

## **To Tax or Not To Tax – Dealing with Sales Tax in a Creative Services Environment**

Once the revelry of celebrating the New Year has ended and confetti has been swept up, that nagging thought rolls around once again. Taxes. Hopefully, the prior year's planning has left your agency in a good position and there are no looming surprises. Unfortunately, one of the issues that continues to crop up does not involve an agency's income tax, but rather what sales taxes an agency is responsible for. Although this tends to be a grey area (even more so with implementation of digital technology) there are a few general rules that may help serve as a guide.

A factor in sales tax determination is whether the work completed was tangible. This includes things such as: brochures, annual reports, ad flyers, mail pieces, posters or even a display booth for a client. This is opposed to an intangible such as professional services or licenses to reproduce work. Taxes are based on the form of the final deliverable. We call this the "touch and hold" test. If the deliverable was something that the client could touch and hold when you gave it to them, then it would likely be tangible property and sales tax should be collected on it. If it was delivered digitally, (where there was nothing tangible or "touchable" which exchanged hands) then there is a likelihood that the deliverable is not subject to sales tax.

A question that often comes up, when delivering an ad piece, is: what parts of the ad piece are subject to sales tax? The general rule is that all input components are includible in determining the final delivered price and are therefore subject to sales tax. This includes all concepting and creative time as well as the other costs such as materials and printing (if they are components of the final delivered ad piece).

Generally services aren't taxed unless they are specifically listed as a "taxable services" in the regulation or statute. Some examples of services are: concepting, creative, lay-out, manipulations, building websites, and most things classified under time and labor. If an agency represents a client's interest in dealing with a printer, the property is still taxed, but the printer is responsible for collecting the tax.

When working with a client it can be beneficial to articulate what work the agency will perform and then delineate the various deliverable components that are subject to sales tax. Invoices to the client also need to be detailed in a way which separates the taxable items from the non-taxable items. Both of these actions can minimize sales tax costs. Working with your client to reduce their sales tax cost can potentially add a value-added benefit to your relationship. Keep in mind, you cannot sell "inclusive of sales tax" or agree to absorb the sale tax liability for your client.

In order to best protect your agency against an unnecessary tax liability, procedures should be put in place to ensure that your work for clients is classified (and reported) in such a way that you are in compliance with the sales tax regulations. A good place to start is to look at your client invoices to determine how well you are differentiating services and whether you are giving consideration to sales tax requirements. Beyond the invoices, look at your internal systems for how you capture time and costs. This is an important area to review to ensure that you are considering all of the component costs. By looking at whether you are being charged sales tax for component costs is significant, as you do not have to pay sales tax on a component cost if you are including that cost in a final deliverable to a client (who you will also charge sales tax). Sale tax only gets paid once, and the person who pays it is the end "consumer" of the deliverable. If you

fail to charge and collect the proper sales tax from your clients, your agency will become responsible to remit the sales taxes that should have been charged and collected.

This article is a limited overview which may help you identify some of the issues and areas pertinent to your business. We encourage you to seek the advice of a professional CPA or attorney to answer questions specific to your situation as this article may not address all details specific to your situation.

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