

REQUEST LETTER

04-016

NAME

ADDRESS

Re: Request for Clarification on Sales/Use Tax Procedures

Company Background:

COMPANY is a Utah corporation. COMPANY is a direct sales company that has independent demonstrators that solicit sales for decorative rubber stamps and accessories across the United States. The demonstrators sell through home parties to hostesses and guests. Product is manufactured in Utah or purchased and shipped from the company's distribution center, also located in Utah.

Under the current hostess plan, depending on the level of sales at a party/demonstration, the hostess is eligible for a stamp set (hostess gift) at no cost. COMPANY Currently remits tax on all hostess gifts to the State of Utah, even those that are shipped to a hostess in another state.

Issue:

COMPANY Has recently completed an audit from the State of 1ST STATE and 2ND STATE. Both states assert that tax is due to their jurisdictions based on the fact that the final use in their state. 2ND STATE stated that COMPANY Incorrectly paid use tax and should have paid sales tax to Utah and therefore did not allow us a credit for taxes paid to another state.

Currently, COMPANY'S basis for paying tax on all hostess gifts is Utah State Administrative Rule R865-19S-68, in which the COMPANY would be considered the donor of the hostess gifts and in accordance with the rule is considered to be the user/consumer and the sale to them is a taxable sale.

Since the statement concerning exempt items is not clearly defined, the issue was raised by the 1ST STATE auditor. His argument was the statute says "Any item given away as a sales incentive is exempt to the donor if the sale of the item would have been exempt." If the statute is based in Utah taxability, then the incentive would be exempt to the donor, because the sale of the item would be exempt from Utah sales tax as a sale made in interstate commerce. He stated that this was reinforced to him by phone conversations he had with the Utah State Tax Commission. He then suggested we get a more formal answer in writing.

Therefore, COMPANY Is requesting an official clarification on the following issues:

- Is the tax due to the state of Utah on all hostess gifts that the company manufacturers and provides as incentives to customers that are located outside of Utah?

- If yes, is the tax we pay on these items sales tax as defined in R865-19S-1 since the “sale” takes place in Utah or use tax?
- If no, are all items not sold that we ship out of state considered to be exempt from Utah tax?

COMPANY Feels this will be a recurring issue with other states we do business in and would appreciate a prompt response.

Respectfully,

NAME
PHONE

RESPONSE LETTER

RE: Private Letter Ruling Request

NAME
ADDRESS

Dear NAME,

We have received your request for a Private Letter Ruling. You have described COMPANY as a direct sales company that has independent demonstrators who solicit sales for decorative rubber stamps and accessories across the United States. The demonstrators sell through home parties to hostesses and guests. The product is manufactured or assembled in Utah and shipped from the company’s distribution center, also located in Utah. Under the current hostess plan the hostess is eligible for a stamp set (hostess gift) at no cost. COMPANY currently remits tax on all hostess gifts to the State of Utah, including those that are shipped to a hostess in another state.

The issue as you have described to us is that your company has been subject to sales tax audits in 1ST STATE and 2ND STATE. Those states have assessed you for sales and use tax on the gift sets, which they assert is due to their jurisdictions. You represented that their position is based on the premise that the final use is in those states.

You asked three specific questions regarding the gift sets. First, you inquire if tax is due on hostess gifts provided to persons hosting parties outside of Utah. You next ask if tax is due, whether it is sales tax or use tax. Finally, you ask if tax was not due, whether all items not sold that you ship out of state are considered to be exempt from Utah tax.

We will first respond to your questions directly. Following that we will analyze what appears to be your overall concern of taxation in multiple states.

In answer to your first question, tax is due on the hostess gifts manufactured in Utah and provided to persons hosting parties outside of Utah. Under the facts that you have presented, COMPANY is the final consumer of the hostess gift. As you noted, under Administrative Rule R685-19S-68 (A), “[d]onors that give away items of tangible personal property as premiums or otherwise are regarded as the users or consumers of those items and the sale to the donor is a taxable sale.” Accordingly, you are giving away the hostess gift stamp set as a “premium” to the hostess for hosting the party. COMPANY is the “donor,” and considered to be the consumer of the gift stamp set. COMPANY “consumes” the hostess gift stamp set in Utah, and is therefore liable for sales and use tax in Utah, regardless of where the hostess receives the gift.

COMPANY is, in other words, responsible for sales or use tax on the cost of “consuming” the hostess gift. The cost upon which use tax is calculated is the total cost to COMPANY to acquire the hostess gift in Utah.

In answer to your second question, the type of tax due depends on how the tax is collected and remitted. R865-19S-1.A. provides that the tax is a sales tax if collected and remitted by a seller, or a use tax if remitted by the purchaser. Therefore, if COMPANY pays tax to a seller on its purchase of parts that it assembles or on individual items that are not assembled it is a sales tax. On the other hand if COMPANY remits the tax directly the Tax Commission, it would be a use tax.

Your third question was whether tax would be due in other States if it were not due here. If no tax were due in Utah, tax may be due in other States that impose sales or use taxes, depending on the laws in each of the respective states.

Having addressed your questions, we would like to expand on the general issue that you have raised concerning the possibility of double taxation. To begin, most states, either through the Multistate Tax Compact or through their own individual statutes, provide reciprocity for sales and use taxes paid to another state. These credits or exemptions provide that the state where the initial non-exempt purchase occurs imposes the tax. Thereafter, another state should impose a tax on the transaction only for any difference between the initial tax (if any) and the subsequent tax.

Utah’s position is consistent with this general arrangement. Unless COMPANY has already paid sales tax on the initial acquisition, the first use, consumption, or storage of the tangible personal property at issue occurs in Utah at the point in time when COMPANY removes the property from inventory held for resale. At that point, the property is subject to the Utah use tax. It is no longer held as inventory for resale and is therefore no longer subject to the resale exemption. Therefore, if COMPANY purchases the items or materials without paying sales tax, it must pay use tax on that transaction once it is determined that the tax is owing.

Because Utah is the first state where use tax becomes due, we consider the company is liable for the entire amount of Utah use tax, even if another state also imposes use tax on the same property. Should the same property subsequently become subject to another state’s use tax, most states allow the company to apply a credit of the use tax paid to the Utah to that liability imposed

by the other state.

Utah's position would be the same if the situation were reversed. That is, if COMPANY were located in another state and the party were hosted in Utah, we would impose a use tax on COMPANY, but would allow a credit for the tax paid to another state.

In short, should another state impose a use tax on COMPANY, it should also provide a credit for taxes paid in Utah. However, we do not know the exact provisions in other states for sales tax imposition or reciprocity in multi-state transactions. However, because Utah is the first state in which the use tax becomes due, even if another state does not allow such a credit, the Utah use tax is unaffected. If 1ST STATE or 2ND STATE have different policies that do not provide for credits for taxes paid to another state, your issue may not be able to be resolved at this level.

Our decision is based on the facts as you have represented them. If the fact should prove different, our opinion may change accordingly.

For the Commission,

Marc B. Johnson
Commissioner

MBJ/SR
04-016