



COMMONWEALTH of VIRGINIA

Department of Taxation

MEMORANDUM

TO: Larry Durbin, Asst. Tax Commissioner, Office of Customer Services
Ron Holt, Asst. Tax Commissioner, Office of Compliance

FROM: Mike Melson, Office of Tax Policy ^{MSM}

DATE: July 31, 2001

SUBJECT: Retail Sales and Use Tax; Virginia Tire Tax
Recall of Firestone Tires by Ford Motor Co.

The purpose of this memorandum is to address the application of the Retail Sales and Use Tax and the Virginia Tire Tax to Ford Motor Company's tire replacement program. The memorandum is intended to address questions that might be raised by Virginia tire retailers and Virginia customers.

Ford Motor Co. recently announced that it would replace 13 million Firestone tires installed on certain Ford vehicles. Ford is notifying its customers to bring their vehicles to Ford dealerships or to tire centers for free replacements. Ford estimates that this replacement program will take up to nine months to complete. Further, Ford indicates that the exchange of tires will take place under two scenarios, referred to as the "designated manufacturer" scenario and the "independent retailer" scenario.

Designated manufacturer scenario

This scenario involves major tire manufacturers, such as Goodyear, General Tire, and Michelin, who have entered into agreements with Ford. Under this scenario, the customer will bring its vehicle to the tire retailer (or Ford dealer). The retailer will remove the Firestone tires and install the new tires. No charge will be made to the customer. Instead, the tire retailer will invoice the manufacturer for the following eligible charges: (1) the cost of the replacement tires, (2) mounting, balancing, valve stems and weights needed to install the replacement tires, (3) disposal fees and state and local environmental impact fees, and (4) state and local taxes (if applicable). The manufacturer will reimburse the tire retailer for the cost of the replacement tires and other eligible charges. The manufacturer will then get reimbursed by Ford for the costs incurred. Ford anticipates that this "designated manufacturer" scenario will account for the bulk of the exchanges.

Memorandum

Larry Durbin and Ron Holt

July 31, 2001

Page 2

Retail Sales and Use Tax: The retail sales and use tax will not apply to the exchange of tires under this scenario. Title 23 of the Virginia Administrative Code (VAC) 10-210-10 provides:

When any taxable article is returned to the dealer for adjustment, replacement or exchange and the consumer is given a new article free or at a reduced price under a warranty or guarantee, the sale or use tax must be computed on the actual additional amount, if any, paid to the dealer for the new article.

Under this scenario, and provided that the customer does not pay any additional amount to the tire retailer, the tire retailer is not required to charge and collect sales tax from the customer. This is because there is a zero sales price associated with this exchange transaction. In other words, computing the retail sales and use tax on a zero sales price results in a zero sales tax.

Virginia Tire Tax: The tire tax does apply to this transaction. Title 23 VAC 10-250-21 provides that:

Under original manufacturers' warranties, the [tire] tax is applicable in those instances in which a retailer requires a payment from a customer to replace a defective tire.

However, the [tire] tax is not applicable in those instances in which a retailer allows the exchange of a defective tire for a new tire without an additional charge to the customer.

In this case, the exchange is not pursuant to the manufacturer's (Firestone) warranty. Further, it does not appear that the tires are defective. Ford is exchanging tires on certain of its vehicles because Ford believes the tires may be unsafe when installed on specific vehicles (such as the Ford Explorer). Further, Firestone vigorously denies that the tires are defective.

Accordingly, there does not appear to be any exemption that would exempt the tire retailers from paying the tire tax on the replacement tires provided to customers, and the tire tax will be imposed on the tire retailer under the "designated manufacturer" scenario. Ford will subsequently reimburse the tire retailer for the tire tax.

Independent retailer scenario

Under this scenario, the customer will pay for the new tires and all associated costs. The customer will then apply to Ford for a refund. Like the "designated manufacturer" scenario, Ford will pay for the new tires, installation charges, and the other eligible charges (including state and local taxes).

Memorandum

Larry Durbin and Ron Holt

July 31, 2001

Page 3

Retail Sales and Use Tax: Under the "independent retailer" scenario, the tire retailer is required to charge and collect the retail sales and use tax on the sale of the replacement tires and any taxable charges associated with the sale. Assuming that Ford approves the customer's refund application, Ford will reimburse the customer for the retail sales and use tax paid to the tire retailer.

The tax is due in this scenario because there is a charge to the customer for the new tires. This differs from the transaction in the "designated manufacturer" scenario whereby the customer simply exchanges tires but pays no additional amount to the tire retailer.

Virginia Tire Tax: The tire retailer is liable for the tire tax on the replacement tires sold to customers. As addressed in 23 VAC 10-250-30, the tire retailer may pass the tire tax on to the ultimate consumer. In some instances, tire retailers recoup the tax as a separately stated item on invoices to customers. In other instances, the tire tax is included in the selling price of the tire. In either case, the tire retailer is responsible for remitting the tire tax to the department.

Additional information

For additional information regarding the recall program, Virginia tire retailers and Virginia customers should be directed to the Ford Motor Company website at www.ford.com or to Ford's toll-free tire exchange hotline at (866) 300-1226.

m:\tx-pl\tire recall