

Policy Letter; Food Sales & Food Preparation Services; August 11, 2016

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Re: Food Sales & Food Preparation Services

Dear Ms. Boschert:

The Iowa Department of Revenue (“Department”) has received your letter regarding the tax implications of numerous scenarios involving food sales and food preparation services.

Facts As You Provided:

You have a client (“Client X”) that provides food ingredients, food products, and food preparation services to various customers, including fraternities. These fraternities are associated with universities, yet are separate non-profit organizations. Universities oversee the fraternities and own either the fraternity houses or the land the houses stand on. In many cases, the universities collect room and board from the residents and distribute funds to the fraternities. Food sales and services provided to these fraternities are structured in the following four ways:

- A. Client X provides unprepared food ingredients to the fraternity. The fraternity prepares and serves the meals.
- B. Client X provides food ingredients to the fraternity and prepares the meals, with the exception of food products that do not require any preparation.
- C. The customer provides food ingredients, purchased from an unaffiliated 3rd party. Client X prepares the meals.
- D. The customer provides the food ingredients, purchased from an affiliated 3rd party. Client X prepares the meals.

In all four scenarios, Client X invoices the fraternities using an unbundled process by separately listing sales of food ingredients, products, and meal preparation services. In scenarios where Client X prepares the meals, this preparation is completed at the fraternity location.

Questions:

1. What is the taxability of scenarios A–D described above in regard to the separately stated invoice components for food ingredients, food products, and food preparation services?
2. In the examples where Client X provides food ingredients to the customer and prepares the meals, can the food ever qualify as unprepared food?
3. If having the separately stated food ingredients, food products, and food preparation services on the same invoice causes multiple line items to be taxable, would the response remain the same if Client X separately contracted with the customer for food products and ingredients and for meal planning and food preparation services and invoiced the food products on a separate invoice from the food preparation services?
4. Can the fraternity qualify as an exempt organization or as an auxiliary University organization? Must the fraternity have its own exemption document or can it utilize the University's exemption document as a flow through for their operations and as an auxiliary organization?
5. If the fraternity provides Client X with an exemption certificate, is Client X required to collect any sales tax on the transaction? Can Client X still claim a resale exemption on the purchase of any items transferred to their customer?

Response:

1. Taxability of the scenarios provided

A) Client X provides unprepared food ingredients to the fraternity. The fraternity prepares and serves the meals.

Iowa Code § 423.2 imposes “a tax of six percent upon the sale price of all sales of tangible personal property, consisting of goods, wares, or merchandise, sold at retail in the state to consumers or users” That said, Iowa Code § 423.3(57) exempts:

[A]ll sales of food and food ingredients. However, as used in this subsection, a sale of ‘food and food ingredients’ does not include a sale of alcoholic beverages, candy, or dietary supplements; food sold through vending machines; or sales of prepared food, soft drinks, or tobacco.

Thus, as long as the sale of food consists only of “food and food ingredients” as defined in the Code, it falls under the § 423.3(57) exemption. Supposing the unprepared food ingredients sold in this scenario are so exempt, the transaction would not be subject to Iowa sales tax.

B) Client X provides food ingredients to the fraternity and prepares the meals, with the exception of food products that do not require any preparation.

The entire sales price of the food would be subject to Iowa sales tax, including the food that you believe does not require preparation, because Client X appears to be a caterer that is selling food for consumption on premises available to it. While “food and food ingredients” generally are exempt from sales tax in Iowa under aforementioned Iowa Code § 423.3(57), this section also states the Code’s definition of “food and food ingredients” does not include sales of “prepared food.”

“Prepared food” as defined by the Iowa Code includes:

- (1) Food sold in a heated state or heated by the seller, *including food sold by a caterer*.
- (2) Two or more food ingredients mixed or combined by the seller for sale as a single item.

Iowa Code § 423.3(57)(f) (emphasis added). “Prepared food” is further defined in Iowa Admin. Code r. 701—231.5(1) as including “food sold with eating utensils provided by the seller, including plates, knives, forks, spoons, glasses, cups, napkins, or straws. A plate does not include a container or packaging used to transport food.” It also states:

If food is sold for consumption on the premises of a retailer, the food is rebuttably presumed to be prepared food. “Premises of a retailer” means the total space and facilities under control of the retailer or that are available for use by the retailer, for the purpose of sale of prepared food and drink or for the purpose of consumption of prepared food and drink sold by the retailer.

See also Iowa Admin. Code r. 701—231.5(1) “Example D” (giving an example of how “premises of a retailer” relates to caterers).

Client X is selling food for consumption on premises made available to it, and Client X appears to be a caterer, so all food sold in this scenario would be treated as “prepared food” under Iowa Code § 423.3(57)(f) and is therefore subject to Iowa sales tax.

The sales price of the food preparation services would not be taxed, provided that they are separately itemized. Iowa Code § 423.2(5) imposes “a tax of six percent upon the sales price from the furnishing of services as defined in section 423.1.” Iowa Code § 423.1(54) defines “services” as:

[A]ll acts or services rendered, furnished, or performed, other than services used in processing of tangible personal property for use in retail sales or services, for an employer who pays the wages of an employee for a valuable consideration by any person engaged in any business or occupation specifically enumerated in section 423.2.

Food preparation services are not one of the enumerated services in Iowa Code § 432.2 and would not be taxed.

C) The fraternity provides food ingredients, purchased from an unaffiliated 3rd party. Client X prepares the meals.

Client X’s transaction would not be subject to tax because it is only a sale of an unenumerated service. In this scenario, Client X is not selling the food it prepares, or preparing food that it has sold; it is preparing food that it never possessed and is currently owned by the fraternity. Thus, a sale of food is not taking place. As explained in Response 1.B, food preparation services are not taxable services under Iowa Code § 432.2. Thus, the transaction would not be subject to sales tax.

D) The fraternity provides the food ingredients, purchased from an affiliated 3rd party. Client X prepares the meals.

In theory, it is possible that if the affiliated 3rd party is a separate legal entity from Client X, the analysis could be the same as that stated in Response 1.C. However, the burden of proof would be on Client X to show that the two companies are bona fide separate entities dealing at arm's length, and not merely an illusory relationship meant to evade the Code's tax on prepared food.

2. Whether food provided and prepared by Client X can ever qualify as unprepared food.

No. For the reasons stated in Response 1.B, all food that is both sold and prepared by Client X is considered prepared food and is thus subject to Iowa sales tax.

3. The effects of separately itemizing food and preparation services.

Separately itemizing food ingredients, food products, and food preparation services on the same invoice does not result in otherwise tax-exempt line items becoming taxable; there is no need to utilize separate contracts. Iowa Code § 423.2(8) states:

a. A tax of six percent is imposed on the sales price from sales of bundled transactions. For the purposes of this subsection, a “*bundled transaction*” is 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. 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.

b. “*Distinct and identifiable products*” does not include any of the following:

(1) Packaging or other materials that accompany the retail sale of the products and are incidental or immaterial to the retail sale of the products.

(2) A product provided free of charge with the required purchase of another product. A product is “*provided free of charge*” if the sales price of the product purchased does not vary depending on the inclusion of the product which is provided free of charge.

(3) Items included in the definition of “*sales price*” pursuant to section 423.1.

c. “*One nonitemized price*” does not include a price that is separately identified by product on binding sales or other supporting sales-related documentation made available to the customer in paper or electronic form.

Following this statute, food preparation services separately itemized on an invoice maintain their tax-exempt status because they are not bundled with other products for “one nonitemized price.” However, the food sold would still be subject to tax for the reasons stated in Response 1.B.

4. Fraternities as exempt entities.

If Client X contracts with the fraternities for an exempt purchase or service, the fraternities would have to provide their own valid exemption certificates. Iowa Code § 423.45(4)(b) states:

The sales tax liability for all sales of tangible personal property and all sales of services is upon the seller and the purchaser unless the seller takes from the purchaser a valid exemption certificate stating under penalty of perjury that . . . the seller is not obligated to collect tax due. . . .

In order for a sale to be tax exempt, Client X must receive a valid exemption certificate from the purchaser, meaning the party Client X is contracting with. If Client X contracts with a university, the university would have to provide an exemption certificate. If instead Client X contracts with a fraternity directly, then the fraternity would be the purchaser and the fraternity, not the university, would have to provide its own exemption certificate. There is no Iowa Code or Rule that would allow a fraternity to utilize another party's exemption certificate.

Furthermore, fraternities are not exempt entities within the context of Iowa sales tax.

A fraternity could still present an exemption certificate to Client X if the sale qualifies for some other exemption, such as if the fraternity was purchasing the prepared food for resale. Iowa Code § 423.3(2).

5. Resale exemptions.

Client X is not liable for sales tax when it purchases personal property for resale. Iowa Code § 423.3(2) exempts from sales tax liability “the sales price of sales for resale of tangible personal property or taxable services” Furthermore, Iowa Admin. Code r. 701—225.4(1)(a) states:

Tangible personal property purchased by a person engaged in the performance of a service is purchased for resale and not subject to tax if (1) the provider and user of the service intend that a sale of the property will occur, and (2) the property is transferred to the user of the service in connection with the performance of the service in a form or quantity capable of a fixed or definite price value, and (3) the sale is evidenced by a separate charge for the identifiable piece or quantity of property.

Because Client X either purchases food for resale outright or purchases it for resale as part of the performance of a service and separately itemizes the food ingredients, such purchases are exempt from sales tax liability. This is true regardless of whether at resale the purchasing party has an exemption certificate or not.

Iowa Code § 423.45(4)(b) provides:

The sales tax liability for all sales of tangible personal property and all sales of services is upon the seller and the purchaser unless the seller takes from the purchaser a valid exemption certificate stating under penalty of perjury that . . . the seller is not obligated to collect tax due. . . . If the tangible personal property or services are purchased tax free pursuant to a valid exemption certificate and the tangible personal property or services are used or disposed of by the purchaser in a nonexempt manner, the purchaser is solely liable for the taxes

If a fraternity provides Client X with a valid exemption certificate, then Client X is not required to collect any sales tax on the transaction. There is no Iowa Code or Rule that invalidates a resale exemption merely because the later purchaser has its own valid exemption certificate.

I hope this information has been helpful to you. Please remember that this letter is an informal opinion based only on the facts you provided and on the current law. In the future, the Department could take a position contrary to that stated in this letter. Any written advice or opinion rendered to members of the public by Department personnel that is not pursuant to a Petition for Declaratory Order under 701 IAC 7.24 is not binding upon the Department. If you have any additional questions regarding this matter please do not hesitate to contact me.

Sincerely,

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