175.0140

STATE OF CALIFORNIA

BOARD OF EQUALIZATION

In the Matter of the Petition for Redetermination Under the Sales and Use Tax Law of:	)	DECISION AND RECOMMENDATION
REDACTED TEXT	)	No. REDACTED TEXT
Taxpayer	)	

The preliminary hearing on the above taxpayer's petition for redetermination was scheduled to be held on July 21, 1987, in Sacramento, California.

On July 17, 1987, petitioner's representative called to inform the hearing officer that REDACTED TEXT will not be pursuing this matter further. This report will be prepared from information available in the Board's files.

Protested Items

Petitioner has filed a written petition for redetermination dated April 8, 1985 which contains written arguments and authority for its position. The protested tax liability for the period 4-1-82 through 3-31-84 is measured by:

	Item	State, Local and County
B.	Sales of premiums not reported.	$113,412

Contentions of Petitioner

Petitioner contends that it is not a retailer of the premiums for the reasons set forth in a hearing report dated March 18, 1965 covering a protest of similar transactions.

Summary of Petition

Petitioner corporation is a well-known manufacturer of breakfast cereals. It maintains a manufacturing plant in San Leandro. All cereals are sold for resale to its wholly-owned subsidiary REDACTED TEXT.

In addition to cereal, petitioner also sells premium items that it advertises on its cereal boxes. These premiums are shipped through mailing houses usually from out-of-state locations to California customers. Petitioner reports sales of those premiums which it owns. It does not report sales of premiums which are not owned by petitioner.

A letter in the file dated August 10, 1978 from Mr. Lynn Thompson, Supervising Auditor of the Board's Chicago Office, addressed to REDACTED TEXT, Manager of Tax Compliance for petitioner corporation is to the effect that petitioner's claim for refund would be allowed for periods prior to the date of the letter but petitioner was put on notice that the prior ruling issued by the hearing officer to REDACTED TEXT on this matter was in error. The letter also states that it is to advise the petitioner that unless the advertising clearly identifies the person for whom it is performed, the tax will be asserted against REDACTED TEXT in future periods.

The advertising in reference to the premium sales at issue here were found not to clearly identify the entity for whom the advertising was being performed. The auditor, therefore, concluded that under the "front man concept" tax would be due from REDACTED TEXT. The measure of the sales is $113,412, the amount at issue here. Although REDACTED TEXT has not specifically stated that it now agrees with the Board's determination, it has decided not to pursue the matter further.

Analysis and Conclusions

Tax counsel has previously held that where a cereal manufacture contracted with a third party to supply the premium items and take care of the handling and mailing of the premiums to the customers and did not specifically hold out that it was selling the premium items, the cereal manufacturer was not a retailer responsible for collecting use tax and premium sales. (Sales and Use Tax Annotations 175.0140 and 280.0220 (4/1/65). We believe, however, that where petitioner does not clearly identify the retailer making the sale ~~or requires proof(s) of purchase of its product(s) as at least one condition for receiving the premium~~, petitioner is regarded as holding out that it is the retailer.

Petitioner refers to these transactions at issue as no guaranteed quantity (NGQ's). These are premiums that petitioner agrees to advertise on its ready-to-eat cereal packaging for an outside supplier of premiums. The supplier: 1) Procures the premium; 2) handles mailing of the premiums; 3) handles collection of funds; 4) pays petitioner a commission on a per sale basis; 5) maintains an adequate supply of premiums; 6) handles any complaints; 7) maintains certain quality standards.

Petitioner then agrees to advertise the product on specific cereal packaging for an agreed length of time. The premiums are advertised on the boxes as being available to the customer for an agreed price plus an agreed number of proofs of purchase for specific cereals sold under petitioner's brand names.

Normally, orders from customers are addressed first referencing the special offer (i.e., jump ropes, space weights) and then to a post office box at some location in the United States. The special offers are invariably described as offers made by petitioner to its customers and any reasonable person would interpret it as being just that, an offer by to its customers.

It is our conclusion that petitioner is holding itself out as the retailer to its customers (chiefly by product identification) and, therefore, is liable for the tax on the general law principle that one who fails to disclose his purported agency may be held liable as if he were the principal. If petitioner clearly identifies in its advertising for whom the advertising is being performed ~~and does not require any proof or proofs of purchase of petitioner's product to secure the premium advertised~~ so that it is clear to the customer that petitioner is merely providing advertising for an identified out-of-state company, we would be prepared to regard such circumstances to be the equivalent of advertising performed by newspapers or other advertising media. In such case, we would not regard petitioner as being the retailer responsible for the tax under Revenue and Taxation Code Section 6203.

This additional requirement regarding proof of purchase is to be deleted from the revised annotation as necessary – DJH 10/6/88

Recommendation

It is recommended that the matter be redetermined without adjustment.

7-21-87
John D. Albu, Hearing Officer Date

REVIEWED FOR AUDIT:

William D. Dunn, Principal Tax Auditor 8-5-87
Date

Proposed Replacement for Annotation 175.0140 and 280.0220

A cereal manufacturer advertises on its cereal boxes that premiums (e.g., jump ropes, space weights) may be purchased for an agreed price, plus proof of purchase (box tops) of the cereal. The cereal manufacturer contracts with the supplier of the premiums that the supplier will (1) purchase the premiums; (2) handle the orders; (3) mail the premiums; (4) collect the price; (5) pay the cereal manufacturer a commission on a per sale basis; (6) handle complaints; and (7) maintain premium quality standards. Orders are addressed by reference to the premium offer (e.g., jump rope offer, space weights offer, etc.) at a post office box. The advertising describes the premium offer as made by the cereal manufacturer. The advertising does not identify the supplier of the premiums.

Given such facts, the cereal manufacturer is holding itself out to customers as the retailer of the premiums (chiefly by product identification) and is liable for the sales tax, or has a duty to collect use tax if nexus with California is present. For the cereal manufacturer to avoid the sales tax or use tax collection duty, the advertising on the cereal box must clearly identify the premium supplier for whom the advertising is performed ~~and must not require any proof of purchase of cereal~~ so that it is clear to the customers that the cereal manufacturer is merely providing advertising for an identified premium retailer.

John Albu

July 21, 1987