


STD 98/5 - Promotional Rebates

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Sales Tax Determination

Title: Promotional rebates

Background

Taxation Ruling SST 6 *Sales tax: taxable value* was issued to help taxpayers determine the taxable value of goods. The Ruling also provides general guidelines for determining which trade incentive payments reduce the price and, therefore, the taxable value of goods sold. These trade incentive payments are referred to in this Determination as *eligible rebates*.

SST 6 makes it clear that to reduce the taxable value of goods sold, the rebate must relate to the sale and the selling price of the goods, so as to bring about a reduction in that price. The Ruling explains that rebates paid to subsidise, compensate or reimburse a purchaser for advertising expenditure undertaken on behalf of the supplier (commonly referred to as promotional rebates) do not reduce the taxable value of goods.

Common examples of promotional rebates include co-operative rebates, co-operative allowances, co-operative payments, advertising rebates and advertising allowances.

While SST 6 lists promotional rebates as an example of a trade incentive payment that does not reduce the taxable value of goods sold, the Ruling makes it clear that neither the form of the contract of sale, by itself, nor the name given to a particular incentive, determines the incentive's character if the actions of the parties or the circumstances surrounding its payment disclose a different character. What is required is an objective assessment of the intention of the parties in the light of all the circumstances.

This Determination outlines the factors that are relevant in determining whether promotional rebates paid or allowed by a supplier to a retailer are *eligible rebates*.

This Determination also addresses whether rebates, paid or allowed in addition to those provided by the terms of the contract of sale, can reduce the taxable value of goods sold and give rise to a credit entitlement for tax overpaid.

Where rebates are paid or allowed on dealings between parties who are not at arm's length, the calculation of the taxable value of goods is determined according to the principles set out in Chapter 5 of SST 6. Although this Determination does not specifically deal with rebates paid or allowed under non-arm's length arrangements, the factors relevant to determining whether they are eligible rebates are the same whether the rebates are given in arm's length or non-arm's length circumstances.

Issues

1. What factors are relevant in determining whether amounts described as promotional rebates are *eligible rebates*?
 2. How is the amount of sales tax included in an *eligible rebate* calculated?
 3. How does a rebate paid partly to reduce the price of goods and partly for some other purpose, affect the calculation of the taxable value?
 4. Can rebates paid in addition to or outside the terms of the contract of sale, reduce the taxable value of goods and give rise to credit entitlements?
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Decision

1. The intention of the parties to the contract of sale is the principal consideration in determining whether amounts described as promotional rebates reduce the price and, therefore, the taxable value of goods (that is, they are *eligible rebates*) or whether they are directed at some other end, for example, as payment or compensation for promotional activities.

The intention of the parties is objectively assessed having regard to:

- (a) written evidence of the obligations and expectations of each party to the contract; and
- (b) the actions or conduct of the parties in relation to their dealings with the goods.

Relevant written evidence may include:

- the contract of sale, including supporting documentation relating to the terms of trade;
- promotional plans drawn up by the parties;
- reports relating to the conduct of or monitoring of promotional activities;
- minutes of meetings between the supplier and the retailer;
- details of the calculation of the amount of the rebate; and
- relevant invoices, claim forms or credit notes.

Relevant actions or conduct may include:

- whether other rebates are paid;
- the actual promotions undertaken by the retailer;
- the degree of monitoring by the supplier of promotions undertaken by the retailer;
- any influence exerted by the supplier in relation to promotional activities undertaken by the retailer; and
- the accounting treatment of the payment in the financial records of each of the supplier and the retailer.

2. If incentives, such as trade discounts, are allowed at the time of the sale, sales tax is calculated on the reduced selling price.

Where *eligible rebates* are allowed after the goods have been invoiced, the calculation of the amount of sales tax included in the rebate is the same, regardless of the basis used to calculate the rebate.

The method for calculating the amount of tax included in any *eligible rebate* is as follows:

$$\text{actual amount of rebate} \times \frac{\text{the rate of tax}}{100 \text{ plus the rate of tax.}}$$

3. Rebates paid partly to reduce the price for which the goods are sold and partly for some other purpose, such as advertising, reduce the taxable value of goods to the extent that the rebate is paid to reduce the price. The apportionment of the rebate should be capable of being ascertained from the terms of the contract of sale.

If the contract does not specify the portion of the rebate allocated to price, the taxpayer is required to show the portion allocated to price is in accordance with the intentions of the parties at the time that the contract was made.

4. A rebate reduces the taxable value of goods only where it relates to the sale and the selling price of the goods so as to bring about a reduction in that price. In practical terms, the rebate must be paid either under the terms of the contract of sale so as to reduce the sale price, or be sufficiently proximate and connected to the sale of the goods as to affect the price of those goods.

Where the terms of the contract of sale do not address the nature of a particular rebate, the rebate is an *eligible rebate* giving rise to a credit entitlement for tax overpaid at time of sale, only where there was a realistic expectation by both parties that a portion of the price would be refunded. An example may be where the terms of the contract do not provide for a volume rebate but where, on the basis of previous dealings, each party has a reasonable expectation that a volume rebate will subsequently be paid or allowed if a specific target volume is reached or exceeded.

On the other hand, the terms of the contract may provide for the payment of an *eligible rebate* as a percentage of the tax exclusive selling price of the goods, but the parties may later agree to calculate the rebate as a percentage of the tax inclusive selling price. In this case, the further rebate cannot be said to arise under either the terms of the contract or from a realistic expectation of the parties. The further rebate is not an *eligible rebate* and there is no credit entitlement in relation to that amount.

Date of effect

This Determination is effective immediately. It applies to all promotional rebates given by suppliers to retailers.

Reasons

We have based our decision on the following case law:

EMI (Australia) Ltd v. FC of T 71 ATC 4112; (1971) 2 ATR 325

Under the sales tax legislation, sales tax is payable on specified assessable dealings on a value known as the taxable value. The taxable value prescribed for wholesale sales is the price (excluding sales tax) for which the goods were sold.

The term, 'the price for which the goods were sold', means the total amount the buyer promises, expressly or tacitly, to pay to get good title to the goods.

However, where the contract incorporates terms or conditions by which the purchaser promises to do something in addition to paying the money consideration (the 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 price for which the goods are sold'. 'The price for which the goods are sold' is the total of the money consideration and the value of the promise.

*Queensland
Independent
Wholesalers Limited v.
FC of T 91 ATC 4492;
(1991) 22 ATR 45;
Colgate Palmolive Pty
Ltd v. FC of T 98 ATC
4748; (1998) 39 ATR
235*

Payments made by a supplier that subsidise, compensate, reimburse, or reward a retailer for carrying out activities or performing services for the supplier, do not reduce the price for which the goods are sold since they are directed to some other end. For example, a retailer may carry out activities or perform services such as advertising, promotion, distribution or other marketing activities, accounting, bookkeeping or debt collection functions, or allow the supplier a right to use the retailer's premises or equipment for these activities.

*AAT Case 50/93 93
ATC 534; AAT Case
9138 (1993) 27 ATR
1038*

Not all agreements between the parties are included in a written contract. The written contract may cover certain elements, but there may exist other understandings, evidenced in other documents or in the conduct of the parties, that place an obligation on one or other of the parties. The specific terms of any contract of sale between the parties are critical in determining the taxable value. However, the form of the contract of sale does not, by itself, determine whether promotional rebates can be deducted from the stated selling price of the goods to calculate the taxable value. Neither do the terms adopted by one or both of the parties to describe a particular incentive, determine the character of the incentive if the actions of the parties or the circumstances disclose a different character.

Where the facts show that a rebate has been paid to subsidise, compensate, reimburse, or reward a retailer for carrying out activities or performing services for the supplier, the rebate does not reduce the selling price and is not an *eligible rebate*.

Promotional rebates
Advertising rebates
Co-operative
advertising rebates

Such a situation may arise where a supplier agrees, under the terms of the contract, to pay a retailer an allowance for promotional activities. There may be no requirement for the retailer to provide the supplier with any evidence of the promotional activities undertaken or even to conduct these promotions. However, there may be an understanding that the retailer will promote the supplier's products by displaying the product in a prominent position and/or by advertising the product. Rebates of this kind do not reduce the taxable value of goods sold.

Although there may be no stipulation in the contract for the retailer to carry out the promotional activities, the supplier will usually have a system in place to monitor the promotional activities, indicating an implied obligation.

Suppliers have argued that payments of promotional rebates to retailers are no more than volume rebates with no strings attached, made according to long-standing commercial practice and expectation. They argue that the fact that the retailer may choose to conduct promotional activities does not alter their purpose, which is to reduce the price and, therefore, the taxable value of the goods.

However, whether a promotional rebate reduces taxable value needs to be objectively determined, having regard to the intentions of the parties in the light of all the circumstances. If the actions or conduct of the parties, viewed objectively, lead to a conclusion that the rebate is not directed at price reduction but at some other end, such as advertising, the payment is not an *eligible rebate*.

Rebates partly directed
to some other end

In some situations, the parties to a contract of sale of goods may agree to the future payment of an all inclusive rebate subject to a variety of conditions. Some part of the rebate may relate to factors that reduce the taxable value of the goods, such as reward for achieving a target volume. Another part of the rebate may be directed at some other end that does not reduce the taxable value, such as compensation for undertaking particular promotional activities.

For example, the terms of the contract may provide for the payment of, say, a 5% rebate. The first 3% of the rebate is subject to a certain target volume being reached and the additional 2% is for providing end-of-aisle display space to promote the supplier's product.

As explained in SST 6, where rebates are partly directed to some other end, that part does not reduce the price for which the goods were sold or the taxable value.

In such situations, the supplier is required to establish the portion of the rebate that is an *eligible rebate*. This may be difficult to establish if the allocation is not provided for under the terms of the contract of sale.

Suppliers involved in such arrangements should ensure that the apportionment of rebates between 'eligible' and 'ineligible' purposes is clearly reflected by the terms of the contract of sale.

*Rebates contracted
outside or separate
from the sale*

Eligible rebates given by a supplier to a retailer reduce the 'price for which the goods are sold' provided they arise under the terms of the contract of sale, or from a realistic expectation in existence at the time of purchase, that some portion of the price would be refunded in future. Although the actual amount of the rebate may have been unknown, a realistic expectation of such a rebate at the time of purchase will have influenced the price negotiations. Therefore, the subsequent payment or allowance of the rebate is sufficiently proximate and connected to the sale of goods to be regarded as affecting the price.

Situations may arise where a supplier and a retailer agree to a rebate, to be calculated on the basis of the tax exclusive selling price and to be paid at some future point in time. Later, the supplier and retailer decide to recalculate the rebate on the tax inclusive selling price. The further or additional rebate is then paid to the retailer.

In the event that the rebate is a payment that reduces taxable value, the supplier is entitled to a credit for the sales tax component of the earlier rebate given. However, the supplier is not entitled to a credit in respect of the later rebate. At the time the contract of sale was entered into, there was no realistic expectation by the parties that the price of the goods would be reduced by the additional rebate. Therefore, its subsequent payment cannot be taken to effect a reduction in the taxable value of the goods.

Examples of calculation of sales tax included in an *eligible rebate*

Example 1. Rebate calculated on a tax exclusive basis

The amount of the *eligible rebate* calculated under the terms of the contract is 10% of the tax exclusive selling price, i.e., the price before sales tax is included.

Assuming the tax exclusive selling price is \$500 and the goods are subject to tax at the rate of 22%, the *eligible rebate* and the amount of tax overpaid is calculated as follows:

| | |
|--------------------------------|-------|
| Tax exclusive selling price | \$500 |
| Sales tax | \$110 |
| Tax inclusive selling price | \$610 |
| Eligible rebate (10% of \$500) | \$50 |
| Adjusted price | \$560 |

Calculation of sales tax credit:

$$\$50 \quad \times \quad \frac{22}{122} \quad = \quad \$9.01$$

The rebate of \$50 includes a price reduction of \$40.99 and a sales tax credit of \$9.01.

Example 2. Rebate calculated on a tax inclusive basis

The amount of the *eligible rebate* calculated under the terms of the contract is 10% of the tax inclusive selling price, i.e., the price including sales tax.

Using the facts outlined in **Example 1**, the *eligible rebate* and the amount of tax overpaid is calculated as follows:

| | |
|--------------------------------|-------|
| Tax exclusive selling price | \$500 |
| Sales tax | \$110 |
| Tax inclusive selling price | \$610 |
| Eligible rebate (10% of \$610) | \$ 61 |
| Adjusted price | \$549 |

Calculation of sales tax credit:

$$\$61 \quad \times \quad \frac{22}{122} \quad = \quad \$11$$

The *eligible rebate* of \$61 includes a price reduction of \$50 and a sales tax credit of \$11.

If the contract between the parties provides that the *eligible rebate* is to be calculated on the tax exclusive selling price (\$50) and it is subsequently calculated on the tax inclusive selling price (\$61), the further amount of rebate (\$11) does not give rise to a credit for sales tax claimed to be overpaid (\$1.99).

However, a credit is allowable if the claimant can show that at the time the contract of sale was entered into, the parties intended that the price of the goods would be reduced by the payment of a further rebate.

Communication of the Decision This Determination has been made available for publication by the sales tax publishing houses.

Commissioner of Taxation

26 August 1998

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Related Determinations:

Related Rulings: SST 6

Subject Ref: advertising rebates; co-operative rebates; promotional rebates; trade incentive payments

Legislative Ref:

Case Ref: EMI (Australia) Ltd v. FC of T 71 ATC 4112; (1971) 2 ATR 325; Queensland Independent Wholesalers Limited v. FC of T 91 ATC 4492; (1991) 22 ATR 45; Colgate Palmolive Pty Ltd v. FC of T 98 ATC 4748; (1998) 39 ATR 235; AAT Case 50/93 93 ATC 534; AAT Case 9138 (1993) 27 ATR 1038

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