



# The Price of Customer Loyalty: Rewards Programs and Sales and Use Tax Issues



Retailers and other businesses use loyalty and rewards programs to draw in customers throughout the year. However, there are several sales and use tax consequences of promoting consumer loyalty. Here’s a brief question and answer guide to help ensure rewards programs are rewarding for everybody.

## Who is required to collect (and remit) sales and use tax when a customer redeems loyalty rewards points?

Retailers with customer loyalty programs, including coupons or discounts and points, rewards or bonus dollars, should be aware that they may be required to collect sales tax on the nondiscounted price in some circumstances.

## What can tax departments do to be proactive?

Because the laws, regulations and official guidance in this area are often tied to the specific structure and payment arrangements in place with each particular program, tax departments are advised to maintain constant communication with their business colleagues. As a loyalty rewards program evolves, so do the tax consequences. While one type of reward may be subject to tax, another may be exempt. Understanding the business arrangements on a current basis will help a tax department stay abreast of potential changes needed in its tax reporting.

## When should a retailer include rewards point redemption, coupons or other discounts in the sales price?

Each type of “reward” may have a different tax treatment, and retailers should review their states’ requirements. For example, in Washington, which has adopted the Streamlined Sales and Use Tax Agreement, generally the sales price includes (among other things) rewards for completing retailer surveys, rewards purchased for cash and rewards received for purchases using a co-branded credit card, for which the bank reimburses the retailer.

## Where can retailers look for state-specific guidance?

Given the state-specific nature of these rules, retailers are advised to review their business and identify the states where the company has the largest amount of loyalty rewards activity to determine how to best treat their redemption programs. Some states, such as New York and Washington, have published rulings and guidance on the treatment of certain types of programs. If a retailer operates in a state that

has adopted the Streamlined Sales and Use Tax Agreement, it can look to its illustrative provisions in determining whether redemptions should be included. In states without clear guidance, retailers may find it advisable to seek a ruling from the state department of revenue.

### **Why should retailers care?**

The risk of noncompliance varies from state to state, but two main risks are universal. If a company does not collect tax when loyalty rewards points are redeemed, it runs the risk of being audited in states where tax is due and assessed for tax that was not collected. Penalties may also apply. If a company collects tax across all of its programs in all of its states, it runs the risk of a class action lawsuit by consumers in states where it has over-collected.

### **How can a retailer find out more?**

[Here is a more detailed description](#) of some of the tax issues, along with in-depth analysis of the sales and use taxation of loyalty programs in New York, Georgia and Washington. For further questions about anticipated tax liability, contact experienced counsel.

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