

**STATE BOARD OF EQUALIZATION**

(916) 445-5550

February 13, 1991

Mr. M--- A---
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--- ---, California XXXXX

Dear Mr A---:

This is in response to your letter dated January 14, 1991. You describe yourself as an industrial design consultant, and you ask whether sales tax applies to your business which you describe as follows:

“As a Design Consultant, companies hire me for my ideas in determining how their products should look, feel and sometimes...function. A large part of what I do pertains to the appearance characteristics and I usually convey my ideas through sketches, renderings or drawings of my ideas. Sometimes however, these methods simply aren't adequate in depicting the true or final color, finish, texture, feel or tactile quality of the concept. I therefore have to resort to using a 3-dimensional study model to accurately and fully convey these qualities.

“Typically, I give my clients the choice of acquiring these studies on their own. But history has proved that it is more efficient for them to have me acquire them, as I have established relationships with local suppliers, usually interface with them during fabrication, and in effect, greatly reduce the burden of paperwork and expense that the client would otherwise bare (sic) in seeking quotes and processing purchase orders. Every time I acquire a study, I pay for it, and also pay sales tax charged by the supplier. I simply coordinate the acquisition as a service to my client, invoicing them for the cost of the study as a reimbursement.

“I do not see the need to charge the client sales tax if I've already paid the tax to the supplier. The State has received their money from the supplier. My idea generation and the communication of my ideas is a service. It is not a product. The use of a 3-D study is merely a form of media required to fully represent my ideas. Some consultants convey their ideas verbally or in writing. I draw and use 3-D studies. In a way, I don't think sales tax should even be charged by the supplier because it is difficult to view the study as a finished product. The mass-produced item that the client eventually will manufacture is where the tax should be assessed. But the suppliers say they are required to charge the tax.

“....

“There are also times when clients will approach me for design ideas for labels, cartons, product specification sheets and such. With requests of this type, I utilize drawings, sketches and comps to show what the printed pieces should look like. I usually provide the client with a ‘mechanical’ which is required by the printer as an outline of the specifications required to manufacture the final printed items. I’ve never charged sales tax for these services.”

You believe that your activities are similar to the service provided by an architect or engineer.* Based upon your description of your business, we disagree. Rather, we believe your business is that of a commercial artist or designer. The application of sales tax to the business of commercial artists and designers is set forth in Regulation 1540, a copy of which is enclosed.

<p>*Note proposed changes to Reg. 1540 (public hearing scheduled for 5/29/02) SPJ 5/13/02.</p>
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The application of sales tax to the sale of mechanicals is covered in the regulation pertaining to the business of printers, Regulation 1541, a copy of which is also enclosed.

You believe that you are providing a service and not a product. Your contract with your client is for the transfer of tangible personal property for consideration. A “sale” under the Sales and Use Tax Law is defined as any transfer of tangible personal property for a consideration. (Rev. & Tax. Code § 6006.) We note that services are almost always necessary in the creation and manufacture of items of tangible personal property which will be sold. Nevertheless, the transfer of that property is a sale for purposes of the Sales and Use Tax Law. Since you are engaged in the business of selling tangible personal property, you are required to hold a seller’s permit. (Rev. & Tax. Code § 6066, Reg. 1699, a copy of which is enclosed.) You should apply for that permit at your local district office of the Board.

A retailer’s gross receipts from the retail sale of tangible personal property in California are subject to sales tax. (Rev. & Tax. Code § 6051.) Although the sales tax is imposed upon the retailer, the retailer may collect sales tax reimbursement (usually itemized on the invoice as “sales tax”) from the purchaser if the contract of sale so provides. (Civ. Code § 1656.1.) You believe that your supplier should not charge you sales tax (reimbursement) because sales tax should be charged on the mass produced item that your client eventually will manufacture. However, a retail sale is defined as a sale of tangible personal property for any purpose other than resale of that actual item in the regular course of business. (Rev. & Tax. Code § 6007.) Thus, sales tax applies to the sale of a machine which is sold for use in manufacturing other items whose sale at retail will also be subject to sales tax since the machine will be used in manufacturing rather than being resold prior to use by the purchaser. In the same manner, sales tax applies to your sale of an item which your client uses in order to manufacture other items whose sale will be subject to sales tax.

You may purchase property that you will resell to your clients prior to any use without paying sales tax reimbursement to your vendor by issuing your vendor a resale certificate in the form described in Regulation 1668, a copy of which is enclosed. As noted above, your sale to your client is subject to sales tax. It appears from your description that your entire charge is subject to sales tax. (See Regs. 1540(c), 1541(f)(5).) If you had paid sales tax reimbursement or use tax to your vendor when purchasing the property, and you resell that property to your client prior to any use, you may take a tax-paid purchases resold deduction as described in Regulation 1701, a copy of which is enclosed. This deduction is taken on line 10 of your Sales and Use Tax Return.

We hope this answers your questions. If you have further questions, feel free to write again.

Sincerely,

David H. Levine
Senior Tax Counsel

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Enclosures: Regulations 1540, 1541, 1668, 1699, 1701