

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING #01-25**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements in Department policy.

SUBJECT

Application of the sales and use tax to the exchange of intangible points for tangible personal property, when the points are obtained by the customer in connection with the purchase of other tangible personal property from the taxpayer.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time.

Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling, and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[TAXPAYER] manufactures and sells [TANGIBLE PERSONAL PROPERTY]. Almost all of the [TANGIBLE PERSONAL PROPERTY] are sold to other dealers for resale. To entice these customers to sign contracts with the taxpayer, the taxpayer's advertising department offers incentive programs through which the customers earn points. The customers then can use the points accumulated to purchase or obtain merchandise, such as jackets, hats, golf shirts, radios, and televisions, from the taxpayer.

Customers earn points in two ways. The customer is initially credited with points when it signs a contract with the taxpayer. The number of points earned depends on the volume of the contract. The customer earns additional points upon the actual purchase of the [TANGIBLE PERSONAL PROPERTY].

The customer may pay for the merchandise entirely with points accumulated through these incentive programs. The customer may also use its points as a partial payment and pay cash for the remaining balance on the merchandise.

The taxpayer maintains an inventory of the merchandise offered to its customers through these incentive programs. Orders for the merchandise are filled from this inventory and shipped to the customers. The taxpayer is located in Tennessee.

The taxpayer reports and pays Tennessee sales and use tax in accordance with Tenn. Comp. R. & Regs. 1320-5-1-.68. Tax is accrued and paid on all merchandise offered to the taxpayer's customers through its incentive programs at the time the merchandise is purchased by the taxpayer. Most of the merchandise is shipped to customers outside of Tennessee.

Because the taxpayer's incentive program is a promotion, the taxpayer accepts the risk of loss in the event that the goods are damaged or lost in transit. The taxpayer arranges for shipment by a third party carrier. Title to and possession of the goods pass to the customer when the customer actually receives the goods.

QUESTIONS

1. If a customer uses its points to purchase merchandise through the taxpayer's incentive program and the merchandise is shipped to the customer outside of Tennessee, is the taxpayer liable for Tennessee sales or use tax on the customer's purchase of the merchandise?
2. If a customer uses its points for a portion of the cost of the merchandise and pays cash for the remaining balance and the merchandise is shipped to the

customer outside of Tennessee, is the taxpayer liable for Tennessee sales or use tax on the customer's purchase of the merchandise?

3. If the taxpayer purchases the merchandise from a vendor located outside of Tennessee and the merchandise is sold and shipped to a customer outside of Tennessee, is the taxpayer liable for Tennessee sales or use tax on the customer's purchase of the merchandise?

RULINGS

1. No. The transfer by the taxpayer to the customer of the tangible personal property obtained through the points is a retail sale. Because title to and possession of the tangible personal property pass to the customer outside of Tennessee, the Tennessee sales tax would not apply.

2. No. The transfer by the taxpayer to the customer of the tangible personal property obtained through a combination of the points and money is a retail sale. Because title to and possession of the tangible personal property pass to the customer outside of Tennessee, the Tennessee sales tax would not apply.

3. No. The transfer by the taxpayer to the customer of the tangible personal property obtained through the points or through a combination of the points and money is a retail sale. Because title to and possession of the tangible personal property pass to the customer outside of Tennessee, the Tennessee sales tax would not apply.

ANALYSIS

1. According to the facts provided by the taxpayer, the taxpayer's sale of [TANGIBLE PERSONAL PROPERTY] includes both the [TANGIBLE PERSONAL PROPERTY] and intangible points for the customer. The customer can utilize the points to obtain items of tangible personal property other than [THE TANGIBLE PERSONAL PROPERTY SOLD IN THE REGULAR COURSE OF BUSINESS] from the taxpayer without paying additional money. In this context, the sale of the [TANGIBLE PERSONAL PROPERTY SOLD IN THE REGULAR COURSE OF BUSINESS] establishes that consideration exists for the points and ultimately for the other items of tangible personal property. Nashville Clubhouse Inn v. Johnson, 27 S.W.3d 542, 547 (Tenn. App. 2000). Thus, the transfer by the taxpayer to the customer of the tangible personal property obtained through the points is a sale. Because the customer is the user and consumer of the tangible personal property obtained through the points, the sale is a retail sale. Tenn. Code Ann. § 67-6-102(24).

A retail sale is subject to the Tennessee sales tax, if either title to or possession of the tangible personal property passes in Tennessee. Eusco, Inc. v. Huddleston, 835 S.W.2d 576, 579 (Tenn. 1992). The "sales price" is "the total

amount for which a taxable service or tangible personal property is sold ... valued in money, whether paid in money or otherwise" Tenn. Code Ann. § 67-6-102(26). In contrast to the facts in Nashville Clubhouse Inn, 27 S.W.2d 542 (Tenn. App. 2000), the taxpayer does not collect tax on the sales price of the combined sale. However, according to the facts provided by the taxpayer, neither title to nor possession of the tangible personal property passes in Tennessee. Therefore, the Tennessee sales tax would not apply.

2. The transfer by the taxpayer to the customer of the tangible personal property obtained through a combination of the points and money is a retail sale. Tenn. Code Ann. § 67-6-102(24)(A). The retail sale of tangible personal property is subject to the Tennessee sales tax, if either title to or possession of the tangible personal property passes in Tennessee. Eusco, Inc. v. Huddleston, 835 S.W.2d 576, 579 (Tenn. 1992). According to the facts provided by the taxpayer, neither title to nor possession of the tangible personal property passes in Tennessee. Therefore, the Tennessee sales tax would not apply.

3. The transfer by the taxpayer to the customer of the tangible personal property obtained through the points or through a combination of the points and money is a retail sale. Because title to and possession of the tangible personal property pass to the customer outside of Tennessee, the Tennessee sales tax would not apply. Eusco, Inc. v. Huddleston, 835 S.W.2d 576, 579 (Tenn. 1992).

Steve Butler
Tax Counsel

APPROVED: Ruth E. Johnson
Commissioner of Revenue

DATE: October 29, 2001