

14-1793

TAX TYPE: SALES & USE TAX

TAX YEAR: 6/1/11 – 2/28/14

DATE SIGNED: 5-26-2016

COMMISSIONERS: J. VALENTINE, M. CRAGUN, R. ROCKWELL

EXCUSED: R. PERO

GUIDING DECISION

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BEFORE THE UTAH STATE TAX COMMISSION

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<p>TAXPAYER,</p> <p style="text-align: center;">Petitioner,</p> <p>v.</p> <p>AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION,</p> <p style="text-align: center;">Respondent.</p>	<p style="text-align: center;"><b>INITIAL HEARING ORDER</b></p> <p>Appeal No. 14-1793</p> <p>Account No. #####</p> <p>Tax Type: Sales &amp; Use Tax</p> <p>Audit Period: 6/1/11 – 2/28/14</p> <p>Judge: Phan</p>
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**Presiding:**

Jane Phan, Administrative Law Judge

**Appearances:**

For Petitioner: REPRESENTATIVE FOR TAXPAYER, Attorney  
For Respondent: REPRESENTATIVE FOR RESPONDENT, Assistant Attorney  
General  
RESPONDENT, Deputy Director, Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission on January 26, 2016 for an Initial Hearing in accordance with Utah Code §59-1-502.5. Petitioner (“Taxpayer”) had filed an appeal of an audit deficiency under Utah Code §59-1-501. The Statutory Notice-Sales and Use Tax deficiency was issued by Respondent (“Division”) on September 2, 2014. The amount of tax deficiency indicated in the Notice was \$\$\$\$\$ in tax and \$\$\$\$\$ in interest for a total of \$\$\$\$\$ as of that date. Interest continues to accrue on any unpaid balance. No penalties were assessed with the audit. The issue addressed in this appeal was whether sales and use tax, including the restaurant tax, should be collected on event service charges.

APPLICABLE LAW

Utah Code §59-12-103(1)(e) (2013)<sup>1</sup> provides that “sales of prepared food” are subject to Utah sales and use tax.

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1 Some of the Utah Code provisions applicable in this case have been revised or renumbered, over

Utah Code §59-12-102(98) defines “purchase price” and “sales price,” as follows in pertinent part:

- (a) "Purchase price" and "sales price" mean the total amount of consideration:
  - (i) valued in money; and
  - (ii) for which tangible personal property, a product transferred electronically, or services are:
    - (A) sold;
    - (B) leased; or
    - (C) rented.
- (b) "Purchase price" and "sales price" include:
  - ....
  - (ii) expenses of the seller, including: (A) the cost of materials used; (B) a labor cost; (C) a service cost; (D) interest; (E) a loss; (F) the cost of transportation to the seller; or (G) a tax imposed on the seller;
  - (iii) a charge by the seller for any service necessary to complete the sale; or
  - ....

Utah Admin. Rule R865-19S-94<sup>2</sup> provides sales and use tax guidance concerning tips and gratuities associated with sales of prepared food as follows in pertinent part:

- (1) Restaurants, cafes, clubs, private clubs, and similar businesses must collect sales tax on tips or gratuities included on a patron's bill that are required to be paid.
  - (a) Tax on the required gratuity is due from a private club, even though the club is not open to the public.
  - (b) Voluntary tips left on the table or added to a credit card charge slip are not subject to sales tax.

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the course of the audit period but the parties do not argue any material differences in the Utah Code provisions. Unless indicated otherwise, the Commission cites the 2013 version of Utah Code.

2 This rule was revised on April 14, 2016, after the Initial Hearing was held, but prior to the issuance of this Order. The Commission applies the rule in effect during the audit period at issue in this matter as the revision to the rule was not made retrospective. Revised Utah Admin. Rule R865-19S-94, which became effective as of April 14, 2016 provides in relevant part:

- (1)(a) Restaurants, cafes, clubs, private clubs, and similar businesses must collect sales tax on service charges, tips, gratuities, cover charges, or other similar charges included on a patron's bill that are required to be paid.
- (b) Voluntary amounts left on the table or added to a credit card charge slip are not subject to sales tax.
- (2) A service charge, tip, gratuity, cover charge, or other similar charge that a restaurant, café, club, private club, or similar business includes on a patron's bill is presumed to be required unless:
  - (a) language on the front of the bill states that the service charge, tip, gratuity, cover charge, or other similar charge is voluntary and may be increased or decreased by the patron; and
  - (b) the language described in Subsection (2)(a) is in the same font size as the service charge, tip gratuity, cover charge, or other similar charge that the restaurant, café, club, private club, or similar business included on the bill.

....

Utah State Tax Commission Publication 55 (Revised June 2009) (“Publication 55”)<sup>3</sup> provides sales and use tax information for restaurants. Throughout the audit period, Publication 55 provided, as follows in pertinent part:

Tips and Gratuities

Tips are subject to sales tax if they are mandatory and are shown on the invoice. Service charges, gratuities or other charges shown on the invoice are also subject to tax.

Any charges subject to sales tax are also subject to restaurant tax.

Utah Code §59-12-603(1)(a)(ii) provides that “a county legislative body of any county may impose a tax of not to exceed 1% of all sales of the following that are sold by a restaurant: (A) alcoholic beverages; (B) food and food ingredients; or (C) prepared food.” Subsection 59-12-603(7)(a)(i) provides that the restaurant tax “shall be administered, collected, and enforced in accordance with: (A) the same procedures used to administer, collect, and enforce the tax under: (I) Part 1, Tax Collection; or (II) Part 2, Local Sales and Use Tax Act; and (B) Chapter 1, General Taxation Policies.”

Utah Code §59-1-1417 provides for the burden of proof and statutory construction as follows:

- (1) In a proceeding before the commission, the burden of proof is on the petitioner . . . .
- (2) Regardless of whether a taxpayer has paid or remitted a tax, fee, or charge, the commission or a court considering a case involving the tax, fee, or charge shall: (a) construe a statute imposing the tax, fee, or charge strictly in favor of the taxpayer; and (b) construe a statute providing an exemption from or credit against the tax, fee, or charge strictly against the taxpayer.

DISCUSSION

The basic facts in this matter were not in dispute. The Taxpayer is a reception center which provides prepared food and beverages with the facility rental for reception events. During the audit period at issue in this appeal, when a prospective customer contacts the Taxpayer about a proposed event, the Taxpayer first prepares a non-binding estimate for the prospective

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<sup>3</sup> Publication 55 was revised after the audit period effective September 2014. The Commission cites to the version of Publication 55 in effect throughout the audit period. Publication 55 and other publications are available on the Tax Commission’s website at <http://www.tax.utah.gov/forms-pubs/>.

customer.<sup>4</sup> The estimate lists out the various charges for the facility rental, linen and decoration packages, and the different food and beverage items. These charges are summed together and a “subtotal” is listed. The line directly below the subtotal states “Recommended Service Charge 18.00%” and then an amount is listed which is 18% of the “subtotal.” The line underneath the service charge states “Restaurant Tax 7.85%” and an amount is listed which is 7.85% of the taxable items listed above the “subtotal” line on the invoice but not on the 18% service charge. The estimate did state, “This estimate is not binding. Its purpose is to provide a basis on which to advise you about your budget. Actual pricing will vary based on your final selections and services.”

If the customer then decided to have the event at the Taxpayer’s facility, the Taxpayer and the customer would enter into a contract. The Taxpayer provided two examples of contracts used during the audit period.<sup>5</sup> Both samples of contracts stated under the Pricing & Payment Policy section that an “18% service charge is added to the entirety of the function bill.”<sup>6</sup> The final amount paid by the customer is determined by a final invoice prepared after the event. The Taxpayer provided a copy of a final invoice at the hearing.<sup>7</sup> This is very similar in format to the estimate. It lists out the charges for the facilities rental, various decoration packages and services along with food and beverage items. Just like the estimate, these charges are totaled for the “subtotal” and then the line under the “subtotal” states “Recommended Service Charge 18%.” An amount that is equal to 18% of the subtotal is filled out on this line and it is added in as part of the total due. All the lines on the invoice are in the same font size. The Taxpayer did not charge sales tax on this service charge fee to its customers.

The issue is whether the 18% service charge fee is subject to sales and use taxes, including the restaurant tax. It was the Division’s position with the audit that this was a service cost or a charge by the seller for a service necessary to complete the sale, so under Utah Code Subsection 59-12-102(98) this charge was part of the purchase price and subject to tax. The Division points as support to Utah Admin. Rule R865-19S-94(1), which during the audit period stated that restaurants and similar businesses “must collect sales tax on tips or gratuities included on a patron’s bill that are required to be paid.” It is the Division’s argument that the service charge is required to be paid by the customer. The Division also points to the language of the

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4 An example of this is Petitioner’s Exhibit 1.

5 Petitioner’s Exhibits 3 & 7.

6 Petitioner’s Exhibit 3, Pg. 2; Petitioner’s Exhibit 7, Pg. 1.

7 Petitioner’s Exhibit 4.

actual contracts which indicate an 18% service charge would be added and clearly negate any position that this service charge was voluntary.

The Taxpayer's representative argued that this service charge is voluntary. Utah Admin. Rule R865-19S-94(1)(b) had gone on to provide, "Voluntary tips left on the table or added to a credit card charge slip are not subject to sales tax." It was the Taxpayer's position that the language on the invoice that lists this as a "Recommended Service Charge" is sufficient to let its customers know that this was a voluntary charge. He points to the definition of "recommend" in the Merriam Webster Dictionary which states "to suggest that someone do (something)." See [www.merriam-webster.com/dictionary/recommend](http://www.merriam-webster.com/dictionary/recommend). It was his contention that a customer could have negotiated the amount of this charge with the Taxpayer.

The Taxpayer's representative stated that, in fact, there had been one event where the customer had increased this service charge amount to 20%, but he could provide no evidence that a customer had ever made the decision to not pay this service charge amount or had reduced the amount to something less than the 18%.

The Representative for the Taxpayer also stated that the Taxpayer is a small business. They had not charged sales tax on their service charge to their customers and the audit deficiency was a lot of money for the Taxpayer to now have to pay.

Both parties pointed to a prior Tax Commission Decision. *Petitioner v. Auditing Div. of the Utah State Tax Comm'n, Appeal No. 13-1970* (Utah State Tax Commission 2015). The issue in that case was whether automatically adding a gratuity to the bill for large parties constituted a mandatory charge. That appeal involved a restaurant that would add an 18% gratuity to parties of six or more to the bill. That restaurant did state in two different places on the menu, "For parties of 6 or more, an 18% gratuity will be added to your check. Please feel free to increase or decrease this gratuity at your discretion." However, on the bill itself the 18% gratuity was added into the subtotal. In that appeal, the Commission found that the "evidence, taken as a whole, does not give reason to find that the Taxpayer's automatic gratuities are voluntary tips." Factors noted by the Commission in that appeal were that the explanation provided on the menus was in very small print. There was no evidence that customers understood and exercised the option to pay less than 18% and the explanation was provided on the menu and not on the bill itself.

In this matter before the Commission, again, the evidence "taken as a whole" does not support that this service charge was voluntary. Utah Code §59-12-103(1)(e) provides that "sales

of prepared food” are subject to Utah sales and use tax.<sup>8</sup> Under Utah Code §59-12-102(98) (2013) “purchase price” includes “a charge by the seller for any service necessary to complete the sale . . .” As noted by the Taxpayer, this is a tax imposition statute. Under Utah Code Subsection 59-1-1417(2), the Tax Commission is to construe a statute imposing a tax strictly in favor of the taxpayer. However, the question of whether the specific charges at issue are for any services necessary to complete the sale turns on a finding of fact. As noted by the Division, the burden of proof, regarding questions of fact, is on the Taxpayer in this hearing at Utah Code Subsection 59-1-1417(1).

Looking at the facts and evidence provided at the hearing, the actual contract signed by the Taxpayer and customer states that an 18% service charge would be added to the total bill and makes it clear that the customer is required to pay this amount. There is no language in the contract indicating this was an optional amount that a customer could choose to pay or not pay. The customer is obligated to pay this by the contract they have signed. The contract language coupled with the fact that there is no clear statement on the final bill that the service charge was a voluntary charge supports the Division’s position in this matter. Merely stating on the final bill, “Recommended Service Charge 18%” is not sufficient to show that a customer could choose not to pay the charge, given the very express language used in the contract. For these reasons the audit should be upheld.

Jane Phan  
Administrative Law Judge

DECISION AND ORDER

Based on the foregoing, the Commission denies the Taxpayer’s appeal of the audit deficiency issued against the Taxpayer for the audit period of June 1, 2011 through February 28, 2014. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed, or emailed, to the address listed below and must include the Petitioner's name, address, and appeal number:

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<sup>8</sup> Utah Code §59-12-603 imposes the restaurant tax on prepared foods.

Utah State Tax Commission  
Appeals Division  
210 North 1950 West  
Salt Lake City, Utah 84134

or emailed to:  
taxappeals@utah.gov

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this \_\_\_\_\_ day of \_\_\_\_\_, 2016.

John L. Valentine  
Commission Chair

Michael J. Cragun  
Commissioner

Robert P. Pero  
Commissioner

Rebecca L. Rockwell  
Commissioner

**Notice of Payment Requirement: Any balance due as a result of this order must be paid within thirty (30) days of the date of this order, or a late payment penalty could be applied.**