

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

In the Matter of the Petition for)	
Redetermination Under the Sales)	DECISION AND RECOMMENDATION
and Use Tax Law)	
)	
REDACTED TEXT)	No. REDACTED TEXT
)	
<u>Petitioner</u>)	

The above-entitled matter came on regularly for hearing on Tuesday, October 6, 1981, in Sacramento, California before Susan M. Wengel, Hearing Officer.

Appearing for Petitioner: REDACTED TEXT

Appearing for the Board: REDACTED TEXT
Tax Auditor

Protested Item

The petitioner has filed a petition for redetermination of a tax deficiency determination issued on July 27, 1981, for the period April 1, 1978 through June 30, 1978. The protest involves tax determined on the following audit item:

Taxable Sales Understated:

A.	Microfilm billing services to medical patients	\$REDACTED TEXT
B.	Tax-paid microfilm resold	-REDACTED TEXT
	TOTAL	\$REDACTED TEXT

Contentions of Petitioner

The microfilm billing of doctor's patients is strictly a service and is not taxable.

Summary of Petition

The petitioner is an individual who, operating as a sole proprietor, makes sales of pegboard accounting systems and microfilm billing services to doctors. The petitioner began his operations in June of 1976. This is his first audit.

The audit staff found that the microfilm billing activities were sales which were subject to tax and a deficiency was assessed. A credit was given for microfilm purchased taxpaid by the petitioner.

The petitioner contends that this is merely a service and is not subject to tax. In support of this position, the petitioner contends that:

1. The true object of the contract is the taking of the pictures as this relieves the doctor's staff from having to leave their regular duties and prepare the bills.
2. The tax was never collected.
3. Although they acknowledge that the process is taxable if the processing is done in California, they contend that their situation is different as the processing is done out of state.
4. They never give the doctor any tangible personal property.

Analysis and Conclusion

MICROFILM BILLING SERVICES

Revenue and Taxation Code §6006 defines a "sale" to include any transfer of title or possession of tangible personal property for a consideration. The gross receipts, or the measure of tax, is defined to mean the total amount of the sale including any services which are a part of the sale. (Revenue and Taxation Code §6012(a) & (b)(1).)

Sales and Use Tax Regulation 1501 provides in part that:

"Persons engaged in the business of rendering service are consumers, not retailers, of the tangible personal property which they use incidentally in rendering the service. Tax, accordingly, applies to the sale of the property to them. If in addition to rendering service they regularly sell tangible personal property to consumers, they are retailers with respect to such sales and they must obtain permits, file returns and remit tax measured by such sales. If their purchases of tangible personal property are predominantly for consumption rather than for resale, they should not give resale certificates covering such purchases but should follow the procedure prescribed in the regulation governing 'Tax-Paid Purchases Resold'.

"The basic distinction in determining whether a particular transaction involves a sale of tangible personal property or the transfer of tangible personal property incidental to the performance of a service is one of the true object of the contract; that is, is the real object sought by the buyer the service per se or the property produced by the service. If the true object of the contract is the service per se, the transaction is not subject to tax even though some tangible personal property is transferred..."

In the present situation the doctors are contracting with the petitioner because they want their patients to receive a bill and an addressed return envelope without having to prepare and mail the bills themselves. Although the petitioner must perform some services for the doctors, the doctors are not paying the petitioner a specific amount per file merely to have the petitioner come in to their offices and take pictures of their ledgers. The true object of the contract is to have the petitioner provide their patients with a bill and an envelope so that they in turn will be paid by their patients. The transfer of the bills and the envelopes to third persons designated by the purchaser/doctor is a transfer of tangible personal property for a consideration. The fact that the bills and envelopes are not delivered directly to the doctor, but rather to persons designated by them, does not mean that the petitioner has not transferred title or possession to the doctor/purchaser. It is concluded that the true object of the contract was the transfer of property (bills and envelopes) produced by the service. Regulation 1501 provides that:

“When a transaction is regarded as a sale of tangible personal property, tax applies to the gross receipts from the furnishing thereof, without any deduction on account of work, labor, skill, thought, time spent, or other expense of producing the property.”

The entire amount of the sale, therefore, was properly included in the measure of tax.

TAX-PAID MICROFILM RESOLD

In cases similar to the facts in this petition, the Board, while finding the sales tax to be applicable, has allowed a tax-paid purchases deduction for such items as copy paper and envelopes purchased. In the present situation, the paper and envelopes are purchased by the petitioner from an out-of-state firm. There is no indication that any tax was paid to this firm for these items. The Petitioner did, however, purchase film to be used by them in photographing the ledgers. The audit staff allowed the petitioner a tax-paid purchases deduction for all film which was purchased tax-paid. We would conclude that this deduction is not warranted.

Sales and Use Tax Regulation 1525(a) provides:

"Tax applies to the sale of tangible personal property to persons who purchase it for the purpose of use in manufacturing, producing or processing tangible personal property and not for the purpose of physically incorporating it into the manufactured article to be sold. Examples of such property are machinery, tools, furniture, office equipment, and chemicals used as catalysts or otherwise to produce a chemical or physical reaction such as the production of heat or the removal of impurities."

Unlike paper and envelopes which are sold to the doctors, the film is merely used in processing or producing the bills and is not resold. It is not incorporated into the finished product. The use of the film was, therefore, a taxable use and no tax-paid purchases resold can be allowed.

It is noted that Revenue and Taxation Code §6563 provides that the amount of a determination may be increased if the increase is asserted prior to an oral hearing before the elected Board members. (Revenue and Taxation Code §6562.)

Recommendation

It is recommended that the tax-paid microfilm resold credit of \$REDACTED TEXT be deleted and that the tax be redetermined on \$REDACTED TEXT. Adjustment to be made by the Petition Unit.

Susan M. Wengel, Hearing Officer

October 20, 1981
Date

REVIEWED FOR AUDIT:

Principal Tax Auditor

October 28, 1981
Date