

Taxing Delivery Charges for Meals: The Latest Delivery Model

by Stephen P. Kranz, Diann L. Smith, Catherine A. Battin, and Mark Yopp



Stephen P. Kranz



Diann L. Smith



Catherine A. Battin



Mark Yopp

Diann L. Smith is counsel, and Mark Yopp, Stephen P. Kranz, and Catherine Battin are partners with McDermott Will & Emery. Battin is in the firm's Chicago office, Kranz and Smith are in Washington, and Yopp is in the New York office.

In this edition of the State Tax Policy Exchange, the four discuss the rapidly emerging issue of taxing delivery charges for meals, including how sales tax is typically imposed on those charges and compliance tips for restaurants.

Just a decade ago, if you wanted a meal, you had to either cook it or drive to a restaurant. Maybe you could order pizza or Chinese food for delivery. But in today's gig economy, hungry consumers can get just about any food or meal delivered directly to them, whether it be a barbecue brisket sandwich or vegan lasagna for 12.

Restaurants are facing enormous pressure to meet the growing demands of consumers who want meals delivered

to their doors.¹ The Internet is making it easier than ever for consumers to place these orders by merely moving a finger,² and more companies are looking to connect consumers with their meal of choice (especially in larger cities).³ As restaurants and consumers use these third-party connections — usually for a price — new and thorny sales tax issues must be considered.

This article will describe the four typical models for prepared meal delivery; present a quick cheat sheet of typical sales tax imposition based on common factors involved in the transaction; provide additional details to aid restaurants, delivery providers, and third-party websites or app companies in evaluating the tax determination; and explain the risks of overcollecting or undercollecting sales tax on the delivery charges.

I. Representative Transactions

Transactions in this new era of food delivery are being structured in various ways, including:

- **Traditional Model:** The customer contacts the restaurant directly (for example, by phone or through the restaurant's website) and the restaurant sells the food to her. Restaurant employees deliver the food to the customer. The restaurant may charge for delivery separately or may provide the delivery without additional charge.
- **Outsourcing Model:** The restaurant sells the food to the customer and hires a third party to deliver it to her. In this case, the restaurant may pass the delivery charge directly to the customer or have the food delivered for free (that is, the restaurant absorbs the delivery cost). The transaction may be arranged directly between the

¹See Sheryl E. Kimes and Philipp F. Laqué, "Online, Mobile, and Text Food Ordering in the Restaurant Industry," *Cornell Hospitality Report*, vol. 11, no. 7 (2011); Cornell Center for Hospitality Research (noting that 40 percent of all adults have placed restaurant orders through a form of online software).

²E.g., Snapfinger, Seamless, GrubHub, Caviar, CityMint, and Delivery; although there are countless other popular service providers — many of which are equally or more popular in some areas.

³The same study found that 25 percent of restaurants now offer online ordering.

Transaction	Are Delivery Charges Subject to Sales Tax?
A Customer is not charged for delivery. Restaurant absorbs delivery cost. How delivery is accomplished is not relevant.	Restaurant (or third-party intermediary) must impose sales tax on entire charge to customer (no reduction for cost of delivery).
B Restaurant increases cost of food to account for delivery cost but does not separately state delivery charge on receipt to customer. How delivery is accomplished is not relevant.	Restaurant (or third-party intermediary) must impose sales tax on entire charge to customer (no reduction for delivery charge).
C Restaurant's own employees make the delivery to the customer <i>and</i> a delivery charge is separately stated on receipt to customer. (Traditional Model)	No universal answer. Options are: 1. If the transaction takes place in one of the 26 jurisdictions that has adopted the Streamlined Sales Tax, the likelihood ^a is that the restaurant (or third-party intermediary) must impose sales tax on delivery charge. ^b <i>Otherwise:</i> 2. Some states will always include the delivery charge in the taxable sales price. 3. Some states will only include the delivery charge in the taxable sales price if delivery is by the restaurant's employees, not a third-party. 4. Some states will impose sales tax, <i>unless</i> the customer has the option to pick up the food for take-out but chooses delivery. 5. Some states will not impose sales tax at all. 6. A very few states will impose tax on the delivery charge, even if the food is not subject to tax.
D Restaurant sells food directly to customer and pays an independent contractor or third-party service to deliver the food. A delivery charge is separately stated on the customer's receipt. (Outsourcing Model)	No universal answer. Options are: 1. If the transactions takes place in one of the 26 jurisdictions that has adopted the SSUTA, the likelihood ^a is that the restaurant (or third-party intermediary) must impose sales tax on delivery charge. ^b <i>Otherwise:</i> 2. Some states will always include the delivery charge in the taxable sales price. 3. Some states will impose sales tax, <i>unless</i> the customer has the option to pick up the food for takeout but chooses delivery. 4. Some states will not impose sales tax at all. 5. A very few states will impose tax on the delivery charge, even if the food not subject to tax.
E Customer arranges for delivery through use of third-party service that acts on behalf of the customer, not the restaurant. Customer pays restaurant for food and pays the third-party service for delivery. This may occur in a single transaction through a website or app. (Customer-Arranged Model)	Restaurant does not have tax collection obligation on the delivery fee. 1. The vast majority of states will not impose a sales tax on a delivery charge if the third-party service provider is not also selling what is being delivered. 2. A very few states will impose tax on the delivery charge.
F Customer arranges for delivery through use of third-party service that acts on behalf of customer, not the restaurant. Customer pays third-party for both food and delivery. Delivery charges are separately stated. (Resale Model)	1. Restaurant does not have tax collection obligation on the delivery fee (but may need to obtain sale for resale certificate from the third party on sale of food). 2. Third-party service provider will have same considerations as restaurant in boxes C or D.
^a However, a small minority of states adopting the SSUTA do not impose sales tax on delivery charges. ^b See http://www.streamlinedsalestax.org/otm/ , reference numbers 11000 and 11010 to determine taxability.	

customer and the restaurant, or the customer may use a third-party website or app to place the order.

- **Customer-Arranged Model:** The restaurant sells the food to the customer but the customer hires a third party to deliver it, typically through a third-party website or app. A delivery fee is usually charged.
- **Resale Model:** A customer purchases the food and the delivery of the food from a third party (typically through a third-party website or an app). The third party purchases the food from the designated restaurant then resells and delivers it to the customer.

The applicability of sales tax depends greatly on the contractual arrangements between the restaurant, the consumer, and the third party. From consumers' perspectives, all four transactions could appear the same: They open a website or an app, select their food, their credit card is

charged, and the food arrives. But legally, the tax treatment can be different based on the agreements among the parties.

II. Cheat Sheet: Sales Tax on Food Delivery Charges⁴

The chart above discusses typical issues and results for determining whether sales tax will apply to the costs or charges for delivering prepared meals to customers.

⁴The information provided here is just a summary and, as with any taxability determination, should not be relied on to determine actual tax responsibility in any jurisdiction.

III. Applying Sales Tax to Delivery Charges for Prepared Food

Unfortunately for anyone trying to comply with sales tax issues surrounding delivery charges for prepared food, there is no universal answer that applies in every state or locality.⁵ There are not even consistent criteria to determine whether those charges are subject to sales tax. There are, however, some factors that are commonly relevant to the tax determination.

When analyzing the taxability of delivery charges for the delivery of prepared meals (food delivery),⁶ there are two main components: the sale of the food and the delivery charges. The sale of prepared meals is taxable in virtually every state with a sales tax.⁷ However, the taxability of the delivery charge is more complicated because states have different provisions regarding the taxability of delivery services. Many factors may affect the taxability of those services, such as who provides the delivery, who pays for it, who arranges it, how delivery charges are billed, where the delivery occurs, and whether there is a pickup option.⁸

First, who arranges for the delivery is a significant taxability factor in many states. Restaurants may arrange for and provide the delivery themselves through their employees or third parties. Customers may purchase food for delivery from a restaurant by phone, via a restaurant website, or through a third-party website or app. Alternatively, consumers may purchase food for delivery not from the restaurant, but through a third party (through an app or other product). The third party may or may not have a direct relationship with the restaurant, but instead may provide delivery on behalf of consumers. For instance, in the Traditional Model, the taxability of delivery charges is typically determined by whether the charges are included by law in the definition of sales price of the tangible personal property (that is, the food) being delivered. However, in the

⁵States also use different terms for identifying those charges. Typically, states may use either the term “delivery charges” or “transportation charges.” This article will adopt the term “delivery charges” for simplicity.

⁶Although the taxability of grocery delivery contains its own issues and could be included in “food delivery,” in this article we will focus on the delivery of prepared meals.

⁷See Jerome R. Hellerstein and Walter Hellerstein, *State Taxation*, 13.09: Food and Meals (3d ed. 1998, current through 2015). Of course, some states will have exemptions for specific products.

⁸Typically, but once again not universally, even if delivery services are not enumerated as taxable, one or more of these factors may determine whether the tax jurisdiction includes the delivery charge in the sales price — the base on which the sales tax is calculated. The concept of sales price (or purchase price or receipts) is of fundamental importance in many states to determining whether delivery charges are subject to sales tax. If delivery charges are included in the sales price and the food is subject to sales tax, the delivery charges will also be subject to sales tax. In a few jurisdictions, even if the delivery charges are not included in the sales price for the taxable food, they may still be subject to tax as a separate, but taxable, service.

Customer-Arranged Model, the customer is purchasing the food and the delivery services separately, which can significantly affect the taxability. In all of these scenarios, the contractual arrangement should be scrutinized. As noted, the same transaction could appear the same to the customer for practical purposes, but the taxability would differ if under an Outsourcing Model or a Resale Model.

Second, whether the delivery charges are separately stated on the consumer’s bill affects their taxability in many states. If the charge is not separately stated, delivery will almost always be subject to tax if the food is taxable.

Other factors may also affect the taxability. Delivery services are exempt in a few states if the meal can be picked up at the restaurant. The sourcing of a transaction — that is, the location where the transaction occurs such that it is subject to sales tax — can affect the taxability. This issue is most likely to occur when the restaurant is in one locality and the place of delivery is in another. The transaction will not always be sourced to the restaurant making the sale, and could be sourced to the delivery location.

A. Who Provides Delivery

1. Traditional Model

If the restaurant is providing the delivery through its employees, the primary question is whether separately stating delivery charges on the customer’s bill would affect the service’s taxability.

If the delivery charges are not separately stated, they would be included in the definition of sales price and thus subject to tax along with the charge for prepared food. If delivery charges are separately stated, the jurisdiction’s tax law should be studied more.

Some states exclude delivery charges from the taxable sales price if they are separately stated on the bill.⁹ This is true regardless of which party arranges for the delivery. Other states (such as New York¹⁰ and Texas¹¹) include the delivery charge in the definition of sales price, even if separately stated, and thus tax it — but only if the restaurant makes or arranges for the delivery.

⁹For example, Massachusetts provides that transportation charges are not taxable if: (1) the charges reflect a cost of preparing and moving the goods to a location designated by a retail customer; (2) *the charge is separately stated on the invoice to the customer*; and (3) the charge is set in good faith and reasonably reflects the actual costs incurred by the vendor. Massachusetts Department of Revenue Directive No. 06-3 (Apr. 4, 2006) (emphasis added). Arizona is another state that does not tax separately stated charges. Under Ariz. Admin. Code section R15-5-133(A), a charge by a retailer for delivery from the retailer’s location to the purchaser’s location, if separately stated on the sales invoice, is not taxable. Similarly, Virginia provides that “tax does not apply to transportation or delivery charges added to a taxable sale provided such transportation charges are separately stated on the invoice to the customer.” Va. Admin. Code 10-210-6000(A).

¹⁰N.Y. Tax Law section 1101(b)(3).

¹¹Texas Tax Code Ann. sections 151.007(a)(3)-(4).

For approximately half of the states, there is a matrix allowing vendors to determine whether a food delivery charge is subject to sales tax. The Streamlined Sales and Use Tax Agreement, a multistate agreement under which 24 states¹² have agreed to uniform definitions for various products, allows states to determine whether specifically defined delivery charges are taxed. Delivery charges are “charges by the [restaurant] . . . for preparation and delivery to a location designated by the purchaser.”¹³ Most SSUTA states include delivery charges in the definition of sales price, even if separately stated, thus taxing those charges.¹⁴

2. Outsourcing Model

Another delivery paradigm is for the restaurant to contract with a delivery service either directly (by hiring a delivery service provider itself) or indirectly (by allowing the restaurant to be listed on a third-party app or other delivery facilitator). The key difference between this situation and one discussed below (in which the customer contracts with the third party) is that the restaurant undertakes an additional obligation associated with the delivery. While the restaurant cannot be responsible for collecting tax on services it did not contract for (as is the case when the customer alone contracts for delivery), when a restaurant contracts with a third party to deliver its food (through an app or otherwise), it may be required to collect tax on the receipts received from the customer for delivery.

In some jurisdictions, even though there may be no difference from the customer’s point of view if the restaurant uses a third party for delivery rather than its employees, this distinction can be crucial for applying the sales tax to delivery charges. For instance, in California, separately stated delivery charges may be included in the sales price when delivery is provided by “facilities of the retailer,” but are not included in the sales price and not taxable when separately stated and provided by a third party (such as a common carrier or independent contractor).¹⁵ In Texas, a third-party carrier (separate legal entity) is not responsible for collecting or remitting tax as long as the third-party carrier only provides transportation and does not sell the taxable item being delivered.¹⁶ However, in New York,

delivery charges are included in the sales price if provided by the vendor or “arranged for by the vendor.”¹⁷

3. Customer Contracts With Third Party

a. Customer-Arranged Model

If a customer contracts with a third party for the delivery, the restaurant should not have a sales tax collection obligation on any delivery service charge. The question becomes whether the delivery service will have to charge sales tax on its delivery charge. While this does not directly affect the restaurant’s tax liability, it does affect the economics of ordering food for delivery from the customer’s point of view. Taxability will depend on how the transaction between the customer and the third party is structured contractually.

b. Resale Model

When the restaurant arranges for delivery by a third party, there may be sale-for-resale considerations. If the business model of the app is such that the delivery company purchases the food from the restaurant and then resells it, including delivery, restaurants should obtain a sale-for-resale certificate from the delivery company. Otherwise, the restaurant could be responsible for sales tax on the food charge — a tax that the restaurant did not collect from the delivery company or its customer.

B. Effect of Allowing Pickup or Delivery

In some states, giving customers the option to pick up the food may affect taxability. For instance, in Florida, if food may be picked up free of charge from the restaurant, delivery charges are not taxable.¹⁸ Therefore, the general rule in Florida is that delivery charges are not subject to tax when two conditions have been met: The charge is separately stated on an invoice or bill of sale; and the charge can be avoided by a decision or action solely on the part of the purchaser (that is, the purchaser can pick up the item for no extra charge).¹⁹ The same is true in Illinois.²⁰

¹²As of October 15, 2015, the states participating are Arkansas, Georgia, Indiana, Iowa, Kansas, Kentucky, Michigan, Minnesota, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, South Dakota, Utah, Vermont, Washington, West Virginia, Wisconsin, Wyoming. Tennessee is in substantial compliance but is not a full member.

¹³See Streamlined Sale and Use Tax Agreement, Appendix C, Part I (defining delivery service), as amended through May 13, 2015.

¹⁴States providing the exemption include Nevada, Oklahoma, and Utah.

¹⁵Calif. Rev. & Tax Code sections 6011(c)(7); 6012(c)(7); and Cal. Code Regs., tit. 18, section 1628.

¹⁶See Texas Admin. Code section 3.303(b); see also Texas Policy Letter Ruling No. 9808700L (August 7, 1998).

¹⁷N.Y. Tax Law section 1105(d)(i)(2). New York recently addressed the tax liability of the app/website operator in the food delivery scenario. See NY TSB-A-14(27)S (Aug. 20, 2014). In this ruling, the New York State Department of Taxation and Finance concluded that a taxpayer that operated a website to facilitate food delivery from over 5,000 restaurants was not operating a restaurant, a catering service, or similar establishment and was therefore not a food vendor responsible for collecting sales taxes on its fees. In the department’s view, the taxpayer was providing a combination of nontaxable Internet advertising services and fulfillment services to the restaurants. Also, because the taxpayer was providing fulfillment services to the restaurants, it could not be treated as a co-vendor jointly responsible for sales tax collection. However, because the restaurant was responsible for delivery, the department held that the restaurant remained responsible for remitting sales tax on delivery charges, in addition to any sales tax remitted for the food. *Id.*

¹⁸Fla. Admin. Code Ann. section 12A-1.045(4)(a).

¹⁹*Id.*

²⁰See 86 Ill. Admin. Code 130.415(d).

C. Sourcing and Local Taxes

As with existing sales tax compliance concerns, restaurants making deliveries in multiple jurisdictions should be aware of the rules in each jurisdiction, regardless of whether the local sales tax is administered by the state, as in Washington,²¹ or the locality, as in Colorado.²²

D. Other Considerations

Restaurants and third parties will have to review other considerations such as tips, sales tax rates, container fees, and additional taxes on products such as alcohol.

VI. Conclusion

The sales tax treatment of delivery services varies among the states and the body of law governing it continues to evolve. As the number of delivery service options increase with the expansion of third-party platforms available to order and deliver food, companies must carefully review the rules in various jurisdictions to ensure compliance and avoid unnecessary tax risks. ☆

²¹Rev. Code Wash. section 82.14.050.

²²Colorado Constitution, Article XX, section 6.

TAX ANALYSTS BOARD OF DIRECTORS

Christopher E. Bergin

Tax Analysts
Falls Church, Virginia

John L. Buckley

Georgetown University Law Center
Washington, D.C.

Edward W. Erickson

Retired
North Carolina State University
Raleigh, North Carolina

Thomas L. Evans

Kirkland & Ellis LLP
Chicago, Illinois

Lawrence B. Gibbs

Miller & Chevalier
Washington, D.C.

David J. Kautter

American University
Washington, D.C.

Larry R. Langdon

Mayer Brown LLP
Palo Alto, California

Richard G. Larsen

Distinguished Professor of Accounting
George Mason University
Retired Partner
National Tax Department
Ernst & Young LLP
Fairfax, Virginia

Martin Lobel, Esq.

Lobel, Novins & Lamont LLP
Washington, D.C.

Pamela F. Olson

PricewaterhouseCoopers LLP
Washington, D.C.

Deborah H. Schenk

NYU School of Law
New York, New York

Arthur W. Wright

Professor Emeritus of Economics
University of Connecticut
Storrs, Connecticut

Eric M. Zolt

UCLA School of Law
Los Angeles, California