

BEFORE THE IOWA DEPARTMENT OF REVENUE  
HOOVER STATE OFFICE BUILDING  
DES MOINES, IOWA

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| IN THE MATTER OF                       | * |                            |
|  | * |                            |
| FAIRYTALE BROWNIES, INC.               | * | DECLARATORY ORDER          |
| 4610 E. Cotton Center Blvd., Suite 100 | * |                            |
| Phoenix, AZ 85040-8898                 | * |                            |
|  | * |                            |
| SALES AND USE TAX                      | * | DOCKET NO. 2018-300-2-0440 |

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Pursuant to a Petition for Declaratory Order filed with the Iowa Department of Revenue (hereinafter referred to as “Department”) by FAIRYTALE BROWNIES, INC. (hereinafter referred to as “FTB”) and in accordance with Iowa Code, section 17A.9 (2016) and Iowa Administrative Code rule 701-7.24(17A), “Declaratory order-in general,” the Director issues the following order.

**I. FACTS**

The findings of fact are based on the Petition for Declaratory Order and other publicly available information made available by FTB on its website.

FTB, an Arizona corporation, manufactures and sells cooked food products at its location in Phoenix. It receives orders from purchasers across the country, including Iowa residents, either through its own website, its Amazon page, or on the telephone. The products are packaged in Phoenix and shipped to purchasers via common carrier. FTB has no offices, warehouses, employees, inventory, or other property in Iowa. FTB has never registered to collect and remit sales or use tax in Iowa.

FTB describes its products as “brownies and cookies in various sizes and flavors.” The products are individually wrapped and delivered unheated without utensils. A review of FTB’s

website, [www.brownies.com](http://www.brownies.com), shows in addition to the food items, purchasers can order “keepsake” metal or wooden boxes with seasonal or holiday-themed messages as well as photos printed on the top. For example, a “Magic Morsel 24” of two dozen brownies costs \$35.95. Fairytale Brownies, <https://www.brownies.com/product/magic-morsel-24.aspx> (last visited Dec. 5, 2018). The same quantity and size brownies sold as a “Holiday Keepsake Tin Morsel 24” costs \$48.95. Customers may also select other customized and premium containers. A “Photo Tin Morsel 24” costs \$54.95. Fairytale Brownies, <https://www.brownies.com/product/holiday-keepsake-tin-morsel-24.aspx>, <https://www.brownies.com/product/photo-tin-morsel-24.aspx> (last visited Dec. 5, 2018).

## **II. ISSUE PRESENTED**

The Petition presents four questions:

1. Does the sale of prepackaged food products to Iowa residents create nexus from an economic presence standpoint when the products are manufactured, sold and shipped from Arizona to Iowa purchasers via common carrier?

2. If the scenario in question 1 above does create sales tax nexus in Iowa, would FTB be required to register with the Iowa Department of Revenue for sales or use tax purposes?

3. Since all products sold to Iowa residents are prepackaged food products intended for human consumption, are these products exempt from Iowa sales or use tax?

4. If economic presence is established and FTB is required to register for sales tax purpose with the Iowa Department of Revenue and the sale of food products is exempt from Iowa sales tax, would FTB be required to file a zero return each month once FTB registers with Iowa?

## **III. TAXPAYER’S POSITION**

FTB believes its products are exempt from Iowa sales tax under Code sections 423.3(25) and 423.3(57).

#### **IV. ANALYSIS AND CONCLUSIONS**

##### **A. Declaratory Orders under the Iowa Administrative Procedure Act.**

The function of a declaratory order is to provide “reliable advice from an agency as to the applicability of unclear law.” Arthur Earl Bonfield, *The Iowa Administrative Procedure Act: Background, Construction, Applicability, Public Access to Agency Law, The Rulemaking Process*, 60 Iowa L. Rev. 731, 805 (1975). Iowa Code section 17A.9 contemplates declaratory orders by administrative agencies on a disclosed set of facts. *City of Des Moines v. P.E.R.B.*, 275 N.W.2d 753, 758 (Iowa 1979). A declaratory order enables the public to secure definitive binding advice as to the applicability of agency-enforced law to a particular set of facts. Bonfield, *supra*, at 822–23.

It is not the function of a declaratory order to resolve issues involving factual analysis “too complicated to handle outside of an actual adjudication.” *Id.* at 807. A declaratory order is not a “contested case” as defined in Iowa Code section 17A.2(5); namely, it is not an evidentiary hearing, which is a separate administrative remedy set forth in Iowa Code chapter 17A and in the Department’s rules. *See* Iowa Admin. Code r. 701-7.41(17A). Consequently, for the purposes of any declaratory order, the Director views the issues raised in the petition as questions of law applicable to future factual situations as disclosed in the petition. This view is consistent with Iowa Administrative Code rule 701-7.41(17A) concerning the issuance of declaratory orders.

##### **B. Statutory Construction and Interpretation of Tax Exemption Statutes.**

“When engaging in statutory interpretation,” the Department “first examine[s] the language of the statute and determine[s] whether it is ambiguous.” *Kay-Decker v. Iowa State Bd.*

*of Tax Review*, 857 N.W.2d 216, 223 (Iowa 2014) (citing *Rolfe State Bank v. Gunderson*, 794 N.W.2d 561, 564 (Iowa 2011)). “Generally, we presume words used in a statute have their ordinary and commonly understood meaning.” *Kay-Decker*, 857 N.W.2d at 223 (quoting *McGill v. Fish*, 790 N.W.2d 113, 119 (Iowa 2010)). “Legislative intent is expressed by what the legislature has said, not what it could or might have said. When a statute’s language is clear, we look no further for meaning than its express terms. Intent may be expressed by the omission, as well as the inclusion of statutory terms . . . .” *Hawkeye Land Co. v. Iowa Utilities Bd.*, 847 N.W.2d 199, 210 (Iowa 2014) (quoting *State v. Beach*, 630 N.W.2d 598, 600 (Iowa 2001) (internal citations omitted)).

In addition to applying the general principles of statutory construction, the Department construes tax exemption statutes narrowly in favor of taxation. See *Dial Corp. v. Iowa Dep’t of Revenue*, 634 N.W.2d 643, 646 (Iowa 2001) (“Tax exemption statutes are construed strictly, with all doubts resolved in favor of taxation.”); see also *Sherwin-Williams Co. v. Iowa Dep’t of Revenue*, 789 N.W.2d 417, 424 (Iowa 2010).

### **C. Measuring Economic Nexus by Gross Revenue from Sales.**

FTB first asks whether the sale of prepackaged food products to Iowa residents establishes economic nexus. Beginning January 1, 2019, a seller with no physical presence in Iowa, known as a “remote seller,” is required to collect and remit sales tax for sales into the state if it has gross revenue from Iowa sales equal to or in excess of \$100,000 or 200 or more separate transactions in an immediately preceding or current calendar year. S.F. 2417, 87<sup>th</sup> G.A., Sec. 203 (Ia. 2018). See also “Remote Sellers,” Iowa Department of Revenue, <https://tax.iowa.gov/remote-sellers> (last visited Dec. 3, 2018). A remote seller must include sales made through a “marketplace facilitator” in determining whether it meets those thresholds. See

“Marketplace Facilitators,” Iowa Department of Revenue, <https://tax.iowa.gov/marketplace-facilitators> (last visited Dec. 3, 2018). A marketplace facilitator is responsible for collecting and remitting Iowa sales tax on all items sold through its marketplace. A remote seller that makes sales through various channels, such as its own website and one or more marketplaces that collect Iowa sales tax, would only be responsible for collecting and remitting sales tax on items sold on its own website.

FTB asserts it sells products on Amazon Marketplace. Petition, p. 1. However, FTB does not provide information relating to its volume or gross revenue from sales into Iowa. Thus, it cannot be determined whether FTB has exceeded economic nexus threshold and must begin collecting January 1, 2019.

#### **D. Some FTB Products Are Subject to Sales Tax.**

##### *1. Food sold by nonprofits.*

FTB asserts its products should be exempt from Iowa sales tax based on Iowa Code section 423.3(25). That provision excludes from sales and use tax “[t]he sales price of food and beverages sold for human consumption by a nonprofit organization which principally promotes a food or beverage product for human consumption produced, grown, or raised in this state and whose income is exempt from federal taxation under section 501(c) of the Internal Revenue Code.” No information in the Petition or available on FTB’s website indicates it is structured as a nonprofit organization or that FTB’s income is exempt from federal income tax under section 501(c). It also does not appear FTB is an organization that is principally engaged in promoting a food or beverage product. Rather, it appears FTB engages in the business of selling gourmet desserts for profit. FTB does not meet the requirements of Iowa Code section 423.3(25).

##### *2. Bakery items.*

FTB also asserts its products should be exempt from Iowa sales tax based on Iowa Code section 423.3(57), which provides an exemption from sales and use tax for “food and food ingredients.” Excluded from that term and thus subject to tax is “prepared food.” *Id.* The Code further excludes “[b]akery items sold by the seller which baked them” from the definition of “prepared food.” Iowa Code section 423.3(57)(f)(3)(c). This means “bakery items sold by the seller which baked them” are exempt from Iowa sales tax. *Id.*

The Code includes the following nonexclusive list of “bakery items:” “breads, rolls, buns, biscuits, bagels, croissants, pastries, donuts, Danish, cakes, tortes, pies, tarts, muffins, bars, cookies, and tortillas.” *Id.* The exemption expressly lists “cookies” as “bakery items.” *Id.* Brownies, though not specifically included in that list, are also bakery items. The cookies and brownies at issue are baked and sold by FTB. Fairytale Brownies, [https://www.brownies.com/images/media\\_room/press\\_releases/FTB\\_Media\\_Kit\\_2018.pdf](https://www.brownies.com/images/media_room/press_releases/FTB_Media_Kit_2018.pdf) (last visited Dec. 3, 2018). Therefore, it appears FTB’s cookies and brownies would qualify for the exemption in section 423.3(57).

### *3. Bundled transactions.*

As discussed above, FTB sells food products and offers purchasers the option of adding premium, customized, reusable, or “keepsake” boxes or tins for an increased price. Fairytale Brownies, <https://www.brownies.com/category/tins-and-keepsakes.aspx> (last visited Dec. 5, 2018). The prices for identical or very similar food products vary significantly based on the premium containers selected by the purchaser. It appears, then, that when a purchaser selects the more expensive package, the purchaser is buying not only the food product but also the premium container. For these sales, FTB needs to consider whether the sale is a “bundled transaction” and

whether the sale of premium containers constitutes the sale of a separate item that is subject to Iowa sales tax.

Iowa Code section 423.2(8) imposes sales tax on the sales price from sales of “bundled transactions,” defined as “the retail sale of two or more distinct and identifiable products, except real property and services to real property, which are sold for one nonitemized price.” “[D]istinct and identifiable products” does not include, among other things, “[p]ackaging or other materials that accompany the retail sale of the products and are incidental or immaterial to the retail sale of the products.” Iowa Code § 423.8(b)(1). A bundled transaction “does not include the sale of any products in which the sales price varies, or is negotiable, based on the selection by the purchaser of the products included in the transaction.” *Id.* at 423.8(a).

Assuming the 24 brownie bites cost the same when they are included in the total sales price with one of FTB’s keepsake boxes, as the brownie bites do on their own, the boxes can add either \$13 or \$19 to the cost of the brownies themselves, depending on the type of box purchased. Fairytale Brownies, <https://www.brownies.com/product/magic-morsel-24.aspx>, <https://www.brownies.com/product/holiday-keepsake-tin-morsel-24.aspx>, <https://www.brownies.com/product/photo-tin-morsel-24.aspx> (last visited Dec. 5, 2018). The customer’s option to select premium containers and the corresponding significant increase in price demonstrates these containers are not “incidental or immaterial to the retail sale of the” bakery items. *See* Iowa Code section 423.8(b)(1). These boxes are “distinct and identifiable” from food products, as they require separate shopping preferences and product selection by the purchaser and are not standard with every order of food products. While the price for the brownie bites with a keepsake box does not itemize the cost of the distinct items, the price of the box itself is discernible for any purchaser by finding the same or similar brownie bites for sale

without the premium box at a materially different price. A purchaser having the option of declining to purchase any of the products where the sales price varies as a result of the selection of products demonstrates the sale was not made for “one non-itemized price” and thus is not a bundled transaction. *Id.*

In a situation where two or more products or services are purchased and it is not a bundled transaction, the sales tax treatment for each product or service follows the tax treatment of the individual products or services being sold. Therefore, for FTB’s sales of baked goods with keepsake boxes and other premium containers, sales tax is due on the sales price of the box.

**E. Permit and Filing Requirements.**


FTB must obtain an Iowa sales tax permit and file Iowa sales tax returns if: (1) FTB exceeds the remote seller thresholds, and (2) FTB makes taxable retail sales into Iowa.

ORDER

THEREFORE, based on the facts presented, foregoing reasoning, and applicable provisions of the law, the issues raised in the Petition for a Declaratory Order are as answered above.

Issued at Des Moines, Iowa this 7th day of December, 2018.

IOWA DEPARTMENT OF REVENUE

By   
Courtney M. Klay-Decker, Director



CERTIFICATE OF SERVICE

I certify that on this 7<sup>th</sup> day of December, 2018, I caused a true and correct copy of the Declaratory Order of the Director of Revenue to be forwarded by U.S. Mail to the following person:

FAIRYTALE BROWNIES, INC.  
4610 E. Cotton Center Blvd., Suite 10  
Phoenix, AZ 85040-8898

  
Hollie Welch, Executive Secretary