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**Differing Views on Repayments by Manufacturers to Dealers for Expenses Required by the Manufacturers as Price Readjustments Under I.R.C. Section 6416(b)(1)—*General Motors Corp. v. United States*;<sup>\*</sup> *Waterman-Bic Pen Corp. v. United States*<sup>\*\*</sup>**

The Internal Revenue Code of 1954 exacts a manufacturer's excise tax based on sales price;<sup>1</sup> if the sales price is readjusted by means of a "bona fide discount, rebate or allowance," the manufacturer is entitled to a tax credit under section 6416(b)(1).<sup>2</sup> In two recent cases, *General Motors Corp. v. United States*,<sup>3</sup> and *Waterman-Bic Pen Corp. v. United States*,<sup>4</sup> manufacturers have sought tax credits, claiming that their reimbursements to dealers for expenses which the manufacturers had required the dealers to incur subsequent to the time of sale constituted price readjustments. The Court of Claims in *General Motors* allowed the tax credit, reasoning that such reimbursements were proper price readjustments because a part of the sales price was repaid to the dealer.<sup>5</sup> However, the Court of Appeals for the Second Circuit denied the credit in *Waterman-Bic*, holding that the reimbursements could not be considered readjustments because the manufacturer could not have excluded the reimbursed expenses from the sales price at the time of the sale.<sup>6</sup>

Despite the apparent conflict over the nature of a price readjust-

\* 339 F.2d 648 (Ct. Cl. 1964).

\*\* 332 F.2d 711 (2d Cir. 1964).

1. INT. REV. CODE OF 1954, § 4216(a) (formerly Int. Rev. Code of 1939, § 3441(a), 53 Stat. 416).

2. INT. REV. CODE OF 1954, § 6416(b)(1) (formerly Int. Rev. Code of 1939, § 3443(a)(2), 53 Stat. 417).

3. 339 F.2d 648 (Ct. Cl. 1964).

4. 332 F.2d 711 (2d Cir. 1964).

5. 339 F.2d at 651. Two payments were involved. The first was a bonus to the dealer of \$75 per car ordered during the month in which a major model change was to occur. The Internal Revenue Service has generally allowed these as price readjustments. Treas. Reg. 46, § 316.13 (1940). The other was a reimbursement to the dealer of \$25 for every car sold during the changeover month, conditioned upon proof by the dealer that he had paid each salesman \$25 extra for every car sold by him during that month. The court reasoned that these payments were inseparable parts of an overall plan and therefore could not be examined separately.

6. 332 F.2d at 714. The manufacturer had reimbursed the dealer for certain local advertising expenses which the manufacturer had required the dealer to bear at a date subsequent to the time of sale. The question whether a reimbursement for local advertising costs is a proper price readjustment has been obviated by recent amendments to the Code specifically allowing such reimbursements as rebates or discounts. INT. REV. CODE OF 1954, § 6416(b)(1), as amended, Act of Sept. 14, 1960, P.L. 86-781, § 2, 74 Stat. 1018. See *General Motors Corp. v. United States*, 149 Ct. Cl. 749, 277 F.2d 929 (1960), decided prior to the amendments, which reached a result contrary to that of *Waterman-Bic* on nearly identical facts.

ment, the actual crux of the disagreement is the definition of "sales price," since both courts agree that a price readjustment is a reduction in the sales price.<sup>7</sup> *General Motors* views sales price as the amount received by the manufacturer (the amount billed).<sup>8</sup> To readjust or reduce the sales price, the manufacturer need only return a portion of the billed amount.<sup>9</sup> The *Waterman-Bic* definition is more inclusive, for it encompasses the amount received by the manufacturer plus any amounts which the manufacturer has required the dealer to pay to persons other than the manufacturer as a condition of the sale.<sup>10</sup> Under *Waterman-Bic*, the manufacturer may readjust or reduce the sales price in two ways. He may either withdraw his requirement that the dealer pay a third party, or refund a portion of the money he has received. Because of the inclusiveness of the definition, however, he cannot effect a reduction subsequent to the time of sale by refunding to the dealer a portion of the billed amount and requiring the dealer to pay the amount of that refund to a third party.<sup>11</sup>

The *Waterman-Bic* definition of sales price is preferable to that of *General Motors* for three reasons. First, it is in accord with the principle that the basis for computing the tax should accurately represent the value of the article taxed.<sup>12</sup> When the tax is based upon the sales price, the value of an article is most accurately represented by the total consideration paid. It is indeed clear that total consideration includes not only the amount paid by the dealer to the manufacturer, but also any amount paid at the manufacturer's insistence to a third party at the time of the sale. Since the *General Motors* definition of sales price is not broad enough to include payments to third parties, it establishes an incomplete and misleading basis for the tax.

Second, the more inclusive *Waterman-Bic* definition of sales price is consonant with the definition of sales price throughout the Code.

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7. See *General Motors Corp. v. United States*, 339 F.2d 648, 651 (Ct. Cl. 1964); *Waterman-Bic Pen Corp. v. United States*, 332 F.2d 711, 714 (2d Cir. 1964).

8. 339 F.2d at 651. *Accord*, *General Motors Corp. v. United States*, 149 Ct. Cl. 749, 753, 277 F.2d 929, 931 (1960).

9. Thus, if a manufacturer charged his dealer \$1000 for a unit, the sales price would be \$1000. If the manufacturer later required the dealer to pay an expense of \$100 and reimbursed him for that expense, he would have reduced or readjusted the sales price to \$900 under the *General Motors* definition.

10. 332 F.2d at 714.

11. Thus, if the manufacturer billed the dealer \$1000 and required him to expend \$100 at the time of the sale, the sales price would equal \$1100. If the sales price at the time of the sale under the *Waterman-Bic* definition was \$1000 and the manufacturer required the dealer to expend \$100 for which he reimbursed the dealer, the reimbursement would not constitute a reduction in sales price. The manufacturer has simply exchanged payment to a third party for payment to himself; both payments are elements of the sales price under *Waterman-Bic*.

12. 10 MERTENS, FEDERAL INCOME TAXATION § 59.01 (1964). This reasoning is used primarily in establishing value as a basis for gift tax purposes.

Section 4216(a), which deals with sales price at the time of sale, provides for the inclusion in the sales price of *all* charges incurred in preparation for shipment.<sup>13</sup> The same section specifically excludes from sales price at the time of sale certain charges not incident to preparation for shipment.<sup>14</sup> In interpreting section 4216(a), the Supreme Court has broadly defined sales price at the time of sale to include *all* payments required by the manufacturer, whether or not billed, unless the payments are among those specifically excluded by section 4216(a).<sup>15</sup> The *Waterman-Bic* court, recognizing the similarities inherent in determining sales price at the time of sale under section 4216(a) and sales price at the time of price readjustment under section 6416(b)(1), held that the two sections must be read *in pari materia*.<sup>16</sup> Thus, the court acknowledged a uniform definition of sales price regardless of the point in time at which a manufacturer might attempt to reduce price. The *General Motors* court, on the other hand, refused to read the two sections *in pari materia* and held that the reasoning of the Supreme Court in interpreting section 4216(a) was inapplicable to price readjustment.<sup>17</sup> The result is a definition of sales price under section 6416(b)(1) which is less inclusive than that under section 4216(a). Consequently, under the *General Motors* definition a manufacturer who is precluded by section 4216(a) from reducing sales price at the time of sale can avoid the excise tax by simply waiting until a date subsequent to the sale to reduce sales price.

Third, the definition in *Waterman-Bic* is in agreement with the regulations established for sections 4216(a) and 6416(b)(1). During the taxable period in *General Motors*, the regulations under section 4216(a) treated sales price as the sum of the manufacturer's costs as measured by the amount billed to the dealer,<sup>18</sup> and the regulations under section 6416(b)(1) stated that a proper readjustment occurred when a part of the price was repaid to the dealer.<sup>19</sup> In 1958, the Service amended the regulations under section 4216(a) to define sales price as including any charge required by the manufacturer to be paid at the time of the sale, whether it is to be paid to the manufacturer or a third party.<sup>20</sup> The regulations pertaining to section 6416(b)(1) were accordingly amended to state that a reimbursement in consideration of a future expenditure by the dealer does not con-

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13. INT. REV. CODE OF 1954, § 4216(a) (formerly Int. Rev. Code of 1939, § 3441(a), 53 Stat. 416).

14. Section 4216(a) specifically excludes any "transportation, delivery, insurance, installation, or other charge [not incident to preparation for shipment]." *Ibid*.

15. *F. W. Fitch Co. v. United States*, 323 U.S. 582, 584 (1945).

16. 332 F.2d at 713.

17. 339 F.2d at 653.

18. Treas. Reg. 46, § 316.12 (1940).

19. See Treas. Reg. 46, § 316.13 (1940).

20. Treas. Reg. § 330.1-1 (1958), CCH FED. EXCISE TAX REP. ¶ 1795.

stitute a price readjustment if the expenditure would have been a part of the price if it had been required at the time of the sale.<sup>21</sup> The 1958 regulations were in effect during the taxable period involved in *Waterman-Bic*, but not during the period involved in *General Motors*.<sup>22</sup> While this distinction would seem to explain the difference in result between the two cases, neither court relied upon the regulations in reaching its decision. Since *Waterman-Bic* reached a conclusion identical to that in the regulations, it would have been to the advantage of both the taxpayer and the Internal Revenue Service if the court had formally recognized its agreement with the regulations. Such a recognition would foster predictability in price readjustments, thus alleviating the uncertainty indicated by the contrary holdings of the principal cases.

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21. Treas. Reg. § 330.1-2 (1958) (now Treas. Reg. 48.6416(b)(1) (1963)).

22. The taxable period in *General Motors* encompassed the year 1954 and the excise tax returns for the year 1955. The period in question in *Waterman-Bic* ran from November 20, 1958, to March 31, 1960.