JIM BRAMBLETT JIM BRAMBLETT PRODUCTIONS 2913 STEEPLE CHASE COURT S. MOBILE, AL 36695-3143,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
Taxpayer,	§	DOCKET NO. S. 05-1067
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

OPINION AND PRELIMINARY ORDER

The Revenue Department assessed Jim Bramblett ("Taxpayer"), d/b/a Bramblett Productions, for State sales tax for June 2001 through May 2004. The Taxpayer appealed to the Administrative Law Division pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on March 22, 2006. The Taxpayer attended the hearing. Assistant Counsel Duncan Crow represented the Department.

The Taxpayer is in the video production business in Mobile, Alabama. The Taxpayer did not have an Alabama sales tax license during the period in issue because he understood that his activities were not subject to sales tax. The Department audited the Taxpayer and determined that some of his activities involved the sale of tangible personal property, and were thus subject to sales tax. It assessed the Taxpayer accordingly.

The Taxpayer concedes that some of his transactions are subject to sales tax. He nonetheless objects to the assessment on several grounds:

(1) The Taxpayer produces television commercials for various customers. The Taxpayer discusses the commercial with the customer and also conducts a site visit, if necessary. The Taxpayer writes a script and shoots the video needed for the commercial. He then adds sound and voiceovers, as needed. The finished commercial is put on a

master tape, which the Taxpayer owns and retains possession of at all times. He then provides copies of the commercial to the television stations as directed by the customer.

The Taxpayer charges the customer for producing the master video. The customer is not required to purchase copies of the video, although they routinely do. The Taxpayer also charges the customers for the video copies sent to the television stations. According to the Taxpayer, the Department does not dispute that his charge for producing the commercial and also his charge for the copies initially sent to the television stations are not subject to sales tax. He claims, however, that the Department is taxing him for any copies that may later be sent to a television station. The Taxpayer argues that if the original tapes are not taxable, the subsequent tapes also should not be taxable. I agree.

In *State v. Harrison*, 386 So.2d 460 (Ala. Civ. App. 1980), the Court of Civil Appeals held that an advertising agency that produced catalogues and brochures and made tapes for television and radio was not subject to sales tax because it was providing a nontaxable service. The Court held that the transfer of the tangible materials was only incidental to those services.

Relying on *Harrison*, the Administrative Law Division subsequently held in *Auvid Production International, Inc. v. State of Alabama*, S. 97-475 (Admin. Law Div. O.P.O. 11/14/00), that custom television commercials produced by the taxpayer were not subject to sales tax. The Department conceded in *Auvid* that custom videos such as commercials should be treated as a service similar to advertising agencies, i.e., the *Harrison* scenario.

In this case, the Taxpayer charged his customers for producing the master tapes. Those charges were not contingent on the customer buying or obtaining a copy or copies of the commercial. Consequently, they were not subject to sales tax. See, *Thigpen*

Photography v. State of Alabama, S. 95-127 (Admin. Law Div. 8/30/95); *Voss v. Gray*, 298 N.W. 1 (1941). Applying the rationale of *Harrison*, the transfer of the tangible commercial videos to the television stations was only incidental to the services provided, and thus not taxable. That rationale would apply to all of the commercial videos, whether provided immediately or at some later date.

(2) The Taxpayer sometimes duplicates a customer's video onto a new format. The Taxpayer then gives the customer the original and the duplicate copy. The Department determined that the Taxpayer was selling the duplicates at retail, and assessed the Taxpayer accordingly. The Taxpayer argues that he was primarily providing a service, and that the duplicates were only incidental to the service. I agree with the Department.

In *Harrison*, the Court in substance applied the "true object" or "dominant purpose" test in holding that the advertising agency was primarily providing a service, and that the transfer of tangible property was only incidental to the service. "The final product created by (Harrison) is the result of (Harrison's) talent and skill. Certainly the catalogues and brochures produced by (Harrison) have no value except for those for whom the materials were designed." *Harrison*, 386 So.2d at 461.

I respectfully question the Court's emphasis on the fact that the advertising agency used "talent and skill" in creating the tangible items. Many tangible items that require great skill and craftsmanship in the making are nonetheless subject to sales tax when sold, the same as mass-produced items. The degree of skill or ability needed to construct or create an item should be of no consequence. Rather, if the true object of a transaction is the transfer of possession and ownership of tangible property, sales tax should apply, unless the transaction is otherwise exempt.

Likewise, the fact that an item may be special-ordered and of no or little use to others should also be of no consequence. In his leading treatise on state taxation, Professor Walter Hellerstein rejects the idea that special-ordered and mass produced items should be treated differently:

> Such considerations have no bearing on sales taxes. On the contrary, the application of the special order rule to sales taxes produces capricious and arbitrary results. Under that rule, a wealthy matron who orders a specially designed semicircular couch for the living room of her Fifth Avenue mansion – a couch that most people could not use or afford – would pay no sales tax, whereas a person of modest means, who buys a ready-made couch from Levitz for a typically modern small home, would be subject to sales tax.

J. Hellerstein & W. Hellerstein*, State Taxation,* (3rd ed. 2000) ¶12.07[1][e].

Notwithstanding the above, *Harrison* is the law of the land in Alabama. However, it should be strictly limited to the facts of that case or similar fact scenarios, such as the television commercials in this case or in *Auvid*. I find that the customer's true object in having a video reformatted is the receipt of the tangible end product. The gross receipts derived from the Taxpayer's sale of the tangible duplicates were thus subject to sales tax.

(3) The Taxpayer produces slides for his customers. He argues that sales tax is not due on his sale of the slides because "[i]t is the creative effort that goes into the product that you are charging for and not the slide." Taxpayer's post-hearing letter brief at 3, 4. I again disagree.

As discussed above, if the true purpose of the transaction is to provide the customer with a tangible item, sales tax applies. The Taxpayer may use creative ideas in producing the slides, but the customer is buying the finished slides, not the Taxpayer's talent. As stated, the holding in *Harrison* should be strictly limited to the facts of that case. Every person that uses skill, talent, creativity, etc. in creating or manufacturing a product should

not be relieved of sales tax liability on the subsequent retail sale of the final product.[1] The Taxpayer's sale of the slides was thus subject to sales tax.

(4) The Taxpayer claims that four portable video fluorescent lights should be taxable at the reduced "machine" rate levied at Code of Ala. 1975, §40-23-2(2). The lights are specially designed with a high flicker rate for use in the production of videos.

The machine rate applies to any device, equipment, etc. used in compounding,

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[1] It is for this reason that I respectfully but strongly disagree with the decision in *State, Dept. of Revenue v. Kennington*, 679 So.2d 1059 (Ala. Civ. App. 1995), rehearing denied, certiorari quashed. The taxpayer in *Kennington* was an artist that painted landscapes and commissioned portraits. She conceded that her landscapes were subject to sale tax, but argued that her commissioned portraits were not. The Court of Civil Appeals agreed. Citing *Harrison*, the Court held that "the transfer of the painted canvas is a mere incident of the professional service rendered by the taxpayer." *Kennington*, 679 So.2d at 1061. I respectfully disagree with that conclusion.

All paintings, including commissioned portraits, should be subject to sales tax. The customer is buying the painting, not the artist's skills in creating the painting. The true object of the transaction is the delivery of the finished painting. The following from Professor Hellerstein's treatise is on point.

> Most paintings are not done by artists on commission, but are offered for sale after they have been completed. And usually, whether the painting is done on commission or otherwise, the artist transfers title and possession to the purchaser, along with the right to exhibit and resell the painting, typically for a lump-sum payment. Such transactions have all the customary characteristics of a sale of goods, so that one tends to view the artist as making sales of paintings, including works painted on commission.

State Taxation at ¶12.07[2]

If an artist paints a stranger sitting on a park bench, the subsequent sale of that painting clearly would be taxable. If, however, the person sitting on the bench commissioned the artist to do the painting, the rationale of *Kennington* holds that the painting would be nontaxable. I see no principled reason for the distinction. The finished painting would be identical, and the artist would have used the same skill and talent in producing the painting. What if the artist was commissioned to paint someone's portrait while the person was standing in front of Niagara Falls. How much of the waterfall would have to be in the picture before the nontaxable portrait became a taxable landscape painting?

processing, or manufacturing tangible personal property. The reduced rate applies "[i]f the article in question performs an integral function in the procedure by which the tangible personal property is produced . . ." *State v. Newbury Mfg. Co.*, 93 So.2d 400, 402 (Ala. 1957).

The cameras and video equipment used by the Taxpayer are taxable at the reduced rate because they are used in processing or manufacturing the resulting photographs or videos. Dept. Reg. 810-6-1-.119(4) confirms that mechanical equipment used in producing photographic negatives is taxable at the reduced machine rate. The special lights in issue are also entitled to the reduced rate because unlike normal overhead lights in a manufacturing facility, which illuminate the area but do not affect or cause change in the product being manufactured, the Taxpayer's lights do cause a change in the photograph or video being produced. That is, they perform a necessary and integral function in the processing/manufacturing of the final product.

In summary, if the Taxpayer charges for an activity that does not involve or require a sales of tangible property, sales tax is not due. "A fixed rate fee for services or labor that is not based on or contingent on the subsequently sale of property is not taxable." *Thigpen Photography v. State of Alabama*, S. 95-127 (Admin. Law Div. O.P.O. 8/30/95) at 5. Also, pursuant to *Harrison*, the Taxpayer's production of television commercials is a non-taxable service, and the transfer of the tangible video is only incidental to that service. However, the holding in *Harrison*, and indeed the "learned profession" exception to sales tax, should as a rule be strictly construed and limited. Doctors and lawyers sell their knowledge and skill, and the tangible items transferred to a patient or client are only incidental to the services provided. The same applies for dentists, see *Alabama Bd. of Optometry v.*

Eagerton, 393 So.2d 1373 (Ala. 1981)., and advertising agencies, see *Harrison*. However, the principle should not be applied to every person that uses skill and ability in creating a product. If that were the case, then only mass-produced machine manufactured items would be subject to sales tax.

The Department is directed to recompute the Taxpayer's liability in accordance with the above. A Final Order will be entered after the Department responds.

This Opinion and Preliminary Order is not an appealable Order. The Final Order, when entered, may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered July 25, 2006.

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BILL THOMPSON
Chief Administrative Law Judge