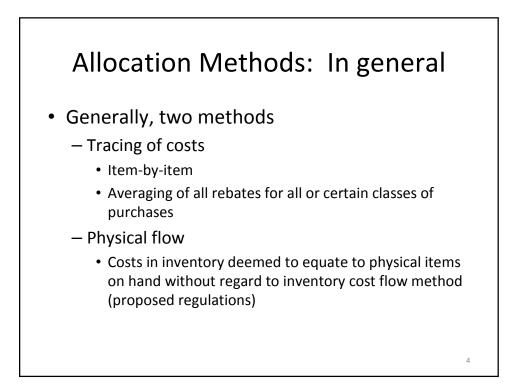
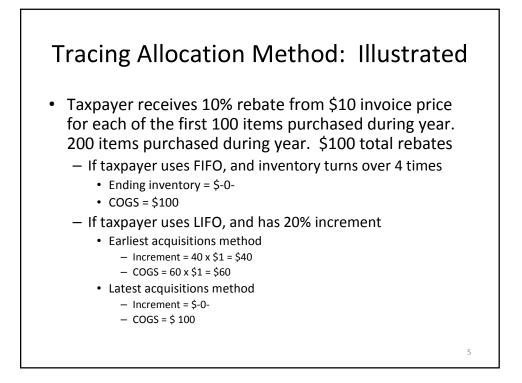
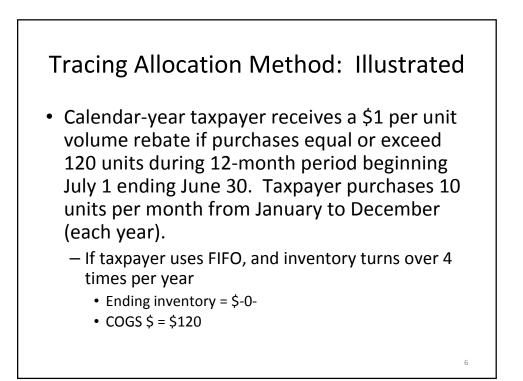


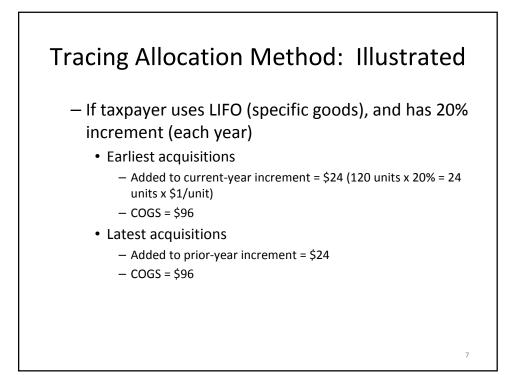
Character: IRS Guidance

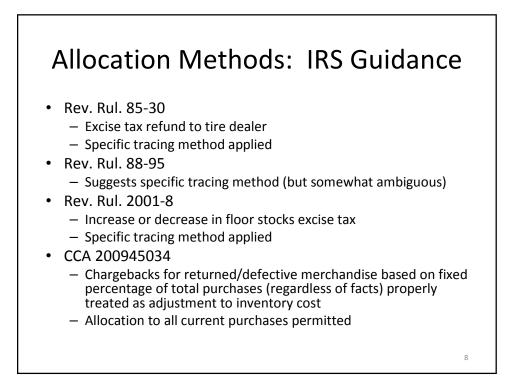
- Since 1976, IRS has generally treated pre-arranged vendor allowances based exclusively on purchases as an adjustment to cost
 - Rev. Rul. 76-96: Auto manufacturer rebates to retail customer
 - Rev. Rul. 84-41: Auto manufacturer rebates to dealer
 - Rev. Proc. 2007-53: Advance trade discounts
- Compare Coordinated Issues Paper/Tier III exam issue
 - Allowances in exchange for services, such as advertising, are not adjustments to the cost of merchandise acquired











If Not Based Exclusively on Purchases: Other Guidance

- Rev. Rul. 88-95: Cotton equalization payments for cotton inventory
- Rev. Rul. 2005-28: Manufacturer Medicaid rebates to retailer

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Prop. Reg. § 1.471-3(e): Sales-based Vendor Allowances

- Proposes to amend current regulations

 As amended, a sales-based vendor allowance is an adjustment only to the cost of merchandise sold during the year
- · Would prohibit use of specific tracing method
- Also proposes to amend Reg. §§ 1.263A-2 and -3 to provide (simplified production and resale methods) as follows:
 - Additional section 263A costs, section 471 costs incurred during year, and section 471 costs remaining on hand at year end do not include cost reductions described in Reg. § 1.471-3(e)
- Does not address application to retail method

 Further guidance pending
- Proposed to be effective for tax years ending on or after publication of final regulations

Examples (Determination of Character and Allocation Method)

- Example 1. Taxpayer (per pre-existing agreement) is entitled to a 10% rebate from invoice price of all purchases during each 12-month period that corresponds to tax year if purchases exceed specified volume threshold during such period
- Example 2. Same as Example 1, except 12-month measurement period spans the end of the tax year and the threshold is satisfied after end of tax year

Examples (cont'd)

- *Example 3.* Same as *Example 1*, except that taxpayer also agrees that manufacturer is its exclusive supplier during the period
- Example 4. Same as Example 1, except that taxpayer also agrees to perform cooperative advertising services during the period. The value of the cooperative advertising is not separately stated, and taxpayer gets no rebate if it fails to reach the volume threshold

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