

**JURISDICTION:** OKLAHOMA TAX COMMISSION - DECISION  
**CITE:** 2000-08-29-015 / PRECEDENTIAL  
**ID:** JM980001  
**DATE:** 08-29-00  
**DISPOSITION:** FINDINGS OF A VIOLATION / LICENSE NOT REVOKED  
**TAX TYPE:** CIGARETTE TAX  
**APPEAL:** OK SUP CT 95,241 / OTC DECISION AFFIRMED

### FINDINGS OF FACT AND CONCLUSIONS OF LAW

1. AN AUDITOR with the Division, testified that she investigated a complaint against RESPONDENT. Pursuant to the investigation, THE AUDITOR reviewed copies of invoices from the cigarette wholesaler which set forth the price per carton of the cigarettes purchased by Respondent. In reaching her conclusion regarding Respondent's basic cost or minimum price, THE AUDITOR stated that she subtracted from the invoice price, buy-down amounts elicited from a letter from MR. ANONYMOUS and the applicable damage credits for the different types of cigarettes, i.e., major and generic brands, reflected on the face of the invoices to arrive at the basic cost of the cigarettes. The auditor multiplied that amount by 6% and added the resulting amount, as the cost of doing business, to arrive at the cost to the retailer or minimum price for which a particular brand of cigarettes could be sold. The auditor reviewed Respondent's advertisements to determine the prices of the cigarettes Respondent sold. As a result of the comparison, the auditor concluded that respondent was in violation of the Unfair Cigarette and Tobacco Products Sales Act ("Act").

2. The period audited was March 16; 1998, to April 4, 1998.

3. The auditor stated that she did not take into account monthly amounts received by Respondent for promotional services in the calculation of minimum price.

4. Cigarette manufacturers make different type of discounts available to retailers. A "buy-down" (described as a promotional amount in the MR. ANONYMOUS letter) is a specific amount per carton of cigarettes paid by the manufacturer to the retailer, who in turn reduces the price per carton charged the consumer by the amount received. The amount given per carton varies between manufacturers and is given for a specific time period or number of units.

5. A "damage credit" is given by the wholesaler to offset losses for damaged products or other casualties suffered by the retailer.

6. The damage credit is subtracted from the invoice price for determining compliance with the Act.

7. The various manufacturers also pay a promotional service discount commonly referred to as "shelf rent". Shelf rent is paid to the retailer by the manufacturer through a rebate program as a reward to the retailer for having a contract with the manufacturer. Shelf rent is calculated by the manufacturer based on the number of units on the shelves in a particular store, the volume of a store's sales, the percentage of the store dedicated to a particular brand, display of advertising in the store and the placement of advertising and products within the store.

8. The shelf rent rebate is not considered to be a trade discount by the Division and was therefore not subtracted from the invoice price for the audit of the Respondent.

9. In its audit, the Division used a damage credit of fifty cents (50¢) per carton for generic brands and fifty-five cents (55¢) per carton for major brands. The evidence shows that Respondent actually receives a credit of fifty-five cents (55¢) per carton for generic brands and sixty-five cents (65¢) per carton for major brands.

10. Respondent's cigarette prices per carton for the audit period are as follows:

Brand	Invoice Cost	Damage Credit	Manuf. Buy-down	6% Operating Cost	Minimum Price	Advertised Price
Camel	16.08	0.65	2.50	0.78	13.71	13.45
Doral	13.30	0.55	3.00	0.59	10.34	10.29
Salem	16.08	0.65	4.00	0.69	12.12	11.95
Winston	16.08	0.65	2.50	0.78	13.71	13.45
Marlboro	16.08	0.65	2.50	0.78	13.71	13.45

11. Even considering the greater amount of damage credits, Respondent's prices are below the minimum prices allowed by the Act.

12. Respondent's accountant testified that during the audit period Respondent received an average amount of \$1.61 per carton of cigarettes for shelf rent.

## ISSUES AND CONTENTIONS

Whether Respondent's advertised prices violate the provisions of the Unfair Cigarette and Tobacco Products Sales Act. 68 O.S. § 326, *et seq.*

2. Whether the shelf rent promotional discount may be subtracted from the cost to the retailer when determining compliance with the Act.

The Complainants contend that shelf rent is an amount paid the retailer for display, advertising and other promotional purposes and thus not deducted from the cost to the retailer pursuant to Section 337 of Title 68. Respondent contends that shelf rent is a trade discount and should be subtracted from the retail price for determining compliance with the Act. When shelf rent is factored into the calculation, Respondent contends that it is well within the limits imposed by the Act: Respondent argues that shelf rent and "buy-downs" are both considered to be promotional discounts by the manufacturer and, therefore, should be treated the same. However, under the Division's interpretation, a buy-down is a trade discount, while shelf rent is not.

## APPLICABLE LAW

The pricing of cigarettes is regulated by the Unfair Cigarette and Tobacco Product Sales Act. 68 O.S. § 326, *et seq.* The Tax Commission is authorized to adopt necessary rules and regulations to administer and enforce the provisions of the Act. 68 O.S. § 344. The Commission may revoke or suspend a license issued under the Act of any person who fails to comply with any provision or any rule or regulation promulgated thereunder. *Id.* The Act makes it a misdemeanor for a retailer or wholesaler to advertise, sell, or offer to sell cigarettes at a price less than the cost to the retailer or wholesaler, with the intent to injure competitors or lessen or substantially destroy competition. 68 O.S. § 328.<sup>1</sup>

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<sup>1</sup> 68 O.S. §328 provides in pertinent part:

It shall be unlawful for any retailer or wholesaler, with intent to injure competitors or destroy or substantially lessen competition, to advertise, offer to sell, or sell, at retail or wholesale, cigarettes and tobacco products at less than cost to such retailer or wholesaler, as the case may be. Any retailer or wholesaler who violates the provisions of this section shall be guilty of a misdemeanor and be punishable by fine of not more than Five Hundred Dollars (\$500.00).

Evidence of advertisement, offering to sell, or sale of cigarettes and tobacco products by any retailer or wholesaler at less than cost to him as defined in this Act shall be prima facie evidence of intent to injure competitors and to destroy or substantially lessen competition.

Evidence of sale or advertising to sell at less than cost is prima facie evidence of intent to injure competition. *Id.* Cost to the retailer is defined as the basic cost of the cigarettes plus the cost of doing business. 68 O.S. § 330<sup>2</sup>. Where there is no evidence of a lesser amount, the cost of doing business is presumed to be 6% of the basic cost of the cigarettes to the retailer. *Id.* The "basic cost of cigarettes" is defined as the invoice cost of cigarettes or replacement cost of cigarettes, whichever is lower, within thirty days prior to the date of sale "less any trade discounts." 68 O.S. § 327(m). "Merchandise given gratis or payment made to a retailer or wholesaler for display, or advertising, promotion purposes, or otherwise, shall not be considered in determining the cost of cigarettes and tobacco products to the retailer or wholesaler." 68 O.S. § 337.

Resolution of this case hinges on the meaning of "trade discount". Trade Discount is not defined in the Act or in the rules promulgated to implement the statutory scheme. When a word is not defined by statute, it is appropriate to interpret the word in accordance with its ordinary, everyday meaning. *U.S. Dept. Of Labor v. Elledge*, 614 F.2d 247 (10th Cir. 1980). "Trade Discount" is defined in Black's Law Dictionary 1457 (6th ed. 1990) as:

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<sup>2</sup> 68 O.S. § 330 provides in pertinent part:

The term "cost to the retailer" shall mean the "basic cost of cigarettes and tobacco products" to the retailer plus the "cost of doing business by the retailer", as evidenced by the recognized statistical and cost accounting practices in allocation of overhead costs and expenses, paid or incurred, and must include, without limitation, labor (including salaries or drawing accounts of owners, salaries of executives and officers, or general and special allocations and charges made by parent organizations), rent, depreciation, selling costs, maintenance of equipment, delivery costs, all types of licenses, taxes, insurance, and advertising, and any other cost: Provided, that any retailer who, in connection with the retailer's purchase, receives not only the discounts ordinarily allowed upon purchases by a retailer but also, in whole or in part, discounts ordinarily allowed upon purchases by a wholesaler, shall, in determining "cost to the retailer". Pursuant to this subsection, add the "cost of doing business by the wholesaler", as defined in Section 4 of this Act, to the "basic cost of cigarettes and tobacco products" to said retailer, as well as the "cost of doing business by the retailer".

In the absence of proof of a lesser cost of doing business by the retailer making the sale, the "cost of doing business by the retailer" shall be presumed to be six percent (6%) of the "basic cost of cigarettes and tobacco products" to the retailer, plus cartage to the retail outlet if performed or paid for by the retailer (and not previously included in the charge by the wholesaler), which cartage cost, in the absence of proof of a lesser cost, shall be deemed to be three-fourths of one percent (3/4 of 1%) of the basic cost of cigarettes and tobacco products to the retailer.

A discount from list price offered to all customers of a given type; e.g. discount offered by lumber dealer to a building contractor. Contrast with a discount offered for prompt payment and quantity discount.

The Tax Commission, as an administrative agency, is not empowered to decide the constitutional validity of statutes. *Dow Jones & Company, Inc. v. Oklahoma Tax Commission*, 787 P.2d 843, 845 (Okl. 1990). The challenged statute is deemed constitutionally valid until a court of competent jurisdiction declares otherwise. See *State ex rel. York v. Turpen*, 681 P.2d 763, 767 (Okl. 1984). Accordingly, the constitutionality of the Act, as raised by the Respondent, will not be addressed.

### CONCLUSIONS OF LAW

1. The Tax Commission has jurisdiction over the parties and subject matter of this hearing. 68 O.S. § 344.

2. The license of a cigarette retailer may be suspended or revoked for refusing or neglecting to comply with any provisions of the Act. 68 O.S. § 326 et seq.

3. A buy-down is a trade discount and should be subtracted from the invoice price to determine the basic cost of cigarettes. A buy-down is distinguishable from shelf rent because it is a discount offered by the manufacturer to the retailer to lower prices in order to make its products more attractive to the consumer.

4. Shelf rent on the other hand, is a reward paid to the retailer for promotional functions performed by the retailer. It falls clearly within the category of "payment made to the retailer . . . for display, or advertising, promotion purposes, or otherwise . . . ." which is explicitly excluded from consideration in determining the cost of cigarettes to the retailer. 68 O.S. § 337. Shelf rent is not a trade discount and therefore, not considered for determining compliance with the Act.

5. Respondent's advertised prices are below the minimum price allowed by the Act and are prima facie evidence of Respondent's intent to injure competition. 68 O.S. § 328(b).

6. Respondent was in violation of the Act during the audit period. However, the facts and circumstances of this case do not warrant the revocation or suspension of Respondent's cigarette license since the operative term trade discount was not defined in the Act or by Commission rules nor were there any policy statements pertaining to the interpretation and treatment of trade discounts.

**DISPOSITION**

It WAS DETERMINED that the Tax Commission, under the discretionary authority of the Act, refrain from taking any action of revoking or suspending the license of Respondent, upon the complaint of Complainants. It WAS further DETERMINED that Respondent be put on notice that any similar violations of the provisions of the Act subsequent to the issuance of this decision shall result in the imposition of a sanction authorized by Section 344.

**OKLAHOMA TAX COMMISSION**