

ARIZONA DEPARTMENT OF REVENUE

ARIZONA TRANSACTION PRIVILEGE TAX RULING

TPR 93-45

(Note: On 9/23/2020 the statute references were changes to reflect their current numbers and footnotes were added. See footnotes for details. No substantive changes were made.)

This substantive policy statement is advisory only. A substantive policy statement does not include internal procedural documents that only affect the internal procedures of the agency and does not impose additional requirements or penalties on regulated parties or include confidential information or rules made in accordance with the Arizona administrative procedure act. If you believe that this substantive policy statement does impose additional requirements or penalties on regulated parties you may petition the agency under Arizona Revised Statutes § 41-1033 for a review of the statement.

ISSUE:

Taxation of premiums, gifts and prizes provided by restaurants and similar food service businesses.

APPLICABLE LAW:

Arizona Revised Statute (A.R.S.) § 42-5001(14)¹ states:

"Sale" means any transfer of title or possession, or both, exchange, barter, lease or rental, conditional or otherwise, in any manner or by any means whatever, including consignment transactions and auctions, of tangible personal property or other activities taxable under this chapter, for a consideration,...

A.R.S. § 42-5061² imposes the transaction privilege tax on the retail classification.

¹ This ruling originally cited A.R.S. § 42-1301.13 which was renumbered to A.R.S. § 42-5001(14).

² This ruling originally cited A.R.S. § 42-1310.01 which was renumbered to A.R.S. § 42-5061.

The retail classification is comprised of the business of selling tangible personal property at retail.

A.R.S. § 42-5061(V)(4)³ defines "selling at retail" as "a sale for any purpose other than for resale in the regular course of business in the form of tangible personal property,..."

A.R.S. § 42-5074(B)⁴ states: The tax base for the restaurant classification is the gross proceeds of sales or gross income derived from the business.

A.R.S. § 42-5151(22)⁵ defines "use or consumption" as the "exercise of any right or power over tangible personal property incidental to owning the property except holding for sale or selling the property in the regular course of business."

A.R.S. § 42-5155(A)⁶ imposes a "tax on the storage, use or consumption in this state of tangible personal property purchased from a retailer, as a percentage of the sales price."

DISCUSSION:

As part of the sale of food to restaurant patrons, restaurants may supply eating utensils, carrying packages, condiments and other related items. These items are often disposable and available to customers upon request. Additionally, a restaurant may conduct promotions in which customers receive prizes or gifts. The cost of the incidental items, such as plastic utensils, paper napkins and other disposable items sold by restaurants, are included in the cost of the food and are not subject to the transaction privilege tax. Restaurant customers are unconditionally entitled to possession of these items. *Shamrock Foods Company v. City of Phoenix*, 157 Ariz. 286, 757 P.2d 90 (1988). See Arizona Department of Revenue Transaction Privilege Tax Ruling TPR 93-25⁷. Similarly, premiums, gifts and prizes supplied as part of a meal package are incidental to selling food by restaurants. The cost of the premiums are included as part of the cost of the meal package upon which the transaction privilege tax is collected under the restaurant

³ This ruling originally cited A.R.S. § 42-1310.01.P.3 which was renumbered to A.R.S. § 42-5061(V)(4).

⁴ This ruling originally cited A.R.S. § 42-1310.14.P.3 which was renumbered to A.R.S. § 42-5061(V)(4).

⁵ This ruling originally cited A.R.S. § 42-1401.8 which was renumbered to A.R.S. § 42-5151(22).

⁶ This ruling originally cited A.R.S. § 42-1408.A which was renumbered to A.R.S. § 42-5155(A).

⁷ TPR 93-25 was rescinded in 2012.

classification. Therefore, a vendor's sale of these types of premiums, gifts and prizes is a nontaxable sale for resale. The restaurant must pay the transaction privilege tax on meal package sales under the restaurant classification. Further, food service businesses may offer premiums or gifts to patrons for visiting the establishment. The patron is not required to purchase any item in order to receive the gift. The gift is not incidental to the purchase of any tangible personal property. Therefore, a vendor selling the gifts to the restaurant must pay transaction privilege tax on gross proceeds from the sale of the gifts. In addition to serving food, restaurants may offer several different types of games and attractions to induce customers to visit the restaurants and increase their enjoyment of the restaurant. The games and attractions award premiums to those who successfully complete the games. The games are played with tokens included as part of a meal package or with tokens purchased from vending machines. A game regularly found at such a restaurant is "Crane Operator." Crane Operator requires the player to move a crane over a mound of toys and stuffed animals. The player attempts to win an item by dropping the crane directly on a toy to retrieve the item. "Skeeball" is another game often played at the restaurants. The game requires players to score as many points as possible by rolling a ball up a ramp and into a number of concentric rings. Skeeball awards its players, based on their score, with coupons which may be exchanged for premiums. The premium awarded to patrons upon successful completion of a game is not incidental to the purchase of the food. Only those who actually score enough points are entitled to possession of a premium. Further, there is no requirement to purchase food in order to obtain a premium and there is no relationship between the amount of food ordered and the premium that may be awarded. In selling a token, the restaurant is not engaging in a retail sale of the premium because there is no transfer of title or possession for a consideration. By purchasing a token, the customer is only receiving the right to play the game and the possibility of winning a prize. Therefore, the restaurant is using the premium as an inducement and attraction to the restaurant customer. The playing of the amusement by the customer and the purchase of the premium by the restaurant are two separate and distinct transactions which are being taxed under different classifications for different privileges. *Rowe International, Inc. v. Arizona Department of Revenue*, 165 Ariz. 122, 796 P.2d 924 (Ariz. App. 1990). The restaurant must pay the transaction privilege tax on token sales under the amusement classification. The vendor of the premium is required to pay transaction privilege tax on the sale of premiums to the restaurant.

RULING:

A premium which is supplied with the purchase of a meal is being transferred to the customer for a consideration as part of the meal, provided the obtaining of the premium is certain and does not depend upon chance or skill. The transaction is regarded as a sale of both the food and the premium. The sale of the premium by a vendor for such use by the restaurant is a sale for resale. Example: FastFood Restaurant sells a "Family Package" and a "Birthday Package" to customers. Each meal package consists of a hamburger, french fries, drink, and a toy. The toy is provided to all purchasers of the package. The sale of the toy by a vendor to the restaurant is a nontaxable sale for resale. Any prize or gift supplied by a restaurant to patrons for merely visiting the restaurant are not considered sales because there is no transfer of possession for a consideration. The sale of a premium for such purposes by a vendor to the restaurant is subject to transaction privilege tax. If the premium can be obtained only by restaurant customers who successfully operate a game dependent upon chance or skill, or if the premium can be obtained by customers who pay separately for the opportunity to acquire the premium, the premium is being used by the restaurant. Under these circumstances, sales of premiums, gifts or prizes to a restaurant are taxable as retail sales. Example: ABC Pizza Parlor sells pizza and food items to customers. The restaurant provides several games for its customers' enjoyment. A customer who purchases a pizza receives tokens which allow the purchaser to play the games. Another customer purchases tokens without purchasing food. Both customers successfully complete the game and are awarded prizes. A vendor is required to pay transaction privilege tax when selling the prizes to ABC Pizza Parlor.

Harold Scott, Director

Date Signed November 16, 1993

Explanatory Notice

The purpose of a tax ruling is to provide interpretive guidance to the general public and to department personnel. A tax ruling is intended to encompass issues of law which are not adequately covered in statute, case law or administrative rules. A tax

ruling is a position statement which provides interpretation, details or supplementary information concerning the application of the law. Relevant statute, case law, or administrative rules, as well as a subsequent ruling, may modify or negate any or all of the provisions of any tax ruling. See GTP 92-1 for more detailed information regarding documents issued by the Department of Revenue.