

ARIZONA TRANSACTION PRIVILEGE TAX RULING

TPR 00-4

(This ruling supersedes and rescinds Arizona Transaction Privilege Tax Ruling TPR 94-10)

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:

Exemption for sales or leases of tangible personal property to nonprofit charitable organizations that regularly serve meals to the needy and indigent on a continuing basis at no cost.

APPLICABLE LAW:

Arizona Revised Statutes (A.R.S.) § 42-5061(A)(25)(e), provides an exemption for tangible personal property sold to:

A nonprofit charitable organization that has qualified under § 501(c)(3) of the internal revenue code and that regularly serves meals to the needy and indigent on a continuing basis at no cost.

A.R.S. § 42-5159(A)(13)(j) provides a corresponding exemption from the use tax.

A.R.S. § 42-5071(B)(2) provides a deduction from the tax base of the personal property rental classification for gross income derived from:

Leases or rentals of tangible personal property which, if it had been purchased instead of leased or rented by the lessee, would have been exempt under ...
Section 42-5061, subsection A, paragraph ... 25.

DISCUSSION:

Sales of tangible personal property to a nonprofit charitable organization that has qualified under Internal Revenue Code (I.R.C.) § 501(c)(3) and that regularly serves meals to the needy and indigent on a continuing basis at no cost, are exempt from transaction privilege tax and use tax. Additionally, leases or rentals of tangible personal property to such an organization are exempt from transaction privilege tax under the personal property rental classification.

Recognition of I.R.C. § 501(c)(3) Status:

The organization must be recognized by the Internal Revenue Service as a nonprofit charitable organization under I.R.C. § 501(c)(3). The Internal Revenue Service (I.R.S.) issues a "Letter of Determination" to an organization meeting the qualifications of I.R.C. § 501(c)(3). The I.R.S. also issues letters of determination on a "group" basis.

An I.R.C. § 501(c)(3) organization may be a central organization that has subordinate organizations under its control. Instead of independently filing for I.R.C. § 501(c)(3) status, a subordinate organization of a larger central organization applies for I.R.C. § 501(c)(3) status through the central organization. The subordinate is subject to the general supervision or control of the central organization. If such a relationship exists between the organizations, the I.R.S. issues a Letter of Determination on a group basis. The central organization acts as the agent of the I.R.S. in ensuring that each subordinate qualifies as an exempt I.R.C. § 501(c)(3) organization.

For purposes of this ruling, a "qualifying organization" means any organization that has been granted I.R.C. § 501(c)(3) status; either as a subordinate I.R.C. § 501(c)(3) organization or as a central I.R.C. § 501(c)(3) organization. However, each I.R.C. § 501(c)(3) organization must independently meet the statutory requirement of regularly serving meals to the needy and indigent at no cost.

Example:

A central I.R.C. § 501(c)(3) organization regularly serves prepared lunches to needy and indigent persons at no cost. Sales or leases of tangible personal property to the central organization qualify for the exemption. A subordinate I.R.C. § 501(c)(3) organization operates a legal aid clinic. Sales or leases of tangible personal property to the legal aid clinic are not exempt because the subordinate organization does not serve meals to the needy. This specific subordinate I.R.C. § 501(c)(3) organization does not qualify for this exemption because of its affiliation with the central organization.

An I.R.C. § 501(c)(3) organization may have component subdivisions that are integral parts of the larger organization. For example, the component subdivisions may include operating divisions or departments that perform different functions for the organization, such as a finance

department, medical clinic, or food service department. By analogy to the terminology used in regard to corporations, these component subdivisions are similar to divisions within a corporation. For purposes of the exemptions at issue, qualifying status is extended to all internal operating or administrative component subdivisions of a qualifying I.R.C. § 501(c)(3) organization.

Example:

An I.R.C. § 501(c)(3) organization has five administrative component entities that operate under the direction and control of its executive board. Three divisions of the organization regularly serve prepared breakfasts and dinners to the needy at no cost. The fourth division operates a medical clinic and the fifth division operates a shelter for the homeless. Because the organization regularly serves meals to the needy at no cost, all types of tangible personal property sold to any division of the organization qualify for the exemption.

In regard to an I.R.S. letter of determination that is issued on a group basis, the subordinate organizations that are deemed separate I.R.C. § 501(c)(3) organizations by the I.R.S., are not considered to be component divisions of the central organization. This applies regardless of whether the subordinate organizations are incorporated or not.

Meal Program:

In addition to being an I.R.C. § 501(c)(3) nonprofit charitable organization, the organization must satisfy the statutory requirement of regularly serving meals to the needy and indigent on a continuing basis at no cost.

First, the organization must serve meals. Meals are hot or cold prepared food. Many organizations provide canned or other prepackaged food items to the needy. The needy then prepare the food on their own. Providing food in this manner does not constitute the serving of meals and the organization would not qualify for the exemptions at issue. Also, in regard to I.R.S. letters of determination that are issued on a group basis, subordinate I.R.C. § 501(c)(3) organizations that provide food or other assistance to affiliated organizations that operate meal programs, do not qualify for exemption. Only the I.R.C. § 501(c)(3) organization that actually conducts or operates a meal program on a continuing basis is entitled to the exemption.

A qualifying organization may also serve meals that are purchased from a catering service or other similar business. The sale of prepared meals by a catering service is taxable under the restaurant classification pursuant to A.R.S. § 42-5074. The exemptions for organizations that serve meals to the needy and indigent at no cost, are applicable only to sales under the retail classification or leases under the personal property rental classification. There is not a corresponding exemption under the restaurant classification applicable to organizations that

serve meals to the needy and indigent.

Second, the meals must be regularly served on a continuing basis. "Regularly served" means serving meals at predetermined intervals or customary times for eating. For example, customary times for eating include meals such as breakfast, lunch and/or dinner. A "continuing basis" means serving the meals at repeated time periods and not on an occasional or casual basis. For example, the daily serving of breakfast is a regularly served meal on a continuing basis. However, an organization that only serves holiday meals, such as Thanksgiving dinner, does not meet the requirement of regularly serving meals on a continuing basis. The department may require substantiation that the meals are served regularly on a continuing basis.

Third, the meals must be served to the needy and indigent. The needy and indigent include individuals who are destitute and helpless and also encompasses those persons who have some limited means, but whose means are not sufficient to adequately provide for their maintenance and support.

Meals provided to homebound persons do not qualify for the exemption unless the homebound persons are needy and indigent. For example, an organization that only delivers meals to senior citizens who cannot prepare meals for themselves but who have sufficient means to pay for such meals, does not qualify for the exemption. Sales of tangible personal property to such an organization are not exempt because the meals are not being provided to the needy and indigent. [Note: These organizations should consult Arizona Transaction Privilege Tax Ruling TPR 94-11 and A.R.S. § 42-5102(C)(4) to determine if sales of food to the organization are exempt.]

Finally, the meals must be served at no cost. An individual cannot be required to pay any monetary amount for the meal. However, the organization can accept donations from individuals who receive the meal as long as no one is required to pay a specific monetary amount in order to receive the meal. Federally subsidized meal programs, such as school lunch programs, do not qualify an organization for the exemptions at issue because the organization is receiving compensation for the meal program.

If the organization meets all of the listed statutory requirements, the organization is a "qualified organization." Sales and leases of tangible personal property to such qualified organizations are exempt from tax. The property does not have to be directly used in the serving of meals, but it must be used by an organization that serves meals to the needy and indigent. For example, sales of tables, chairs, and office supplies to a qualified organization are exempt from tax. Also, the sale of a television and clothing to the qualified organization for use in a shelter sponsored by the organization, are exempt from tax.

Documenting an Exempt Sale or Lease:

A.R.S. § 42-5009 outlines the requirements for an acceptable exemption certificate. Arizona Transaction Privilege Tax Procedure TPP 00-3, *Procedure for Use of Exemption Certificates*, explains how to use an exemption certificate. The department's ADOR Form 5000 is recommended. If an organization has a tax license number, it should be noted on the certificate; however, if it does not have a license number, it should notate "nonprofit 501(c)(3) organization." The department may challenge the validity of an exemption certificate if it has reason to believe that the vendor did not act in good faith in accepting the certificate, or that the certificate is not completed in its entirety.

A qualified organization should keep appropriate documentation to demonstrate that it is an I.R.C. § 501(c)(3) organization and that it regularly serves meals to the needy and indigent on a continuing basis at no cost. Usually, a vendor is not going to have sufficient information to determine that a particular organization qualifies as an I.R.C. § 501(c)(3) organization that regularly serves meals to the needy and indigent. To assist the vendors from which the organization purchases or leases tangible personal property, the department recommends that qualified organizations obtain a letter from the department that addresses the applicability of this exemption to the specific organization. By providing the appropriate documentation and facts about the organization and its meal program, the department can then issue a letter that can be copied and provided to vendors in conjunction with an exemption certificate.

RULING:

Gross income from sales or leases of tangible personal property to a qualified organization is exempt from transaction privilege tax. To be a qualified organization, the organization must be a nonprofit charitable I.R.C. § 501(c)(3) organization. The organization must serve cold or hot prepared meals. These meals must be served on a repeated basis at regularly defined intervals. Additionally, the meals must be provided to needy and indigent persons at no cost. The needy and indigent include individuals who are destitute and helpless, and also persons whose means are not sufficient to adequately provide for their maintenance and support.

An exempt sale or lease should be documented with an acceptable exemption certificate accompanied by a letter from the department. The nonprofit organization should also retain records which indicate that it qualifies for the exemption.

Mark W. Killian, Director
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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 that are not adequately covered in statute, case law or administrative rules. A tax ruling is a position statement that provides interpretation, detail, or supplementary information concerning 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 96-1 for more detailed information regarding documents issued by the Department of Revenue.