COLOR CRAFT, INC. 1616 Mt. Meigs Road Montgomery, Alabama 36103-4279,	'	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
Taxpayer,	'	DOCKET NO. S. 96-323
v.	'	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	'	

AMENDED FINAL ORDER
ON APPLICATION FOR REHEARING

At the March 18, 1997 rehearing in this case, the Department was allowed three weeks to file a brief, and the Taxpayer was allowed three weeks to reply. The Department submitted a letter on May 2, 1997 indicating it would not file a brief. The Taxpayer thus had until May 23 to respond. Unfortunately, the Final Order on Application for Rehearing was prematurely entered on May 20, before the Taxpayer's deadline for filing its brief.

The Taxpayer timely filed its response on May 23, and requested reconsideration of the Final Order on Application for Rehearing. I have carefully reviewed the Taxpayer's brief. The May 20 Final Order adequately addressed all of the arguments in the brief, except one. That argument is the Taxpayer's contention that the computer alterations in issue are analogous to custom computer software, which is not subject to sales tax. See, Wal-Mart Stores, Inc. v. City of Mobile, 1996 Ala. Lexis 720 (11/27/96).[1] I disagree.

[1]In Wal-Mart, the Alabama Supreme Court overruled its prior decision in State v. Central Computer Services, Inc., 349 So.2d 1169 (1977), and held that computer software

was tangible personal property subject to sales tax. However, the case involved only generic "canned" software sold by Wal-Mart. Although not stated specifically, the Court's analysis indicates that custom software should still be considered an intangible, and thus not subject to sales tax. The Department thus distinguished between taxable canned software and nontaxable custom software in its newly enacted Reg. 810-6-1-.37. I do not necessarily agree in theory with the distinction between canned and custom software, but that unrelated issue need not be addressed at this time.

The Taxpayer's custom computer software analogy would be appropriate if the Taxpayer only computer altered the photograph, and then downloaded the altered image onto a disk for delivery to the customer. If the customer provided the disk, then obviously no sale of tangible property occurred, and no sales tax would be due. The same is true if the altered image was electronically transmitted to the customer. Again, no sale of tangible property would have occurred, and no sales tax would be due. If the Taxpayer provided the disk, then applying the custom software rationale, the transfer of the tangible disk would be only incidental to the information being transmitted, and no sale subject to sales tax would have occurred. The Department recognizes this, and thus does not charge sales tax on the alteration services delivered by disk.

The computer services in issue can be distinguished, however, because the Taxpayer performs the services and then uses the resulting product, the altered photograph image, to produce the color separation for sale. The sale of the tangible color separation by the Taxpayer is subject to sales tax. The computer alteration services are a cost incurred in producing the color separation, and thus cannot be deducted from taxable gross proceeds of sale pursuant to Code of Ala. 1975, '40-23-1(a)(6).

Although well-argued, the Taxpayer's motion for reconsideration is denied. The Final Order is affirmed. This Amended Final Order on Application for Rehearing may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, '40-2A-

9(g).

Entered June 3, 1997.

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BILL THOMPSON
Chief Administrative Law Judge