

M e m o r a n d u m**120.2788**

To: J. E. Warner
Out-of-State - Auditing

Date: May 22, 1984

From: John Abbott
Tax Counsel

Subject: F--- D--- R---, Inc. – SS OHA XX-XXXXXX
Data processing – microfiche copies

This is in reply to your memorandum of March 22, 1984 to Legal asking for a legal opinion on certain charges made by F--- D--- to its customers. The charges are numbered 10, 11, and 12 on the memo from the Chicago office to Out-of-State auditing dated March 20, 1984 as follows:

These following charges are also made and their tax status under Regulation 1502 is requested.

10. Microfiche Original and
Microfiche Duplicates

Taxpayer furnishes customer a tabulated listing daily of the output of processing information. This is included in the exempt processing fees.

In addition customer contracts for microfiche copies (and duplicates of some) of these tabulated listings. The process is that the microfiche is sent to the customer about four days after the tabulated listing – it is prepared by an outside firm from the taped data sent to them.

Regulation 1502(d)(5) paragraph 5 – wording is “instead” not in addition to.

Do these microfiche charges fall under Regulation 1502(d)(4)?

11. Warning Notice Distribution

Example – [service bureau] distributes lists of bad card numbers to merchants (hard copy). [service bureau] bills charges for this to F--- D--- -R--- Inc. FDR bills on to the customers with a mark-up.

12. Postmailers

As part of the embossing work there is often a charge for a notice sent a few days after the credit cards are mailed to individual cardholders. It is to be returned if no card has been received.

You also helpfully attached the legal section's previous opinion memorandum on F--- D---, from Richard H. Ochsner to Out-of-State dated August 3, 1981. Mr. Ochsner's memorandum covered other types of charges then made by F--- D--- [FDR] and summarized the general nature of F--- D---'s business operations as follows:

FDR contracts with banks and airlines to process their charge card transactions.... FDR maintains computer master files on the client's customer charge accounts and, in the case of [service bureau] and [service bureau] systems for banks, on the participating merchant accounts. FDR receives charge accounts sales documents or tapes reflecting the transactions and enters same in its computer system....FDR produces and mails out customer and merchant charge account statements. It also provides embossing services using plastic supplied by, or purchased from the account of, the client to produce and imprint the plastic charge cards and merchant plates. FDR provides the printed card carrier with envelope and mails the card to the cardholder.

Our conclusions regarding F--- D---'s questioned charges are as follows:

10. Microfiche originals and microfiche duplicates. The issue you raise concerns Regulation 1502(d)(5), which states in part:

Where a service bureau enters into a contract for the processing of customer-furnished information...and the output is in part or in whole transferred to the customer in tabulated listing or similar human readable form, the true object of the contract is regarded to be the rendition of a service....

* * *

Where a service bureau enters into a contract to process customer-furnished information, tax will not apply even though the computer output media may be microfilm or photorecording paper, instead of a tabulated listing....

The Chicago office points out that F--- D--- is preparing these microfiche originals and duplicates in addition to, rather than instead of, the tabulated listing, and therefore asks whether Regulation 1502(d)(4) applies instead. As relevant, Regulation 1502(d)(4) states:

Tax applies to charges for microfilming or photorecording except, as provided in paragraph (d)(5), where the microfilming or photorecording is done under a contract for the processing of customer-furnished information.

Our opinion is that tax applies to the charges for microfiche, but our conclusion is based not on subsection (d)(4), but instead on subsection (d)(5)(A), which states in part:

Where a service bureau has entered into a contract which is regarded as a service contract under this paragraph (d)(5) and the service bureau, pursuant to the contract, transfers to its customer...(2) inventory control cards for use by the customer, membership cards for distribution by the customer, labels (other than address labels) or similar items for use, tax applies to the charges made for such items.

We consider that subsection (d)(4) cannot apply because the contract between F--- D--- and its customers is unquestionably for the processing of customer-furnished information. And the phrase "instead of" rules out a conclusion that the above-quoted provisions of subsection (d)(5) could apply. We consider that this provision of subsection (d)(5) merely means that a service bureau's customer could elect to receive the service bureau's output in microfiche form, instead of tabulated listing form, without changing the essential characterization of the contract as a service transaction.

We consider that subsection (d)(5)(A)(2) renders these charges taxable because the microfiche originals and duplicates are "similar items for use" by the customer; like inventory control cards, the customer has a use for the microfiche quite apart from a mere record of the service bureau's output.

11. Warning notice distribution. We conclude these lists of bad card numbers are either taxable as additional copies of records or tabulations, pursuant to Regulation 1502(d)(5)(B), or taxable as printed matter under Code section 6006(f), depending upon what facts apply.

12. Postmailers. Here Regulation 1504(b) and (c) applies. F--- D---'s charges for the notices sent to cardholders are for the sale of printed matter and are taxable. Services rendered in the preparing of material for mailing are, however, nontaxable. The charges for the printed matter should be separately stated from the charges for mailing services.

JA:ss