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Directive 11-2: Sales/Use Taxation of Cellular Telephones in Bundled Transactions

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Introduction

The subject of this Directive is sales and use tax on cellular telephones or other wireless communication devices sold in bundled transactions with service contracts including telecommunications services, a subject that was previously addressed in Directives 93-9 and 94-2. This Directive announces new rules effective July 1, 2011. In the context of this Directive, a "bundled transaction" is a sale of a cellular telephone or other wireless communication device in which the customer gets a reduced price on the phone or device if he or she enters into a contract including telecommunications services at the time the phone or device is purchased, including renewals, upgrades and modifications to existing service contracts. [\[1\]](#)

In Directives 93-9 and 94-2, the tax result depended on who sold the cellular phone, that is, whether the phone was sold by a retailer as part of a bundled transaction including a contract with a third party telecommunications carrier, or the phone was sold by a telecommunications carrier as part of a contractual arrangement including both the phone and telecommunications services. The business models in this industry have evolved in more than 16 intervening years, and it may not be readily apparent to the retail customer which party owns the store where they are making a purchase and which of the existing sales tax rules would apply.

Directives 93-9 and 94-2 are superseded prospectively to the extent they are inconsistent with this Directive. The rules in this Directive apply to bundled transactions including both (i) a cellular phone or other wireless device and (ii) taxable telecommunications services; this directive does not address bundled transactions involving taxable and non-taxable tangible personal property, taxable property and exclusively non-taxable services, or promotional items in non-bundled transactions as described in 830 CMR 64H.1.4(1).

Issue 1

What is the sales price of cellular telephones or other wireless communications devices that are sold in "bundled" transactions including taxable telecommunications services, either by an independent retailer (which may include a franchisee of a telecommunications carrier) or by a telecommunications carrier?

Directive 1

The sales price of cellular telephones or other wireless communications devices that are sold in "bundled" transactions including taxable telecommunications services, either by an independent retailer (which may include a franchisee of a telecommunications carrier) or by a telecommunications carrier, is the higher of the amount paid by the retail customer or the wholesale cost of the phone or

other wireless communications device. Massachusetts sales/use tax must be paid on that sales price amount.

Issue 2

How is the applicable tax on cellular telephones or other wireless communications devices that are sold in "bundled" transactions including taxable telecommunications services to be paid and collected?

Directive 2

Generally the vendor is responsible for collecting and remitting tax on the sales price determined in accordance with Directive 1, above. In situations where the wholesale cost of the phone or other device is used for calculating the tax (because it is higher than the amount paid by the customer), the seller may collect and remit tax from the customer on the wholesale cost. Alternatively, the vendor may elect to assume a portion of the tax [2] by collecting tax from the customer only on the lesser amount actually paid by the customer, in which case, the vendor must also remit tax on the difference between that lesser amount and the wholesale cost, as illustrated in the examples below.

In either situation, the tax paid by the retail customer must be separately stated on any invoice or receipt issued to the customer by the vendor as required by G.L. c. 64H, § 5.

Discussion

Massachusetts imposes an excise upon sales at retail of tangible personal property and telecommunications services, measured by a vendor's gross receipts from such sales. G.L. c. 64H, § 2. A "sale at retail" is defined in pertinent part as a sale for any purpose other than resale in the regular course of business. G.L. c. 64H, § 1. A "sale" includes "any transfer of title or possession, or both, exchange, barter, lease, rental, conditional or otherwise, of tangible personal property...for a consideration, in any manner or by any means whatsoever." For purposes of the sales tax, the term "gross receipts" is defined as "the total sales price received by a [vendor] as a consideration for retail sales." The term "sales price" is further defined (in pertinent part) as "the total amount paid by a purchaser to a vendor as a consideration for a retail sale, valued in money or otherwise." G.L. c. 64H, § 1.

A complementary use tax is imposed on the storage, use or consumption in the Commonwealth of tangible personal property or telecommunications services purchased from any vendor. The use tax is calculated on the sales price of the property or services to the party making the use. G.L. c. 64I, §§ 1, 2.

DD 93-9 concluded that when an independent retailer sold a phone in a bundled transaction involving a phone and a telecommunications services contract, the commission received by the retailer from the telecommunications carrier was additional consideration for the sale of the phone and should be included in the taxable sales price of the phone. Since the actual amount of commission would be unknown to the retail customer and considered proprietary by the carrier, the sales price of the phone was deemed to be the published price for the phone in an "unbundled" transaction, whether or not any phones were sold at such a price.

In DD 94-2, a different analysis was applied to phones provided by a telecommunications carrier to a customer at no additional charge or for nominal consideration in connection with a sale of telecommunications services. With respect to these sales, the phones have been treated as "promotional items." Directive 94-2 provided that when property such as the cell phone is transferred by a vendor to a customer for no additional consideration, or for a nominal consideration, or for an amount substantially below cost, the property constitutes a promotional item for sales and use tax purposes, and the vendor is considered its consumer, citing Letter Ruling 84-48; *Parfums-Corday, Inc. v. State Board of Equalization*, 187 Cal. App. 3d 630 (1986); *Wallace Berrie & Co. v. State Board of Equalization*, 40 Cal. 3d 60 (1985); and *The Drackett Products Co. v. Limbach*, Ohio Board of Tax Appeals, No. 87-C-975 (1992).

Effective July 1, 2011, regardless of the identity of the vendor or its relationship to a

telecommunications carrier, the Department will require tax to be paid on an amount higher than that paid by the retail customer only in situations where a cellular phone or other wireless device is sold at an amount less than the wholesale cost to the vendor. [3] In that situation, the vendor of a cellular phone or other wireless device is responsible for remission of tax on the wholesale cost. As provided in Directive 2 and discussed in the following paragraph, the seller may collect part or all of that tax from the retail customer. If the cellular phone or other wireless device is sold for an amount equal to or greater than the wholesale cost, the taxable sales price is the amount actually paid by the retail customer.

Section 50 of Chapter 131 of the Acts of 2010 repealed chapter 64H, § 23, a provision that prevented retailers from advertising that they will assume or absorb the sales tax. [4] The taxability of any item of tangible personal property or telecommunications service was unchanged by the repeal of G.L. c. 64H, § 23. The requirement for all Massachusetts vendors to separately state the tax is also unchanged. See G.L. c. 64H, §§ 3, 5. In the case of the bundled transactions described in this TIR in which the vendor is collecting tax from the retail customer, only the amount of tax collected from the retail customer must be shown on the invoice or receipt issued to the customer.

This Directive announces a prospective change in policy as required by G.L. c. 62C, § 3, and applies to transactions, *i.e.*, sale or use, taking place on or after July 1, 2011. The rules in Directives 93-9 and 94-2 remain in effect for periods prior to July 1, 2011.

Examples

1. A vendor offers to sell a new cellular phone for \$219.95 to any customer who also signs a one year service contract including taxable telecommunications services. The wholesale cost to the vendor of the cellular phone is \$200.00. The vendor is required to collect and remit tax from the retail customer of \$13.75 (6.25% of \$219.95).
2. A vendor offers to sell a new cellular phone for \$119.95 to any customer who also signs a two year service contract including taxable telecommunications services. The wholesale cost to the vendor of the cellular phone is \$200.00. The vendor may collect the entire tax due, \$12.50 (6.25% of \$200.00), from the retail customer. If the vendor elects to collect and remit tax from the customer only on the amount actually paid, \$7.50 (6.25% of \$119.95), then the vendor must also remit tax of \$5.00 (6.25% of \$200.00, less \$7.50 credit for tax collected from the retail customer). In either case, the vendor must remit the total tax due of \$12.50. The customer's receipt must reflect the amount of tax collected from the retail customer.
3. A vendor offers to sell a new cellular phone for \$19.95 to any customer who also signs a three year service contract including taxable telecommunications services. The wholesale cost to the vendor of the cellular phone is \$200.00. The vendor may collect the entire tax due, \$12.50 (6.25% of \$200.00), from the retail customer. If the vendor elects to collect and remit tax from the customer only on the amount actually paid, \$1.25 (6.25% of \$19.95), then the vendor must also remit tax of \$11.25 (6.25% of \$200.00, less \$1.25 credit for tax collected from the retail customer). In either case, the vendor must remit the total tax due of \$12.50. The customer's receipt must reflect the amount of tax collected from the retail customer.

/s/Navjeet K. Bal

Navjeet K. Bal
Commissioner of Revenue

NKB:MTF:ecl

April 27, 2011

DD 11-2

[1] For some wireless devices, the bundle may include taxable telecommunications services and non-taxable Internet access charges.

[2] See TIR 10-11, Section X, concerning the repeal of the prohibition against a vendor advertising that it will assume or absorb all or part of the sales tax.

[3] The rules in this Directive will be applied regardless of whether the presumption described in 830 CMR 64H.1.4(1) has been created by selling an item for 50% or less of cost.

[4] Chapter 64H, § 23 had stated, in part, that it was “unlawful for any vendor to advertise or hold out or state to the public or any consumer, directly or indirectly, that the tax or any part thereof will be assumed or absorbed by the vendor or that it will not be added to the selling price of the property or services sold, or, if added, it or any part thereof will be refunded.”