

Cite as Det. No. 13-0291, 36 WTD 209 (2017)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of)	<u>D E T E R M I N A T I O N</u>
Assessments of)	
)	No. 13-0291
)	
...)	Registration Nos. . . .
)	

RULE 244; RCW 82.08.0293: RETAIL SALES TAX – MOVIE THEATER POPCORN – PREPARED FOOD – SOLD IN A HEATED STATE – TWO OR MORE FOOD INGREDIENTS COMBINED – SOLD BY WEIGHT OR VOLUME. To sell a product by weight or volume, the price of the product must vary based upon the weight or volume of the product purchased. A movie theater does not sell its popcorn “by weight or volume” when it offers varying sizes of popcorn (small, medium, and large), because those sizes are not actually “measured” by any standard of weight or volume.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

Pardee, A.L.J. – Movie theatres (Taxpayers) object to the Department of Revenue’s (Department’s) assessment of retail sales tax on popcorn they sell to customers. We deny the petition.¹

ISSUE

Do Taxpayers sell popcorn to customers by weight or volume in an unheated state such that the popcorn is exempt from retail sales tax under RCW 82.08.0293(2)(b)(ii)(B) and WAC 458-20-244(4)(b)?

FINDINGS OF FACT

[Theater A] and [Theater B], operate movie theatres in . . . , Washington. [Theater C] operates a movie theatre in . . . , Washington. [Theaters A, B, and C], referred to collectively as “Taxpayers,” have the same managing member.

As part of their theatre operations, Taxpayers prepare and sell popcorn to customers. Taxpayers combine popcorn kernels, half-and-half mixture of corn and canola oil, and seasoning salt to produce popcorn, which it sells to its customers. Taxpayers’ Appeal Petitions, Page 3. Taxpayers

¹ Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

sell the popcorn in small, medium, large, and extra large open containers, and charge a different flat rate price for each size container of popcorn.

Assessment of [Theater A]

The Department's Audit Division (Audit) examined [Theater A's] books and records for the period of July 1, 2009, through March 31, 2012 ([Theater A's] audit period). On August 20, 2012, the Department issued [Theater A] an assessment (Document No. . . . – "Assessment 1") for [Theater A's] audit period totaling \$. . . , comprised of a \$. . . credit for syrup business and occupation (B&O) tax paid, a credit for \$. . . for retailing B&O tax paid, retail sales tax of \$. . . , service and other B&O tax of \$. . . , use tax and/or deferred sales tax of \$. . . , a 5 percent assessment penalty of \$. . . , and interest of \$ At Schedule 4 of Assessment 1, Audit explains that it made a reconciliation of [Theater A's] taxable income under the retail sales tax classification through amounts recorded in [Theater A's] business records with amounts they reported to the Department. Audit notes that the taxable differences were the result of [Theater A's] position that popcorn it sells is not a prepared food, but rather sold by weight or volume. Audit disagreed and assessed [Theater A] retail sales tax on such sales.

Assessment of [Theater C]

[Audit] examined [Theater C's] books and records for the period of January 1, 2008, through March 31, 2012 ([Theater C's] audit period). On August 20, 2012, the Department issued [Theater C] an assessment (Document No. . . . – "Assessment 2") for [Theater C's] audit period totaling \$. . . , comprised of a \$. . . credit for syrup [B&O] tax paid, retailing B&O tax of \$. . . , retail sales tax of \$. . . , service and other B&O tax of \$. . . , use tax and/or deferred sales tax of \$. . . , a 5 percent assessment penalty of \$. . . , and interest of \$ At Schedule 4 of Assessment 2, Audit explains that it made a reconciliation of [Theater C's] taxable income under the retail sales tax classification through amounts recorded in [Theater C's] business records with amounts they reported to the Department. Audit notes that the taxable differences were the result of [Theater C's] position that popcorn it sells is not a prepared food, but rather sold by weight or volume. Audit disagreed and assessed [Theater C] retail sales tax on such sales.

Assessment of [Theater B]

[Audit] examined [Theater B's] books and records for the period of November 1, 2009, through March 31, 2012 ([Theater B's] audit period). On August 20, 2012, the Department issued [Theater B] an assessment (Document No. . . . – "Assessment 3") for [Theater B's] audit period totaling \$. . . , comprised of a credit of \$. . . for retailing B&O tax paid, retail sales tax of \$. . . , service and other B&O tax of \$. . . , use tax and/or deferred sales tax of \$. . . , a 5 percent assessment penalty of \$. . . , and interest of \$ At Schedule 4 of Assessment 3, Audit explains that it made a reconciliation of [Theater B's] taxable income under the retail sales tax classification through amounts recorded in [Theater B's] business records with amounts they reported to the Department. Audit notes that the taxable differences were the result of [Theater B's] position that popcorn it sells is not a prepared food, but rather sold by weight or volume. Audit disagreed and assessed [Theater B] retail sales tax on such sales.

Taxpayers timely appealed the Department's issuance of Assessments 1-3.²

ANALYSIS

The retail sales tax is imposed on every retail sale occurring in the State of Washington. RCW 82.08.020(1). A "sale" for purposes of the retail sales tax includes "the furnishing of food, drink, or meals for compensation whether consumed upon the premises or not." RCW 82.04.040. A "retail sale" is "every sale of tangible personal property . . . to all persons irrespective of the nature of their business" RCW 82.04.050(1). The sale of food is a sale of tangible personal property. *See Sacred Heart Medical Center v. Dep't of Revenue*, 88 Wn. App. 632, 637, 946 P.2d 409 (1997).

Retail sales tax does not apply to sales of food and food ingredients:

(1) The tax levied by RCW 82.08.020 does not apply to sales of food and food ingredients.

...

RCW 82.08.0293 (emphasis added).³ *See also* WAC 458-20-244(2)(a) (Rule 244(2)(a)).

This same statute defines "food and food ingredients," and explains that the sale of "prepared food" is not exempt from retail sales tax:

"Food and food ingredients" means substances, whether in liquid, concentrated, solid, frozen, dried, or dehydrated form, that are sold for ingestion or chewing by humans and are consumed for their taste or nutritional value. "Food and food ingredients" does not include:

(a) "Alcoholic beverages," which means beverages that are suitable for human consumption and contain one-half of one percent or more of alcohol by volume; and

(b) "Tobacco," which means cigarettes, cigars, chewing or pipe tobacco, or any other item that contains tobacco.

(2) The exemption of "food and food ingredients" provided for in subsection (1) of this section does not apply to prepared food, soft drinks, or dietary supplements. For purposes of this subsection, the following definitions apply:

* * *

(b)(i) "Prepared food" means:

(A) Food sold in a heated state or heated by the seller;

² Taxpayers have paid nothing towards Assessments 1-3.

³ However, even if a sale of food or food ingredients is exempt from retail sales tax, gross proceeds from such sales remain subject to retailing B&O tax. WAC 458-20-244(1)(a).

(B) 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 the food; or

(C) Two or more food ingredients mixed or combined by the seller for sale as a single item, except:

(I) Food that is only cut, repackaged, or pasteurized by the seller; or

(II) Raw eggs, fish, meat, poultry, and foods containing these raw animal foods requiring cooking by the consumer as recommended by the federal food and drug administration in chapter 3, part 401.11 of The Food Code, published by the food and drug administration, as amended or renumbered as of January 1, 2003, so as to prevent foodborne illness.

(ii) "Prepared food" does not include the following food or food ingredients, if the food or food ingredients are sold without eating utensils provided by the seller:

(A) Food sold by a seller whose proper primary North American industry classification system (NAICS) classification is manufacturing in sector 311, except subsector 3118 (bakeries), as provided in the "North American industry classification system -- United States, 2002";

(B) Food sold in an unheated state by weight or volume as a single item; or

(C) Bakery items. The term "bakery items" includes bread, rolls, buns, biscuits, bagels, croissants, pastries, donuts, Danish, cakes, tortes, pies, tarts, muffins, bars, cookies, or tortillas.

RCW 82.08.0293 (emphasis added).

WAC 458-20-244 (Rule 244), the Department rule implementing RCW 82.08.0293, explains further what is included under the umbrella of prepared food, and states in relevant part:

(i) **Prepared food.** Prepared food is excluded from the exemptions. Prepared food generally means heated foods, combined foods, or foods sold with utensils provided by the seller, as described in more detail in subsection (4) of this section. "Prepared food" does not include food sold by a seller whose proper primary North American industry classification system (NAICS) classification is manufacturing in sector 311, except subsector 3118 (bakeries), unless the food is sold with utensils provided by the seller (see subsection (4)(c) of this section).

(4) **What is "prepared food"?** Food or food ingredients are "prepared foods" if any one of the following is true:

(a) **Heated foods.** Food or food ingredients are "prepared foods" if sold in a heated state or are heated by the seller, except bakery items. "Bakery items" include bread, rolls, buns, biscuits, bagels, croissants, pastries, donuts, Danish, cakes, tortes, pies, tarts, muffins, bars,

cookies, and tortillas. Food is sold in a heated state or is heated by the seller when the seller provides the food to the customer at a temperature that is higher than the air temperature of the seller's establishment. Food is not sold in a heated state or heated by the seller if the customer, rather than the seller, heats the food in a microwave provided by the seller.

(b) **Combined foods.** Food or food ingredients are "prepared foods" if the item sold consists of two or more foods or food ingredients mixed or combined by the seller for sale as a single item, unless the food or food ingredients are any of the following:

- Bakery items (defined in (a) of this subsection);
- Items that the seller only cuts, repackages, or pasteurizes;
- Items that contain eggs, fish, meat, or poultry, in a raw or undercooked state requiring cooking as recommended by the federal Food and Drug Administration in chapter 3, part 401.11 of *The Food Code*, published by the Food and Drug Administration, as amended or renumbered as of January 1, 2003, so as to prevent foodborne illness; or
- Items sold in an unheated state as a single item at a price that varies based on weight or volume.

(Emphasis added).

Taxpayers do not dispute that the popcorn it sells is a prepared food (i.e., two or more foods or food ingredients mixed or combined for sale as a single item) under RCW 82.08.0293(2)(b)(i)(C) and Rule 244(4)(b). At page 3 of their Appeal Petitions, Taxpayers explain that the ingredients of their popcorn includes Popcorn kernels, a half-and-half mixture of corn and canola oil, and seasoning salt. In Det. No. 07-0282, 27 WTD 162 (2008), the Department held that a similar combination of ingredients was a prepared food, stating:

“Prepared food” is defined in the current statute to include two or more ingredients mixed or combined by the seller for sale as a single item. In the present case, the taxpayer combines raw popcorn, oil, salt, and sugar to produce kettle corn for sale.

We conclude that the popcorn Taxpayers sell is a “prepared food” under RCW 82.08.0293(2)(b)(i)(C) and Rule 244(4)(b), since it is the result of two or more food ingredients mixed or combined by the seller for sale as a single item. Taxpayers argue, however, that an exception to the definition of prepared food applies to their sale of popcorn, since they sell popcorn to customers without utensils in an unheated state by weight or volume as a single item, which is exempt from retail sales tax under RCW 82.08.0293(2)(b)(ii)(B) and Rule 244(4)(b). We first address whether Taxpayers sell popcorn by weight or volume as a single item. With respect to sales by weight or volume, interpretations of the Streamlined Sales and Use Tax Agreement (SSUTA) by the Streamlined Sales Tax Governing Board helps resolve this issue. RCW 82.02.210(3) requires the Department to administer and apply the retail sales tax in a manner consistent with the SSUTA. *See also North Central Washington Respiratory Care Services, Inc. v. Dep’t of Revenue*, 165 Wn. App. 616, 641-644, 268 P.3d 972 (2011).

Appendix C, Part II of the SSUTA, within the food and food products category, defines prepared food, in part, as follows:

“Prepared food” means:

- A. Food sold in a heated state or heated by the seller;
- B. Two or more food ingredients mixed or combined by the seller for sale as a single item; or
- C. 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 the food. . . .

The following may be taxed differently than “prepared food” and each other, if sold without eating utensils provided by the seller, but may not be taxed differently than the same item when classified under “food and food ingredients.” . . .

2. Food sold in an unheated state by weight or volume as a single item.

The definition of prepared food in the SSUTA is similar to the definition of prepared food in RCW 82.08.0293 and Rule 244. Rule 244(4)(b), which indicates that to sell in an unheated state as a single item by weight or volume means that the sale price must *vary* based on weight or volume. The language in Rule 244(4)(b) is consistent with guidance from the SSUTA on this issue. A Streamlined Sales Tax Project Discussion Paper (Paper), entitled “Food Definition Issues,” which the Streamlined Sales Tax Governing Board issued on January 10, 2005, explains:

Food sold by weight or volume means that the price will vary based on the weight or volume of the product a purchaser selects (e.g., it is sold by the pound and the price is determined by multiplying the weight selected by the price per pound).

Page 6 (emphasis added). *See also* New Jersey Division of Taxation Technical Bulletin NO. TB-71, issued May 13, 2013 (quoting the standard above of food sold by weight or volume, and giving examples of potato salad, roast beef, and cheese sold by the pound at a deli counter in a supermarket, and concluding that they are not subject to retail sales tax because they are sold by weight or volume); Michigan Revenue Administrative Bulletin No. 2009-8, issued October 21, 2009 (giving examples of cold macaroni salad sold by the pound, or deli items such as a potato salad, coleslaw, sliced meats, and vegetables sold by weight or volume, as not being subject to retail sales tax); reference tool authored by Utah Tax Commission, entitled “Sales and Use Tax Reduction and Food Ingredients, issued on December 19, 2006 (providing an example of a customer shopping at a grocery store that goes to the self-serve salad bar, makes a salad, and then has it weighed *and* priced at the cash register. Reference material concluded the grocery store sold salad to customer by weight).

Consistent with the SSUTA Paper above, we conclude that Taxpayers do not sell popcorn by weight or volume because the price does not vary based upon the weight or volume of the product purchased. Taxpayers’ customers (i.e., patrons of their movie theatres) do not select a certain quantity of popcorn, have that quantity weighed or measured, and then pay a price for that popcorn that is determined by multiplying the weight or measure of the popcorn by a price per unit; as the

example in the SSUTA Paper requires. Rather, Taxpayers' customers select a certain size container (small, medium, large, or extra large) of popcorn to purchase, and pay a set amount for that size container. In a similar scenario, the Department held that the sale of popcorn to customers by size of container does not qualify for the exclusion from prepared food in RCW 82.08.0293(2)(b)(ii)(B) and Rule 244(4)(b):

The taxpayer contends that the kettle corn is excluded from the definition of "prepared food" by RCW 82.08.0293(2)(b)(ii), which excludes food that is not sold with eating utensils provided by the seller, and is sold in an unheated state by weight or volume as a single item. The taxpayer argues that it sells popcorn by volume because it sells the popcorn in three different size bags. We agree that the popcorn is generally sold at room temperature and without eating utensils. However, we disagree with the taxpayer's claim that "sold ... by volume" means sold in more than one size. . . .

When food is sold by volume, the price of the food is based on the measured volume of the food sold. . . .

In the present case, the taxpayer sells at a price that varies by size rather than by unit of measure. The taxpayer's customers do not know the measured volume of popcorn they are purchasing and the price of the popcorn is not expressed as a function of measured volume. Therefore, the exception to the definition of prepared food for food sold in an unheated state by weight or volume does not apply. Accordingly, the taxpayer's sales of prepared food do not qualify for the food exemption and are subject to retail sales tax.

Det. No. 07-0282, 27 WTD 162 (2008) (footnotes omitted, emphasis added).

"Strained, unlikely or unrealistic" statutory interpretations are to be avoided. *Bour v. Johnson*, 122 Wn.2d 829, 835 (1993); *Christie-Lambert v. McLeod*, 39 Wn. App. 298, 302 (Div. 1 1984)(A statutory provision should be interpreted to avoid strained or absurd consequences that could result from a literal reading). If we were to equate size with food sold by weight or volume, than any retailer could simply have a list of food items for sale by small, medium, large or other similar measure, and under Taxpayers' reading of 82.08.0293(2)(b)(ii)(B) and Rule 244(4)(b), that item would be exempt from retail sales tax. This represents a strained and unrealistic interpretation of those provisions.

If Taxpayers sold popcorn to customers whereby the customer had a portion scooped from a large container, and then had it weighed on a scale, and the customer paid a price for the popcorn which equaled the ounces of popcorn multiplied by a price per ounce, then we would have a sale by weight or volume. However, Taxpayers' sale of small, medium, large, or extra large containers of popcorn is not exempt from retail sales tax under RCW 82.08.0293(2)(b)(ii)(B), Rule 244, the SSUTA, or 27 WTD 162.⁴ Therefore, we affirm the Department's issuance of Assessments 1-3.

⁴ Because of our holding on the sold by weight or volume issue, we do not need to address whether Taxpayers sell popcorn in a heated or unheated state. We reach no conclusion on that issue.

DECISION AND DISPOSITION

Taxpayers' petitions are denied.

Dated this 20th day of September 2013.