The above-entitled matter came on regularly for hearing on Wednesday, May 14, 1975, in Sacramento, California.

 Appearing for the Petitioner:        Mr. F. D. E---,  
  Mr. F. D. E---, Certified Public Accountant  
  Mrs. G. L. J---, Co-owner  

 Appearing for the Board:             Mr. C. N. Warner,  
  Mr. C. N. Warner, District Principal Auditor  
  Mr. J. Enfield, Auditor  

Protested Item  
(Period 1/1/71 to 8/14/73)  

<table>
<thead>
<tr>
<th>Total Sales Understated</th>
<th>Measure of Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Misinterpretation of the taxpayer’s return for March 1971 led to sales thought to be exempt being netted. Also, clerical errors in 1972 caused an understatement.</td>
<td>$13,804</td>
</tr>
</tbody>
</table>

Resale and Service Reduction Overstated  

B. Combined charges for photo copies, envelopes, inserting and sealing, and mailing deducted as exempt services and sales for resale | 39,533 |

C. Tax-paid purchases of paper and envelopes Resold in connection with B above: | -$6,571 |
Petitioner’s Contentions

A. With respect to the proposed understatement of taxable sales resulting from “misinterpretation of returns filed for 3-71” an amended return was filed and the proper tax paid.

B. The billing service constitutes and exempt service pursuant to Regulation 1501. Furthermore, no tax should be asserted since Petitioner was advised by representatives of the Board at its district office that its service was not subject to tax.

C. This item is dependent upon the outcome of Item B above.

Summary of Petition

Petitioner operated what is described as a “mobile billing service”, under franchise agreement with C--- V--- Inc. The operations were carried on in a van containing the necessary equipment for photocopying, folding and inserting statement billings into envelopes upon which metered postage was placed for mailing. A window envelope and a return envelope were provided by Petitioner. Petitioner also made retail sales of peg board accounting systems.

Petitioner’s customers generally were persons engaged in the medical profession. The billing statements were photocopied from the customer’s accounts receivable ledger card upon which the charges for the month had been entered by an employee of the customer.

Charges for the service were based on the number of statements processed plus the postage for mailing and were made in a lump-sum amount. Petitioner considered these charges nontaxable on the theory that the activity constituted and exempt service.

Tax reimbursement was paid by Petitioner on its purchases of photocopy paper and the envelopes furnished for mailing.

Petitioner filed sales tax returns and remitted the tax applicable to its sales of peg boards and forms. The billing services were claimed as exempt deductions on its returns.

The audit verification procedure resulted in additional measure of tax due to clerical errors in reporting, and the disallowance of the deduction applicable to Petitioner’s charges for photocopying, folding and inserting the billing statements. Charges for postage were allowed as exempt. The audit also has computed a credit for tax-paid purchases resold in connection with the paper and envelopes considered to have been resold.

Since Petitioner’s charges in connection with the “service” performed did not separately state that applicable to folding, sealing and mailing, the total charges with the exception of that applicable to postage was regarded by the audit as taxable in accordance with Regulation 1541.
Analysis and Conclusions

1. **Total Sales Understated**

As a result of Petitioner’s contention the audit staff has reviewed the method by which the auditor determined the understatement of taxable sales. The review revealed that the indicated additional measure under this item was misplaced, in that it should have been included under Item B. The review and recomputation disclosed that the overall measure of the additional tax was essentially correct.

It is directed that the audit staff contact Mr. E--- for the purpose of review and explanation of the revised computations to resolve the auditing problems involved. Any warranted adjustment should be made.

2. **Resale and Service Deduction Overstated**

Petitioner’s contention that its operations constitute an exempt service enterprise cannot be sustained.

Persons engaged in the business of rendering service are consumers, not retailers of the tangible personal property which they use incidentally in rendering the service. If in addition to rendering service they regularly sell tangible personal property to consumers they are retailers with respect to such sales.

In the instance case Petitioner’s activities involve a combination of distinct performances. The production and sale of photocopies of its client’s records and the sales of envelopes, and the rendering of a service consisting of the folding, inserting, sealing, metering and mailing of the photocopy statements.

The object of the contract between the parties cannot be classified as solely for the rendition of a service. Petitioner’s clients also contract for the tangible personal property in the form of photocopies and the envelopes in which they are mailed.

In view of the combined performance contracted for, it is our opinion that the taxability of Petitioner’s activities is controlled by the provisions of Regulation 1541, which provides in pertinent part that tax applies to charges for mimeographing, photostating and similar operations for consumers, regardless of whether or not the paper and other materials are furnished by the consumer.

Tax does not apply to charges for postage or for addressing for the purpose of mailing, folding for the purpose of mailing, enclosing, sealing, preparing for mailing or mailing letters or other printed matters, provided such charges are separately stated on invoices and in the accounting records. Tax applies, however, to charges for envelopes.
Since Petitioner’s charges were billed on a lump-sum basis, the requirement for exemption from the tax has not been met. However, the auditor was able to establish the charges for postage which was quoted to the client as a separate amount and has allowed such postage as exempt from the tax on the basis of postage meter readings.

Petitioner has stated that on three separate occasions advice was obtained from Board of Equalization representatives that its business activities as related to the “billing service” were not subject to the sales tax. Petitioner contends that any erroneous reporting which may have occurred in this respect was the result of reliance on the advice obtained.

Whether the erroneous reporting was due to misinformation or to misunderstood facts is not absolutely clear. No documentary evidence appears from which the cause can be determined since only oral information was obtained. Petitioner’s testimony appears credible; however, even though misinformation may have been given the state is not estopped from collecting the tax which is properly due (Market Street Railway Co. v. State Board of Equalization, 137 Cal. App. 2d 87).

**Recommendation**

Review revised computation of the understatement of total sales (protested Item A above) with Petitioner’s representative. Prepare any warranted adjustment.

No adjustment is recommended to protested Items B and C.

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Joseph Manarolla, Hearing Officer           Date

7/14/75