

TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 18-01

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This ruling is based on the particular facts and circumstances presented, and is an interpretation of the law at a specific point in time. The law may have changed since this ruling was issued, possibly rendering it obsolete. The presentation of this ruling in a redacted form is provided solely for informational purposes, and is not intended as a statement of Departmental policy. Taxpayers should consult with a tax professional before relying on any aspect of this ruling.

SUBJECT

The application of the Tennessee business tax to an advertising agency engaged in the procurement of advertising space, time, or placement.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department, and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time. Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[TAXPAYER] (the "Taxpayer") [REDACTED] engages in the business of providing advertising services, including the purchasing of media time, space, or placement on behalf of its clients. The type of advertising the Taxpayer purchases for its clients varies but includes radio and television spots,

newspaper advertising, magazine advertising, billboard and other outdoor advertising, direct mail, promotional products, promotional activities, online advertising, digital media, search results, blogs, social media, websites, and text messages. The types of advertising the Taxpayer could purchase for its clients continue to change and expand.

When a client hires the Taxpayer, the Taxpayer initially spends a substantial amount of time consulting with the client to develop a general advertising strategy and engages in account planning activities, such as budgeting. When an advertising strategy involves the creation of paid advertising, the Taxpayer produces the materials required, for example, a television commercial, a print advertisement, or an Internet banner. Then, the Taxpayer picks the best advertising medium to accomplish the client's goals and schedules the advertising. The Taxpayer purchases the advertising time, space, or placement, bills the client for the costs, and pays the advertising medium after verifying that the advertising occurred as ordered.

A client pays the Taxpayer for developing strategy, account planning, the creation of the advertising materials, the costs of planning the media buy, purchasing of the advertising time, space, or placement, and verifying that the advertising occurred as requested.¹ The client also reimburses the Taxpayer for amounts the Taxpayer paid to a media outlet, for example, the payments to a television station for running an advertisement on the evening news program.

In the purchasing of media and payment for advertising time, space, or placement, the Taxpayer negotiates a fee for its services or receives a commission from the advertising medium. For example: the commission rate is 15% and an advertising placement costs \$1,000; the client will pay \$1,000 to the Taxpayer and the Taxpayer will remit \$850 to the advertising medium. The Taxpayer retains the remaining \$150 as a commission.

RULING

What amounts that the Taxpayer receives for purchasing advertising space, time, or other media placement on behalf of its clients are subject to the Tennessee business tax?

Ruling: Amounts that a Taxpayer receives from clients for advertising space, time, or other media placement that the Taxpayer transfers to the media outlet and does not ultimately retain are not subject to the Tennessee business tax. Any amounts that the Taxpayer receives and ultimately retains in transactions related to obtaining advertising time, space, or other media placement are subject to the Tennessee business tax. The structure of how the Taxpayer is paid or receives funds for facilitating media placement does not affect this outcome.

¹ A client may not purchase all parts of the advertising process from the Taxpayer but may use the talents of different advertising agencies and other entities to achieve its advertising goals. Therefore, the Taxpayer bills its clients separately for specific services.

ANALYSIS

The Tennessee Business Tax Act² (the “Act”) is one component of Tennessee’s broader privilege and excise taxation statutes. The Act imposes a tax on the privilege of “making sales by engaging in any occupation, business, or business activity enumerated, described, or referred to in [TENN. CODE ANN.] § 67-4-708(1)-(5).”³

Pursuant to TENN. CODE ANN. § 67-4-709 (Supp. 2017), for exercising a privilege set forth in TENN. CODE ANN. § 67-4-708, the business tax applies to all sales of a retailer or a wholesaler according to its dominant business activity at the rate set forth in that section. “Sale” is defined, in pertinent part, as “any transfer of title or possession . . . by any means whatsoever of tangible personal property for a consideration” and “includes the furnishing of any of the things or services taxable under this part.”⁴

The business tax is computed upon the total sales price of property or services sold and “is based upon actual consideration passed, or agreed to be passed between the purchaser and the vendor.”⁵ For purposes of the business tax, “sales price” is “the total amount paid for which tangible personal property or services rendered is sold . . . without any deduction from the price on account of the cost of the property sold, the cost of materials used, labor or service costs, or any other expense whatsoever.”⁶

In this case, the Taxpayer is only facilitating the media placement transaction for its customer. The media placement is not a cost of property sold, materials used, or labor or service costs or other expenses of the Taxpayer in providing its advertising materials or services. The Taxpayer in this case should only pay business tax on amounts it receives as consideration for rendering advertising services, which include facilitating the purchase of media placement.⁷ With regard to the actual advertising time, space, or other media placement, the Taxpayer is not furnishing such service.⁸ Rather, the third party advertising medium, who retains control over advertising time, space, or other media placement, is furnishing that service. Thus, amounts that a Taxpayer receives from clients for the purchase of advertising space, time, or media placement that the Taxpayer does not ultimately retain are not part of the sales price upon which the Taxpayer’s Tennessee business tax is computed.

On the other hand, any fees that the Taxpayer receives for facilitating media placement are subject to the Tennessee business tax. Regardless of the structure or order of the Taxpayer’s billing or

² Tennessee Business Tax Act, ch. 387, §§ 1-27, 1971 Tenn. Pub. Acts 994, 994-1019 (codified as amended at TENN. CODE ANN. § 67-4-701 to -730 (Supp. 2017)).

³ TENN. CODE ANN. §§ 67-4-704(a), -705(a) (Supp. 2017).

⁴ TENN. CODE ANN. § 67-4-702(a)(18).

⁵ TENN. COMP. R. & REGS. 1320-04-05-.08(2) (2016).

⁶ TENN. CODE ANN. § 67-4-702(a)(19); *see also* TENN. COMP. R. & REGS. 1320-04-05-.08(1) (defining “sales price” similarly).

⁷ *See* TENN. CODE ANN. § 67-4-702(a)(18).

⁸ *See id.*

receipt of funds, any amount that the Taxpayer actually retains with regard to its purchase of advertising space, time, or other media placement on behalf of its clients is part of the sales price of the Taxpayer's services rendered. Such amount includes any fees that a client pays to the Taxpayer in excess of the cost of the advertising media as well as any commission or other consideration from the media outlet.⁹

In the example provided in the facts, the \$850 that the Taxpayer remits to the advertising medium is not subject to the Tennessee business tax because it relates to the Taxpayer's costs to purchase advertising time, space, or other media placement on behalf of its client and does not relate to a taxable sale by the Taxpayer; however, the \$150 that the Taxpayer retains as a commission is subject to the Tennessee business tax and included in the Taxpayer's sales for purposes of calculating its Tennessee business tax liability because it is a fee for the Taxpayer's performance of the taxable service of facilitating and procuring the media purchases.

Jennifer Wilson
Senior Tax Counsel

APPROVED: David Gerregano
Commissioner of Revenue

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⁹ The Taxpayer in this ruling is distinguishable from a business that holds itself out to its customers as the provider of a particular service. For example, a business contracts to repair tangible personal property. The business then subcontracts with a third party to perform the labor. That business is selling a repair service to consumers at retail and cannot deduct the amount paid to the third party. All of the business's receipts are part of the sales price of its service and accordingly are subject to the Tennessee business tax. The Taxpayer in this ruling does not hold itself out as a seller or provider of media time or space.