



Direct Selling Industry – The Alternate Collection Method for Independent Sales Contractors

Generally, businesses in the direct selling industry sell their products either directly to consumers through commission-based sales representatives or to independent sales contractors (ISCs) who, in turn, sell the products to other ISCs of the direct seller or to purchasers.

In either case, direct selling businesses may apply for approval to use a method that simplifies the operation of the GST/HST:

- Direct selling businesses that sell their products to consumers through commission-based sales representatives may apply to use the Network Sellers Method (NSM).
- Direct selling businesses that sell their products to ISCs may apply to use the Alternate Collection Method (ACM).

Therefore, persons involved in selling products of a direct selling business may be sales representatives or ISCs for GST/HST purposes.

If a person receives a commission for arranging for the sale of products of a direct selling business, this person is most likely a sales representative to which the NSM rules may apply. For more information on the NSM, refer to GST/HST Info Sheet GI-052, *Direct Selling Industry – The Network Sellers Method for Network Sellers and Sales Representatives*.

If a person purchases products from a direct selling business and sells them to purchasers, this person is most likely an ISC to which the ACM rules may apply.

This info sheet explains how the ACM applies to ISCs, including distributors that have not been granted approval to use the ACM. For information

on how the ACM applies to direct sellers and distributors that have been granted approval to use the ACM, refer to GST/HST Info Sheet GI-125, *Direct Selling Industry – The Alternate Collection Method for Approved Direct Sellers and Approved Distributors*.

What is an independent sales contractor?

“Independent sales contractor” (ISC) means a person that:

- is not an agent or an employee of a direct seller or of a distributor;
- has an agreement to purchase a direct seller’s exclusive products from the direct seller or a distributor;
- purchases a direct seller’s exclusive products for resale to other ISCs of the direct seller or to purchasers who are not acquiring the products for resale; and
- does not solicit sales or sell a direct seller’s exclusive products primarily (more than 50%) at a fixed place of business, except if it is the ISC’s home.

Therefore, an ISC is a person who purchases a direct seller’s exclusive products and sells the products to other ISCs of the direct seller or to purchasers. A person who does not meet this requirement is not an ISC for the purposes of the ACM, even if this person is referred to as an ISC by the direct seller.

For the purposes of this info sheet, an ISC includes a distributor that has not been granted approval to use the ACM.

Meaning of other terms used in this info sheet

“Approved direct seller” means a registrant direct seller that has been granted approval to use the ACM.

“Approved distributor” means a registrant distributor that has been granted approval to use the ACM.

“Direct seller” means a person that sells exclusive products to ISCs.

“Distributor” means an ISC that purchases a direct seller’s exclusive products and sells some or all of those products to other ISCs of the direct seller.

“Exclusive product” means any personal property that a direct seller acquires, manufactures, or produces for sale to ISCs who ultimately sell, or intend to sell, the property to purchasers.

“Input tax credit” (ITC) means a credit registrants may claim to recover the GST/HST they have to pay on their business purchases.

“Non-approved distributor” means a distributor that has not been granted approval to use the ACM pursuant to a joint application with the direct seller.

“Personal property” means property that is not real property”.

“Purchaser” means an individual, business or organization that purchases a direct seller’s exclusive product and does not intend to resell it.

“Registrant” means a person who is registered, or is required to be registered, for GST/HST purposes.

“Sales aids” means property that is a customized business form or a sample, demonstration kit, promotional or instructional item, catalogue, or other personal property that a direct seller or an ISC acquires, manufactures or produces for sale to assist in the promotion, sale or distribution of the direct seller’s exclusive products. A sales aid also includes the service of shipping or handling, or processing an order for other sales aids or exclusive products. However, it does not include an exclusive product

or property that an ISC purchases for use as capital property. For more information, refer to GST/HST Info Sheet GI-023, *Direct Seller’s Sales Aids*.

“Suggested retail price” of a product means the lowest price before tax published by a direct seller for sale to purchasers. It is usually the price set out in a direct seller’s catalogue of products, including any amount set out for shipping and handling.

“Taxable” means subject to the 5% GST or to the HST rate in effect in a participating province (i.e. 12%, 13% or 15%).

“Zero-rated” means subject to GST/HST at 0%.

What is the ACM?

The ACM is a method that simplifies the operation of the GST/HST for direct sellers, distributors and ISCs. However, before they can use the ACM, the direct seller must apply to the CRA, either alone or jointly with one or more of its distributors, for approval to use the method and must have been granted approval, from the CRA, to use the method.

When an approval to use the ACM is in effect, either the approved direct seller or the approved distributor, as the case may be, charges the ISC the GST/HST on the suggested retail price of the exclusive products sold to the ISC, even if the ISC pays a lower price for the products.

When the ACM is in effect, the ACM rules apply to all ISCs whether or not they are registrants.

Sales of exclusive products to purchasers

When an ISC sells an exclusive product to a purchaser, the ISC charges the GST/HST on the price charged to the purchaser (which is usually the suggested retail price of the product). However, the ISC does not account for the tax. By keeping that amount, the ISC recovers the amount of tax (or part of it) paid to the approved direct seller or approved distributor, as the case may be, on the purchase of the product.

ISCs cannot claim an ITC or a rebate for tax paid in error to recover the GST/HST they have to pay on their purchases of exclusive products.
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The following examples use taxable exclusive products to explain these rules. See the information under the heading “Zero-rated sales of exclusive products” for information on how the ACM applies to those sales.

Example 1

An ISC purchases candles for \$18 from an approved direct seller in Ontario. The suggested retail price of the candles is \$25. Although the ISC pays \$18 for the candles, the HST is calculated on the suggested retail price of \$25. The direct seller’s invoice to the ISC shows the following:

Candles	\$18.00
HST (\$25 × 13%)	<u>3.25</u>
Amount payable by the ISC	\$21.25

The ISC sells the candles to a purchaser for the suggested retail price of \$25 and issues the following invoice:

Candles	\$25.00
HST (\$25 × 13%)	<u>3.25</u>
Amount payable by the purchaser	\$28.25

The ISC does not account for the \$3.25 HST charged to the purchaser. By keeping that amount, the ISC recovers the amount of HST paid to the direct seller on the purchase of the candles.

Sales of exclusive products to other ISCs

When an ISC sells an exclusive product to another ISC of the approved direct seller, the ISC charges the other ISC the GST/HST on the suggested retail price of the product. However, the ISC does not account for the tax. By keeping that amount, the ISC recovers the amount of tax paid to the approved direct seller or approved distributor on the purchase of the product.

Example 2

An approved direct seller in Nova Scotia sells cookware to a non-approved distributor for \$60 who, in turn, sells the cookware to an ISC for \$80. The suggested retail price of the cookware is \$100.

Although the non-approved distributor pays \$60 for the cookware, the direct seller charges the HST on the suggested retail price of \$100. The direct seller issues the following invoice to the non-approved distributor:

Cookware	\$60
HST (\$100 × 15%)	<u>15</u>
Amount payable by the non-approved distributor	\$75

The non-approved distributor sells the cookware to the ISC for \$80 and charges the HST on the suggested retail price. The non-approved distributor’s invoice to the ISC shows the following:

Cookware	\$80
HST (\$100 × 15%)	<u>15</u>
Amount payable by the ISC	\$95

The non-approved distributor does not account for the \$15 HST charged to the ISC. By keeping that amount, the non-approved distributor recovers the amount of HST paid to the direct seller on the initial purchase of the cookware.

The ISC sells the cookware to a purchaser for the suggested retail price of \$100 and issues the following invoice:

Cookware	\$100
HST (\$100 × 15%)	<u>15</u>
Amount payable by the purchaser	\$115

The ISC does not account for the \$15 HST charged to the purchaser. By keeping that amount, the ISC recovers the amount of HST paid to the distributor on the purchase of the cookware.

Zero-rated sales of exclusive products

GST/HST does not apply to zero-rated exclusive products, such as basic groceries. Therefore, ISCs do not pay the GST/HST when they purchase these products. As well, ISCs do not charge the GST/HST when they sell these products to other ISCs of the approved direct seller or to purchasers.

For information on zero-rated sales, refer to Chapter 4, *Zero-Rated Supplies*, of the GST/HST Memoranda Series.

Example 3

An ISC pays \$15 for spices purchased from an approved direct seller in New Brunswick. The suggested retail price of the spices is \$20. Because spices are zero-rated, the ISC does not pay the HST when purchasing them from the direct seller and does not charge the HST when selling them to purchasers.

Sales of exclusive products back to an approved direct seller or approved distributor

GST/HST does not apply when an ISC sells an exclusive product back to the approved direct seller or the approved distributor from whom the ISC purchased the product. Therefore, an ISC going out of business does not charge the GST/HST when it sells inventory back to the approved direct seller or the approved distributor.

Sales aids

GST/HST does not apply when an approved direct seller sells a sales aid to an ISC. As well, GST/HST does not apply when an ISC (e.g., a distributor) sells a sales aid to another ISC of the approved direct seller. However, GST/HST applies when a registrant ISC sells a sales aid to any other person. For more information on sales aids, refer to GST/HST Info Sheet GI-023, *Direct Seller's Sales Aids*.

Example 4

An approved direct seller in Prince Edward Island sells cosmetics. To assist in the promotion and sale of the cosmetics, the direct seller sells to the ISC a demonstration kit containing samples and disposable applicators. A year later, the ISC, who is a registrant, purchases a new kit and sells the old one to a purchaser.

Sales of sales aids from an approved direct seller to an ISC are not subject to tax. Consequently, the ISC does not pay the GST on the purchase of the demonstration kit. However, the ACM rules do not apply to sales of sales aids to a purchaser. Therefore, as a registrant, the ISC has to charge and account for the GST on the sale of the demonstration kit to the purchaser.

Bonus payments

A bonus payment is any amount which is paid to an ISC because of the volume of purchases or sales of exclusive products or sales aids. It could be an amount of money, goods or services.

GST/HST does not apply when the approved direct seller makes a bonus payment to an ISC. The same rule applies when an ISC makes a bonus payment to another ISC of the approved direct seller.

However, if the amount is paid on any other basis, the payment is not a bonus payment and the supply for which the amount is paid may be subject to tax.

Example 5

An ISC receives a bonus payment of \$200 based on the volume of sale of exclusive products made by other ISCs who are sponsored into the direct seller's compensation plan. The bonus payment paid by the direct seller to the ISC is not subject to tax.

Host gifts

A host gift is property given to a person for the service of hosting an occasion organized for the promotion or sale of exclusive products to purchasers. Usually, the host gift is an exclusive product or a credit to be used against the purchase

of an exclusive product (i.e., a host credit). It may also be an item that is not an exclusive product.

Host receives from an ISC an exclusive product or a credit to be used against the purchase of an exclusive product

When an approved direct seller or an approved distributor, as the case may be, supplies an exclusive product to an ISC who, in turn, gives the product to a host as a host gift, the approved direct seller or the approved distributor charges the ISC the GST/HST on the suggested retail price of the product and accounts for that tax on line 103 of its GST/HST return, even if the product is supplied to the ISC at no cost. Afterwards, the approved direct seller or the approved distributor may choose to pay or credit an amount of tax to the ISC in respect of the supply and deduct an equal amount from its net tax.

When the ISC gives the host gift to the host, GST/HST does not apply to the gift or to the host services. Therefore, the ISC may recover the amount of the tax paid to the approved direct seller or the approved distributor for the exclusive product. For more information on payment or credit of tax, see the heading "Tax payment or credit."

However, when the host is given a credit to be used against the purchase of an exclusive product, and the suggested retail price of the product exceeds the value of the credit, the ISC has to charge the GST/HST on the actual price charged to the host for the exclusive product but does not account for that tax.

Example 6

For hosting purposes, an ISC gives a host a credit of \$60 to be applied against the purchase of a product. The host chooses a product with a suggested retail price of \$80. The ISC orders the exclusive product from an approved direct seller in Alberta who supplies the product to the ISC at no cost. The direct seller charges the GST on the suggested retail price of \$80 and accounts for that tax on line 103 of its GST/HST return. The direct seller issues the following invoice to the ISC:

Product	\$0
GST (\$80 × 5%)	\$4
Amount payable by the ISC	\$4

The ISC charges the GST on the amount paid by the host and issues the following invoice to the host:

Suggested retail price of product	\$80
Minus the credit amount	- \$60
Subtotal	\$20
GST (\$20 × 5%)	<u>1</u>
Total amount paid by the host	\$21

The ISC does not account for the \$1 GST charged to the host. By keeping that amount, the ISC recovers part of the GST paid to the direct seller. The ISC may be able to recover the rest of the tax paid to the direct seller.

Host receives from an ISC an item (other than an exclusive product)

An item (other than an exclusive product) is considered as a sales aid when an approved direct seller supplies it to an ISC who will give it to a host as a host gift. Consequently, GST/HST does not apply to that supply. The same rule applies when an ISC (e.g., a distributor) supplies the item to an ISC who will give it to a host as a host gift.

GST/HST does not apply when the ISC gives the item to the host as a host gift.

Tax payment or credit

ISCs pay the GST/HST on the suggested retail price of exclusive products when they purchase the products from an approved direct seller or an approved distributor and they recover the amount of tax when they sell the products to purchasers or other ISCs of the approved direct seller. Sometimes, ISCs cannot recover the full amount of tax they have paid on the purchase. This happens when an ISC:

- sells an exclusive product for less than its suggested retail price, but more than a nominal price;
- gives away an exclusive product to a purchaser or keeps an exclusive product for its own personal use;
- exports an exclusive product in a situation where the sale to the purchaser is zero-rated (for example, when an ISC sends the product by courier to an address outside Canada);
- sells an exclusive product outside Canada;

- sells an exclusive product to a person who does not have to pay tax because of legislation, such as an Indian purchasing an exclusive product on a reserve in a situation where the Indian does not have to pay tax;
- gives to a host a host gift that is an exclusive product; or
- sells an exclusive product, but the amount payable for the product and the GST/HST become in whole or in part a bad debt that is written off in the ISC’s books of account.

In these situations, the approved direct seller or approved distributor from whom the ISC purchased the product may choose to pay or credit the ISC with an amount of tax. The amount that may be paid or credited depends on the deduction the approved direct seller or approved distributor is entitled to claim in its GST/HST return.

Refer to GST/HST Info Sheet GI-125, *Direct Selling Industry – The Alternate Collection Method for Approved Direct Sellers and Approved Distributors* for information on how the payment or credit amount is calculated.

The ISC has to provide the approved direct seller or approved distributor with documentary evidence to substantiate the reason for the payment or credit and the amount of tax paid.

Example 7

An ISC purchases a necklace for \$75 from an approved direct seller in Manitoba. The suggested retail price of the necklace is \$100. The direct seller issues the following invoice to the ISC:

Necklace	\$75
GST (\$100 × 5%)	<u>5</u>
Amount payable by the ISC	\$80

The ISC sells the necklace to a purchaser for \$80, which is less than the suggested retail price and issues the following invoice:

Necklace	\$80
GST (\$80 × 5%)	<u>4</u>
Amount payable by the purchaser	\$84

The ISC does not account for the \$4 GST charged to the purchaser. By keeping that amount, the ISC recovers part of the amount of the GST paid to the direct seller.

The ISC provides documentary evidence to the direct seller to prove that the sale was made for less than the suggested retail price. As a result, the direct seller agrees to credit the \$1 tax difference to the ISC.

ITCs

Registrant ISCs cannot claim ITCs to recover the GST/HST they have to pay on their purchases of exclusive products. However, they may claim ITCs to recover the GST/HST paid or payable on their other business purchases that relate to their commercial activities.

Keeping records

ISCs have to keep all sales and purchase invoices and other records related to their business operations for six years from the end of the year to which they relate. They should also request and keep in their records evidence from the direct seller or distributor that it has been approved to use the ACM.

GST/HST registration

Generally, businesses have to register for GST/HST purposes when their total taxable revenues from all their businesses are more than \$30,000 over four consecutive calendar quarters.

However, most ISCs do not have to register for GST/HST purposes, because the revenues from the following activities are not included in the calculation of the \$30,000 amount:

- sales of exclusive products;
- sales of sales aids to other ISCs; and
- bonus payments.

This means that an ISC is not required to register for GST/HST purposes where the ISC's only revenues are from these activities, even if the ISC's revenues from these activities exceed \$30,000.

Example 8

A self-employed florist sells exclusive products of an approved direct seller on a part-time basis. Over the last four consecutive calendar quarters, he earned \$28,000 from selling flowers and \$5,000 from selling exclusive products.

The florist is not required to register for GST/HST. The \$5,000 revenues from the sale of exclusive products are not considered when determining whether he has to register.

ISCs engaged in other activities or other businesses

When the approval to use the ACM is in effect, this does not necessarily mean that all of an ISC's activities fall under the ACM. For example, the ACM rules do not apply to sales of sales aids to purchasers or services provided to the approved direct seller or approved distributor. As well, the ACM rules do not apply to other businesses of an ISC.

Registrant ISCs who make taxable supplies of property or services that do not fall under the ACM have to charge and account for the GST/HST on those supplies. ISCs who are not registrants have to consider the revenues from those taxable supplies in determining whether they have to register for GST/HST purposes.

Example 9

An individual proprietor, who is not a registrant, works from her home for two direct selling businesses. The first business is an approved direct seller that sells children's toys. The direct selling business applied for and received approval to use the ACM. As an ISC, she purchases the toys and sells them to purchasers and also receives bonus payments from the direct seller. She also provides training to other ISCs for which she charges a fee to the direct seller.

The second business is a network seller that sells women's clothing. The direct selling business is not approved to use the NSM. As a sales representative, she receives a commission for each sale of products she arranges for the network seller.

For each activity, she has to determine how GST/HST applies. With respect to her activities as an ISC of the approved direct seller, she determines that the ACM rules apply to her purchases and sales of the children's toys and to the bonus payments, but not to the training services that she provides to the direct seller.

With respect to her activities as a sales representative of the network seller, she determines that the commissions she receives from the network seller do not fall under the NSM and are subject to the normal GST/HST rules.

In her calculation to determine if she has to register for GST/HST purposes, she includes the revenues she receives for the training services she provides to the approved direct seller and the commissions she receives from the network seller for arranging for the sales of the products.

If you are not sure whether a particular activity falls under the ACM, you may ask for a written ruling or interpretation. For more information, see GST/HST Memorandum 1.4, *Excise and GST/HST Rulings and Interpretations Service*.

Additional information

This document outlines the most common situations that may affect ISCs. For situations not covered in this info sheet, call a GST/HST Rulings Centre at 1-800-959-8287.

This info sheet does not replace the law found in *the Excise Tax Act* (the Act) and its regulations. It is provided for your reference. As it may not completely address your particular operation, you may wish to refer to the Act or appropriate regulation, or contact any CRA GST/HST rulings office for additional information. A ruling should be requested for certainty in respect of any particular GST/HST matter. Pamphlet RC4405, *GST/HST Rulings – Experts in GST/HST Legislation* explains how to obtain a ruling and lists the GST/HST rulings offices. If you wish to make a technical enquiry on the GST/HST by telephone, please call 1-800-959-8287.

Reference in this publication is made to supplies that are subject to the GST or the HST. The HST applies in the participating provinces at the following rates: 13% in Ontario, New Brunswick and Newfoundland and Labrador, 15% in Nova Scotia, and 12% in British Columbia. The GST applies in the rest of Canada at the rate of 5%. If you are uncertain as to whether a supply is made in a participating province, you may refer to GST/HST Technical Information Bulletin B-103, *Harmonized Sales Tax – Place of Supply Rules for Determining Whether a Supply is Made in a Province*.

If you are located in Quebec and wish to make a technical enquiry or request a ruling related to the GST/HST, please contact Revenu Québec at 1-800-567-4692. You may also visit the Revenu Québec Web site to obtain general information.

All technical publications related to GST/HST are available on the CRA Web site at www.cra.gc.ca/gsthsttech.