

M e m o r a n d u m**430.0146.250**

To: Mr. Morris Verna, Jr.
San Francisco – Audit

Date: October 31, 1989

From: David H. Levine
Tax Counsel

Subject: X-----

This is in response to your memorandum dated September 20, 1989 regarding the application of sales tax in the following situation:

X----- prepares items for mailing for such clients as X----- and X-----
----- . Typically all material (looseleaf sheets, tab dividers, binders, folders, fibreboard kit
containers, etc.) are furnished by the clients. X----- puts together these various
separate items, usually in some desired order, to create a completed training kit,
promotion kit, sales folder, loan application folder, product binder, etc. Once these items
are assembled, they are then prepared for mailing to various client locations. In some
cases, X----- forwards the completed items to another warehouse/mailer of the
client for final shipping.

X----- usually makes a separate charge for shipping/ mailing. It also has various
charges for making up the various kits, folders, etc. certain materials of X-----, if
any, are usually charged as a separate line item to the client. Some examples of various
invoices are enclosed for reference.”

Initially, I assume that the exemption provided by Revenue and Taxation Code Section
6379.5 and explained in Regulation 1541.5 does not apply to these transactions. I also assume
sales of tangible personal property by X----- are not otherwise exempt (e.g., the
container exemption does not apply) or for resale. Finally, I assume that all items about which
you inquire with respect to mailing services are printed matter. Only the mailing of printed
matter comes within the provisions of Regulations 1504(b) and 1541(c). Otherwise, such
activities are services part of the sale and are subject to tax unless separately stated charges for
transportation. (Rev. & Tax. Code §§ 6011, 6012.)

Regulations 1504 and 1541, as well as annotations you noted, 340.0140 (9/1/66), 430.0060 (6/1/65), and 435.1160 (12/5/58), are applicable to these transactions. Subdivision (b) of Regulation 1504 and subdivision (c) of Regulation 1541 discuss the activities regarded as nontaxable mailing services. Annotation 340.0140 explains that if a person's activities would otherwise be regarded as nontaxable mailing services, those activities will not be regarded as sales of tangible personal property even if that person does not perform the actual mailing but rather transfers the items to another person for mailing. Thus, X-----'s transfer of items it prepares to another person for mailing does not alter the analysis. If the activities would have been regarded as nontaxable mailing services had X----- performed the actual mailing, the activities will still be regarded as nontaxable mailing services even if another person performs the actual mailing.

Annotation 430.0060 distinguishes between mere collating of diverse advertising materials preparatory to mailing (nontaxable) or collating which is a step in the fabrication of an end product (taxable). For example, the collating of a number of unrelated pages into a certain order followed by stapling would not be taxable fabrication if the stapling was merely preparatory to mailing and the attached pages did not form a distinct end product. If, on the other hand, the pages were consecutively numbered, this is a strong indication that the attached pages then form a distinct end product. Methods of binding such as with a book or with plastic strips (unfortunately, I cannot remember this method's technical name, but a strip is placed on each side of the pages and are attached to each other through the pages) would be conclusive evidence that an end product has been created. It seems that insertion of pages into binders would always, or almost always, be regarded as the creation of an end product. Examples are our Business Taxes Law Guide binders. Even items that are not attached may be regarded as creating an end product. For example, insertion of unattached pages into a folder to form a loan application folder would likely be regarded as the creation of an end product since the pages are all related and necessary to a specific purpose, applying for a loan. When considering a question, it would be useful to determine whether the item(s) to be mailed is commonly created in substantially the same form for delivery in person (e.g., a loan application folder would usually be identical whether mailed to the applicant or retained by the bank for delivery in person with no envelope). If so, an end product has probably been created.

X----- charges for creating an end product are subject to sales tax, even if all tangible personal property is furnished by the purchaser. (Rev. & Tax. Code §§ 6006(b), 6012, 6051.) However, even if it is the seller of the printed matter to be mailed, its charges for mailing services described in Regulations 1504(b) and 1541(c) are not subject to tax and it is the consumer of any items it uses to perform such services. Address labels are examples of such consumables, but X----- is the retailer of items such as envelopes and other containers it provides or fabricates. (See Reg. 1541(c).)

In answer to your specific question, an allocation should be made between X-----'s charge for sales of tangible personal property and its charge for nontaxable mailing services. Although the invoices you have provided us indicate that X----- has acted as a seller of the invoiced items, we cannot make definitive conclusions based on those invoices. We hope this discussion is sufficient to assist you in completing your audit. If not, or if you have further questions, feel free to write again.

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Bc: Mr. Donald J. Hennessy
Mr. E. L. Sorensen, Jr.