



**STATE BOARD OF EQUALIZATION**

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April 22, 2003

\_\_\_\_\_  
JAMES E. SPEED  
Executive Director

Mr. --- --- ---  
--- and --- ---.  
--- --- ---, Suite ----  
--- ---, California 92101

Re: --- and ---, Inc.  
SR --- --- ---

Dear Mr. ---:

This is to acknowledge receipt of your September 23, 2002 letter addressed to Assistant Chief Counsel Janice Thurston of the State Board of Equalization's Legal Department. Your letter has been assigned to me for reply. I apologize for the delay in responding.

You stated:

“We are requesting a legal letter ruling regarding the revision of regulation 1540.

“Our request is on behalf of many of our Advertising Agency Clients but we will use only one client, --- ---, -----, for our example.

“This letter is directed at the numerous legal letter rulings I have just received back from Jeffrey Graybill, Senior Tax Counsel. In all Jeff's letters he states that if Advertising Agencies purchase TPP for their Clients (acting as an agent) and make a single charge for the TPP that includes a markup, the advertising agency will become the retailer of the TPP and tax will apply to the entire separately stated charge. (subdivision (c) (2) (c) of Reg. 1540)

“Here in lies the problem. Most Advertising Agencies estimate their purchases made on behalf of their Clients and pre-bill their Clients for these purchases. These estimates are sometimes over or under the invoiced price from their vendors depending on overruns, discounts, etc.

“Example: An Advertising Agency contracts with Client to design and then have printed from an outside printer, 100,000 3-color brochures. They work with a few different printers and usually can estimate fairly close to what the bill from the printer will be, including tax. Let's say they estimate this print job will cost \$150,000 plus tax of \$11,625.00, total \$161,625.00. They will pre-bill their Client for the estimated cost plus tax of \$161,625.00. The Client pays the Advertising Agency the \$161,625.00. Then an invoice comes from the printer for printing of \$161,247.88, tax included. Cost of printing is \$-377.12 less than the estimated billed price.

“Note: The printer's paper costs were not as much as estimated thus the price from the printing was less than the [\$161,625.00] billed the Client.

“According to all the Legal Letter Rulings I have just received this would technically create a markup on the single charge to the Client and make the Advertising Agency the retailer for the entire charge to their Client. And since it makes the Advertising Agency the retailer this also could trigger other items to become subject to tax such as separately stated commissions/markups for the acquisition of the print job.

“My two questions are:

“1) Will an estimated amount billed the client over the actual invoiced price from the printer for purchases made, acting as agent of TPP cause the Advertising Agency to become a retailer, thus making the entire estimated charge subject to tax and why?

“2) If in fact the Advertising Agency is deemed to be the retailer in the above scenario, what other charges would now be subject to tax and why?

“3) And if the Advertising Agency is now deemed to be the retailer in the above scenario and most all Advertising Agencies must pre-bill their clients in order to pay their vendors, how will Advertising Agency be able to act as an agent for their Clients?

“In many cases the Client dictates to the Advertising Agency that they will act as an agent for legal and title transfer reasons.

“As this will greatly affect the whole Advertising Agency industry we would greatly appreciate your attention to this important issue. Feel free to contact me with questions.”

You requested a “legal letter ruling.” As we have previously explained, this office does not issue “rulings.” Only the five-member Board issues rulings, and only when dealing with cases pending before it. This letter instead constitutes the opinion of the Legal Department of the Board of Equalization.

You should also note that while you reportedly represent many advertising agencies, this letter only applies to --- and ---, Inc. Any relief that may be available pursuant to Revenue and Taxation Code section 6596 would only apply to that entity.

Discussion:

Subdivision (c)(2)(C) of Regulation 1540 explains:

“When an advertising agency invoices its client for tangible personal property provided by the advertising agency without separately stating the amount paid to the supplier for that property, the advertising agency is the retailer of the tangible personal property to its client. For example, when the advertising agency invoices a single charge to its client for tangible personal property that includes the amount paid to the supplier for the tangible personal property together with a markup, the advertising agency is the retailer of that tangible personal property and tax applies to that separately stated charge. If the advertising agency makes a combined charge to its client that includes the charge for the tangible personal property as well as the charge for any nontaxable services or reproduction rights under subdivision (b), the advertising agency is the retailer of the tangible personal property provided and the measure of tax on the sale of that tangible personal property is calculated as provided in subdivision (b).”

I assume that the advertising agency does not issue a “final” bill to its client until some time after the printer bills the advertising agency. Additionally, I assume the transaction is not reported on a Sales and Use Tax Return by the printer until the time of delivery of the brochures. At the time of delivery of the brochures by the printer, and issuance of the printer's invoice, the advertising agency will be able to avoid the operation of subdivision (c)(2)(C) of Regulation 1540 (invoicing its client without separately stating the amount paid to the vendor, and thereby becoming the retailer of the brochures). It can simply issue a “final” bill, separately stating the amount paid to the printer. Your letter does not state how the advertising agency discloses and/or adjusts the price discrepancy. If it issues a credit with its final bill, separately stating the amount invoiced by the printer, then the printer will be the retailer of the printed material, and the advertising agency will have made the purchase as an agent for its client. Alternatively, if it chooses not to reveal the overcharge, then subdivision (c)(2)(C) will apply to make the

advertising agency the retailer. It is not the fact of the pre-billing that makes the advertising agency the retailer in the transaction, rather, it is the failure of the advertising agency to separately state for its client the amount billed by the vendor. In order to qualify as an agent making purchases on behalf of its client, the advertising agency must disclose the price charged by the vendor. Otherwise, subdivision (c)(2)(C) of Regulation 1540 of the Sales and Use Tax Law deems the advertising agency to be making the sale as a retailer.

I trust the explanation in this letter sufficiently addresses your concerns. If you need further assistance, please write again.

Sincerely,

Jeffrey H. Graybill  
Senior Tax Counsel

JHG/sw

Enclosure: Regulation 1540, Advertising Agencies and Commercial Artists

cc: Ms. Laura Jonoubei, MIC: 50  
Mr. Larry Bergkamp, MIC: 44  
Santa Ana District Administrator (EA)