



QUESTION: ARE THE MANUAL AND/OR AUTOMATED FRAUD PREVENTION ACTIVITIES PERFORMED AS PART OF THE TAXPAYER'S COUPON PROCESSING SERVICES TAXABLE AS PROTECTIVE SERVICES UNDER SECTION 212.05(1)(I)1, F.S.?

ANSWER – BASED ON THE FACTS BELOW: THE “MANUAL AND/OR AUTOMATED FRAUD PREVENTION ACTIVITIES” PERFORMED AS PART OF THE TAXPAYER'S COUPON PROCESSING SERVICES DO NOT FALL WITH THE NAICS CLASSIFICATIONS LISTED IN S. 212.05(1)(I)1., F.S., AND, AS A RESULT, ARE NOT SUBJECT TO SALES TAX.

THE TAXPAYER'S PURCHASE OF THIRD-PARTY INVESTIGATIVE SERVICES IS SUBJECT TO SALES TAX WHEN THE SERVICES ARE USED WITHIN FLORIDA OR WHEN THE PRIMARY BENEFIT OF THE SERVICES IS WITHIN FLORIDA.

December 9, 2016

Re: Technical Assistance Advisement 16A-019
Sales and Use Tax – Coupon Redemption Services
Sections 212.05 and 215.26, Florida Statutes (F.S.)
Rules 12A-1.0092 and 12A-1.0161, Florida Administrative Code (F.A.C.)
XXXX (the Taxpayer)
EIN XXXX

Dear XXXX:

This is in response to your letter dated July 21, 2016, received by this office on July 26, 2016, requesting this Department's issuance of a Technical Assistance Advisement (“TAA”) pursuant to section 213.22, F.S., and Rule Chapter 12-11, F.A.C., concerning the taxability of “manual and/or automated fraud prevention activities” provided by the Taxpayer. An examination of your letter has established you have complied with the statutory and regulatory requirements for issuance of a TAA. Therefore, the Department is hereby granting your request for a TAA.

Facts

Your letter dated July 21, 2016, provides that following in part:

... The Taxpayer provides coupon clearing services for discount coupons redeemed at retail stores located in the state of Florida by consumers who reside in Florida. The Taxpayer's client is the retailer who redeems the coupons or the advertiser whose product or service is subject to the discount offered via the coupon. The Taxpayer does not design, print, or distribute coupons. Instead, the Taxpayer's clients engage the Taxpayer to manage coupon information and the monetary transactions connected with the redemption of physical and electronic coupons by consumers.

Child Support – Ann Coffin, Director • General Tax Administration – Maria Johnson, Director
Property Tax Oversight – Dr. Maurice Gogarty, Director • Information Services – Damu Kuttikrishnan, Director

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. . . The Taxpayer is a coupon clearinghouse that facilitates the flow of data and funds for its clients. Each of the Taxpayer's clients must enter into a written coupon clearing services agreement that explicitly establishes a formal agency relationship between the Taxpayer and the client. This agency relationship is disclosed to all retailers and advertisers with whom the Taxpayer interacts on behalf of the client. Further, standard industry practice ensures that all parties interacting with the Taxpayer recognize that the Taxpayer is a formal agent on behalf of its client.

. . . The Taxpayer's services as provided to advertisers typically consist of:

1. Receipt and separation of coupons
2. Manual scanning of coupons into the Taxpayer's production system
3. Manual review of coupons for fraud prevention
4. Automated analysis of coupons by the Taxpayer's system to support fraud prevention
5. Automated application of advertiser payment policies (regarding coupon expiration dates and redemption exceptions)
6. Destruction of the physical coupons after processing
7. Transmission of coupon data to the Taxpayer's servers for storage
8. Tabulation of payments owed by advertisers to retailers, transmission of the required funds to retailers, and management of an advertiser's on-going funding requirements

The Taxpayer's services for retailers contemplate coupon verification, but they do not contain the fraud prevention activities specifically required by advertisers. The Taxpayer's base coupon clearing service fee is a bundled charge that contains three components - one of which is "payment processing." The payment processing component of the Taxpayer's fee covers the fraud prevention aspects of the Taxpayer's coupon clearing activities.

In performing its services, the Taxpayer populates databases within its production systems with the offer and coupon data obtained from scanning and validating the coupons submitted by the retailers. All scanning activities occur outside Florida; the servers on which the data is stored are located outside the state of Florida; and the maintenance of the servers occurs outside the state of Florida.

The Taxpayer has no facilities, employees, or inventory in Florida. However, the Taxpayer's employees visit clients and solicit new business within Florida. . . .

* * *

On September 8, 2016, you e-mailed electronic copies of the Taxpayer's "two contract templates," and provided that the "'Manufacturer' template applies to the 'advertiser' clients I reference in our ruling. The 'Retailer' template applies to our 'retailer' clients."

The Agreement for Manufacturer Services provides the following in part:

[The Taxpayer] and . . . ("Client") hereby agree that [the Taxpayer] will provide Client coupon redemption services on the following terms:

1. Client designates [the Taxpayer] as its exclusive agent to redeem and process all merchandise coupons in any form including, but not limited to, paper, electronic, mobile, digital and any other forms, issued or authorized by Client.

2. [The Taxpayer] shall perform the following services for Client:

- a) Provide redemption services for both paper and electronically distributed offers . . .
- b) Secure and assign Client a redemption address to which all coupon submissions will be sent.
- c) Maintain the [Taxpayer] Retailer Master File and verify the existence of each submitter. If a submitter is not in the [Taxpayer] Retailer Master File, [the Taxpayer] will initiate verification procedures to be completed at the earliest possible date. Should the [the Taxpayer] verification procedures determine that a submitter is not a valid retailer, [the Taxpayer] shall suspend payments.
- d) Determine the appropriate count and value for all retailer coupon submissions and pay said submissions in accordance with Client's Redemption Policy, written payment policies, and any other written instructions ("Written Instructions") provided to [the Taxpayer] . . .
- e) Promptly destroy all redeemed coupons and provide a yearly affidavit of such destruction, upon request. . . .
- f) For twelve (12) months, maintain invoice and store tag documentation, as well as coupons that [the Taxpayer] has identified as potentially physically misredeemed. . . .
- g) Provide Client via the internet with one current transaction register of all coupon submissions and current monthly offer redemption reports in up to two different formats. . . .
- h) As an adjunct to [the Taxpayer] service, [the Taxpayer] will provide Client with a URL and passwords that will allow designated users to access the [Taxpayer's] software [product] via an internet browser to aid in the administration and management of Client's coupon programs. . . .
- i) Accumulate and maintain the most current twelve (12) rolling months of Client's transaction history for Client's reference. . . .
- j) Provide general information and assistance on common retailer and retailer clearinghouse inquiries

3. Client shall:

- a) Pay the greater of (i) [the Taxpayer] service fees . . . or (ii) a minimum fee of \$___ per month for [the Taxpayer] to administer and execute Client's redemption policies and the systems necessary to provide services outlined in Section 2 of this Agreement. . . .

* * *

c) Pay a per invoice record and store tag record transaction fee of \$____ (“Transaction Records Fee”) for [the Taxpayer] to maintain a record of all submitting entities for purposes of audit support and analysis.

d) Reimburse [the Taxpayer] for expenses incurred in relationship to:

...

- Retailer site audit, verification and fraud detection expenses incurred by [the Taxpayer], which will be invoiced three (3) times per year for the prior four (4) month period.

* * *

6) [The Taxpayer] will employ reasonable and diligent precautions against errors in receiving, handling and accounting for Client’s coupons and for the analysis and reporting of information hereunder, but shall not be liable for any errors or the redemption of forged or improperly acquired coupons. . . .

* * *

The Agreement for Retailer Services provides the following in part:

[The Taxpayer] and (“Client”) hereby agree that [the Taxpayer] will provide Client a consolidated coupon settlement service program (“Services”) on the following terms:

1. Client designates [the Taxpayer] as its exclusive agent to invoice and submit coupons to coupon issuers for redemption on its behalf and request such issuers to reimburse [the Taxpayer] as Client’s authorized agent.

2. [The Taxpayer] shall perform the following Services for Client:

a) For coupons which [the Taxpayer] is responsible for arranging shipping from Client’s locations

b) Receive coupons which Client submits and based on the scanning of coupons and a reasonable visual review, will sort, audit, and determine the count and value.

c) Invoice and submit coupons or electronic data to the coupon issuer. . . .

d) Use reasonable commercial efforts to collect the payments for invoices submitted to coupon issuers

e) Pay for the coupon face value plus handling allowance less [Taxpayer’s] service fees and any adjustments

f) As an adjunct to [the Taxpayer’s] service, [the Taxpayer] will provide you with a URL and passwords that will allow designated users to access the [Taxpayer] software via an internet browser to aid in the administration and management of Client’s coupon programs.

...

3. Client shall:

- a) Pay the [Taxpayer] service fees for Services, as described in Exhibit 1. The [Taxpayer] service fees set forth on Exhibit 1
- b) Pay [the Taxpayer] for any additional services provided by [the Taxpayer]

* * *

5. In view of the nature of the Services to be performed, it is agreed that [the Taxpayer] shall not be liable for any loss, injury or damage of any kind caused in whole or in part by contingencies beyond the control of [the Taxpayer]

* * *

In an e-mail dated September 21, 2016, you provided the following regarding the Client's responsibility to reimburse the Taxpayer for items identified in Section 3)d), of the Agreement for Manufacturer Services:

1. Advertiser Contract Provision - The clause identified from paragraph 3(d) refers to our third-party costs for verifying the existence of a retail store location and the nature of the business conducted at that retail store location.

a. . . . If [the Taxpayer] is suspicious about the validity of a submission received from a particular store, [the Taxpayer's] personnel will perform certain investigative services via the internet, etc. to try to confirm that the store is real and that it sells the type of products for which the store is submitting coupons. . . . If [the Taxpayer's] personnel cannot successfully verify the store, [the Taxpayer] sends a third-party into the field to perform the investigation. This contract clause refers to the client's obligation to compensate [the Taxpayer] for the third-party's services.

b. . . . [The Taxpayer] is continuously sending this third party into the field to verify store existence and product mix to support the requirements of multiple manufacturers. . . . As such, [the Taxpayer] accumulates the fees billed by the third party over the course of a quarter, allocates the sum between clients, and separately bills each client an allocated portion of the third party's fees. [The Taxpayer] has a separate billing item that covers this fee.

2. Services When Fraud Detected - [the Taxpayer] essentially has three prongs to its fraud detection services as performed for advertisers. (These services do not apply to retailers.) First, [the Taxpayer's] fees include certain retailer verification services. The scope of these services is described under 1a above. When the services are performed by [the Taxpayer's] personnel, the service is covered by [the Taxpayer's] base coupon clearing fee. When the service is performed by a third party, [the Taxpayer] uses a unique billing item to charge the client. Second, [the Taxpayer's] services include certain automated analytical retailer comparison services. The [Taxpayer's] system contains algorithms that compare similarly situated retailers to each other to verify comparable coupon volumes and coupon types. When a retailer's submissions fall outside the accepted parameters, the system flags the submission as potentially fraudulent. These services are included in [the Taxpayer's] base coupon clearing fee. Third, [the Taxpayer's] plant personnel

perform a physical review of a sample from each shipment received that contains between 5 to 2,000 coupons in order to try to visually identify fraud. Examples of observable fraud include coupons that are gang-cut, mass-torn, in mint condition, or purposely washed and wrinkled. This physical review service is covered by [the Taxpayer's] base coupon clearing fee. Assuming [the Taxpayer] believes a submission is fraudulent (based on any of these three techniques), [the Taxpayer] advises the manufacturer that a submission is potentially fraudulent and recommends an amount that should not be paid to the submitting retailer. [The Taxpayer's] services stop there. If the client wants further information or wants to take any kind of specific action, the obligation to pursue further action resides with the advertiser.

* * *

Requested Advisement

The Taxpayer requests advisements with respect to the following:

1. Are the manual and/or automated fraud prevention activities performed as part of the Taxpayer's coupon processing services taxable as protective services under Fla. Stat. §212.05(1)(i)1[.]?
2. If certain of the Taxpayer's services are taxable protective services, what is the sourcing methodology applicable to the Taxpayer's taxable services?

Applicable Authority and Discussion

Section 212.05(1)(i)3., F.S., imposes sales and use tax on only certain specifically identified services. The laws governing sales and use tax on services mandates that the Department rely upon the North American Industry Classification System (NAICS) for guidance in determining whether a service is subject to sales and use tax.¹ The services subject to tax include "detective, burglar protection, and other protection services," which are any of the services enumerated in NAICS National Numbers 561611, 561612, 561613, and 561621 of the North American Industry Classification System, as published in 2007 by the Office of Management and Budget, Executive Office of the President.

Rule 12A-1.0092(2)(a), F.A.C., clarifies that "detective, burglar protection, and other protection services are those services which are rendered to minimize or prevent loss or damage to life, limb, or property and are of a kind typically performed by security or alarm system companies, or are those investigative services which are rendered to obtain evidence or other information for legal, business, employment, or personal purposes of a kind typically performed by detective or investigative agencies." According to s. 212.05(1)0)4., F.S., and Rule 12A-1.0092(3)(a), F.A.C., where any sale of a service involves both the sale or use of a service which is taxable and the sale or use of a service which is not taxable, the charges for the taxable portion of the transaction must be separately stated from the charges for the nontaxable portion or the entire transaction will be presumed taxable.

¹ The NAICS provides business establishment classifications for use by Federal agencies when describing various statistical analyses of the U.S. economy.

A review of NAICS codes reveals that “coupon processing services” and “coupon redemption services” are listed under NAICS code #561990, “All Other Support Services.” Accordingly, given this is not a taxable NAICS code as identified under s. 212.05(1)(i), F.S., the Taxpayer’s coupon redemption services, as described in the Agreement for Manufacturer Services and the Agreement for Retailer Services, are not subject to tax.

However, the investigative services referenced in paragraph 3(d) of the Agreement for Manufacturer Services are provided to the Taxpayer in order to “minimize or prevent loss . . . [and are] of a kind typically performed by detective or investigative agencies.” These investigative services are akin to the type of activity that is included in the Industry Group #561611.² Section 212.05(1)(i)3., F.S., and Rule 12A-1.0092(2)(f), F.A.C., provide that charges for investigative services are subject to Florida sales tax when performed within or outside Florida and used within Florida by the purchaser or when the purchaser’s primary benefit of the service is within Florida. If the taxable service is performed within Florida but used outside this state by the purchaser or when the purchaser’s primary benefit of the service is located outside Florida, then the service is not subject to tax.

Rule 12A-1.0161(4), F.A.C., provides that in order for a purchase of taxable services to be considered exempt from sales tax when the service is later resold, there are four conditions that must be met. The first requirement is that the purchase must provide direct and identifiable benefit to a single client or customer. You have provided that the investigative services performed by the third party on behalf of the Taxpayer “support the requirements of multiple manufacturers.” The Taxpayer “allocates the sum between clients, and separately bills each client an allocated portion of the third party’s fees.” Because of this, the Taxpayer cannot purchase the investigative services exempt from sales tax. The Taxpayer is considered to be the end user, or consumer, of the third party investigative services.

Conclusions

The “manual and/or automated fraud prevention activities” performed as part of the Taxpayer’s coupon processing services do not fall with the NAICS classifications listed in s. 212.05(1)(i)1., F.S., and, as a result, are not subject to sales tax.

The Taxpayer’s purchase of the third-party investigative services described in your e-mail dated September 21, 2016, is subject to sales tax when the services are used within Florida or when the primary benefit of the services is within Florida.

In the event the Taxpayer has collected sales tax from its customer on nontaxable services, the Taxpayer must first refund its customers and then file an Application for Refund - Sales and Use Tax Form DR-26S, within the 3-year statute of limitations. See s. 215.26(2), F.S.

² 561611 Investigation Services: This U.S. industry comprises establishments primarily engaged in providing investigation and detective services. <http://www.census.gov/cgi-bin/sssd/naics/naicsrch>

This response constitutes a Technical Assistance Advisement under section 213.22, F.S., which is binding on the Department only under the facts and circumstances described in the request for this advice as specified in section 213.22, F.S. Our response is predicated on those facts and the specific situation summarized above. You are advised that subsequent statutory or administrative rule changes, or judicial interpretations of the statutes or rules, upon which this advice is based, may subject similar future transactions to a different treatment than that expressed in this response.

You are further advised that this response, your request and related backup documents are public records under Chapter 119, F.S., and are subject to disclosure to the public under the conditions of section 213.22, F.S. Confidential information must be deleted before public disclosure. In an effort to protect confidentiality, we request you provide the undersigned with an edited copy of your request for Technical Assistance Advisement, the backup material, and this response, deleting names, addresses, and any other details which might lead to identification of the taxpayer.

Your response should be received by the Department within 15 days of the date of this letter.

Sincerely,

Brinton Hevey
Tax Law Specialist
Technical Assistance and Dispute Resolution
850/717-6839

Record ID: 211513