**Opinion Letter**

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| **Letter Number:** | **O-2009-004** |

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| **Tax Type:** | **Kansas Retailers' Sales Tax** |
| **Brief Description:** | **Advertising and design agency charges for industrial design and mechanical engineering design services.** |
| **Keywords:** |  |
| **Approval Date:** | **03/10/2009** |

**Body:**

Office of Policy & Research

March 10, 2009

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XXXX

RE: Your letter dated March 3, 2009

Dear XXXX:

Thank you for your recent letter. You work for an advertising and design agency that intends to begin offering industrial design and mechanical engineering design services. Your company's website lists the services your company currently provides:

**What we do.**

*Marketing*

Brand development
Strategic planning
Applied research
Creative consultation

*Graphic Design*

Brand identity
Logo design and development
Print promotion
Sales collateral
Internal communications

*Advertising*

Market research
Direct marketing
Creative concepts
Media planning and buying
Print, broadcast, and internet campaigns
Database integration
Displays and exhibits
Promotional packaging
Billboard and outdoor signage
Photography and video coordination
Public relations management

*Rich Media*

Website design and development
Multi-media presentations
HTML email
Corporate videos

You ask how Kansas sales tax will apply to your company's charges for industrial design and mechanical engineering design services. Charges for these services are taxed in much the same way as charges for graphic design and advertising services.

As a general rule, an advertising agency's or graphic designer's charges to a customer for creative services and the resulting proof of concept, which typically is delivered to the customer as tangible personal property, are not subject to Kansas sales tax. These charges are for creative concept development services, which are not enumerated, taxable services under the sales tax act. However, to be exempt, these charges must be separately stated when a customer is billed for employee-fabricated property, or for property that is fabricated by a third-party and billed to the customer by the advertising agency or graphic designer.

For example, an advertising agency's or graphic designer's charge to a customer for designing a logo is not subject to Kansas sales tax. However, when an advertising agency or graphic designer imprints the logo on T-shirts for a customer, the charge to the customer for the T-shirts is taxable. If the charge for the creative concept development services to create the logo is not separately billed or separately stated on the customer's invoice for the T-shirts, the lump-sum charge for the T-shirts and design services is taxable. When this type of transaction is undertaken, the department recommends that the advertising agency or graphic designer issue one invoice for the nontaxable creative concept development services, and a second invoice for the customer's taxable purchase of the imprinted T-shirts or other tangible personal property.

Similarly, if the same underlying transaction occurs except that a third party imprints the logo on T-shirts and the advertising agency or graphic designer then charges the customer for the T-shirts, sales tax should be charged on the total amount that is billed to the customer unless the creative concept development services are separately billed or separately stated on the customer's invoice for the T-shirts. If an advertising agency or graphic designer provides creative concept development services and sells tangible personal property that it fabricates or another company fabricates for it, it should register with the department as a retailer for purposes of collecting sales tax on its sales of the tangible personal property.

From your web-site's "What we do" section, your business appears be making taxable retail sales whenever it custom designs and fabricates (or pays to have fabricated) displays, exhibits, billboard advertisement, or outdoor signage for a customer's use. The sale of a single finished display, exhibit, billboard advertisement, or outdoor sign is taxable if it is fabricated with the understanding that the customer will use the finished product. As discussed above, the total amount billed to the customer is subject to sales tax unless the charge for the creative concept development services are separately billed to the customer or are separately stated on the customer's invoice for the taxable display, exhibit, billboard advertisement, or outdoor sign

This same sales-tax treatment applies to your company when it provides industrial design and mechanical engineering design services. Your company's charges for the design services are not subject to sales tax. This is because the Kansas retailers' sales tax act does not list design services as services that are subject to sales tax. Similarly, an industrial design and mechanical engineering design service is not required to collect sales tax when it provides property to a customer as a proof of concept for the design services.

A charge for industrial design and mechanical engineering design services is taxed when the charge is lumped together with a charge for tangible personal property that is based on the design services and sold to the customer for its use. As with advertising agencies or graphic designers, taxable sales do not include transferring a proof-of-concept design drawing, prototype, computer medium containing the concept, or similar item to a customer that is paying for design services.

When your business charges a customer for industrial design and mechanical engineering design services, the company should avoid installing the finished product for either the customer or for another end user. Assisting with installation or repair of something that you designed could have sales tax consequences if the installation or repair services are taxable. As with advertising and graphic design services, your charges for industrial design and mechanical engineering design services should be billed separately from or as a separate non-taxable, line-item charge whenever any property is sold to a customer for its use.

Since your company is providing non-taxable services, everything it buys is subject to sales or use tax. The only exception to this would be if you produce or fabricate something for a customer that you sell to them at retail. These things could include advertising goods, a single finished display, an exhibit, a billboard advertisement, or an outdoor sign. If you are engaged in making taxable retail sales, you should register as a retailer with the department. The materials that go into the items being sold can then be purchases tax exempt as a sale for resale or as an ingredient or component part of the item being sold.

If you have any questions about the taxability of your services, please call me at 785-296-3081.

Sincerely,

Thomas E. Hatten
Attorney/Policy & Research

**Date Composed: 03/12/2009 Date Modified: 03/12/2009**