

PRIVATE TAXPAYER RULING LR99-010

November 15, 1999

The following private taxpayer ruling is provided in response to your letter dated September 13, 1999. Your letter requests a department ruling whether the sale of "gift cards" is subject to the Arizona transaction privilege tax.

The following is a restatement of the relevant facts as presented in your request for a private taxpayer ruling on behalf of ***.

Statement of Facts:

- *** is a retailer of tangible personal property.
- *** will be offering a *prepaid* merchandise card to be called a "gift card".
- The gift card may be purchased in specific denominations from any store location.
- The gift card may be presented for the purchase of merchandise at any *** location.
- The total purchase price of the merchandise including the transaction privilege tax will be deducted from the prepaid denomination on the gift card.
- Customers may add funds to the card by purchasing the desired amount from any store location subject to some restrictions. Gift cards with a cash value of less than five dollars are redeemable for cash.

Your Position:

Gift cards are indistinguishable from gift certificates except that a customer may increase the cash value of the gift card by adding funds to the card. The sale of gift certificates is not subject to tax because it is considered a cash equivalent. Therefore gift cards are a cash equivalent and similar to gift certificates.

Furthermore, taxing the sale of gift cards and taxing the merchandise subsequently purchased with that gift card would be double taxation.

Applicable Statutory Provisions:

Arizona Revised Statutes (A.R.S.) § 42-5001(13) provides that a "sale" includes any transfer of title or possession of tangible personal property for a consideration in any manner or by any means.

A.R.S. § 42-5061 imposes the transaction privilege tax on the business of selling tangible personal property at retail.

A.R.S. § 42-5155 imposes the use tax on tangible personal property purchased from a retailer that was not subject to the transaction privilege tax, and is used, stored or consumed in Arizona.

Legal Reference:

State Tax Commission v. Ryan-Evans Drug Stores, 89 Ariz. 18, 357 P.2d 607 (1960), described the receipt of trading stamps by a retail establishment's customer as the transfer of intangible property which gave the customer the claim or right to a future benefit.

Discussion:

*** intends to sell *plastic* cards called "gift cards". The use of these cards will allow merchandise to be purchased against a prepaid account. The gift card purchaser pays for a predetermined amount of monetary value. A charge for each purchase is deducted after each use and the user is notified of the monetary value, which remains.

When a retailer sells these cards to a customer, the transaction represents a prepayment of charges for merchandise and retail services. The gift card represents a claim or right against the retailer.

A retailer's sale of gift cards or a gift certificate is a nontaxable transaction. The customer receives an intangible right to prepaid merchandise and services. There is no exchange of title, possession or services at the point of sale. Like a money order, check, or gift certificate, a gift card represents an intangible future claim. In the case of a gift card, the claim is for merchandise and retail services. The gift card itself does not provide access to the merchandise and services; access is provided by the intangible information printed or encoded on the card.

In *Ryan-Evans*, the Arizona Supreme Court addressed the issue of trading stamps, which a retailer gave to its customers with each retail purchase. The trading stamps could be compiled by the customer and redeemed for merchandise at the trading stamp company's redemption center. Even though the retailer merely purchased the trading stamps from the trading stamp company and gave the stamps to its customers, the court described the retailer as the agent or licensee of the trading stamp company. In giving the trading stamps to its customers, the

retailer transferred a claim against the trading stamp company. The court specifically described the trading stamps as "intangible property".

Like trading stamps, gift cards represent an intangible right to prepaid merchandise and services. When a retailer sells gift cards, the retailer neither is neither selling tangible personal property nor retail services, but is instead selling the intangible right to receive merchandise and services. The gift card is merely the inconsequential tangible personal property, like a gift certificate, accompanying the purchase of the right to receive merchandise and services.

The gross proceeds of sales or gross income derived from the sales of gift cards by a retailer are not initially taxable to the retailer. However, subsequent use of the card by the ultimate purchaser to buy merchandise and retail services results in the prepaid income then becoming a part of the retailer's taxable proceeds.

Arizona's use tax is imposed on the storage, use or consumption of tangible personal property in this state, when the purchase was not subject to the transaction privilege tax. The use tax is imposed as a percentage of the sales price. For the retailer, who sells the gift cards as an inconsequential transfer of tangible personal property accompanying the sale of the intangible right to receive merchandise and services; the use tax is applicable to the use, storage or consumption of the cards in Arizona if the purchase of the cards was not subject to the transaction privilege tax.

Conclusion:

Sales of gift cards, which provide an intangible right to receive future merchandise and retail services, are not taxable when sold by ***. *** gross proceeds of sales or gross income derived from the sale of the gift cards are excludable from the tax base at the time of the sale.

Subsequent purchases of merchandise and retail services charged against the value of the prepaid gift cards are included in the tax base.

The use tax may be applicable to the use, storage or consumption of the cards in Arizona.

This response is a private taxpayer ruling and the determinations herein are based solely on the facts provided in your request. The determinations in this taxpayer ruling are the present position of the department. The determinations are subject to change should the facts prove to be different on audit. If it is determined that undisclosed facts were substantial or material to the department's making of an accurate determination, this taxpayer ruling shall be null and void. Further, the determination is subject to future change depending on changes in statutes, administrative rules, case law or notification of a different department position.