

**STATE OF NORTH CAROLINA**

**BEFORE THE  
SECRETARY OF REVENUE**

**COUNTY OF WAKE**

**In the Matter of:**

The Proposed Assessment of Additional Sales )  
 and Use Tax for the period October 1, 1999 )  
 through September 30, 2003, by the Secretary )  
 of Revenue of North Carolina )  
 )  
 vs. )  
 )  
 [Taxpayer] )  
 d/b/a [Taxpayer's Company] )

**FINAL DECISION**  
 Docket No. 2006-243

This matter was heard before the Assistant Secretary of Revenue, Eugene J. Cella, in the City of Raleigh, on October 24, 2006, upon application for hearing by the Taxpayer wherein he protested the proposed assessment of tax, penalty and interest for the period October 1, 1999 through September 30, 2003. The hearing was held by the Assistant Secretary of Revenue pursuant to G.S. 105-260.1 and was attended by W. Timothy Holmes, Assistant Director, and Danny R. Fulcher, Administration Officer of the Sales and Use Tax Division. Neither the Taxpayer nor a representative attended the hearing.

Pursuant to G.S. 105-241.1, the Department mailed a Notice of Proposed Assessment to the Taxpayer on December 17, 2003 assessing additional tax, penalty and interest of \$27,362.14. The Taxpayer's attorney filed a timely protest to the proposed assessment and requested a hearing before the Secretary of Revenue.

**ISSUES**

1. Did the Taxpayer purchase non-taxable advertising services or tangible personal property in the form of printed advertising material for distribution in this State which is subject to use tax on its cost price?
2. Is the charge for postage on the printed advertising material considered a part of the "sales price" of the printed advertising material distributed to donees in North Carolina taxable?

## EVIDENCE

The following items were introduced into evidence at the hearing:

1. Copy of Memorandum dated May 16, 2001 from the Secretary of Revenue to the Assistant Secretary of Administrative Hearings, designated Exhibit E-1.
2. Copy of auditor's report sales and use tax dated December 5, 2003, covering the period October 1, 1999 through September 30, 2003, designated Exhibit E-2.
3. Copy of Notice of Sales and Use Tax Assessment dated December 17, 2003, designated Exhibit E-3.
4. Copy of letter dated January 8, 2004 from the Taxpayer's attorney to the Sales and Use Tax Division (Division), designated Exhibit E-4, with the following attachment:
  - a. Copy of Notice of Sales and Use Tax Assessment dated December 17, 2003.
5. Copy of letter dated February 4, 2004 from the Division to the Taxpayer's attorney, designated Exhibit E-5.
6. Copy of letter received by facsimile dated February 23, 2004 from the Taxpayer's attorney to the Division, designated Exhibit E-6.
7. Copy of letter dated March 5, 2004 from the Division to the Taxpayer's attorney, designated Exhibit E-7.
8. Copy of letter received by facsimile dated March 12, 2004 from the Taxpayer's attorney to the Division, designated Exhibit E-8.
9. Copy of letter dated March 19, 2004 from the Division to the Taxpayer's attorney, designated Exhibit E-9.
10. Copy of facsimile dated May 18, 2004 from Taxpayer's attorney to the Division, designated Exhibit E-10.
11. Copy of letter dated August 2, 2004 from the Division to the Taxpayer's attorney, designated Exhibit E-11.
12. Copy of letter received by facsimile dated August 13, 2004 from the Taxpayer's attorney to the Division, designated Exhibit E-12, with the following attachments:

- a. Advertisement for [Print Broker].
  - b. Copy of ad from [*publication name*].
  - c. Copy of Schedule E-1 from the auditor's report.
  - d. Copy of statement from [an out-of-state printer] dated August 22, 2003.
  - e. Copy of print and label order form dated July 13, 2003.
  - f. Copy of publisher summary from [a print broker] dated September 17, 2003.
  - g. Copy of print and label order form dated November 17, 1999.
  - h. Copy of publisher summary from [a print broker] dated July 29, 2003.
  - i. Copy of Sales and Use Tax Technical Bulletin Section 7-1 Commercial Printers and Publishers.
  - j. Copy of Sales and Use Tax Technical Bulletin Section 7-10 Typesetting and Sales and Use Tax Technical Bulletin Section 7-11 Postage Charges by Printers.
13. Copy of letter dated August 30, 2004 from the Taxpayer to the Division, designated Exhibit E-13.
  14. Copy of letter dated November 19, 2004 from the Division to the Taxpayer, designated Exhibit E-14.
  15. Summary sheets showing postage charges by [a print broker], to the Taxpayer, designated Exhibit E-15, with the following attachments:
    - a. Summary sheets showing postage charges by the printer to the Taxpayer.
    - b. Print and label order forms sent to [a print broker] by the Taxpayer.
  16. Copy of facsimile dated February 18, 2005 from the Taxpayer to the Division, designated Exhibit E-16.

17. Copy of facsimile dated March 11, 2005 from the Taxpayer to the Division, designated Exhibit E-17.
18. Copy of letter dated March 31, 2005 from the Division to the Taxpayer, designated Exhibit E-18.
19. Copy of letter dated April 25, 2005 from the Taxpayer to the Division, designated Exhibit E-19.
20. Copy of letter dated April 27, 2005 from the Division to the Taxpayer, designated Exhibit E-20, with following attachment:
  - a. Copy of letter dated April 25, 2005 from the Taxpayer to the Division.
21. Copy of letter dated June 2, 2005 from the Taxpayer to the Division, designated Exhibit E-21, with the following attachment.
  - a. Copy of letter dated May 5, 2005 from [Taxpayer] to the Division.
22. Copy of letter received by facsimile dated July 26, 2005 from the Taxpayer to the Division, designated Exhibit E-22.
23. Copy of letter dated August 15, 2005 from the Division to the Taxpayer, designated Exhibit E-23.
24. Copy of letter dated October 17, 2005 from the Taxpayer to the Division, designated Exhibit E-24, with the following attachment:
  - a. Copy of facsimile dated October 17, 2005 including letter dated October 17, 2005 from the Taxpayer to the Division.
25. Copy of facsimile dated November 1, 2005 from the Taxpayer to the Division, designated Exhibit E-25.
26. Copy of letter dated February 27, 2006 from the Division to the Taxpayer, designated Exhibit E-26.
27. Copy of facsimile dated March 8, 2006 from the Taxpayer to the Division, designated Exhibit E-27, with the following attachment:
  - a. Copy of letter dated December 19, 2005 from Neurologist regarding the Taxpayer's medical condition.
28. Copy of letter dated April 11, 2006 from the Division to the Taxpayer, designated Exhibit E-28.

29. Copy of Sales and Use Tax Technical Bulletin 24-1 B. (revised June 1, 2002), designated Exhibit E-29.
30. Copy of a facsimile dated August 18, 2006 from the Taxpayer to the Division, designated Exhibit E-30.
31. Copy of letter dated August 22, 2006 from the Assistant Secretary of Administrative Hearings to the Taxpayer, designated Exhibit E-31.

### **FINDINGS OF FACT**

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

1. During the audit period the Taxpayer at all material times was engaged in business as a publisher for [a print broker] located in [out of state].
2. The Taxpayer was not registered for sales and use tax prior to the audit.
3. [A print broker] is not registered for sales and use tax in North Carolina.
4. The Taxpayer solicited clients in the [North Carolina cities] area to advertise in its circular, [*publication name*], which contains coupons and advertisements from various retailers and which is mailed to citizens in the [North Carolina] area on a regular basis at no charge
5. The advertisements were sent to [a print broker] on a computer disk along with an order form with the quantity to be mailed, and payments for labels, printing and postage.
6. The circulars were printed by [out-of-state printer], for [a print broker].
7. After the circulars were printed, addressed and sorted by zip code, they were weighed and metered by the United States Postal Service. The publications were then wrapped and sealed and shipped to a postal distribution center in [City], North Carolina. At this point the packages were unwrapped, sorted and delivered to the appropriate post offices to be mailed to the Taxpayer's clients' customers in North Carolina free of charge.
8. The Taxpayer provides an advertising service to its clients which is not subject to sales tax.

9. Additional tax was assessed against the Taxpayer for the audit period based on the Taxpayer's failure to remit use tax on group printed advertising matter which it directed to be shipped into the State for ultimate distribution to its clients' potential customers via the U. S. Postal Service. Additional tax was assessed against the Taxpayer for postage or delivery charges for the printed material effective January 1, 2002.
10. It is the Taxpayer's position that the Department is attempting to levy a use tax on intangible personal property and services rather than tangible personal property. The Taxpayer contends that it actually purchases only non-taxable advertising services and does not "sell" the circulars since *[publication name]* circulars are distributed free to the public. The Taxpayer contends that the relationship between the parties is that [an out-of-state printer] prints the free distribution circulars and the Taxpayer sells advertising in the circulars in its geographic area.
11. Another objection raised by the Taxpayer is that distribution from out-of-state is not a taxable use in North Carolina prior to January 1, 2002 due to the Department's policy of not proposing to tax catalogs or other printed matter committed to the U.S. Mail outside of North Carolina prior to January 1, 2002.
12. The Taxpayer states that the Department did not allow credit for the sales tax paid in other states.
13. No information was ever furnished by the Taxpayer to substantiate that any taxes were paid in other states; therefore, no credit could be allowed in the audit report.
14. A Notice of Proposed Assessment was mailed to the Taxpayer on December 17, 2003.
15. The Taxpayer's attorney notified the Department that it protested the assessment and requested a hearing.

### **CONCLUSIONS OF LAW**

Based on the foregoing findings of fact, the Assistant Secretary of Revenue for Administrative Tax Hearings makes the following conclusions of law:

- (1) Under the McNamara v. D. H. Holmes Co., Ltd., 486 U.S. 24 (1988), Supreme Court case, catalogs printed by a nonresident printer for a Louisiana resident

corporation which were mailed outside of Louisiana to resident recipients were considered taxable. The Sales and Use Tax Division did not follow this determination and did not tax the Taxpayer on similar transactions prior to January 1, 2002.

- (2) G.S. 105-164.3(46) defines “Tangible personal property” to include “Personal property that may be seen, weighed, measured, felt or touched or is in any other manner perceptible to the senses. . . .” The circulars purchased by the Taxpayer are tangible personal property which can be weighed, measured, felt and touched.
- (3) Effective October 1, 1999, the exemption provided in G.S. 105-164.13(39) for paper, ink and other tangible personal property sold to commercial printers and publishers for use in free circulation publications as well as the exemption for sales by printers of free circulation publications to the publishers of these publications was repealed.
- (4) Separately stated postage charges are not subject to sales or use tax prior to January 1, 2002, under G.S. 105-164.3(18).
- (5) Effective January 1, 2002, the definition of “use” in G.S. 105-164.3(18) and G.S. 105-164.3(49) (effective January 1, 2002) includes “. . . any withdrawal from storage, distribution, installation, affixation to real or personal property, or exhaustion or consumption of tangible personal property by the owner or purchaser thereof, . . .” The addition of the word “distribution” (effective January 1, 2002) means that postage is a part of the tax base for sales and use tax purposes.
- (6) G.S. 105-164.3(4), prior to January 1, 2002, provides that “‘cost price’ means the actual cost of articles of tangible personal property without any deductions therefrom on account of the cost of materials used, cash discounts, labor or service costs, transportation charges or any expenses whatsoever.” Effective January 1, 2002, “purchase price” under G.S. 105-164.3(33) provides that “The term has the same meaning as the term ‘sales price’ when applied to an item subject to use tax.”
- (7) The “true object” of the printed advertisement sought by the Taxpayer’s clients and placed into the mail on their behalf by the Taxpayer was the printed advertisement sent to potential customers.
- (8) The consideration paid to [a print broker] represents a purchase of taxable tangible personal property rather than a purchase of indefinite rights to “advertising services” or a franchise fee.
- (9) The essence of what [a print broker] conveyed, in substance, in exchange for consideration paid by the Taxpayer is taxable tangible printed matter and the

Taxpayer owned and used the property in North Carolina, fulfilling the definition of “use.”

- (10) The Taxpayer is liable for the use tax based on its “use” of the taxable tangible personal property in North Carolina pursuant to G.S. 105-164.3(18) and (49).
- (11) The Notice of Proposed assessment was issued to the Taxpayer pursuant to G.S. 105-241.1.

### **DECISION**

I agree with the Sales and Use Tax Division that the consideration paid by the Taxpayer to [a print broker] clearly represents a purchase of taxable tangible personal property and not some obscure, indefinite rights to “advertising services” or a franchise fee. The circulars are tangible and corporeal as well as owned and used by the Taxpayer in North Carolina. It is my opinion that the printed matter is purchased by the Taxpayer in order to fulfill its contractual obligations to its clients. The true object of the transactions are the circulars and without their periodic delivery to the Taxpayer’s clients, there would be no business operations for the Taxpayer.

The 2001 General Assembly amended G.S. 105-164.3(18) to add “distribution,” effective January 1, 2002, to the list of activities that constitute “use” for sales and use tax purposes and recodified the statute under G.S. 105-164.3(49). The addition of the word “distribution” (effective January 1, 2002) means that postage charges (“distribution”) are subject to sales tax whether or not they are set forth separately.



Therefore, the proposed assessment is deemed correct under the law and the facts and is hereby sustained in its entirety. The proposed assessment is declared to be finally determined and immediately due and collectible.

Made and entered this 11th day of January 2007.

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Eugene J. Cella  
Assistant Secretary of Revenue For  
Administrative Tax Hearings