

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 22-02**

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This ruling is based on the particular facts and circumstances presented and is an interpretation of the law at a specific point in time. The law may have changed since this ruling was issued, possibly rendering it obsolete. The presentation of this ruling in a redacted form is provided solely for informational purposes and is not intended as a statement of Departmental policy. Taxpayers should consult with a tax professional before relying on any aspect of this ruling.

SUBJECT

The application of the Tennessee sales and use tax to certain charges to third parties made by a delivery network company electing to be a marketplace facilitator.

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

A company (the "Taxpayer") connects third-party sellers ("Sellers") of tangible personal property to persons seeking to purchase tangible items ("Purchasers"). It also connects Purchasers to third-party service providers ("Service Providers") to deliver the items sold by Sellers. The Taxpayer connects Sellers, Service Providers, and Purchasers via its website ("web-based interface") or downloadable mobile application ("App"). Purchasers use the web-based interface or App to view available items for

sale by Sellers and to place an order. The web-based interface is accessed free of charge, and the App is downloaded and accessed free of charge.

The Taxpayer states it is a “delivery network company” as defined in TENN. CODE ANN. § 67-6-102(26) (Supp. 2020), excluded from registering with the Tennessee Department of Revenue (the “Department”) as a marketplace facilitator unless it chooses to elect to be a marketplace facilitator pursuant to TENN. CODE ANN. § 67-6-102(56)(B)(iv) (Supp. 2020).¹

The items sold by Sellers are taxable as tangible personal property in Tennessee. The Taxpayer elected to be a marketplace facilitator and is responsible for remitting Tennessee sales tax to the State on its taxable sales. The delivery of the tangible personal property is separately provided by Service Providers to Purchasers.

The Taxpayer charges a fee to the Sellers (the “Seller Fee”) for connecting the Sellers to Purchasers and for processing the payment for the purchase of the items. The Taxpayer characterizes the Seller Fee as a fee for the Taxpayer’s lead generation and payment processing services. The Taxpayer is only paid the Seller Fee when the Sellers connect with Purchasers who purchase the Sellers’ tangible personal property. The Seller Fee is computed based on a percentage of the payments made by Purchasers to Sellers.

Sellers also have access to the Taxpayer’s web-based interface or App. The Taxpayer does not provide the web-based interface as a separate product, and it does not charge a separate fee to access the web-based interface. Using the web-based interface, Sellers list their items for sale, add new items, adjust the price and availability of items, add pictures or descriptions of items, and adjust the hours of the Sellers. Sellers also use the web-based interface to view orders from Purchasers, accept and confirm orders from Purchasers, be notified of orders, and view other transaction activity. The web-based interface also provides Sellers the ability to print a receipt showing charges for items ordered by Purchasers, pause, delay, or cancel orders, notify Purchasers and Service Providers when an item is ready to be delivered or picked-up and delivered, track the progress of orders, and view order history. The web-based interface also provides some data analytics features that cannot be customized or manipulated by the Seller. The Sellers may not change or manipulate the web-based interface.

The Taxpayer also charges a fee to the Service Providers (the “Service Fee”). The Taxpayer characterizes the Service Fee as a charge to the Service Providers for connecting them with Purchasers and processing the payment for the delivery service. The Taxpayer is only paid a Service Fee if the connection successfully occurs, and a Service Provider delivers the tangible item to the Purchaser. The Service Fee is a variable fee charged by the Taxpayer to the Service Providers for connecting the Service Providers to Purchasers and processing the payment.

Service Providers have access to the web-based interface. Using the web-based interface they can accept requests for delivery service, receive the address of Sellers for pick-up, receive the address of

¹ The facts herein assume that the Taxpayer is properly defined as a delivery network company, and the ruling contains no analysis regarding whether the Taxpayer comes within the scope of this definition, or whether fees charged to Purchasers for goods and services are subject to sales tax. The ruling solely addresses whether the fees charged to the Sellers and Service Providers are independently subject to sales tax.

Purchasers for delivery, receive notification that an order is ready for pick-up from Sellers, gain access to GPS tracking which provides directions to the Sellers and Purchasers (the Service Providers are not required to use this and can use other mapping functionality if preferred), confirm delivery to Purchasers, report any issues, access trip and earnings information, and access Form 1099s, if applicable.

The Taxpayer also acts as a limited collection agent for processing payments from the Purchasers. The Taxpayer charges sales tax on the full amount charged to Purchasers. The Taxpayer then pays the Sellers and Service Providers from the processed transaction. The Taxpayer retains its Seller Fee and Service Fee out of the amount that it pays to the Sellers and Service Providers. Retaining the Seller Fee and Service Fee eliminates a separate step where the Taxpayer would otherwise require the Sellers and Service Providers to pay the fees directly to the Taxpayer. The Taxpayer sends a statement to the Sellers and Service Providers showing the fees that they were charged by the Taxpayer.

RULINGS

1. Is the Seller Fee subject to the Tennessee sales and use tax?

Ruling: No, the Seller Fee is not subject to the Tennessee sales and use tax.

2. Is the Service Fee subject to the Tennessee sales and use tax?

Ruling: No, the Service Fee is not subject to the Tennessee sales and use tax.

ANALYSIS

Neither the Seller Fee nor the Service Fee are subject to the Tennessee sales and use tax because the Taxpayer's non-taxable lead generation and payment processing services are the true object of the transactions covered by these fees, and the taxable web-based interface and App are merely incidental. When a transaction involves taxable and non-taxable components, Tennessee uses the true object test to determine if the transaction is taxable.² If the transaction's true object is subject to sales tax, the entire transaction is subject to sales tax.³ Only if the true object of the transaction is not independently subject to sales tax and the items that would be subject to sales tax are "merely incidental" to the true object of the transaction will the transaction not be subject to sales tax.⁴ To begin this analysis, we first determine which components of the transaction are subject to sales and use tax.

² See generally Tenn. Dept. of Rev. Ltr. Rul. 14-10 (Oct. 14, 2014) (discussing Tennessee law regarding bundling and the "true object" test), available at <https://www.tn.gov/content/dam/tn/revenue/documents/rulings/sales/14-10.pdf>, last visited March 1, 2022).

³ *Id.*

⁴ See *Commerce Union Bank v. Tidwell*, 538 S.W. 2d 405 (Tenn. 1976) (finding that transfer of non-taxable information on magnetic tapes was not taxable because the tapes were merely incidental to the purchase of the intangible information; superseded by statute to the extent that previous non-taxable information is considered taxable tangible personal property).

The Seller Fee and Service Fee

The Tennessee sales and use tax applies to services that are specifically enumerated in the Retailers' Sales Tax Act.⁵ The Taxpayer contends that the Seller Fee and the Service Fee are for non-taxable services, claiming that the Seller Fee and the Service Fee are fees for the Taxpayer's lead generation and payment processing services. (These fees are separate transactions from the transactions with Purchasers, which are not addressed in this ruling.)

Sellers use the software to connect with Purchasers who wish to buy their items, and Service Providers use the software to connect with Purchasers who need their items delivered. The Taxpayer characterizes making these connections as lead generation. Connecting these entities is not an enumerated taxable service. The Taxpayer also performs a limited payment processing role between the Sellers, Service Providers, and Purchasers. Payment processing is also not a taxable service.⁶

The Web-Based Interface or App

Computer software is a set of coded instructions designed to cause a computer to perform a task,⁷ and it is subject to Tennessee sales tax even when the software is accessed remotely.⁸ Sellers use the limited functionality of the Taxpayer's web-based interface or App to list items and make sales; Service Providers may use the Taxpayer's web-based interface to track deliveries with GPS, confirm deliveries, accept delivery requests, and report issues. To the extent that the software is in the possession of the Taxpayer and is accessed by users in Tennessee, the use of the web-based interface or App is properly characterized as remotely accessed software.

The True Object of the Transaction

Now, the analysis turns on whether the non-taxable lead generation and payment processing services are the true object of the transaction, and if so, whether the use of the software is merely incidental to those services. When Sellers use the software, their objective is to connect with Purchasers who wish to buy their items. When Service Providers use the software, their objective is to connect with Sellers who need their items delivered. Sellers and Service Providers also have the objective of getting paid. The Taxpayer's objective is to facilitate these connections and process payments. Considering the objectives of all the parties, the true object of the transaction comprises non-taxable lead generation and payment processing services.

The software that grants the Sellers and Service Providers access to the platform merely facilitates lead generation and payment processing. Without connecting to Purchasers who pay for items and have them delivered, the software would be of little to no use to the Sellers and Service Providers. The limited functionality of the software supports the notion that the software is a merely incidental mode

⁵ TENN. CODE ANN. § 67-6-231(b) ("Nothing in this subsection (b) shall be construed to impose a tax on any services that are not currently subject to tax under this chapter...."); *see generally* Tennessee Retailers' Sales Tax Act (codified at TENN. CODE ANN. §§ 67-6-101 to -907 (2018 & Supp. 2020)).

⁶ TENN. CODE ANN. §67-6-231(b).

⁷ TENN. CODE ANN. § 67-6-102(18) (Supp. 2021).

⁸ TENN. CODE ANN. § 67-6-231(b) (2018).

or mechanism for delivering lead generation and payment processing services. Accordingly, the Seller Fee and the Service Fee are not subject to the Tennessee sales and use tax.

APPROVED: David Gerregano
Commissioner of Revenue

DATE: 4/11/2022