STATE BOARD OF EQUALIZATION

January 21, 1970

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Gentlemen:

We have completed our review of your petitions for Redetermination of sales and use taxes.

We have conducted a thorough review of the work descriptions, brochures, billings, and other information made available to this date. We have concluded that the work descriptions provided in your letter of May 9, 1969 should be accepted as representative of the work performed for the periods covered by the deficiency determination.

We understand that the activity described in the first category consists primarily of time surveys of training means, evaluation of existing training programs, and the issuance of oral or written recommendations for improvement or alteration of the programs. Since no substantial element of tangible personal property was produced and transferred to the customer the charges in this category are properly classified as exempt services.

The second category of business activity consists primarily of the creation and delivery of a customized training program and production of the training aids selected for its presentation. Frequently, the text of the training program was embodied on films, slides, tapes, etc. In other instances a type written outline or manuscript of the program was delivered to the customer.

Where the program was delivered on films, tapes, slides, etc., the entire charge would be subject to the tax because the acquisition of tangible property was a true object of the customer's order. While the production of such items may have consisted primarily of the performance of specialized services no deduction may be allowed because the services were rendered in connection with the production of the specialized property. Section 6012 of the Revenue and Taxation Code expressly provides that charges for such services constitute gross receipts from the sale. This interpretation has been approved by the District Court of Appeal in People v. Grazer, 138 Cal. App. 2d 274. No deduction is allowable by reason of the creative nature of the services.

Where the training program was delivered in type written form (as distinguished from reproduced printed material) the charge for the development of the concepts and ideas contained therein would not represent services that were a part of the sale if the program had value independent of the training aids. We believe it is reasonable to conclude that such training programs had independent value. Accordingly, the charges attributable to these services will be excluded from the measure of tax.

The audit report and other information presented does not provide any satisfactory basis for verification of the form in which the actual training program was delivered. For purposes of resolving these deficiency determinations, we have concluded that an allowance should be made for exempt services by reclassifying the transactions for a representative test period on the following basis:

(1) All charges in the first category not clearly related to the production of a tangible property are to be classified as an exempt service.

(2) All production charges in the second category and one-third of the charges for creative services billed in conjunction with the production charge are to be considered to represent gross receipts from the production and sale of training aids except where the invoice description indicates that the creative service is related entirely to the production of a tangible personal property in which case the entire charge is to be included (see invoice number 205, dated 2-28-67 for an example of such a billing).

We have selected the period October 1, 1966 to March 31, 1967 as the test period because our review of the invoice descriptions indicates that the classification of the charges into the various categories was reasonably accurate for this period. A reclassification of the charges using the standard prescribed above indicates that the protested measure of tax should be reduced from $81,332 to $33,582 (see attached schedule). We have directed that the tax be recomputed on this basis.

In the event you do not agree with our conclusions and the further action recommended you may have the petitions considered by the full Board at an oral hearing. If you desire to have such a hearing a written request for hearing should be forwarded to this office within 30 days of the date of this letter.

Very truly yours,

W. E. Burkett
Tax Counsel

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