OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 18113964
	) CDTFA Case ID 782985
TRUEBALLOT, INC.	)
	)
	)
	)

OPINION ON PETITION FOR REHEARING

Representing the Parties:

For Appellant: Betty J. Williams, Attorney

For Respondent: Joseph Boniwell, Tax Counsel III

A. KWEE, Administrative Law Judge: On December 20, 2022, the Office of Tax Appeals (OTA) issued an Opinion sustaining a decision issued by respondent California Department of Tax and Fee Administration (CDTFA).[1] CDTFA's decision denied, in part, a petition for redetermination filed by TrueBallot, Inc. (appellant) of a Notice of Determination (NOD) dated October 31, 2013. The NOD is for $39,300.40 in tax, plus applicable interest, and a penalty of $3,930.11 for the period January 1, 2009, through June 30, 2013 (liability period).

On January 17, 2023, appellant timely petitioned for a rehearing with OTA on the basis that OTA erred in determining that the true object of the contract test set forth in California Code of Regulations, title 18, (Regulation) section 1501 was inapplicable (or could not be applicable) under the facts of appellant's case. OTA concludes that the ground(s) set forth in this petition do not constitute a basis for a new hearing.

OTA may grant a rehearing where one of the following grounds exists and materially affects the substantial rights of the party seeking a rehearing: (1) an irregularity in the appeal proceedings, which occurred prior to issuance of the Opinion, that prevented the fair consideration of the appeal; (2) an accident or surprise, which occurred during the appeal proceedings and prior to the issuance of the Opinion, that ordinary caution could not have

[1] Sales and use taxes were formerly administered by the State Board of Equalization (board). In 2017, functions of the board relevant to this case were transferred to CDTFA. (Gov. Code, § 15570.22.) For ease of reference, when this Opinion refers to events that occurred before July 1, 2017, "CDTFA" shall refer to the board.

prevented; (3) newly discovered, relevant evidence, which the petitioning party could not have reasonably discovered and provided prior to issuance of the Opinion; (4) insufficient evidence to justify the Opinion; (5) the Opinion is contrary to law; or (6) an error in law that occurred during the appeals hearing or proceeding. (Cal. Code Regs., tit. 18, § 30604(a)(1)-(6).)

To find that there is insufficient evidence to justify the Opinion, OTA must find that, after weighing the evidence in the light most favorable to the prevailing party, including reasonable inferences therefrom, that the Opinion clearly should have reached a different result. (*Appeal of Swat-Fame, Inc.*, 2020-OTA-045P.) Effective March 1, 2021, OTA's Rules for Tax Appeals split the ground for a rehearing due to "insufficient evidence to justify the written opinion or the opinion is contrary to law" into two separate and distinct grounds. (Former Cal. Code Regs., tit. 18, § 30604(d) [effective from January 2, 2019, to February 28, 2021]; see also Cal. Code Regs., tit. 18, § 30604(a)(4)-(5) [effective on and after March 1, 2021].) This may be relevant, for example, because, the appeal might turn on a purely legal question of whether the Opinion correctly applied the law.[2]

In its review to determine if the Opinion is contrary to law, OTA must indulge "in all legitimate and reasonable inferences" to uphold the Opinion and ascertain whether the Opinion is unsupported by any substantial evidence. (*Appeal of Swat-Fame, Inc.*, *supra*.) The relevant question on a petition for rehearing does not involve examining the quality or nature of the reasoning behind OTA's Opinion, but whether the Opinion can or cannot be valid according to the law. (*Appeal of NASSCO Holdings, Inc*. (2010-SBE-001) 2010 WL 5626976.)

The pertinent background facts for this appeal are straightforward. Appellant provides election-related services and products to customers. Appellant issued billing invoices to customers which included separately stated charges totaling $240,509 for tangible personal property (printed materials). Appellant also billed for election-related services, which both parties agree are nontaxable. Finally, appellant billed for TrueBallot Fees totaling $450,406. The charges for tangible personal property represent 48.91 percent of the total billed charges, excluding the TrueBallot Fees.

The parties disputed the application of tax to the TrueBallot Fees, and to the separately stated charges for tangible personal property. There is no argument or evidence that appellant's

[2] In its petition for rehearing, appellant cites to the prior version of Regulation section 30604. Based on OTA's understanding that appellant only argues that the Opinion at issue is contrary to law, OTA does not further address the sufficiency of the evidence ground for a rehearing.

charges for the tangible personal property were below cost. CDTFA's decision determined that tax applied to the separately stated charges for tangible personal property, and to 48.91 percent of the TrueBallot Fees. OTA's Opinion sustained CDTFA's decision and, in connection with the issue of whether appellant made taxable sales of tangible personal property (Issue 1),[3] OTA opined:

> [W]e find that appellant's $240,509 in separately stated charges for printed materials are taxable. [¶] … [¶] We decline to address the parties' arguments regarding the proper interpretation of the true object of the contract test. The true object of the contract test is not relevant in cases where, as here, the taxpayer included a separately stated charge for tangible personal property. Under such circumstances Regulation section 1501 provides that service providers are retailers with respect to sales of tangible personal property.

Appellant cites a portion of the above language in its petition for rehearing and contends that OTA's Opinion is contrary to law. On this ground, appellant specifically raises three contentions with respect to its separately stated charges for tangible personal property: (1) the text of Regulation section 1501 contains no limitation prohibiting the true object of the contract from being services where there is a separately stated charge for tangible personal property; (2) there is no caselaw or other authority prescribing such a limitation; and (3) OTA's Opinion is contrary to the analysis in *Appeal of Asgarinejad*, 2019-OTA-445.

With respect to appellant's first contention, Regulation section 1501 does not stand, and has never stood, for the proposition that a seller's separately stated retail charges for the transfer of tangible personal property may be excluded from the measure of tax. To the contrary, Regulation section 1501 specifies that persons engaged in the business of rendering service (service providers) are consumers, not retailers, of the tangible personal property which they use incidentally in rendering the service. (Cal. Code Regs., tit. 18, § 1501). The keyword here is "consumer." In other words, under Regulation section 1501, tax does not apply to the extent a service provider incidentally *consumes* tangible personal property in the performance of the service. A person who transfers tangible personal property at retail in exchange for a separately stated charge for the tangible personal property meets the statutory definition of a retailer, as

[3] Appellant did not specifically dispute the Opinion's analysis of Issue 2 (which concerned the TrueBallot Fees) in its petition. If appellant were regarded as the consumer of the tangible personal property, OTA understands it would be undisputed that Issue 2 (the TrueBallot Fees) would be moot because the taxable ratio would be reduced to 0 percent.

opposed to the consumer, with respect to the sale of that tangible personal property. (R&TC, § 6015(a); see also R&TC, § 6019 [further expanding the definition of retailer].)

As provided in the reference notes to Regulation section 1501, the stated purpose of Regulation section 1501 is to interpret and implement the definitions of "sale" in R&TC section 6006 and "retailer" in R&TC section 6015. (See Cal. Code Regs., tit. 1, § 14(b)(2).) Thus, Regulation section 1501 clarifies the application of tax to transactions involving service providers when it may otherwise be unclear under the existing statutory framework if they are considered a "retailer" making a "sale" of tangible personal property which they transfer while providing services. (See R&TC, §§ 6006, 6015.) To do this, Regulation section 1501 sets forth the true object test to determine whether the service provider is a consumer or retailer of such tangible personal property. However, the true object test does not apply when the person clearly meets the statutory definition of a "retailer" making a "sale" of tangible personal property because the Sales and Use Tax Law imposes sales tax on a retailer, measured by the retailer's gross receipts, from the retail sale of tangible personal property in this state, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, §§ 6012, 6051.)

In summary, Regulation section 1501 clarifies whether a bundled transaction involving services and tangible personal property, and which is not readily separable, is considered as a retail sale of tangible personal property versus the nontaxable provision of services. (*Dell, Inc. v. Superior Court* (2008) 159 Cal.App.4th 911, 924.) Regulation section 1501 does not constrict the statutory definition of "retailer," and the true object test likewise does not carve out an exception to the statutory definition of a "retailer."

A retailer is clearly defined to include every seller who makes any retail sale of tangible personal property. (R&TC, § 6015(a)(1).) A seller includes every person engaged in the business of selling tangible personal property of a kind the gross receipts from the retail sale of which are required to be included in the measure of the sales tax. (R&TC, § 6014.) A "sale" means and includes the transfer of title or possession, exchange, or barter, in any manner or by any means, of tangible personal property for consideration. (R&TC, § 6006.) The term "gross receipts" means the total amount of the sale price of the retail sale of retailers, valued in money, whether received in money or otherwise. (R&TC, § 6012(a).) Here, there was a transfer of printed materials (i.e., tangible personal property) at retail in exchange for a separately stated fee (i.e., consideration). There is no evidence or argument that the fee charged was substantially

below cost. The facts of this transfer meet the definition of a "sale." Appellant's gross receipts are the separately stated fees charged for the tangible personal property. Under these facts, appellant is a retailer, appellant made a "sale," and appellant's gross receipts are subject to tax. (R&TC, §§ 6006, 6012, 6051.)

Furthermore, there is nothing in the text of Regulation section 1501 which states or implies that the true object test could be applied to make a retailer's separately stated charges for the retail sale of tangible personal property nontaxable. To the contrary, Regulation section 1501 starts off by acknowledging that service providers who regularly sell tangible personal property to consumers "are retailers with respect to such sales." (Cal. Code Regs., tit. 18, § 1501.)

In summary, OTA has no authority to constrict the clear and specific provisions of R&TC section 6051. OTA cannot apply the true object test to conclude that appellant is a consumer of the tangible personal property, because doing so would require OTA to disregard the clear and unambiguous language of R&TC sections 6006, 6012 and 6051. Appellant meets the definition of a retailer making a sale of tangible personal property and, as such, appellant's retail sales are subject to tax. (R&TC, § 6051; see also, e.g., Sales and Use Tax Annotations 515.0069 (1/27/94), 515.1181.300 (7/15/96), 515.1450 (6/8/94.).)[4]

Appellant's second contention is that there is no caselaw or other authorities to support OTA's Opinion. With respect to appellant's second contention, OTA's Opinion summarized the pertinent facts as follows:

> CDTFA implicitly conceded that appellant provides nontaxable election administration services in a mixed transaction because CDTFA deleted the administration fees from the audit liability and conceded they are nontaxable..... CDTFA has treated this as a mixed transaction involving both: (1) non-taxable administration services and (2) the taxable sale of printed matter.

Next, OTA's Opinion correctly cited *Dell, Inc. v. Superior Court*, *supra*, for the proposition that in mixed transactions, the separate elements of the transaction are analyzed as separate transactions for tax purposes. (*Dell, Inc. v. Superior Court*, *supra*, at. p. 925.) The tangible property aspect of the transaction is taxed, and the service aspect of the transaction is not taxed. (*Ibid*.) For the reasons explained above in response to appellant's first contention, OTA fully analyzed the first transaction involving separately stated charges for printed matter and

[4] Annotations do not have the force or effect of law but may be entitled to some consideration by OTA. (*Yamaha Corp. of America v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 15.)

concluded that it is a retail sales transaction involving tangible personal property and, as such, it must be taxed. The second transaction, involving election-related services, has already been conceded. Regarding the third transaction, OTA sustained CDTFA's determination that a percentage of the TrueBallot Fees were taxable (i.e., that it was a mixed transaction) and appellant did not dispute the application of tax to the third transaction in its petition for rehearing. In summary, OTA's Opinion, concluding that the true object of the contract test is inapplicable to appellant's first transaction involving printed matter, under the facts cited above, is also consistent with and supported by California caselaw interpreting Regulation section 1501, which the Opinion cited.

Finally, appellant also cites *Appeal of Asgarinejad*, 2019-OTA-445, which is a nonprecedential OTA Opinion with a separate concurrence. In *Appeal of Asgarinejad*, *supra*, the taxpayer provided educational services and computers, and billed for the computers at 25 percent of cost. CDTFA asserted tax on the sale of computers based on cost, but not on the sale of educational services provided with the computers. OTA applied the true object of the contract test and concluded that the entire charge was subject to tax, and, as such, CDTFA had erroneously failed to bill the taxpayer for the educational services. As a preliminary matter, this Opinion is nonprecedential and, as such, it is not citable authority in an appeal before OTA. (Cal. Code Regs., tit. 18, § 30502(b).) Furthermore, the facts of this nonprecedential case are different from the instant appeal because it involved sales for 25 percent of cost.[5] Finally, the *Appeal of Asgarinejad*, *supra*, ultimately concluded that all charges were taxable, and, as such, it could not be considered to stand for the proposition that a retailer's separately stated charges for tangible personal property may be considered nontaxable under Regulation section 1501. As such, the cited nonprecedential case presents no inconsistency with the conclusions of the instant appeal.

[5] Under certain circumstances, persons who make gifts of property, such as transfers for less than 50 percent of cost, may be considered the consumers, as opposed to the retailers, of such property and in such instances, tax could apply based on the cost, as opposed to the separately stated selling price. (Cal. Code Regs., tit. 18, § 1670(a), (b); see, e.g., Sales and Use Tax Annotations 280.0185 (12/5/88), 280.0769 (6/4/87), and 280.1096 (9/26/95).)

Based on the above, OTA finds that appellant failed to establish that the Opinion is contrary to law. Appellant asserts no other grounds in its petition for rehearing. As such, the petition is denied.

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Andrew J. Kwee
Administrative Law Judge

I concur:

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Huy "Mike" Le
Administrative Law Judge

Date Issued: 6/5/2023

A. WONG, Administrative Law Judge, concurring:

I concur with the majority that the Office of Tax Appeals' (OTA's) Opinion in this case is not contrary to law, but I write separately to provide my rationale.

The transactions at issue involved the sale of printed materials, the charges for which appellant separately stated on invoices, along with nontaxable election administration services. Respondent California Department of Tax and Fee Administration conceded that these were mixed transactions.

In its petition for rehearing, TrueBallot, Inc. (appellant) contends that California Code of Regulations, title 18, (Regulation) section 1501 "has no limitation prohibiting the object of the contract from being services where there is a separately stated charge for tangible personal property, nor is there any case law or administrative authority prescribing such a limitation." In other words, appellant contends that there is no authority prohibiting OTA from applying the true object test to the mixed transactions at issue. This is incorrect because such case law exists.

Bundled transactions are distinguishable from mixed transactions where goods and services are sold together yet are readily separable. (*Dell, Inc. v. Superior Court* (2008) 159 Cal.App.4th 911, 936.) "Where services and tangible property are inseparably bundled together, determination of the taxability of the transaction turns upon whether the purchaser's 'true object' was to obtain the finished product or the service." (*Id.* at p. 935.) However, "'when there is a fixed and an ascertainable relationship between the value of the article and the value of the services rendered, and each is a consequential element capable of a separate and distinct transaction, then the elements must be analyzed as separate transactions for tax purposes.'" (*Id.* at p. 930, quoting *New England Tel. & Tel. Co. v. Clark* (R.I. 1993) 624 A.2d 298, 301.) Thus, the true object test in Regulation 1501 does not apply to mixed transactions such as the ones at issue.

Regarding appellant's specific contention: Regulation 1501 contains no limitation or prohibition against applying the true object test to the mixed transactions at issue because the true object test simply does not apply to them (per case law). I find that this analysis sufficiently addresses appellant's specific contention. Further, I concur with the majority's determination that *Appeal of Asgarinejad*, 2019-OTA-445, is inapplicable because it is factually distinguishable and is not precedential. For these reasons, I concur with the majority that OTA's Opinion is not contrary to law.

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Andrew Wong
Administrative Law Judge

Date Issued: 6/5/2023