

FINAL PRIVATE LETTER RULING

REQUEST LETTER

15-008

December 10, 2015

Office of the Commission
Utah State Tax Commission
Office of the Commission
210 N 1950 W
Salt Lake City, UT 84134

Dear Commissioners:

COMPANY 1. sells nutritional, dietary, and skin care products through a multi-level network of independent distributors. COMPANY 1 is considered an "MLM" or multi-level marketer such as COMPANY 2. COMPANY 1's only United States-based physical location is in CITY 1, STATE 1. COMPANY 1 charges sales tax based upon the address to which we ship and based upon full suggested retail price. On behalf of COMPANY 1 and its COMPANY 1 independent distributors, COMPANY 1 files one consolidated state sales/excise tax return in lieu of each independent distributor filing a separate return with your state.

While we have obtained previous rulings from your state on the taxability of our products and charges, we would like to ensure that our sales tax collection procedures are in compliance with all current law. Please provide us with a letter ruling or binding opinion on the taxability of our renewal, dashboard and personal website fees.

Renewal fees:

Distributors are required to renew their status annually. The annual renewal fee of \$\$\$ is paid by each distributor to remain in "active" status. All "active" distributors receive a MAGAZINE on a quarterly basis and maintain their wholesale discount on products purchased. Distributors earn a percentage discount off the retail price on the products purchased based on the distributor's *volume* of products purchased. Active distributors are also eligible to receive distributor business support services and access to the COMPANY 1 web site.

Please note customers are not required to pay a renewal fee, yet may also be eligible to receive a percentage discount off the retail price on the products purchased based on varying promotions.

Dashboard and personal website fees (sold as a bundle):

Distributors have the option of purchasing the dashboard and personal website (*sold as a bundle only*). The COMPANY 1 distributor dashboard service provides a distributor with immediate 24/7 access to information on all activity on the distributorship and online tools to track, manage

and grow the business. Personal websites allow the distributor to give COMPANY 1 presentations through a mobile device. The Personal websites also enable the distributor to add customers and downline distributors to their own shopping cart and online sponsoring.

Please send the letter rulings or binding opinions to my attention at the address provided. My contact information is listed below in case further information is required to issue an opinion.

Thank you for your assistance in this matter.

Sincerely,

NAME 1
TITLE 1
COMPANY 1
EMAIL 1
PHONE 1
FAX 1

RESPONSE LETTER
PRIVATE LETTER RULING 15-008

July 20, 2016

NAME 1
TITLE 1
[EMAIL 1](#)
COMPANY 1
ADDRESS 1
CITY 1, STATE 1 ZIP CODE 1

Dear NAME 1:

This letter is in response to your request for a private letter ruling for COMPANY 1 Inc. (“Company”), a multi-level marketer. You have asked about the Utah sales and use tax treatment of Company’s charges to its independent distributors for (1) a required annual renewal fee (“renewal fee”) and (2) an optional fee for a distributor dashboard and personal website. You provided us with information about these fees through your letter and other communications.

I. Facts

This Facts section discusses (1) the renewal fee and (2) the optional fee for the distributor dashboard and personal website.

A. Renewal Fee

You explained the renewal fee provides the distributor with the following items: (1) the quarterly MAGAZINE (“magazine”), (2) a wholesale discount on products purchased (“wholesale discount”), (3) the distributor business support services, and (4) access to the Company’s website.

First, for the magazine, you explained it promotes the health benefits of the Company’s products, encourages having distributorships, and informs distributors of special distributor promotions.

Second, for the wholesale discount, you explained a distributor can purchase products for a discounted price, with the percentage of the discount being based on the distributor’s volume of

products purchased. Often, the wholesale discount does not affect the taxable purchase price of the products. In your letter, you wrote the following:

[The Company] charges sales tax based upon the address to which we ship and based upon full suggested retail price. On behalf of [the Company] and [the Company's] independent distributors, [the Company] files one consolidated state sales/excise tax return in lieu of each independent distributor filing a separate return with your state.

In the above quote, you indicated the Company “charges sales tax . . . based upon the full suggested retail price.” Through subsequent communications, you clarified that when a distributor purchases products for the distributor’s personal consumption, the Company charges sales tax on those purchases based on the suggested retail price reduced by the wholesale discount. You explained that when the distributor purchases products for resale, not for the distributor’s personal consumption, the Company charges sales tax based on the suggested retail price, regardless of the distributor’s wholesale discount.

Third, for the distributor business support services, you explained that a distributor may call the Company with questions about the details of the Company’s products and about how to run a distributorship. The Company answers these questions through either its employees or its call center.

Fourth, for access to the Company’s website, you explained this access allows a distributor to retrieve order forms and pricing and to order products through this website. You also explained that a customer who is not a distributor could get an account with the Company and place orders through the Company’s website by providing the Company with the customer’s personal information.

B. Optional Fee for a Distributor Dashboard and Personal Website

You explained that the distributor dashboard and the personal website are sold as bundled items only.

For the distributor dashboard, you explained it grants a distributor immediate access to the Company’s information about the activities of that distributor’s customers and downline distributors. These activities affect the distributor’s commission checks. With the online tools associated with the distributor dashboard, the distributor can see which of the distributor’s downline distributors are close to advancing. This information allows the distributor to contact the downline distributors and encourage them to complete additional sales. Distributors without access to the distributor dashboard can receive similar information by calling the Company or by receiving printed statements later.

For the personal website, you explained the personal website is a mobile website, while the Company’s website currently is not. Also, with the personal website it is easier for a distributor to sign up both customers and downline distributors. Furthermore, the personal

website allows a customer of a distributor to place an order for the Company's products without knowing the distributor's WORD REMOVED, which is an identification number. Additionally, through a personal website a customer can view the Company's presentations on his or her mobile device. Lastly, a distributor with a personal website can customize it by adding his or her picture and story and by selecting the color, icons, and featured products the distributor wants.

II. Applicable Law

Utah Code Ann. § 59-12-103 imposes tax on certain transactions and explains how tax is imposed on bundled transactions. It states the following, in pertinent part:

- (1) A tax is imposed on the purchaser as provided in this part for amounts paid or charged for the following transactions:
 - (a) retail sales of tangible personal property made within the state;
 -
- (2)
 - (d)
 -
 - (iii) Subject to Subsection (2)(d)(iv), for a bundled transaction . . . :
 - (A) if the sales price of the bundled transaction is attributable to tangible personal property, a product, or a service that is subject to taxation under this chapter and tangible personal property, a product, or service that is not subject to taxation under this chapter, the entire bundled transaction is subject to taxation under this chapter unless:
 - (I) the seller is able to identify by reasonable and verifiable standards the tangible personal property, product, or service that is not subject to taxation under this chapter from the books and records the seller keeps in the seller's regular course of business; or
 - (II) state or federal law provides otherwise; . . .
 -
 - (iv) For purposes of Subsection (2)(d)(iii), books and records that a seller keeps in the seller's regular course of business includes books and records the seller keeps in the regular course of business for nontax purposes.

Utah Code Ann. § 59-12-102(18) defines "bundled transaction," stating in pertinent part:

- (a) "Bundled transaction" means the sale of two or more items of tangible personal property, products, or services if the tangible personal property, products, or services are:
 - (i) distinct and identifiable; and
 - (ii) sold for one nonitemized price.

....

III. Analysis

This section analyzes the Utah sales tax treatment of (1) the renewal fee and (2) the optional fee for the distributor dashboard and personal website.

A. The Renewal Fee is Subject to Utah Sales Taxes based on the Taxability of the Magazine and Wholesale Discount.

The renewal fee provides a distributor with the following items:

1. The magazine
2. The wholesale discount to be applied to a distributor's purchases of products for the distributor's personal consumption
3. The wholesale discount to be applied to a distributor's purchases of products for resale
4. The distributor business support services
5. Access to the Company's website

In Section I. Facts, this private letter ruling lists the wholesale discount as one item. In this Section III. Analysis, the wholesale discount is separated into two items to aid in the analysis.

To analyze the taxability of the renewal fee, the taxability of the underlying items must be considered. In Private Letter Ruling ("PLR") 99-025 issued to the Company, the Commission instructed, "Although you have labeled these charges 'annual renewal fees,' we look beyond that label to examine the underlying nature of the transaction. What the distributor is actually purchasing [for PLR 99-025] is a monthly newsletter and support services."¹

Below, the sales taxability of the five items listed above is analyzed, first, as the sale of each item if sold separately and, next, as the sale of the five items together for one nonitemized price.

1. Taxability of Each of the Items if Sold Separately

If the magazine were sold separately, it would be taxable under § 59-12-103(1)(a), as a "retail sale[] of tangible personal property made within the state."

¹ Private letter rulings are accessible through the tax.utah.gov website.

If the wholesale discount to be applied to a distributor's purchase of products for the distributor's personal consumption were sold separately, it would be taxable under § 59-12-103(1)(a), as a "retail sale[] of tangible personal property made within the state." When the wholesale discount is applied to a distributor's purchase of products for the distributor's personal consumption, the wholesale discount reduces the taxable purchase price of those products. The amount a distributor pays the Company for a wholesale discount is taxable, as part of the purchase price of the products the distributor subsequently purchases for his or her personal consumption. The Company's sale of the wholesale discount in this situation is akin to a company's sale of coupon books, which are addressed in Utah Administrative Code R865-19S-62 A., which states the following:

Meal tickets, coupon books, or merchandise cards sold by persons engaged in selling taxable commodities or services are taxable, and the tax shall be billed or collected on the selling price at the time the tickets, books, or cards are sold. Tax is to be added at the subsequent selection and delivery of the merchandise or services if an additional charge is made.^[2]

This administrative rule indicates that both of the following sales are subject to tax: the sale of an item such as a coupon book entitling a buyer to a discount on a future taxable sale *and* the subsequent retail sale of the discounted product. PLR 00-003 addresses a similar situation, the taxability of the sales of memberships entitling members to discounts on retail prices of taxable products and services. In PLR 00-003, the Commission concludes the sales of the membership fees presented are taxable. The Commission states, "[T]he membership fees . . . would be considered part of the purchase price for the products or services sold" to the members and "if these goods and services are of a type subject to sales tax, the discount memberships sold . . . are also taxable." Applying R865-19S-62 and PLR 00-003 to the situation you presented, the Company's sale of the wholesale discount that allows the distributor to purchase discounted products for his or her personal consumption would be subject to Utah sales taxes.

If the wholesale discount to be applied to a distributor's purchase of products for resale were sold separately, it would not be subject to Utah sales tax. When the wholesale discount is applied to a distributor's purchase of products for resale, the wholesale discount does not reduce the taxable purchase price of those products. Instead, the Company charges and remits sales tax based upon the full suggested retail price of those products when the products are sold to the distributors.

If the distributor business support services were sold separately, they would not be taxable. These services are not among those enumerated in § 59-12-103(1) as taxable.

If access to the Company's website for the purposes of ordering and of obtaining information necessary to submit orders were sold separately, it would not be taxable. This access is not among the services enumerated in § 59-12-103(1) as taxable.

In summary, if the five items were sold separately, their taxability would be as follows:

² Administrative rules such as R865-19S-62 are accessible through the tax.utah.gov website.

<u>Item</u>	<u>Utah Sales Tax Treatment</u>
1. The magazine	Taxable
2. The wholesale discount to be applied to a distributor's purchases of products for the distributor's personal consumption	Taxable
3. The wholesale discount to be applied to a distributor's purchases of products for resale	Not taxable
4. The distributor business support services	Not taxable
5. Access to the Company's website	Not taxable

2. Taxability of the Five Items When Sold Together for One Nonitemized Price

Next, the sales taxability of the five items sold together must be analyzed. The five items sold together are “distinct and identifiable” and “sold for one nonitemized price,” so their sale meets the definition of “bundled transaction,” found in § 59-12-102(18)(a). Section 59-12-103(1)(d)(iii) provides “the entire bundled transaction is subject to taxation . . . unless: . . . the seller is able to identify by reasonable and verifiable standards the tangible personal property, product, or service that is not subject to taxation . . . from the books and records the seller keeps in the seller's regular course of business . . . ” Thus, if the Company knows the values of the items not subject to tax versus the value of the items subject to tax, then only the portion of the bundled transaction relating to the taxable items would be subject to Utah sales taxes.

B. The Optional Fee for a Distributor Dashboard and Personal Website is Subject to Utah Sales Taxes Based on the Personal Website.

The optional fee for a distributor dashboard and personal website includes the following two items:

1. The distributor dashboard
2. The personal website

Below are analyses of the sales taxability of these two items assuming each item had been sold separately and then the analysis of the taxability when the two items are sold together.

1. Taxability of the Distributor Dashboard if Sold Separately

If the distributor dashboard were sold separately, it would not be taxable. For this sale, the distributor obtains both the right to use the distributor dashboard, which includes the use of the computer software to access the Company's information about the activities of that distributor's distributorship. The use of the software and the access to the Company's information through the software are not two "distinct and identifiable" items; thus, the sale is not a bundled transaction. The taxability of the sale of the distributor dashboard depends on the essence or primary object of the transaction.

The Utah Supreme Court explained the essence of the transaction as follows:

[T]he essence of the transaction theory[] focuses on the nature of what was sold and whether it primarily entails tangible personal property. . . . This theory examines the transaction as a whole to determine whether the essence of the transaction is one for services or for tangible personal property. The analysis typically requires a determination either that the services provided are merely incidental to an essentially personal property transaction or that the property provided is merely incidental to an essentially service transaction. . . .

B.J.-Titan Services v. State Tax Comm'n, 842 P.2d 822, 825 (Utah 1992) (internal citations removed).

To decide whether the essence of the transaction is one for the use of the software or for the Company's information, the nature and extent of the use of the software must be compared with the use of the Company's information. The Commission acknowledges that this is a very fact specific determination that depends on the extent to which the Company provides facts showing the essence of the transaction. For this private letter ruling, the transaction is analyzed to determine if its essence is for the distributor's use of the Company's information with the software being incidental, which is a nontaxable service, or if the essence is for the distributor's use of the Company's computer software with the Company's information being incidental, which is a taxable transaction. For the facts presented, the comparison of the nature and extent of the use of the software versus the use of the Company's information is as follows. The computer software is used to convey to a distributor the Company's information about the activities of the distributor's customers and downline distributors. Part of the computer software has been described as online tools. The online tools use the Company's information to inform the distributor which of his or her downline distributors are close to advancing. You presented no facts suggesting a distributor can apply the software to any information or data other than to the Company's. The Company's information is not only available through the computer software; a distributor can also obtain the information by calling the Company or from statements. Thus, a distributor chooses to purchase the distributor dashboard to obtain a more convenient way to access the Company's information. The essence of the transaction is for more convenient access to the Company's information, not to obtain the use of the computer software through which such information is conveyed. Such a sale of the Company's information is not subject to Utah sales tax. Thus, if the sale of the distributor dashboard were sold separately, the transaction would not be taxable under § 59-12-103(1)(a).

2. *Taxability of the Personal Website if Sold Separately*

If the personal website were sold separately, it would be taxable. The sale of the personal website involves computer software and possibly the services of the Company's personnel as well. Whether this sale is essentially one for the use of the website's software or for the services of the Company's personnel is determined based on the essence or primary object to the transaction.

In general, nontaxable services are the primary object of the transaction if the seller's personnel "conceptualize, design, program or maintain a website" and "the [seller]'s expertise [is] knowing what works best and how to incorporate designs into a website . . ." See PLR 09-002, page 7.³ On the other hand, if a seller's services are secondary to the prewritten computer software, the prewritten computer software, not the services, is the primary object of the transaction. In footnote 3 of PLR 01-030, the Commission explained that it "would probably consider" the sale of a website to be taxable if "the design of [the] website entail[ed] only the bundling of preexisting programs into a unique website for a specific client."⁴

Applying PLR 09-002 and PLR 01-030 to the personal website you presented, the Company's sale of the personal website to a distributor is a taxable sale of the use of prewritten computer software. The Company is not developing websites for individual distributors. The primary object of this transaction does not involve the services of the Company's personnel. Instead the distributors are purchasing the use of a standard website that the distributors can customize in limited ways.

In summary, if the two items were sold separately, their taxability would be as follows:

<u>Item</u>	<u>Utah Sales Tax Treatment</u>
1. Distributor dashboard	Not Taxable
2. Personal website	Taxable

3. *Taxability of the Distributor Dashboard and the Personal Website When Sold Together for One Nonitemized Price*

Next, the sales taxability of the two items sold together must be analyzed. The two items sold together constitute a bundled transaction. They are "distinct and identifiable" and "sold for one nonitemized price," so their sale meets the definition of "bundled transaction" found in § 59-12-102(18)(a).

³ Private letter rulings are accessible through the tax.utah.gov website.

⁴ See above note 3.

Applying § 59-12-103(1)(d)(iii), “the entire bundled transaction is subject to taxation . . . unless: . . . the seller is able to identify by reasonable and verifiable standards the tangible personal property, product, or service that is not subject to taxation . . . from the books and records the seller keeps in the seller’s regular course of business . . .” Thus, the whole optional fee for a distributor dashboard and personal website is subject to tax unless the Company can identify the value of the distributor dashboard compared with the value of the personal website. If the Company can identify such values, then only the personal website portion of the bundled transaction would be subject to Utah sales taxes.

IV. Conclusion

The renewal fee for distributors in Utah is subject to Utah sales taxes based on the taxability of the magazine and the wholesale discount. The sale of the renewal fee is taxed as a bundled transaction, with the entire renewal fee taxable unless the Company sufficiently identifies the nontaxable portion of the transaction from its records.

The optional fee for the distributor dashboard and personal website is subject to Utah sales taxes as a bundled transaction. The entire optional fee is taxable unless the Company sufficiently identifies from its records the nontaxable portion of the transaction relating to the distributor dashboard.

The Tax Commission’s conclusions are based on the facts as you described them and the Utah law currently in effect. Should the facts be different or if the law were to change, a different conclusion may be warranted. If you feel we have misunderstood the facts as you have presented them, you have additional facts that may be relevant, or you have any other questions, please feel free to contact the Commission.

Additionally, you may also appeal the private letter ruling in the following two ways.

First, you may file a petition for declaratory order, which would serve to challenge the Commission's interpretation of statutory language or authority under a statute. This petition must be in written form, and submitted within thirty (30) days after the date of this private letter ruling. You may submit your petition by any of the means given below. **Failure to submit your petition within the 30-day time frame could forfeit your appeal rights and will be deemed a failure to exhaust your administrative remedies.** Declaratory orders are discussed in Utah Administrative Code R861-1A-34 C.2., available online at <http://tax.utah.gov/commission/effective/r861-01a-034.pdf>, and in Utah Administrative Code R861-1A-31, available online at <http://tax.utah.gov/commission/effective/r861-01a-031.pdf>.

Second, you may file a petition for redetermination of agency action if your private letter ruling leads to an audit assessment, a denial of a claim, or some other agency action at a division level. This petition must be written and may use form TC-738, available online at <http://tax.utah.gov/forms/current/tc-738.pdf>. Your petition must be submitted by any of the means given below, within thirty (30) days, generally, of the date of the notice of agency action that describes the agency action you are challenging.

You may access general information about Tax Commission Appeals online at <http://tax.utah.gov/commission-office/appeals>. You may file an appeal through any of the means provided below:

- **Best way**—by email: taxappeals@utah.gov
- By mail: Tax Appeals
USTC
210 North 1950 West
Salt Lake City, UT 84134
- By fax: 801-297-3919

For the Commission,

Rebecca L. Rockwell
Commissioner

RLR/aln
15-008