

**ALABAMA DEPARTMENT OF REVENUE  
REVENUE RULING 02-007**

**This document may not be used or cited as precedent. Code of Ala. 1975, §40-2A-5(a).**

TO:

FROM:       Commissioner of Revenue  
              Alabama Department of Revenue

DATE:        January 17, 2003

RE:         The liability of tobacco tax when there is a change in who receives replacement products and the entitlement of tobacco tax credits.

Dear Sir:

Taxpayer A, a foreign corporation, is engaged in the promotion and sale of smokeless tobacco products in the State of Alabama. Taxpayer A is planning to change its current procedures in which it processes replacement and returned tobacco products. Instead of Taxpayer A allowing its sales representatives to exchange products with wholesale distributor customers and allowing the wholesale distributor customers to ship the returned tobacco products back to the manufacturer, Taxpayer A plans to now allow the sales representatives to ship the returned products directly to the manufacturer.

**ISSUES**

In your request for a Revenue Ruling you have asked for the Alabama Department of Revenue's ("Department") position concerning the following issues:

1.       Whether, under Taxpayer A's Proposed Change, Taxpayer A is liable for the tobacco products tax when replacement product is received by its Sales Representatives ("Sales Reps")?
  
2.       Whether, under Taxpayer A's Proposed Change, Taxpayer A is entitled to receive credits for the taxes paid on products returned by its Sales Reps?

## FACTS

### **The facts as stated by Taxpayer A, as a subsidiary of Parent:**

#### Current Returned Goods Procedures

Taxpayer A holds a valid Occupational License in a County in Alabama. Most of Taxpayer A's customers are licensed wholesale distributors who resell the products to retailers and remit the tax on tobacco products. Taxpayer A purchases the tobacco products exclusively from U.S. Smokeless Tobacco Manufacturing Limited Partnership ("Taxpayer B"). Both Taxpayer A and Taxpayer B are wholly owned subsidiaries of Parent.

Taxpayer A employs sales representatives ("Sales Reps"), who act as representatives for the Company. These Sales Reps, furnished with company cars and a supply of stock ("car stock"), provide a service on behalf of its distributors by traveling to retail customers to sample and otherwise promote the sale of the Company's tobacco products and to regularly replace outdated or damaged products ("returned products") with car stock. Returned products are accumulated by Sales Reps and periodically exchanged for an equivalent amount of fresh products ("replacement products") through certain of the Company's wholesale distributor customers ("Central Service Jobbers" or "CSJs"). CSJs ship returned products back to Taxpayer B's manufacturing facility where Taxpayer B accepts such products on behalf of Taxpayer A and issues affidavits of their return to the CSJ and Taxpayer A. Taxpayer A then issues a refund or credit to the CSJ for the original purchase price of the tobacco products. Currently, CSJs pay the tobacco tax on replacement products and obtain a credit of tax paid on replacement products and obtain a credit of tax paid on returned products. Taxpayer A pays the tobacco tax on the initial issuance of car stock at the time it is first received by Sales Reps.

#### Proposed Changes to Returned Goods Procedures

Taxpayer A is considering changing the manner in which it processes replacement and returned products (the "Proposed Change"). Sales Reps will continue to replace outdated or damaged products. Under the Proposed Change, however, Sales Reps (not CSJs) will ship returned products directly to Taxpayer B's manufacturing facility. Taxpayer B will accept such products on behalf of Taxpayer A and issue affidavits of their return solely to Taxpayer A. Furthermore, under the Proposed Change, Sales Reps will order replacement products (in order to replenish their car stock) directly from Taxpayer A rather than through a CSJ. Taxpayer A will accordingly ship replacement products directly to the Sales Reps.

Note, Taxpayer A will ship car stock to locations where Taxpayer A rents warehouse space for Sales Reps pickup. These locations for the most part coincide with our distributors' locations.

Under the Proposed Change, Taxpayer A will separately account for each transaction (i.e., the sale of replacement product and the credit sale of returned product) on its books and records. Note that although a Sales Rep exchanges tobacco products on a can-for-can basis, a Sales Rep's order of replacement stock will generally not equal the number of cans returned at any point in time. This difference, which is due primarily to timing, may result in a net tax liability or credit in any particular tax reporting period. For example, a Sales Rep may order two cases of replacement product on December 31<sup>st</sup> but not ship two cases of returned products back to the manufacturer until the following month when he accumulates a substantial quantity of products to return. Consequently, should these be the only transactions that occur within these respective monthly tax reporting periods, a tax would be due in December and an equal amount of tax would be credited in January.

Note that under the Proposed Change, CSJs will no longer be paying tax on replacement products ordered by a Sales Rep or filing for tax credits on products returned by a Sales Rep since the new process will not involve the CSJ.

## **ANALYSIS OF ALABAMA LAW**

### Tax Liability

In addition to all other taxes of every kind now imposed by law, every person, firm, corporation, club or association, within the State of Alabama, who sells or stores or receives for the purpose of distribution to any person, firm, corporation, club or association within the State of Alabama, cigars, cheroots, stogies, cigarettes, smoking tobacco, chewing tobacco, snuff, or any substitute therefor, either or all, shall pay to the State of Alabama for state purposes only a license or privilege tax which shall be measured by and graduated in accordance with the volume of sales of such person, firm, corporation, club or association in Alabama. (Code of Alabama "Code" §§ 40-25-2(a)).

Currently, CSJ pays the tobacco tax on the replacement product. Under the provisions of the Proposed Change, the Sales Reps will now return the products to and the replacement products will be ordered directly from Taxpayer A (not the CSJs). Consequently, when a Sales Rep receives replenishment product for the purpose of exchanging such product for outdated product, Taxpayer A would be "receiving" such tobacco products for the purpose of distribution and would be subject to the State of Alabama tobacco products tax. All applicable County taxes would also be due at the point the products are placed with retailers.

### Credit and/or Refund Entitlement

Pursuant to Code of Ala. 1975, § 40-2A-7(c)(1), "Any Taxpayer may file a petition for refund with the department for any overpayment of tax or other amount erroneously paid to the department or concerning any refund, which the department is required to

administer..." The following documentation is to be submitted to the Department of Revenue by any wholesale dealer of tobacco products in applying for a tobacco tax refund: (1) The original affidavit from the manufacturer certifying as to the tobacco products received, listing these in detail, and also certifying that the required Alabama stamps were fixed and that the stamps have been destroyed. (2) A copy of the credit memorandum from the manufacturer showing the merchandise returned. (3) A copy of the wholesale dealer's invoice to the manufacturer showing in detail the tobacco products returned and the tax value of these tobacco products. (Alabama Regulation, 810-7-1-.02).

Joint petitions for refund must be filed for taxes in which the Taxpayer collects and remits the tax on behalf of the purchaser/consumer. Such taxes include, but may not be limited to the following: sales or use taxes, public utilities taxes, and any transient occupancy tax. Joint petitions for refund should include the following:

- (a) a written statement that the Taxpayer And the consumer/purchaser are requesting a refund, such statement must be signed by both the Taxpayer And the consumer/purchaser;
- (b) the Taxpayer's and the consumer's/purchaser's names, social security number or FEIN, and addresses;
- (c) the type of tax;
- (d) the tax periods or years involved;
- (e) the amount of refund requested;
- (f) a statement of the relevant facts and the reason the payment was erroneous; and
- (g) an attachment of any documentation sufficient to provide proof of an erroneous payment. (Examples of documentation may include: invoices, receipts, check copies, accrual records, copies of returns, etc.)

(Alabama Regulation, 810-14-1-.18(3)).

Since CSJs currently pay the tobacco tax, they receive a credit. Therefore, there is a direct relationship between paying the tax and receiving the credit for any overpayment of tax or other amount erroneously paid to the department in Alabama. Because of the Proposed Change, Taxpayer A will be required to pay the tobacco products tax on replacement products; therefore, it should be entitled to a credit for damaged and outdated tax-paid products received from retailers and returned to the manufacturer through its Sales Reps in exchange for such replacement product. The credits, however, will only be allowed up to the amount of the corresponding tobacco tax payable for a given month.

If the amount of credits exceeds the corresponding amount of the tobacco tax payable for a given month, then credits will not be allowed which exceed the taxes. If Taxpayer A's credits exceed its amount of tobacco tax paid to the Department, Taxpayer A and CSJs will be required to file a Joint Petition for refund.

**RULING**

Based upon an analysis of Alabama's laws and regulations, it is the position of the Department of Revenue that Taxpayer A will be liable for the State of Alabama tobacco products tax at the time of receipt because Taxpayer A would be "receiving" such tobacco products for the purpose of distribution. Taxpayer A will also be liable for all applicable County taxes at the point the tobacco products are placed with retailers. Taxpayer A is also entitled to receive credits for taxes Taxpayer A has paid on products returned by its Sales Reps. For any credits that exceed the amounts of corresponding taxes actually payable for a given month, a Joint Petition for refund should be filed and the requirements must be met in order for Taxpayer A to receive credits.

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Cynthia Underwood,  
Commissioner  
Department of Revenue

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