07-0054
SALES AND USE TAX
TAX YEARS: 2002, 2003, 2004 & 2005
SIGNED 04-05-2010
COMMISSIONERS: R. JOHNSON, D. DIXON, R. CRAGUN
RECUSED: M. JOHNSON
GUIDING DECISION

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER, Petitioner, v. AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION, Respondent.	**FINDINGS OF FACT, CONCLUSIONS OF LAW, AND FINAL DECISION** Appeal No. 07-0054 Account No. ##### Tax Type: Sales and Use Tax Audit Period: 01/01/02 – 12/31/05 Judge: Chapman

Presiding:
Michael J. Cragun, Commissioner
Kerry Chapman, Administrative Law Judge

Appearances:
For Petitioner: PETITIONER REP., from PETITIONER
For Respondent: RESPONDENT REP. 1, Assistant Attorney General
RESPONDENT REP. 2, from Auditing Division
RESPONDENT REP. 3, from Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for a Formal Hearing on March 1, 2010. Based upon the evidence and testimony presented by the parties, the Tax Commission hereby makes its:

FINDINGS OF FACT

1. The tax at issue is sales and use tax.

2. The audit period at issue is January 1, 2002 through December 31, 2005.

3. Auditing Division ("Division") has issued several Statutory Notices to PETITIONER ("PETITIONER") in this matter. On July 1, 2008, the Division issued a 2nd Amended Utah Tax Audit Summary ("2nd Amended Audit Summary"), in which it imposed additional sales and use tax in the amount of $$$$$, additional municipal telecommunications license tax of $$$$$ and interest of $$$$$ (computed through March 31, 2010), for a total assessment of $$$$$. Exhibit R-1.

4. The 2nd Amended Audit Summary appears to be comprised of ten separate schedules. The parties resolved the amounts associated with the first nine schedules prior to the hearing. Remaining at issue is the tax assessed under Schedule 10, which concerns the Division's determination that PETITIONER provided ITEMS and accessories (collectively referred to as "ITEMS") free of charge to customers who signed a AGREEMENT to purchase ITEM service ("SERVICE") from PETITIONER, yet failed to pay use tax on its costs for the ITEMS. No evidence was submitted to show that the taxes assessed in Schedule 10 were asserted after the first notice of deficiency. The unreported taxable purchases shown on Schedule 10 total $$$$$, which equates to approximately $$$$$ of additional tax, plus interest. Exhibit R-2; Testimony of RESPONDENT REP. 2.

5. PETITIONER is a ITEM service provider. It also sells ITEMS.

6. The taxes assessed under Schedule 10 concern ITEMS that PETITIONER marketed as "free." For circumstances where ITEMS were marketed as "free," customers signed up for SERVICE and received invoices that are divided into two sections, the first section relating to the ITEM the customer received and the second section relating to the SERVICE plan that was purchased. Exhibit R-3.

7. In the ITEM section of an invoice, the "regular price" of the ITEM the customer received is shown (e.g., $$$$$). The invoice also shows that the charge for the ITEM is $$$$$ and specifically indicates that the "amount due" for the ITEM is $$$$$. Exhibit R-3.

8. In the SERVICE plan section of the invoice, information about the type of plan purchased is shown (e.g., "2 YR CONSUMER AGREEMENT PLAN"). However, the invoices generally do not show the price the customer is paying for the SERVICE. Exhibit R-3.

9. PETITIONER purchases all ITEMS tax-free, including the ITEMS at issue that it marketed as "free" and that it invoiced for a $$$$$ "amount due."

10. The Division contends that PETITIONER provided the ITEMS at issue as an inducement for PETITIONER's customers to purchase SERVICE and that the purchase prices of the SERVICE did not include the ITEMS. As a result, the Division contends that PETITIONER consumed the ITEMS at issue and owes use tax on them. For these reasons, the Division asks the Commission to sustain the additional tax imposed under Schedule 10.

11. PETITIONER argues that it did not give the ITEMS at issue away for free or as an inducement for customers to purchase SERVICE. It argues that the ITEMS were included in the purchase price of the taxable SERVICE it sold. As a result, it argues that it was entitled to purchase the ITEMS tax-free under the resale exemption and that it did not use or consume the ITEMS. PETITIONER also argues that it would be a violation of the equal protection and the uniform operation of laws provisions to impose a use tax on the ITEMS at issue. On these bases, PETITIONER asks the Commission to find that it does not owe the tax imposed under Schedule 10.

12. For any ITEM that PETITIONER did not market as "free" and did not invoice with a $$$$$ "amount due," PETITIONER collected and remitted sales tax on the price it charged for the ITEM. The Division did not assess any use tax on the ITEMS that PETITIONER sold to its customers for at least $$$$$ and on which it collected and remitted sales tax.

13. The Division submitted four versions of service agreements that PETITIONER entered into with its customers during the audit period. Exhibits R-4, R-5, R-6 and R-7. Although the

agreements make some references to ITEMS, they do not specify that the purchase price of the SERVICE include the ITEMS at issue.

14. All four of the service agreements include provisions describing the timeframes within which a customer may cancel the SERVICE without incurring a termination fee and return ITEMS for a full refund. All of the service agreements provide that a $$$$$ fee is due for early termination of service contracts. PETITIONER claims that the early termination fee is charged to reimburse PETITIONER, at least in part, for ITEMS that the customers received at a reduced price or that they invoiced for a $$$$$ "amount due." However, three of the agreements provide that if a customer cancels service within two years, the customer agrees to pay "an early termination fee of $$$$$ for each line of service" that is cancelled. Exhibits R-4, R-5 and R-7. This provision suggests that the early termination fee may be dependent on the number of lines cancelled, not on the number of ITEMS that a customer may have received or the price at which the ITEMS were received.

15. PETITIONER submitted two documents in support of its argument that the early termination fee provisions in its service contracts are intended to recoup the cost of ITEMS that it provided at a discount or that it invoiced for a $$$$$ "amount due." Exhibit P-1 and P-2. PETITIONER REP., however, declined to point out to the Commission those specific portions of the two documents that were relevant to or supported the arguments he made on behalf of PETITIONER.

16. The first document PETITIONER submitted is a June 6, 2006 *Ex Parte* paper that PERSON 1 .submitted to the FEDERAL COMMISSION ("FCC") in regards to *In the Matter of CTIA Petition for Expedited Declaratory Ruling on Early Termination Fees*, WT Docket No. 05-194. Exhibit P-1. In his paper, PERSON 1specifically refers to "customer equipment costs" separately from "customer acquisition costs and other fixed costs of service." He further states that "[c]onsumers with term contacts and [early termination fees] sometimes receive greater discounts on purchasing (X) than consumers with

prepaid or hybrid plans. Nevertheless, the primary purpose of the [early termination fee] appears to be related to customer acquisition and retention costs." Exhibit P-1, p. 27. As a result, it appears that PERSON A believes that early termination fees are primarily related to customer acquisition and retention costs, not to customer equipment costs.

17. In addition, PERSON 1 stated that a prohibition or limitation of early termination fee provisions in service contracts might lead to increased initialization or activation fees or to increased monthly rates. Exhibit P-1, pp. 37, 40. However, he did not indicate that the elimination of early termination fees might lead to increased charges for ITEMS that a carrier may currently provide at a discount or for free. For these reasons, it appears from PERSON 1's paper that early termination fees are intended to recoup costs other than those associated with ITEMS that PETITIONER provides at a discount or invoices for a $$$$$ "amount due."

18. The second document PETITIONER submitted, which is entitled "PETITIONER Corporation Comments" and dated August 5, 2005, was submitted by PETITIONER in regards to two FEDERAL COMMISSION matters concerning early termination fees docketed as WT Docket No. 05-193 and WT Docket No. 05-194. Exhibit P-2. In this document, PERSON 2, PETITIONER's Vice President of (WORDS REMOVED), asserts that many customers chose term plans with early termination fees because of the benefits that they receive from such plans, including "heavily discounted phones." Exhibit P-2, p. ii. She even states that the elimination of early termination fees could reduce or eliminate the amount of subsidy provided on the "handset." Exhibit P-2, p. 2, ft. 3. However, she does not specifically state that early termination fees are intended to recoup PETITIONER's costs of ITEMS. In addition, she stated that the FEDERAL COMMISSION "has already found that subsidized (X) are 'a legitimate promotional strategy. . . .'" (citing *CMRS Resale Reconsideration Order,* 14 FEDERAL COMMISSIONR cd 16340, 16454 ¶ 29

(1999). Exhibit P-2, pp. 2-3. Giving away ITEMS for free as an incentive for customers to purchase SERVICE would appear to qualify as a promotional strategy.

19. In addition, PERSON 2 cites a number of authorities that conclude that early termination fees impact the cost of services and result in reduced rates. Exhibit P-2, p. 15, ft. 58; p. 16; and p. 21, ft. 80. None of these authorities, however, indicate that the purpose of early termination fees is to recoup costs associated with a discounted or free ITEM. For these reasons, it appears from this document, as well, that early termination fees are related to costs other than the costs associated with ITEMS provided at discount or invoiced with a $$$$$ "amount due."

20. The Commission asked PETITIONER REP. a number of questions in an attempt to discover how early termination fees worked in certain situations or why PETITIONER advertised ITEMS for "free" if the ITEMS are, as PETITIONER argues, included instead in the prices charged for SERVICE. In most instances, PETITIONER REP. indicated that he did not know. For example, when asked why PETITIONER advertised ITEMS for "free," he answered that he did not know because he was not in the "marketing department." In addition, when asked if a customer's SERVICE rates would go down after a SERVICE PLAN had ended to account for the costs of a ITEM having been recouped, he stated that he did not know.

21. PETITIONER REP. admitted that a SERVICE customer can buy a ITEM separately from a SERVICE plan. However, when asked if a different SERVICE rate would apply to a SERVICE customer who already owned a ITEM (i.e., where PETITIONER would have no need to "recoup" the cost of a discounted ITEM), he stated that he did not know. When asked if the early termination fee provisions apply to a SERVICE customer who already owned a ITEM (i.e., where PETITIONER would again have no need to "recoup" the cost of a discounted ITEM), he stated that he did not know.

22. PETITIONER collects and remits sales tax on its charges for SERVICE. A portion of the telecommunication services provided by PETITIONER is subject to Utah taxation, specifically intrastate service, while the portion associated with interstate service is not subject to Utah taxation. In its reports to the FCC, PETITIONER allocates 71.5% of its total SERVICE revenue in Utah to taxable intrastate services. It allocates the remaining 29.5% of the revenue to nontaxable interstate services. PETITIONER does not allocate any of its SERVICE revenue to ITEMS.

23. Given the information provided at the Formal Hearing, the purpose of the early termination fees in PETITIONER's SERVICE plan contracts is found to relate to costs other than those associated with ITEMS that PETITIONER provides to its (X) customers at a discount or that it invoices for a $$$$$ "amount due."

24. In addition, it is found that the evidence does not show that PETITIONER's prices for SERVICE include the ITEMS that it provides at a discount or that it invoices for a $$$$$ "amount due."

25. The ITEMS at issue, which PETITIONER provides to its SERVICE customers and invoices for a $$$$$ "amount due," are found to be provided to the customers free of charge as an inducement or an incentive for customers to purchase SERVICE.

APPLICABLE LAW

1. Throughout the audit period, Utah Code Ann. §59-12-103(1) (2005)[1] imposed a sales and use tax on the purchaser for amounts paid or charged for the following transactions:

> (a) retail sales of tangible personal property made within the state;
> . . . .
> (l) amounts paid or charged for tangible personal property if within this state the tangible personal property is:
> (i) stored;
> (ii) used; or
> (iii) consumed; . . .

1 The 2005 version of Utah law will be cited unless otherwise indicated.

2. UCA §59-12-102(90) defines "use" as follows:

> (a) "Use" means the exercise of any right or power over tangible personal property, a product transferred electronically, or a service under Subsection 59-12-103(1), incident to the ownership or the leasing of that tangible personal property, product transferred electronically, or service.
> (b) "Use" does not include the sale, display, demonstration, or trial of tangible personal property, a product transferred electronically, or a service in the regular course of business and held for resale.

3. UCA §59-12-104(25) provides an exemption from sales and use tax for "property purchased for resale in this state, in the regular course of business, either in its original form or as an ingredient or component part of a manufactured or compounded product[.]"

4. Utah Admin. Rule R865-19S-68 ("Rule 68")[2] provides guidance concerning gifts, as follows in pertinent part:

> A. Donors that give away ITEMS of tangible personal property as premiums or otherwise are regarded as the users or consumers of those ITEMS and the sale to the donor is a taxable sale. Exceptions to this treatment are ITEMS of tangible personal property donated to or provided for use by exempt organizations that would qualify for exemption under R865-19S-43 or R865-19S-54 if a sale of such ITEMS were made to them. An item given away as a sales incentive is exempt to the donor if the sale of that item would have been exempt. An example is prescribed medicine given away by a drug manufacturer.
> B. When a retailer making a retail sale of tangible personal property that is subject to tax gives a premium together with the tangible personal property sold, the transaction is regarded as a sale of both articles to the purchaser, provided the delivery of the premium is certain and does not depend upon chance.
> . . . .
> F. If a retailer agrees to furnish a free item in conjunction with the sale of an item, the sales tax applies only to the net amount due. If sales tax is computed on both ITEMS and only the sales value of the free item is deducted from the bill, excess collection of sales tax results. The vendor is then required to follow the procedure outlined in R865-19S-16 and remit any excess sales tax collected.
> . . . .

2 Although Rule 68 was amended and renumbered on July 1, 2005, the changes to the cited subsections were nonsubstantive.

5. UCA §59-1-1417 (2009) provides that the burden of proof is upon the petitioner in proceedings before the Commission, with limited exceptions as follows:

> In a proceeding before the commission, the burden of proof is on the petitioner except for determining the following, in which the burden of proof is on the commission:
>
> (1) whether the petitioner committed fraud with intent to evade a tax, fee, or charge;
>
> (2) whether the petitioner is obligated as the transferee of property of the person that originally owes a liability or a preceding transferee, but not to show that the person that originally owes a liability is obligated for the liability; and
>
> (3) whether the petitioner is liable for an increase in a deficiency if the increase is asserted initially after a notice of deficiency is mailed in accordance with Section 59-1-1405 and a petition under Part 5, Petitions for Redetermination of Deficiencies, is filed, unless the increase in the deficiency is the result of a change or correction of federal taxable income;
>
> (a) required to be reported; and
>
> (b) of which the commission has no notice at the time the commission mails the notice of deficiency.

DISCUSSION

PETITIONER contends that the "purchase price" it charges a customer for SERVICE is a bundled price that includes charges not only for SERVICE, but also for any ITEM that it may provide at a discount or that it invoices for a $$$$$ "amount due." However, the facts, as described earlier, indicate otherwise. PETITIONER provides the ITEMS at issue (i.e., those that it invoices for a $$$$$ "amount due") free of charge as an inducement for customers to purchase SERVICE. PETITIONER does not resell the ITEMS at issue in the regular course of business and, as a result, may not purchase them tax-free under Section 59-12-104(25). Instead, PETITIONER has "used" or "consumed" the ITEMS at issue pursuant to Rule 68(A) and Section 59-12-102(90) and is liable for use tax on the ITEMS pursuant to Section 59-12-103(1)(l). Accordingly, the Division's assessment in Schedule 10 is sustained.

This ruling is consistent with prior Commission rulings. The Commission has addressed similar circumstances in *USTC Appeal No. 02-1355* (Formal Hearing Decision Jun. 30, 2003). In *Appeal No.*

02-1355, the Commission considered a company that provided ITEMS free of charge to customers who purchased SERVICE. The company did not charge for the ITEM unless the customer reneged on the service contract. In this case, the Commission sustained the use tax that the Division had imposed on the price the company paid for each ITEM. The Commission found that under the circumstances, the company provided the ITEMS as an incentive to purchase SERVICE and that it owed use tax pursuant to Rule 68(A), as follows:

> When tangible personal property is purchased and given away at no charge for promotional advertising or as a gift, a prize or an incentive to buy another item, it is not purchased for resale. Under [Rule 68(A)], when a retailer, like Petitioner, offers an item to a customer at no additional charge on condition that the customer buys a service, that item is regarded as a gift or a promotional incentive. In that case, there is no taxable sale by the retailer, and the retailer's purchase of the item is taxable because the resale exemption does not apply.

As indicated earlier, Rule 68(A) applies to PETITIONER's circumstances, as well. PETITIONER employed a marketing strategy so that customers who purchased SERVICE could receive a free ITEM. PETITIONER's service plan contracts do not indicate that a ITEM is provided as part of the purchase of the plan. Invoices are given to customers who receive a free ITEM that indicate that the "amount due" for the ITEM is $$$$$. PETITIONER gives the ITEMS at issue away as an inducement or an incentive for customers to purchase its SERVICE. Although PETITIONER contends otherwise, the ITEMS are not a "premium," as described in Rule 68(B), or a "free item [furnished] in conjunction with the sale of [another] item" as described in Rule 68(F).

PETITIONER argues that *Appeal No. 02-1355* is inapplicable to the circumstances in this case because PETITIONER is a SERVICE provider and the company in *Appeal No. 02-1355* was not. The company in *Appeal No. 02-1355* sold SERVICE on behalf of SERVICE providers. This distinction, however, does not warrant a different result in the present case. In both instances, the Petitioning taxpayer offered free ITEMS as an inducement or incentive for customers to purchase SERVICE. Furthermore, the Commission

has issued private letter rulings in which it has specifically ruled that a SERVICE provider who provides ITEMS free of charge as an incentive to purchase its SERVICE owes use tax on the ITEM.[3]

In addition, PETITIONER's argument that the Commission's ruling in *USTC Appeal 00-0616* (Formal Hearing Decision Aug. 21, 2001) precludes the Commission from imposing use tax in the present case is unpersuasive. In *Appeal 00-0616*, the Division argued that a company selling ITEMS below cost, but for at least $$$$$, in connection with SERVICE was escaping "the payment of sales and use tax on the difference between the price at which [the company] purchases ITEMS and the discounted price at which it sells ITEMS." Because the company collected and remitted sales tax on the discounted price at which it sold the ITEMS, the Commission found that the company did not owe use tax on the difference.[4] *Appeal No. 00-0616* did not address the issue in the present case, specifically whether use tax is due on ITEMS provided free of charge.[5]

PETITIONER's argument that the ruling in *USTC Private Letter Ruling 95-032* (July 12, 1995) ("*PLR 95-032*") precludes the Commission from finding that PETITIONER owes use tax in this case is also unpersuasive. One sentence in *PLR 95-032* provides that "[w]hen an agent sells the phone equipment along with the SERVICE and the contract price includes the cost of the service and the phone equipment, the agent must collect sales tax on the entire contract price." However, immediately following this sentence, the Commission further explains that "if the price of the contract covers only the service, and the value of the (X) phone equipment is not included in the contract price, the agent, as the end consumer of the phone equipment, must pay sales tax on his or her cost of the equipment." It has been found that PETITIONER does

3 *See USTC Private Letter Ruling 96-127* (September 27, 1996) ("*PLR 96-127*") and *USTC Private Letter Ruling 96-129* (September 30, 1996) ("*PLR 96-129*").

4 The ruling in *Appeal No. 00-0616* is also consistent with the Commission's rulings in *USTC Private Letter Ruling 95-064* (October 3, 1995) and *PLR 96-127*.

5 The Commission notes that the Division properly applied the ruling in *Appeal No. 00-0616* when it audited PETITIONER because the Division did not impose any use tax on PETITIONER's below-cost sales

not sell its SERVICE and the ITEMS at issue in this case for a bundled price. PETITIONER gave away the ITEMS at issue free of charge. As a result, the Commission's ruling in the present case is consistent with its ruling in *PLR 95-032*.

Although PETITIONER argues otherwise, the Commission's ruling in the present case is also consistent with USTC Publication 25 (Revised 5/08) ("Publication 25"), which provides as follows:

> A premium or gift given away with the sale of a product subject to tax is part of that sale, and the purchase of the premium or gift by the seller is not taxable. ITEMS given away without requiring a specific purchase and ITEMS given away as advertising are consumed by the seller and the seller must pay tax on the seller's cost of those ITEMS.

PETITIONER is providing ITEMS free of charge with the purchase of a service, specifically SERVICE. In this case, the ITEMS at issue are not given away with the sale of tangible personal property or products. If the latter circumstances had existed, PETITIONER could have bought the ITEMS tax-free in accordance with Rule 68(B), (F). However, under the circumstances that exist in this case, PETITIONER gives away the ITEMS at issue as an inducement or incentive to purchase services. As a result, the Commission ruling in the present matter is not only consistent with Publication 25, but is also consistent with the Commission's prior rulings and with Rule 68.

PETITIONER further argues that another portion of Publication 25 provides that it has not consumed the ITEMS at issue. On page 11, Publication 25 provides that:

> ITEMS consumed by the seller are subject to use tax on the amount of the seller's cost of the ITEMS, not the selling price. ITEMS consumed by the seller include:
> - ITEMS taken from a seller's inventory and used by the seller;
> - samples given away for advertising; and,
> - products consumed by employees without payment.

PETITIONER argues that the ITEMS at issue are not subject to use tax because they do not meet any of the three specified scenarios listed above, specifically that the ITEMS are not ITEMS: 1) taken from inventory; 2)

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of ITEMS on which it collected and remitted tax on its sales price.

given away for advertising; or 3) consumed by its employees. PETITIONER's argument is unpersuasive. First, the three examples listed in this portion of Publication 25 are not an exclusive list. Second, PETITIONER has consumed the ITEMS by providing them free of charge as an inducement or incentive to purchase it SERVICEs. Third, PETITIONER's marketing strategy is to advertise ITEMS for free to customers who are considering a purchase of PETITIONER's SERVICEs. These actions qualify the ITEMS at issue as "ITEMS consumed by the seller." Accordingly, this portion of Publication 25 also provides that PETITIONER is liable for use tax on the ITEMS at issue.

As mentioned earlier, Rule 68(B), (F) specifically provide that use tax is not due when tangible personal property is given away with other tangible personal property. Rule 68, however, is silent as to whether tangible personal property given away for free with the sale of taxable services is subject to use tax. In *Sine v. State Tax Comm'n*, 390 P.2d 130 (Utah 1964), the Utah Supreme Court found that a motel consumed and owed use tax on ITEMS of tangible personal property (soap, wash rags, etc.) that it provided in association with its sales of taxable accommodation services. The Court denied the taxpayer's argument, which is similar to PETITIONER's argument, that it qualified for and could purchase the ITEMS tax-free under the resale exemption. PETITIONER has failed to cite any court precedent that supports its argument that it qualifies for the resale exemption or that the Commission's ruling results in double taxation. The Commission's ruling is consistent not only with Rule 68, but also with Utah Supreme Court precedent.

PETITIONER also asserts that other states have enacted laws and regulations and issued rulings in support of its position. For example, statutes in STATE 1 and STATE 2 specifically provide that a consumer who sells telecommunications services is not considered to have used or consumed a ITEM it provides as an inducement to purchase telecommunications services. However, the laws and regulations of other states are not applicable to Utah. The Utah Legislature may, like other states' legislatures, pass laws to exempt the tax due on ITEMS given away as incentives to purchase SERVICE. However, it has not done so.

In addition, the Tax Commission is not authorized to exempt a taxable transaction, regardless of whether other states have done so. That other states may have passed such legislation also suggests that the ITEMS would be taxable in those states without such legislation. For these reasons, the laws and regulations that exist in other states do not show that the Commission's decision in this matter is incorrect.

PETITIONER also argues that the Commission's ruling violates constitutional provisions concerning equal protection and the uniform operation of laws. As an example, PETITIONER states that a restaurant can "bundle" a hamburger, fries and drink together for a price that is lower than the total price of the ITEMS if purchased separately and that the restaurant, under Utah law, would need only collect and remit taxes on the lower, bundled price. PETITIONER argues that although it is offering a bundled price for SERVICEs and ITEMS, the Division is requiring it to remit tax on the separate, individual prices of the bundled ITEMS. PETITIONER also argues that it is improper that the sales tax due on a ITEM that a customer purchases for $0.01 is $0.00 (the sales tax due on a sale for $$$$$ rounds to $$$$$), while the use tax that PETITIONER has been assessed for a ITEM that its invoices for a $$$$$ "amount due" is much higher (the use tax is calculated on PETITIONER's cost of the ITEM).

PETITIONER's constitutional arguments are unpersuasive. First, PETITIONER has not bundled separate ITEMS of tangible personal property for sale. Spring provides the ITEMS at issue for free as an inducement or incentive for a customer to purchase its SERVICEs. Second, it has been found earlier that the price PETITIONER charges for its SERVICEs is not a bundled purchase price that includes the price for the ITEMS. Third, the *Sine* case and Rule 68 warrant a different treatment for tangible personal property provided free of charge with the purchase of taxable services as opposed to other tangible personal property. Fourth, use tax is generally due on cost the user or consumer paid for the item, while sales tax is generally due on the customer's purchase price. That the sales tax due on a $$$$$ sale is $$$$$ is a mathematical product that is unrelated to the amount of use tax due on an item that a seller gives away for free as an inducement or

incentive to purchase a taxable service. For these reasons, the Division's assessment of use tax on the ITEMS at issue is not a violation of constitutional provisions concerning equal protection and uniform operation of laws.

In summary, PETITIONER owes the use tax that the Division assessed in Schedule 10. In matters before the Commission, the petitioner has the burden of proof with limited exceptions pursuant to Section 59-1-1417. Although one of those exceptions involve "an increase in a deficiency if the increase is asserted initially after a notice of deficiency is mailed," no evidence was submitted to show that the taxes assessed in Schedule 10 of the 2nd Amended Audit Summary were asserted subsequent to the mailing of a notice of deficiency. Accordingly, PETITIONER has the burden to show that the Division's assessment of use tax on the ITEMS at issue is incorrect. It has not done so. The evidence shows that PETITIONER gave the ITEMS away for free as an inducement or incentive for customers to purchase SERVICEs. Given these circumstances, PETITIONER is liable for the use tax assessed in Schedule 10.

CONCLUSIONS OF LAW

1. PETITIONER has the burden to show that the Division's assessment of use tax in Schedule 10 is incorrect.

2. PETITIONER provides the ITEMS at issue to its customers free of charge as an inducement or incentive to purchase SERVICEs. The amount that PETITIONER charges a customer for SERVICEs is not a bundled purchase price for both the SERVICEs and the ITEM. Under the circumstances present in this case, PETITIONER uses or consumes the ITEMS at issue and is subject to use tax on them in accordance with Section 59-12-103(1)(l).

3. PETITIONER has not shown that the amount of use tax that the Division calculated on the ITEMS at issue is incorrect. Accordingly, the Division's assessment of use tax in Schedule 10 is sustained in its entirety.

_____
Kerry R. Chapman
Administrative Law Judge

DECISION AND ORDER

Based upon the foregoing, the Commission sustains the use taxes, plus any resulting interest, that the Division imposed in Schedule 10 of the 2nd Amended Audit Summary that it issued to PETITIONER.

It is so ordered.

DATED this _____ day of _____, 2010.

R. Bruce Johnson
Commission Chair

Marc B. Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

Michael J. Cragun
Commissioner

Notice of Appeal Rights: You have twenty (20) days after the date of this order to file a Request for Reconsideration with the Tax Commission Appeals Unit pursuant to Utah Code Ann. §63G-4-302. A Request for Reconsideration must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Reconsideration with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code Ann. §§59-1-601et seq. and 63G-4-401 et seq.

KRC/07-0054.fof