

1987

Mark O. Haroldsen, Inc., dba Marko Enterprises, a Utah Corporation v. State Tax Commission, an agency of the State of Utah : Brief of Appellant

Utah Supreme Court

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UTAH SUPREME COURT

BRIEF

870468

IN THE SUPREME COURT OF THE STATE OF UTAH

MARK O. HAROLDSSEN, INC., d/b/a)
MARKO ENTERPRISES, a Utah)
corporation,)

Case No. 870468

Plaintiff-Appellant,)

vs.)

(Priority Classification 14b)

STATE TAX COMMISSION, an agency)
of the State of Utah,)

Defendant-Respondent.)

BRIEF OF APPELLANT
MARK O. HAROLDSSEN, INC.

ON APPEAL FROM THE JUDGMENT OF THE TAX DIVISION
OF THE THIRD JUDICIAL DISTRICT COURT FOR THE COUNTY OF
SALT LAKE, STATE OF UTAH, HONORABLE TIMOTHY R. HANSON,
DISTRICT JUDGE, PRESIDING.

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STATE TAX COMMISSION, an agency)	
of the State of Utah,)	
)	
Defendant-Respondent.)	

BRIEF OF PLAINTIFF-APPELLANT
MARK O. HAROLDSEN, INC.

ISSUES PRESENTED FOR REVIEW

1. Did the taxpayer's lease or purchase of mailing lists contained on magnetic computer tape or preprinted labels constitute a use of "tangible personal property" within the meaning of Utah Code Ann. § 59-16-3 (repealed; superseded by Section 59-12-103(1)(k) and (1) (1987))?

2. Was the taxpayer's payment to the owners of the mailing lists a payment primarily for services and for intangible information rather than for the lease or purchase of "tangible personal property"?

3. Is Mark O. Haroldsen, Inc., entitled to a refund of taxes paid in connection with the use of the mailing lists obtained from the magnetic tapes and printed lists?

4. Is Utah Code Ann. 59-16-3 ambiguous in its provisions regarding taxation of "tangible personal property" and should the ambiguity be resolved in favor of the taxpayer?

STATEMENT OF THE CASE

A. Nature of the Case.

This is an appeal from the dismissal with prejudice of plaintiff's Complaint against the Utah State Tax Commission as ordered by the lower court in its Order Disposing of Reciprocal Motions for Summary Judgments and Affirming Decision of Utah State Tax Commission, entered on November 12, 1987. (R. 120-25.)

B. Disposition of the Case Below.

Plaintiff-appellant Mark O. Haroldsen, Inc., (the "taxpayer" or the "Company") commenced this action by filing a Complaint and Appeal to Tax Division on May 28, 1985, appealing from an adverse ruling of the Utah State Tax Commission (the "Tax Commission"). (R. 2-6.) Defendant State Tax Commission filed an Answer on June 28, 1985. (R. 19-22.) The parties stipulated as to all of the evidence in this case. The lower court entered an order on the stipulation on September 10, 1985. (R. 23-25.) Each of the parties filed a motion for summary judgment, which were argued at a hearing on April 14, 1987. In a Memorandum Decision dated May 12, 1987, the court denied the taxpayer's motion for summary judgment and granted

the Tax Commission's. (R. 103-10.) The court subsequently entered its Order Disposing of Reciprocal Motions for Summary Judgment and Affirming Decision of Utah State Tax Commission, on November 12, 1987, dismissing the case with prejudice. (R. 120-25.) On December 2, 1987, the taxpayer filed a Notice of Appeal. (R. 126.)

C. Statement of Facts.

The taxpayer Mark O. Haroldsen, Inc., is a company engaged in the business of marketing real estate information. It publishes books and tapes on real estate investment, and conducts real estate seminars. (Tr. 8-9.)¹ As a marketing technique, the taxpayer engages in direct mail advertising. It mails to prospective customers circulars and advertisements relating to its products, and invitations relating to its seminars. (Tr. 9.) The Company obtains names and addresses for these mailings from mailing list brokers, either through leasing or purchasing the lists. During the period at issue, July 1, 1979, through June 30, 1982, the Company paid a total of \$154,844.10 to list brokers. (Tr. 14.) The issue in this

¹The references to the transcript are to the transcript of the formal hearing before the Utah State Tax Commission on February 20, 1985, which is included in the record on appeal. By the lower Court's order of September 10, 1985, the transcript constitutes part of the stipulated facts in this case. (R. 23-25.) The facts set forth in the Statement of Facts are not in dispute.

case is whether the purchase of lists through the list brokers during the period in question constituted a use of "tangible personal property" within the meaning of Utah Code Ann. § 59-16-3.

The taxpayer most frequently used the services of Dependable Lists, a mailing list broker, during the period at issue, from whom the taxpayer purchased approximately 92 percent of its lists. The taxpayer used Dependable Lists because of the excellent service it provided. (Tr. 15, 26.) In purchasing or leasing a mailing list, the taxpayer would typically contact a broker, such as Dependable Lists. The taxpayer would describe the particular product that it wanted to market and would often send a sample of the product to the broker for evaluation. Once the broker had examined the product to be marketed, it would suggest a number of lists for the taxpayer's review. After consultation with the broker, the taxpayer would choose from the broker's set of suggested lists. (Tr. 29, 33-34, 41-42.)

Having selected a particular mailing list or lists, the taxpayer would then consult with the broker to refine the lists chosen. In the process of refining lists, the taxpayer relied heavily on the expertise of the broker. It was not unusual for the broker and the taxpayer to spend a great deal of time identifying the demographic characteristics of people

most likely interested in the product to be marketed. Lists were refined by choosing the characteristics, or "selects," of the group of persons on the list to which the taxpayer desired to offer its products. (Tr. 29-31, 33-34, 40-43.) The categories, or "selects," requested by the company included sex, geographic locale, income bracket, home ownership, number of children, ages of children, subscribership to certain periodicals, the kinds of books purchased through the mail, and the types of prior investments. The taxpayer, in consultation with the list broker, would choose the appropriate selects, and the broker would refine the list on these criteria. Every list that the taxpayer used was refined in this fashion. (Tr. 30, 51.)

Having determined which selects to use, the broker then uses a computer program to refine the list. The difficulty of the programming varies, depending on how complicated the selects are. (Tr. 94-95.) The primary expertise of the broker is more in determining which selects to use rather than in the refining of the list through the computer program. (Tr. 95.) Where the taxpayer purchased the use of more than one list for the same marketing campaign, the lists would be run through a computer to delete name duplicates, a process called "merge-purge." (Tr. 44-46.)

The services of a list broker are critical to the taxpayer's direct mail campaigns. Payments to brokers are far more for services than for access to "raw," or unrefined, lists of names. "Raw" lists are not profitable in direct mailing. During the period at issue the taxpayer bought no "raw" lists. Each list purchased was substantially refined through the use of selects. The success or failure of a direct mail marketing campaign depends on the services of the broker in selecting proper lists and in refining the lists with proper selects. The cost of lists varies to reflect the amount of services rendered by the list broker, and the value of the information on the list. (Tr. 32, 41, 52-57, 62, 94-95.)

Having refined the chosen list through the use of selects, the taxpayer would then place an order for the use of the list through the list broker. The taxpayer would send a sample of the "mailing piece" to the list broker who would, in turn, submit it to the list owner for approval. (Tr. 43). Once the mailing piece is approved, the list is processed and delivered to the taxpayer, which would then be allowed a limited, one-time license to use the mailing list. List owners seed the mailing list with coded "control" names in order to detect unauthorized use of the mailing list. (Tr. 12-13, 43, 47.)

The information rented by the taxpayer from the list owner is transferred to the taxpayer on computer tape or on preprinted labels. During the period in issue, the taxpayer received 63.4 percent of its lists on labels, and 36.6 percent on computer tapes. Once the limited, one-time use of the tape has been made, the tape must be returned, erased, or destroyed. In situations when the tape may be kept, a separate fee is charged for the tape. (Tr. 11-14, 44, 46-47.)

Following the formal hearing before the Tax Commission, the Commission found that the mailing lists were tangible personal property and upheld the challenged use tax assessment. The taxpayer paid the contested amount of \$7,750.00, and commenced this action seeking a judgment that the assessment was erroneous and ordering a refund of that amount to the taxpayer. The tax division of the Third District Court for Salt Lake County also held that the lists were tangible personal property. It is from that determination that the taxpayer appeals.

SUMMARY OF ARGUMENT

1. Because the lower court decided the case on stipulated facts, this Court should consider the matter on a de novo basis.

2. The taxpayer purchased or leased mailing list information through out-of-state list brokers. The information

was transferred through the medium of either magnetic tape or printed lists. The magnetic tapes and printed lists used by the taxpayer were incidental to the sale of services performed by the list brokers in preparing and refining the lists for the purposes of the taxpayer's marketing program.

3. The magnetic tapes and printed lists used by the taxpayer were incidental to the purchase of intangible information. Every court that has considered the issue has held that mailing lists contained on magnetic tape are not taxable as tangible personal property. Computer software is analogous, which is also generally not held to be tangible personal property subject to a sales or use tax.

4. Any ambiguities in the taxing statute, Section 59-16-3, must be strictly construed and resolved in favor of the taxpayer. If the legislature intends that the state should tax the transfer of information by magnetic tape, or other similar means, it should specifically so provide by statute. The statute in question should not be given a forced interpretation to accommodate computer-age transfers of information which could be transferred by other means than magnetic tape or printed lists.

ARGUMENT

I.

BECAUSE THE FACTS WERE STIPULATED TO BY THE PARTIES
THIS COURT SHOULD CONSIDER THE MATTER DE NOVO.

The parties stipulated that the evidence adduced and stipulated to at the formal hearing before the State Tax Commission on February 20, 1985, including the transcript of hearing and all exhibits introduced at the hearing, constituted a full and complete record of all facts relevant to the subject matter of the action. On September 10, 1985, the lower court entered an order on the stipulation. (R. 23-25). Because the facts are not in dispute, but have been stipulated to, this Court should review the issues raised in this appeal de novo. The Court previously held in Sacramento Baseball Club, Inc. v. Great Northern Baseball Company, 748 P.2d 1058 (Utah 1987) that when a trial court relies on stipulated facts to decide a case, "this court does not apply the clearly erroneous standard, but will sustain the lower court's decision only if convinced of its correctness. . . . Thus, we examine the facts de novo." Id. at 1060.

II.

THE MAGNETIC TAPES AND PRINTED LISTS
USED BY THE TAXPAYER WERE INCIDENTAL TO
A SALE OF INTANGIBLE SERVICES.

Utah Code Ann. § 59-16-3(a)(Supp. 1986) imposes a tax on "storage, use, or other consumption in this state of

tangible personal property." For a transaction to be taxable under Section 59-16-3, two separate and independent elements must be present: (1) There must be a use of property, and (2) the property used must be tangible. Except for specific services as outlined in Utah Code Ann. § 59-16-3(b), there is no tax on the use of services. By its terms, the statute subjects only tangible personal property to taxation. The use of intangible property is not taxable.

Not all transactions involving a use of property come within the terms of the statute. Property is often transferred incidentally in a sale of services. Tangible property is often transferred incidentally to a sale of services. The transfer of tangible property is often incidental to a sale of intangible property. Courts have recognized that transactions often mix taxable and non-taxable elements. Thus, in determining the taxability of such transactions under sales and use taxes, courts generally attempt to determine the "true or real object of the sale." For example, the "true object" test was applied in the case of Bullock v. Statistical Tabulating Corporation, 549 S.W.2d 166 (Tex. 1977). There the issue was whether the transfer of compiled statistical data on computer cards constituted the sale of tangible personal property. Holding in the negative, the court stated that "the true object

of this transaction is not the data processing card as contended by the Comptroller, but the purchase of coded or processed data, an intangible." Id. at 168 (emphasis in original). See Spencer Gifts, Inc. v. Director, Division of Taxation, 182 N.J. Super. 179, 440 A.2d 104, 117-18 (1981); Fingerhut Products Co. v. Commissioner of Revenue, 258 N.W.2d 606 (Minn. 1977).

This Court used a version of the "real object test" to determine the taxability of such "mixed" transactions in Thorne and Wilson, Inc. v. Utah State Tax Commission, 681 P.2d 1237 (Utah 1984). There, the Court upheld a district court's ruling that a sale of rare United States and foreign coins was a sale of tangible property. The Court noted that "[i]t is the substance of the transaction and not the property actually transferred that controls. . . . In order to determine whether the metal tokens were sold as tangible personal property, the essence of the transaction must be examined." Id. at 1238 (emphasis added) (quoting Michigan National Bank v. Department of Treasury, 127 Mich. App. 646, 339 N.W.2d 515, 517 (1983)). Thus, in determining the taxability of the case at issue, the "true object" or "essence of the transaction" of the sale must be determined.

As noted above, there is no tax on services under Utah Code Ann. § 59-16-3(a). In this case, the Company paid for the

services of the mailing list broker. The evidence presented at the hearing before the Tax Commission demonstrated that the real object of the transaction was the purchase of the services of the list broker. Thomas Tolman testified that "the actual money paid, from our point of view, to the broker, is far more for the broker's services and what he is able to give us than it is for the actual tape and paper." (Tr. 54). All the lists rented by the company were selected and refined with the assistance of the list broker and its computer programmer, and were tailored to the company's needs. (Tr. 32, 41, 52-57, 62, 94-95). The taxpayer relied on the list broker in selecting lists, and in pinpointing possible customers from each list. (Tr. 29, 43). A "raw" list has little, if any, value to the company. (Tr. 32, 94).

Essentially, the list brokers used by the Company engaged in the service of gathering and collating demographic and marketing research and providing it to the Company to assist the Company's sales efforts. The lists purchased by the Company were not "canned" or "raw," but were specifically tailored to fit the individual needs of the Company. Courts in situations similar to the present case have found that tangible property transferred or used in a manner incidental to the sale of services did not involve a taxable use of tangible personal

property. For instance, in Williams & Lee Scouting Service, Inc. v. Calvert, 452 S.W.2d 789 (Tex. Civ. App. 1970), the taxpayer provided the service of gathering information pertaining to oil and gas fields and then selling reports containing the information. The court held that the company provided a service and that the sale of the written reports was not a transfer of tangible personal property. The court noted that the reporting of the information purchased by the taxpayer "can take any form from handwritten notes, telephone, or telegraph communications to printed material. The method of its communication is unimportant. The value lies in the intangible facts secured by the service." Id. at 792.

In Maccabees Mutual Life Insurance Company v. State, Department of Treasury, 122 Mich. App. 666, 332 N.W.2d 561 (1983), the court considered whether a sale of computer software was a taxable transfer of tangible personal property under a statute virtually identical to Utah's. Observing that the software programs "represent a personalized service, customized to fit plaintiffs' particular computer configuration," the court held that the sale of the software was not taxable. Id. at 563-64. The Maccabees court cited University Microfilms v. Scio Township, 76 Mich. App. 616, 257 N.W.2d 265 (1977), which considered whether master negative microfilm copies of printed materials, rare books, periodicals,

and other sources were personal property. The University Microfilms court distinguished the plaintiff's microfilms from computer software:

We agree with plaintiff that its master negatives are similar to abstracts and computer 'software' in that all contain information, but we disagree that that is what controls the determination of intangibility. The value of an abstract is personal, that is, it is dependent on the work of the one who controls the information. If it is left to go out of date or is inaccurate rate, it loses its value. . . . Similarly, the value of computer "software" is not in the card or disc itself, but rather in the synthesization, compilation, organization and creation of the computer programs contained therein. . . . The value is personal. Payment is made for the service and the expert knowledge.

275 N.W.2d at 267 (emphasis added; citations omitted). See Detroit Automobile Interinsurance Exchange v. Department of Treasury, 361 N.W.2d 373, 374-75 (Mich. App. 1985) (court held that sale of computer software was not taxable since the tapes and disks were not tangible personal property, but represented a service distinguished from TV games, albums, and cassette tapes); Dun & Bradstreet, Inc. v. City of New York, 276 N.Y. 198, 11 N.E.2d 728, 731 (1938) (court held that credit report prepared by taxpayer involved a service and was not a use of tangible personal property).

The list brokers in the present case gather and categorize demographic marketing information which is of great value to the Company in its sales efforts. The brokers

unquestionably provide a service for which the taxpayer should not be taxed. The one-time use of the lists by the taxpayer was not a taxable event. The tangibility of the physical magnetic tape was purely incidental to the real object of the transaction: the use of information resulting from the expert services of the list brokers with whom the taxpayer dealt.

III.

THE TAXPAYER PURCHASED INTANGIBLE INFORMATION, NOT TANGIBLE PROPERTY.

- A. The weight of authority recognizes that mailing lists are not tangible personal property and use thereof is not a taxable transaction.

The magnetic tapes and labels used by the taxpayer were not purchased for their tangible worth as tapes and labels, but rather for their value as a method of transmitting information. Every case that has considered the question raised by the present case had held that the use of mailing lists contained on magnetic tape is not taxable as tangible personal property. In Spencer Gifts, Inc. v. Director, Division of Taxation, 182 N.J. Super. 179, 440 A.2d 104 (1981), the court held that mailing lists transferred by magnetic tape were not tangible personal property. The court stated:

Plaintiff is not subject to sales or use tax when it leases mailing lists. The leasing of computer information is not the leasing or sale of tangible personal property and is not taxable under our act.

Plaintiff is leasing information. It is not leasing tangible personal property. The tapes which are tangible personal property and which transmit the information are only incidental to the underlying transaction between the parties. . . .

The tapes are an inconsequential part of the transaction whose real object is the obtaining of mailing list information. . . . Under such circumstances the form of delivery of the information should not control its taxability. The inconsequential aspect of the magnetic tapes in the subject transactions may be compared to the inconsequential aspect of the paper used in connection with an accountant's services by way of reports or with an attorney's services by way of wills, other legal documents or letters giving advice.

Id. at 117-18 (citations omitted).

In Fingerhut Products Co. v. Commissioner of Revenue, 258 N.W.2d 606 (Minn. 1977), the court reached an identical result in a case involving printed mailing lists. Observing that software on computer cards and tapes is analogous to the typed mailing lists at issue, the court held:

Like the transfer of computer programs through the use of punch cards, the use of the tangible medium of typed mailing lists is merely incidental to the use of the incorporeal information contained in those lists. The typed lists themselves were not used within the contemplation of the statute; what was used was the information contained in the lists. Such use, in our opinion, is not taxable under the current statute.

Id. at 610.

In Mertz v. State Tax Commission, 89 A.D.2d 396, 456 N.Y.S.2d 501 (1982), the court held that mailing lists recorded on magnetic computer tape were "merely the medium by which the information that was the essence of the transaction was transmitted." Id. at 503. The court accordingly held that there was no sale of tangible personal property. Id.

The same result is required in the present case, which involves nearly identical facts to Spencer Gifts, Fingerhut, and Mertz, the only difference being that the brokers in the present case also provide demographic research services for the Company in connection with categorizing the lists that are transferred.

Although the undisputed evidence demonstrated that the mailing lists were not "raw" or "canned" lists, but were refined by the broker through the use of selects, the same result should obtain even if the Company purchased only "raw" lists. Moreover, even though the same list may be sold by a broker to more than one purchaser, it does not mean that the broker performed any less of a service, or that the information somehow becomes tangible personal property. In First National Bank of Fort Worth v. Bullock, 584 S.W.2d 548 (Tex.Civ.App. 1979), the court rejected the state's argument that certain computer software contained on magnetic tape should be taxed because they were "canned" standard items sold to numerous

customers. Holding that the sale of the software was not taxable, the court disagreed that the distinction between canned and customized programs was valid. "The test in each case," stated the court, "is not whether the product is 'customized' or 'canned,' but whether the object of the sale is tangible personal property." Id. at 550.

The court in First National Bank of Springfield v. Dept. of Revenue, 85 Ill. 2d 84, 421 N.E.2d 175 (1981), also declined to hold that the sale of "canned" computer programs on magnetic tape was a taxable event. The court refused to "draw such an artificial distinction" between custom and prewritten software. Id. at 178. Other courts have similarly held that informational reports or mailing lists were not tangible personal property in spite of the apparent "canned" nature of the information. See Washington Times-Herald v. District of Columbia, 213 F.2d 23 (D.C. Cir. 1954) (comic strip mats sold by syndicate to newspaper); Fingerhut Products Co. v. Commissioner of Revenue, 258 N.W.2d 606 (Minn. 1977) (typed mailing lists); Spencer Gifts, Inc. v. Director, Division of Taxation, 182 N.J. Super. 179, 440 A.2d 104 (1981) (mailing lists on magnetic tape); Mertz v. State Tax Commissioner, 89 A.D. 396, 456 N.Y.S.2d 501 (1982) (mailing lists on magnetic tape); Dun & Bradstreet, Inc. v. City of New York, 276 N.Y. 198, 11 N.E.2d 728 (1937) (credit reports); Williams & Lee

Scouting Service, 452 S.W.2d 789 (Tex. Civ. App. 1970)(oil and gas scouting reports).

B. Computer software is analogous to mailing lists and is treated as an intangible by the majority of courts.

The courts in Spencer Gifts and Fingerhut each analogized mailing list information to computer software. The analogy is helpful in considering whether the transfer of a mailing list is of tangible personal property. Courts that have so ruled with respect to computer software² have emphasized the following factors, each of which is equally applicable to the present question regarding mailing lists:

1. Tapes and cards are incidental to the transfer of information. The "real object" or "essence" of transactions involving magnetic tape or cards is the transfer of information. Once the information has been conveyed from a

²The great majority of cases that have addressed the question of the tangibility of computer software have held that software is not taxable as tangible personal property. See Honeywell Information Systems v. Maricopa County, 118 Ariz. 171, 575 P.2d 801, 803 (1977) ("There is little doubt that computer software is intangible property. . . . [E]very jurisdiction which has considered the issue agrees"); James v. TRES Computer Systems, Inc., 642 S.W.2d 347, 348 (Mo. 1982) (en banc) (most courts that have addressed the issue have ruled that the intangibility of data and programs is not lost because of their presence on tapes). See also Note, "Software and Sales Taxes: the Illusory Intangible," 63 B.U.L. Rev. 181, 186 (1983) ("Every court that has addressed the issue of tangibility has held that software is intangible").

tape to a computer the tape is discarded, erased, or returned. This is exactly what the Company does in the present case when it is finished with a tape. As with many software transactions, the Company is required by its contracts with the brokers not to make more than a one-time use of the tapes it receives. (Tr. 13-14, 47.) Once the information is taken from the magnetic tape and put into the computer, the information is treated as totally separate from the tape. The information cannot be used again, but the tapes can. As Mr. Tolman testified at the hearing before the Tax Commission, "I mean, we can't use the information on the mag tape again or we could get ourselves in a lot of trouble, but we can use the mag tape itself for other computer purposes." (Tr. 47, 12). The distinction between the magnetic tape and the information encoded on it is emphasized by the fact that the taxpayer is charged separately for the tape. Most of what the taxpayer pays to the list brokers is for the services rendered and the resultant information. The brokers charge a \$15 to \$25 fee for the tape itself, separate and apart from the mailing list information. (Tr. 47.)

Courts have emphasized in the software cases that the magnetic tapes and punched cards are only the media through which the transfer of information is accomplished. In Commerce Union Bank v. Tidwell, 538 S.W.2d 405 (Tenn. 1976), the court

held that the software at issue was not tangible personal property, even though it was sold on magnetic tape:

When the information is transferred from the tape to the computer, the tape is no longer of any value to the user; and it is not retained in the possession of the user. The information on the tape, unlike the phonograph record, is not complete and ready to be used at the time of its purchase. It must be translated into a language understood by the computer. Once this information has been translated and introduced into the computer and the tapes returned or the punch cards destroyed, what actually remains in the computer is intangible knowledge; this is what was purchased, not the magnetic tapes or the punch cards. . . . Transfer of tangible personal property under these circumstances is merely incidental to the purchase of the intangible knowledge and information stored on the tapes.

Id. at 497 (emphasis added). See District of Columbia v. Universal Computer Associates, Inc., 465 F.2d 615, 617 (D.C. Cir. 1972) (punched cards of insignificant value compared with the information stored on the cards); State v. Central Computer Services, Inc., 349 So.2d 1160, 1162 (Ala. 1977) (held that the commingling of intangible information with tangible tapes and cards was incidental); First National Bank of Springfield v. Dept. of Revenue, 85 Ill.2d 84, 421 N.E.2d 175, 179 (1981) (held that the magnetic tapes were not the subject of the transaction, but the information); University Microfilms v. Scio Township, 76 Mich. App. 616, 257 N.W.2d 265, 267 (1977) ("the value of computer 'softwear' [sic] is not in the card or

disc itself, but rather in the synthesization, compilation, organization and creation of the computer programs contained therein"); James v. TRES Computer Service, Inc., 642 S.W.2d 347, 349 (Mo. 1982) (en banc) (held that the tapes were only a medium to convey the data and were incidental to the transfer of intangible information).

2. The information can be transferred by alternate means. The fact that the information on the magnetic tapes and printed lists may be transferred by other means lends support to the conclusion that the essence of the transaction involves an intangible. To the Company the important thing is the receipt of the information. The magnetic tapes and printed lists merely facilitate the conveyance of that information. The court in Spencer Gifts, Inc. v. Director, Division of Taxation, 182 N.J.Super. 179, 440 A.2d 104 (1981), observed that the magnetic tapes were an "inconsequential part of the transaction." The court found support for its holding in the fact that "it is possible to dispense with the delivery of tapes altogether and to transmit the mailing list information by telephone from one computer to another." Id. at 118. "Under such circumstances," concluded the court, "the form of delivery of the information should not control its taxability." Id. Similarly, in Fingerhut Products Co. v. Commissioner of Revenue, 258 N.W.2d 606 (Minn. 1977),

the court stated that the mailing lists there at issue "could have been transmitted orally by telephone, or someone could have contacted the broker and manually copied the information from the broker's lists." Id. at 609.

Courts have uniformly adopted this rationale in holding that sales of software and computer data are not taxable transactions. See James v. TRES Computer Service, Inc., 642 S.W.2d at 349 (the information being bought need not have been put on tape, but could have been fed directly into the computer through electronic communications); Commerce Union Bank v. Tidwell, 538 S.W.2d at 406-07, 408 (the same information on the tape could have been transmitted by telephone lines or fed directly into the computer); First National Bank of Fort Worth v. Bullock, 584 S.W.2d 548, 550 (Tex. Civ. App. 1979) (the information on the tapes could have been programmed by telephone or by hand); Bullock v. Statistical Tabulating Corp., 549 S.W.2d 166, 168 (Tex. 1977) (the information on the cards could have been "transformed into several forms").

C. Mailing lists are not analogous to phonograph records, books, or films.

The Tax Commission argued below that the taxation of phonograph records, books, and films is analogous to the present situation involving magnetic tape and printed pages.

The analogy breaks down, however, when one considers that the real object of a purchase of record, book, or film is the ownership of the particular item. The magnetic tapes and printed pages used by the Company are used merely to transfer information after which their value is minimal. Once the information is transferred from the tape to the computer, the tape may be used over, for other purposes, while the information may only be used once. The information and the tape, at that point, are entirely separate and distinct. (Tr. 12, 47.)

Courts have uniformly drawn a distinction between records, books, and films, on the one hand, and magnetic tapes or other media whose purpose is merely to convey information, on the other hand. The tapes and lists at issue in the present case are treated in fact as only a means of conveying the list of names. They are subordinate to the intangible information which is the object of the sale. Records and books are not analogous. Consumers are not given the limited kind of rights in the use of the book that plaintiff is given in the mailing lists. No separate fee is stated for the paper or plastic used to make the book or record. The contents of a book or record never become separate and distinct from the paper or plastic.

The court in First National Bank of Springfield v. Dept. of Revenue, 85 Ill.2d 84, 421 N.E.2d 175 (1981),

addressed a similar argument that computer software ought to be taxed similarly to phonograph records and books. The court rejected the contention, stating:

The tapes were certainly not the only medium through which the information could be transferred. In this way, the tapes differ from a movie film, a phonograph record or a book, whereby the media used are the only practicable ways of preserving those articles. Thus, while those articles and the tapes are similar in that they physically represent the transfer of ideas or artistic processes, a more significant distinction is that those articles are inseparable from the ideas or processes, whereas computer programs are separable from the tapes.

Id. at 178.

In Commerce Union Bank v. Tidwell, 538 S.W.2d 405 (Tenn. 1976), the court rejected the same argument in holding that the taxpayer's purchase of magnetic tapes and punch cards was not taxable. The court considered whether it was a finished product that was created and sold, as opposed to information. Id. at 407. The court observed that the purchase of a magnetic computer tape, which could only be used once, was unlike the purchase of a phonograph record:

One who buys a phonograph record intends to obtain possession of a tangible item. Granted the sound which emanates from the record when it is played is the object of the purchase; but the purchaser has no other viable method of bringing the music of, say, Caruso into his living room.

The phonograph record remains in the possession of the purchaser after its purchase, both during periods of use and non-use.

The instant case presents a different situation. A magnetic tape is only one method whereby information may be transmitted from the originator to the computer of the user. That same information may be transmitted from the originator to the user by way of telephone lines or it may be fed into the user's computer directly by the originator of the program.

When the information is transferred from the tape to the computer, the tape is no longer of any value to the user; and it is not retained in the possession of the user. The information on the tape, unlike the phonograph record, is not complete and ready to be used at the time of its purchase. It must be translated into a language understood by the computer. Once this information has been translated and introduced into the computer and the tapes returned or the punch cards destroyed, what actually remains in the computer is intangible knowledge; this is what was purchased not the magnetic tapes or the punch cards. . . . Transfer of tangible personal property under these circumstances is merely incidental to the purchase of the intangible knowledge and information stored on the tapes.

Id. at 408 (emphasis added; citation omitted).

Other courts have similarly distinguished information-bearing tapes, cards, and lists from phonograph records, books, and films. See District of Columbia v. Universal Computer Associates, Inc., 465 F.2d 615, 618 (D.C. Cir. 1972) (distinguishes computer cards, tapes, and discs from films); State v. Central Computer Services, Inc., 349 So.2d 1160, 1162 (Ala. 1977) (distinguishes tapes and cards from

movie films; the right to publish or broadcast the motion picture is "physically inseparable from the movie film itself"); James v. TRES Computer Service, Inc. 642 S.W.2d 347, 350 (Mo. 1982) (distinguishes magnetic tapes from films and records; the "physical presence of the movie film is essential to broadcasting the intangible artistic efforts of the actors"); First National Bank of Fort Worth v. Bullock, 584 S.W.2d 548, 550 (Tex. Civ. App. 1979) ("Unlike a phonograph record or filmstrip, when the information on the tape, in the present case, is transferred to the computer, the tape is no longer of any value or importance to the user").

The Company urges the Court to adopt the same rationale as in these analogous cases involving computer software³ and hold that the mailing list information used by the Company was intangible and not subject to taxation.

D. The use of tapes and printed lists is not a use of "tangible personal property" under the Utah statute.

³The Internal Revenue Service has characterized software as intangible, although in a different context than personal property taxation. Rev. Proc. 69-21 § 4, 1969-2 C.B. 303. Several academic commentators have also urged the position that computer software is an intangible and should not be subject to personal property taxation. See Heinzman, "Computer Software: Should it be Treated as Tangible Property for Ad Valorem Tax?" 37 J. of Taxation 184 (Sept. 1972); Bryant & Mather, "Property Taxation of Computer Software," 18 N.Y.L.F. 61 (1972); Note, "The Revolt Against the Property Tax on Software: An Unnecessary Conflict Growing Out of Unbundling," 9 Suff. L. Rev. 118 (1974).

The Tax Commission may argue that Utah Code Ann. § 59-16-3 is broader in scope than the statutes of other states that have held that mailing lists are not "tangible personal property." The Tax Commission, by regulation, has defined tangible personal property as follows:

Tangible personal property embraces all goods, wares, merchandise, produce, and commodities, all tangible or corporeal things and substances which are dealt in or capable of being possessed or exchanged. It does not include real estate or any interest therein or improvements thereon nor does it include bank accounts, stocks, bonds, mortgages, notes and other evidence of debt, insurance certificates or policies, personal or governmental licenses. The term does not include water in pipes, conduits, ditches or reservoirs but does include water in bottles, tanks or other containers. Tangible personal property includes all other physically existing articles or things including property severed from real estate. A sales or use tax is imposed on the sale of tangible personal property.

Utah State Tax Commission Reg. A12-02-526.⁴

⁴Utah Code Ann. § 59-12-102(13)(a) (1987) now defines "tangible personal property" as meaning:

(i) all goods, wares, merchandise, produce, and commodities;

(ii) all tangible or corporeal things and substances which are dealt in or capable of being possessed or exchanged;

(iii) water in bottles, tanks, or other containers; and

(iv) all other physically existing articles or things, including property severed from real estate.

Although Tax Commission Regulation A12-02-526 does not specifically limit the definition of tangible property to objects that can be perceived with the senses, the word "tangible" is itself limiting. This Court has stated that "the terms of a statute are used advisedly and should be given an interpretation and application which is in accord with their usually accepted meanings." Board of Education v. Salt Lake County, 659 P.2d 1030, 1035 (Utah 1983). The usually accepted meaning of the word "tangible" according to Websters Third New International Dictionary (1976) is "capable of being touched: able to be perceived as materially existent esp. by the sense of touch." This definition is supported by the regulation, which indicates that tangible personal property embraces "all goods, wares, merchandise, produce, and commodities, all tangible or corporeal things and substances which are dealt in or capable of being possessed or exchanged." In the context of this definition, the mailing list information used by the Company clearly falls outside the definitional parameters of the statute, which evidences a clear legislative intent to tax only personal property that can be touched or otherwise perceived by the sense.

E. The mailing lists were treated as intangibles by the parties and are generally so treated in business contexts.

In the context of competitive torts "customer lists" have been recognized as trade secrets, which are a form of

intangible property. The lists in the present case have the same characteristics of intangibility and were treated as trade secrets by the parties. "Written customer lists generally have been regarded as trade secrets when the nature of the industry permits the list to be kept secret and the list cannot readily be duplicated by independent means." Developments in The Law -- Competitive Torts, 77 Harv. L. Rev. 888, 955 (1964). In Microbiological Research Corp. v. Muna, 625 P.2d 690, 696 (Utah 1981), the Utah Supreme Court recognized that a trade secret is "a type of intellectual property, in effect, a property right in discovered knowledge." (Emphasis added). See Leo Silfen, Inc., v. Cream, 29 N.Y.2d 387, 278 N.E.2d 636, 328 N.Y.S.2d 423 (1972) (court held that customer lists may be protected as trade secrets where the customers are not known in the trade, and are discoverable only by extraordinary efforts); Abbott Laboratories v. Norse Chemical Corp. 33 Wis. 2d 445, 147 N.W. 2d 529, 538 (1967) (court held that customer lists may be protected as trade secrets where the list is secret and not readily duplicated by independent means); Olschewski v. Hudson, 262 P. 43 (Cal. App. 1927) (court held that "a list of laundry customers is a property right which may be appropriately protected, but it is not a tangible right" (Emphasis added)).

In the present case both the Company and the list brokers treated the mailing lists as if they were intangible property. First, the seller restricted the taxpayer's use of the information sold, but was not concerned about reuse of the physical object sold, namely the magnetic tape, once the information was erased. (Tr. 12-13, 47.) Second, the value of the tangible means of exchange was slight in comparison to the value of the list, and was separately stated and charged on the bill to the taxpayer. (Tr. 47, 49.) Third it was possible to obtain the information by alternate means. The Company specified, as a matter of convenience, the method by which it preferred to receive the lists of names.

Since the mailing lists are generally recognized as intangible property in legal and business contexts generally, they ought to be treated consistently by the taxing authority. See Fingerhut, 258 N.W.2d at 609.

IV.

UTAH CODE ANN. § 59-16-3 MUST BE
STRICTLY CONSTRUED AND AMBIGUITIES
RESOLVED IN FAVOR OF THE TAXPAYER.

The essential difficulty in this case is that section 59-16-3 simply was not designed for the computer age. Notions of tangibility, while perhaps once useful in determining what should be taxed, are outmoded in the context of transfers of information by magnetic computer tape. Utah Code Ann. §

59-16-3, at best, is ambiguous and, being so, should be resolved in favor of the taxpayer. The rule in Utah, as in other jurisdictions, is that "statutes imposing taxes and prescribing tax procedures should generally be construed favorably to the taxpayer and strictly against the taxing authority." Builders Components Supply Co. v. Cockayne, 22 Utah 2d 172, 450 P.2d 97, 99 (1969). See also Continental Telephone Company of Utah v. State Tax Commission, 539 P.2d 447, 450 (Utah 1975).

The court in Spencer Gifts, in considering the ambiguities of the statute under which it was urged that mailing lists ought to be taxed as tangible personal property, held that the statute must be resolved in favor of the taxpayer. 440 A.2d at 120. The opinion considered the difficulty in resolving the questions of tangibility at issue:

It is not sensible to apply concepts such as tangible and intangible, applicable to a very different world, to the computer world. Even the distinction between property and services is not helpful here where definitions appropriate to the subject matter of the tax are needed. Significant tax burdens should not be predicated on largely irrelevant concepts developed in different times for different purposes.

Id. (emphasis added).⁵ Other courts have similarly ruled

⁵The court stated in conclusion that "[i]t doesn't make sense to predicate significant consequences on the outcome of debates regarding largely irrelevant concepts developed in different times for different purposes." 440 A.2d at 104 (quoting Wessel, Freedom's Edge, "Controlling the Computer," 126 (1974)).

that tax statutes must be resolved in favor of taxpayers where the issues involved transfers of information by magnetic tapes or cards, such as software. See First National Bank of Springfield v. Dept. of Revenue, 85 Ill.2d 84, 421 N.E.2d 175, 177 (1981); First National Bank of Fort Worth v. Bullock, 584 S.W.2d 548, 551 (Tex. Civ. App. 1979); Jamesville Data Center, Inc., 84 Wis. 2d 341, 267 N.W.2d 656, 658 (1978).

The pertinent Utah statute should similarly be resolved against the taxing authority and in favor of the Company.

CONCLUSION

Because the taxpayer purchased information resulting from a service rendered by mailing list brokers, which was separate and distinct from the tape and the labels by which the information was communicated, this Court should hold that the purchases by the taxpayer during the period at issue were not taxable and that the taxpayer is entitled to a refund of \$7,750.00. Any ambiguities in the statute should be resolved in favor of the taxpayer.

ADDENDUM

The taxpayer has appended to this brief copies of the following documents:

1. Lower court's Memorandum Decision dated May 12, 1987 (R. 103-10).

2. Lower court's Order Disposing of Reciprocal
Motions for Summary Judgment and Affirming Decision of Utah
State Tax Commission. (R. 120-25.)

DATED this 16th day of May, 1988.

VAN COTT, BAGLEY, CORNWALL & McCARTHY
Steven D. Woodland
R. Stephen Marshall

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CERTIFICATE OF MAILING

I hereby certify that I caused four true and correct copies of the within and foregoing Brief to be mailed, postage prepaid, this 17th day of May, 1988, to the following:

David L. Wilkinson
Attorney General
Stephen G. Schwendiman
Division Chief
Michael F. Skolnick
Assistant Attorney General
Tax and Business Regulations Division
130 State Capitol
Salt Lake City, Utah 84114

RS Marshall

MAY 12 1987

IN THE THIRD JUDICIAL DISTRICT COURT
IN AND FOR SALT LAKE COUNTY, STATE OF UTAH

H. Dixon Hixley, Clerk 3rd Dist. Court
E. Thompson
Deputy Clerk

MARK O. HAROLDSON,
dba MARKO ENTERPRISES,
a Utah Corporation,

Plaintiff,

v.

UTAH STATE TAX COMMISSION,

Defendant.

MEMORANDUM DECISION

CIVIL NO. C85-3384

Before the court are reciprocal Motions for Summary Judgment wherein this court is asked to review a decision of the Utah State Tax Commission regarding the assessment of "use taxes." The matter came before the court on a special setting for argument of the issues. Prior to the hearing on the matter, both parties submitted Memoranda in support of their respective positions. The court has also received the complete record from the Utah State Tax Commission which has been marked as Court's Exhibit One and made a part of the court's official file. After hearing argument of counsel, the court took the matter under advisement to further consider the authorities cited by the respective parties and to further examine the record from the Utah State Tax Commission. The material facts in this case are not in dispute. The court has now had an opportunity to consider this matter and being otherwise fully advised, enters the following Memorandum Decision.

The plaintiff has appealed from a decision of the Utah State

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Tax Commission which assessed use taxes against the value of mailing lists used in the course of his business. The issue to be resolved is whether the sales of these lists, in the form of printed sheets and computer tapes, are subject to sales and use taxes as tangible personal property. The plaintiff argues that the transactions involved the sale of services, and that any transfer of tangible personal property was incidental to the sale of intangible property. The Tax Commission takes the position that any services provided were incidental to the sale of tangible personal property. It is the opinion of the court that these lists are tangible personal property, and that their sale or use is subject to taxation.

Both parties have moved for summary judgment, and the undisputed facts, briefly stated, are as follows. The plaintiff is a Utah corporation engaged in the marketing of real estate information. As a marketing technique, the plaintiff purchases mailing lists from mailing list brokers to use in direct mail advertising. These lists are generated by the brokers based on the target market specified by the plaintiff. Such factors as age, sex, income level, family status, and investment history are used to define those individuals selected to receive the plaintiff's advertising. The completed lists are delivered to the plaintiff for a one-time usage,¹ and they are contained in

¹Mailing lists are commonly "salted" with names of employees of the broker to detect unauthorized use of the list.

either printed sheets or computer tapes. The printed sheets are converted into mailing labels by a machine that cuts the names from the sheet and gums them, and the computer tapes are read by word processing equipment that prints the labels. Approximately thirty-five percent of the lists purchased by the plaintiff were on computer tape, and sixty-five percent were on printed sheets. Of the \$154,844.10 paid by the plaintiff for these lists, the Tax Commission assessed a use tax deficiency of \$19,711.21, plus interest and penalty. The plaintiff has paid about \$15,000, and approximately \$7,750 remains in dispute.

This inquiry focuses on the language of the Use Tax Act of 1937, Utah Code Ann. § 59-16-1, et seq. (1953). The scope of the use tax is defined in § 59-16-3(a) (Supp. 1986), which states that an excise tax shall be levied upon the "storage, use, or other consumption of tangible personal property" Tangible personal property is defined in the Utah Sales and Tax Book of Regulations as "all tangible or corporeal things . . . capable of being possessed or exchanged." Tax Reg. A12-02-S26. Although this definition provides little assistance, it is clear that tangible personal property does not include such intangibles as services.

The line of demarcation between tangible and intangible property is not always clear. Courts grappling with this question have examined the "real object" sought by the buyer to determine whether the buyer's object was to obtain an act by an

individual chosen for his skill, or whether it was the buyer's object to obtain a product not dependent on the skills of the individual providing it. Accountant's Computer Serv. v. Koysdar, 298 N.E.2d 519, 527, 35 Ohio St.2d 120 (1973). If the true object of the contract is the service per se, the transaction is not subject to tax even though some tangible personal property is transferred incidental to the transaction.

The problem is that many transactions involve an inseparable combination of services and tangible personal property. Accountant's involved three cases that were disposed of in the following manner:

1. A data processing firm was supplied by the taxpayer with raw data. The firm transcribed in onto punch cards, and the cards were sorted, classified and arranged. The cards were then delivered to the taxpayer. This transaction was found to be a taxable sale of a product accompanied by an inconsequential personal service. Id. at 527-28.

2. The additional service of data analysis transformed the transaction to a nontaxable service transaction. The delivery of printed matter in the form of a report was determined to be the inconsequential element of the transaction. Id. at 528.

3. A market research company compiled statistical data and analyzed it for presentation to clients. Again the court found a service transaction that was exempt from taxation, stating "it

was the intellectual and manual personal efforts . . . that was sought . . . not the inconsequential tangible personal property which was transferred, for purposes of communication, as an incidental element without a separate charge." Id. at 520.

Other jurisdictions, including Utah, have applied this reasoning in different factual contexts. Thorne and Wilson, Inc. v. Utah State Tax Commission, 681 P.2d 1237, 1238 (Utah 1984) ("it is the substance of the transaction and not the property actually transferred that controls."); Old West Realty v. Idaho State Tax Commission, 716 P2. 1318 (Idaho 1986) (transfer of multiple listing books from listing service to real estate broker was a taxable transaction). In the present case it seems clear that the generation of the lists for the taxpayer involved little expertise, marketing skill or analysis on the part of the broker. Although the plaintiff did consult the mailing list broker to a limited extent, the purpose was to define the parameters of the desired list, and this was done primarily by the plaintiff. The court finds that this service was incidental to the generation of the lists, which were the real object of the transaction. There still remains the question of whether these sales involved the transfer of tangible or intangible personal property.

Regarding the printed sheets, it is clear that a sale of tangible personal property has occurred. These lists were processed by a machine that converted them to gummed labels, and

they were affixed to the taxpayer's mailings. The tax imposed on the use of these lists was proper. Fingerhut Products Co. v. Commissioner of Revenue, 258 N.W.2d 606 (Minn. 1977) (sale of mailing lists in the form of gummed labels constituted taxable sale of tangible personal property); Matter of Alan Drey Co. v. State Tax Commission, 67 A.D.2d 1055, 413 N.Y.S.2d 516 (1979) (same).

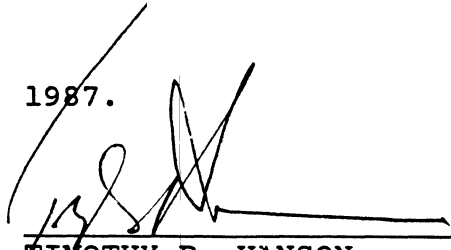
Turning to the transfer of the computer tapes a more difficult question is presented. Courts have distinguished gummed mailing labels from computer tapes in refusing to find computer tapes tangible personal property. Mertz v. State Tax Commission, 89 A.D.2d 396, 456 N.Y.S.2d 501, 503 (1982) ("the tapes . . . were merely the medium by which the information that was the essence of the transaction was transmitted."); Spencer Gifts, Inc. v. Taxation Div. Director, 182 N.J. Super 179, 440 A.2d 104, 117 (N.J. Tax 1981) ("The leasing of computer information is not the leasing or sale of tangible personal property and is not taxable."); Fingerhut Products Co. v. Commissioner of Revenue, 258 N.W.2d 606, 610 (Minn. 1977) ("the use of the tangible medium of typed mailing lists is merely incidental to the use of the incorporeal information contained in those lists.").

It is the opinion of this court that these prior cases have made a distinction where there is no practical difference. Whether the information is supplied on gummed labels, typed

lists, or computer tape, an item of tangible personal property is transferred, and the transaction is taxable. Although the information contained by the tapes is incorporeal, it cannot be possessed without some item of tangible personal property, and it is of no value to the user until it is transformed into a tangible mailing label. It is not simply the intangible information that the taxpayer seeks, but the list in the form of mailing labels. The value of the media is determined by the information it contains, and in this respect the sale of information on a computer tape is no different from the sale of the same information contained in a book. The ruling of the Tax Commission is affirmed.

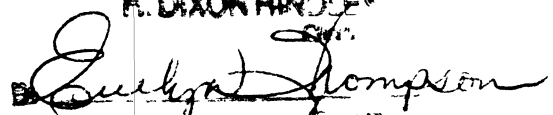
Counsel for the Tax Commission is requested to prepare an appropriate Order in accordance with this Memorandum Decision and submit the same to the court for review and signature as provided in the local rules of practice.

DATED this 12 day of May, 1987.


TIMOTHY R. HANSON
DISTRICT COURT JUDGE


ATTEST

R. DIXON HINDLE
CLERK



CERTIFICATE OF MAILING

I hereby certify that a true and correct copy of the foregoing Memorandum Decision was mailed postage prepaid to the following attorneys on the 13 day of May, 1987.

A handwritten signature in cursive script, appearing to read "Evelyn Thompson", written in dark ink.

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P.O. Box 4000
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MAY 12 1987

IN THE THIRD JUDICIAL DISTRICT COURT
IN AND FOR SALT LAKE COUNTY, STATE OF UTAH

F. Dixon Haggerty, Clerk, 3rd Dist. Court

Deputy Clerk

MARK O. HAROLDSON,
dba MARKO ENTERPRISES,
a Utah Corporation,

Plaintiff,

v.

UTAH STATE TAX COMMISSION,

Defendant.

MEMORANDUM DECISION

CIVIL NO. C85-3384

Before the court are reciprocal Motions for Summary Judgment wherein this court is asked to review a decision of the Utah State Tax Commission regarding the assessment of "use taxes." The matter came before the court on a special setting for argument of the issues. Prior to the hearing on the matter, both parties submitted Memoranda in support of their respective positions. The court has also received the complete record from the Utah State Tax Commission which has been marked as Court's Exhibit One and made a part of the court's official file. After hearing argument of counsel, the court took the matter under advisement to further consider the authorities cited by the respective parties and to further examine the record from the Utah State Tax Commission. The material facts in this case are not in dispute. The court has now had an opportunity to consider this matter and being otherwise fully advised, enters the following Memorandum Decision.

The plaintiff has appealed from a decision of the Utah State

Tax Commission which assessed use taxes against the value of mailing lists used in the course of his business. The issue to be resolved is whether the sales of these lists, in the form of printed sheets and computer tapes, are subject to sales and use taxes as tangible personal property. The plaintiff argues that the transactions involved the sale of services, and that any transfer of tangible personal property was incidental to the sale of intangible property. The Tax Commission takes the position that any services provided were incidental to the sale of tangible personal property. It is the opinion of the court that these lists are tangible personal property, and that their sale or use is subject to taxation.

Both parties have moved for summary judgment, and the undisputed facts, briefly stated, are as follows. The plaintiff is a Utah corporation engaged in the marketing of real estate information. As a marketing technique, the plaintiff purchases mailing lists from mailing list brokers to use in direct mail advertising. These lists are generated by the brokers based on the target market specified by the plaintiff. Such factors as age, sex, income level, family status, and investment history are used to define those individuals selected to receive the plaintiff's advertising. The completed lists are delivered to the plaintiff for a one-time usage,¹ and they are contained in

¹Mailing lists are commonly "salted" with names of employees of the broker to detect unauthorized use of the list.

either printed sheets or computer tapes. The printed sheets are converted into mailing labels by a machine that cuts the names from the sheet and gums them, and the computer tapes are read by word processing equipment that prints the labels. Approximately thirty-five percent of the lists purchased by the plaintiff were on computer tape, and sixty-five percent were on printed sheets. Of the \$154,844.10 paid by the plaintiff for these lists, the Tax Commission assessed a use tax deficiency of \$19,711.21, plus interest and penalty. The plaintiff has paid about \$15,000, and approximately \$7,750 remains in dispute.

This inquiry focuses on the language of the Use Tax Act of 1937, Utah Code Ann. § 59-16-1, et seq. (1953). The scope of the use tax is defined in § 59-16-3(a) (Supp. 1986), which states that an excise tax shall be levied upon the "storage, use, or other consumption of tangible personal property . . ." Tangible personal property is defined in the Utah Sales and Tax Book of Regulations as "all tangible or corporeal things . . . capable of being possessed or exchanged." Tax Reg. A12-02-S26. Although this definition provides little assistance, it is clear that tangible personal property does not include such intangibles as services.

The line of demarcation between tangible and intangible property is not always clear. Courts grappling with this question have examined the "real object" sought by the buyer to determine whether the buyer's object was to obtain an act by an

individual chosen for his skill, or whether it was the buyer's object to obtain a product not dependent on the skills of the individual providing it. Accountant's Computer Serv. v. Koysdar, 298 N.E.2d 519, 527, 35 Ohio St.2d 120 (1973). If the true object of the contract is the service per se, the transaction is not subject to tax even though some tangible personal property is transferred incidental to the transaction.

The problem is that many transactions involve an inseparable combination of services and tangible personal property. Accountant's involved three cases that were disposed of in the following manner:

1. A data processing firm was supplied by the taxpayer with raw data. The firm transcribed in onto punch cards, and the cards were sorted, classified and arranged. The cards were then delivered to the taxpayer. This transaction was found to be a taxable sale of a product accompanied by an inconsequential personal service. Id. at 527-28.

2. The additional service of data analysis transformed the transaction to a nontaxable service transaction. The delivery of printed matter in the form of a report was determined to be the inconsequential element of the transaction. Id. at 528.

3. A market research company compiled statistical data and analyzed it for presentation to clients. Again the court found a service transaction that was exempt from taxation, stating "it

was the intellectual and manual personal efforts . . . that was sought . . . not the inconsequential tangible personal property which was transferred, for purposes of communication, as an incidental element without a separate charge." Id. at 520.

Other jurisdictions, including Utah, have applied this reasoning in different factual contexts. Thorne and Wilson, Inc. v. Utah State Tax Commission, 681 P.2d 1237, 1238 (Utah 1984) ("it is the substance of the transaction and not the property actually transferred that controls."); Old West Realty v. Idaho State Tax Commission, 716 P2. 1318 (Idaho 1986) (transfer of multiple listing books from listing service to real estate broker was a taxable transaction). In the present case it seems clear that the generation of the lists for the taxpayer involved little expertise, marketing skill or analysis on the part of the broker. Although the plaintiff did consult the mailing list broker to a limited extent, the purpose was to define the parameters of the desired list, and this was done primarily by the plaintiff. The court finds that this service was incidental to the generation of the lists, which were the real object of the transaction. There still remains the question of whether these sales involved the transfer of tangible or intangible personal property.

Regarding the printed sheets, it is clear that a sale of tangible personal property has occurred. These lists were processed by a machine that converted them to gummed labels, and

they were affixed to the taxpayer's mailings. The tax imposed on the use of these lists was proper. Fingerhut Products Co. v. Commissioner of Revenue, 258 N.W.2d 606 (Minn. 1977) (sale of mailing lists in the form of gummed labels constituted taxable sale of tangible personal property); Matter of Alan Drey Co. v. State Tax Commission, 67 A.D.2d 1055, 413 N.Y.S.2d 516 (1979) (same).

Turning to the transfer of the computer tapes a more difficult question is presented. Courts have distinguished gummed mailing labels from computer tapes in refusing to find computer tapes tangible personal property. Mertz v. State Tax Commission, 89 A.D.2d 396, 456 N.Y.S.2d 501, 503 (1982) ("the tapes . . . were merely the medium by which the information that was the essence of the transaction was transmitted."); Spencer Gifts, Inc. v. Taxation Div. Director, 182 N.J. Super 179, 440 A.2d 104, 117 (N.J. Tax 1981) ("The leasing of computer information is not the leasing or sale of tangible personal property and is not taxable."); Fingerhut Products Co. v. Commissioner of Revenue, 258 N.W.2d 606, 610 (Minn. 1977) ("the use of the tangible medium of typed mailing lists is merely incidental to the use of the incorporeal information contained in those lists").

It is the opinion of this court that these prior cases have made a distinction where there is no practical difference. Whether the information is supplied on gummed labels, typed

lists, or computer tape, an item of tangible personal property is transferred, and the transaction is taxable. Although the information contained by the tapes is incorporeal, it cannot be possessed without some item of tangible personal property, and it is of no value to the user until it is transformed into a tangible mailing label. It is not simply the intangible information that the taxpayer seeks, but the list in the form of mailing labels. The value of the media is determined by the information it contains, and in this respect the sale of information on a computer tape is no different from the sale of the same information contained in a book. The ruling of the Tax Commission is affirmed.

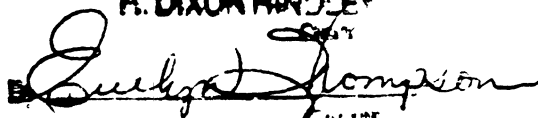
Counsel for the Tax Commission is requested to prepare an appropriate Order in accordance with this Memorandum Decision and submit the same to the court for review and signature as provided in the local rules of practice.

DATED this 12 day of May, 1987.


TIMOTHY R. HANSON
DISTRICT COURT JUDGE

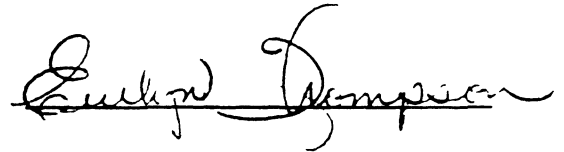
ATTEST

R. DIXON HINDLEY


R. DIXON HINDLEY
CLERK

CERTIFICATE OF MAILING

I hereby certify that a true and correct copy of the foregoing Memorandum Decision was mailed postage prepaid to the following attorneys on the 13 day of May, 1987.

A handwritten signature in cursive script, appearing to read "Eugene Thompson", written over a horizontal line.

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NOV 12 1987

H. Dixon Hindey, Clerk Pro Dist Court
By [Signature]
Deputy Clerk

IN THE THIRD JUDICIAL DISTRICT COURT
IN AND FOR SALT LAKE COUNTY, STATE OF UTAH

MARK O. HAROLDSSEN,	:	
dba MARKO ENTERPRISES,	:	ORDER DISPOSING OF
a Utah Corporation,	:	RECIPROCAL MOTIONS FOR
	:	SUMMARY JUDGMENT AND
Plaintiff,	:	AFFIRMING DECISION OF
	:	UTAH STATE TAX COMMISSION
v.	:	
	:	Civil No. C85-3384
UTAH STATE TAX COMMISSION,	:	(tax case)
	:	
Defendant.	:	Judge Timothy R. Hanson

POSTURE OF THE CASE

Reciprocal Motions for Summary Judgment came on for hearing before the Honorable Timothy R. Hanson on the 14th day of April, 1987. R. Stephen Marshall and Steven D. Woodland appeared on behalf of the plaintiff, Mark O. Haroldsen, Inc., Mary Beth Walz, Assistant Attorney General, appeared on behalf of the defendant, the Utah State Tax Commission. Both parties submitted Memoranda in support of their respective positions. Pursuant to the

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stipulation of the parties, the complete record of the formal hearing before the Utah State Tax Commission was placed before the court in lieu of a trial. Exhibits were submitted and received. Arguments of counsel were presented.

FINDINGS OF FACT

1. The plaintiff is a Utah corporation engaged in the marketing of real estate information. As a marketing technique, the plaintiff purchases mailing lists from mailing list brokers for use in direct mail advertising.

2. The lists are marketed by a brokerage agent who narrows the raw lists according to a customer's specific requests in order to create a list of names targeted towards a particular market. Such factors as age, sex, income level, family status, and investment history are used to define those individuals selected to receive the customer's advertising.

3. The lists consist of printed sheets or computer tapes and are delivered to the plaintiff for a one-time usage. The printed sheets are converted into mailing labels by a machine that cuts the names from the sheet and gums them, and the computer tapes are read by word processing equipment that prints the labels. The plaintiff purchased approximately thirty-five percent of the lists on computer tape and sixty-five percent on printed sheets and paid a total of \$154,844.10 for the use of these lists.

4. The Tax Commission assessed a use tax deficiency of \$19,711.21, plus interest and penalty. The plaintiff has paid about \$15,000.00 and approximately \$7,750.00 remain in dispute.

ANALYSIS OF CASE LAW AND APPLICABLE UTAH STATUTES

1. The Use Tax Act of 1937, Utah Code Ann. §59-16-3(a) (Supp. 1986) states that an excise tax shall be levied upon the "storage, use, or other consumption of tangible personal property..."

2. Tangible personal property is defined in the Utah Sales and Tax Book of Regulations as "all tangible or corporeal things...capable of being possessed or exchanged." Tax Reg. A12-02-S26. Tangible personal property does not include such intangibles as services.

3. Courts apply the "real object" test to determine whether the buyer's object was to obtain an act by an individual chosen for his skill, or whether the buyer sought a product not dependent on the skills of the individual providing it.

Accountant's Computer Serv. v. Kosydar, 35 Ohio 2d 120, 298 N.E.2d 519, 527 (1973). The Utah Supreme Court has also applied this reasoning in a different factual context. Thorne and Wilson, Inc. v. Utah State Tax Commission, 681 P.2d 1237, 1238 (Utah 1984) ("[I]t is the substance of the transaction and not the property actually transferred that controls"). Old West Realty v. Idaho State Tax Commission, 716 P.2d 1318 (Idaho 1986)

(holding that a transfer of multiple listing books from a listing service to a real estate broker was a taxable transaction).

4. In the present case, the generation of the lists involved little expertise, marketing skill or analysis on the part of the broker. The function of defining the parameters of the desired list was done primarily by the plaintiff. The service was incidental to the generation of the lists, which were the real object of the transaction.

5. The printed sheets constitute tangible personal property. Fingerhut Products Co. v. Commissioner of Revenue, 258 N.W.2d 606 (Minn. 1977).

6. Although some courts distinguish printed sheets from computer tapes by saying that the latter is nontangible, these cases have made a distinction where there is no practical difference. The information contained by the computer tapes, while incorporeal, is valueless until possessed in some tangible form. The value of the media is determined by the information it contains, and in this respect, the sale of information on a computer tape is no different from the sale of the same information contained in a book.

CONCLUSIONS OF LAW

1. The mailing lists in the form of printed sheets and in the form of computer tapes are tangible personal property within the meaning of Tax Reg A12-02-S26

2. The service provided by the broker was incidental to the transaction to acquire the mailing lists.

3. The mailing lists were the "real object" of the transaction.

4. The sale or use of the mailing lists is subject to taxation as stated in U.C.A. §59-16-3(a) (Supp. 1986).

5. The decision of the Utah Tax Commission is affirmed.

ORDER

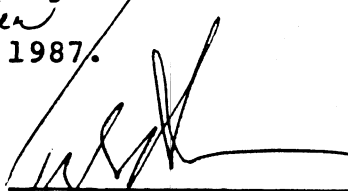
1. Defendant's Motion for Summary Judgment is granted and the final ruling of the Utah State Tax Commission is affirmed.

2. Plaintiff's Motion for Summary Judgment is denied.

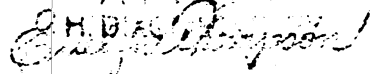
3. The appealed use tax assessment in the amount of roughly \$7,750.00 and the accompanying interest imposed by the Utah State Tax Commission against the plaintiff will become final after the period for appeal from this order has expired.

4. This case is dismissed with prejudice.

DATED this 12 day of ^{November}~~October~~, 1987.


TIMOTHY R. HANSON
District Court Judge

ATTEST



By _____
Deputy Clerk

MAILING CERTIFICATE

I hereby certify that I mailed a true and correct copy of the foregoing document to R. Stephen Marshall at 50 South Main, Suite 1600, P.O. Box 45340, Salt Lake City, Utah 84145, postage pre-paid, this 23 day of October, 1987.

R. Schiefel