



STATE BOARD OF EQUALIZATION

LEGAL DIVISION - MIC 82
450 N STREET, SACRAMENTO, CALIFORNIA
(P.O. BOX 942879, SACRAMENTO, CALIFORNIA 94279-0082)

Telephone No.: (916) 445-6450
Fax No: (916) 323-3387

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June 20, 1995

Mr. T--- S---
M--- M---
XXX --- ---, Suite XXX
--- ---, CA XXXXX

SR -- XX-XXXXXX

Dear Mr. S---:

This is in reply to your March 20, 1995 letter regarding the application of sales tax to your charges for multi-media presentations.

You note you and your wife started a new business on January 1, 1995. You provide to your clients video production, art direction, graphic design, custom computer programming, and multi-media productions. Your company will produce interactive corporate training and sales presentations that are custom computer programs you will deliver to customers on computer disks or CD ROMs. You asked whether you should charge your client sales tax on your charge for the presentations.

The sales tax is imposed upon retailers at the applicable rate of the gross receipts from the retailers' retail sales of tangible personal property in this state. Since the sales tax on your sales is imposed directly upon you as the retailer, whether or not you collect reimbursement from your customer is a matter of contract between you and the customer.

We agree with your conclusion that, although the interactive presentation you provide to your client has some characteristics common to motion pictures, your transfers of them are not covered by Sales and Use Regulation 1529, Motion Pictures. Since interactive presentations are not produced for display, we believe they are not qualified motion pictures as defined in Regulation 1529 at subdivision (b)(1). However, we believe that the interactive presentations

you produce to run on automatic data processing equipment qualify as computer programs. Whether or not the interactive presentations you transfer to your clients qualify as custom computer programs depends upon further facts. Revenue and Taxation Code 6010.9 excludes from the respective definitions of “sale” and “purchase” the transfer of a custom computer program:

“‘Sale’ and ‘purchase,’ for the purposes of this part, do not include the design, development, writing, translation, fabrication, lease, or transfer for a consideration of title or possession, of a custom computer program, other than a basic operational program (as defined in Section 995.2), either in the form of written procedures or in the form of storage media on which, or in which, the program is recorded, or any required documentation or manuals designed to facilitate the use of the custom computer program so transferred. . . .”

If you completely design and transfer the interactive presentation rather than modify a prewritten program, tax does not apply to your charge. If you modify an existing program, tax applies to your charge to your client for the presentation; however, tax does not apply to your separately stated charge for modification you made to the program for the customer. Further, if you modify an existing program and do not separately state your charges for custom modification, tax applies to your entire charge to the customer unless your modification is so significant that the new program qualifies as a custom program based on the following criteria:

1. If you previously marketed the prewritten program, the new program qualifies as a custom program if your price for the prewritten program is 50 percent or less than your price for the new program.
2. If you have not previously marketed the prewritten program, the new program qualifies as a custom program if your records show your charge for the custom modifications was more than 50 percent of your contract price to the customer. (Sales and Use Tax Reg. 1502, subd. (f)(2)(B).)

You go on to note that, when you create a multi-media presentation, you may hire an artist to create a digital illustration or animation specifically for your particular presentation. When the artist completes the illustration or animation, you copy it and incorporate the images into the presentation you transfer to your client. You asked whether sales tax applies to the artist’s charge to you.

We assume the artist transfers the illustration or animation to you on a computer disk. In such case, the artist makes a transfer of title to, or possession of, tangible personal property for a consideration, and the transfer is a retail sale subject to sales tax. You may not give the artist a resale certificate, because you do not sell the artwork to your client. Rather, you use it to copy the images into the presentation. The sale of the artwork to you for your use and your sale of a

presentation which may display a reproduction of the image, are two separate and distinct transactions.

Finally, you note other companies will hire your company to design and create digital artwork. You believe that, if you create the artwork for final use in a video or film, under Sales and Use Tax Regulation 1529, Motion Pictures, tax does not apply to your charge. You believe that, on the other hand, if you create the work for final use in printed materials, tax applies to your charge under Sales and Use Tax Regulation 1540, Advertising Agencies, Commercial Artists and Designers.

When you create digital artwork and transfer it to a person to use in producing a video or motion picture film which qualifies as a "qualified motion picture," you perform qualified production services as defined at subdivision (b)(2) of Regulation 1529. Tax does not apply to your transfer of the artwork. (Reg. 1529, subd. (b)(1)(B).) Rather, you are the consumer of property, such as a diskette, you transfer to your client. Tax applies to the sale of the property to you, or tax applies to your use of the property. If you have purchased the property under a resale certificate, you should report and pay use tax on your use of the property by reporting your cost of the property on line 2 of your sales and use tax return.

You are correct that, when you transfer the artwork to a person to use to make printed materials, tax applies to your charge for the artwork.

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

Very truly yours,

Ronald L. Dick
Supervising Staff Counsel

RLD:sr

cc: --- --- District Administrator