cash for each sale the dealer makes in a specific period of time, the cash payment is subject to B&O tax. After *Klein Honda*, DOR reviewed its policy regarding bona fide discounts and found its guidance in the Excise Tax Advisory is inconsistent with the court decision.

All new tax preference legislation must include a tax preference performance statement. Tax preferences include deductions, exemptions, preferential tax rates, and tax credits. The performance statement must clearly specify the public policy objectives of the tax preference as well as the specific metrics and data used by the Joint Legislative Audit and Review Committee (JLARC) to evaluate the efficacy of the tax preference. New tax preferences expire ten years after the effective date of the tax preference, unless otherwise provided.

Summary of Bill: A B&O tax deduction is provided on scan-down allowances for food and pet food products. "Scan-down allowance" is generally defined as payment or credit offered to a seller by a manufacturer or wholesaler of products where:

- the amount of payment or credit is based on the quantity of product sold at retail by the seller within a specified period of time;
- the seller knew the terms of the offer before making the sales that generated payment or credit from the manufacturer or wholesaler; and
- the seller is not required to provide any services to the manufacturer or wholesaler or engage in any business activities directly or indirectly benefiting the manufacturer or wholesaler, to receive the payment or credit from the manufacturer or wholesaler.

The bill is exempt from JLARC review and the automatic ten-year expiration date.

Appropriation: None.

Fiscal Note: Available.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: We would like to commend the Department of Revenue for not beginning to tax our industry before there was a legislative session to get the issue clarified. This bill is very important to our industry and only impacts small to mid-size grocery stores and convenience stores who are not vertically integrated. Most of these discounts flow through the system as off invoice allowances deducted from the normal cost of the product as a discount that appears right on the invoice. We put a huge emphasis on providing groceries to our customers at low prices. Scan down allowances play a large part in our ability to provide these low retail prices to our customers. Manufacturers have begun emphasizing the use of scan-down allowances as their way of giving us promotions. Therefore, a business and occupation tax on these discounts will impact not only profitability, but affordability for customers as well.

Persons Testifying: PRO: Kyle Saar, Samar's Grocery Stores; Jeff Clemens, UNFI/Supervalu; Jan Gee, Washington Food Industry Association.

Persons Signed In To Testify But Not Testifying: No one.