

New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Technical Services Division

TSB-A-07(14)S
Sales Tax
May 17, 2007

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S060411B

On April 11, 2006, the Department of Taxation and Finance received a Petition for Advisory Opinion from Apple Computer, Inc., c/o Terry Ryan, Director of Tax, 1 Infinite Loop, Cupertino, California 95014. Petitioner, Apple Computer, Inc., furnished additional information with respect to the Petition on May 15, 2006.

The issues raised by Petitioner are:

1. Whether the sale of alphanumeric codes conveying the right to download specific audio files is subject to sales tax when the codes are delivered electronically.
2. Whether the sale of codes conveying the right to download specific audio files is subject to sales tax when the codes are delivered on tangible media.
3. Whether the sale of digital music delivered electronically via the Internet is subject to sales tax when a code which must be entered into a computer to receive the music or other content is transferred to a customer on a plastic card.

Petitioner submitted the following facts as the basis for this Advisory Opinion.

Petitioner, headquartered in California, is, among other things, engaged in the business of digital distribution of music over the Internet to customers located throughout the United States, including New York.

Customers use their personal computers to order music over the Internet to be delivered to the customers' computers or other electronic devices. Customers pay for the digitized content in one of a number of ways, including with a credit card serviced by a third-party financial institution. The downloaded music files remain on the customers' computers and may be copied to a limited number of CDs, personal computers, or handheld electronic devices.

In certain circumstances, the purchase of electronically downloaded music will be effected through the acquisition, use, or transfer of alphanumeric codes. The alphanumeric code provides the holder with the right to electronically download a music file. Each code has a designated value allowing purchases of digital music available on Petitioner's Web site. Codes can be furnished to purchasers via e-mail, paper certificates, or plastic cards. Codes may be distributed to consumers by a third party as part of a promotional campaign. Some examples of promotional distribution are when customers obtain a code on a sales register receipt from an unrelated third-party retailer, or on bottle caps manufactured by an unrelated soda manufacturer; or online promotions through which Internet Web site visitors may register and obtain a code

online or in an e-mail. Petitioner anticipates the circumstances and delivery mechanisms used to distribute these codes may continue to grow in number and complexity in the future.

In some cases, alphanumeric codes printed on physical media like a plastic card or paper certificate will be sold by retailers. In those situations, the codes on the physical media held for sale by retailers are not “live” until activated. Activation occurs when the card or other physical medium is scanned at the point-of-sale register. At that time, the point-of-sale register “pings” (sends an electronic signal) to Apple’s server, which returns a signal indicating that particular code is now active. The customer may redeem activated digital codes regardless of whether or not the customer is in possession of the plastic card, paper certificate, or other medium. Once the code is entered into the user’s computer, the plastic card itself is of no further use even if the code has not been redeemed.

Applicable law and regulations

Section 1105 of the Tax Law provides, in part:

Imposition of sales tax. On and after June first, nineteen hundred seventy-one, there is hereby imposed and there shall be paid a tax . . . upon:

(a) The receipts from every retail sale of tangible personal property, except as otherwise provided in this article.

Section 1110 of the Tax Law provides, in part:

Imposition of compensating use tax. (a) Except to the extent that property or services have already been or will be subject to the sales tax under this article, there is hereby imposed on every person a use tax for the use within this state on and after June first, nineteen hundred seventy-one except as otherwise exempted under this article, (A) of any tangible personal property purchased at retail, . . .

Opinion

Petitioner distributes music digitally over the Internet. A customer downloads digital music files which remain on the customer’s computer and may be copied to a limited number of CDs, personal computers, or handheld electronic devices. Petitioner provides various payment methods for customers to use to make their purchases. Customers may make advance payments for future purchases of digital music files. These customers will obtain Petitioner’s digital music files using an alphanumeric code. Each code has a designated value allowing purchases of digital music available on Petitioner’s Web site.

With respect to Issues 1 and 2, Petitioner provides purchasers with an alphanumeric code via e-mail, printed on a paper certificate, or imprinted on plastic cards. The codes may also be

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distributed by a third party as a promotional item or sold in a tangible format by third-party retailers. The code provides the means by which an individual can access and download the digital music. Once the designated value of the code has been expended, the code is of no further use. The individual who uses a code to download digital music is purchasing the same digital music as individuals who directly purchase digital music for download by making payment at the time of purchase by credit card or through third-party financial institutions. Accordingly, for sales tax purposes, Petitioner's sales of the code, as described in this Opinion, are sales of an intangible regardless of whether a physical medium such as a paper certificate or plastic card is used to transmit the code. See *First Colony Company*, Adv Op Comm T&F, March 1, 1999, TSB-A-99(13)S. Such sales, therefore, are not subject to sales or compensating use tax under section 1105(a) or 1110(a)(A) of the Tax Law.

With respect to Issue 3, the sale of digital music delivered electronically to customers for download on their computers or other devices as described in this Opinion constitutes the sale of intangible property and is not subject to sales or use tax. See *Universal Music Group*, Adv Op Comm T&F, April 18, 2001, TSB-A-01(15)S. Therefore, Petitioner's charges for the electronic transfer of digital music via the Internet to customers, downloaded for use on the customers' computers or similar devices, are not subject to tax regardless of whether customers make payment by credit card or by using Petitioner's alphanumeric code previously purchased and transferred to the customer on a physical medium, by e-mail, or otherwise.

DATED: May 17, 2007

/s/
Jonathan Pessen
Tax Regulations Specialist IV
Technical Services Division

NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion.