

This letter discusses the tax consequence of reward credits. See 86 Ill. Adm. Code 130.401(c). (This is a GIL.)

December 27, 2010

Dear Xxxxx:

This letter is in response to your letter dated July 19, 2010, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

Please be advised that I represent a direct selling company that is registered for the collection and payment of sales taxes with your state. The company has an agreement with your state to pre-collect and remit the applicable tax on its sales to its independent business owners (IBOS) that retail the products in your state.

My client sells products to the IBOS at suggested retail plus shipping charges and pre-collects the sales tax on the suggested retail price and other taxable charges.

The IBO receives commissions on the products based on sales volumes and downline activity.

The IBO sells the products using the party plan. The party plan method of selling is where the IBO holds a party at an individual's (referred to as a hostess) home. The hostess invites individuals to attend for the purpose of having the IBO display and take orders for the products

As an incentive to hold a party and based on the purchases of the individuals attending the party, the hostess may receive product credit that can be redeemed for a gift and a ½ priced item

Based on the above facts, my client requests a ruling on the following:

- If the Company gives product credit redeemable for free product to a hostess for having the party, is sales/use tax due on the suggested retail price of the redeemed item or on the Company's wholesale cost?
- When a hostess purchases products for her own use, is sales tax computed on the sales price before **or** after subtracting the ½ priced discounts?

If you have any questions regarding this request, please contact me.

## **DEPARTMENT'S RESPONSE:**

The Retailers' Occupation Tax Act, 35 ILCS 120/1 *et seq.*, imposes a tax upon persons engaged in the business of selling tangible personal property at retail. The State tax rate is 6.25% of gross receipts for most items, and a lower rate of 1% for qualifying food, drugs and medical appliances. Local occupation taxes may also be applicable.

Regarding your first question, the Department's regulations provide that credits awarded to a host or hostess for sponsoring a party for friends at which a seller may show and solicit orders for her merchandise, and which are awarded based upon the amount of sales generated at the party, are included in gross receipts subject to tax when applied toward purchases of the seller's merchandise. The value of the reward credit equals the dollar amount credited when the reward credit is applied. See 86 Ill. Adm. Code 130.401(c).

When you provide free merchandise to consultants or customers, as a donor, you owe Use Tax on the cost price of the merchandise that you give away to the consultants or customers. See 86 Ill. Adm. Code 150.305(c). Your consultants or customers do not incur a tax liability. As a result, when you purchase tangible personal property that you will give to your consultants or customers, you may not provide your suppliers with a Certificate of Resale because no resale is made. Rather, the supplier must charge, and you must pay, tax on your cost price of the tangible personal property. If the vendor or supplier is an unregistered out-of-state retailer, you must self-assess Use Tax on the cost price of the merchandise and pay that tax directly to the Department of Revenue.

Regarding your second question, gross receipts subject to Retailers' Occupation Tax are defined as all the consideration actually received by the seller. If a seller provides a discount to a purchaser and does not receive a reimbursement or rebate for that discount, only the (discounted) amount received by the seller is taxable. If a seller receives a reimbursement or rebate for a discount, the amount of that reimbursement or rebate is considered part of the taxable gross receipts received by the seller. See 86 Ill. Adm. Code 130.2125.

For information regarding the Department's regulation on the treatment of transportation and delivery charges under the Retailers' Occupation Tax Act, please see 86 Ill. Adm. Code 130.415. Transportation and delivery charges, also designated as shipping and handling charges, are not taxable if it can be shown that the charges are agreed to separately from the selling price of the tangible personal property sold and the charges are actually reflective of the costs of shipping. To the extent the transportation and delivery charges exceed the costs of shipping, the charges will be subject to tax. As noted in subsection (d) of Section 130.415, if the seller and the buyer agree upon the transportation or delivery charges separately from the selling price of the tangible personal property which is sold, then the cost of the transportation or delivery service is not a part of the "selling price" of the tangible personal property which is sold, but instead is a

service charge, separately contracted for, and need not be included in the figure upon which the seller computes his Retailers' Occupation Tax liability.

The best evidence that transportation or delivery charges were agreed to separately and apart from the selling price is a separate and distinct contract for transportation or delivery. However, documentation which demonstrates that the purchaser had the option of taking delivery of the property, at the seller's location, for the agreed purchase price, or having delivery made by the seller for the agreed purchase price, plus an ascertained or ascertainable delivery charge, will suffice. Please be advised that where retailers send merchandise to party hosts or hostesses who then distribute the merchandise to purchasers, shipping and handling charges are generally considered part of the retailer's costs of doing business and are subject to tax. Please refer to Section 130.410.

Information concerning the "Filing of Returns for Retailers by Suppliers Under Certain Circumstances" may be found at 86 Ill. Adm. Code 130.550. This regulation explains that manufacturers, importers or wholesalers can enter into an "agency agreement" with the Department, whereby they register, file returns and remit Retailers' Occupation Tax on behalf of their local distributors.

I hope this information is helpful. If you require additional information, please visit our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) or contact the Department's Taxpayer Information Division at (217) 782-3336.]

Sincerely,

Richard S. Wolters  
Associate Counsel

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