

New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Taxpayer Guidance Division

TSB-A-08(34)S
Sales Tax
July 24, 2008

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S070327A

On March 27, 2007, the Department of Taxation and Finance received a Petition for Advisory Opinion from Ernst & Young LLP, 5 Times Square, New York, New York 10036. Petitioner, Ernst & Young LLP, furnished additional information with respect to the Petition on July 16, 2007.

The issue raised by Petitioner is whether the value of hardware and related services traded in on the purchase of new hardware and related services may be excluded from the receipt subject to New York sales and use tax.

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

A purchaser corporation (Purchaser) has a continuing business relationship with a seller corporation (Seller) for the purchase of computer hardware and related services.

On June 30, 2003, Purchaser and Seller entered into a five-year prepaid maintenance contract (Maintenance Agreement), whereby Purchaser agreed to prepay for maintenance services on certain equipment previously acquired or to be acquired from Seller.

In December 2003, Purchaser entered into an agreement (2003 Purchase Agreement) with Seller to purchase computer hardware to upgrade its computer technology. This hardware was subject to the Maintenance Agreement.

When the Maintenance Agreement and the 2003 Purchase Agreement were executed, Purchaser had an agreement with the New York City Industrial Development Agency (IDA) in which Purchaser was entitled to sales and use tax exemptions for the purchase and use of computer equipment and the installation, maintenance, repair, and replacement of such equipment and other property acquired under the agreement at certain approved locations where Purchaser conducted business. The authorization letter for sales tax exemption was issued by the IDA on June 27, 2002, and was effective through June 30, 2004. As provided by the IDA exemption letter, Purchaser's prepayment of maintenance services under the Maintenance Agreement and the subsequent purchase of computer hardware under the 2003 Purchase Agreement were exempt from sales and use tax.

In December 2004, Purchaser entered into a new agreement with Seller (2004 Purchase Agreement) to purchase additional computer hardware for Purchaser's upgrade to newer technology. Included in the 2004 Purchase Agreement was a new agreement for prepaid hardware maintenance services. The computer hardware was shipped to Purchaser on or about

December 31, 2004, and installed on or about January 31, 2005. In the same manner as the 2003 Maintenance Agreement, Purchaser prepaid maintenance costs on such hardware.

When the 2004 Purchase Agreement was executed, Purchaser's IDA exemption letter was no longer in effect. Thus the Seller collected sales tax on the purchase of new hardware and maintenance services.

The purchase price under the 2004 Purchase Agreement was offset by reimbursements for the trade-in values of certain equipment (the Trade-in Hardware) purchased under prior agreements with Seller and for unused prepaid maintenance (Unused Maintenance) on such Trade-in Hardware (collectively, the Purchase Reimbursements). The 2004 Purchase Agreement further provided that Purchaser was entitled to apply these reimbursements toward the payment of any Seller invoice.

Seller issued the Purchase Reimbursements to Purchaser, and Purchaser applied the Purchase Reimbursements toward the payment for the new hardware under the 2004 Purchase Agreement and toward the payment for the newly purchased prepaid maintenance.

For an additional charge provided in the 2004 Purchase Agreement, Seller allowed Purchaser to use the Trade-in Hardware after Seller took back title to the Trade-in Hardware. The 2004 Purchase Agreement also provided a schedule outlining the transition period during which Purchaser could continue to use the Trade-in Hardware and the scheduled dates for Purchaser to deliver the Trade-in Hardware to Seller.

Applicable law and regulations

Section 1101(b) of the Tax Law provides, in part:

When used in this article for the purposes of the taxes imposed by subdivisions (a), (b), (c) and (d) of section eleven hundred five and by section eleven hundred ten, the following terms shall mean:

* * *

(3) Receipt. The amount of the sale price of any property and the charge for any service taxable under this article, including gas and gas service and electricity and electric service of whatever nature, valued in money, whether received in money or otherwise, including any amount for which credit is allowed by the vendor to the purchaser, without any deduction for expenses or early payment discounts and also including any charges by the vendor to the purchaser for shipping or delivery . . .but excluding any credit for tangible personal property accepted in part payment and intended for resale. . . .

* * *

(5) Sale, selling or purchase. Any transfer of title or possession or both, exchange or barter, rental, lease or license to use or consume (including, with respect to computer software, merely the right to reproduce), conditional or otherwise, in any manner or by any means whatsoever for a consideration, or any agreement there for, including the rendering of any service, taxable under this article, for a consideration or any agreement therefor.

Section 1105 of the Tax Law provides, in part:

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 1132(e) of the Tax Law provides, in part:

The commissioner may provide, by regulation, for the exclusion from taxable receipts . . . of amounts representing sales where the contract of sale has been cancelled . . . or, in case the tax has been paid upon such receipt . . . for refund of or credit for the tax so paid.

Section 525.2 of the Sales and Use Tax Regulations provides, in part:

Nature of tax. (a) Sales tax. (1)(i) Except as specifically exempted or excluded, sales tax is imposed on the receipts from:

(a) every retail sale of tangible personal property, as provided in section 1105(a) of the Tax Law;

(b) every sale, other than a sale for resale, of specifically enumerated services, as provided in sections 1105(b) and (c); . . .

* * *

(2) Except as specifically provided otherwise, the sales tax is a "transactions tax," with the liability for the tax occurring at the time of the transaction. Generally, a taxed transaction is an act resulting in the receipt of consideration for the transfer of title to or possession of (or both) tangible personal property or for the rendition of an enumerated service. The time or method of payment is generally immaterial, since the tax becomes due at the time of transfer of title to or possession of (or both) the property or the rendition of such service

Section 526.5(f) of the Sales and Use Tax Regulations provides, in part:

Trade-in. Any allowance or credit for any tangible personal property accepted in part payment by a vendor on the purchase of tangible personal property or services and intended for resale by such vendor shall be excluded when arriving at the receipt subject to tax. Only the net sale price of tangible personal property or the charge for services would be subject to tax.

Section 526.7 of the Sales and Use Tax Regulations provides, in part:

(a) Definition. (1) The words *sale*, *selling* or *purchase* mean any transaction in which there is a transfer of title or possession, or both, of tangible personal property for a consideration.

(2) Among the transactions included in the words *sale*, *selling* or *purchase* are exchanges, barters, rentals, leases or licenses to use or consume tangible personal property.

* * *

(c) Rentals, leases, licenses to use. (1) The terms *rental*, *lease and license to use* refer to all transactions in which there is a transfer for a consideration of possession of tangible personal property without a transfer of title to the property. Whether a transaction is a "sale" or a "rental, lease or license to use" shall be determined in accordance with the provisions of the agreement. . . .

Section 534.6(a) of the Sales and Use Tax Regulations provides, in part:

Cancelled sales and returned merchandise. (1) Exclusion from return. Where a contract of sale has been cancelled or the property returned within the reporting period in which the sale was made, a vendor of tangible personal property or services . . . may exclude such receipts . . . from his sales and use tax return.

(2) Credit where tax previously remitted. Where a contract of sale has been cancelled or the property returned and the tax collected thereon refunded to the customer, and such tax had been paid and reported on a return by the vendor of tangible personal property or services . . . an application for refund or credit for the tax paid upon such receipt, charge, or rent shall be filed with the Department of Taxation and Finance within three years from the date when the tax was payable by such person to the Department of Taxation and Finance. The applicant may, as part of the application for credit, take the credit on the return which is due coincident with or immediately subsequent to the time such application is filed. The application for refund or credit shall be subject to the

provisions of subdivisions (a), (b) and (c) of section 1139 of the Tax Law and section 534.2 of this Part.

Opinion

Purchaser entered into agreements in 2003 to purchase computer hardware and related prepaid maintenance services from Seller. Seller and Purchaser entered into a new agreement in 2004 for the purchase of new computer hardware and a new agreement for prepaid maintenance services. Seller agreed to allow Purchaser to trade in hardware originally sold to Purchaser by Seller. Pursuant to the terms of the 2004 Purchase Agreement, reimbursements for the value of the Trade-in Hardware are allowed by Seller to Purchaser against the purchase price of the new hardware. Further, Seller gave Purchaser an offset in the amount of the unused 2003 prepaid maintenance. For an additional charge, Seller also allowed Purchaser to continue to use the Trade-in Hardware for a period of time after Seller took title to the Trade-in Hardware.

Pursuant to section 1101(b)(3) of the Tax Law, any allowance or credit for any tangible personal property accepted in part payment by a vendor on the purchase of tangible personal property or services and intended for resale by such vendor shall be excluded when arriving at the receipt subject to sales tax. When Seller allowed Purchaser to continue to use the Trade-in Hardware for an additional charge, Seller was reselling (or renting) the Trade-in Hardware to Purchaser. Therefore, Seller's receipt subject to sales tax for the sale of the new hardware would exclude the amount of credit allowed for the Trade-in Hardware. Seller's additional charge for the use of the Trade-in Hardware is a receipt from the sale of tangible personal property subject to sales tax under section 1105(a) of the Tax Law. See section 526.7(c) of the Sales and Use Tax Regulations.

The unused prepaid maintenance services described in Petitioner's facts are not considered to be tangible personal property. Though section 1101(b)(3) of the Tax Law provides for an exclusion from taxable receipts for a trade-in allowance for tangible personal property accepted in trade and held for resale, there are not any similar provisions for a trade-in allowance for services. Even were the trade-in provision applicable to a service being offered in trade by Purchaser, the unused portion of the maintenance services were not purchased by Seller with the intent that such unused maintenance would be resold by Seller. Therefore, the amount of the reimbursement allowed in regard to unused services that were initially prepaid under the 2003 Maintenance Agreement is not excluded from Seller's receipts from the new purchases of hardware and maintenance under the 2004 Purchase Agreement as a trade-in allowance.

It does appear, however, that Seller's reimbursement to Purchaser for the amount prepaid by Purchaser for the unused balance of the maintenance services under the 2003 Maintenance Agreement could be considered a cancelled sale of the remaining portion of such maintenance services. Purchaser may be entitled to a refund of any sales tax paid attributable to the amount reimbursed for such unused prepaid maintenance. Seller may be allowed a refund or credit of the amount of sales tax collected and remitted for the unused portion of the prepaid maintenance

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services to the extent the tax is reimbursed to Purchaser. See section 534.6(a) of the Sales and Use Tax Regulations. As discussed above, any reimbursement by Seller to Purchaser for such unused prepaid maintenance does not reduce the amount of the receipts subject to tax or the amount of tax due on the purchase of the new computer hardware and the new maintenance agreement.

DATED: July 24, 2008

/s/
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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.