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April 10, 1996

Ms. J--- M---
The A--- G---
XXXX W. --- ---, Suite X
---, California XXXXX

E. L. Sorensen, Jr.
Executive Director

Re: Account No. SR --- XX-XXXXXX

Dear Ms. M---:

This is in response to your March 8, 1996 letter to Assistant Chief Counsel Gary J. Jugum regarding the application of tax to your company's operations.

You state:

"H--- - P--- Company contracts with The A--- G--- to gather data regarding customer satisfaction. HP provides A--- with a computer disk of the names and addresses of their customers.

"From this disk, A--- creates a custom letter and address label. We also print a custom survey card and envelop, and imprint a pen with the HP logo to be enclosed in the survey mailing (in order to motivate responses). The printing and assembly is all done in California. A--- mails the survey cards and pen, and personalized letter to HP customers all over the county via the U.S. Mail.

"A--- receives responses from customers, analyzes data, and provides a written report to H--- - P--- summarizing this information.

"Two invoices are sent to HP for this transaction. The first invoice is generated upon the mailing of the survey forms, etc., and bills HP for our material and printing costs (plus a small mark-up) and for the out-going postage. The second invoice is generated when we submit our written report to HP and invoices HP for the balance of the contract amount, plus incoming postage."

You ask a series of questions based on the above facts. For purposes of clarity, we have separately responded to each of your questions below.

“1) Has A--- made a sale of tangible personal property to HP on our first invoice? If so, what is the correct measure of tax - 100% of the invoiced amount or just the percentage associated with the mailings to CA recipients? We believe that the U.S. postage charge on this invoice is not subject to tax.”

California imposes a sales tax on a retailer's gross receipts from the retail sale of tangible personal property in this state unless the sale is specifically exempt from taxation by statute. (Rev. & Tax. Code § 6051.) Taxable gross receipts include all amounts received with respect to the sale, with no deduction for the cost of the materials, service, or expense of the retailer passed on to the customer. (Rev. & Tax. Code § 6012.) Subdivisions (a) and (b) of Regulation 1541 provide that tax applies to the gross receipts from the sale of printed material as well as any services that are part of the sale of these materials regardless of whether the paper or any other materials are furnished by the customer.

A sale of tangible personal property takes place where the property is physically located at the time title is transferred for consideration. (See Rev. & Tax. Code §§ 6006, 6010.5; Cal. U. Com. Code § 2401.) Title to property generally passes no later than the time when the seller completes its responsibilities with respect to physical delivery of the property. (Cal. U. Com. Code § 2401.) In this case, we assume that A--- completes its responsibilities with respect to physical delivery of its printed matter and pens when it places these items in the mail inside this state for delivery to HP's customers. This means that A--- is making a retail sale of property inside this state and tax applies to this transaction unless an exemption otherwise exists.

The only basis for an exemption on the materials mailed by your company is the exemption set forth in Revenue and Taxation Code section 6396. That provision exempts sales in this state from sales tax when goods are shipped outside the state under specific conditions. These conditions are explained in Regulation 1620(a)(3)(B) as follows:

"Sales tax does not apply when the property pursuant to the contract of sale, is required to be shipped and is shipped to a point outside this state by the retailer, by means of:

1. Facilities operated by the retailer, or
2. Delivery by the retailer to a carrier, customs broker or forwarding agent, whether hired by the purchaser or not, for shipment to such out-of-state point. As used herein the term `carrier' means a person or firm regularly engaged in the business of transporting for compensation tangible personal property owned by other persons, and includes both common and contract carriers. The term `forwarding agent' means a person or firm regularly engaged in the business of preparing property for shipment or arranging for its shipment. An individual or firm not otherwise so engaged does not become a `carrier' or `forwarding agent' within

the meaning of this regulation simply by being designated by a purchaser to receive and ship goods to a point outside this state...."

Thus, tax does not apply to A---'s gross receipts from the sale of pens and printed materials that it ships outside this state by US Mail provided A--- actually ships these materials outside the state (or directly sends the goods to a carrier, customs broker or forwarding agent for shipment outside this state) and neither HP nor its agents obtain possession of the property inside this state. Tax does apply, however, to the gross receipts A--- receives from its sales of printed material and pens to HP that are shipped to HP's customers inside this state.

You also ask whether tax applies to A---'s postage charges to HP for the transportation of its pens and printed materials to HP's customers inside this state. Subdivision (a) of Regulation 1628 (copy enclosed) provides that:

"[T]ax does not apply to 'separately stated' charges for transportation of property from the retailer's place or business or other point from which shipment is made 'directly to the purchaser [or purchaser's designee],' provided the transportation is by other than facilities of the retailer, i.e., United States mail, independent contract or common carrier...."

"Transportation charges will be regarded as 'separately stated' only if they are separately set forth in the contract for sale or in a document reflecting that contract, issued contemporaneously with the sale, such as the retailer's invoice. The fact that the transportation charges can be computed from the information contained on the face of the invoice or other document will not suffice as a separate statement. If a separately stated charge is made designated 'postage and handling' or 'shipping and handling', only that portion of the charge which represents actual postage or actual shipment may be excluded from the measure of tax. Such amounts may be excluded from the measure even though such amounts are not affixed to, or noted on, the package. A separately stated charge designated 'handling' or 'handling charge' is not a separate statement of transportation charges. Tax applies to such charges, notwithstanding the fact that postage or shipment charges may or may not be affixed to or noted on the package.

"...."

This means that tax does not apply to A---'s charges for transportation (postage) of the pens and printed materials provided that its charges for transportation are separately set forth in its contract of sale to HP, the charges represent only that amount for shipment (and not "handling") of the property, and A--- ships the material by U.S. mail. You have not, however, provided us with enough information in your letter to determine whether A---'s postage charges to HP meet the foregoing requirements.

You also state that A--- provides HP with a written report summarizing the information collected from the customer survey cards. We assume these reports are specifically created, collected, or compiled at the request of HP such that the transaction is a non-taxable service transaction. (See, e.g., Reg. 1501.) If so, the transfer of a *single* copy of the compiled information on a computer disk or paper is considered incidental to the providing of the service and tax only applies to the sale of such materials to A--- as the seller of the service. (*Id.*) However, if A--- is providing a report that includes information not customized to HP's specific order (i.e., a report A--- previously prepared for a different customer on a custom basis or a report that is furnished to several different customers even if the report was custom prepared for the entire group of customers), the transaction is a sale of tangible personal property and is subject to tax unless an exemption otherwise applies. (Rev. & Tax. Code §§ 6051, 6201.) Information on computer disk or a paper report is generally not considered "custom" when the seller maintains an established price based on the item ordered, the product sold or leased to the customer is generic in nature (i.e., the product is available on a state or county-wide basis), or the product is delivered on a medium generally requiring mass production.

"2) If the answer to question one is 'yes,' can the transaction be invoiced differently to avoid the application of CA tax? For example if A--- did not associate the first invoice with tangible personal property (printed material & pen) and instead identified the invoice as 'milestone' billing, would this language render the tax inapplicable?"

No. Tax applies to the sale of tangible personal property inside this state regardless of how the parties to such a sale may describe the transaction.

"3) How would tax status be affected if we were to invoice HP for the entire transaction on one invoice?"

As set forth above, taxable gross receipts include all amounts received with respect to the sale, with no deduction for the cost of the materials, service, or expense of the retailer passed on to the customer. (Rev. & Tax. Code § 6012.) That is, where a retailer sells both property and a service in a single transaction, tax applies to the entire gross receipts from that sale unless the service portion of the transaction is specifically exempt or otherwise excluded from tax. Conversely, where a retailer provides a service and sells tangible personal property to a single customer pursuant to two separate purchase orders, tax does not apply to the gross receipts from the service provided the retailer is not under an obligation to deliver any tangible personal property as part of a single contract. (See, e.g., Annot. 515.0720 (1/22/58).)

We assume from your letter that A---'s contract with HP provides for separate phases (e.g., data collection phase and report phase) wherein HP has the right to terminate the contract prior to commencement of the next phase without further obligation except for compensation for work completed. That is, we assume that HP is not required to purchase a written report from A--- where, for example, your company does not receive a predetermined number of responses to the customer surveys. Under these facts, tax does not apply to A---'s transfer of its written

report to HP provided the report is separately invoiced and constitutes "custom" research as discussed in our response to question one above.

If you have any further questions, please write again.

Sincerely,

Warren L. Astleford
Staff Counsel

WLA:rz

Enclosure - Reg. 1628

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