



STATE OF CALIFORNIA

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**STATE BOARD OF EQUALIZATION**

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August 10, 1994

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BURTON W. OLIVER  
Executive Director

Ms. N--- S---, Partner  
S--- S--- Studios  
XXX XXth Street  
---, CA XXXXX

Re: **SR -- XX-XXXXXX**

Dear Ms. S---:

This is in reply to your May 23, 1994 letter regarding the application of sales tax to your charges to publishers for your transfers of layouts of printed matter.

You listed 21 items and asked that we inform you whether or not your charges for the items are taxable. As we discussed on the telephone on June 13, 1994, we would not be able to give you a definitive answer as to each charge without further information.

The Sales and Use Tax Law imposes the sales tax on retailers for the privilege of making retail sales of tangible personal property in this state. The tax is measured by the gross receipts of the sale. The law defines the term "gross receipts" to mean the total amount of the sale price, valued in money, whether received in money or otherwise, without any deduction for the cost of the property sold, the cost of materials used, labor or service cost, or any other expense. As we discussed, although a charge solely for consultation is not subject to sales tax, when the consultation is provided as a part of the sale of tangible personal property, the charge for the consultation is includible in the taxable gross receipts of the sale. The same result applies to any other services that are performed as part of the sale.

Sales and Use Tax Regulation 1543, Publishers, subdivision (b)(4), provides a basis for you to exclude from the gross receipts of your sale your charge for author design, and art direction services which you perform before obtaining authorization from your client for you to prepare camera-ready copy or camera-ready art. You may also exclude from the taxable measure your charges for the following production functions if you complete them before you enter into a contract for camera-ready copy or camera-ready art: Manuscript mark-up,

formatting, typesetting, proofreading, production coordination, and production editing. See Regulation 1543, subdivision (b)(3)(B). Definitions of the terms are at subdivision (a)(4) of the regulation. After you obtain the authorization to prepare the camera-ready art or camera-ready copy, tax applies to your total charge for work you perform after obtaining that authorization. See subdivisions (a)(4) and (b)(3) of the Regulation.

With this background information, we believe tax applies as follows to the charges you listed:

The charges you described for consultation, preliminary design supervision, preliminary design, copyedits, coding and preliminary layout are all charges for author or design services which are services that are a part of your sale of the final product, and the charges are includible in the taxable gross receipts of the sale. You may exclude your charge for those services from the measure of tax only if you separately state the charge for the services and you do not transfer title to or possession of layouts other than a brief transfer of possession solely for the purpose of the client's review and approval before you receive authorization to prepare the camera-ready copy or camera-ready art. It is very important for you to document in your records the date you receive authorization to prepare the camera-ready art or camera-ready copy. You note that you furnish "several copies" of laser printouts to your client. You must retrieve all such copies you furnish to the client, because, as noted above, you may only transfer temporary possession of the layouts for the client's review and approval.

Your charges for "file conversion" and "importing files"; that is, converting text files to make the files compatible with your word processing program and importing those text files into your program, are charges for work that is part of typography which is a "production function" as that term is defined at subdivision (a)(4) of Regulation 1543. Your charge for typography is includible in the taxable gross receipts of your sale of the final product unless you complete the function before you contract to furnish the client with your final product. (Sales and Use Tax Reg. 1543, subd. (b)(3)(B).)

We agree with your conclusion that your charges for the following functions you described are includible in your taxable gross receipts. As charges for services that are part of the sale:

**"Production Management:**

Overseeing production which leads to a final product: taxable."

**"Final Composition:**

We follow client's instructions, usually in the form of corrections written on laser proofs, to make a final electronic document in a graphics software program. Taxable."

**"Corrections:**

Corrections or revisions made after the second pass are part of the final composition; they are often charged additional to the agreed upon page rate for page composition. Taxable."

We also agree that your charges for the following are includible in your taxable gross receipts:

**"Lino (Imagesetter) output, film positives or negatives:**

Materials to be used for making printing plates. Taxable."

**"Photography:**

Taking photographs to be used in printed materials: taxable."

**"Graphics Camera:**

Stats, veloxes, halftones, other photographically generated materials to be used in the printing process or in assembling camera ready artwork: taxable."

**"Materials:**

We occasionally are asked to provide framed or mounted artwork, usually copies of printed pieces we have made, for clients. Taxable. Other special materials might include props for photo shoots, which the client ends up owning. Taxable."

When you sell illustrations to your client, tax applies to the entire charge including the part of your charge attributable to "comprehensive renderings" and preliminary sketches unless you follow the criteria specified at subdivision (b)(5) of Regulation 1543 to exclude from the charge separately stated charges for preliminary art. The term "preliminary art" is defined at subdivision (a)(6) of the regulation.

You are correct that sales tax applies to your retail sale of printing. However, there are exemptions from the tax for certain sales of newspapers and periodicals and "printed sales messages." In order for us to give you a definitive answer, we will need a description of the printed matter and how you deliver the products to the recipients.

You asked for the application of tax to your transfers of "electronic design templates." You provided the following description:

"We furnish an electronic file by modem or on disk containing only specifications and layout parameters for documents generated in a specific graphics program. We do no work on the actual project to be printed; the client later may use the design template we furnish for executing projects. This is something like an electronic set of specifications, with the electronic file simply conveying a set of

"styles" for different kinds of material. It might be accompanied by a memo listing the type specifications, and/or a set of laser proofs with dummy text (not the final text) showing how it should look if one used the template to make up pages. It takes the place of what we formerly furnished, which was a pencil sketch accompanied by a type of specification memo. At that time the Board described these design services as nontaxable."

When you create and transfer to a design template in the form of a diskette or other electronic storage media which the client may use as a tool to format data into the correct font and style, your sale of the template embodied on storage media is subject to sales tax. If you furnish the template to the client by modem, your charge is not subject to sales tax, because you have not made a sale of tangible personal property. The reason the Board's staff considered your former product as nontaxable was because the true object of your contract with the client was the performance of a service; that is, the client contracted with you for the written instructions in the type specification memorandum, and your transfer of the pencil sketch was merely incidental to those instructions. By contrast, your transfer of a diskette, which is physically useful as a tool to format text, is subject to sales tax. The true object of the transaction is not your transfer of only information but, rather, the transfer of tangible personal property, (Cf. Sales and Use Tax Reg 1501, Service Enterprises Generally.)

You note that you believe that charges for shipping and deliveries from you to your client are nontaxable. Enclosed is a copy of Sales and Use Tax Regulation 1628, Transportation Charges. Generally, tax does not apply to separately stated charges for transportation of property from your place of business or other point from which you ship the property directly to the purchaser when you deliver the property by other than your facilities; that is, you ship the property by mail, independent contract carrier, or common carrier.

We hope this answers your questions; however, if you need further information, feel free to write again.

Very truly yours,

Ronald L. Dick  
Senior Tax Counsel

RLD:plh

Enclosures: Regs. 1541.5, 1543 1628 and proposed Reg. 1590

cc: Oakland District Administrator - CH