

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition :  
of :  
**APPLE INC.** : DETERMINATION :  
for Revision of a Determination or for Refund of Sales and : DTA NO. 827287 :  
Use Taxes under Articles 28 and 29 of the Tax Law for :  
the Period December 1, 2009 through November 30, 2012. :  
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Petitioner, Apple Inc., filed a petition for revision of a determination or for refund of sales and use taxes under articles 28 and 29 of the Tax Law for the period December 1, 2009 through November 30, 2012.

A hearing was held before Kevin R. Law, Administrative Law Judge, in New York, New York, on November 29, 2017 at 10:30 a.m., with all briefs to be submitted by May 4, 2018, which date began the six-month period for the issuance of this determination. Petitioner appeared by McDermott, Will and Emery, LLP (Peter L. Faber, Esq., Mark W. Yopp, Esq. and Stephen P. Krantz, Esq., of counsel). The Division of Taxation appeared by Amanda Hiller, Esq. (David Gannon, Esq., of counsel).

***ISSUE***

Whether petitioner properly collected and remitted sales tax on qualifying device sales made during its 2011 and 2012 Back to School promotion.

***FINDINGS OF FACT***

1. Petitioner, Apple Inc., is a corporation organized under the laws of California that designs and markets consumer electronics, software, and personal computers. Petitioner's electronic device products included mobile communication devices (e.g., iPhones), personal computers (e.g., MacBook, iMac, MacBook Pro, Mac Mini), portable digital music players (i.e., iPods), device peripherals and accessories (e.g., computer displays), entertainment platforms devices (e.g., Apple TV), and, beginning in 2010, tablets (e.g., iPads).

2. Petitioner sells its products through a variety of channels, i.e., indirectly, through traditional retailers, and directly to customers via its retail stores and over the internet via its online stores.

3. Petitioner's online stores include the Mac App Store, the iTunes Store, the App Store, and the iBookstore (online stores).

4. In addition to electronic devices, petitioner's online stores sell digital content, including computer software, digital music, digital movies, applications for phones and tablets, games, and digital books.

5. In August 2012, the Division of Taxation (Division) commenced a sales and use tax audit of petitioner. The audit examined petitioner's sales, expense purchases and capital asset purchases. Petitioner and the Division reached agreement on all but one aspect of the audit. The focus of this proceeding relates to the amount of sales tax charged by petitioner on sales of electronic devices made during petitioner's 2011 and 2012 Back to School promotion (BTS promotion).

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<sup>1</sup>The parties executed a stipulation of facts in connection with this matter. Such stipulated facts have been substantially incorporated into the findings of fact set forth herein.

6. In 2011 the Mac App Store was launched. In order to raise awareness of the Mac App Store, petitioner offered a BTS promotion starting in 2011. The BTS promotion was also offered in 2012.

7. During 2011 and 2012, petitioner published terms and conditions for the BTS promotion on its website. The terms and conditions described the terms and conditions of the BTS promotion and were publicly accessible.

8. Under the terms and conditions of the BTS promotion, Qualified Education Individuals included faculty, staff, students, and parents as follows:

“K-12 - Any employee of a public or private K-12 institution in the United States is eligible. In addition, school board members who are currently serving as elected or appointed members are eligible. [Parent-Teacher Association] or [Parent-Teacher Organization] executives currently serving as elected or appointed officers are eligible.”

“Higher Education - Faculty and staff of higher education institutions; and students attending, or accepted into a higher education institution are eligible.”

“Higher Education Parents - Parents purchasing on behalf of their child, who is a student currently attending or accepted into a public or private higher education institution in the United States, are eligible.”

9. Under the terms and conditions of the BTS promotion, “Qualified Education Individuals” who purchase a qualifying Apple Computer or iPad between [a designated time frame] “may receive a Back to School Gift Card in the following amounts that can be used at the Mac App Store, the iTunes Store, the App Store, and the iBookstore.”

10. A qualifying product for the BTS promotion included certain qualifying computers and certain qualifying iPads. Qualifying computers and the qualifying iPads are referred to as the “qualifying products.”

11. A gift card was received by the customer in connection with the BTS promotion (BTS card). The BTS card had a value of either \$100.00 or \$50.00, depending on the qualifying product purchased.

12. The 2011 BTS promotion was the first Apple promotion to include a gift card that could be used in an App Store. Aside from the inclusion of the iPad in the 2012 BTS promotion, the 2011 BTS promotion and the 2012 BTS promotion did not have any material differences.

13. A customer that purchased a qualifying product in a BTS promotion could decline the BTS card. If the BTS card were declined the full price of the product with applicable tax was charged.

14. Per the terms and conditions if a qualifying product was returned, the BTS card was required to be returned with the qualifying product in order for the customer to receive a full refund. If the BTS card was not returned or had been redeemed, the full value of the BTS card was deducted from the refund of the qualifying product.

15. The disagreed part of the audit resulted from a one day test period wherein customer invoices from petitioner's retail stores were reviewed, with the subtotal on the invoice being multiplied by the applicable tax rate. This review led to a discrepancy between the amount of tax the Division determined should have been collected and the amount actually collected by petitioner for sales subject to the BTS promotion. Upon inquiring with petitioner, it was explained that tax was computed on the price of the qualifying device less a discount equal to the value of the BTS gift card received by the customer.

16. The Division's audit also examined petitioner's on-line sales made during the BTS promotion. Unlike retail store sales, the Division did not find a discrepancy in the computation of sales tax due on the purchase of qualifying products as part of petitioner's BTS promotion.

The Division explored why the issue discovered with retail store sales was not occurring with on-line sales, and found an on-line message board posting of a chat exchange between one of petitioner's employees and a customer. The exchange reflects a customer trying to complete an on-line BTS transaction but having a problem because when the \$100.00 gift card was an item in his shopping cart, petitioner's on-line system was charging him for it. Petitioner's employee advised the customer to remove the gift card from his shopping cart, telling him "[t]hat will set you up with the proper price" and "[o]ur processing department are [sic] manually adding cards to your orders today."

17. Alexis Sapsford was the primary contact for marketing promotions in petitioner's retail stores in 2011 and 2012 and was responsible for implementing the BTS promotion in the retail stores. According to Mr. Sapsford, it took approximately six to seven months to implement and roll out the BTS promotion in retail stores. During this time, Mr. Sapsford and his team tested the feasibility of the offer, drafted the terms and conditions for the BTS promotion, and designed marketing materials for the BTS promotion. Mr. Sapsford also worked with the point of sale (POS) systems team to make sure that petitioner's POS system could support the offer. Petitioner's tax, accounting, and legal teams were required to approve the terms and conditions of the BTS promotion before the BTS promotion was rolled out. Similarly, petitioner's tax and legal teams were required to approve the marketing materials for the BTS promotion before it was released. In addition, the petitioner's POS, tax, accounting, and legal teams reviewed sample invoices for sample BTS promotion transactions before the BTS promotion was rolled out.

18. According to Mr. Sapsford, when the promotion was brought to the POS team to make sure that the POS system could support the offer, the POS team told him that the POS system

was unable to discount a gift card and, thus, that the BTS Card could not be processed as free. The only way that the POS system could process the BTS promotion was to discount the price of the qualifying product (the computer or the iPad) and charge the customer for the full value of the BTS card. According to Mr. Sapsford, the BTS promotions were structured such that the BTS card was not free because the POS system could not process the transaction otherwise.

19. Sheila Bayley was the person on petitioner's tax team responsible for reviewing and approving the BTS promotion. Ms. Bayley was Mr. Sapsford's primary contact on the tax team with respect to the BTS promotion. When Mr. Sapsford approached Ms. Bayley about the BTS promotion, she said that the BTS card should not be given to the customer for free because if the BTS card was given to the customer for free petitioner would over-collect sales tax when the BTS card was used to purchase a taxable item and, thus, petitioner could be subject to class action lawsuits for such overcollection. Petitioner has been subject to over-collection suits in the past and overcollection is always a primary concern of the tax team when reviewing promotions.

20. Ms. Bayley also indicated that petitioner did not treat the BTS gift card as current revenue on petitioner's books for accounting purposes but booked the gift card as deferred revenue.

21. Consistent with the terms and conditions, the word "free" was not used in petitioner's advertising. The advertisements consistently state that if the customer buys a qualifying product, he or she will receive a gift card or get a gift card or some variation thereof.

22. One particular advertisement reviewed by the Division states in part:

"Congratulations. Your Mac will come with a \$100 Back to School Gift Card. We'll add your \$100 Back to School Gift Card to your order. You'll see it appear in your cart, but you will not be charged for it at checkout."

23. In a FAQ contained on petitioner's website related to the 2012 promotion the following question and answer were published:

“Why was I charged for the free Back to School Gift Card?”

“Your invoice or receipt will also show an equivalent discount amount to cancel out the charge for the card. As a result, your invoice or receipt will amount to the cost of the Mac or iPad only including applicable shipping cost and sales tax.”

24. On or about June 2, 2014, the Division issued two statements of proposed audit changes that asserted additional tax and interest. The first was for adjustments that petitioner agreed to that asserted additional tax of \$620,466.22, interest of \$76,542.20, and a credit of \$28,077.37 (agreed proposed audit change). The second statement asserted tax of \$955,197.44 and interest of \$141,744.70 related to the BTS promotion (BTS assessment); this statement was based upon the Division's determination that petitioner had under-collected tax on qualifying device sales made during the BTS promotion.

25. Prior to June 2, 2014, petitioner made a \$1,000,000.00 prepayment of sales tax to the Division.

26. On or after June 2, 2014, the Division applied the prepayment to the agreed proposed audit change and the BTS assessment.

27. On June 26, 2014, the Division issued a notice of determination (notice # L-041615716) to petitioner, for the periods ending August 31, 2011, November 30, 2011, August 31, 2012, and November 30, 2012 (notice). The notice reflects a balance due of \$731,882.84, consisting of tax of \$995,197.44, interest of \$144,296.55, and credit for payments of \$407,611.15.

28. On or about March 27, 2014, petitioner made a second payment to the Division for \$805,873.19 which was applied to the balances of the agreed proposed audit change and the BTS

assessment. Both the agreed proposed audit change and the BTS assessment have been paid in full.

### ***CONCLUSIONS OF LAW***

A. Tax Law § 1105 (a) imposes a sales tax on the receipts from every retail sale of tangible personal property except as otherwise provided in article 28 of the Tax Law. 20 NYCRR 526.5 (a) defines receipt as “. . . the amount of the sale price of any property and the charge for any service taxable under articles 28 and 29 of the Tax Law, valued in money, whether received in money or otherwise.” Tax Law § 1132 (c) (1) sets forth a presumption that all sales receipts for tangible personal property are subject to tax “until the contrary is established,” and sets the burden of proving the contrary upon the vendor or its customer (20 NYCRR 532.4 [a] [1]; [b] [1]). Discounts that represent a reduction in price are deductible from receipts (20 NYCRR 526.5 [d]). The amount of a discount of a store-issued coupon, where the store is not reimbursed by a third party, is not included in taxable receipts (20 NYCRR 526.5 [c] [3]). In the case of gift cards, the Division does not impose sales tax on the sale or transfer thereof; instead sales tax is imposed when the customer exchanges the gift card in whole, or in part, for an item subject to sales tax (*see* TB-ST-806).

B. The question for resolution herein is whether the BTS promotion required the purchaser to purchase a gift card to receive a discount equal to the value of the card on the qualifying purchase of a computer or tablet or whether the promotion required the purchase of a qualifying computer or tablet in order to receive a gift card for free. The answer to that question is determined based upon the terms and conditions of the BTS promotions as well as the surrounding facts and circumstances. Because sales of gift cards are not subject to sales tax, if the customer purchased the gift card along with the qualifying device, then sales tax would only



be imposed upon that part of the purchase price attributed to the qualifying device. Conversely, if the customer received the gift card for free then sales tax was required to be collected on the total purchase price. An examination of the BTS promotion's terms and conditions and the relevant facts and circumstances lead to the conclusion that the BTS promotion required the purchase of a qualifying computer or tablet in order to receive the BTS card for free.

C. First, although the BTS terms and conditions did not state that the gift card was "free," the terms and conditions also did not state that the purchase of a gift card was required in order to receive a discount of equal value on the purchase of the qualifying product. The terms and conditions are clear: they require the purchase of a qualifying device in order to receive a gift card. The implication is clear that the gift card was free. Petitioner's advertisements support this conclusion; i.e., purchase a computer get a gift card to spend on apps. In this case, the offer must be interpreted as an average customer would view the offer. In fact, one of petitioner's advertisements directly contradicts petitioner's witnesses testimony on this score wherein it states:

"Congratulations. Your Mac will come with a \$100 Back to School Gift Card. We'll add your \$100 Back to School Gift Card to your order. You'll see it appear in your cart, but you will not be charged for it at checkout."

Petitioner's FAQs related to the 2012 promotion also support this point wherein the following question and answer were posed:

"Why was I charged for the free Back to School Gift Card?"

"Your invoice or receipt will also show an equivalent discount amount to cancel out the charge for the card. As a result, your invoice or receipt will amount to the cost of the Mac or iPad only including applicable shipping cost and sales tax."

D. Petitioner's assertion that the BTS promotions were structured to require purchase of a qualifying device and a gift card with it in order to receive a discount equal to the amount of the

gift card off the price of the qualifying device is further undermined by petitioner's treatment of its online sales made during this promotion. As noted the Division examined petitioner's online sales and did not find the discrepancy at issue herein.

E. Although petitioner has a legitimate interest in not over collecting sales tax on its sales, that interest does not dwarf the Division's interest in seeing that sales tax is properly collected in the first instance. Petitioner's argument focuses on the situation where a customer pays sales tax on the purchase of a qualifying device and later, upon redemption of the BTS card, pays sales tax on items subject to tax. According to petitioner, this scenario creates double taxation. Petitioner claims that the Division's interpretation leads to the risk of double taxation and offers the following example as illustrative of its concerns. Assume that the computer cost \$1,000.00 and the customer received a free \$100.00 BTS card with the purchase. When the customer purchased the computer under the BTS Promotion, he or she would pay \$1,000.00 and pay sales tax on \$1,000.00. Assuming that the customer used the entire \$100.00 BTS card to purchase taxable applications from a New York billing address, the customer would pay tax on the full \$100.00. According to petitioner, although the customer only paid \$1,000.00 to petitioner, he or she was required to pay tax on \$1,100.00; therefore according to petitioner, double taxation would occur.

Petitioner's assertion is rejected as the hypothetical involves two separate transactions which must be treated as such. In this case, the perceived double taxation occurs during the second transaction which is not the subject of this proceeding and therefore is not subject to review herein. However, even if that transaction were the subject of this proceeding, it is determined that double taxation does not occur. In the first transaction, the customer is taxed on the amount paid for computer, which is the full \$1,000.00. In the second transaction where the customer uses the gift card to purchase taxable applications, sales tax is imposed upon the value

of the gift card used to consummate the purchase (*see* 20 NYCRR 526.5 [a]). The gift card is something of value, whether paid for by cash or whether given to the customer for free. As such, it qualifies as a receipt under the Tax Law (*id*). The incidence of taxation does not relate back to how petitioner obtained the gift card. While petitioner's argument and reporting position might set forth a basis for abatement of penalties if such had been imposed, this is not the case herein.

F. The petition of Apple Inc., is denied and the notice of determination, dated June 26, 2014, is sustained.

DATED: Albany, New York  
November 01, 2018

/s/Kevin R. Law  
ADMINISTRATIVE LAW JUDGE