

**STATE OF NORTH CAROLINA**

**BEFORE THE**

**COUNTY OF WAKE**

**SECRETARY OF REVENUE**

**IN THE MATTER OF:**

The Proposed Assessment of Sales and Use )  
 Tax for the period July 1, 2002 through )  
 December 31, 2002, by the Secretary of )  
 Revenue )  
 )  
 vs. )  
 )  
 [Direct Mail Marketing Firm] )  
 D/B/A [Magazine] )

**FINAL DECISION**  
 Docket No. 2004-220

This matter was heard before the Assistant Secretary of Revenue for Administrative Tax Hearings, Eugene J. Cella, in the City of Raleigh, on August 5, 2004, upon application for hearing by the Taxpayer wherein it protested the assessment of tax, penalty, and interest for the period July 1, 2002 through December 31, 2002. The hearing was held by the Assistant Secretary pursuant to the provisions of G.S. 105-260.1. The Taxpayer was represented by [attorney], Counsel for the Taxpayer, and [officer of corporation], President of the Corporation. The Sales and Use Tax Division was represented by William C. Shelton, Administration Officer, and Amy A. McLemore, Administration Officer.

Pursuant to G.S. 105-241.1, the Department mailed a Notice of Sales & Use Tax Assessment to the Taxpayer on February 26, 2003. The Taxpayer objected to the assessment in a letter dated March 11, 2003 and timely requested a hearing.

**ISSUES**

The issues to be decided are as follows:

- (1) Are the fees the Taxpayer paid to its out-of-state printer for the printing of advertising circulars subject to use tax?
- (2) Are the fees the Taxpayer paid to its out-of-state printer for delivery of the advertising circulars via the United States Postal Service to recipients in this State subject to use tax?

## EVIDENCE

The following items were introduced into evidence by the Department:

- (1) Memorandum dated May 16, 2001 from the Secretary of Revenue to the Assistant Secretary of Administrative Tax Hearings, designated as Exhibit E-1.
- (2) Copy of audit report dated February 14, 2003, covering the period July 1, 2002 through December 31, 2002, designated as Exhibit E-2.
- (3) Copy of Notice of Sales and Use Tax Assessment dated February 26, 2003, designated as Exhibit E-3.
- (4) Copy of [Magazine], an advertising circular published by the Taxpayer, designated as Exhibit E-4.
- (5) Letter dated March 11, 2003, from the Taxpayer to the Department, designated as Exhibit E-5.
- (6) Letter dated March 28, 2003, from the Sales and Use Tax Division to the Taxpayer, designated as Exhibit E-6.
- (7) Letter dated April 17, 2003, from the Taxpayer's representative, an attorney, to the Sales and Use Tax Division, designated as Exhibit E-7.
- (8) Letter dated May 19, 2003, from the Sales and Use Tax Division to the Taxpayer's representative, designated Exhibit E-8.
- (9) Letter dated May 22, 2003, from the Taxpayer's representative to the Sales and Use Tax Division, designated Exhibit E-9.
- (10) Letter dated June 30, 2003, from the Sales and Use Tax Division to the Taxpayer's representative, designated Exhibit E-10.
- (11) Letter dated July 25, 2003, from the Sales and Use Tax Division to the Taxpayer's representative, designated Exhibit E-11.
- (12) Letter dated August 5, 2003, from the Taxpayer's representative to the Sales and Use Tax Division, designated Exhibit E-12.
- (13) Letter dated August 22, 2003, from the Sales and Use Tax Division to the Taxpayer's representative, designated Exhibit E-13.

- (14) Letter dated September 10, 2003, from the Taxpayer's representative to the Sales and Use Tax Division, designated Exhibit E-14.
- (15) Copy of Section 7-1B. of the North Carolina Sales and Use Tax Technical Bulletins, designated Exhibit E-15.
- (16) Copy of Section 7-11B. of the North Carolina Sales and Use Tax Technical Bulletins, designated Exhibit E-16.
- (17) Memorandum dated December 2, 2003, from Assistant Attorney General to the Sales and Use Tax Division, designated Exhibit E-17.
- (18) Copy of H.J. Wilson Company, Inc. v. State Tax Commission of the State of Mississippi, 737 So. 2d 1981 (1998), designated Exhibit E-18.
- (19) Copy of Affiliated Food Cooperative v. State of Nebraska, 259 Neb 549 (2000), designated Exhibit E-19.
- (20) Letter dated April 26, 2004, from the Assistant Secretary of Administrative Hearings to the Taxpayer's representative, designated Exhibit E-20.
- (21) Letter dated May 6, 2004, from the Assistant Secretary of Administrative Hearings to the Taxpayer's representative, designated Exhibit E-21.
- (22) Undated letter received by facsimile on June 2, 2004, from the Taxpayer's representative to the Assistant Secretary of Administrative Hearings, designated Exhibit E-22.
- (23) Letter dated June 7, 2004, from the Assistant Secretary of Administrative Hearings to the Taxpayer's representative, designated Exhibit E-23.
- (24) Copy of House Bill 1414 signed by the Governor on July 20, 2004, designated Exhibit E-24.

The following items were introduced into evidence by the parties during the hearing:

- (25) Brief for Tax Hearing presented by the Sales and Use Tax Division, designated Exhibit E-25.
- (26) An exhibit showing copies of two checks, one numbered 1110 in the amount of \$27,100.00, and the other numbered 1178 in the amount of \$26,208.00, both of which were written to the United States Post Office on dates after the close of the audit period, designated as Exhibit TP-1.

## **FINDINGS OF FACT**

Based on the foregoing evidence of record, the Assistant Secretary makes the following findings of fact:

- (1) The Taxpayer was an S Corporation engaged in business as a direct mail marketing firm that mails the [Magazine], an advertising circular, during the audit period.
- (2) The Taxpayer was not registered with the Department for sales and use tax purposes until contacted by an auditor with the Department.
- (3) During the audit period, the Taxpayer's customers paid to have advertisements included in the Taxpayer's advertising circulars, which were printed by an out-of-state printer.
- (4) The oral publishing agreement between the Taxpayer and the printer granted the Taxpayer the right to publish the circulars in North Carolina and provided that the printer would produce the circulars, including providing the art work and graphics; print and label the circulars; and mail them to recipients in this State.
- (5) The agreement between the Taxpayer and the printer required the Taxpayer to make four separate payments to the printer each time the circulars were printed; one payment was for labels, another was for printing, a third was for graphics, and the final payment was for postage.
- (6) The payment for postage was paid to the out-of-state printer and was equal to the amount paid by the printer to the United States Postal Service to have the circulars delivered to recipients in this State.
- (7) The Taxpayer did not pay any North Carolina sales or use tax to its out-of-state printer, nor did it accrue and remit any use tax to the Department for its purchase of the circulars.
- (8) A notice of proposed sales and use tax assessment was mailed to the Taxpayer on February 26, 2003.
- (9) The Taxpayer objected to the assessment and timely requested a hearing to resolve the matter.

## **CONCLUSIONS OF LAW**

Based on the foregoing findings of fact, the Assistant Secretary makes the following conclusions of law:

- (1) The advertising circulars were purchased by the Taxpayer from the out-of-state printer for use as advertising material in this State; therefore, all of the costs associated with the purchase are subject to North Carolina use tax.
- (2) The sales price of the circulars is the total amount the printer charged the Taxpayer, including the printer's cost of materials used, labor and service costs, transportation costs, all costs for any services necessary to complete the sale, and all delivery charges.
- (3) Delivery charges are charges imposed by a retailer for preparation and delivery of tangible personal property or services to a location designated by the purchaser.
- (4) The fact that the charges for printing represents the printer's actual cost for the United States postage to deliver the circulars to the Taxpayer's recipients in this State does not exclude it from being one of the printer's costs to produce the taxable tangible personal property and deliver it in this State for use in this State.
- (5) The Taxpayer is liable for the State and applicable county use tax.
- (6) The Notice of Sales & Use Tax Assessment for the audit period was issued pursuant to G.S. 105-241.1 on February 26, 2003.

## **DECISION**

The Taxpayer objects to the use tax assessed on its vendor's charge for delivering the advertising circulars, via the United States Postal Service, to recipients in this State because the payment was for postage which is an obligation of the federal government that is exempt from sales and use tax. The Taxpayer contends that if the printer had delivered the circulars to the Taxpayer in this State and the Taxpayer had then mailed the circulars to the intended recipients, the Taxpayer's purchase of postage directly from the Post Office would have been exempt from tax. The Taxpayer also

points to a Mississippi Supreme Court case, H.J. Wilson Company, Inc. v. State Tax Commission of the State of Mississippi (737 So. 2d 981 (1998)), to show that another state has determined that postage charges are always considered an obligation of the federal government, regardless of whether or not the party charging a fee for the postage is the United States Postal Service.

It is true that if the printer had delivered the circulars directly to the Taxpayer in this State and the Taxpayer had then mailed the circulars using the Postal Service and paid the Postal Service directly for the postage, then that postage would be exempt from tax because the transaction would be a direct purchase from the federal government. The Taxpayer, however, chose to transact with the out-of-state printer for the delivery of the circulars to its intended recipients; the transactions upon which use tax has been assessed are not between the Taxpayer and the Postal Service.

I must agree with the Sales Tax Division that the statutes clearly provide that delivery charges are considered part of the sales price of tangible personal property. As the statutory definition of “delivery charges” provides that the term means charges imposed by a retailer for the preparation and delivery of personal property to a location designated by the purchaser, I find that all of the printer’s charges for the preparation and delivery of the advertising circulars, including the postage charges, are subject to this State’s use tax. While a court in another state may have reached a different conclusion regarding the taxability of postage, I do not see how that decision affects this State’s authority to assess the use tax in this case.

With the passage of House Bill 1414, which includes a new and specific provision for an exemption from sales or use tax on delivery charges for delivery on direct mail if the charges are separately stated on the invoice or similar billing document given to the purchaser, the issue at hand becomes moot for sales and purchases of direct mail made on or after October 1, 2004. However, for the period in question here, no such exemption applies.

I do feel that the mistakes made in accruing and remitting use tax during the audit period were inadvertent. Therefore, I am authorizing the waiver of the penalties included in the assessment, provided the tax and accrued interest are paid in full.

Therefore, the assessment of tax and interest is deemed correct under the law and the facts and is hereby declared to be finally determined and immediately due and payable as allowed by law.

Made and entered this 4th day of October, 2004.

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Eugene J. Cella  
Assistant Secretary of Administrative Hearings