


ST 2458 - SALES TAX : WHETHER TRADE INCENTIVE PAYMENTS (INCLUDING PROMOTIONAL REBATES) EFFECT A REDUCTION IN THE SALE VALUE OF GOODS

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TAXATION RULING NO. ST 2458

SALES TAX : WHETHER TRADE INCENTIVE PAYMENTS (INCLUDING
PROMOTIONAL REBATES) EFFECT A REDUCTION IN THE SALE
VALUE OF GOODS

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OTHER RULINGS ON TOPIC ST 2039; AUSTRALIAN SALES TAX (AST)
PARAS 377-378

PREAMBLE By virtue of paragraph 18(1)(a) of Sales Tax Assessment Act (No.1), the sale value of goods sold by a manufacturer by wholesale is "the amount for which the goods are sold". A comparable provision applies in other Assessment Acts, e.g., subsection 4(1) of Sales Tax Assessment Act (No.2), subsection 4(1) of Sales Tax Assessment Act (No.3), section 4 of Sales Tax Assessment Act (No.6) and subsection 4(1) of Sales Tax Assessment Act (No.7).

2. Trade incentive payments, also known variously as trade discounts, trade price rebates, volume rebates, promotional rebates, incentive rebates, co-operative advertising allowances and deferred credits are commonly negotiated between suppliers of goods (manufacturers or wholesale merchants) and purchasers (retailers). These incentives, as their various descriptions suggest, take a variety of different forms and are allowed by suppliers in many different circumstances. They are often initiated by or paid at the behest of purchasers rather than their suppliers. These incentives include :

- (a) allowances provided to purchasers to either increase sales of goods by suppliers to purchasers or to agree on a temporary reduction of retail prices of the supplier's products; and
- (b) allowances to purchasers in relation to:
 - . the incurring by the purchaser of advertising expenditure,
 - . promoting the supplier's products by displaying them at prime locations in the retailer's

- premises,
- . ullage,
- . warehousing,
- . distribution or
- . other marketing arrangements.

3. The question arises whether, in determining for sales tax purposes "the amount for which goods are sold", trade incentive payments provided by suppliers of goods to purchasers/retailers effect a reduction in that "amount". If so, the sale value of the goods is reduced accordingly, and consequently, the amount of sales tax payable is reduced.

4. This issue was addressed in part in Taxation Ruling No. ST 2039. The purpose of this Ruling is to expand upon and to clarify the principles contained in the earlier Ruling. That Ruling is qualified accordingly.

5. In this ruling, the terms "allowance", "credit", "discount", "incentive", "payment", "rebate", "reimbursement", "subsidy" and "trade incentive payment", unless the context reveals otherwise, are used as follows:

- . "allowance" - a term used to describe an amount allowed by a seller (supplier) to a purchaser (customer) which encompasses a credit, discount, rebate, reimbursement or subsidy.
- . "credit" - a term similar to an allowance.
- . "discount" - an allowance given by a seller to a purchaser before or at the time of billing the purchaser and ordinarily (though not necessarily) shown on an invoice.
- . "incentive" - an abbreviated reference to a trade incentive payment.
- . "payment" - a neutral term similar to an allowance.
- . "rebate" - an allowance given by a seller to a purchaser after the time of billing the purchaser and ordinarily effected by cheque or credit note.
- . "reimbursement" - a payment by a seller to a purchaser to repay or recompense (in whole or in part) the purchaser for having incurred expenditure or having agreed to incur expenditure.
- . "subsidy" - a payment by a seller to a purchaser as a contribution towards expenditure to be incurred by the purchaser ordinarily (though not necessarily) paid before the expenditure is incurred by the purchaser.
- . "trade incentive payment" - an all encompassing term similar to an allowance used to describe any allowance, credit, discount, rebate, reimbursement and subsidy

provided by a seller to a purchaser inducing (or tending to induce) the purchaser to do something or to allow the seller to take some action.

RULING Amount for which goods are sold - Set-Off

6. One approach to the question whether trade incentive payments effect a reduction in "the amount for which the goods are sold", and thus, reduce the sale value of the goods examines a set-off of considerations as explained below.

7. The words "amount for which those goods are sold" in subsection 18(1) of Sales Tax Assessment Act (No.1) were considered by the High Court of Australia in Commonwealth Quarries (Footscray) Pty Ltd v FC of T (1938) 59 CLR 111 and EMI Australia Ltd v FC of T 71 ATC 4112 ; (1971) 2 ATR 325.

8. In the Commonwealth Quarries case, Dixon and McTiernan JJ (at p.121) said:

"To us these words appear necessarily to mean the contract price. In a contract under which for a single lump sum of money a party undertakes to do various things, including the transfer of property in goods, it is quite true that the entire money consideration or contract price cannot be regarded as the amount for which the goods are sold. In such a case the amount for which the goods were sold could not be ascertained from the transaction except by allocating part of the consideration to the other acts or things to be done by the seller."

9. As a corollary of this, it is equally true that the contract price cannot be regarded as "the amount for which the goods are sold", where a purchaser undertakes to do various things, in addition to payment of the price. Under a contract a purchaser (retailer) might undertake, for example, to incur advertising, promotional or other marketing expenses for consideration. The purchaser and the supplier of goods might also agree, in order to arrive at the contract price, to set-off that consideration against the money consideration (i.e. the price) payable for the transfer of property in the goods. In such a case, the Commissioner does not accept that the contract price represents "the amount for which the goods are sold".

10. Unlike the contract involved in the Commonwealth Quarries case, namely, "an ordinary contract for the sale and delivery of goods" (per Latham CJ at p.116), a contract under which a purchaser (retailer) undertakes to do various things in addition to paying the money consideration or price of the goods (e.g., incur advertising, display, etc. expenses) is something more than an ordinary contract for the sale of goods. The act of delivery involved in the Commonwealth Quarries case was so essential to the sale of goods that it could not be distinguished from the sale as a separate and independent act or service to which part of the consideration forming the selling price of the goods must be allocated. The act of the retailer in undertaking to incur advertising, display, etc. expenses, however, is not an essential element of the sale of the goods. It can be distinguished from sale and purchase as a separate and independent act or service so that the consideration forming the selling price of the goods (i.e. the amount for which the goods

were sold) is not affected by, and must not be reduced by, consideration payable by the supplier to the retailer for that undertaking.

11. In the EMI case *Windeyer J* (at p.4118 ; p332) said:

"... as used in the Assessment Act, 'the amount' for which a thing is sold means I consider the sum total of all moneys the buyer promises, expressly or tacitly, to pay to, or for, the seller in order that he, the buyer, may get a good title to goods that he has agreed to buy."

12. His Honour also later referred (at p.4118 ; p.333) to "the total amount that the buyer must pay to get the property in the goods free of claims by third parties."

13. In an ordinary contract for the sale of goods it is the transfer of property in the goods in return for a money consideration called "the price" which of itself constitutes full satisfaction of the contract. In such a case the contract price may well represent "the amount for which the goods were sold".

14. Where, however, the contract incorporates terms or conditions by which the purchaser promises to do something in addition to paying the money consideration (price) for the goods, it is no longer an ordinary contract for the sale of the goods. The contract price in this situation - being a net amount of consideration after a set-off to recompense the purchaser for the promise - no longer represents "the amount for which the goods are sold". It is therefore not acceptable to the Commissioner as the sale value of the goods.

Amount for which goods are sold - Aggregation

15. An alternative approach to the question whether trade incentive payments effect a reduction in the sale value of goods involves an aggregation of different kinds of considerations as explained below.

16. The consideration in a contract for the sale of goods is ordinarily a price in money. A pure exchange of goods without any reference to a money value is not a sale but is a contract of exchange or barter. Where, however, parties agree that the consideration be partly in money and partly in some other form on which a fixed or ascertainable money value is put (e.g. where goods are traded-in in part exchange), the contract may be construed as a contract of sale.

17. Where, therefore :

- (i) a purchaser of goods (the retailer), in addition to paying a money consideration for the goods, agrees:
 - (a) to sell to a supplier of the goods (manufacturer or wholesale merchant) other commodities;
 - (b) to provide a service to, for or at the direction of the supplier; or
 - (c) to discharge a debt of the supplier; and

- (ii) a fixed or ascertainable money value is put on that transaction,

the contract may constitute a contract of sale for the aggregate sum as the price. In this event, the sale value of the goods will also be the aggregate sum.

18. In determining "the amount for which the goods are sold" for the purposes of the sale value provisions in the sales tax law, any discount, rebate or credit deducted from the selling price of the goods therefore needs to be subjected to careful scrutiny before it may be accepted that it effects a reduction in that "amount".

Eligible Trade Incentive Payments.

19. The following paragraphs outline the requirements that need to be satisfied before the Commissioner will accept that a trade incentive payment effects a reduction in the sale value of goods.

20. The Commissioner has for many years adopted the view that an incentive, however described, does not effect any reduction in the sale value of goods, with any consequent reduction in the amount of sales tax payable, unless all the following fundamental requirements are satisfied:

- (i) The purchaser (i.e., the retailer) has a legal right to the incentive from a manufacturer or wholesale merchant by virtue of an express or implied condition of the contract for sale of the goods (AST para. 378).
- (ii) The incentive is in respect of the price payable for goods under a contract for sale of goods between the parties concerned.
- (iii) The granting of the incentive must relate to, so as to effect a reduction of, the selling price of the goods. In determining sale values, it is the amount for which the goods are sold in each individual transaction which must be determined. Unless an incentive provided by a vendor can be allocated to a particular article or sale so that an ascertainable amount of the incentive can be applied to the particular article or sale, it cannot be said the incentive affects the amount for which those particular goods (i.e. that article or the goods the subject of that particular sale) are sold.

21. These are fundamental requirements that must be satisfied for there to be any reduction in sale value in respect of a trade incentive payment. They do not, however, exhaustively state all the necessary requirements to be met. Even where these fundamental requirements are satisfied, whether or not a particular trade incentive payment effects a reduction in the sale value of goods will turn on the true nature or character of the incentive bearing in mind such matters as:

- (a) the particular circumstances which gave rise to the payment of the incentive and in which the incentive is calculated and made available to a retailer;

- (b) the accounting treatment of the incentive in the financial records of the manufacturer or wholesale merchant and the retailer; and
- (c) the reasonableness of the amount of the incentive in the sense of the commercial reality of the amount of the incentive in relation to the value of the goods sold.

22. The following features of a trade incentive payment are not necessarily conclusive of the incentive effecting a reduction in sale value :

- (i) the name or description given to an incentive by the parties;
- (ii) the incentive is calculated by reference to either the volume or the value of sales made under the particular contract for the sale of goods to the retailer;
- (iii) that the underlying reason for the payment of an incentive is either to secure a particular sale to the retailer or to increase sales to the retailer;
- (iv) the only contract or agreement entered into between the manufacturer or wholesale merchant and the retailer is an ordinary contract for the sale of the goods; and/or
- (v) at the time of the sale of the goods the retailer is aware, from the course of past ordinary commercial dealings with the manufacturer or wholesale merchant or by the terms of a written agreement, of the amount of the incentive to which the retailer is entitled.

Examples of Eligible Incentive Payments

23. Some trade incentive payments by their true nature or character properly effect a reduction in "the amount for which goods are sold". The following are examples of incentives which, provided the fundamental requirements set out in paragraph 20 above are met, the Commissioner would accept effect a reduction in sale value:

Trade Discount : where because of trade practice contractual arrangements are entered into between a manufacturer or a wholesale merchant and a retailer resulting in the sale of goods at a price calculated by deducting a trade discount (of a reasonable amount) from a gross price, the gross price, the trade discount, the net price and the sales tax calculated on the net price being shown separately on the invoice.

Volume or Value Rebates and Deferred Credits : where these rebates and credits are calculated at a reasonable level by reference to, and are attributable only to, the volume or value of goods sold under a contract of sale of the goods between a manufacturer or wholesale merchant and a retailer with no other strings attached (i.e. no obligation on the retailer or on any employee or associate of the retailer to do such things as to incur any advertising, promotion or other marketing expenses in relation to the goods.)

Settlement Discount : where a discount calculated at a reasonable level is provided by the supplier on the basis of payment being made by a retailer in cash or being received promptly and is based on the value of the goods sold under a contract of sale of the goods.

NOTE: This discount is allowable on the basis that the consideration for the sale of goods is ordinarily due and payable at the time of the sale. Goods may be sold, for example, at \$97 with payment due and payable at the time of sale or promptly. If they are not paid for at that time the sale price is to be \$100. This would be reflected on the invoice as sale price \$100 less 3% discount for cash or prompt payment. In such a case the amount for which the goods are sold is in reality \$97.

Anti-Avoidance Provisions

24. It should also be noted that the provisions of section 18A and sub-section 18(4) of Sales Tax Assessment Act (No. 1), and comparable provisions in other Assessment Acts, may be relied on in appropriate cases to ensure that the sale value of goods includes a trade incentive payment.

25. It is not proposed to explore in detail in this Ruling which cases might be appropriate for these anti-tax avoidance provisions to apply. However, the Commissioner would need to consider whether or not these anti-avoidance provisions apply :

- (a) where, for example, a trade incentive payment is set at, or increased to, a level disproportionate to the value of the goods sold; or
- (b) where a trade incentive payment is paid, not to the retailer, but to an employee, relative or associate of the retailer.

Ineligible Trade Incentive Payments

26. Some trade incentive payments by their intrinsic nature or character do not effect a reduction in "the amount for which goods are sold". Ineligible incentives are those paid by a supplier to a retailer which really answer the description of either:

- (i) a reimbursement of expenditure incurred (or a subsidising of expenditure to be incurred) by a retailer on such things as advertising, promotion, warehousing, distribution or other marketing activities, accounting, bookkeeping or debt collection functions ; or
- (ii) a reward or other consideration provided to a retailer for either undertaking such things as advertising, promotion, warehousing, distribution or other marketing activities, accounting, bookkeeping or debt collection functions or for allowing the supplier a right to use the retailer's premises or equipment for such activities.

27. Where a trade incentive payment is made by a supplier to secure a sale by the supplier or to obtain an increase in the supplier's sales and :

- . there is some service provided (or to be provided) by the purchaser, some act done (or to be done) by the purchaser or some transaction or operation effected (or to be effected) by the purchaser of benefit to the supplier; and
- . the service, act, transaction or operation is one which, if it had been undertaken by the supplier, would have involved a cost that would have formed part of the sale value of the goods sold by the supplier,

the Commissioner takes the view that the incentive does not effect a reduction in the sale value of the goods. This is so whether or not the incentive is calculated by reference to the volume or value of the goods sold.

28. Similarly, an incentive does not effect a reduction in the sale value of goods where it is provided by a supplier to a purchaser (retailer), for example, either:

- . in return for the retailer providing "gondola ends" (i.e. end-of-aisle fixtures in the retailer's supermarket premises) to display and promote the supplier's products; or
- . in return for the retailer allowing the supplier to assemble "gondola ends" in the retailer's premises.

29. Where a manufacturer or a wholesale merchant pays an incentive to a retailer or to a retail group buying organisation in return for the group buying organisation providing some services such as accounting, book-keeping or debt collection services for the benefit of the manufacturer or wholesale merchant (i.e. services expenditure on which would otherwise have been included in the wholesale selling price of the goods), the incentive does not constitute a reduction in the sale value of goods sold by the manufacturer or wholesale merchant.

30. An incentive of the type mentioned in subparagraph 26(i) or 26(ii) above, while possibly having some connection with a contract for the sale of goods to the retailer, is in reality separate and distinct from the amount for which the goods are sold. For example, a manufacturer (A) might contract with a retailer (B) to sell 1000 chain saws to B for \$100,000 and B contracts (whether or not in a separate contract) with A that:

- (a) B will undertake at its own expense certain advertising or promotion of A's chain saws for \$15,000;
- (b) A will reimburse (in whole or in part) B for the expenditure that B incurs; but
- (c) rather than A reimbursing B by a cash payment of \$15,000 for that expenditure, A will set-off against the selling price of the chain saws (\$100,000) an amount equal to the amount of the expenditure incurred by B (\$15,000). The invoice would show a net price of

\$85,000.

31. Such a set-off constitutes a payment by A to B of \$15,000 to extinguish A's contractual obligation to reimburse B for incurring the expenditure in question. It does not affect the price payable by B to A under the contract for the sale of the chain saws, namely, \$100,000. Nor does it affect, for sales tax purposes, the amount for which the chain saws are sold. Alternatively, the contract when properly construed constitutes a sale of the chain saws for a money consideration (\$85,000) plus a consideration in kind (advertising or promotion services valued at \$15,000).

32. The Commissioner considers unacceptable any arrangement by which a reduction in sale value is sought to be achieved by a retailer incurring expenses which in the absence of that arrangement would have been:

- (a) incurred by a manufacturer or a wholesale merchant; and
- (b) recovered in the amount for which goods are sold by the manufacturer or a wholesale merchant.

33. The following features of a trade incentive payment, when carefully scrutinised in the context of the overall transaction or dealings between the parties, will clearly point to an incentive being, by its intrinsic nature or character, one that does not effect a reduction in the sale value of goods:

- (i) the incentive is only payable (whether or not under a separate collateral contract) with strings attached - other than a requirement that the retailer will purchase a specific quantity or value of goods - for example, an incentive payable only where the retailer is to incur advertising, promotion or other marketing expenses or is to engage in some marketing activity for, on behalf of, at the direction of, or by arrangement directly or indirectly with the manufacturer or wholesale merchant;
- (ii) the amount of the incentive is conditional and payable for a specific purpose, e.g., where it is dependent on a proposed level of advertising, promotion or other marketing expenses to be borne initially by the retailer;
- (iii) no incentive is available to a retailer who does not achieve a predetermined target level of advertising, promotion or other marketing expenditure;
- (iv) there is an obligation imposed on the retailer, in the same or another contract, for example to perform or pay for promotional or advertising services or to display goods in a particular manner, and the Commissioner is satisfied that this obligation has a value which has (notionally or expressly) been set-off against the sale price of the goods to produce the price stated in the contract for sale.
- (v) the manufacturer or wholesale merchant exercises, or is able to exercise, some degree of direction and/or

control over the retailer in performing any relevant marketing activity or incurring any relevant marketing expenditure e.g. insists on giving final approval for advertising material or for the particular location and manner in which goods are displayed for retail sale;

- (vi) the incentive is payable under a contract, agreement or arrangement separate and distinct from the contract for the sale of goods yet the contract price is sought to be reduced by the amount of the incentive;
- (vii) the incentive results in effect in a reimbursement or subsidy being provided to a retailer for incurring advertising, promotion or other marketing expenses or for engaging in some marketing activity advantageous to the manufacturer or wholesale merchant; and
- (viii) the incentive for promotional or other marketing activity is retrospective, e.g., credited after goods have been sold by a retailer either at regular intervals during the period of the promotion or in full after the promotion period has elapsed.

34. In most cases of the types falling within paragraph 33, there would be no necessity to apply the anti-tax avoidance provisions, because the effect of the arrangements would be that the true "sale price" would be the higher figure. Where necessary, however, the anti-tax avoidance provisions will be invoked in such cases.

Examples of Ineligible Incentive Payments

35. The following are examples of trade incentive payments which the Commissioner would not accept result in a reduction of the sale value of goods:

- . Promotional Rebate - Dependent on Advertising Expenditure, etc. : where a rebate is only payable if :
 - . a retailer incurs advertising, promotion or other marketing expenditure on a manufacturer's products;
 - . the rebate is calculated on the basis of a percentage of the retailer's expenditure on advertising, display etc.;
 - . no rebate is payable unless the agreed level of expenditure is reached; and
 - . there is no correlation between the amount of the rebate and the value or volume of the retailer's purchases of the manufacturer's products.
- . Promotional Rebate - Dependent on Retailer's Purchases : where a rebate is dependent on :
 - . a retailer advertising, displaying or otherwise promoting a manufacturer's or wholesaler's products;
 - . the rebate is calculated as a percentage of the retailer's purchases; and

- . is dependent on the retailer reaching an agreed level of purchases (even though there may be no direct correlation between the amount of the rebate and the amount spent by the retailer on advertising etc. and even though the retailer is not directed or controlled as to how or which goods are advertised, etc.)
- . Reimbursement of Retailer's Expenditure or Subsidies Given to Retailers for Expenditure Incurred :
 - . where on a consideration of all the particular circumstances which gave rise to the payment of the trade incentive and in which the incentive is calculated and made available to a retailer;
 - . where one or more of the features listed in paragraph 33 above are present; and,
 - . where the only reasonable conclusion to be drawn, irrespective of whether or not the payment is calculated on the basis of the value or volume of the retailer's purchases of goods, is that the payment really answers the description of a reimbursement of the retailer's promotional, display, etc. expenditure or a subsidy given to a retailer for expenditure incurred.
- . Promotional Rebate - Retailer Charging Set Fees :
 - . where allowances are given for advertising or promotional expenses which are based on a retailer charging set fees for particular advertising or promotional activity. (This is so notwithstanding the fact that the sum of these allowances paid in a year to the retailer does not exceed a previously agreed percentage of the value of sales in that year to the retailer.)

Section 12D of the Sales Tax Procedure Act

36. Finally, consideration has been given to the possible application of section 12D of the Sales Tax Procedure Act in relation to Taxation Ruling No. ST 2039. On critical reflection, ST 2039 did not adequately draw the necessary distinction between rebates or credits which the Commissioner would accept as effecting a reduction in the sale value of goods and reimbursements or subsidies given to retailers for their advertising or promotion expenditure.

37. ST 2039 clearly enough states that "allowances given for advertising expenses, etc. are not accepted as reducing the sale value of goods". However, this passage follows immediately on a statement that "a reduction in sale value only occurs where the rebate is attributable to the volume or value of the sales made to the retailer concerned". These two statements were meant to be read independently of one another. A reading of the two passages in conjunction with one another, however, could have misled some taxpayers to have claimed rebates of sales tax on allowances given for advertising expenses or promotion expenses merely because those allowances have been based on the volume or

value of sales made to the relevant retailer(s).

38. The mere fact that a trade incentive payment is based on the volume or the value of sales made to a retailer does not mean that the incentive necessarily effects a reduction in the sale value of the goods.

39. Nonetheless, where a taxpayer has acted in accordance with the above incorrect construction of ST 2039 section 12D will be applied to remit tax unpaid by the taxpayer or claimed by the taxpayer as a credit against tax payable - provided the taxpayer has not otherwise been given a further written ruling by the Taxation Office that corrects any such misunderstanding.

40. Where section 12D so operates to require the remission of unpaid tax in relation to ST 2039, the Commissioner is prepared to accept that the section will continue to apply to sales of goods that occur during a period of three full months commencing from the first day of the month after the close of the month in which this Ruling is issued. In such cases the date of effect of this Ruling is therefore effectively prospective. It does not extend, however, to any trade incentive payments made in circumstances to which section 12D does not apply.

41. Section 12D only applies to require the remission of tax unpaid. Neither section 12D nor any other provision in the sales tax law permits refunds of tax to be paid where in the past a taxpayer has paid the correct amount of tax on trade incentive payments.

42. Where :

- (a) a retailer has carried out some advertising or promotional activity on behalf of a manufacturer or wholesale merchant; and
- (b) the charge made by the retailer or the allowance paid by the manufacturer or wholesale merchant in respect of that activity was attributable to some factor other than the volume or value of sales by the manufacturer or wholesale merchant to the retailer (e.g. the level of the expenses incurred on that activity by the retailer),

the Commissioner does not accept that a taxpayer in this situation has acted in accordance with ST 2039, incorrectly construed or not, and section 12D would not apply to require any remission of unpaid tax.

43. Taxpayers who are in any doubt as to the effect (if any) that their trade incentive payments may have on the sale value of their products should contact their local Taxation Office for a ruling.

COMMISSIONER OF TAXATION
25 January 1990