[Date]

[Name]
[Company]
[Address]
[Address]

Re: Formal Ruling 14-__

Dear [Taxpayer]:

This is a formal ruling for your company, ("Taxpayer"), regarding the applicability of Vermont use tax to free samples Taxpayer distributes from alcoholic beverages it manufacturers. This ruling is based upon representations in your letter of April 17, 2013 (received in this office by email on February 10, 2014), and our telephone conversation of February 26, 2014.

RULING

Based upon the facts presented, Taxpayer would be liable for use tax on free samples it distributes from the alcoholic beverages it produces.

FACTS

Taxpayer is a Vermont distillery which is licensed by Vermont to distill and rectify alcoholic beverages. Taxpayer manufactures blends of various spirituous liquors to create products such as [product name] and [product name]. Taxpayer provides free one-half ounce samples of its products to potential customers and others. You have asked for a ruling on whether Taxpayer is liable for use tax on the free samples it provides.

DISCUSSION

1. Meals and rooms tax - the tax does not apply to a free sample.

Vermont's "Meals and Rooms Tax" laws, in Chapter 225 of Title 32, actually impose not two, but three separate taxes: (1) the rooms tax, on the rent for a hotel "occupancy," (2) the meals tax, on the charge for a "taxable meal," and (3) the alcoholic beverage tax, on the charge for a serving of an "alcoholic beverage." 32 V.S.A. Chapter 225, § 9241(a), (b), (c).

The "alcoholic beverage tax" is found in Section 9241(c) of that chapter. It applies to each "sale" of a serving of an alcoholic beverage, and the tax applies to the "total charge" for the drink. 32 V.S.A. § 9241(c). "Alcoholic beverages" for this purpose are defined as "any malt beverages, vinous beverages, or spirituous liquors" served by a first- or third-class liquor-licensee. 32 V.S.A. § 9202(11). If an alcoholic beverage is given away as a free sample, there is no "sale" of the beverage, and no "charge" for the drink, so no alcoholic beverage tax would be due.

2. Meals and rooms tax - "alcoholic beverage" is not a "meal".

The "meals tax" is found in Section 9241(b) of Chapter 225. A "taxable meal" is any "food or beverage" served by a restaurant. 32 V.S.A. § 9202(10). The phrase "food or beverage" means any food or drink "except alcoholic beverages." 32 V.S.A. § 9202(12). Since a "taxable meal" is "food or beverage," and "food or beverage" excludes "alcoholic beverages," an alcoholic beverage cannot be a "taxable meal" and is therefore not subject to the meals tax. This point is important for the next portion of the analysis, under the sales and use tax laws:

3. Sales and use tax - "meals" exemption does not apply to "alcoholic beverages".

Vermont sales and use tax laws are found in Chapter 233 of Title 32. The sales tax is imposed on retail sales of tangible personal property. 32 V.S.A. § 9771(1). The use tax is

imposed on (among other things) uses of tangible personal property by the manufacturer of that property (with certain exceptions, discussed below). 32 V.S.A. § 9773(2).

The sales and use tax does not apply to "sales of meals taxed or exempted under chapter 225." 32 V.S.A. § 9741(10). You have asked whether this "meals" exemption would apply to Taxpayer's free samples. Since a "meal" under chapter 225 excludes alcoholic beverages, this sales and use tax exemption for "meals taxed or exempted" does not apply to alcoholic beverages. Thus, alcoholic beverages are subject to the sales and use tax, unless a sales and use tax exemption is applicable.

4. Sales and use tax - no general exemption for spirituous liquors, vinous beverages, or malt beverages.

Under prior law, the sales and use tax exempted sales of malt and vinous beverages and sales of spirituous liquors. 32 V.S.A. § 9741(5), (6). The exemption for vinous beverages was repealed in 1991, and the exemption for malt beverages and spirituous liquors was repealed in 2003, effective in 2007. No. 32 of the Acts of the General Assembly of 1991, §§ 13, 27; No. 68 of the Acts of the General Assembly of 2003, § 58; No. 152 of the Acts of the General Assembly of 2003, § 27. Thus, sales and uses of these beverages are no longer exempted, as a general matter, from the sales and use tax.

4.a. Sales tax - free samples are not a sale, and no sales tax is due.

Since Taxpayer is not selling the samples, but is giving them away, there is no "sale" and therefore no sales tax due.

4.b. Use tax - Taxpayer is using the liquor it manufactures, and the use by the manufacturer as a free sample is not exempt, but is subject to use tax.

Taxpayer is using the liquor it manufactures in the free samples it gives to customers. Use tax is imposed, *inter alia*, on items which are used by the person who manufactured, processed or assembled them. 32 V.S.A. § 9773(2). There is an exemption from the use tax, however, if the use by the manufacturer is "for demonstrational or instructional purposes." Id. The full text of that law reads:

> **§ 9773. Imposition of compensating use tax**
>
> [T]here is imposed . . . a use tax at the rate of six percent for the use . . . :
>
> . . .
>
> (2) Of any tangible personal property manufactured . . . by the user, if items of the same kind of tangible personal property are offered for sale by him or her in the regular course of business, but the mere storage, keeping, retention, or withdrawal from storage of tangible personal property or the use for demonstrational or instructional purposes of tangible personal property by the person who manufactured . . . such property shall not be deemed a taxable use by him or her . . . .

Id. You have asked whether this use tax exemption, for items used by the manufacturer "for demonstrational or instructional purposes," would apply to Taxpayer's free samples. It does not apply, because the "demonstrational or instructional" exemption covers only items which are retained by the manufacturer to demonstrate the product or instruct or train the customer. It does not apply to items which the manufacturer does not retain, but instead, gives away.

As I mentioned in our telephone conversation, when there is no Vermont case law on an issue, the Department will sometimes turn to other states' case law, if the state has a similar statute and the issue in the court case is similar. Georgia has a use tax statute similar to Vermont's, and the Georgia courts have in at least two cases held that free samples do not qualify as an exempt use "for demonstration or display." CIBA Vision Corp. v. Jackson, 248 Ga.App. 688, 548 S.E.2d 431, cert. den. (Sept. 7, 2001); Collins v. Prince Street Technologies Ltd., 220 Ga.App. 492, 469 S.E.2d 700 (1996). The text of the Georgia statute provides that a manufacturer is taxable if it "makes any use of the article of tangible personal property other than

retaining, demonstrating, or displaying it for sale."[1] Ga. Code Ann. § 48-8-39. Id. at (b)(1)(A). In *CIBA*, a manufacturer of contact lenses gave free samples to eye-care professionals, who used the samples to demonstrate the product for their patients or to test the lens fit on their patients. 548 S.E.2d at 434. The court cited favorably its earlier case, *Prince Street*, in which it held that a carpet manufacturer was taxable on free samples of carpet which it distributed to interior decorators and interior design firms. The court in *CIBA* first noted that the statute "govern[s] the situation where the [manufacturer] never sells the goods but instead puts them to his own use." Id. The court reasoned that "giving away free samples is different from demonstrating your product without giving it away," and the use tax exemption "implies that the [manufacturer] still owns the item." Id. at 435. "It follows that where the ownership of the item has changed, e.g., where the item has been given away, it cannot be said the [manufacturer] is 'retaining, demonstrating, or displaying it for sale.'" Id. The court concluded that "The use of the free samples is simply a marketing scheme designed to promote the sale of CIBA lenses," and so, the manufacturer was taxable on its marketing use of its own product. Id.

As noted above, the Vermont statute is very similar to the Georgia statute, in that Vermont exempts a use by the manufacturer which is a "retention . . . or the use for demonstrational or instructional purposes." The reasoning of the Georgia court in *CIBA* is equally applicable here, since Taxpayer is not retaining the product, but is giving away the samples to market and promote the sale of its product. As a result, Taxpayer's use of its product as free samples would not be exempt from Vermont's use tax.

[1] This Georgia statute does not call the tax a "use tax," but instead calls it a "deemed retail sale." The court in *CIBA* noted, however, that "a deemed retail sale is nothing more than a 'use ' of the product which is also a taxable event." Id. at 434.

5. Tax exemptions must be construed strictly against the taxpayer

Finally, tax exemptions must be strictly construed against the taxpayer, by confining their meaning to the express letter or necessary scope of their language. Hopkinton Scout Leaders Ass'n. v. Town of Guilford, 176 Vt. 577, 578 (2004); Richard and Amy Tarrant v. Department of Taxes, 169 Vt. 189, 206 (1999); Wettereau, Inc. v. Department of Taxes, 141 Vt. 324, 329-330 (1982). "Any tax exemption provision must be strictly construed against the exemption, and to doubt is to deny the exemption; the taxpayer has the burden of clearly establishing the exemption beyond a reasonable doubt." World Publications, Inc. v. Vermont Dept. of Taxes, 192 Vt. 547, 550, ¶ 8 (2012). Construing the manufacturer's use tax exemption narrowly, and resolving any doubts against the taxpayer, transfers by Taxpayer of free samples of its alcoholic beverage are not exempt, and so, are subject to Vermont's use tax.

GENERAL PROVISIONS

This ruling will be made public after deletion of the parties' names and any information which may identify the parties. A copy of this ruling showing the proposed deletions is attached, and you may request within 30 days that the Commissioner delete any further information that might identify the parties. The final discretion as to deletions rests with the Commissioner.

This ruling is issued solely to the taxpayer and is limited to the facts presented, as affected by current statutes and regulations. Other taxpayers may refer to this ruling, when redacted to protect confidentiality, to determine the department's general approach, but the Department will not be bound by this ruling in the case of any other taxpayer or in the case of any change in the relevant statutes or regulations.

You have the right to appeal this ruling within 30 days. 3 V.S.A. §§ 808, 815.

_____ _____

Emily Bergquist Date

Approved:

_____ _____

Mary N. Peterson Date
Commissioner of Taxes