



COLORADO
Department of Revenue

Taxation Division

Physical Address:
1375 Sherman Street
Denver, CO 80203

Mailing Address:
P.O. Box 17087
Denver, CO 80217-0087

GIL-16-012

July 6, 2016

XXXXXXXXXXXXXXXXXXXX
Attn: XXXXXXXXXXXXXXX
XXXXXXXXXXXXXXXXXXXX
XXXXXXXXXXXXXXXXXXXX

Re: Distributor Fees

Dear XXXXXXXXXXXXX,

You submitted on behalf of XXXXXXXXXXXXX (“Company”) a request for guidance on whether Company is liable for sales tax on fees paid by distributors to Company.

The Colorado Department of Revenue (“Department”) issues general information letters and private letter rulings. A general information letter provides a general overview of the relevant tax issues and is not binding on the Department. A private letter ruling provides a specific determination for a specific set of facts, is binding on the Department but not on the taxpayer, and requires payment of a fee. For more information about general information letters and private letter rulings, please see Department Rule 1 CCR 201-1, 24-35-103.5.

The Department treats your request as a general information letter. It is important to remember that general information letters, such as this one, are general discussions of tax law and are not a determination of the tax consequence of any particular action or inaction. If you would like the Department to issue a private letter ruling on the issues you raise, you must submit a new request and provide the fee in compliance with Department Rule 1 CCR 201-1, 24-35-103.5.

Issues

1. Is Company’s renewal fee subject to sales tax?
2. Is Company’s Dashboard and personal website fee subject to sales tax?

Background

Company is a multi-level marketing company that sells goods through its network of distributors. Distributors pay an annual renewal fee to Company to be maintained on

Company's records as "active" distributors. Active distributors purchase Company's goods at discounted prices. The discount is measured by the distributor's volume of sales. Active distributors also receive Company's magazine on a quarterly basis.

Company offers distributors the option to purchase Company's "Dashboard" and a personal website. The Dashboard gives distributors access to information on all activity on the distributorship and online tools to track and manage business. The personal website allows distributors to add customers and downline distributors to their own shopping cart and online sponsoring.

Structure of Analysis

To determine whether Company is required to collect sales tax on the fees, the Department will examine the following questions:

1. Is the fee the purchase of taxable tangible personal property at retail pursuant to § 39-26-104(1)(a), C.R.S.?
2. Is the Dashboard and personal website tangible personal property as defined in § 39-26-102(15), C.R.S.?
 - a. Is Company an application service provider?
 - b. Is the computer software tangible personal property pursuant to § 39-26-102(15), C.R.S.?

Discussion

Colorado levies sales tax on the retail sale of tangible personal property.¹ Tax is calculated on the purchase price paid by the buyer.² The specific issue you raise is whether the renewal fee, which is a fee paid by a customer, is included in the sales tax calculation. To decide this issue it is important to point out that you have identified two items of tangible personal property that are transferred to the buyer (i.e., the distributor) in connection with the payment of the membership fee: the distribution of a magazine and purchases of discounted goods. We examine each item of property below.

We previously issued a general information letter in which we stated that a membership fee is part of the sales tax calculation if payment of the fee results in the transfer of taxable tangible personal property to the buyer.³ In that case, the membership fee was taxable because members received a guidebook, materials for their use in marketing their business to consumers, and a magazine in exchange for the membership fee.

However, there are important differences between Company's membership and the membership described in our prior guidance. Company represents that not only does it give the magazine to distributors but it also gives the magazine to customers for free. This suggests to us that Company is not selling the magazine to distributors in exchange for payment of the renewal fee. Rather, the magazine appears to be more appropriately characterized as promotional material used by Company to market its business plan and

¹ § 39-26-104(1), C.R.S.

² § 39-26-104(1)(a) and 102(7)(a), C.R.S.

³ See, General Information Letter (GIL) 14-008.

goods to distributors and customers. Payment of the membership fee is primarily for the purpose of staying on the “active” list of distributors who are entitled to purchase goods at a discounted price. The magazine is, in this light, incidental to the renewal fee. Therefore, we believe that payment of the renewal fee does not constitute the sale of the magazine.

We next turn to the question of whether buyer’s access to discounted goods is a basis for subjecting the fee to tax. In some instances, fees paid by buyers to access discounted goods may be subject to tax. For example, if a retailer has a membership program that allows members who pay a membership fee to purchase goods for \$1, but nonmembers pay \$3, the payment of the “membership” fee is likely a partial payment of the purchase price and the retailer’s gross taxable sales and, therefore, should be included in the calculation of sales tax.

However, the membership fee is not taxable if the purchase of the discounted tangible personal property is itself not taxable. For example, the fee is not taxable if the member’s purchase of goods is an exempt purchase for resale. In the case you describe, distributors are making nontaxable wholesale purchases for resale to the ultimate consumer. Therefore, the membership fee itself also appears to be nontaxable.

With respect to the Dashboard and personal website fee, Colorado does not impose sales tax on application service providers of software.⁴ Application service providers (ASP) typically offer customers access to computer software maintained on the ASP’s servers. In contrast to an ASP business model, if Company actually delivers computer software to distributors, then the software is subject to tax if it is pre-packaged for repeated sale, has a non-negotiable license, and is delivered in a tangible medium.⁵ If the computer software does not meet each of these three requirements, then it is not taxable.

Miscellaneous

This ruling applies only to sales and use taxes administered by the Department. Please note that the Department administers state and state-collected city and county sales taxes and special district sales and use taxes, but does not administer sales and use taxes for self-collected home rule cities and counties. You may wish to consult with local governments which administer their own sales or use taxes about the applicability of those taxes. Visit our web site at www.colorado.gov/revenue/tax for more information about state and local sales taxes.

This ruling is premised on the assumption Company has completely and accurately disclosed all material facts. The Department reserves the right, among others, to independently evaluate Company’s representations. This ruling is null and void if any such representation is incorrect and has a material bearing on the conclusions reached in this ruling. This ruling is subject to modification or revocation in accordance to Department Regulation 24-35-103.5.

Enclosed is a redacted version of this ruling. Pursuant to statute and regulation, this redacted version of the ruling will be made public within 60 days of the date of this letter. Please let me know in writing within that 60 day period whether you have any suggestions or

⁴ § 39-26-102(15)(C)(ii)(a), C.R.S.

⁵ § 39-26-102(15), C.R.S.

concerns about this redacted version of the ruling.

Sincerely,

Neil L. Tillquist
Colorado Department of Revenue