



STATE OF ARKANSAS
**Department of Finance
and Administration**

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October 25, 2019

[REDACTED]
[REDACTED]
[REDACTED]

Re: Opinion No. 20190923

Dear [REDACTED],

This is in response to your letter dated September 16, 2019 to the Arkansas Department of Finance and Administration ("DFA"). That letter requested a formal legal opinion regarding whether Arkansas sales tax should be paid on an [REDACTED] membership. Your request was assigned to me for response.

Your letter provided the following explanation:

I believe [REDACTED] membership is not taxable. Reasoning behind this opinion is I am paying for a right to buy product on [REDACTED] website and paying Arkansas tax on my purchases. [REDACTED] offers "freebies" to entice membership such as "free shipping", "free" movies, "free" music...some movies and some music are for "rent or buy".

RESPONSE

For the reasons explained more fully below, the amount paid by a customer for an [REDACTED] membership is subject to Arkansas sales tax.

LAW

Arkansas law imposes sales tax on all sales of tangible personal property and on selected services. Among the services subject to tax are certain television, video, and radio services. More specifically, Arkansas Code Annotated § 26-52-301(3)(C)(i) imposes sales tax on the gross receipts or gross proceeds derived from the sale of:

(C)(i) Service of cable television, community antenna television, and any and all other distribution of television, video, or radio services with or without the use of wires provided to subscribers or paying customers or users, including all service charges and rental charges, whether for basic service, premium channels, or other special service, and including installation and repair service charges and any other charges having any connection with the providing of these services.

(ii) The tax levied by this section does not apply to services purchased by a radio or television company for use in providing its services.

(iii)(a) The tax levied by this section applies to the sale of a subscription for digital audio-visual work and digital audio work to an end user that does not have the right of permanent use granted by the seller and the use is contingent on continued payments by the purchaser.

(b) As used in this subdivision (3)(C)(iii):

- (1) “Digital audio-visual work” means an electronically transferred series of related images that when shown in succession, impart an impression of motion, together with accompanying sounds, if any; and
- (2) “Digital audio work” means an electronically transferred work that results from the fixation of a series of musical, spoken, or other sounds, including ringtones

Some transactions include more than one product as part of a retail sale. Those transactions are referred to by state law as “bundled transactions”. State law contains special rules for bundled transactions. The term “bundled transactions” is defined in Ark. Code Ann. § 26-52-103(2) as follows:

(2)(A) “Bundled transaction” means a retail sale of two (2) or more products, except real property and services to real property, in which:

- (i) The products are otherwise distinct and identifiable; and
- (ii) The products are sold for one (1) nonitemized price.

(B) “Bundled transaction” does not include the sale of any product in which the sales price varies or is negotiable based on the selection by the purchaser of the products included in the transaction.

(C) The Department of Finance and Administration shall promulgate rules to implement this subdivision (2);

As directed by Ark. Code Ann. § 26-52-103(2)(C), DFA promulgated Gross Receipts Tax Rule GR-93 concerning the treatment of bundled transactions. That rule reads, in relevant part, as follows:

- A. Except as otherwise provided by this rule, sales tax must be collected on the sales price of a bundled transaction if any product included in the bundled transaction would be taxable if sold separately.
- B. **PRODUCTS.** For purposes of this rule, products include tangible personal property, services, intangibles, and digital goods. Products do not include real property and services to real property.

Examples: Services to real property include building framing, roofing, plumbing, electrical, painting, janitorial, pest control, and window cleaning.

- C. **BUNDLED TRANSACTION.** A bundled transaction is the retail sale of two (2) or more products where the products are otherwise distinct and identifiable, and the products are sold for one non-itemized price.
 - 1. **Distinct and Identifiable Products.** A bundled transaction is a retail sale of two (2) or more products that are “distinct and identifiable”. The following are not distinct and identifiable products.
 - a. Packaging is not a separate and distinct product when it accompanies the retail sale of a product and is incidental or immaterial to the retail sale thereof.

Examples: Packaging that is incidental or immaterial to the retail sale include grocery sacks, shoeboxes, dry cleaning garment bags, express delivery envelopes and boxes, bottles, or other materials such as wrapping, labels, tags, and instruction guides.

- b. A product provided free of charge with the purchase of another product is not a separate and distinct product. A product is considered to be provided free of charge if the sales price of the product purchased does not vary based on the inclusion of the product that was provided free of charge. Such products provided free of charge are considered “promotional products”.

Examples: A free car wash with the purchase of gasoline, or free dinnerware with the purchase of groceries.

- c. Items included in the definition of “sales price” and “purchase price” are not distinct and identifiable products. (See GR-3 and UT-3.)

2. One Non-itemized Price. If a retail sale of two (2) or more distinct and identifiable products is not made for one non-itemized price, then the retail sale is not a bundled transaction. A retail transaction is not sold for one non-itemized price in the following scenarios:
 - a. If, by negotiation or otherwise, the sales price varies or is negotiable based on the purchaser's selection of the products being sold;
 - b. If the purchaser has the option of choosing products or declining to purchase any of the products being sold and, as a result of the purchaser's selection of products, the sales price varies, or a different price is negotiated;
 - c. The price is separately identified by product on binding sales or other supporting sales-related documentation, which is made available to the customer in paper or electronic form, such as an invoice, bill of sale, receipt, contract, service agreement, lease agreement, periodic notice of rates and services, rate card, or price list;
 - d. If a seller bills or invoices one (1) price for the sale of distinct and separate products, but the price invoiced is equal to the total of the individually priced or itemized products contained in the supporting sales related documentation, such as a catalog, price list, or service agreement; or
 - e. If the seller bills or invoices one price for a transaction that includes a bundle of products and also includes one (1) or more additional products that are individually priced or itemized in a catalog or price list, the additional products individually priced or itemized will not be considered to be a part of the bundled products sold for one non-itemized price.
 - f. If a transaction does not qualify as a bundled transaction because of the provisions in GR-93(C)(2)(a)-(C)(2)(e), the transaction will not be classified as a bundled transaction as a result of the seller offering a subsequent discount of the total sales price without itemizing the amount of the discount for each product. In such a situation, if there is no sales-related documentation showing the allocation of the discount, the discount will be considered to be allocated pro rata among the otherwise separately itemized products.
- D. EXCLUSIONS FROM BUNDLED TRANSACTIONS. A transaction that otherwise meets the definition of a bundled transaction as defined above is not considered a bundled transaction if the transaction falls within one of the following exceptions.

1. True Object Exclusion. This exclusion only applies to transactions that include a service. The exclusion does not apply to transactions that include only tangible personal property.

a. The retail sale of tangible personal property and a service where the true object of the transaction is the service and the tangible personal property is essential to the use of the service and is provided exclusively in connection with the service. If the transaction is not a bundled transaction as a result of this exception, then the true object of the transaction will be the retail sale of the service and should be taxed accordingly.

Example: Computer programming services where the client is given a back-up disk and instruction manual. The true object of the transaction is the provision of the programming services. The computer programmer is selling nontaxable services and is not making a sale of a bundled transaction. Arkansas sales tax is not due on the programmer's charge for services; sales tax is due on the programmer's purchases of tangible personal property used to fulfill the service.

b. The retail sale of services where one (1) service is provided that is essential to the use or receipt of a second service and the first service is provided exclusively in connection with the second service, and the true object of the transaction is the second service. If the transaction is not a bundled transaction as a result of this exception, then the true object of the transaction will be the retail sale of the second service and should be taxed accordingly.

c. Factors that should be considered to determine the true object of a transaction are the following: the seller's line of business; the purchaser's object of the transaction; whether the tangible personal property or service that is essential to the second service is available for sale separately without the second service; and how the tangible personal property or service is essential to the second service.

d. Sellers of a bundled transaction that includes tangible personal property and a service or a bundled transaction that includes multiple services may use the true object exclusion or the de minimis exclusion.

2. De Minimis Exclusion. This exclusion may be applied to transactions that include all types of products. If the taxable product in a transaction is de minimis, then the transaction is not taxable.

a. "De minimis" means the seller's purchase price or sales price of the taxable product is ten percent (10%) or less of the total purchase price or sales price of the products.

b. A seller may use either the purchase price or the sales price of the products to determine if the price of the taxable products is de minimis. A seller may not

use a combination of the purchase price and sales price of the products to determine if the price of the taxable products is de minimis.

- c. A seller must use the full term of a service contract to determine if the taxable products in the transaction are de minimis. For the purpose of determining whether services in the transaction are de minimis, the price of the services shall not be prorated based on the term of the service contract.
 - d. Sellers of a bundled transaction that includes tangible personal property and a service or a bundled transaction that includes multiple services may use the true object exclusion or the de minimis exclusion.
3. Food, Drugs, and Medical Items. This exclusion does not apply to transactions that include services. If the nontaxable products in a transaction are the primary products of the transaction (more than fifty percent (50%)), then the transaction is not taxable.
- a. For this exclusion to apply, at least one (1) product must be food and food ingredients, drugs, durable medical equipment, mobility enhancing equipment, over-the-counter drugs, a prosthetic device, or disposable medical supplies. (See GR-3, GR-38, and GR-38.2 for definitions of these terms.)
 - b. A seller may use either the purchase price or the sales price of the products to determine if the taxable tangible personal property is fifty percent (50%) or less of the total purchase price or sales price of the tangible personal property. A seller may not use a combination of the purchase price and sales price of the tangible personal property when making the fifty percent (50%) determination for a transaction.

Example: A retailer prepares and sells gift boxes that consist of the following items: a mug, a book, and coffee beans. The seller's purchase prices for the items are \$3.00, \$5.00, and \$3.00, respectively; the total purchase price for the items is \$11.00. The purchase price of the non-food items, subject to the full state sales tax rate, is \$8.00. The purchase price of the coffee, subject to the reduced state sales tax rate on food and food ingredients, is \$3.00. The gift box is subject to the full state sales tax rate and any applicable local tax because the percentage for the non-food items is 73% ($\$8.00/\$11.00 = .727$). (Note: If the percentage for the food and food ingredients in the gift box was more than fifty percent (50%), then the gift box would be subject to the reduced state sales tax rate and any applicable local tax.)

ANALYSIS

The applicability of the Arkansas sales and use tax to a [REDACTED] depends first on whether the membership falls within the definition of a “bundled transaction” as defined in Ark.

Code Ann. § 26-52-103. If it is determined that a █████ Membership does fall within the definition of a bundled transaction, it will then be necessary to determine whether any of the specific benefits provided as part of a █████ Membership would be taxable transactions if provided separately.

Your letter indicates that the █████ membership involves the customer paying for the right to purchase product and, in addition, receiving a package of free goods and services. Our research regarding an █████ membership reveals that the facts surrounding an █████ membership are somewhat different than you describe.

That research reveals that the █████ membership allows the customer to pay a monthly or annual fee to receive the membership. The member gains the intangible right to access certain benefits associated with shopping on █████ and gain access to additional benefits that include:

- Free or discounted shipping;
- Access to view movies and television shows;
- Lending Library allowing members who own █████ devices to access books;
- Receive free e-books;
- Access to █████ products, such as baby wipes;
- Discounted pricing on certain items;
- Early access to certain products and deals;
- Unlimited access to music that is steamed or downloaded;
- Photo and video storage;
- Original programs, comedy, lectures, and audio editions of published articles;
- Access to a rotating selection of books, magazines, comics, etc.;
- Interactive video game platform.

That research also reveals that most of these membership benefits expire if the member cancels their membership. Accordingly, the member is paying for a package of membership benefits with the right to make purchases from █████ website being just one of benefits acquired through the purchase of the membership.

A █████ Membership entitles the customer to use various goods, services, and other benefits upon payment of a single monthly or annual price. A █████ Membership includes the retail sale of two or more products which are distinct and identifiable, and which are sold for one nonitemized price. Consequently, a █████ Membership is a bundled transaction as defined in Ark. Code Ann. § 26-52-103(2) and Gross Receipts Tax Rule GR-93.

A █████ Membership is subject to Arkansas sales and use tax as a bundled transaction if at least one of the Prime Membership benefits if sold separately. A review of the various benefits provided under a █████ Membership reveals that several of those benefits would be subject to Arkansas sales and use tax if sold separately. Specifically, Ark. Code Ann. § 26-52-301(3)(C)(i) provides that sales tax is due on the:

Service of cable television, community antenna television, and any and all other distribution of television, video, or radio services with or without the use of wires provided to subscribers or paying customers or users, including all service charges and rental charges, whether for basic service, premium channels, or other special service, and including installation and repair service charges and any other charges having any connection with the providing of these services.

Accordingly, a [REDACTED] Membership is subject to sales tax as a bundled transaction because components of that transaction are taxable television, video, or radio services.

This opinion is based upon my understanding of the facts as set out in your inquiry and as current Arkansas laws and rules govern those facts. Any change in the facts or law could result in a different opinion. Please be advised that this opinion may only be relied upon by the company and will only be binding upon the Department for three (3) years from the date of issuance. Arkansas Gross Receipts Rule GR-75.

Sincerely,

John Theis
Revenue Legal Counsel