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May 2, 1995

Mr. J--- C---, Jr.  
Senior Manager  
--- & --- ---  
XX --- Street  
--- ---, CA XXXXX-XXXX

Re: K---, Inc.  
SR -- XX-XXXXXX

Dear Mr. C---:

This is in reply to your February 22, 1995 letter regarding sales of CD-ROM disks by your client, K---, Inc.

Since we have previously corresponded regarding these transactions, we will summarize the facts here. As part of the sale of a multi-media subscription, K--- sells a CD-ROM disk which embodies software programs. The purchaser of the disk has access only to certain software but may examine demonstrations of other software embodied on the disk. K--- has an "800" telephone number which the purchaser may call to pay a fee to obtain an "unlock code" which enables the purchaser to access other programs on the disk. You believe sales tax applies only to K---'s charge for the initial transfer of the CD-ROM disk and does not apply to K---'s charges for providing access codes.

You note you believe the charge for the unlock code should be seen as a separate and distinct transaction from the sale of the disk and title has been transferred and tax reimbursement has been collected on the CD-ROM disk long before K--- provides the unlock code. You believe the unlock code merely facilitates the electronic transmission of the program from the subscriber's disk to the subscriber's computer. You also believe the situation is similar to one where a person purchases a computer program, and the vendor, under a separate contract, transfers modifications electronically over a modem.

We disagree. When a person purchases a disk from K--- which contains a number of programs, the transfer of the disk containing the programs is a sale of tangible personal property. The payment of a fee to obtain a code to unlock or access the programs on the disk is a payment for use of the disk which is tangible personal property. Under Revenue and Taxation Code section 6012, the taxable gross receipts of K---'s sale are the total amount of the sale price of the disk. The purchaser's having to pay part of the sale price after it receives delivery of the disk in order to make a further use of the disk is not a basis for excluding the amount from K---'s gross receipts of the sale. Obviously, when the purchaser of a disk agrees to pay an amount to K--- in order to use new parts of the disk, the amount is payment for the disk. The communication of a password is merely K---'s means of enforcing the purchaser's obligation to pay for the further use of the disk. The situation is akin to that where a vendor sells tangible personal property for a fixed price and charges a royalty for the purchaser's future use of the property. Payments made years later for the use of the property are part of the taxable selling price. (See Bus. Taxes Law Guide Annots. 295.0560 and 295.0570.)

Further, we do not believe the transaction is akin to one where a person makes a nontaxable transfer of information by telecommunications, such as by modem. In that situation, the charge is nontaxable only when the transferor does not provide tangible personal property, such as storage media, in the transaction. (Sales and Use Tax Reg. 1502, subd. (f)(1)(D).)

We hope this answers your questions.

Very truly yours,

Ronald L. Dick  
Supervising Staff Counsel

RLD:sr

cc: San Jose District Administrator