

**STATE BOARD OF EQUALIZATION**

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June 30, 1995

BURTON W. OLIVER
Executive Director

C--- W---
Project Manager
B--- D--- I---
XXX --- Ave., Suite XXX
---, CA XXXXX

Re: Tax Consequence of Contracts

Dear Ms. W---:

This is in response to your March 16, 1995 letter to Mr. Gary Jugum.

You inquired what the taxable consequences are of B--- D--- I---'s ("BDI") performance of a contract with K---, a Los Angeles television station. You sent a copy of a portion of that contract, and we discussed the matter over the telephone.

BDI has contracted to design a news set for K---. BDI will provide preliminary sketches; 3-D drawings of the approved design concept; specifications for carpets, paints and laminate; a color rendering of the finished product; and detailed blueprints and working drawings merging all these elements with the architect's drawings for K---'s use in its construction of the set. You have not indicated whether BDI will give the preliminary sketches to K--- to keep. The contract provides that K--- will reimburse BDI for per diem, mileage expenses, and other expenses associated with the completion of the contract. You inquire what sales tax, if any, will be due on the K--- contract.

A short review of general sales tax law follows.

Section 6051 of the Revenue and Taxation Code imposes the sales tax on retailers for the privilege of selling tangible personal property at retail in this state. A retail sale means a sale for any purpose other than resale in the regular course of business in the form of tangible personal property. (Rev. & Tax. Code §6007.) The measure of tax is the gross receipts from the retail sale in this state of tangible personal property. Gross receipts means the total amount of the retail sales of retailers valued in money, whether received in money or otherwise, without any deduction for the cost of the materials used, labor or service cost, interest paid, losses or any other expense. (Rev. and Tax. Code §6012.)

Sales tax applies to the entire amount charged by commercial artists or designers for items of tangible personal property such as drawings, paintings, designs or sketches transferred to the client. (Sales and Use Tax Reg. 1540(c).) However, tax does not apply to separate charges for preliminary art which is defined as roughs, visualizations layouts and comprehensives, title to which does not pass to the client. Preliminary art is prepared by the designer solely for the purpose of demonstrating an idea or message for acceptance before a contract is entered into or before approval is given for the preparation of finished art. Tax does not apply to separately stated charges for preliminary art except where the preliminary art becomes physically incorporated into the finished art. (Sales and Use Tax Reg. 1540(b)(4)(A).)

Based on the two page portion of the contract you sent, it appears that BDI will perform two functions under the contract. One function is titled, "Design/Consulting Services." Under the contract, BDI contracts to design a newsroom for K---. As noted above, under Sales and Use Tax Regulation 1540, subdivision (c), tax applies to the total gross receipts of your sales of designs. Tax does not apply to your separately stated charges for preliminary art if the charges qualify under the criteria of subdivision (b)(4)(A) of the regulation.

The taxable gross receipts include your charge for all expenses you incur including travel expenses and costs of blueprints you use. You may issue a resale certificate to purchase blueprints ex-tax when you sell the blueprints to your clients prior to your making any use of them.

The other function is titled "News Set - Move to New Studio." The specific charges are for BDI's providing consultation to facilitate moving the news set and design consultation to select colors and wall coverings; charges for an "install tech"; and charges for per diem for the "install tech."

If K--- has the option whether or not to have BDI perform that function, we believe BDI's charge is not a service that is part of the sale of tangible personal property. In that case, tax does not apply to BDI's charge for those separately stated consultation charges.

You sent a portion of a copy of a contract BDI had to design and construct a set for a news program for K--- of Houston, Texas. The contract lists 44 separate items, some of which K--- is responsible for furnishing.

You asked for our opinion as to the application of tax to the contract if the sale had occurred in California instead of out-of-state. Tax would apply to your sale of designs as described above. Sales tax applies to your sale of the furniture items. Transportation charges associated with this sale may or may not be taxable dependant upon various factors. I am enclosing a copy of Sales and Use Tax Regulation 1628 for your information.

Your list contains a number of items which a construction contractor would typically furnish and install. However, your facts also indicate you may construct items of tangible personal property, such as portable walls and platforms, and deliver them to the customer's site and install them. In such case, your sale is subject to sales tax. Your charges for installing the property sold are excluded from the measure of tax. However, your charges to fabricate property in place are taxable. (Sales and Use Tax Reg. 1546, subd. (a).)

Given the lack of facts as to the nature of the property and whether or not you affix the property to realty, we are unable to give you a definitive answer. However, enclosed is a copy of Sales and Use Tax Regulation 1521, Construction Contractors, for your information. As the regulation provides, if you erect or construct an improvement on to realty, you perform a construction contract. In that case, you would be the consumer of "materials" you furnish and install. You would be the retailer of "fixtures" you furnish and install.

We note that, under item 24 of the contract, BDI furnishes carpeting. Under item 25, the customer is responsible for installing the carpeting. In that event, BDI is the retailer of the carpeting, and sales tax would apply to BDI's total sale price of the carpeting.

If, after you review Regulation 1521, you have questions as to the application of tax to your charges, feel free to write again. If so, please provide a description of the facts surrounding your sale.

If you have any further questions, please do not hesitate to write.

Sincerely,

Anthony I. Picciano
Staff Counsel

AIP:es

Encs: Regs. 1521, 1540, 1628

cc: --- --- District Administrator (--)