

Excise Tax Advisory

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ETA 3191.2022

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Rewards Programs

Introduction and Scope

This Excise Tax Advisory (ETA) addresses the following regarding rewards programs:

- The application of “sales price” to selected types of rewards program awards. Specifically, this ETA provides guidance on:
 - When awards must be included in the sales price of a customer’s purchase for retail sales tax purposes, or
 - When the awards represent a discount excluded from the sales price.
- The seller’s tax liability when a customer redeems awards for the full price of a good or service.
- The tax treatment of rewards programs that commingle both awards representing taxable consideration and awards representing bona fide discounts.

This ETA does not address rewards program awards that differ materially from the examples provided. This ETA does not address gift cards, gift certificates, or discount vouchers purchased by consumers and subsequently redeemed in retail transactions.

Relevant Laws and Definitions

For purposes of this ETA, the following laws and definitions apply:

Retail sales tax is imposed on the selling price of each retail sale in Washington. RCW 82.08.020(1).

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- **“Retail sale”** includes the sale of tangible personal property and certain services to consumers. RCW 82.08.010; RCW 82.04.050.
 - **“Sale”** means any transfer of the ownership of, title to, or possession of property for a valuable consideration and includes any activity classified as a “retail sale” under RCW 82.04.050. RCW 82.04.040.
 - **“Selling price”** or **“sales price”** means the total amount of consideration for which tangible personal property, extended warranties, or other services or anything else defined as a retail sale under RCW 82.04.050 are sold. RCW 82.08.010; WAC 458-20-108.

In general, use tax is imposed when a person uses, as a consumer in Washington, tangible personal property or services, if the sale or use was not already subject to retail sales tax. RCW 82.12.020.¹

- **“Consumer”** includes any person who purchases, acquires, or uses tangible personal property or any service defined under RCW 82.04.050(2)(a) other than for resale or for the purpose of satisfying an obligation under an extended warranty. RCW 82.12.010; RCW 82.04.190.
- **“Use”** has its ordinary meaning and means as follows, with respect to tangible personal property and services defined under RCW 82.04.050(1)-(2):
 - The first act within Washington by which a taxpayer takes or assumes dominion or control over the tangible personal property (as a consumer); or
 - The first act after the service has been performed by which a taxpayer takes or assumes dominion or control over the article of tangible personal property upon which the service was performed (as a consumer).

What is a rewards program?

A **rewards program** is a program that provides customers with an award to encourage customer loyalty based on the occurrence of a specified event or conditioned upon specified customer behavior, activity, promise, or payment. Functionally, these programs permit customers to earn awards and then apply the awards to present or future purchases. Rewards program awards are often referred to as “points,” “checks,” “discounts,” “rewards,” “rebates,” or “coupons.” The retail sales tax treatment of any rewards program award depends on the facts and circumstances of the specific program award and does not depend on how the program provider identifies the program or its related awards in its sales, marketing, or other similar materials.

¹ Where this ETA concludes that use tax applies to an item, it assumes that the user had not previously paid retail sales tax on that item.

Rewards programs differ from discount voucher programs. Discount vouchers are offered and sold by third-party companies to customers. The customers then redeem the vouchers with sellers in exchange for goods or services. Discount vouchers are often purchased by customers at a reduced or discounted price. See [ETA 3233.2022](#) and [WAC 458-20-108](#) for more information on the taxation of discount vouchers.

Taxability of rewards program awards generally

Sales Tax is Imposed on the Sales Price

Retail sales tax is imposed on the sales price of a retail sale. The “sales price” includes the total amount of consideration paid for a product or service, including cash, credit, property, and services, valued in money, whether received in money or otherwise. See [RCW 82.08.010](#). The “sales price” does not include bona fide discounts. See [RCW 82.08.010](#).

Awards that are not Bona Fide Discounts

Reward program awards representing consideration paid by the customer to the seller are not bona fide discounts and must be included in the sales price upon redemption for the seller’s products (goods and services). An example of a rewards program award representing consideration paid by the customer is any award provided in exchange for property, service, credit, or cash. Awards that may be purchased for cash, redeemed for cash, or converted to cash are also considered taxable consideration as cash equivalents.

In this context, a rewards program member’s provision of their name, telephone number, email address, and/or physical address in the ordinary course of business does not represent consideration to the seller for retail sales tax purposes because this information is presumed necessary to operate the seller’s rewards program.

Awards that are Bona Fide Discounts

Awards that are bona fide discounts are excluded from the sales price (discount awards). These discount awards will be excluded from the sales price unless the seller receives consideration from a third party as provided in [RCW 82.08.010](#). Discount awards include awards provided solely for enrollment in a rewards program, the passage of time, or purchasing the seller’s products. Bona fide discount awards also include price reductions provided to customers solely for their membership in a seller rewards program.

Taxability of rewards programs with commingled awards

A rewards program may issue program members awards, some of which represent taxable consideration (taxable awards) and some of which are treated as discounts to the sales price (discount awards). In some cases, sellers may commingle these awards. For example, under a rewards program, a seller may issue discount awards to members on each member’s birthday and also provide taxable awards to

members in exchange for completing a survey. Or, for example, a seller may issue discount awards to members based on the volume of purchases from the seller and also provide taxable awards to members based on purchases with co-branded credit cards.

Sellers have two options regarding the tax treatment of commingled awards. One, the seller may accurately track the taxable and non-taxable awards. Two, if the seller cannot accurately track the taxable and non-taxable awards, the seller can prepay the tax at the time of issuance of the awards. If sellers do not follow one of these two options, all the awards will be presumed to be taxable at the time of redemption.

Option 1: Track Taxable and Nontaxable Awards Until Redeemed

Sellers that track taxable and non-taxable awards must maintain sufficient records to identify retail-taxable awards within a comingled program and must calculate the combined state and local tax rate using the cascading steps outlined in [RCW 82.32.730](#). Discount awards will not be considered bona fide discounts unless the seller maintains proper documentation, which must be available for examination by the Department. See RCW [82.32.070](#) and WAC [458-20-254](#). The documentation must demonstrate that tax was accurately calculated and remitted, and reflect the method used for calculating the tax.

Option 2: Prepayment

When sellers comingle taxable and discount awards, the Department will recognize a prepayment method in place of the general presumption under limited circumstances. To qualify for the prepayment method, the seller must prepay retailing B&O and retail sales tax on taxable awards that have been comingled with discount awards at the time the taxable awards are issued, based on the combined state and local tax rate of the customer's address that is available from the business records of the seller. See [RCW 82.32.730\(1\)\(c\)](#). Under this method, no retail sales tax will be due when the discount awards are redeemed.

Again, the seller must maintain adequate records and documentation to demonstrate that tax was accurately calculated and remitted, and they must reflect the method used for calculating the tax.

General Presumption

The Department will presume that all comingled awards are taxable awards at the time of redemption unless the seller utilizes Option 1 or Option 2. Sellers may rebut the presumption by maintaining records that identify retail-taxable rewards within a comingled program. With respect to the taxable awards, the seller must calculate the combined state and local tax rate using the cascading steps for sourcing the

sales detailed in [RCW 82.32.730](#). The records must be available for examination by the Department. See RCW [82.32.070](#) and WAC [458-20-254](#).

Deferred sales or use tax

Generally, where a customer redeems discount awards for retail sales-taxable items and the seller receives no additional consideration for the purchase from the consumer or a third party, the seller will owe deferred sales or use tax on the items given away. See [RCW 82.04.190](#), [82.08.020](#), [82.12.020](#), and [WAC 458-20-116](#).

Note: Persons who sell products on a "two for the price of one" or similar basis in a single sales transaction are not giving away free products, but rather are selling two products at a discounted price. B&O and retail sales taxes should be calculated on the reduced sales price actually received by the seller, and no deferred sales or use tax is due. See [WAC 458-20-124](#).

Examples

The remainder of this ETA addresses different types of rewards program awards under specific sets of facts. The types of awards and examples provided are not exhaustive. The tax results of specific programs must be determined separately upon review of all the facts and circumstances.

Example 1 – Bona fide discounts: Price reductions provided to customers solely for membership in a rewards program

- **Facts:** GroceryCo, located in Washington, offers a loyalty scan card to customers. Sara uses the card to buy a tube of retail sales-taxable toothpaste, which has a stated price of \$4.00. The card entitles Sara, and any program member, to a 10% (\$0.40) reduction in the product's stated price as a member. Sara pays \$3.60 in cash at the time of sale.
- **Result:** Because Sara's price reduction is solely attributable to her membership in GroceryCo's rewards program and there is no third-party consideration, the price reduction is a bona fide discount and the sales price of the toothpaste is \$3.60. Retail sales tax is due on the \$3.60.

Example 2 – Bona fide discounts: Awards provided to customers solely for program enrollment or on the passage of time

- **Facts:** RedCo, located in Washington, is a store that sells goods and services. Any RedCo customer can enroll in RedCo's rewards program. When signing up for the program a customer receives 10 points, then another 10 points six months after enrollment, and 10 points on each customer birthday while the customer is enrolled. Anna enrolls in the program and receives the 30 points as described above. Anna redeems the 30 points when purchasing retail sales-taxable cookware from RedCo, which RedCo sells for a stated price of \$100.00. Anna pays \$70.00 in cash and applies the points to the \$30.00 remaining balance.
 - **Result:** Anna's points were provided solely for program enrollment and the passage of time with no third-party reimbursement. Therefore, the points awarded represent a bona fide discount upon redemption. The sales price
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of the cookware is \$70.00, which does not include the value of the points redeemed. Retail sales tax is due on the \$70.00.

Example 3 – Bona fide discounts: Awards provided to customers solely for purchasing a total dollar amount from the seller

- **Facts:** BlueCo, located in Washington, is a store that sells goods and services. Any BlueCo customer can enroll in BlueCo's rewards program. Connor enrolls in the program. Under the program, Connor receives 10 points for every \$100.00 he spends on BlueCo products. Connor receives 90 points after buying \$900.00 in BlueCo products, which he redeems when purchasing a retail sales-taxable stereo from BlueCo that sells for a stated price of \$100.00. Connor pays \$10.00 in cash and applies the points to the \$90.00 remaining balance due.
- **Result:** Because the points were provided to Connor solely for his purchase of BlueCo products with no third-party consideration, the points will be treated as a bona fide discount when redeemed. The sales price of the stereo is \$10.00, which does not include the value of the points redeemed. Retail sales tax is due on the \$10.00.
- **Similar situation:** A similar outcome would occur for awards provided to customers solely for purchasing seller's products with a specific dollar value, such as if Connor receives the 90 points for purchasing clothing from BlueCo with a stated price of \$30.00 or more.

Example 4 – Bona fide discounts: Awards provided to customers solely for purchasing a certain product or type of products from the seller

- **Facts:** CoffeeCo operates an espresso stand in Washington. CoffeeCo offers frequent purchaser coffee cards, available to all customers. The card is used to record a customer's purchases of retail sales-taxable espresso drinks. Each time an espresso drink is purchased, the card is punched by CoffeeCo. A customer must record nine espresso drinks on the card. On the tenth espresso drink, the customer may redeem the card and receive the tenth drink without additional charge. When ordering his tenth espresso drink, Sam uses the card and receives an espresso drink at no charge.
- **Result:** Because the recorded award was provided solely for the purchase of CoffeeCo's products, the award represents a bona fide discount on redemption. No retail sales tax must be collected from Sam when Sam receives his tenth espresso drink. CoffeeCo owes deferred retail sales tax on the cup, lid, and other sales-taxable items given away with the free espresso drink to Sam.

Example 5 – Deferred sales and use tax: Redeeming discount awards for goods with no additional taxable consideration

- **Facts:** ShoeSeller offers frequent buyer cards to all customers. The card is used to record a customer's dollar purchases of retail sales-taxable shoes. For every \$10.00 spent, the customer earns a one-dollar point towards future purchases. Nancy has spent \$700.00 to earn 70 points. She redeems

65 points for a pair of retail sales-taxable sandals with a stated sales price of \$65.00.

- *Result:* Because the points were provided to Nancy solely for her purchase of ShoeSeller products with no third-party consideration, the points are treated as a bona fide discount when redeemed. Because the points cover the full price of the sandals, no retail sales tax must be collected from Nancy. However, ShoeSeller owes deferred retail sales tax on the price it paid in acquiring the sandals.

Example 6 – Non-bona fide discounts: Awards provided in exchange for property and services

- *Facts:* PurpleCo, located in Washington, is a store that sells goods and services. Under PurpleCo’s rewards program any PurpleCo customer can enroll in the program. Mary enrolls in the program. Under the program, Mary can receive 10 points for completed surveys. Mary is awarded 10 points from PurpleCo for a completed survey. Mary redeems the 10 points when purchasing a retail sales-taxable toy train from PurpleCo, which PurpleCo sells for a stated price of \$20.00. Mary applies the points to her purchase and pays \$10.00 in cash on the remaining balance due.
- *Result:* Because the points were provided to Mary in exchange for property and services, the points are consideration included in sales price upon redemption. Accordingly, the sales price for Mary’s purchase is \$20.00, which consists of the redeemed points and the cash paid. Retail sales tax is due on the \$20.00 sale.
- *Similar situation:* A similar outcome would result if Mary received the 10 points in exchange for performing services for PurpleCo as a secret shopper (Mary is asked to gather and provide quality of service and other valuable feedback about PurpleCo in exchange for the points).
- *Similar situation:* The same outcome would result if Mary were an employee of PurpleCo and achieved specific incentive goals for sales or service and so earned rewards points.²

Example 7 – Non-bona fide discounts: Awards provided in exchange for cash

- *Facts:* TealCo, located in Washington, is a store that sells goods and services. Under TealCo’s rewards program any TealCo customer can enroll in the program. Zack enrolls in the TealCo rewards program. Under the program, Zack can buy 10 points for \$10.00 in cash. Zack redeems the 10 points when purchasing a retail sales-taxable mirror from TealCo, which TealCo sells for a stated price of \$100.00. Zack applies the points to his purchase and pays \$90.00 in cash on the remaining balance due.

² Note that where a retailer/employer simply offers all its employees a present discount (e.g., 10%) on regularly priced merchandise that it sells, the reduction in price is treated as a bona fide discount. This is because the employee discount is available to all employees simply due to their employment status rather than in exchange for undertaking some additional activity for the employer.

- *Result:* Because the points were provided to Zack in exchange for cash, the points are consideration included in sales price upon redemption. Accordingly, the sales price for Zack's purchase is \$100.00, which consists of the redeemed points and cash. Retail sales tax is due on the \$100.00 sale.

Example 8 – Third-party consideration: Seller receives third-party consideration for an offered price reduction or purchases using rewards points

- *Facts:* TangerineCo, located in Washington, offers a loyalty card. For every \$100.00 in purchasing activity at TangerineCo, customers receive the right to \$1.00 off any purchase made at Shopquick, a separate entity. To obtain the award, a purchaser must provide Shopquick with the telephone number associated with the card or present the card at the time of purchase. Under an agreement with Shopquick, TangerineCo pays consideration to Shopquick for the reduction in price given to card holders.
- *Result:* Because Shopquick is receiving third-party consideration, i.e., payment from TangerineCo in exchange for the price reduction, the Shopquick must include that consideration in the sale price.
- *Similar situation:* The same outcome would result if TangerineCo cobranded a credit card with BankCo that provided points for customer purchases on the credit card and BankCo provided cash and services as consideration to TangerineCo for customer purchases using points.

Example 9 - Commingled rewards programs – Option 1: Track taxable and nontaxable rewards and pay tax on taxable rewards at time of sale

- *Facts:* ShoeSeller offers a customer loyalty rewards program to all its Washington customers. During ShoeSeller's quarterly reporting period, ShoeSeller issued 20,000 discount points and 1,000 taxable points. ShoeSeller commingles the program points and maintains sufficient records to identify the type of points used at the time of redemption.
- ShoeSeller calculates any tax owed on the taxable rewards using the combined state and local tax rate directed by the sourcing provisions in [RCW 82.32.730](#). ShoeSeller does not calculate tax on any nontaxable rewards.
- *Result:* For the reporting period in question, ShoeSeller is able to rebut the general presumption that all awards are taxable at the time of redemption because ShoeSeller maintained records that identified the retail-taxable rewards within its comingled program and accurately calculated and remitted the tax due.

Example 10 – Comingled rewards program – Option 2: Prepayment method for a comingled rewards program

- *Facts:* ShoeSeller offers a customer loyalty rewards program to all its Washington customers. During ShoeSeller's quarterly reporting period, ShoeSeller issued 20,000 discount points and 1,000 taxable points. ShoeSeller commingles the program points and does not identify which

type of points is used at the time of redemption. Because ShoeSeller rewards few taxable points through its rewards program, it decides that it will use the prepayment method. For purposes of this example, each point is at all times valued at \$1.00.

- For the reporting period in question, ShoeSeller remits retailing B&O tax and retail sales tax consistent with the address of the program members to whom the points have been awarded. For example, if ShoeSeller's books and records kept in the ordinary course of business indicated Tacoma addresses for all program members, then ShoeSeller would remit retailing B&O tax on the \$1,000 point value, and retail sales tax of \$95.00 (\$1,000.00 point value x 9.5% (the combined state and local sales tax rate)). ShoeSeller maintains proper documentation to support its calculation.
- *Result:* ShoeSeller will not need to report as sales the subsequent redemptions of these awards unless ShoeSeller receives additional taxable consideration.

Example 11 – Comingled rewards program – General presumption applies

- *Facts:* ShoeSeller offers a customer loyalty rewards program to all its Washington customers. During ShoeSeller's quarterly reporting period, ShoeSeller issued both discount points and taxable points under the rewards program. ShoeSeller commingles the program points and does not maintain records sufficient to accurately identify the types of points used at the time customers redeem the points.
 - *Result:* Because ShoeSeller did not accurately track the taxable and non-taxable awards, all the comingled rewards are presumed taxable at the time of redemption.
-