



STATE BOARD OF EQUALIZATION

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February 14, 1995

BURTON W. OLIVER
Executive Director

Mr. J--- -. V---, esq.
---, --- & ---
Attorneys at Law
Suite XXX --- Square
XXXXX East --- Street
---, CA XXXXX

Re: S--- A---, Inc.
Account No. SR -- XX-XXXXXX

Dear Mr. V---:

This is in reply to your October 20, 1994 letter regarding the application of sales tax to your client's charges for preliminary art.

You provided us with the following statement which your client proposes to incorporate into its purchase orders relating to preliminary art:

"The roughs, visualizations, layouts and/or comprehensives which The S--- A--- Group will prepare according to this purchase order will be for the purpose of demonstrating the ideas of The S--- A--- Group. These ideas are being presented to the client in order to gain its acceptance of our ideas before entering into a contract for finished art. If the client determines that it wishes The S--- A--- Group to prepare finished art, such work will be the subject of a separate purchase order.

"The title to all ideas prepared pursuant to this purchase order remains the property of The S--- A--- Group. These roughs, visualizations, layouts and/or comprehensives must be returned to The S--- A--- Group after the client has had

sufficient time to review them, or the client may dispose of them if directed to do so by The S--- A--- Group."

You ask for our confirmation that, if your client incorporates the proposed statement into its purchase order forms for preliminary art and your client requires separate purchase orders for the finished art, then sales tax would not apply to the client's charges for tangible personal property transferred to its customers pursuant to the purchase order for preliminary art.

As you know, the application of sales tax to charges for preliminary art is provided at subdivision (b)(4)(A) of Sales and Use Tax Regulation 1540, Advertising Agencies, Commercial Artists and Designers:

"Preliminary art' means roughs, visualizations, layouts and comprehensives, title to which does not pass to the client but which is prepared by an advertising agency, commercial artist or designer solely for the purpose of demonstrating an idea or message for acceptance by the client before a contract is entered into or before approval is given for preparation of finished art to be furnished by the agency, commercial artist or designer to its client. Tax does not apply to separate charges for preliminary art except where the preliminary art becomes physically incorporated into the finished art, as, for example, when the finished art is made by inking directly over a pencil sketch or drawing, or the approved layout is used as camera copy for reproduction. If the preliminary art is prepared on data processing equipment, the advertising agency, commercial artist, or designer shall produce a hard copy of each of the roughs, visualizations, layouts or comprehensives presented for client approval and retain such copies in accordance with subdivision (d) of Regulation 1698.

"The charge for preliminary art must be billed separately to the client, either on a separate billing or separately charged for on the billing for the finished art. It must be clearly identified on the billing as preliminary art. Proof of ordering or producing the preliminary art, prior to the date of the contract or approval for finished art, shall be evidence by purchase orders of the buyer, or by work orders or other records of the agency, commercial artist or designer. No other proof shall be required."

Essential to the nontaxability of preliminary art is that the agency does not pass title to the preliminary art to the customer. Under the language of the proposed statement, if S--- does not require the client to return the layouts, S--- has sold them to the client, and tax applies to the charge for the sketches or layouts.

Therefore, we suggest you delete the last clause of the last sentence of the proposed statement. When S--- provides preliminary art to clients, it should retrieve the artwork after the client reviews it.

We hope this information answers your questions; however, if you need further information, feel free to write again.

Very truly yours,

Ronald L. Dick
Senior Staff Counsel

RLD:sr

cc: --- --- District Administrator - - -