

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition :
of :

AUTOMATIQUE, INC. :

for Revision of a Determination or for Refund :
of Sales and Use Taxes under Articles 28 and 29 :
of the Tax Law for the Period September 1, 1985 :
through May 31, 1988. :

In the Matter of the Petition :
of :

ROBERT A. LAUDICINA, :
OFFICER OF AUTOMATIQUE, INC. :

for Revision of a Determination or for Refund :
of Sales and Use Taxes under Articles 28 and 29 :
of the Tax Law for the Period September 1, 1985 :
through May 31, 1988. :

In the Matter of the Petition :
of :

DONALD A. SILVERSTONE, :
OFFICER OF AUTOMATIQUE, INC. :

for Revision of a Determination or for Refund :
of Sales and Use Taxes under Articles 28 and 29 :
of the Tax Law for the Period September 1, 1985 :
through May 31, 1988. :

In the Matter of the Petition :
of :

ARTHUR STEVENS, :
OFFICER OF AUTOMATIQUE, INC. :

for Revision of a Determination or for Refund :
of Sales and Use Taxes under Articles 28 and 29 :
of the Tax Law for the Period September 1, 1985 :
through May 31, 1988. :

DECISION
DTA NOS. 806584,
806585, 806586,
806587 & 806588

In the Matter of the Petition	:
of	:
WALTER S. WELYTOK,	:
OFFICER OF AUTOMATIQUE, INC.	:
for Revision of a Determination or for Refund	:
of Sales and Use Taxes under Articles 28 and 29	:
of the Tax Law for the Period September 1, 1985	:
through May 31, 1988.	:

The Division of Taxation and petitioners Automatique, Inc., Robert A. Laudicina, Donald A. Silverstone, Arthur Stevens, and Walter S. Welytok, officers of Automatique, Inc., 3269 Roanoke Road, Kansas City, Missouri 64111, each filed an exception to the determination of the Administrative Law Judge issued on May 23, 1991 with respect to petitioners' petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period September 1, 1985 through May 31, 1988. The Division of Taxation appeared by William F. Collins, Esq. (Robert J. Jarvis, Esq., of counsel). Petitioners appeared by Morrison & Hecker, Esqs. (George F. Crawford, Esq., of counsel).

Petitioners filed a brief on exception and a reply brief to the Division of Taxation's exception. The Division of Taxation did not file any briefs. Oral argument, at petitioners' and the Division of Taxation's request, was heard on September 10, 1992.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

ISSUES

- I. Whether Automatique, Inc.'s recurring purchases of paper and plastic products were purchases for resale not subject to the sales and use tax.
- II. Whether Automatique, Inc. may claim a manufacturing exemption for certain equipment purchased for use in the production of food at its manufacturing facility.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law judge except for finding of fact "1" which has been modified, and findings of fact "13" - "18" and "20" which have been deleted.¹ We have also made an additional finding of fact. The Administrative Law Judge's findings of fact, the modified finding of fact and the additional finding of fact are set forth below.

We modify the Administrative Law Judge's finding of fact "1" as follows:

The corporate petitioner, Automatique, Inc.² (hereinafter "Automatique"), is a Delaware corporation with three branches in the Midwest (Kansas City, St. Louis and Des Moines) and a New York City branch, which has been authorized to do business in New York since August 10, 1972. The New York City operation involves primarily food production, while the Midwest operation involves primarily vending machine services. Automatique's business in New York City is essentially twofold: the preparation and sale of bulk food to certain exempt organizations; and the operation of cafeterias at certain educational institutions.³

The Division of Taxation issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due dated November 18, 1988 against Automatique asserting tax due of \$81,890.79, plus penalty and notices, also

¹Findings of fact "13," "14," "15," "16," "17," "18" and "20" have been omitted as they relate to issues decided by the Administrative Law Judge but not excepted to by either petitioners or the Division of Taxation.

²

On August 1, 1989, Automatique changed its name to Ambassador Food Services Corporation.

³

Finding of fact "1" of the Administrative Law Judge's determination originally read as follows:

"The corporate petitioner, Automatique, Inc.^{*} (hereinafter "Automatique"), is a Delaware corporation with three branches in the Midwest (Kansas City, St. Louis and Des Moines) and a New York City branch, which has been authorized to do business in New York since August 10, 1972. The New York City operation involves primarily food production, while the Midwest operation involves primarily vending machine services.

^{*}"On August 1, 1989, Automatique changed its name to Ambassador Food Services Corporation."

Finding of fact "1" of the Administrative Law Judge's determination was modified to include more detail from the record.

dated November 18, 1988, were issued against each of the four named officers of Automatique. None of the officers challenged their status as persons required to collect sales tax on behalf of Automatique.

Automatique's records were adequate to warrant an audit method that utilized all records within the audit period. However, in lieu of such an audit of recurring purchases, Automatique agreed to the utilization of a representative test period audit method. Petitioners did not challenge the methodology of such estimated audit.

The field audit report summarized the results of the audit performed as follows:

	<u>Additional Taxable</u>	<u>Additional Tax Due</u>
Sales	\$ 50,846.00	\$ 4,194.79
Purchases/Expenses	692,944.00	57,167.88
Assets	<u>248,826.00</u>	<u>20,528.12</u>
Totals	<u>\$992,616.00</u>	<u>\$81,890.79</u>

The additional tax due for purchases/expenses was determined by a test of such expenses for the month of September 1987. An error percentage was calculated in relationship to gross sales for the test month and was then applied to gross sales for each quarter in the audit period.

According to the audit report:

"Vendor did not report purchases of plastic flatware, napkins, straws, and other supply items which were purchased and used by vendor on a recurring basis as tax exempt items." (Emphasis added.)

The additional tax due for sales was based upon the auditor's disallowance of nontaxable sales claimed of \$50,846.00 for the entire audit period:

"Vendor did not have exempt certificates on file, and the resale and exempt numbers relating to the nontaxable sales were found to be nonexistent in NYS Tax & Finance files."

The additional tax due for assets was based upon a detailed audit of the fixed asset purchases of Automatique during the entire audit period:

"Vendor did not pay any sales tax on the majority of its asset purchases from its suppliers for the audit period."

Subsequent to the issuance of the notices, the assessment was reduced by the Division of Taxation to \$67,588.59, plus penalty and interest. Petitioners are contesting only \$25,976.68 of the \$67,588.59 asserted as due.⁴ The \$25,976.68 includes the following sales and use taxes asserted as due:

<u>Amount</u>	<u>Description of Tax Asserted as Due</u>
\$ 9,967.75	Tax on recurring purchases of paper and plastic products which petitioners claim were resold to exempt organizations along with the sale of bulk foodstuffs
\$ 6,810.06	Tax on recurring purchases of paper and plastic products which petitioners claim were resold at cafeterias it operated for exempt organizations
\$ 3,286.07	Tax on purchases of items petitioners claim were installed as capital improvements to real property of exempt organizations or, in the alternative, were resold to such exempt organizations
\$ 1,149.14	Tax on purchases of equipment petitioners claim were resold to Brooklyn College
\$ 943.14	Tax on purchases of equipment petitioners claim were resold to Bronx Community College
\$ 2,560.59	Tax on purchases of equipment petitioners claim were resold to Long Island University
\$ 1,259.94	Tax on purchases of equipment petitioners claim were for use in producing tangible personal property
<u>\$25,976.68</u>	Total

The \$9,967.75, which represents tax assessed on what petitioners claim were resales of paper and plastic products (napkins, stirrers, straws, utensils), as part of the sale of bulk foodstuffs to exempt organizations, is made up of the following:

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It appears that petitioner conceded liability for additional sales and use tax on certain recurring purchases of operating supplies and for repair and maintenance services, although the record does not include a clear explanation by either party concerning the conceded portion of the audit.

	Tax Asserted as Due
1. New York City Human Resources Administration	
Crisis Intervention Services	\$6,508.17
Special Services for Children	259.82
Emergency Assistance Units	<u>980.06</u>
Total H.R.A.	\$7,748.05
2. Salvation Army	1,051.97
3. American Red Cross	<u>1,167.57</u>
	<u>\$ 9,967.59</u>

Automatique was the successful bidder on several proposals for bids for food services issued by the Human Resources Administration, Department of Social Services of the City of New York (hereinafter "HRA"). The HRA, as a governmental entity, was exempt from payment of sales and use taxes. Automatique introduced evidence of 10 formal contracts which it entered into with the HRA on the basis of its successful bids in accordance with HRA specifications. The HRA contracts provided for the furnishing of meals and other food and beverage products to facilities operated by the following subunits of the HRA:

Crisis Intervention Services (hereinafter, "CIS")
 Economic Assistance Units (hereinafter, "EAU")
 Special Services for Children (hereinafter, "SSC")

There were four CIS contracts in effect during the audit period as follows:

<u>Petitioners'</u> <u>Exhibit</u>	<u>Period Covered</u>	<u>Maximum Amount</u>
20-1	December 1985 through December 31, 1986	Unstated
20-2	January 29, 1987 through June 30, 1987	\$1,885,717.35
20-3	July 1, 1987 through August 31, 1987	\$1,885,717.35
20-4	September 1, 1987 through June 30, 1988	\$5,331,025.00

These contracts all required Automatique to prepare and deliver meals to family emergency centers at various locations throughout New York City. The meals were prepared and delivered by Automatique personnel in (steam-table type) aluminum foil pans, and

approximately 80 people could be fed from one pan. Automatique personnel did not serve the meals and had no contact with the persons to whom the meals were served. Invoices for such meals were submitted to HRA on a weekly basis, and payment was made periodically by the City of New York.

The specifications in the CIS contracts included the following requirements regarding the products to be furnished:

Petitioners' Exhibit 20-1 (Page 52):

"3. The food must be delivered at the beginning of the serving period of each meal. The food for each meal must be delivered to the specifically designated Crisis Intervention Services employee or employees on duty, and a signed receipt must be obtained from such person(s). The identity of the staff person will be revealed upon the award of the contract. Crisis Intervention Services will call to inform the contractor, prior to the delivery of each meal, of the number of clients to be fed. The calls will be made at least two (2) hours prior to the scheduled serving time of each meal....

4. The contractor shall deliver all meals in large covered serving bins. Sandwiches must be wrapped in clear plastic wrappers. Food must be transported in vehicles equipped with refrigeration for the storage of cold foods, and with heaters for the storage of hot foods....

5. The contractor must provide steam tables at the Family Shelter to keep the food hot while it is served at the site. The contractor shall provide soup bowls as applicable, heavy duty sectioned paper plates, plastic flatware, packets of sugar, pepper, salt, margarine, slices of lemon and other necessary items with each meal. The contractor must also provide heavy duty trays for each person served at each meal. The contractor will be responsible for cleaning the serving bins and the heavy duty trays. At the contractor's option, the trays may be inventoried and stored at the site. All meals shall be served by the staff of Family Shelter." (Emphasis added.)

The other three CIS contracts included substantially identical specifications.

There were three EAU contracts in effect during the audit period as follows:

<u>Petitioners' Exhibit</u>	<u>Period Covered</u>	<u>Maximum Amount</u>
21-1	July 1, 1985 through June 30, 1986	Unstated
21-2	April 1, 1986 to June 30, 1987	\$602,321.69
21-3	August 1, 1987 to July 31, 1988	\$537,268.44

The EAU contracts included the following provisions:

Petitioners' Exhibit 21-1 (Page 52):

"Catering service for the provision of assorted sandwiches, whole milk and fruit juices seven (7) days per week as set forth in Exhibits Ia - Ih which are attached and made a part of this agreement for the Human Resources Administration Emergency Assistance Unit locations at 241 Church Street, New York, New York; 92-16 147th Place, Queens, New York; 414 E. 147th Street, Bronx, New York; and 114 Willoughby Street, Brooklyn, New York.... The number of sandwiches, whole milk and fruit juices that are stipulated in Exhibits Ia - Ih are to be delivered no later than 4:00 p.m. each day.

The food must be delivered to a specifically designated staff member of EAU and a signed receipt obtained from said staff person. The identity of the staff person will be revealed upon the award of the agreement. All food provided must meet quality standards set forth in the USDA codes which are attached hereto and made a part of this agreement (Attachment A). One half the number of sandwiches must be made with white bread, and one half with whole wheat bread. All sandwiches must be individually wrapped in clear plastic wrappers and transported in vehicles equipped for this service." (Emphasis added.)

The other two EAU contracts included substantially identical specifications.

The cover sheets for the proposals for bids for two of the three contracts were marked into evidence as part of petitioners' Exhibit "21". These cover sheets both refer to the service to be provided as a "catering service". The cover sheet for the contract covering the period July 1, 1985 through June 30, 1986 noted that the bidder was "(t)o furnish al [sic] labor and materials necessary and required for catering service."

There were three SSC contracts in effect during the audit period as follows:

<u>Petitioners' Exhibit</u>	<u>Period Covered</u>	<u>Maximum Amount</u>
22-1	February 4, 1987 to January 31, 1988	\$251,652.74
22-2	Date of Award through June 30, 1987	Unstated
22-3	March 20, 1987 through June 30, 1988	\$446,692.95

The SSC contracts required the delivery of "preplated frozen" meals to special service units of HRA at various specified locations. These contracts included the following provisions:

Petitioners' Exhibit 22-1 (Pages 80-81):

"4. The food must be delivered at the beginning of the serving period of each meal. At each site, the contractor shall deliver all food and supplies to the point or points and at the times specified by the Field Office Director or his/her designee. The food for each meal must be delivered to the designated employee on duty, and a signed receipt must be obtained for each such delivery. Upon the award of the contract, the contractor shall be informed of the identity of SSC staff members authorized to accept food deliveries. SSC will telephone to inform the contractor, prior to the delivery of meals, of the number of clients to be fed. The call will be made at least two (2) hours prior to the scheduled serving time of each meal as indicated in Exhibit II which is attached hereto and made a part hereof. Upon request, the contractor will provide meals for persons with special dietary requirements.

* * *

6. The contractor shall provide soup bowls as applicable, heavy duty sectioned paper plates, plastic flatware, packets of sugar, pepper, salt, margarine, slices of lemon and all other necessary items to complete each meal. The contractor will be responsible for cleaning the serving bins and the heavy duty trays. At the contractor's opinion [sic], the trays may be inventoried and stored at the location. All meals shall be served by the staff of SSC." (Emphasis added.)

Petitioners' Exhibit 22-2 (Page not numbered):

"4. Upon the award of the contract, the contractor shall be informed by the agency's Director of Institutional Field Service or his/her designee of the identity of the person/persons in charge of the special Diet Program. The agency shall order the meals on a per case basis (a case shall consist of 24 meals.) The designated person/persons will telephone the contractor, one week in advance of the requested delivery date to advise the Contractor of the number of cases of each particular meal needed at each location(s). All meals shall be delivered in a solid frozen state. Contractor shall not substitute for any ordered entree without the prior approval of person/persons in charge of the special diet program, [sic] Said substitution must be requested at least 48 hrs prior to a scheduled delivery.

5. The meals shall be delivered on a bi-weekly basis, Monday through Friday between the hours of 6:00 AM and 2:00 PM in accordance with the provisions of this paragraph and paragraph 4 above. Said Meals shall be delivered and off-loaded onto receiving platforms or at such other agency designated area at each location. An invoice must accompany each delivery. The invoice must be signed by the designated HRA staff member and one copy left with said person." (Emphasis added.)

Petitioners' Exhibit 22-3: This SSC Contract related to the same locations as Exhibit 22-2 and represented an extension thereof.

A review of the pages from the latter two contracts, submitted into evidence as part of petitioners' Exhibit "22", does not disclose any explicit reference to the provision of paper products by Automatique. These contracts describe the scope of Automatique's performance in

terms of it supplying preplated, frozen, and microwavable meals. Nonetheless, Automatique apparently provided all necessary paper goods and eating utensils.

None of Automatique's contracts with HRA involved service or transactional relationships between Automatique personnel and the persons to whom the meals were provided by HRA. All of the contract prices charged by Automatique to the HRA included all necessary paper goods, eating utensils and appropriate condiments.

Automatique also provided meals on a contract basis to the Salvation Army, a tax-exempt organization. Under the Salvation Army contracts, Automatique delivered meals, as prescribed in menus⁵ included in the contracts, in bulk form, to specified locations for service by Salvation Army personnel. The prices charged to the Salvation Army included paper goods (plates, bowls, cups and napkins) and eating utensils (plastic spoons, knives and forks). Under these contracts, Automatique was paid by the Salvation Army on a per diem basis per client served by the Salvation Army.

Automatique also provided meals to the Red Cross, a tax-exempt organization, for service to its clients at two family centers in New York City, pursuant to a letter agreement dated March 3, 1987. The letter agreement specified that the contract price included spoons and paper products, and also made clear that such meals were provided on a "drop-off" basis. Automatique's activities in performance of this agreement were contracts. An Automatique invoice dated September 23, 1987 in the amount of \$689.38 was submitted to the Red Cross for paper plates, cups, cereal bowls, napkins and spoons provided and sold to the Red Cross by Automatique during the test period. No explanation was provided why, apparently in this one instance, a separate invoice was issued for paper and plastic goods.⁶ It appears that the usual practice was for Automatique to bill for such items as part of its overall charge and invoices did not separately show the price of paper and plastic products.

⁵These menus noted that paper goods and utensils were included.

⁶Robert Laudicina testified that on two contracts, including one with the Red Cross, Automatique's charges were based on its total costs. Automatique would get 9 or 10 percent as a management fee. This might explain why the paper products delivered to the Red Cross in this instance were separately invoiced.

We make the following additional finding of fact:

The letter agreement between Automatique and the American Red Cross required Automatique to provide, in addition to the prepared food, all necessary paper and plastic products as well as "chafing dishes, sternos, ladles . . . to be dropped off and set up . . ." (Petitioners' Exhibit "12").

Sales and use tax in the amount of \$1,259.94 was asserted as due on Automatique's purchases of equipment which petitioners claim was for use in producing tangible personal property. These purchases consisted of a work table grill, walk-in cooler and walk-in freezer at a cost of \$15,272.00 which were installed in Automatique's commissary in Long Island City and used entirely in the production of food for delivery and sale in bulk to its institutional purchasers, principally HRA. It was not used to produce food products for delivery and sale to consumers at institutions where Automatique operated cafeteria services.

OPINION

In the determination below, the Administrative Law Judge concluded that: (1) Automatique's recurring purchases of napkins, straws, stirrers, plastic knives, forks, and spoons (hereinafter "paper and plastic products") for its bulk food operation were subject to sales and use tax; (2) sales tax regulation 20 NYCRR 528.20(d) prohibits the purchase of the above items for resale as such, or their classification as packaging materials or components of packaging materials purchased for resale; (3) even though Automatique was required by its contracts with its customers to provide the paper and plastic products, the provision of such products was "purely incidental to the primary purpose of [Automatique's] business" (Matter of Custom Mgt. Corp. v. New York State Tax Commn., 148 AD2d 919, 539 NYS2d 550, 551); and (4) petitioners were entitled to a manufacturing exemption for the equipment purchased for production of bulk food in Automatique's manufacturing facility as the food produced was sold as tangible personal property and not as "restaurant food."⁷

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No exceptions were taken to the following conclusions of law of the Administrative Law Judge: 1) Automatique's recurring purchases of paper and plastic products for its cafeteria operations were subject to sales and use tax; 2) various purchases made by Automatique (Findings of Fact "15" and "16") were purchases of tangible personal property for resale as such; 3) equipment purchased by Automatique for installation at Bronx Community College

In its exception, the Division of Taxation (hereinafter the "Division") asserts that the food produced using the equipment for which petitioners have claimed the manufacturing exemption constituted "restaurant food" (Tax Law § 1105[d]) and not tangible personal property (Tax Law § 1105[a]) and, therefore, the manufacturing exemption in Tax Law § 1115(a)(12) is not applicable, citing Matter of Burger King v. State Tax Commn. (51 NY2d 614, 435 NYS2d 689).

In its exception, petitioners argue that: 1) Automatique's recurring purchases of the paper and plastic products were purchases for resale and, therefore, were not subject to sales and use taxes; 2) sales tax regulation 20 NYCRR 528.20(d) represents a narrowly defined exception to the resale exclusion of Tax Law § 1101(b)(4)(i) and is not applicable as Automatique was neither a "restaurant" nor a "similar establishment"; 3) the paper and plastic products purchased by Automatique qualify for the resale exclusion as broadly defined in sales tax regulation 20 NYCRR 526.6(c)(1); and 4) the paper and plastic products provided to the exempt organizations were not "purely incidental" to the primary purpose of Automatique's business but were "integral components" of Automatique's contracts with the organizations.

In response to the Division's exception, petitioners assert that: 1) the food produced at Automatique's Long Island City manufacturing facility was sold as tangible personal property within the meaning of Tax Law § 1115(a)(12); and 2) Automatique is entitled to the claimed manufacturing exemption on the purchase of the production equipment, citing Matter of Marriott Family Rests. v. Tax Appeals Tribunal (174 AD2d 805, 570 NYS2d 741, lv denied 78 NY2d 863, 578 NYS2d 877, affg Matter of Howard Johnson Co., Tax Appeals Tribunal, July 19, 1990).

We affirm in part and reverse in part the determination of the Administrative Law Judge.

(Finding of Fact "14") were not purchased for resale; 4) petitioners failed to sustain their burden of proving that certain items (Finding of Fact "15") were capital improvements to real property; 5) petitioners failed to sustain their burden of proving that the practice of treating all of its fixed asset and recurring expense purchases as exempt was reasonable; and 6) the absence of willful neglect and the extensive nature of petitioners' presentation did not provide sufficient grounds for abating the penalties.

For the reasons stated below, we agree with the Administrative Law Judge that Automatique's recurring purchases of paper and plastic products for its bulk food operation are subject to the sales and use tax.

Tax Law § 1105(a) imposes a sales tax on the receipts from every retail sale of tangible personal property, except as otherwise provided in Article 28. Tax Law § 1101(b)(4)(i) broadly defines a retail sale as "[a] sale of tangible personal property to any person for any purpose." Tax Law § 1101(b)(6) defines tangible personal property as "[c]orporeal personal property of any nature." An exclusion from the sales tax exists for sales of tangible personal property purchased "for resale as such or as a physical component part of tangible personal property . . ." (Tax Law § 1101[b][4][i][A]).

Automatique was in the business of producing, selling, and delivering bulk food to various exempt organizations. The paper and plastic products purchased by Automatique were transferred to the exempt organizations with the sale of the food. In general, Automatique was required to provide the paper and plastic products by specific provisions in its contracts with the exempt organizations.

In determining the sales tax treatment of the paper and plastic products, the sales tax classification of Automatique's sales of bulk food must be examined. If the food is tangible personal property under Tax Law § 1105(a), the paper and plastic products would also be treated as tangible personal property. If the food is "restaurant food" under Tax Law § 1105(d), the paper and plastic products would not be sold as tangible personal property, but as part of Automatique's provision of "restaurant food."⁸ The distinction between Tax Law § 1105(a) and Tax Law § 1105(d) is crucial. The Court of Appeals in Matter of Burger King v. State Tax Commn. (supra, 435 NYS2d 689, 691), noted that Tax Law § 1105(d) does not refer to "tangible personal property" and held that to define "restaurant food" merely as "tangible

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The term "restaurant food" was coined by the court in Burger King in describing the food subject to tax under section 1105(d) of the Tax Law.

personal property" would create an ambiguity between sections 1105(a) and 1105(d) of the Tax Law. The Court concluded that the Legislature chose to tax "restaurant food" under Tax Law § 1105(d) as a separate and distinct category of taxable goods and services.

Tax Law § 1105(d)(i) imposes a tax on the sale of food "sold in or by restaurants, taverns or other establishments in [New York] state, or by caterers":

"(1) in all instances where the sale is for consumption on the premises where sold;

"(2) in those instances where the vendor . . . after the delivery of the food or drink by or on behalf of the vendor for consumption off the premises of the vendor, serves or assists in serving, cooks, heats or provides other services with respect to the food or drink; and

"(3) in those instances where the sale is for consumption off the premises of the vendor, except where food (other than sandwiches) or drink or both are (A) sold in an unheated state and, (B) are of a type commonly sold for consumption off the premises and in the same form and condition, quantities and packaging, in establishments which are food stores other than those principally engaged in selling foods prepared and ready to be eaten."

From this language, the Legislature's scheme for the treatment of prepared foods is apparent. Food sold in restaurants or other establishments which provide a combination of prepared food and service is taxed under Tax Law § 1105(d)(i). As the Court stated in Burger King, the "purchase of restaurant food is more than the mere receipt of an edible or a potable," but "a delivery of food and service in combination" whether the service is a major portion of the combination as it might be in a gourmet restaurant, or a small portion as it might be at a hot dog stand (Matter of Burger King v. State Tax Commn., *supra*, 435 NYS2d 689, 691). In contrast, food of the type and in the form commonly sold in food stores for off the premises consumption is not taxed as "restaurant food." Ordinarily, a supermarket does not supply a service element with food purchased for home consumption because the service elements are intended to be supplied by the consumer.

Thus, the existence of this service element controls the tax classification. In a restaurant, the service element is clearly present: the vendor is providing its premises for the consumption of the food and whatever additional amenities it deems appropriate for the type of restaurant it

is. For vendors who supply food for off the premises consumption, it is necessary to determine whether a service component is also present. When a service element is present, however, the combination of food and service provided by such vendors is equivalent to that provided by a restaurant, that is, it is more than "the mere receipt of an edible or a potable" (Matter of Burger King v. State Tax Commn., *supra*, 435 NYS2d 689, 691). In such cases, the tax treatment should be equivalent and the food classified as "restaurant food."

Applying Tax Law § 1105(d)(i) to Automatique's operations, we conclude that the food transferred to the exempt organizations constituted "restaurant food" because in each case a service element was present.⁹ As stated above, tax is imposed under Tax Law § 1105(d)(i)(2) when a vendor, after delivery of the food, either 1) "serves or assists in serving" the food or 2) "provides other services with respect to the food or drink." While Automatique's employees did not serve or assist in serving the food to the exempt organizations after the food was delivered,¹⁰ Automatique provided "other services" to the exempt organizations with respect to the food. First, the paper and plastic products themselves were "other services" Automatique provided in conjunction with its provision of the food. These items are similar to those provided in restaurants. Like the similar items (plastic spoons, cups, paper supplies) discussed in Custom Mgt. Corp., the items were not incidental to Automatique's business, but rather "were purchased and used as a part of the service which petitioner provided to its clients" (Matter of Custom Mgt. Corp. v. New York State Tax Commn., *supra*, 539 NYS2d 550, 552.)

Further evidence supporting the conclusion that "other services" were provided or at least were contracted for can be found in the contracts between Automatique and the HRA-CIS Unit which specifically required Automatique to provide steam tables and serving trays (Exhibit "20"). The contracts between Automatique and HRA-SSC contained similar provisions with

⁹We do not separately address petitioners' assertion that Automatique is not an "other establishment" within the meaning of Tax Law § 1105(d) since the crucial factor is whether it sells food subject to tax under section 1105(d), i.e., restaurant food.

¹⁰The contracts between Automatique and the exempt organizations specifically stated that the bulk food was to be delivered to an employee of the exempt organization.

respect to serving trays (Exhibit "22"). Additionally, the letter agreement between Automatique and the American Red Cross called for Automatique to provide chafing dishes, sternos, and ladles to be "dropped off and set-up" as part of a dinner program at a rate of "\$2.75 per person" (Exhibit "12"). The food products produced by Automatique in accordance with contracts entered into with the Salvation Army must be classified as "restaurant food" because Automatique's services to the Salvation Army included the provision of paper goods (plates, bowls, cups and napkins) and eating utensils (plastic spoons, knives and forks). Based upon the facts in the record and the specific contractual provisions, we conclude that the food sold to these organizations would be considered "restaurant food" under subsection (2) of Tax Law § 1105(d)(i) because in addition to providing the prepared food, Automatique provided "other services" to the exempt organizations.

The food sold to HRA-CIS would also be classified as "restaurant food" under Tax Law § 1105(d)(i)(3). Subsection (3) states that if food sold for consumption off the premises of the vendor is sold in a "heated state," the food is taxable as "restaurant food." The terms "heated state" and "unheated state" are defined in the sales tax regulations as follows:

"[i]f the vendor attempts to maintain food at a temperature which is warmer than the surrounding air temperature by using heating lamps, warming trays, ovens or similar units, or cooks to order, the vendor is selling food in a heated state" (20 NYCRR 527.8[e][1][i]).

"If the vendor sells prepared foods from units maintained at or below surrounding air temperature, such sales are sales of prepared food in an unheated state" (20 NYCRR 527.8[e][1][ii]).

The HRA-CIS contracts called for delivery vehicles equipped with heaters for the storage of hot foods (Exhibits "20" and "22"). Taken together, the provisions calling for heated delivery vehicles and the provisions calling for steam tables (see above) support the inference that the food delivered to HRA-CIS was delivered in a "heated state."

An analysis of the HRA-EAU contracts leads to the conclusion that the food provided constituted "restaurant food" for a different reason. These contracts called for the production and delivery of foods consisting primarily of sandwiches and various juice drinks (Exhibit "21"). While the sandwiches were apparently not delivered in a heated state, we conclude that

sandwiches are an item of "restaurant food" because the language of Tax Law § 1105(d)(i)(3) specifically excludes sandwiches from its exceptions to "restaurant food."

Based upon our conclusion that all the food produced by Automatique for the exempt organizations constituted "restaurant food" under the statute, the paper and plastic products cannot be classified as tangible personal property. These items would be subject to the sales and use tax unless they are "critical elements" of the product sold as discussed below.

In our view, the resale exclusion is inapplicable to the paper and plastic products purchased because the transferred items cannot be considered "critical elements" of the food service provided to the exempt organizations. Characterizing the purchases at issue as "critical elements" conflicts with previous judicial application of that phrase. The courts and this Tribunal have held that items purchased for resale are classified as such based upon 1) the classification of the purchased items as tangible personal property which retain their separate identity in the transactions contracted for, and 2) the relationship of the items to the transaction as a whole (Celestial Food of Massapequa Corp. v. New York State Tax Commn., 63 NY2d 1020, 484 NYS2d 509; Matter of Burger King v. State Tax Commn., *supra*; Matter of Helmsley Enters., Tax Appeals Tribunal, June 20, 1991, affd ___ AD2d ___ [Jan. 21, 1993]).

The court in Celestial Food, made it clear that only when the items are "necessary to contain the product for delivery" can they be considered a critical element of the product sold" (Celestial Food of Massapequa Corp. v. New York State Tax Commn., *supra*, 484 NYS2d 509, 510, emphasis added). By this language, the Court indicated that the "critical element" test is only applicable to situations involving actual transfer or delivery of a product which requires a container. To enlarge the scope of the "critical element" doctrine to encompass transactions other than those which require the delivery of a container would, in the words of the State's highest court, give rise to "potentially limitless application" (Celestial Food of Massapequa Corp. v. New York State Tax Commn., *supra*, 484 NYS2d 509, 510). As the purchased items here were clearly not necessary to contain the food for delivery, we agree with the Administrative Law Judge that the items were "more akin to items of overhead, enhancing the

comfort of . . . patrons consuming the food products" (Celestial Food of Massapequa Corp. v. New York State Tax Commn., supra, 484 NYS2d 509, 510). Accordingly we hold that the paper and plastic products would not be critical elements of the food sold.

We next address whether the manufacturing exemption in Tax Law § 1115(a)(12) is available to petitioners for certain machinery and equipment purchased and installed in Automatique's Long Island City manufacturing facility and used solely in the preparation of food sold by Automatique as bulk food to various exempt organizations. The Administrative Law Judge determined that petitioners were entitled to claim the manufacturing exemption citing Matter of Howard Johnson Co., (supra). We disagree.

Tax Law § 1115(a)(12) specifically provides an exemption from the sales tax imposed under section 1105(a) for receipts from the sale of "[m]achinery or equipment for use or consumption directly and predominantly in the production of tangible personal property . . . by manufacturing [or] processing" (Tax Law § 1115[a][12], emphasis added). "Predominantly," as used in Tax Law § 1115(a)(12), means that the machinery or equipment is used more than 50% in the production of tangible personal property (see, 20 NYCRR 528.13[c][14]; Matter of Howard Johnson Co., supra).

We find that petitioners have failed to prove that the machinery and equipment were used predominantly in the production of tangible personal property. The findings of fact indicate that the machinery and equipment at issue were a worktable grill, a walk-in cooler, and a walk-in freezer, and that these items were used primarily in the production of bulk food for the HRA contracts. We have already determined that the food produced under each of the HRA contracts was "restaurant food" and not tangible personal property under the statute. As the requirements of Tax Law § 1115(a)(12) have not been satisfied, petitioners cannot claim the manufacturing exemption for this equipment (Matter of Burger King v. State Tax Commn., supra, 435 NYS2d 689, 693).

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of petitioners Automatique, Inc., Robert A. Laudicina, Donald A. Silverstone, Arthur Stevens, and Walter S. Welytok, as officers of Automatique, Inc. is denied;
2. The exception of the Division of Taxation is granted;
3. The determination of the Administrative Law Judge is affirmed in part and reversed in part;
4. The petition of Automatique, Inc., Robert A. Laudicina, Donald A. Silverstone, Arthur Stevens, and Walter S. Welytok, as officers of Automatique, Inc. is denied; and
5. The notices of determination dated November 18, 1988 issued to petitioners Automatique, Inc., and Robert A. Laudicina, Donald A. Silverstone, Arthur Stevens, and Walter S. Welytok, as officers of Automatique, Inc. are sustained.

DATED: Troy, New York
March 4, 1993

/s/John P. Dugan
John P. Dugan
President

/s/Maria T. Jones
Maria T. Jones
Commissioner