

Janet Napolitano
Governor



J. Elliott Hibbs
Director

ARIZONA DEPARTMENT OF REVENUE

OFFICE OF TAX POLICY & LEGAL SUPPORT

1600 WEST MONROE, ROOM 810
PHOENIX, ARIZONA 85007-2650

Telephone: (602) 542-4672 • Fax: (602) 542-4680

PRIVATE TAXPAYER RULING LR03-008

July 8, 2003

This private taxpayer ruling responds to your letter of February 10, 2003, as supplemented by your letters of March 7, 2003 and June 14, 2003. In your original letter, you requested the Department to rule that merchandise and artwork sold through your business, . . . ("Business"), to certain organizations and entities are exempt from Arizona transaction privilege tax.

The following are facts as presented in your letter:

[Requester] is sole owner of [Business]

One aspect of my business is creating photographic artwork that is printed on products, including t-shirts. For purposes of this request, I am considering producing t-shirts for public schools, chambers of commerce, the Arizona Department of Tourism, and/or non-profit organizations. I would either sell the t-shirts, or other products, to such organizations for fund raisers or to promote tourism, and/or I would get businesses to sponsor the fund raising in exchange for advertising on the t-shirts or other merchandise.

You further note that, in certain situations, a business may sponsor a fundraising activity "by paying [you] for creating the advertising that would appear on the t-shirts" that are then "sold or given to a public school, chamber of commerce or non-profit organization for the purpose of fund raising." In such an arrangement, a business sponsor would agree to subsidize the cost of T-shirts to a sponsored organization or entity by paying a fee to Business that is applied to reduce the cost of the T-shirts to the sponsored organization. The business sponsor's logo or business name is printed on the T-shirts sold or given to the sponsored organization in addition to any design or artwork printed for the sponsored organization.

One "CONTRACT TO PARTICIPATE IN FUND RAISING and LICENSING AGREEMENT" includes the following provisions in an agreement to be signed by you (referred to as "PHOTO-ARTIST" in the contract) and a business sponsor ("SPONSOR" in the contract) for T-shirts that are ultimately sold by the fundraising organization ("RECIPIANTS" [sic] in the contract):

PRIVATE TAXPAYER RULING LR03-008

July 8, 2003

Page 2

3. The PHOTO-ARTIST will create and use his own artwork in conjunction with artwork, logos, trademarks, and/or copyrighted designs supplied by the RECIPIANTS and/or SPONSORS and authorized for the PHOTO-ARTIST'S use to create full color artwork for the t-shirts. The PHOTO-ARTIST will also supply all t-shirts, and materials needed for transferring the designs onto the t-shirts. All artwork created by the PHOTO-ARTIST is copyrighted, and the PHOTO-ARTIST has sole and exclusive rights to all of his artwork, unless a written Licensing Agreement is signed by the PHOTO-ARTIST. No SPONSOR may make copies of any advertising artwork created by the PHOTO-ARTIST, even if such artwork includes the SPONSOR'S artwork, logos, trademarks, and/or copyrighted designs, unless the PHOTO-ARTIST issues a written Licensing Agreement to the SPONSOR.

4. Each SPONSOR will pay, to the PHOTO-ARTIST, a fee to help cover the costs of labor for designing the final artwork and production of the t-shirts to be supplied to the RECIPIANTS. The fee to be paid by each SPONSOR will be based upon the size of the advertising the SPONSOR wants on the t-shirts and number of t-shirts to be produced with the SPONSOR'S advertising.

5. The amount of the fees that a SPONSOR will pay will be set forth in each CONTRACT TO PARTICIPATE IN FUND RAISING, and those fees may change from one Contract to the next. For this Contract, the SPONSOR agrees to pay a fee of \$___ (\$___ per t-shirt) to the PHOTO-ARTIST ([Requester]) in exchange for having ___ t-shirts produced with the SPONSOR'S ___ (size) advertising printed on each t-shirt. The size of the advertisement may be adjusted to a slightly smaller size for youth sized t-shirts.

6. . . . If the PHOTO-ARTIST fails to produce and deliver all t-shirts that a SPONSOR has paid a fee toward the labor costs of producing and delivering . . . , the SPONSOR will be entitled to a refund, at the "per t-shirt" rate listed in term number 5 above, for each t-shirt not produced and delivered to one or more RECIPIANTS within the agreed upon time limit, unless the SPONSOR signs a written extension to the time limit. . . .

Another "CONTRACT TO PARTICIPATE IN FUND RAISING and LICENSING AGREEMENT" that is an agreement between the "PHOTO-ARTIST" and "RECIPIANT" provides other terms:

3. The RECIPIANT agrees to payment to the PHOTO-ARTIST for the production and delivery of the t-shirts with full-color artwork by the following method:

___ a. RECIPIANT agrees to allow businesses to sponsor the production and delivery of the t-shirts by SPONSORS paying a fee, to the PHOTO-ARTIST, for having advertising for the SPONSORS printed on the back and/or sleeves of the t-shirts produced for the fund raising. (Adult sizes XXL or XXXL will cost the RECIPIANT three dollars and twenty five cents (\$3.25) per shirt in addition to any fees paid by the SPONSORS.

___ b. RECIPIANT will pay the PHOTO-ARTIST \$___ for each t-shirt (sizes youth small to adult XL) ordered by the RECIPIANT. Adult sizes XXL or XXXL will cost the RECIPIANT an additional three dollars and twenty five cents (\$3.25) per shirt. Half of the total payment is due at the time of ordering, and the other half of payment is due at the time of delivery.

. . .

PRIVATE TAXPAYER RULING LR03-008

July 8, 2003

Page 3

8. If the PHOTO-ARTIST fails to meet the requirements of term numbers 6 and 7 above [related to t-shirt artwork and timing of delivery similar to provisions in the "PHOTOARTIST-SPONSOR" contract *supra*] and the RECIPIANT has paid a fee to the PHOTO-ARTIST, the RECIPIANT will be entitled to only a refund of fees paid for t-shirts not delivered on time. . . .

You clarify that "artwork for these transactions would not be unique, one-of-a-kind artwork, but would instead be composites created from various photographs."

The issues you raise in your request are summarized as follows:

1. Are gross proceeds from Business's sale of merchandise to a nonprofit organization that resells the merchandise in fundraising taxable?
2. Are gross proceeds from Business's sale of merchandise to a school district or public school that resells the merchandise in fundraising taxable?
3. Are gross proceeds from Business's sale of merchandise to a chamber of commerce, business sponsor, or the Arizona Department of Tourism taxable?
4. Are Business's gross proceeds from the fees paid by a business sponsor taxable when the fees: (a) defray the cost of T-shirts sold or given to a business, public school, chamber of commerce, nonprofit organization, or the Arizona Department of Tourism and (b) are paid by the business sponsor to include its advertising on the T-shirts sold or given?

Your Position

Your position is that:

1. Gross proceeds from Business's sale of merchandise printed with artwork produced by Business to a nonprofit organization are exempt from Arizona transaction privilege tax, regardless of whether the sale is from the Business to the organization or from the Business to a business that sponsors the organization by purchasing the merchandise.
2. Gross proceeds from Business's sale of merchandise printed with artwork produced by Business to a school district or public school are exempt from Arizona transaction privilege tax, regardless of whether the sale is from the Business to the school or school district or from the Business to a business that sponsors the school or school district by purchasing the merchandise.

PRIVATE TAXPAYER RULING LR03-008

July 8, 2003

Page 4

3. Gross proceeds from Business's sale of merchandise printed with artwork produced by Business to a chamber of commerce, business sponsor, or the Arizona Department of Tourism are exempt from Arizona transaction privilege tax, regardless of whether the sale is from the Business to one of these entities or from the Business to a business that sponsors the entity by purchasing the merchandise.
4. Gross proceeds from Business's sale of advertising artwork created by Business to appear on promotional or fundraising items sold or given to a business, public school, chamber of commerce, nonprofit organization, or the Arizona Department of Tourism are exempt from transaction privilege tax.

Conclusion and Ruling

Arizona does not provide any blanket exemptions from transaction privilege tax for purchases by entities that, for federal income tax purposes, are considered nonprofit or tax-exempt. Nevertheless, gross proceeds from the sale of tangible personal property are not subject to transaction privilege tax under the retail classification if it constitutes a sale for resale in the regular course of the purchaser's business.

The following ruling is given based on the facts presented in your request:

1. Sales to a nonprofit organization: The Department rules that Business's sale of merchandise to a nonprofit organization that resells the merchandise in a fundraising activity constitutes a sale for resale. Gross proceeds from this sale are exempt from transaction privilege tax. To document the exemption, you may follow the procedure for using an Arizona Transaction Privilege Tax Resale Certificate (Arizona Form 5000A) found in *Arizona Transaction Privilege Tax Procedure* TPP 00-3. The nonprofit organization purchaser should present both an Arizona Transaction Privilege Tax Resale Certificate and attach a copy of the organization's "letter of determination" issued by the Internal Revenue Service certifying its status as a § 501(c)(3) organization.
2. Sales to a school district or public school: The Department rules that Business's sale of merchandise to a school district or a component public school that resells the merchandise in a fundraising activity constitutes a sale for resale, which is exempt from transaction privilege tax. A school district or its component school is expressly excluded from the definition of a "person" subject to transaction privilege tax under A.R.S. § 42-5001(8). Therefore, it is not subject to tax on its sale of merchandise. Nevertheless, even though a sale *by* the school is not taxable, a sale *to* the school district or school is still a sale for resale and not subject to tax. The school district or school may thus purchase merchandise for resale with an Arizona Transaction Privilege Tax Resale Certificate and note its status as a school district or public school in lieu of a

PRIVATE TAXPAYER RULING LR03-008

July 8, 2003

Page 5

transaction privilege tax license number. More information on the use of the Resale Certificate is found in *Arizona Transaction Privilege Tax Procedure* TPP 94-1.¹

3. Sales to other organizations and entities: The Department rules that Business's sale of merchandise to a chamber of commerce, a business sponsor, or the Arizona Department of Tourism for a purpose other than resale in the regular course of business is not a sale for resale. Lacking express statutory exemption for the activity, gross proceeds from such a sale are subject to Arizona transaction privilege tax under the retail classification. Likewise, Business's sale of merchandise to a corporate sponsor that gives the merchandise to another entity is not a sale for resale, is outside the scope of any statutory exemption, and is thus a taxable activity under the retail classification.

4. Fees collected from sponsors: The Department rules that Business's gross proceeds from fees received from a business sponsor for advertising on a T-shirt are taxable under the retail classification. Based on the arrangement described in the facts you provided between a business sponsor and a sponsored organization, the sponsor's fees are applied toward part or even all of the cost of the T-shirts that Business produces.² Although part of the consideration provided to a business sponsor may be the addition of the sponsor's advertising on the T-shirts, the fees Business collects are for sales of T-shirts, and such sales are the transactions to which the business sponsor intends for the fees to apply. Consequently, the fees are gross proceeds of sales subject to transaction privilege tax under the retail classification.

The conclusion of this private taxpayer ruling does not extend beyond the facts presented in your letters dated February 10, March 7, and June 14, 2003.

This response is a private taxpayer ruling and the determination herein is based solely on the facts provided in your request. The determinations are subject to change should the facts prove to be different on audit. If it is determined that undisclosed facts were substantial or material to the Department's making of an accurate determination, this taxpayer ruling shall be null and void. Further, the

¹ Two caveats should be noted:

a. Individual teachers or school groups are not the same as a school district or school. If teachers or school groups (e.g., parent-teacher organizations) purchase merchandise, they either must pay transaction privilege tax on their purchases or must be engaged in the business of selling tangible personal property and have a transaction privilege tax license showing their business under the retail classification.

b. School districts or public schools will be liable for use tax if merchandise purchased for resale is subsequently used or consumed by the school district or school rather than sold.

² The agreement does not provide for a situation where Business sells the T-shirts to a business sponsor for resale by the sponsor to a sponsored organization, although under such circumstances the gross proceeds may be exempt if the resale was within the sponsor's regular course of business and the sponsor holds a transaction privilege tax license.

PRIVATE TAXPAYER RULING LR03-008

July 8, 2003

Page 6

determination is subject to future change depending on changes in statutes, administrative rules, case law, or notification of a different Department position.

The determinations in this private taxpayer ruling are only applicable to the taxpayer requesting the ruling and may not be relied upon, cited, nor introduced into evidence in any proceeding by a taxpayer other than the taxpayer who has received the private taxpayer ruling.

Lrulings/03-008-D