

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

TSB-A-08(47)S
Sales Tax
October 16, 2008

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. S071019B

On October 19, 2007, the Department of Taxation and Finance received a Petition for Advisory Opinion from Icor Systems, LLC, 152 West 36th Street, Suite 306, New York, New York 10018.

The issues raised by Petitioner, Icor Systems, LLC, are:

1. Whether Petitioner's fee for basic services described below is subject to New York sales and use tax.
2. Whether Petitioner's fees for premium services described below are subject to New York sales and use tax.
3. Whether Petitioner's notice and collection of sales tax as described below for premium services, provided such services are subject to sales tax, meet the requirements in section 1132 of the Tax Law.

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

Petitioner provides Internet access to customers at coffee bars, food service businesses, and other retail locations within New York City. Petitioner helps create an Internet cafe by placing Internet workstations in service inside existing retail businesses. The workstations consist of a chair, desk, and an Internet-connected computer that runs Petitioner's proprietary software.

Petitioner provides pay-per-use Internet service in conjunction with retail merchants and hotels on a profit-sharing basis. However, in rare cases, Petitioner enters into a fixed rent agreement whereby it pays a fixed fee to the merchant in exchange for the right to install its equipment at the location.

Petitioner does not sell food or beverages. Customers may, however, purchase food and beverages from the unrelated vendor in which Petitioner's Internet workstations are located. Food and beverage purchases by customers from the vendors are made independent of the purchase of Internet access by customers from Petitioner. There are no cover fees, minimum purchase requirements, or requirements that Internet access customers purchase food or beverages.

Basic Service

A customer logs on at any available workstation computer to access the Internet. The customer cannot reserve a specific workstation or time to use the workstation. Before access to the Internet is granted, the customer must enter a unique User ID printed on a ticket purchased for Internet access time. Upon logon, a banner across the top of the screen shows the customer how much credit is remaining and the amount of time, if any, which has already been deducted. The customer can then begin to browse the Internet.

Customers can browse the Internet for varying periods of time by using search engines. Customers may also send and receive instant messaging. Although the workstation computers have certain software applications, such as *Microsoft Word Viewer*, *Excel Viewer*, and *PowerPoint Viewer*, the customer cannot edit or save documents related to such software or insert a diskette or CD into the computer to download or save information. The customer can merely launch documents from Websites or e-mail and view such documents at the workstation. The computers do not have games or other “canned” entertainment software packages (e.g., the customer cannot upload or download music). Some workstations have the ability to print documents, but a separate, additional charge upon which sales tax is collected is made for such service.

Payment and Pricing for Basic Service

Petitioner provides several payment methods as follows:

1. Purchase a prepaid card.
2. Insert cash into an automated bill acceptor.
3. Use credit card by entering card number manually or by swiping the credit card at a workstation.

Not all payment methods are available at every location, but all locations include the ability to accept a credit card either by swiping the card at the workstation or manually entering the information.

Customers utilizing Petitioner’s service receive a fixed amount of Internet time up front for a specific price. Pricing for the service typically begins at 20¢ per minute, but is generally structured so that large dollar purchases enable the customer to purchase time at a lower rate. If prepaid cards are sold, the customer has the ability to purchase one of several pricing options. The least expensive card entitles the holder to 10 minutes and costs \$2.00. The most expensive prepaid card entitles the holder to 60 minutes and costs \$8.00. At locations with automated bill acceptors, customers can purchase any dollar amount of time at a rate of 20¢ per minute, but are awarded bonus minutes at the purchase thresholds of \$5.00, \$10.00, and \$20.00. When customers purchase time with a credit card, they choose from a list of price and minute

combinations that start at \$5.00 for 30 minutes, including purchases of up to 600 minutes for \$39.00.

Premium Service

When using the basic Internet work stations, customers can also purchase certain premium services for an additional charge. The premium services allow customers access to the following software:

- *Microsoft Word*
- *Microsoft Excel*
- *Microsoft PowerPoint*

Premium services also allow customers to download information from the Internet to the local computer and allow the customer to use the selected software functions. For example rather than just being able to view screens, customers will also be able to use the software to edit the content which they download.

Once a customer attempts to access a premium service, a user notification pop-up window is displayed on the screen. This initial pop-up window presents the customer with “OK” and “cancel” buttons asking the customer to confirm that he or she wishes to access the set of premium services and agrees to the additional charge for the service. If the customer makes no decision within 20 seconds, the window screen closes and the customer is directed back to the basic Internet access service. If the customer does accept the additional charges, the customer is permitted to use the premium services.

Payment and Pricing for Premium Service

Petitioner charges an additional 2.5¢ per minute for the use of its premium service. Petitioner collects and remits the New York State and New York City sales tax at the rate of 8.375% on the additional charge associated with the premium service. Accordingly, the additional per minute cost of the service, including sales tax, is 2.7¢ per minute.

The following is an example of a typical premium service transaction:

A customer purchases a 10-minute card for \$2.00 and will incur a charge for the use of Petitioner’s basic service of 20¢ per minute. If such customer chooses to utilize Petitioner’s premium service, he or she will incur an additional fee for such service at the rate of 2.5¢ per minute. At the conclusion of the customer’s usage of the premium service, Petitioner will collect New York State and City sales tax on such additional fee. Assuming that the customer utilizes Petitioner’s premium service for 5 minutes, he or she will incur a charge of 12.5¢. In addition, Petitioner will collect and remit 1.05¢ of

New York State and City sales tax on such charge. Thus, including the charge of \$1.00 for access to Petitioner's basic service, the customer will incur total fees of \$1.14 (rounded) during his or her 5 minute session.

In this example, the time deduction associated with the basic charge of \$1.00 (i.e., 5 minutes) is made in real-time as the customer uses the service. In addition to such 5 minute deduction, the time deduction associated with the additional 14¢ in fees is accrued while the premium service is used at a translated rate of one second deducted per 7.4 seconds of usage (20¢ per minute / 2.7¢ per minute). The accrued time deduction for the 14¢ additional charge will amount to roughly 41 seconds after 5 minutes of use. At the end of the 5 minutes of premium usage, the additional accrued balance of 41 seconds will be deducted from the main balance. The customer will have 4 minutes 19 seconds remaining instead of the full 5 minutes that they otherwise would have had remaining if they had only used the basic service and had not used the premium service.

At the conclusion of the session, a session summary screen will summarize the total time accrued in accessing the Internet, the time spent on the premium service, the charges for the premium service, and New York State and City sales tax associated with those charges.

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:

* * *

(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, . . .

* * *

(6) Tangible personal property. Corporeal personal property of any nature. However, except for purposes of the tax imposed by subdivision (b) of section eleven hundred five, such term shall not include gas, electricity, refrigeration and steam. Such term shall also include pre-written computer software, whether sold as part of a package,

as a separate component, or otherwise, and regardless of the medium by means of which such software is conveyed to a purchaser. . . .

* * *

(14) Pre-written computer software. Computer software (including pre-written upgrades thereof) which is not software designed and developed by the author or other creator to the specifications of a specific purchaser. The combining of two or more pre-written computer software programs or pre-written portions thereof does not cause the combination to be other than pre-written computer software. Pre-written software also includes software designed and developed by the author or other creator to the specifications of a specific purchaser when it is sold to a person other than such purchaser. Where a person modifies or enhances computer software of which such person is not the author or creator, such person shall be deemed to be the author or creator only of such person's modifications or enhancements. Pre-written software or a pre-written portion thereof that is modified or enhanced to any degree, where such modification or enhancement is designed and developed to the specifications of a specific purchaser, remains pre-written software; provided, however, that where there is a reasonable, separately stated charge or an invoice or other statement of the price given to the purchaser for such modification or enhancement, such modification or enhancement shall not constitute pre-written computer software.

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 1115(v) of the Tax Law provides:

Receipts from the sale of Internet access service, including start-up charges, and the use of such service, shall be exempt from the taxes imposed under this article. For purposes of this subdivision, the term "Internet access service" shall mean the service of providing connection to the Internet, but only where such service entails the routing of Internet traffic by means of accepted Internet protocols. The provision of communication or navigation software, an e-mail address, e-mail software, news headlines, space for a website and website services, or other such services, in conjunction with the provision of such connection to the Internet, where such services are merely incidental to the provision of such connection, shall be considered to be part of the provision of Internet access service.

Section 1132(a)(1) of the Tax Law provides:

Every person required to collect the tax shall collect the tax from the customer when collecting the price, amusement charge or rent to which it applies. If the customer is given any sales slip, invoice, receipt or other statement or memorandum of the price, amusement charge or rent paid or payable, the tax shall be stated, charged and shown separately on the first of such documents given to him. The tax shall be paid to the person required to collect it as trustee for and on account of the state.

Section 532.1(b) of the Sales and Use Tax Regulations provides, in part:

Statement of and reference to tax. (1) Whenever the customer is given any sales slip, invoice, receipt, or other statement or memorandum of the price, amusement charge, or rent paid or payable, the tax shall be stated, charged and shown separately on the first of such documents given to him.

(2) Whenever the sales and use tax is separately stated on such document, it may be referred to as *tax*.

(3) The words *tax included* or words of similar import, on a sales slip or other document, do not constitute a separate statement of the tax, and the entire amount charged is deemed the sales price of the property sold or services rendered.

(4) No written receipt. For sales other than sales of gasoline and diesel fuel a unit price method of accounting for sales may be used where no written receipt is given to the customer. The *unit price* is the price, including sales tax, at which the sale is recorded. Since the customer must be made aware of the inclusion of sales tax in the total sales price, every business establishment employing the unit price method must visibly display, to all customers a placard stating that the prices of all taxable items include sales tax. If the sale is recorded on a cash register it may be rung up on a single ring, a quantity of individual items may be rung up in total, or a quantity of items can be rung up individually with a total. In addition, the vendor shall, for the benefit of his customers, distinguish between taxable and nontaxable items offered for sale. This may be done by such methods as:

(i) attaching labels to merchandise to indicate taxable or nontaxable status;

(ii) displaying taxable and nontaxable merchandise separately; or

(iii) having available detailed listings of taxable and/or nontaxable items. It is the responsibility of every vendor who sells both taxable and nontaxable items to maintain accurate records indicating such sales.

Section 1106(a) of the federal Internet Tax Freedom Act (cited in the note following 47 U.S.C. § 151) provides:

In general. If charges for Internet access are aggregated with and not separately stated from charges for telecommunications or other charges that are subject to taxation, then the charges for Internet access may be subject to taxation unless the Internet access provider can reasonably identify the charges for Internet access from its books and records kept in the regular course of business.

Opinion

Petitioner operates an Internet cafe located in New York City. Petitioner provides customers with a pay-per-use Internet service also described by Petitioner as basic service. Basic service is available for a specified per-minute charge. After a customer logs-on to use Petitioner's basic service the customer is also offered the option of accessing prewritten software described by Petitioner as premium service for an additional charge. Customers choosing to use the premium service will incur a per-minute charge for the premium service in addition to the basic service charge.

Petitioner's charges for basic service are considered to be for Internet access. Charges for such Internet access are exempt from sales tax under section 1115(v) of the Tax Law. See *Wealth and Tax Advisory Services, Inc.*, Adv Op Comm T&F, December 14, 2004, TSB-A-04(27)S.

Section 1101(b)(6) of the Tax Law provides that prewritten software is deemed to be tangible personal property for sales tax purposes. Petitioner's receipts for premium service include additional charges for the use of prewritten software. The fee paid for the lease or license to use or consume prewritten computer software, regardless of the medium by means of which such software is conveyed to the purchaser, is subject to New York State sales tax under section 1105(a) of the Tax Law. When the charge for Internet access is aggregated with the charge for use of the prewritten software for a single lump sum charge, the entire charge will be subject to sales tax unless the Internet access provider can reasonably identify the charges for Internet access from its books and records kept in the regular course of business. See section 1106(a) of the Internet Tax Freedom Act (cited in the note following 47 U.S.C. § 151). Since in this instance, the charges for Internet access bundled into the charge for premium service are separately determinable, the amount charged to provide Internet access as part of the premium service (i.e., the cost for basic Internet access service) is excludible from the receipt subject to sales tax. However, Petitioner's additional charge for premium service is subject to sales tax under section 1105(a) of the Tax Law.

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At the conclusion of the session, a screen will summarize the total time accrued in accessing the Internet, the time spent on the premium service, the charges for the premium service, and New York State and City sales tax associated with such charges. While it is not clear if a customer may also obtain a printout of a session summary screen, it does appear that the tax is stated, charged, and shown separately on the first of statement of charges provided to the customer by Petitioner as required by section 1132 of the Tax Law.

DATED: October 16, 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.