

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

432.0071.400

APPEALS SECTION

In the Matter of the Petition)
for Redetermination Under the) DECISION AND RECOMMENDATION
Sales and Use Tax Law of:)
)
D--- A--- M--- INC.) No. SR --- XX-XXXXXX-020
)
Petitioner)

The Appeals conference in the above-referenced matter was held by Tax Counsel Steve Ryan on April 10, 19XX, in Santa Ana.

Appearing for Petitioner:

Mr. B--- K---
Chief Financial Officer

Mr. A--- F---
Price Waterhouse

Appearing for the
Sales and Use Tax Department:

Mr. Ed Moore
Tax Auditor

Ms. Angela Vu
Supervising Tax Auditor

Type of Business: Direct mail marketing company

Protested Item

The protested tax liability for the period January 1, 1991 through June 30, 1994, is measured by:

<u>Item</u>	<u>State, Local and County</u>
B. "Printing expenses subject to tax"	\$7,692,913

Petitioner's Contentions

The printed sales message exemption applies.

Summary

Petitioner has operated as a direct mail marketing company which mails materials to others. The last Board audit covered a period which ended on December 31, 1989.

The Board's Sales and Use Tax Department ("Department") established a use tax deficiency against petitioner. This tax is measured by petitioner's ex-tax prices paid to suppliers to purchase mailers pursuant to resale certificates. However, rather than reselling those mailers, petitioner gifted them to the public in mass mailings. The auditor represented that all but one of the requirements of the printed sales message exemption were met by petitioner.

The auditor focuses on the part of petitioner's marketing actions regarding the printed sales message requirement that the mailers have the principal purpose of advertising or promoting goods or services (see Regulation 1541.5(a)(1)). A 2-page sample mailer is attached hereto as exhibit 1. The Department's position is that a substantial portion of each mailer promotes/solicits a contest and the contest prizes through the use of 900 telephone numbers, but not goods or services. Also attached hereto is petitioner's business marketing brochure (exhibit 2). Reference is made to the contents of the two exhibits for the particulars, including the subjects of the 900 telephone number and the discount coupons. The Department represented that as to these contests, petitioner was not paid by the retailers who supplied the discount coupons, but that petitioner received its sole income from its 900 telephone number services.

The Department's Legal Section concedes that petitioner's offer of the 900 telephone number is a service within the meaning of the applicable statute (Revenue and Taxation code section 6379.5) and that this is a close case, but the principal purpose of the mailer is not to promote the 900 number service [a "secondary matter"] or to offer the \$100 discount coupons, but merely petitioner's contest itself which does not constitute goods or services.

We note that two of the three purchase invoice copies in the audit workpapers indicate the requirement that the supplier ship the property to petitioner. We do not know if these invoices are related to the mailers in dispute.

Analysis and Conclusions

Although at first glance solely to the contents of the exhibit 1 mailer it might appear that advertising or promoting goods or services may not be the principal purpose thereof, an understanding of the entire situation in and for which the mailer is used shows that the principal purpose is the advertising and promoting of petitioner's 900 telephone number services. Since the Department's counsel concedes that such 900 telephone services constitute services within the meaning of section 6379.5, the exemption applies to petitioner (with one possible type of exception, *infra*).

The evidence, including the contents of the two exhibits, shows that the bottomline aspect of petitioner's sweepstakes program is for petitioner to make money when people call the 900 telephone number. That is how it makes a profit, and that is the real reason why the program exists. The sweepstakes is just a gimmick to sell the 900 number services. Petitioner uses the sweepstakes scheme: (1) to sell its 900 number services so that it can make money; and (2) to distribute the discount coupons so that its client-retailer-marketers can also make money by having significantly more customers purchase their products or services (while redeeming the discount coupons). Through the scheme itself as well as the highlighted 900 number provisions on the mailer, those printed sales messages directly push the 900 number as the preferred method of response. Thus, although in a manner which is not immediately apparent in form, the principal purpose of petitioner's mailers is to advertise or promote certain services.

The one possible type of exception is any disputed printed matter which was delivered to petitioner. No exemption can then apply to petitioner's cost thereof since the statute requires that the printed sales messages be delivered by the seller, seller's agent, or a mailing house, acting as the agent for the purchaser, through a carrier or the U. S. Postal Service directly to the donee (Rev. & Tax. Code § 6379.5). The Department can file a request of reconsideration if that situation exists.

Recommendations

Grant the petition to delete audit item B.

Steve Ryan, Tax Counsel

December 31, 1996
Date

(w/Exhibits 1 & 2)