

PRIVATE TAXPAYER RULING LR02-014

September 6, 2002

The following private taxpayer ruling is in response to your letter dated July 18, 2002. You have requested a ruling on behalf of . . . regarding the Arizona luxury privilege tax ("luxury privilege tax") implications on replacement products as well as the availability of refunds for tobacco products returned to the manufacturer.

Statement of Facts:

. . . is engaged in the promotion and sale of smokeless tobacco products in the State of Arizona and elsewhere throughout the United States. . . . holds a valid Arizona tobacco distributor's license. Most of . . . 's customers are licensed wholesale distributors who resell the products to retailers and remit the tax on tobacco products. . . . purchases the tobacco products exclusively from Both . . . and . . . are wholly owned subsidiaries of

Currently, . . . employs sales representatives ("Sales Reps"), who act as representatives for the Company. These Sales Reps are furnished with company cars and a supply of stock ("car stock"). They 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to retail customers to sample and otherwise promote the sale of the Company's tobacco products and to regularly replace outdated or damaged products ("returned products") with car stock.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 Company wholesale distributor customers ("Central Service Jobbers" or "CSJs"). CSJs ship returned products back to . . . 's manufacturing facility where . . . accepts such products on behalf of . . . and issues affidavits of their return to the CSJ and then issues a refund or credit to the CSJ for the original purchase prices of the tobacco products. To date, . . . pays the luxury privilege tax on the initial issuance of car stock at the time it is first received by the Sales Reps. CSJs pay the luxury privilege tax on replacement products and obtain a credit for tax paid on returned products.

. . . is considering changing the manner in which it processes replacement and returned products ("Proposed Change"). Under the Proposed Change, Sales Reps will continue to replace outdated or damaged products with their available car stock; however, Sales Reps, rather than CSJs, will ship returned products directly to . . . 's manufacturing facility. . . . will accept such products on behalf of . . . and issue affidavits of their own solely to Further, under the Proposed Change, Sales Reps will order replacement products, to replenish their car stock, directly from . . . rather than through a CSJ. Essentially, the new process will no longer involve the CSJ. Accordingly, . . . will ship replacement products directly to the Sales Reps.

Under the Proposed Change, . . . will separately account for the sale of replacement product and the credit sale of returned products on its books and records. Although Sales Reps exchange 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 one point in time. This is a timing issue, which may result in a tax due in one month and a refund of an equal amount due in another month.

Issues:

1. Under the Proposed Change, is . . . liable for the luxury privilege tax on replacement products received by Sales Reps?
2. Under the Proposed Change, is . . . entitled to receive a refund for the taxes paid on products returned by its Sales Reps?

Your Position:

It is your position that . . . is liable for luxury privilege tax on car stock shipped to Sales Reps used to replace outdated or damaged products. Therefore, . . . should be entitled to a refund for damaged and outdated products returned to the manufacturer on which tax was previously paid.

Applicable Law:

Arizona Revised Statutes ("A.R.S.") § 42-3001(5) defines "distributor" to include any person who manufactures, produces, ships, transports or imports into this state or in any manner acquires or possesses for the purpose of making the first sale of cigars or other tobacco products upon which the taxes have not been paid as required by this chapter.

A.R.S. § 42-3001(11) defines "person" as "any individual, firm, partnership, joint venture, association, corporation, municipal corporation, estate, trust, club, society or other group or combination acting as a unit...."

A.R.S. § 42-3001(8) defines "first sale" as the first sale or distribution in intrastate commerce or the first use or consumption of cigarettes, cigars or other tobacco products.

A.R.S. § 42-3008 states that tax imposed under the luxury privilege tax upon any articles or substances shall be refunded when the luxury becomes unfit for sale due to breakage or spoilage.

A.R.S. § 42-3051 levies luxury privilege tax "on all cigarettes, cigars, smoking tobacco, plug tobacco, snuff and other forms of tobacco."

A.R.S. § 42-3251 levies luxury privilege tax on smoking tobacco, snuff, fine cut chewing tobacco, cut and granulated tobacco, shorts and refuse of fine cut chewing tobacco, and refuse, scraps, clippings, cuttings and sweepings of tobacco used exclusively for agricultural or horticultural purposes and unfit for human consumption.

Discussion:

Arizona imposes a tax on the sale of cigarettes and other tobacco products in the state. A.R.S. §§ 42-3001 through 42-3406. Tobacco products include cigarettes, smoking tobacco, snuff, fine cut chewing tobacco, cut and granulated tobacco, refuse, scrap, clippings and sweepings of tobacco, cavendish, plug, twist tobacco, and cigars. Pursuant to A.R.S. § 42-3201 distributors selling or offering for sale any tobacco product shall obtain a license to sell tobacco. The license shall be nontransferable, shall be valid for one year unless earlier revoked by the department, and shall be displayed in the applicant's place of business. A.R.S. § 42-3201.

A distributor is defined as "any person who manufactures, produces, ships, transports ... or in any manner acquires or possesses for the purpose of making the first sale of ... tobacco products upon which the taxes have not been paid as required by this chapter." A.R.S. § 42-3001(5). For purposes of luxury privilege tax a person is "any individual, firm, partnership, joint venture, association, corporation, municipal corporation, estate, trust, club, society or other group or combination acting as a unit...." A.R.S. § 42-3001(11).

Based on the information provided in your request, . . . is a licensed distributor engaged in the promotion and sale of smokeless tobacco products in the State of Arizona. Under the Proposed Change, . . . will continue to pay the luxury privilege tax on the initial issuance of car stock at the time it is first received by the Sales Rep. In addition, it will directly ship replacement products to its Sales Reps to replenish their car stock. As a result, . . . is liable for luxury privilege tax on the replacement products it ships to the Sales Reps to replace damaged or outdated products at retailer locations.

Accordingly, . . . is entitled to a refund for damaged or outdated products returned to the manufacturer in exchange for replacement products. Pursuant to A.R.S § 42-3008 the tax imposed upon tobacco products shall be refunded when the amount of the tax has been paid and when the luxury becomes unfit for sale due to breakage or spoilage.

Conclusion and Ruling:

The following ruling is based on the facts presented in your request. The department rules that . . . is liable for the luxury privilege tax on replacement products and is entitled to a refund for returned products that are unfit for sale due to breakage or spoilage.

The conclusions in this private taxpayer ruling do not extend beyond the facts presented in your letter dated July 18, 2002, and subsequent information received July 29, 2002.

This response is a private taxpayer ruling and the determinations herein are based solely on the facts provided in your request. The determinations are subject to change should the facts prove to be different on audit. If it is determined that undisclosed facts were substantial or material to the department's making of an accurate determination, this taxpayer ruling shall be null and void. Further, the determination is subject to future change depending on changes in statutes, administrative rules, case law or notification of a different department position.

The determinations in this private taxpayer ruling are only applicable to the taxpayer requesting the ruling and may not be relied upon, cited nor introduced into evidence in any proceeding by a taxpayer other than the taxpayer who has received the private taxpayer ruling.